

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE: *
*
ANGELO G. DePASCALE and *
NELDA O. DePASCALE, * CASE NUMBER 05-43659
*
Debtors. *
*

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DAVID M. SPOTTS, *
*
Plaintiff, *
*
vs. * ADVERSARY NUMBER 05-4225
*
ANGELO G. DePASCALE, et al., *
*
Defendants. *
*

M E M O R A N D U M O P I N I O N

This matter is before the Court upon Cross-Motions for Summary Judgment. Debtors/Defendants Angelo G. DePascale ("Mr. DePascale") and Nelda O. DePascale ("Mrs. DePascale") (collectively "Defendants") filed their Motion on August 1, 2006. With leave of Court, Plaintiff David M. Spotts ("Plaintiff") filed his Motion on August 3, 2006. Plaintiff filed his response to Defendants' Motion on August 15, 2006. Defendants filed their response to Plaintiff's Motion on August 16, 2006. Defendants filed their Chapter 7 Petition on June 21, 2005. The Complaint initiating the above-captioned adversary proceeding was filed on September 19, 2005 ("Adversary Complaint").

The Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1334. Venue in this Court is proper pursuant to 28 U.S.C. §§ 1391(b), 1408, and 1409. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I).¹

In Count One of his Adversary Complaint, Plaintiff alleges that two debts, which were the subject of judgments entered by the Ashtabula Municipal Court ("Municipal Court Judgments")² in favor of Plaintiff and against Defendants, are nondischargeable pursuant to 11 U.S.C. § 523(a)(2), (4), and (6).³ (Compl. ¶¶ 4, 5.)

In Count Two, Plaintiff states that, on or about April 29, 2005, he filed a complaint in the Ashtabula County Court of Common Pleas, captioned *Spotts v. DePascale, et al.*, 05CV439 ("Common Pleas Court Complaint" or "Common Pleas Court Case"), against Defendants alleging violations of the Ohio Uniform Fraudulent Transfer Act, R.C. § 1336.01, et seq., as well as conspiracy to defraud creditors, based upon Defendants' August 7, 2000 transfer of their residence to their son, Angelo N. DePascale ("Angelo Jr."). (Compl. ¶ 6.)

¹In the Joint Stipulation of Facts, both parties assert that the above-captioned case is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I) and (J). Stipulations of Fact ("Stip.") ¶ 1. Because Plaintiff does not seek a denial of Defendants' general discharge pursuant to 11 U.S.C. § 727, but, instead, only a determination that the debts owed to Plaintiff by Defendants are nondischargeable pursuant to 11 U.S.C. § 523, 28 U.S.C. § 157(b)(2)(J) is inapplicable.

²The Municipal Court Judgments at issue were entered on November 30, 2004 in two consolidated cases, *Spotts v. Angelo DePascale*, 2003-CVF-00762, and *Spotts v. Nelda DePascale*, 2003-CVF-00763. The Municipal Court entered judgment against Defendants in two separate entries: The first entry addressed Defendants liability on defaulted loan agreements with Plaintiff, see *infra*. at 6-9, and the second entry granted attorneys' fees to Plaintiff, see *infra*. at 9-10.

³Although Plaintiff alleges in his Complaint that the Municipal Court Judgments are nondischargeable pursuant to 11 U.S.C. §§ 523(a)(2), (4), and (6), he abandons his fraud and defalcation claims in his Motion, and, instead, dedicates the entirety of his nondischargeability argument to willful and malicious injury under subsection (6).

Plaintiff argues that the debts arising from the Common Pleas Court Case are also nondischargeable pursuant to 11 U.S.C. § 523(a)(2), (4), and (6). (*Id.*)

Plaintiff further states in Count Two that he "anticipate[s] that discovery in the [Common Pleas Court Case] will reveal additional facts and details of the alleged fraud and/or other fraud by [Defendants] and others as to concealing, hiding and transferring assets, including, for example, their prior residence and their tangible personal property." (Compl. ¶ 7.) Plaintiff concludes, "If not already included in the [Common Pleas Court Complaint], Plaintiff has or will have claims against [Defendants] and the others for these acts for which a new or amended complaint in [Common Pleas Court] will be filed and which are similarly [nondischargeable] pursuant to [11 U.S.C. § 523(a)(2), (4), and (6)]". (*Id.*)

Despite the representations in his Adversary Complaint, Plaintiff never sought a motion for relief from stay from this Court in order to proceed with the Common Pleas Court Case, or to amend his Common Pleas Court Complaint to include a claim for the alleged fraudulent conveyance of Defendants' personal property. However, Defendants stipulate that they transferred all the contents of the real estate and buildings thereon to their children on August 7, 2000. (Stip. ¶¶ 3, 10.)

