United States Bankruptcy Court
Northern District of Illinois
Eastern Division

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Bankruptcy Caption: In re William W. Fawell

Bankruptcy No. 98 B 01274

Adversary Caption: Davis, Mannix & McGrath and Brenda Porter Helms v. William W. Fawell

Adversary No. 98 A 01306

Date of Issuance: July 26, 1999

Judge: John H. Squires

Appearance of Counsel:

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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

IN RE: WILLIAM W. FAWELL, Debtor.	)	Chapter 7 Bankruptcy No. 98 B 01274 Judge John H. Squires
DAVIS, MANNIX & McGRATH and BRENDA PORTER HELMS, Plaintiffs, v. WILLIAM W. FAWELL, Defendant.	)	Adversary No. 98 A 01306

O R D E R

For the reasons set forth in a Memorandum Opinion dated the 26th day of July, 1999, the Court hereby grants judgment, in part, in favor of Davis, Mannix & McGrath and Brenda Porter Helms. The Debtor's discharge is denied and the objections thereto under 11 U.S.C. § 727(a)(2)(A) and § 727(a)(4)(A) are sustained. The objections under 11 U.S.C. § 727(a)(3) and § 727(a)(5) are overruled. The Court denies the Debtor's motion for directed findings.

ENTERED:

DATE: _____

John H. Squires
United States Bankruptcy Judge

cc: See attached Service List

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

IN RE: WILLIAM W. FAWELL, Debtor.	)	Chapter 7 Bankruptcy No. 98 B 01274 Judge John H. Squires
DAVIS, MANNIX & McGRATH and BRENDA PORTER HELMS, Plaintiffs, v. WILLIAM W. FAWELL, Defendant.	)	Adversary No. 98 A 01306

MEMORANDUM OPINION

This matter comes before the Court on the complaint of Davis, Mannix & McGrath, (the "Creditor") and Brenda Porter Helms, as Chapter 7 Trustee (the "Trustee"), (collectively the "Plaintiffs") objecting to the discharge of William W. Fawell (the "Debtor") pursuant to 11 U.S.C. §§ 727(a)(2), (a)(3), (a)(4) and (a)(5) and on the Debtor's motion for directed findings under Federal Rule of Bankruptcy Procedure 7052. For the reasons set forth herein, the Court grants judgment, in part, in favor of the Plaintiffs. The Debtor's discharge is denied and the objections thereto under § 727(a)(2)(A) and § 727(a)(4)(A) are sustained. The objections under § 727(a)(3) and § 727(a)(5) are overruled. The Court denies the Debtor's motion for directed findings.

I. JURISDICTION AND PROCEDURE

The Court has jurisdiction to entertain this matter pursuant to 28 U.S.C. § 1334 and General Rule 2.33(A) of the United States District Court for the Northern District of Illinois. This matter constitutes a core proceeding under 28 U.S.C. § 157(b)(2)(J).

II. FACTS AND BACKGROUND

The Debtor filed a Chapter 7 petition on January 15, 1998. Thereafter, the Trustee was duly appointed. The Debtor has been engaged in the construction industry for years and involved with multiple business entities. The meeting of creditors under 11 U.S.C. § 341 was commenced on March 23, 1998, and was continued for the purpose of obtaining documents from the Debtor. The Creditor is an unsecured creditor of the Debtor in the amount of $106,000.00 for unpaid legal services provided to the Debtor.

A. The Plaintiffs' Complaint

On July 31, 1998, the Plaintiffs filed a complaint objecting to the Debtor's discharge. The Plaintiffs base their single-count complaint upon 11 U.S.C. §§ 727(a)(2), (a)(3), (a)(4) and (a)(5). They contend that the Debtor has not provided all requested documents relating to prepetition transfers of the Debtor's property to statutory insiders. They further allege that the Debtor's scheduled assets and liabilities, and the answers he provided to the questions in the Statement of Financial Affairs, are false and misleading. In his original and amended answers to the complaint, the Debtor denied any wrongful conduct.

Specifically, the Plaintiffs allege that the Debtor's Schedules show that in December 1996, he transferred his interest in U.S. Breaker, Inc., an Illinois corporation ("USB"), to a

friend and business associate, Jeffrey Osterle ("Osterle"). The Plaintiffs contend, however, that Osterle testified at his examination under Federal Rule of Bankruptcy Procedure 2004 that he and the Debtor each retained a forty-five percent interest in USB and that the Debtor did not transfer his interest in USB to Osterle.

The complaint further alleges that the Debtor's Schedule B showed him as a twenty-five percent member of American Motivate, LLC ("AMLLC"), but that the Debtor transferred that interest to Osterle in December 1996. It is further alleged that the Debtor gave a financial statement dated July 9, 1997 to a bank which showed the Debtor still held the twenty-five percent interest in AMLLC, and that other documents furnished subsequently revealed that through January 22, 1998, the Debtor was still a member and manager of AMLLC.

Next, the Plaintiffs allege that at the § 341 meeting, the Debtor testified that he refinanced the mortgage on his home and used the $40,000.00 proceeds as follows: paid a $20,000.00 judgment; paid Historic Contractors, Ltd., a corporation controlled by the Debtor ("Historic"), to excavate a garage at his residence; and paid various bills. At the end of the meeting, however, the Debtor allegedly admitted he had paid his fiancé, Cindy Pepple ("Pepple"), $6,000.00 of the proceeds as repayment for some of the utilities for the residence. The Debtor's answers to the relevant questions in the Statement of Financial Affairs did not reveal that he had made certain payments during the relevant preference period under 11 U.S.C. § 547.

