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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

FILED
99 FEB 17 PM 2:24
NORTHERN DISTRICT OF OHIO
CLEVELAND

In re:)	Case No. 98-13180
)	
RONALD J. ANNOTICO,)	Chapter 7
)	
Debtor.)	Judge Pat E. Morgenstern-Clarren
)	
_____)	
)	
SYSCO FOOD SERVICES OF)	Adversary Proceeding No. 98-1224
CLEVELAND, INC.,)	
Plaintiff,)	
)	
v.)	
)	
RONALD J. ANNOTICO,)	<u>MEMORANDUM OF OPINION</u>
)	
Defendant.)	

Sysco Food Services of Cleveland, Inc. ("Sysco") filed a Complaint to determine the dischargeability of a debt under 11 U.S.C. § 523 (a)(2)(A).¹ The trial was held on February 2, 1999 and the parties filed trial and post-trial briefs. (Docket 11, 14, 17, 18).

JURISDICTION

The Court has jurisdiction to determine this matter under 28 U.S.C. § 1334 and General Order No. 84 entered in this District on July 16, 1984 by the United States District Court for the Northern District of Ohio. This is a core proceeding under 28 U.S.C. § 157 (b)(2)(I).

¹ While the Complaint also invoked §§ 523(a)4 and (a)(6), counsel stated at trial that he was limiting the claim to § 523 (a)(2)(A).

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FACTS²

In 1985, the Debtor Ronald J. Annotico purchased a company called Krzys Provision Co., Inc. ("Krzys") which was in the business of selling meat and seafood products to restaurants and institutions. He operated the business until June 1996, at which time he entered into an agreement to sell it to Joseph Sidoti. The purchase price for the inventory, equipment, and assets was \$200,000, with \$50,000 to be paid that same month and the balance to be paid at the rate of \$2,000 a month starting in February or March 1997. Mr. Sidoti paid \$40,000 in June 1996. The plan was that the men would run the business together until December 1996, at which time Mr. Annotico would turn over all operations to Mr. Sidoti and Mr. Sidoti would be the sole owner. They agreed that Mr. Sidoti would collect the receivables after this transfer; from those funds, he would pay the suppliers according to their payment terms and also pay Mr. Annotico. In general, this is the same method by which Mr. Annotico had purchased the business from a former owner.

Mr. Sidoti and Mr. Annotico did run the business together from July through mid-December 1996, although Mr. Annotico spent quite a bit of time out of town on personal business. Mr. Sidoti had a somewhat different business approach than did Mr. Annotico. In particular, Mr. Sidoti wanted to focus on increasing volume by selling meat at less profit. He also wanted to purchase name brand goods from Sysco, which Krzys did starting in July 1996.

From some point in November through December 18, 1996, Sysco made the sales that are the subject of this dispute. The amount purchased was in the range of \$38,000 to \$39,000. This amount exceeded purchases in other months both because of Mr. Sidoti's different business

² Sysco presented its case through the testimony of Ronald J. Annotico, as if on cross-examination, and exhibits. The Debtor called as witnesses William Lesho, a State of Ohio enforcement agent for the Department of Agriculture, and Mark Schlachet, counsel to Mr. Annotico in the state court action described below.

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strategy and also because the company historically did more business during the end-of-the-year holiday season. Mr. Annotico testified that the sale was of meat products, but there was no evidence as to the exact date(s) of sale, the items sold, the sales price, or the exact payment terms.³ Neither was there evidence as to any communications between the parties at the time the sales were made. The record is also unclear as to the name of the buyer; i.e., was the meat sold to “Krzys” or to “Ronald Annotico” personally?⁴ Additionally, there is no conclusive evidence as to whether it was Mr. Annotico or Mr. Sidoti who placed the orders with Sysco. What is clear is that Mr. Annotico did not intend to pay Sysco for the goods personally; instead, he intended that Sysco--and other vendors--would be paid according to their regular credit terms by Mr. Sidoti as he collected the receivables.