In his Motion, Plaintiff requests an order of this Court finding that the debts arising from the Municipal Court Judgments and the Common Pleas Court Case, including his yet-to-be-pled

personal property/fraudulent conveyance claim, are nondischargeable debts as a matter of law.

In addition, Plaintiff asks this Court to hear his fraudulent conveyance claims. Although the Common Pleas Court Case was never removed to this Court pursuant to FED. R. BANKR. P. 7027, Plaintiff dedicates over seven pages of his 17-page Motion to the legal argument that Defendants violated R.C. § 1336.04(A)(1) when they conveyed their residence to Angelo Jr. in 2000 and when Defendants conveyed their personal property to their children.

At the end of the R.C. § 1336.04(A) analysis in Plaintiff's Motion, he concludes, "This constitutes non-dischargeable conduct as both fraud and intentional malicious injury for which summary judgment to that effect should be rendered *on the liability issues*. The question of an award of punitive damages, being discretionary with the finder of fact, and the amount thereof, and attorneys fees, must wait for trial, *either in this Court or in the pending state action*." (Plaintiff's Mot. at 11-12.) (Emphasis added.)

In fact, Plaintiff does not have standing to pursue his fraudulent conveyance/conspiracy to defraud creditors claims in either Court at this time. Although the issue of standing was not briefed by the parties, the Court is required to determine as an initial matter whether Plaintiff's standing to maintain the state fraudulent conveyance/conspiracy to defraud creditors action survives the filing of the Chapter 7 Petition in this case.

I. Standing

Standing is a jurisdictional element which cannot be waived and can be raised at any time. *United States v. Van*, 931 F.2d 384, 387 (6th Cir. 1991). A trial court may *sua sponte* deny any claim for lack of standing of the party attempting to bring the claim. *FW/PBS, Inc. v. City of Dallas*, 493 U.S. 215, 231, 110 S.Ct. 596, 607 (1990).

As of the commencement of a bankruptcy case, and to the extent that any fraudulent conveyance actions may exist in favor of the estate pursuant to 11 U.S.C. § 544,⁴ such actions must be brought by the trustee for the benefit of the estate and all creditors of the estate. See *Normali v. O'Donnell (In re O'Donnell)*, 2005 WL 1279268 (6th Cir. BAP Ohio, May 19, 2005) (Court granted trustee's objection to individual creditor's proofs of claim based on state court lawsuits to recover fraudulent transfers because such claims belonged to the bankruptcy estates and could only be asserted by the bankruptcy trustee for each of those estates) and *Honigman v. Comerica Bank (In re Van Dresser Corp.)*, 128 F.3d 945, 947 (6th Cir. 1997) ("A creditor does not have standing to bring an action that belongs to the bankruptcy trustee.") Consequently, after Defendants initiated their Chapter 7 case, Plaintiff no longer has the right

⁴Section 544(b)(1) of the Bankruptcy Code permits the trustee to "avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title[.]" 11 U.S.C. § 544 (1998). For the purposes of this case, "[Section] 544(b) allows the trustee to step into the shoes of a debtor's creditors and take advantage of state law concerning fraudulent conveyances." *Rieser v. Hayslip, (In re Canyon Systems Corp.)*, 343 B.R. 615, 656 (Bankr. S.D. Ohio 2006).

to pursue the recovery of the value of an asset of the estate for his sole benefit.⁵

Likewise, because Plaintiff's conspiracy claim is premised exclusively upon the alleged fraudulent conveyances, Plaintiff cannot pursue this common law claim. Where a creditor's claim is "so similar in object and purpose to the claims that the trustee could bring in bankruptcy court," the creditor lacks standing to pursue those claims as well. *National American Insurance Co. v. Ruppert Landscaping*, 187 F.3d 439, 441 (dismissing tortious interference and conspiracy claims premised upon pre-petition fraudulent transfers). Accordingly, Plaintiff is foreclosed from asserting both of his state law claims. As a consequence, the only issue before the Court is the dischargeability of the Municipal Court Judgments.

II. Facts

Plaintiff loaned Mr. DePascale \$15,000.00 on or about June 29, 1998. (See Compl. in 03-CVF-762; ¶ 1, Ans. in 03-CVF-762; ¶ 1.) The following year, Plaintiff loaned Mrs. DePascale \$12,000.00, in two installments of \$6,000.00. Mrs. DePascale conceded the first \$6,000.00 loan in 1999, but denied the existence of the second loan. (See Compl. in 03-CVF-763; ¶¶ 1, 4, Ans. in 03-CVF-762; ¶¶ 1, 3.)