The Debtor's Schedule B listed only one checking account with a balance of $100.00 as of the time he filed his bankruptcy petition. The underlying bank statement for that

checking account, however, allegedly showed that $2,270.00 was in the account during the period January 13, 1998 through January 16, 1998, the day after the filing of the petition.

The Plaintiffs additionally allege the Debtor's Schedule B listed certain collateral with a fair market value of $150,000.00, subject to a secured claim of Forrest Financial of $200,000.00. According to Osterle's testimony, the Plaintiffs assert that the debt to Forrest Financial was only $156,000.00 as of March 1998, two months post-petition. Similarly, the Debtor's Schedule B listed collateral with a fair market value of $7,500.00, subject to the $4,000.00 secured claim of Pioneer Bank & Trust. According to Osterle's testimony, the debt to Pioneer was only $1,680.00 and was paid off in March 1998, approximately three and one-half months post-petition. Furthermore, the Plaintiffs contend that on July 9, 1997, when the Debtor gave his financial statement listing his assets and liabilities to Midwest Mortgage, it showed only three liabilities totaling $134,664.00. The Debtor's Schedules and Statement of Financial Affairs, however, listed multiple liabilities totaling $692,600.00. Lastly, the Plaintiffs allege that the Debtor's Statement of Financial Affairs failed to list a lawsuit with Old Kent Bank.

B. Evidence Adduced at Trial

The principal witness who testified at trial was the Debtor. There was much testimony (some less than crystal clear) concerning his involvement over the years in various construction related businesses in which he had various offices, duties and equity interests. The Debtor testified that he filled out the original Schedules and answered the questions in the Statement of Financial Affairs truthfully and correctly. See Creditor's Exhibit No. 1 and Debtor's Exhibit No. 1. It was his intent to advise the Trustee and Creditor at the § 341

meeting of his financial affairs. He further contended that he produced all the documents in his possession to the Trustee per her request. See Debtor's Exhibit Nos. 11-16. According to the Debtor, he fully complied with the requests made upon him.

The Debtor admitted he operates Historic. He had also been involved with an entity formerly known as American Motivate, Inc. ("AMI"). He further admitted that he had been a twenty-five percent owner and manager of AMLLC. The Debtor testified that he gave all his interest in that company to Osterle for no additional consideration in December 1996 because Osterle had previously made capital contributions through prior loans to the Debtor aggregating $125,000.00.

Concerning USB, the Debtor stated that he had 400 shares in that company which he also transferred to Osterle in December 1996. Currently, once a month he makes phone calls for USB which in return pays his health insurance premiums. These payments were admittedly not disclosed in the Schedules, but according to the Debtor, this was disclosed at the § 341 meeting. See Creditor's Exhibit No. 1, Schedule I and Debtor's Exhibit No. 1, Schedule I..

The Debtor testified he advised the Trustee at the § 341 meeting that he had paid Pepple $500.00 for living expenses. He further admitted to paying $5,000.00 from the home refinancing proceeds to a Chevrolet dealer for the leased Chevrolet Tahoe motor vehicle he used, which was in Pepple's name, but that was not disclosed in the original Schedules. He made all the lease payments and insurance payments on the Tahoe motor vehicle beginning in July 1997. He further stated that it was not disclosed in the Schedules that he paid $19,000.00 to Osterle in July 1997. The Debtor signed and submitted an application to

refinance his home with a disclosure of his statement of assets and liabilities in July 1997 in connection therewith, and listed few liabilities. This financial statement is in marked contrast to the liabilities of over $692,000.00 listed on his Schedules. Compare Creditor's Exhibit No. 9 with Creditor's Exhibit No. 1. The Debtor certified for the bank loan that the home was valued at $210,000, in contrast to its value listed on Schedule A at $175,000.00. Id. As another example of the discrepancies in values, his Bronco motor vehicle was scheduled at $1,000.00 on his Schedules, but valued at $5,000.00 in his loan application. Id. Additionally, the household goods and furnishings were valued at $1,000.00 on the Schedules in contrast to a $10,000.00 valuation in his loan application to the bank. Id.

The Debtor conceded that his Schedules and the information contained in his answers to the questions in the Statement of Financial Affairs did not list any accounts receivable owed under contracts between Historic and AMLLC. He admitted Schedule I listed $4,000.00 as his estimate of average monthly income from AMLLC at the time he filed his petition, but he had no income that year and was actually employed by Historic, not AMLLC. He stated that his Schedule J was his estimate of his current monthly expenditures. He testified that he scheduled he had no income, other than from employment or operation of business, in answer to Question 2 of his Statement of Financial Affairs, but admitted that Osterle had loaned him money during the two years prepetition. In addition, the Debtor further testified that Pepple had given him money during that two-year prepetition period that was not disclosed. He admitted that he had not disclosed other payments to creditors made within the ninety-day period prior to the filing of the petition. He attempted to correct these and other deficiencies in this original Schedules by virtue of his amended Schedules and

Statement of Financial Affairs that were filed on May 14, 1999, one week before the commencement of trial. See Debtor's Exhibit No. 2.

The Debtor admitted he did not list the debt he owed Osterle in his original Schedules. He further admitted that his original Statement of Financial Affairs listed no closed financial accounts, but the amendment listed two. He admitted receiving letters from his attorney requesting additional information sought by the Trustee, which he believed he provided at the § 341 meeting, including his check journal.