Krzys sold some of the Sysco meat during the November/December holiday season, but there was no evidence as to the amount sold or the amount of money collected for any such sale. On about December 17, 1996, Mr. Annotico “turned the business over” to Mr. Sidoti. As Mr. Annotico still had not received \$10,000 of the money that was to have been paid in July 1996, he and Mr. Sidoti agreed that he would instead be paid “out of the company.” Mr. Annotico accomplished this by writing two checks to himself that totaled \$50,000. There was no evidence offered to explain the difference between the unpaid portion of the first installment (\$10,000) and the amount of the December checks (\$50,000). The Krzys bank account had about \$10,000 in it after this withdrawal. There was no evidence as to the rest of the Krzys financial picture in December 1996 other than Mr. Annotico’s unchallenged testimony that he left behind

³ Plaintiff’s Exhibit 1, a state court complaint, has attached to it a document described in that complaint as the Krzys account statement, but there was no testimony offered about it.

⁴ While there is a factual gap on this point, there is no legal significance to it as discussed below.

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approximately \$100,000 in inventory when he moved to Las Vegas at the end of December 1996.

Mr. Annotico paid some money to Sysco before he left.

Mr. Sidoti, who moved the business location sometime between December 20 and December 30, 1996, soon ran into difficulties with the State of Ohio Department of Agriculture (the "Department"). Some of Mr. Sidoti's business operations were in compliance with state laws and regulations, but others were not. On January 6 and 7, 1997, the Department seized the meat inventory that was being sold out of compliance. Mr. Sidoti attempted to correct the problems, but he ended up closing the business on an unspecified date.

On January 29, 1997, Sysco sued Mr. Annotico in the Cuyahoga County Court of Common Pleas, Case No. 329474 alleging that Mr. Annotico ". . . personally and with intent to defraud, purchased goods from [Sysco] knowing that he had no intention of paying [Sysco] in that he has closed the business and absconded with the monies received from the resale of said goods. . ." and seeking judgment in the amount of \$40,057.64. (Plaintiff's Exh. 1, ¶ 3). The parties settled that lawsuit at the close of the evidence, but before the jury returned its verdict. The settlement is set forth in these two documents dating from February 9, 1998:⁵

1. A Cognovit Note in the principal amount of \$40,057.64 payable to Sysco and signed by Mr. Annotico personally (the "Note"). This is a demand note. (Plaintiff's Exh. 2); and
2. A Compromise Settlement, Mutual Release, and Mutual Agreement entered into by Sysco and Mr. Annotico, personally (the "Agreement"). (Plaintiff's Exh. 3). The Agreement states in part that:

⁵ The Note is dated 1997, but the parties agree that it should have been dated 1998.

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IV. Annotico has denied and still denies having perpetrated a fraud of any kind against Sysco. Nevertheless, and intending to be fully bound hereby, Annotico admits that his obligations hereunder are not dischargeable under the Bankruptcy Code and, to the extent necessary, admits wrongdoing sufficient to mandate such non-dischargeability; and further acknowledges that in the spirit of compromise and cooperation, Sysco has agreed to resolve the matter privately hereby rather than on the public record.

In Mr. Annotico's mind, the "wrongdoing" was that he never intended for Sysco to be harmed by not being paid. Other than that, he did not know what he was admitting to in this part of the Agreement. Mr. Annotico's attorney advised him when he entered into the Agreement that this paragraph was enforceable and Mr. Annotico understood that if he filed for protection under the bankruptcy laws this debt would not be discharged. He made a \$2,000 payment on the Note, although no demand was ever made under it. Mr. Annotico filed this Chapter 7 case on April 29, 1998.

Additional facts are stated below.

THE POSITIONS OF THE PARTIES

Sysco argues that its debt is not dischargeable because Mr. Annotico obtained product without intending to personally pay for it. It contends that Mr. Annotico obtained the goods by false pretenses or false representations within the meaning 11 U.S.C. § 523(a)(2)(A).⁶ Sysco suggests that the Agreement is an admission of facts sufficient to prove that the debt is not dischargeable. Mr. Annotico takes the position that he was not personally liable for the products which Krzys purchased from Sysco, although he is now personally liable for the purchases

⁶ Sysco's Complaint requested a determination that its debt is not dischargeable because Mr. Annotico executed the Agreement and Note with the intention of filing bankruptcy to discharge his obligations under them. Counsel stated at trial, however, that Sysco was not pursuing this issue. He also stated that Sysco was relying only on the "false pretenses" language, but this Opinion will address the case under both phrases of the statute.