According to Plaintiff, Defendants made a number of payments on the loans, and, by the end of September 1999, there was approximately \$13,000.00 of principal still due on the loans. (Aff. of

⁵In *In re O'Donnell*, the trustee intervened as a party plaintiff in the state cases and removed the fraudulent conveyance claims to the bankruptcy court. *O'Donnell*, 326 B.R. at *5.

David Spotts at ¶ 1.) Plaintiff further states that the method in which the loans were paid made it impossible to determine what payments, or what portion of the payments, were intended to be applied to each specific loan. (*Id.*, see also Dep. of Nelda DePascale at 21.)

On August 7, 2000, Defendants transferred the real property located at 3226 Blair Avenue, Ashtabula, Ohio and an adjacent vacant lot to Angelo Jr. by quitclaim deed. (Stip. ¶¶ 2, 3.) Defendants retained life estate in the real property at the time of the transfer. (*Id.* ¶ 3.) On the same date, Defendants also transferred all of the contents of the real estate and buildings thereon to their children. (*Id.* ¶ 10.) Defendants concede that at the time of the transfers, the loans at issue in this case were "due, owing and partially unpaid." (*Id.* ¶ 9.)

In 2003, Plaintiff filed two collection actions in Ashtabula Municipal Court: *Spotts v. Angelo DePascale*, 2003-CVF-00762, and *Spotts v. Nelda DePascale*, 2003-CVF-00763, which were ultimately consolidated ("Municipal Court Complaints"). Despite the partial payment of the loans, the Municipal Court Complaints alleged that the total amount of both loans, that is, \$15,000.00 and \$12,000.00, respectively, plus interest was outstanding.⁶ (See Compl. in 03-CVF-762; ¶¶ 2, 4, and Compl. in 03-CVF-763; ¶¶ 3, 6.) In their Answers, Defendants asserted that Plaintiff was barred from recovery based upon the doctrine of accord and satisfaction.

⁶Plaintiff provides no explanation for his assertion in the Municipal Court Complaints that the entire amount of both loans was due and owing on the date the complaints were filed.

(See Ans. 03-CVF-762 at ¶ 4, and Ans. in 2003-CVF-00763 at ¶ 5.)

In addition, Mrs. DePascale asserted the defenses of payment and release. (Ans. in 2003-CVF-00763 at ¶ 5.)

Although Defendants answered the Municipal Court Complaints, they failed to appear for depositions on at least four separate occasions. Frustrated by Defendants' repeated refusals to appear, Plaintiff filed a Motions for Sanctions, or, in the alternative, to Compel Discovery and for Fees. In a decision issued on November 12, 2004, Magistrate Jon T. Field found that Defendants had been "purposefully dilatory in complying with discovery and scheduling depositions," and characterized the termination of their attorney as "another of their dilatory tactics." (Magistrate Judge's decision dated November 12, 2004 in consolidated cases 03CVF762 and 763, Findings of Fact at ¶ 6 .) The Magistrate also noted that Defendants failed to respond to the Motion for Sanctions. (*Id.* at ¶ 7.)

Because Magistrate Field believed an entry of judgment against Defendants was too harsh of a sanction at that time, he recommended, instead, the issuance of an order requiring Defendants to appear for deposition on a date selected by the Court. (Magistrate Judge's decision dated November 12, 2004 in consolidated cases 03CVF762 and 763, Recommendations at ¶ 1.) In the event that Defendants failed to appear on the chosen date, Magistrate Field recommended that judgment should then be entered in favor of Plaintiff and against Defendants for the relief requested in the Municipal Court

Complaints as well as attorneys' fees and expenses. (*Id.* at ¶¶ 2, 3.)

No objections were filed to Magistrate Field's recommendation. As a result, on November 30, 2004, the Honorable Albert S. Campese issued a Judgment Entry that set forth a deposition date, which was not subject to postponement or cancellation, and clearly stated that the sanction for Defendants' failure to appear would be judgment in favor of Plaintiff and against Defendants on the Municipal Court Complaints. (Judgment Entry dated November 30, 2004 in consolidated cases 03CVF762 and 763 at 2.) In the November 30, 2004 Entry, Judge Campese also rendered judgment in favor of Plaintiff "for expenses and attorney's fees associated with the filing of [the Motion for Sanctions.]" (*Id.*) Defendants neither objected to the selected date nor appeared for their court-ordered depositions.