In answer to the questions propounded at Question 3a regarding payments to creditors in the ninety days prepetition, the original Statement of Financial Affairs disclosed none. However, the amended Statement of Financial Affairs disclosed seven payments. See Debtor's Exhibit No. 2, Addendum 1 to Amended Statement of Financial Affairs No. 3a. The amended answer to Question 3b detailed payments to insiders made in the one-year period immediately preceding the filing of his petition, revealing approximately thirty-four checks drawn on two checking accounts in stark contrast to the original answer to this question, wherein he stated no payments were made to insiders. See Debtor's Exhibit No. 2, Addendum 2 to Amended Statement of Financial Affairs No.3b and Debtor's Exhibit No. 1. These payments to insiders disclosed on the amended Statement of Financial Affairs totaled almost $43,000.00.

Osterle testified that he entered into a variety of business transactions with the Debtor. According to Osterle, he lent money on numerous occasions to the Debtor totaling approximately $150,000.00. See Creditor's Exhibit No. 21. Osterle was also co-guarantor along with the Debtor on some equipment leases in favor of Forrest Financial, which was

owed approximately $150,000.00 as of March 1998.

The Trustee testified that she conducted the § 341 meeting in the Debtor's case. In contrast to the Debtor's recollection, she did not recall the Debtor bringing any documents with him or disclosing at that time any payments that he had made to Osterle during the relevant prepetition period. She did not recall any discussion by which the Debtor disclosed his prepetition payments to Pepple, nor did the Debtor disclose the $5,000.00 prepetition payment he made on the leased Tahoe vehicle. She requested documents from the Debtor after the § 341 meeting. See Debtor's Exhibit No. 11. According to the Trustee, she received documents in "dribs and drabs" from the Debtor that totaled about two inches thick. After she received the documents she sent them to the Creditor for review. On cross-examination, the Trustee admitted she could not recall the specific questions asked of the Debtor. No transcript was furnished of that meeting. In her view, more investigation was needed after the meeting.

Thomas Springer, one of the Debtor's attorneys who also testified, stated that the Trustee's document request was extensive and he provided everything to the Trustee that the Debtor furnished to him. He did not recall the Debtor refusing to answer any questions at the § 341 meeting. In his opinion, the Debtor cooperated with the Trustee as required by 11 U.S.C. § 521. He testified that he prepared Addendum Exhibit Nos. 1 and 2 to Schedule B as part of the amended Schedules in order to address all the Debtor's prior and ongoing business interests. See Debtor's Exhibit No. 2.

On cross-examination, he admitted that the Debtor's prepetition payments to Historic, Osterle and others were not referred to in the original Schedules. In addition, the original

Schedules did not disclose that the Debtor had used $40,000.00 of the refinancing proceeds to repay other creditors. Springer further conceded that the original Schedules did not disclose the $5,000.00 payment for the Tahoe vehicle. No satisfactory explanation was offered for these omissions.

III. APPLICABLE STANDARDS FOR OBJECTIONS TO DISCHARGE

The discharge provided by the Bankruptcy Code is to effectuate the "fresh start" goal of bankruptcy relief. In exchange for that fresh start, the Bankruptcy Code requires debtors to accurately and truthfully present themselves before the Court. A discharge is only for the honest debtor. In re Garman, 643 F.2d 1252, 1257 (7th Cir. 1980), cert. denied, 450 U.S. 910 (1981). Consequently, objections to discharge under 11 U.S.C. § 727 should be liberally construed in favor of debtors and strictly against objectors in order to grant debtors a fresh start. Soft Sheen Prods., Inc. v. Johnson (In re Johnson), 98 B.R. 359, 364 (Bankr. N.D. Ill. 1988) (citation omitted). Because denial of discharge is so drastic a remedy, courts may be more reluctant to impose it than to find a particular debt nondischargeable. See Johnson, 98 B.R. at 367 ("The denial of discharge is a harsh remedy to be reserved for a truly pernicious debtor.") (citation omitted). The plaintiff has the burden of proving the objection. See Fed. R. Bankr. P. 4005; In re Martin, 698 F.2d 883, 887 (7th Cir. 1983) (the ultimate burden of proof in a proceeding objecting to a discharge lies with the plaintiff). The objector must establish all elements by a preponderance of the evidence. In re Scott, 172 F.3d 959, 966-67 (7th Cir. 1999).

IV. DISCUSSION

A. 11 U.S.C. § 727(a)(2)

Pursuant to 11 U.S.C. § 727(a)(2)(A), the Court will grant the Debtor a discharge unless the Plaintiffs can prove by a preponderance of the evidence that the Debtor:

> (2) with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be transferred, removed, destroyed, mutilated, or concealed--
>
> (A) property of the debtor, within one year before the date of the filing of the petition. . . .

11 U.S.C. § 727(a)(2)(A).

Denial of discharge under this section requires proof of actual intent to hinder, delay or defraud a creditor. In re Snyder, 152 F.3d 596, 601 (7th Cir. 1998); In re Krehl, 86 F.3d 737, 743 (7th Cir. 1996);In re Smiley, 864 F.2d 562, 566 (7th Cir. 1989). "[P]roof of harm is not a required element of a cause of action under Section 727." Id. at 569. In determining whether a debtor has acted with intent to defraud under § 727, the Court should consider the debtor's "whole pattern of conduct." Bennett & Kahnweiler Assocs. v. Ratner (In re Ratner), 132 B.R. 728, 731 (N.D. Ill. 1991) (quoting In re Reed, 700 F.2d 986 (5th Cir. 1983)). The issue of a debtor's intent is a question of fact to be determined by the bankruptcy judge. See Smiley, 864 F.2d at 566.