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based on the Note. He also argues that Sysco failed to prove its case under 11 U.S.C.

§ 523(a)(2)(A).

DISCUSSION

I.

As a preliminary matter, Mr. Annotico argues that any money owed is due from Krzys, rather than from him personally. He bases this on the fact that Krzys was an Ohio corporation at the time he purchased it. Two years later, and unbeknownst to Mr. Annotico, the State of Ohio canceled Krzys' corporate charter. Despite that, Mr. Annotico continued to do business under the same name apparently in the belief that the corporation existed. He concludes that since he believed that he was doing business in a corporate form that any purchases from Sysco were made by Krzys and not by him personally. This does not appear to be a correct statement of Ohio corporate law. It is not, however, necessary to address that in detail because Mr. Annotico ended all doubt about his personal liability to Sysco when he signed the Note in his individual capacity. That Note signed in connection with the Agreement establishes Mr. Annotico's personal liability for the purchases. Mr. Annotico does not dispute this. This makes the debt at issue a debt owed by Mr. Annotico unless it is non-dischargeable in this bankruptcy proceeding.

II.

The Agreement as an Admission of Facts

Sysco acknowledges that the Agreement is not enforceable as a waiver of Mr. Annotico's discharge.⁷ Sysco argues instead that the Agreement provides a sufficient, independent factual

⁷ Section 727(a)(10) "permits a waiver of the bankruptcy discharge but only if executed postpetition. Further, case law provides that a provision in a prepetition settlement agreement which waives a party's right to discharge is unenforceable as against public policy." *Ed Schory & Sons, Inc. v. Francis (In re Francis)*, 226 B.R. 385, 390 (B.A.P. 6th 1998); 11 U.S.C. § 727(a)(10).

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basis for determining that the debt is not dischargeable because the Agreement is an admission or stipulation of facts sufficient to establish that its debt is not dischargeable. Such a result, according to Sysco, is what the parties intended. Mr. Annotico argues that he did not admit specific facts that can be given preclusive effect.

Sysco cites various cases for the proposition that stipulations of fact included in a judgment entry are entitled to collateral estoppel effect in dischargeability proceedings. Under the doctrine of collateral estoppel, or issue preclusion, certain state court judgments are given preclusive effect in later lawsuits. *Bay Area Factors v. Calvert (In re Calvert)*, 105 F.3d 315 (6th Cir. 1997). The terms of the Agreement in this case, however, are not a part of a state court judgment and issue preclusion is not applicable. Additionally, the Agreement is not a stipulation or admission of facts which would provide a basis for this Court to find that Sysco's debt is not dischargeable under § 523(a)(2)(A). There are circumstances in which a debtor's pre-petition stipulation of facts can provide the factual basis for a determination that a debt is not dischargeable. *See for example Goff v. Internal Revenue Serv. (In re Goff)*, 180 B.R. 193 (Bankr. W.D. Tenn 1995). Mr. Annotico's admission is not sufficient for that purpose, however, because it does not admit to any specific facts. Moreover, Mr. Annotico denies in the Agreement that he has "perpetrated a fraud of any kind against Sysco." Mr. Annotico also testified that the only thing he intended to admit in the Agreement was that he owed the money to Sysco. This Agreement does not support Sysco's argument that Mr. Annotico admitted facts sufficient to prove that the debt is non-dischargeable.

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III.

11 U.S.C. § 523(a)(2)(A)

A discharge under 11 U.S.C. § 727(b) does not discharge an individual from a debt:

- (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by--
 - (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's . . . financial condition;

11 U. S.C. § 523(a)(2)(A). Because the Bankruptcy Code's policy is to give honest debtors a fresh start, exceptions to discharge are to be narrowly construed against the creditor and in favor of the debtor. *Manufacturer's Hanover Trust Co. v. Ward (In re Ward)*, 857 F.2d 1082 (6th Cir. 1988).