In a Judgment Entry dated January 21, 2005, Judge Field (who in the interim had been elevated from the Magistrate position to an acting judgeship) awarded judgment to Plaintiff in the amount of \$15,000.00 on the complaint against Mr. DePascale plus interest at 10% per annum from August 29, 1999 plus costs, and judgment in the amount of \$6,000.00 plus interest of 4% per annum from February 11, 1999 and \$6,000.00 plus interest of 4% per annum from June 4, 1999 on the complaint against Mrs. DePascale ("Judgment on the Complaints"). (Judgment Entry dated January 21, 2005 in consolidated cases 03CVF762 and 763 at 1-2.) In a separate Judgment Entry issued the same day, Judge Field awarded attorneys' fees in favor of Plaintiff and against Defendants in the amount of \$3,000.00

("Judgment for Attorneys' Fees"). (Second Judgment Entry dated January 21, 2005 in consolidated cases 03CVF762 and 763 at 1-2.)

III. Standard Of Review

The procedure for granting summary judgment is found in FED. R. CIV. P. 56(c), made applicable to this proceeding through FED. R. BANKR. P. 7056, which provides in part that:

The judgment sought shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

FED. R. BANKR. P. 7056(c). Summary judgment is proper if there is no genuine issue of material fact, and the moving party is entitled to judgment as a matter of law. FED. R. CIV. P. 56(c); *Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986). A fact is material if it could affect the determination of the underlying action. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986); *Tennessee Department of Mental Health & Retardation v. Paul B.*, 88 F.3d 1466, 1472 (6th Cir. 1996). An issue of material fact is genuine if a rational fact-finder could find in favor of either party on the issue. *Anderson*, 477 U.S. at 248-49; *SPC Plastics Corp. v. Griffith (In re Structurlite Plastics Corp.)*, 224 B.R. 27 (B.A.P. 6th Cir. 1998). Thus, summary judgment is inappropriate "if the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson*, 477 U.S. at 248.

In a motion for summary judgment, the movant bears the initial burden to establish an absence of evidence to support the nonmoving party's case. *Celotex*, 477 U.S. at 322; *Gibson v. Gibson (In re Gibson)*, 219 B.R. 195, 198 (B.A.P. 6th Cir. 1998). The burden then

shifts to the nonmoving party to demonstrate the existence of a genuine dispute. *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 590 (1992). The evidence must be viewed in the light most favorable to the nonmoving party. *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 158-59 (1970). However, in responding to a proper motion for summary judgment, the nonmoving party "cannot rely on the hope that the trier of fact will disbelieve the movant's denial of a disputed fact, but must 'present affirmative evidence in order to defeat a properly supported motion for summary judgment.'" *Street v. J.C. Bradford & Co.*, 886 F.2d 1472, 1476 (6th Cir. 1989) (quoting *Anderson*, 477 U.S. at 257). That is, the nonmoving party has an affirmative duty to direct the court's attention to those specific portions of the record upon which it seeks to rely to create a genuine issue of material fact. *Street*, 886 F.2d at 1479.

However, neither party may re-try an issue already litigated in Municipal Court. Generally, the doctrine of collateral estoppel "precludes relitigation of issues of fact or law actually litigated and decided in a prior action between the same parties and necessary to the judgment, even if decided as part of a different claim or cause of action." *Markowitz*, 190 F.3d at 461 (quoting *Sanders Confectionery Products, Inc. v. Heller Financial, Inc.*, 973 F.2d 474, 480 (6th Cir. 1992)). More specifically, collateral estoppel, or "issue preclusion," will apply where: (1) the law of collateral estoppel in the state in which the issue was litigated would preclude relitigation of such issue, and (2) the issue was fully and fairly litigated in state court. *Markowitz*, 190 F.3d at 461 (citing 28 U.S.C. § 1738).

In Ohio, the following elements must be established to apply the doctrine of collateral estoppel: 1) A final judgment on the merits in the previous case after a full and fair opportunity to litigate the issue; 2) The issue must have been actually and directly litigated in the prior suit and must have been necessary to the final judgment; 3) The issue in the present suit must have been identical to the issue in the prior suit; and 4) The party against whom estoppel is sought was a party or in privity with a party to the prior action. *Gonzalez v. Moffit (In re Moffitt)*, 252 B.R. 916, 921 (6th Cir. B.A.P. 2000).

The United States Supreme Court has held that the doctrine of collateral estoppel is applicable in bankruptcy proceedings. See *Grogan*, 498 U.S. at 284, 111 S.Ct. at 658. "[T]he party asserting preclusion bears the burden of proof." *Spectrum Health Continuing Care Group v. Anna Marie Bowling Irrecoverable Trust Dated June 27, 2002*, 410 F.3d 304, 310 (6th Cir. 2005) (quoting *United States v. Dominguez*, 359 F.3d 839, 842 (6th Cir.), cert. denied, 543 U.S. 848, 125 S.Ct. 261 (2004)).