Actual fraudulent intent can be inferred from extrinsic evidence. Id.; Krehl, 86 F.3d

at 743; Filmar, Inc. v. White (In re White), 63 B.R. 742, 744 (Bankr. N.D. Ill. 1986) ("a debtor is unlikely to directly testify that his intent was fraudulent, the court may deduce fraudulent intent from all the facts and circumstances of a case"). "Thus, where the evidence on the intent question is such that two permissible conclusions may rationally be drawn, the bankruptcy court's choice between them will not be viewed as clearly erroneous." Krehl, 86 F.3d at 744 (citation omitted). "Intent to defraud involves a material representation that you know to be false, or, what amounts to the same thing, an omission that you know will create an erroneous impression." In re Chavin, 150 F.3d 726, 728 (7th Cir. 1998) (citations omitted).

Perhaps most egregious is the omission in the Debtor's Statement of Financial Affairs of numerous prepetition payments made to creditors, both in answer to Questions 3a and 3b. Most significant are the omitted payments to insiders. The original Schedules disclosed no payments to insiders whatsoever within the year prior to filing. See Debtor's Exhibit No. 1 and Creditor's Exhibit No. 1. Yet, the relevant addendum to the amended Schedules details over $40,000.00 in insider payments. See Debtor's Exhibit No. 2. Similarly, the Creditor points out that the Debtor's response to Question 4 was incomplete wherein he listed only two pending lawsuits. By contrast, the amended Schedules disclosed four pending lawsuits at the time the bankruptcy petition was filed. Moreover, the Creditor states that the answer to Question 7 was inadequate because the Debtor failed to itemize gifts to Ms. Guerrero and others, including Pepple, and that his response to Question 10 failed to list the transfer of property which included the $5,000.00 down payment he made on behalf of Pepple to the car dealer for the Tahoe motor vehicle. The Court concludes that all of these are significant

omissions which constitute concealment of property of the Debtor within one year before the date of the filing of the petition. The Debtor's testimony that although he failed to disclose these matters in his original Schedules, he did so at the § 341 meeting does not vitiate the glaring falsity and inaccuracy of the original Schedules and Statement of Financial Affairs.

According to the Debtor, there were some items that should have been more fully addressed on the Schedules, but the items not fully explained in the original Schedules were disclosed and documented at the § 341 meeting and the subsequent document production requested. The Debtor places strong reliance on in In re Doody, 92 F.2d 653 (7th Cir. 1937) for the proposition that when a transaction is revealed at the § 341 meeting there is no fraudulent concealment. In dicta, the Doody court stated concerning an alleged fraudulent transfer almost three years prepetition:

> The only secrecy . . . was the fact that the . . . deeds were never recorded. It may be said, however, that at the first meeting of creditors the bankrupt fully disclosed the transaction, and at the referee's hearing on appellant's objections to the discharge, the bankrupt fully described the entire transaction. . . . Under these circumstances we think there was no error in hold that there was neither trust nor fraudulent concealment proved.

Id. at 655 (citation omitted).

The evidence adduced in this matter is uncertain and conflicting on just what the Debtor disclosed at the § 341 meeting. It is abundantly clear, however, that the Debtor's original Schedules and Statement of Financial Affairs concealed many insider transfers and other material matters within the year prior to filing. Thus, the Doody case is inapposite to the matter at bar.

Inasmuch as the Debtor's testimony is at odds with the Trustee's recollection of what was disclosed at the § 341 meeting, the Court finds the Trustee more credible than the Debtor. This is in part because of the significant aggregate material omissions and deficiencies in the Schedules and Statement of Financial Affairs. The Debtor contends that the amended Schedules show that any initial omissions were inadvertent. If that is so, why did the Debtor wait until almost the eve of trial to amend? No credible explanation was forthcoming from the Debtor regarding the inordinate delay. The Debtor's eleventh hour amendments and somewhat protracted and piecemeal responses furnished per the Trustee's document request do not sufficiently or satisfactorily explain the material omissions in the original Schedules and Statement of Financial Affairs, which were filed months after he began consulting with attorneys.

The Creditor contends that the Debtor misrepresented the transfer of his interest in AMLLC to Osterle in December 1996, as disclosed on Schedule B, but at trial admitted that at all relevant times until April 1998, he was a member of that company in order to be its manager. See Creditor's Exhibit Nos. 11 and 12. The Creditor also contends that the Debtor falsely represented in his original Schedules that he had made a prepetition transfer of his shares in USB to Osterle. According to Osterle's testimony, the Debtor was the chief operating officer of that corporation and he kept the books and records for USB. Osterle testified that he never received the purported transfer of the shares from the Debtor. The Court found Osterle's testimony generally more credible than the Debtor's version of his dealings with Osterle.

With regard to the Debtor's home refinancing disclosed on his Schedule A, the

Debtor testified that he had brought his checkbook register to the § 341 meeting to review the individual payments that had been paid out refinancing proceeds. The Debtor's attorney and the Trustee did not recall whether the Debtor brought his checkbook register to the § 341 meeting.

The Court finds for the Plaintiffs on this point as the documentary evidence shows that as a matter of public record, the Debtor's interest therein was not transferred until over three months post-petition, not over a year prepetition. The transfers, as subsequently disclosed in the amended Schedules, reveal a pattern of multiple concealed transfers, and the Court is not satisfied that the Debtor has provided a credible, satisfactory or timely explanation. Consequently, the Debtor's discharge is denied under § 727(a)(2)(A).

B. 11 U.S.C. § 727(a)(3)

Section 727(a)(3) of the Bankruptcy Code provides as follows:

> (a) The court shall grant the debtor a discharge, unless--
>
> > (3) the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or preserve any recorded information, including books, documents, records, and papers, from which the debtor's financial condition or business transactions might be ascertained, unless such act or failure to act was justified under all of the circumstances of the case.