Sysco argues that Mr. Annotico obtained its property through false pretenses or false representations within the meaning of § 523(a)(2)(A). A false pretense is "an implied misrepresentation or conduct intended to create or foster a false impression." *Blascak v. Sprague (In re Sprague)*, 205 B.R. 851, 859 (Bankr. N.D. Ohio 1997). "By comparison a 'false representation' involves an expressed misrepresentation by a debtor." *Id.* A debtor's intentional failure to disclose material facts can constitute a misrepresentation under § 523(a)(2)(A). *Semaan v. Allied Supermarkets, Inc. (In re Allied Supermarkets, Inc.)*, 951 F.2d 718 (6th Cir. 1991). In order to have a debt declared non-dischargeable under this section, a creditor must prove that the debtor obtained property through a material misrepresentation known to the debtor to be false when made or made with gross recklessness as to its truth; the debtor intended to deceive the creditor; the creditor justifiably relied on the misrepresentation; and the reliance was the proximate cause of the loss. *Rembert v. AT & T Universal Card Servs., Inc. (In re Rembert)*,

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141 F.3d 277 (6th Cir. 1998), *cert. denied*, 119 S.Ct. 438 (1998). The creditor must prove these elements by a preponderance of the evidence. *Grogan v. Garner*, 498 U.S. 279 (1991).

The November and December 1996 Sales

In closing argument, Sysco's counsel stated in essence that its case is based on these facts: Mr. Annotico intended to leave the business, he intended to deplete assets of the business' bank account, and he intended to leave the state without paying the debt to Sysco. While these facts may have provided a starting point for proving a fraudulent scheme, they are insufficient to meet the creditor's burden of proof under this Code section.

The evidence showed that Krzys began purchasing products from Sysco in July of 1996. Sysco provided no evidence regarding the terms of those initial purchases. The purchases which are the subject of this dispute were made in November and December of 1996 and the record is also devoid of evidence as to their terms. The record does not establish whether the meat products were sold to Mr. Annotico personally, or to "Krzys," regardless of whether Krzys was a legal entity at the time. There is no evidence establishing the payment terms on the purchases. There is no evidence regarding any communications between the parties at the time these purchases were made. All that the record shows is the purchase of goods at a time when the owner knew he intended to complete a sale to a third party and had in place a plan for that third party to pay for the goods in a manner that is reasonable on its face, even if it proved unsuccessful in practice. These facts do not prove that Mr. Annotico's acts constituted false pretenses within the meaning of § 523(a)(2)(A).

Similarly, the evidence fails to establish that Mr. Annotico made an express misrepresentation to Sysco regarding the purchases; there is, in fact, no evidence that Mr. Annotico made *any* direct representation to Sysco in connection with the meat purchase. There

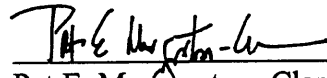
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is insufficient evidence that Mr. Annotico intentionally failed to disclose material facts. In the absence of proving misrepresentation, Sysco obviously also failed to prove that it justifiably relied on any such representation or that its loss resulted from such reliance. Sysco, therefore, has failed to prove that its debt is not dischargeable under 11 U.S.C. § 523(a)(2)(A).

CONCLUSION

For the reasons stated above, judgment will be entered in favor of Defendant Ronald J. Annotico. A separate judgment will be entered in accordance with this Memorandum of Opinion.

Date: 17 Feb 1999



Pat E. Morgenstern-Clarren
United States Bankruptcy Judge

Served by mail on: Susan Gray, Esq.
Stephen Hobt, Esq.

By: Joyce L. Gordon, Secretary
Date: 2/17/99

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RONALD J. ANNOTICO,)	Chapter 7
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Debtor.)	Judge Pat E. Morgenstern-Clarren
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SYSCO FOOD SERVICES OF)	Adversary Proceeding No. 98-1224
CLEVELAND, INC.,)	
)	
Plaintiff,)	
)	
v.)	
)	
RONALD J. ANNOTICO,)	<u>JUDGMENT</u>
)	
Defendant.)	

For the reasons stated in the Memorandum of Opinion filed this same date,

IT IS, THEREFORE, ORDERED that Judgment on the Complaint is entered in favor of

Defendant Ronald J. Annotico.

Date: 17 February 1999

Pat E. Morgenstern-Clarren
Pat E. Morgenstern-Clarren
United States Bankruptcy Judge

Served on: Stephen Hobt, Esq. (by mail)
Susan Gray, Esq. (by mail)

By: Joyce L. Gordon, Secretary

Date: 2/17/99