IV. Law

Section 523(a) provides several exceptions to the general rule that pre-petition debts are dischargeable under the Code. Plaintiff bears the burden of proving by a preponderance of the evidence that a debt is excepted from discharge under section 523(a) of the Bankruptcy Code. *Meyers v. I.R.S. (In re Meyers)*, 196 F.3d 622, 624 (6th Cir. 1999) (citing *Grogan v. Garner*, 498 U.S. 279, 290-91, 111 S.Ct. 654, 661 (1991)). Exceptions to discharge are narrowly

construed "to promote the central purpose of discharge: relief for the 'honest but unfortunate debtor.'" *Id.* (quoting *Grogan*, 498 U.S. at 286-87, 111 S.Ct. at 654).

Section 523(a)(2) states in pertinent part:

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any 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 or an insider's financial condition.

In most cases, in order to except debt from discharge under § 523(a)(2)(A), a creditor must prove that: (1) the debtor obtained money through a material misrepresentation that, at the time the representation was made, the debtor knew was false or made with gross recklessness as to its truth; (2) the debtor intended to deceive the creditor; (3) the creditor justifiably relied on the false representation; and (4) the reliance was the proximate cause of the loss. *Longo v. McLaren (In re McLaren)*, 3 F.3d 958, 961 (6th Cir. 1993).

However, the Bankruptcy Appellate Panel of the Sixth Circuit Court of Appeals recognized in 2001 that the phrase "actual fraud" in § 523(a)(2)(A) is broader than misrepresentation and misleading omission. In *Mellon Bank v. Vitanovich (In re Vitanovich)*, 259 B.R. 873, 877 (6th Cir. BAP 2001), the Panel wrote, "When a debtor intentionally engages in a scheme to deprive or cheat another of

property or a legal right, that debtor has engaged in actual fraud and is not entitled to the fresh start provided by the bankruptcy Code." *Id.* (internal citations omitted).

Like fraud based upon misrepresentation, a debtor's subjective intent at the time the debt is incurred is critical to proving actual fraud. *Id.*; *Accord Rembert v. AT&T Universal Card Services, Inc. (In re Rembert)*, 141 F.3d 277 (6th Cir. 1998) (debtor's subjective intent to defraud essential to nondischargeability claim under § 523(a)(2)(A)).

Section 523(a)(6) of the Bankruptcy Code provides that "a discharge under [the Bankruptcy Code] does not discharge an individual debtor from any debt . . . for willful and malicious injury by the debtor to another entity or to the property of another entity." 11 U.S.C. § 523 (West 2006).

The Supreme Court has held that only acts done with intent to cause injury, and not merely acts done intentionally, rise to the level of willful injury for the purposes of satisfying section 523(a)(6). *Kawaauhau v. Geiger*, 523 U.S. 57, 57-58, 118 S.Ct. 974, 975 (1998). In *Markowitz v. Campbell (In re Markowitz)*, 190 F.3d 455 (6th Cir. 1999), the Sixth Circuit expanded the definition of "willfulness" to include the debtor's subjective belief that the injury is "substantially certain to result " from his actions. *Id.* at 464.

A person acts maliciously when that person acts in conscious disregard of his or her duties or without just cause or excuse. See *Heyne v. Heyne (In re Heyne)*, 277 B.R. 364, 368 (Bankr. N.D. Ohio

2002) (*citing Murray v. Wilcox (In re Wilcox)*, 229 B.R. 411, 419 (Bankr. N.D. Ohio 1998)); *see also In re Saad*, 319 B.R. at 156 (*citing Tinker v. Colwell*, 193 U.S. 473, 485-86, 24 S.Ct 505 (1904) (defining "malice" under § 17(a)(2) of the former Bankruptcy Act [now § 523(a)(6)] as "a wrongful act, done without just cause or excuse") (internal quotation marks and citations omitted)).

As the requirements of the statute are set forth in the conjunctive, a creditor must establish both willfulness and malice in order to prevail in a section 523(a)(6) action. However, two bankruptcy courts in this district have recognized that, in the great majority of cases, the same factual events giving rise to a finding of willfulness will likewise be indicative of malice. *Superior Metal Products v. Martin (In re Martin)*, 321 B.R. 437, 442 (Bankr. N.D. Ohio 2004); *CMEA Title Agency v. Little (In re Little)*, 335 B.R. 376, 383 (Bankr. N.D. Ohio 2005) ("Although the 'willful' and 'malicious' requirements will be found concurrently in most cases, the terms are distinct, and both requirements must be met under § 523(a)(6).") Both courts, however, acknowledge that the "malice" element requires "a heightened level of culpability transcending mere willfulness." *In re Martin*, 321 B.R. at 442, *In re Little*, 335 B.R. at 384.