11 U.S.C. § 727(a)(3).

The statute places an affirmative duty on the debtor to create books and records accurately documenting his business affairs. In re Juzwiak, 89 F.3d 424, 429 (7th Cir. 1996) ("The debtor has the duty to maintain and retain comprehensible records.") (citations

omitted). To prevail under the complaint, the Plaintiffs must prove that the Debtor failed to keep adequate records. Bay State Milling Co. v. Martin (In re Martin), 141 B.R. 986, 995 (Bankr. N.D. Ill. 1992); Calisoff v. Calisoff (In re Calisoff), 92 B.R. 346, 356 (Bankr. N.D. Ill. 1988). "Section 727(a)(3) does not require proof of criminal or quasi-criminal conduct; rather, a transfer or removal of assets, a destruction or other wasting of assets, or a concealment of assets is all the trustee must prove." Scott, 172 F.3d at 969. Intent is not an element of proof under § 727(a)(3). Juzwiak, 89 F.3d at 430. ("creditors do not need to prove that the debtor intended to defraud them in order to demonstrate a § 727(a)(3) violation"). Every debtor has a duty to take reasonable precautions to maintain and preserve records of their financial transactions and affairs. Brandt v. Carlson (In re Carlson), 231 B.R. 640, 654 (Bankr. N.D. Ill. 1999) (citation omitted). The purpose of § 727(a)(3) is "to make the privilege of discharge dependent on a true presentation of the debtor's financial affairs." Scott, 172 F.3d at 969. This statute ensures "that trustees and creditors will receive sufficient information to enable them to 'trace the debtor's financial history; to ascertain the debtor's financial condition; and to reconstruct the debtor's financial transactions.'" Juzwiak, 89 F.3d at 427-28 (quoting Martin, 141 B.R. at 995) (citations omitted). The creditors and the trustee are not required to accept a debtor's oral recitations or recollections of his transactions; rather to quality for a discharge in bankruptcy, a debtor is required to keep and produce written documentation of all such transactions. Id. at 429-30.

"Records are not 'adequate' if they do not provide the trustee or creditors with enough information to ascertain the debtor's financial condition and track his financial dealings with substantial completeness and accuracy for a reasonable period past to present."

Martin, 141 B.R. at 995 (citations omitted). The completeness and accuracy of a debtor's records are to be determined on a case-by-case basis, considering the size and complexity of the debtor's business. Community Bank of Homewood-Flossmoor v. Bailey (In re Bailey), 145 B.R. 919, 924 (Bankr. N.D. Ill. 1992) (citations omitted). The Court should consider the sophistication of the Debtor, his business experience, and other relevant circumstances. Calisoff, 92 B.R. at 356 (citation omitted).

The Creditor concludes for purposes of § 727(a)(3) that the Debtor failed to preserve records from which his financial status could be determined as shown by the Debtor's admission that he did not have records for Historic, USB, AMLLC or AMI, even though he was the chief financial and operating officer for those entities at some points in time. Likewise, the Debtor failed to produce records regarding his Discover credit card debt, documentation regarding the Internal Revenue debt scheduled in excess of $80,000.00 and the title to the 1990 Bronco motor vehicle. The Creditor thus concludes that the Debtor failed to meet his required duty to take reasonable precautions to maintain and preserve records of his financial transactions and affairs.

The Court overrules this objection for several reasons. It is the Debtor, personally, who is the bankrupt, not any of those business entities. Thus, his failure to produce all their books and records is not fatal to his personal discharge, per se. Moreover, his involvement with these various entities has changed from time to time and some may now be either inactive corporate shells or entities over whose books and records he no longer exercises effective control. Furthermore, the Debtor's failure to produce statements and purchase receipts on his credit card account, the title to a nine year old motor vehicle, and whatever

unpaid tax claims the taxing authorities may or may not be asserting against him personally, did not obstruct the Court, the Trustee or the Creditor from reviewing the records that were produced by him in order to reasonably, albeit imperfectly, understand his financial history. What was furnished the Plaintiffs enabled them and the Court to piece together the somewhat complicated, and at times confusing, past involvement of the Debtor with the various businesses and his personal finances and banking account activities. Thus, the Court finds in favor of the Debtor and overrules the Creditor's objection to discharge under § 727(a)(3).

C. 11 U.S.C. § 727(a)(4)(A)

Section 727(a)(4)(A) provides:

> (a) The court shall grant the debtor a discharge, unless--
> (4) the debtor knowingly and fraudulently, in or in connection with the case–
> (A) made a false oath or account.

11 U.S.C. § 727(a)(4)(A). The purpose of § 727(a)(4) is to enforce a debtor's duty of disclosure and to ensure that the debtor provides reliable information to those who have an interest in the administration of the estate. Carlson, 231 B.R. at 655; Bensenville Community Center Union v. Bailey (In re Bailey), 147 B.R. 157, 163 (Bankr. N.D. Ill. 1992) (citations omitted).

In order to prevail, the Plaintiffs must establish five elements under § 727(a)(4)(A): (1) the Debtor made a statement under oath; (2) the statement was false; (3) the Debtor knew the statement was false; (4) the Debtor made the statement with the intent to deceive; and (5) the statement related materially to the bankruptcy case. Bailey, 147 B.R. at 162 (citations omitted). If made with the requisite fraudulent intent, a false statement, whether made in the

schedules or orally at a § 341 creditors' meeting is sufficient grounds for denying a discharge provided it was knowingly made and is material. Armstrong v. Lunday (In re Lunday), 100 B.R. 502, 508 (Bankr. D. N.D. 1989). It is a debtor's role to consider the questions posed on the schedules and at the creditors' meeting carefully, and answer them accurately and completely. Id.

In In re Yonikus, 974 F.2d 901 (7th Cir. 1992), the Seventh Circuit held that a debtor's failure to list a pre-petition personal injury and worker's compensation claim on his schedules constituted grounds for revocation of the debtor's discharge (the Yonikus trustee sought to revoke debtor's discharge under 11 U.S.C. § 727(d)(2), the post-discharge equivalent to § 727(a)(4)(A)). In rejecting the debtor's argument that the worker's compensation award was exempt and the personal injury claim was property of his employer and not him, the court stated, "[d]ebtors have an absolute duty to report whatever interests they hold in property, even if they believe their assets are worthless or are unavailable to the bankruptcy estate." Id. at 904 (citations omitted).

Turning to the matter at bar, the Plaintiffs first must establish that the Debtor made a statement under oath. A debtor's petition and schedules constitute a statement under oath for purposes of a discharge objection under § 727(a)(4). See Nof v. Gannon (In re Gannon), 173 B.R. 313, 320 (Bankr. S.D. N.Y. 1994) (citations omitted). The Schedules and Statement of Financial Affairs filed by the Debtor constitute statements under oath. Hence, there is no dispute that this element has been met.

Second, the Plaintiffs must show that such statements were false. Whether the Debtor made a false oath within the meaning of § 727(a)(4)(A) is a question of fact.

Williamson v. Fireman's Fund Ins. Co., 828 F.2d 249, 251 (4th Cir. 1987); Continental Ill. Nat. Bank & Trust Co. of Chicago v. Bernard (In re Bernard), 99 B.R. 563, 570 (Bankr. S.D. N.Y. 1989) (citing Williamson). "Filing of false schedules with material omissions or misrepresentations with an intent to mislead creditors and the trustee as to a debtor's actual financial condition constitutes a false oath under section 727(a)(4)(A)." Britton Motor Serv., Inc. v. Krich (In re Krich), 97 B.R. 919, 923 (Bankr. N.D. Ill. 1988) (citation omitted). Subsequent voluntary disclosure through testimony or amendment to the schedules does not expunge the falsity of the oath. Bailey, 147 B.R. at 165 (citation omitted).

The focus of the Creditor's arguments relates to the inaccuracies in and omissions from the Debtor's original Schedules and Statement of Financial Affairs. The Debtor admittedly reviewed these documents prior to filing and made changes on the preliminary drafts. He had several months prepetition, after retaining counsel, to prepare true and correct Schedules. As illustrative of the falsity and inaccuracy of the Schedules, the Creditor points to the Debtor's checking account which was scheduled as having $100.00 in the account as of the petition filing date. Yet the Debtor's bank statement showed on January 16, 1998, the day after filing, that the Debtor had an ending balance in the account of $2,270.98. See Creditor's Exhibit No. 3, p. 9. The Debtor's defense is that he relied on his check register (Debtor's Exhibit No. 20, last page) not the bank statement in making that entry on his original Schedule B. This is an understandable explanation, so the Court cannot find for the Creditor on this point.

Next, the Creditor points out that less than a week before the petition was filed, the Debtor was supposedly given a check in the amount of $5,000.00 from Osterle dated January

9, 1998. See Creditor's Exhibit No. 21, p. 8. This sum was not disclosed on the Schedules.

The Creditor also points out that the Debtor valued his home at $175,000.00 on Schedule A, although he had previously valued his home at $250,000.00; (Creditor's Exhibit No. 19 declaration page of the Debtor's homeowner's insurance policy); $210,000 (Creditor's Exhibit No. 9, 1997 loan application, p. 2); and $187,000.00 (Creditor's Exhibit No. 20, real estate appraisal dated June 24, 1997). According to the Debtor, the evaluation of his home was essentially a matter of opinion, and the value listed in the Schedules was fairly accurate and more in accord with the appraisal of the bank that did the refinancing on the property.

The Creditor further contends that the Debtor undervalued his personal property on Schedule B by listing household goods at $1,000.00. This was in marked contrast to the $187,500.00 valuation listed on his homeowner's insurance (Creditor's Exhibit No. 19) and in his July 9, 1997 loan application of to the bank wherein the goods were valued at $10,000.00. See Creditor's Exhibit No. 9, p. 2. The Creditor further contends that the Debtor misstated the value of his Ford Bronco automobile at $1,000.00 on Schedule B, but listed it as having a $5,000.00 value on the loan application. See Creditor's Exhibit No. 9, p.2. Furthermore on Schedule B, the Debtor listed stone inventory as having an unknown fair market value (Addendum No. 1 to Schedule B), which is now being marketed for $112,500.00. See Debtor's Exhibit No. 18 (750 granite slabs priced at $150.00 each equals $112,500.00).

The Court is mindful that the valuation of real and personal property is a matter of opinion, sometimes subjective, and subject to change. The Court finds more problematical

the substantial variations in values between the amounts for those respective items in the loan application approximately six months prepetition from those listed in the Schedules. The Court concludes that the insufficient or unexplained differences tend to erode the Debtor's credibility and show the falsity of the latter Schedules because he made no satisfactory explanation for the substantially higher values he listed in July 1997 from those on the original Schedules in January 1998. Except for the high mileage and mechanical unreliability of the motor vehicle, and the fact that the stone inventory is still unsold and was abandoned by the Trustee, the substantial differences in the values for the home and the other items of personal property seriously calls into question the Debtor's credibility.

The Creditor further argues that the Debtor's Schedule B, Item 12 incorrectly valued his stock and interests in incorporated and unincorporated businesses as zero, and that he did not disclose that Historic had a $545,000.00 contract with AMLLC on the Moline Foundry project. See Creditor's Exhibit No. 16. The Creditor asserts that the Debtor had a duty to disclose this asset even though he was advised that the contract was invalid and thus worthless to the bankruptcy estate.