V. Analysis

In an argument raised for the first time in his Response, Plaintiff asserts that the Municipal Court Judgments are non-dischargeable based on the allegedly fraudulent nature of the conveyance of Defendants' residence and personal property in 2000. (Plaintiff's Resp. at 1-4.) Because Defendants concede that their loan obligations to Plaintiff were due and owing in 2000, Plaintiff concludes that Defendants engaged in "actual fraud" when they conveyed their residence and personal property. (*Id.*)

Plaintiff's "actual fraud" claim is premised upon the Seventh Circuit Court of Appeals' decision in *McClellan v. Cantrell*, 217 F.3d 890 (8th Cir. 2000). As such, a brief review of the facts in *McClellan* are instructive.

McClellan sold his business assets, which included ice-making machinery, to Cantrell's brother and retained, but did not perfect, a security interest in the machinery. *Id.* at 892. When Cantrell's brother defaulted on the sale agreement, McClellan sued him in state court seeking, among other things, an injunction against any transfer of the machinery. *Id.* While the state court case was pending, Cantrell's brother transferred the machinery to Cantrell in exchange for \$10.00. *Id.* At the time of the transfer, Cantrell was fully aware of the pending state court action. Cantrell, in turn, sold the machinery for \$160,000.00. *Id.* The following year, McClellan added Cantrell to the state court complaint, claiming that her brother's transfer of the machinery to her constituted a fraudulent conveyance. *Id.*

During the pendency of the state court case, Cantrell filed her Chapter 7 petition. *Id.* Shortly thereafter, McClellan filed an adversary proceeding in which he asserted that Cantrell, as the knowing recipient of the fraudulently transferred assets that secured her brother's debt, owed him a nondischargeable debt. *Id.*

The Seventh Circuit Court of Appeals agreed. The Court wrote, "The debt that McClellan is seeking to collect from [Cantrell] (and prevent her from discharging) arises by operation *from her fraud*. That debt arose not when her brother borrowed money from McClellan, but when she prevented McClellan from collection from the brother the money that the brother owed him." *Id.* at 895 (Emphasis in original).

Of course, unlike the debt in *Cantrell*, the debt in the instant case was not created by the fraudulent conveyance, but, instead, arose when Defendants defaulted on their loan obligations to Plaintiff. However, the *Cantrell* Court, finding it paradoxical that Cantrell could not discharge her fraud debt in bankruptcy but that her brother could discharge the same debt if he declared bankruptcy, wrote, in *dicta*:

What is true is that if [Cantrell's brother] had merely defaulted on his original debt to McClellan, which so far as appears was not created by a fraud, and later declared bankruptcy, that debt would have been dischargeable. If, however, he had rendered the debt uncollectible by making an actually fraudulent conveyance of the property that secured it, his actual fraud would give rise to a new debt, nondischargeable because created by fraud, just as in the case of the sister, his accomplice in fraud. But it would be a new debt only to the extent of the value of the security that he conveyed, for that would be the only debt created by the fraud itself.

Id.

Although, at first blush, the Court's *dicta* appears applicable to the facts in this case, a careful reading reveals that the *Cantrell* Court's conclusion turns on the secured nature of the debt. In order to further illustrate the mechanics of the "actual fraud" theory announced in *Cantrell*, the Court wrote, ". . . [i]f [Cantrell's brother] owed McClellan \$100,000 and defaulted after having transferred to [Cantrell] *property securing the debt* worth \$10,000, he would be entitled to discharge \$90,000 of the debt, for only the \$10,000 was a debt created by fraud." *Id.* (Emphasis added); see also *Central Credit Union v. Logan (In re Logan)*, 327 B.R. 907 (Bankr. N.D. Ill. 2005) (undertaking *Cantrell* analysis of a secured debt).

Likewise, as set forth in the foregoing block quote, the *Cantrell* Court clearly limited its "actual fraud" theory to the fraudulent transfer of secured property. The Court stated that a new nondischargeable debt arises where a debtor had rendered the original debt uncollectible "by making an actually fraudulent conveyance of the property that secured it." *Id.*

Finally, the public policy underlying the ruling in *Cantrell* supports the conclusion that the decision should be strictly limited to secured debts. Generally, the attachment of a security interest in collateral gives the secured party certain rights to proceeds. See Uniform Commercial Code § 9-203 (West 2006). As such, when a debtor transfers collateral to a third party for value, he has not injured the secured creditor because the creditor retains a security interest in the proceeds. However, when a debtor fraudulently

conveys collateral for little or no consideration, he has defrauded the secured creditor by impairing his legal rights under the security agreement.