The Court is unpersuaded on these points regarding the value of the Debtor's interest in these various business entities inasmuch as the record is devoid of financial statements for any or all of the incorporated or unincorporated businesses. It is therefore impossible for the Court to determine from this record whether or not the Debtor's equity or other interest therein was worth zero, as his Schedules indicated, or something more. Moreover, if the disputed contract between Historic and AMLLC had value, it would have been of value only to those artificial entities, not the Debtor, if the legal fictions of separate corporate

partnership and/or limited liability company are to be adhered to. In the absence (as here) of any evidence with which to properly pierce those respective "corporate veils" and attribute the contract as an asset of the Debtor, which became a part of the bankruptcy estate under 11 U.S.C. § 541(a), the Court finds that the Debtor did not make a false oath regarding the value of his stock and interests in his various businesses.

The Creditor next turns to the Debtor's liabilities and asserts that they are overstated for several creditors. On Schedule D, the Debtor allegedly falsely claimed the liability on a piece of equipment. See Creditor's Exhibit No. 1, Schedule D, p. 1, item 2. The Creditor notes that the underlying debt is not owed by the Debtor but by Historic. See Creditor's Exhibit No. 18. In addition, the Creditor asserts that Schedule D lists a debt owed to Forrest Financial of $200,000.00, but that the actual debt was only $156,811.82 on which the Debtor is co-guarantor. See Creditor's Exhibit No. 24. Moreover, the Debtor inaccurately scheduled the Internal Revenue Service on Schedule E for nondischargeable federal income tax and withholding taxes in excess of $88,000.00. He admitted at trial there were no documents reflecting any tax liability in that regard, while pointing out that the tax debt was not listed on his July 9, 1997 financial statement (Creditor's Exhibit No. 9) in which the Debtor stated he was not delinquent or in default on any such obligation. The Creditor further contends that the Debtor failed to list all his liabilities on Schedule F, including debts to Osterle ($150,000-$180,000); AMLLC ($40,000); and Mr. Wherli ($18,000).

The Court finds that the Debtor's failure to disclose these liabilities on his Schedules constitutes a false oath. It is very telling against the Debtor for him to have omitted scheduling the unpaid indebtedness he owed Osterle, his friend and business associate, and

to AMLLC, the company of which he was a member and record manager until several months post-petition.

The Creditor further correctly points out that the Debtor failed to list all his occupations or employment and sources of income on Schedule I. Therein, he did not disclose he was also a licensed real estate broker, with a current Illinois real estate license; that he was chief operating officer for USB and received health insurance benefits as a result of his work there; and that he was president, secretary and registered agent for AMLLC. Failure to disclose those supplemental sources of income is sufficient to deny discharge. See Cole Taylor Bank v. Yonkers (In re Yonkers), 219 B.R. 227, 233-34 (Bankr. N.D. Ill. 1997). Moreover, the Creditor also correctly notes that the Debtor initially failed to disclose the leased Chevrolet Tahoe on which he made regular monthly payments for the mutual benefit of Pebble and himself.

In determining whether a debtor's discharge should be denied based on false oath or account, amendments of schedules do not expunge the falsity of the original petition or schedules even though a motion to amend has been granted by the court. See Gannon, 173 B.R. at 320; Golden Star Tire, Inc. v. Smith (In re Smith), 161 B.R. 989, 992 (Bankr. E.D. Ark. 1993) (filing corrected schedules only after the fraud was discovered did not cure the initial falsity of the schedules, or preclude denial of the debtors' discharge based on their "false oaths").

The Court cannot, in light of the conflicting testimony between the Debtor, the Trustee, and the Debtor's attorney regarding exactly what transpired at the § 341 meeting, in the absence of a transcript of that proceeding, determine that the Debtor timely cured the

obvious omissions and significant discrepancies in the original Schedules.

_____While the Court does not expect every individual item of clothing or piece of furniture to be scheduled and valued, or that each scheduled liability be listed with absolute arithmetic precision, there comes a point when the aggregate errors and omissions cross the line past which a debtor's discharge should be denied. Wherever that fine and elusive line is, the Court is of the view it has been crossed here. The Court can understand there may be an occasionally innocently omitted deminimus transfer by way of gift to a family member or friend. The omissions and disclosures from the instant Schedules, however, are simply too numerous and substantial to overlook or attribute to mere negligence or simple inadvertence on the part of the Debtor. He had several months to make complete disclosure to his attorney for the purpose of preparing fairly complete and reasonably accurate Schedules and Statement of Financial Affairs. Those documents filed in January 1998 were woefully inadequate, incomplete and disclosed absolutely no prepetition transfers to an insider.

Debtors sometimes intentionally omit assets from the schedules in order to conceal them. In such circumstances, the debtor can be denied a discharge either for concealing assets under § 727(a)(2) or for making a false oath under § 727(a)(4), or on both grounds. See R. Ginsberg and R. Martin, 1 Ginsberg & Martin on Bankruptcy § 11.02[E] at 11-31 (4th ed. 1999).

The Court observes there are some other significant differences between the Debtor's original and amended Schedules and answers to the questions on the Statement of Financial Affairs. For example, in his original Schedule A the Debtor merely listed his home with

values in amounts of secured claims. In his amended Schedule A, however, he detailed the application and disposition of the home refinancing proceeds received in July 1997. The amended Schedules included a new addendum to Schedule B listing the Debtor's various interests in incorporated and unincorporated businesses. Amended Schedule F listed three unsecured nonpriority creditors, AMLLC, Discover Card Services and Osterle totaling $221,200.00 in claims, in marked contrast to the seven different creditors whose claims were scheduled on the original Schedule F for a total of $141,400.00. The amended Schedule J discloses the previously undisclosed payment of $371.00 a month for the 1997 Tahoe motor vehicle. In his amended Statement of Financial Affairs, the answer to Question 4 (regarding suits and administrative proceedings to which the Debtor was a party within the one year preceding the filing of the bankruptcy case) increased from the two matters that were originally scheduled by the Debtor, including the Creditor's claim against the Debtor, to four suits including the previously undisclosed litigation against him brought by Old Kent Bank.