Because the plain language in *Cantrell*, as well as the public policy supporting the decision, instruct that the "actual fraud" theory announced in that case is properly limited to fraudulent conveyances of secured property, that rule of law is inapplicable to the facts in this case. As a consequence, Plaintiff's nondischargeability argument based upon § 523(a)(2)(A) fails as a matter of law.

Plaintiff next argues that the conduct of the Defendants that led to the entry of the Judgment on the complaints and the Judgment for attorneys' fees resulted in debts for willful and malicious injury under § 523(A)(6).

According to Plaintiff, the fact that judgment was entered for the full amount pled in the Municipal Court Complaints, rather than the actual amount owed, demonstrates the punitive nature of the Judgment on the complaints. (Plaintiff's Mot. at 15.) ("In view of the punitive nature of the judgment, the full amount, or at least the additional principal and/or attorney fees are nondischargeable.") He likewise concludes that attorneys' fees cannot be awarded in Ohio without a showing of willfulness or malice. Finally, Plaintiff argues that the doctrine of collateral estoppel prevents Defendants from arguing that their refusal to attend their Municipal Court case depositions was merely negligent rather than purposefully dilatory.

Plaintiff cites *Toney v. Berkemer*, 6 Ohio St.3d 455, 452 N.E.2d 700 (1983) for the rule of law that "the harsh remedies of dismissal and default should be used only when the failure to comply [with discovery orders] has been due to willfulness, bad faith, or any fault of the petitioner." *Id.* at 458, 702 (internal citations omitted.) Because Plaintiff believes the Judgment on the complaints was a sanction for contumacious conduct, rather than an effort by the Municipal Court to make Plaintiff whole on his breach of contract claims, he concludes that the Judgment on the Complaints as well as the Judgment for Attorneys' Fees are debts which resulted from "intentional, malicious acts" that "obviously caused injury to Plaintiff." (Plaintiff's Mot. at 16.)

The foregoing argument misses the mark with respect to the Judgment on the Complaints because it improperly characterizes the nature of the relief awarded by the Municipal Court. Simply stated, the conduct of the Defendants that created the debts at issue was their default on the various loans, not their failure to appear for depositions.

Defendants' conduct during the discovery process prevented Plaintiff from gathering evidence to prove the allegations in the Municipal Court Complaints. As such, Judge Field entered judgment in Plaintiff's favor without requiring evidentiary support, not as a punishment for Defendants' willful and malicious conduct, but as a remedy for Defendants' intentional frustration of Plaintiff's ability to gather evidence.

Although Plaintiff attempts to recast the original loan debt based upon the subsequent conduct of Defendants *ala Cantrell, supra*, such re-characterization is inappropriate in this case. Because the Judgment on the Complaints represents recovery on the breach of contract claims as pled in the Municipal Court Complaints, rather than a debt for the fraudulent transfer of secured property, the judgment debt is dischargeable as a general unsecured debt.

Similarly, Plaintiff's argument that the entry of judgment for the full amount alleged in the Municipal Court Complaints, rather than the actual amount due, somehow converts the debt for breach of contract into a debt for willful and malicious injury is equally unavailing.

Although Plaintiff argues that Judge Field entered judgment for the full amounts alleged in the Municipal Court Complaints as a sanction, there is no evidence before this Court that Judge Field knew that Plaintiff had alleged twice the amount due and owing on the loan agreements. As a matter of fact, it is equally as reasonable to conclude that it was Plaintiff's fraud on the Municipal Court in pleading amounts greater than the amounts actually owed - rather than Defendants' conduct - that resulted in an entry of judgment for the larger amount.⁷ As a consequence, the Court will not rely on the amount of damages awarded in the Judgment on the

⁷The Court ultimately rejects all of the arguments advanced by Plaintiff on the issue of the nondischargeability of the Judgment on the Complaints. However, even assuming *arguendo* that Plaintiff had advanced a compelling § 523(a)(2)(A) or (a)(6) claim, the Court would be loathe to find that the debt represented by the Judgment on the Complaints was nondischargeable due to Plaintiff's unclean hands in asserting amounts in the Complaints that were virtually twice the amount actually owed by Defendants.

Complaints to conclude that the Municipal Court found Defendants' conduct to have caused willful and malicious injury to Plaintiff.

The Court finds that Defendants, because of their refusal to provide evidence in Municipal Court, were foreclosed from mounting a defense to the breach of contract claims. Therefore, the debt represented by the Judgment on the Complaints is a debt for breach of contract. As the Judgment on the Complaints merely placed the authority of the Court behind the original defaulted loan debts, as pled to the Municipal Court, no "new debt" based upon fraud was created. *Cantrell*, 217 F.3d at 895. Accordingly, the debt memorialized in the Judgment on the Complaints is dischargeable.

On the other hand, Plaintiff's argument that the Judgment for Attorneys' Fees is a debt for willful and malicious injury has merit. Ohio follows the "American rule," which provides that each party is responsible for its own attorney's fees except as provided in certain statutory actions or when the opposing party is found to have acted in bad faith, vexatiously, wantonly, obdurately, for oppressive reasons, or the party somehow engaged in malicious conduct. *Sharp v. Norfolk & W. Ry. Co.*, 72 Ohio St.3d 307, 314, 649 N.E.2d 1219 (1995) (citing *Sorin v. Warrensville Hts. School Dist. Bd. of Educ.*, 46 Ohio St.2d 177, 181, 75 O.O.2d 224, 347 N.E.2d 527 (1976)).

Furthermore, bankruptcy courts in Ohio have concluded that collateral estoppel applies to the facts in this case because a finding of malice is required by Ohio law for the award of attorneys' fees. *S.L. Peirce Agency, Inc. v. Painter (In re*

Painter), 285 B.R. 669, 675 (Bankr. S.D. Ohio 2002) (citing *Rowe Oil, Inc. v. McCoy (In re McCoy)*, 189 B.R. 129, 134 (Bankr. N.D. Ohio 1995)).

Likewise, in *Sarff v. Spring Works (In re Sarff)*, 242 B.R. 620 (6th Cir. B.A.P. 2000), the Bankruptcy Appellate Panel for the Sixth Circuit held that the debtor's liability for discovery sanctions would be excepted from discharge as a debt for willful and malicious injury. *Id.* at 628. Although the bankruptcy court in *Sarff* premised the nondischargeability of the sanctions on the nondischargeability of the ancillary debt, the BAP held, instead, that the debtor was collaterally estopped from challenging the nondischargeability of the sanctions because the state court awarded them for "reprehensible" conduct on the part of the debtor. *Id.*

In a decision ultimately adopted in its entirety by Judge Campese, then Magistrate Judge Field found the conduct of the Defendants to be "purposefully dilatory."⁸ The phrase chosen by Magistrate Field indicates that he believed Defendants' conduct was intentional and undertaken for the purpose of delaying the entry of judgment against them in Municipal Court. As such, there is no question that Defendants' refusal to attend their respective

⁸In their Response, Defendants contend that their failure to appear for depositions reflected a post-answer decision to abandon their defenses to the lawsuit due to their advanced age. (Defendants' Resp. at 2.) In fact, the Judgment on the Complaints reveals that Defendants filed a "Request for Hearing on Damages" in Municipal Court, but that it was not considered because it was improperly filed. (Judgment Entry dated January 21, 2003 in consolidated cases 03CVF762 and 763 at 3.) Counsel for Defendants also appeared at the hearing for the determination of attorneys' fees conducted on January 12, 2005. (Second Judgment Entry dated January 21, 2005 in consolidated cases 03CVF762 and 763 at 1-2.) Therefore, even if this Court found that collateral estoppel did not prevent Defendants from offering evidence, Defendants' eleventh-hour negligence argument is directly contradicted by the evidence before the Court.

depositions was the motivating factor in Magistrate Field's recommendation for attorneys' fees.

Insofar as a court of competent jurisdiction found that Defendants' objective in refusing to attend the depositions was to delay the entry of judgment against them, and that such a finding was necessary to the award of attorneys' fees in the Municipal Court cases, Defendants are collaterally estopped from asserting that they did not intentionally and maliciously injure Plaintiff by deliberately delaying the Municipal Court proceedings. Accordingly, the debt memorialized by the Judgment for Attorneys' Fees is nondischargeable pursuant to 11 U.S.C. § 523(a)(6).

An appropriate order will follow.

HONORABLE KAY WOODS
UNITED STATES BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE: *
*
ANGELO G. DePASCALE and *
NELDA O. DePASCALE, * CASE NUMBER 05-43659
*
Debtors. *
*

*
DAVID M. SPOTTS, *
*
Plaintiff, *
*
vs. * ADVERSARY NUMBER 05-4225
*
ANGELO G. DePASCALE, et al., *
*
Defendants. *
*

O R D E R

For the reasons set forth in this Court's memorandum opinion entered on this date, the Court finds that the debt represented by the Judgment on the Complaints is dischargeable, and the Judgment for Attorneys' Fees is nondischargeable pursuant to 11 U.S.C. § 523(a)(6). The Court further finds that Plaintiff does not have standing at this time to pursue his state law claims in this Court.

IT IS SO ORDERED.

HONORABLE KAY WOODS
UNITED STATES BANKRUPTCY JUDGE