The Debtor cannot rely on the advice of counsel defense regarding errors in the Schedules where the Debtor has declared under penalty of perjury that he has read the Schedules, and to the best of his knowledge they were true and correct. See Morton v. Dreyer (In re Dreyer), 127 B.R. 587, 597-98 (Bankr. N.D. Tex. 1991). The Court has no doubt of the integrity and professionalism of the Debtor's lawyers and their long proven track record before the Court in many cases over the years.

Based on the foregoing, the Court finds that the Debtor made a false oath under § 727(a)(4)(A). His subsequent voluntary disclosure through testimony or amendment to the Schedules does not expunge the falsity of the oath.

Third, the Plaintiffs must establish that the false statements were knowingly made. Considering the totality of the evidence, in light of the Debtor's testimony and demeanor, the Court finds this element has been proven. The Debtor is an intelligent, experienced and articulate businessman who knew at all times his personal and business situation, and thus knew or should have known that his original Schedules were incomplete and incorrect as discussed above.

Fourth, the Plaintiffs must prove that the Debtor made the false statements with fraudulent intent. To find the requisite degree of fraudulent intent, the Court must find that the Debtor knowingly intended to defraud or engaged in behavior which displayed a reckless disregard for the truth. Yonikus, 974 F.2d at 905; Bailey, 147 B.R. at 165 (citing Yonikus). If a debtor's bankruptcy schedules reflect a "reckless indifference to the truth" then the plaintiff seeking denial of the discharge need not offer any further evidence of fraud. Calisoff, 92 B.R. at 355. The requisite intent under § 727(a)(4)(A) may be inferred from circumstantial evidence. Yonikus, 974 F.2d at 905 (citations omitted). However, discharge should not be denied where the untruth was the result of mistake or inadvertence. Lanker v. Wheeler (In re Wheeler), 101 B.R. 39, 49 (Bankr. N.D. Ind. 1989). When a debtor is in doubt concerning disclosure, it is unquestioned that he is obligated to disclose. See Bank of India v. Sapru (In re Sapru), 127 B.R. 306, 315-16 (Bankr. E.D. NY 1990) ("multitude" of false oaths and omissions were material and justified denial of discharge); Behrman Chiropractic Clinics Inc. v. Johnson (In re Johnson), 189 B.R. 985, 994-95 (Bankr. N.D. Ala. 1995) (failure to disclose transferred assets warranted denial of discharge).

The Court infers the requisite fraudulent intent from all of the circumstantial

evidence. The surrounding circumstances showed that the Debtor had close business or personal relationships with the insider transferees or beneficiaries of the transfers not disclosed in the original Schedules. At the very least he showed reckless disregard or indifference to the truth of his situation, which was untimely revealed. See Calisoff, 92 B.R. at 355; Croge v. Katz (In re Katz), 203 B.R. 227, 235 (Bankr. E.D. Pa. 1996) (existence of more than one falsehood, plus failure to clear up all inconsistencies when filing amendments may constitute a reckless disregard and be sufficient for denial for discharge).

There has been no showing that the subsequent disclosures and corrections were made spontaneously by the Debtor which might evidence nonfraudulent intent. Rather, the disclosures were made as the Trustee testified "in dribs and drabs"after her request for additional information subsequent to the § 341 meeting. The amended Schedules, which were filed on the eve of trial, have convinced the Court that the Debtor attempted to hide or improperly shield assets. The Court is not convinced that the Debtor has acted in good faith to explain his affairs and his continued involvement with some of the business entities from which he earns his livelihood.

Finally, the Plaintiffs must show that the statement related materially to the bankruptcy case. The debtor's false oath must relate to a material matter before it will bar a discharge in bankruptcy. In re Agnew, 818 F.2d 1284, 1290 (7th Cir. 1987) (citation omitted). The test for materiality of the subject matter of false oath is whether it "bears a relationship to the bankrupt's business transactions or estate, or concerns the discovery of assets, business dealings, or the existence and disposition of his property." Bailey, 147 B.R. at 162 (citations omitted). A false oath may be material even though it does not result in any

detriment or prejudice to the creditor. Scimeca v. Umanoff, 169 B.R. 536, 543 (D. N.J. 1993), aff'd, 30 F.3d 1488 (3d Cir. 1994); Congress Talcott Corp. v. Sicari (In re Sicari), 187 B.R. 861, 881 (Bankr. S.D. N.Y. 1994). The above discussed omissions from the Schedules and Statement of Financial Affairs are material to the bankruptcy case. Failure to disclose transfers to insiders, all sources of income, correct valuation of property, both real and personal, and failure to disclose liabilities hinder the administration of the estate and obfuscate the financial situation.

After considering the totality of the evidence, and having the benefit of hearing the testimony of the witnesses, the Court believes that there has been a preponderance of the evidence shown that the Debtor's discharge should be denied. In sum, the Court finds that the Plaintiffs have shown by a preponderance of the evidence each element under § 727(a)(4)(A). Therefore, the Court denies the Debtor's discharge.

D. 11 U.S.C. § 727(a)(5)

Section 727(a)(5) provides that "[t]he court shall grant the debtor a discharge, unless . . . the debtor has failed to explain satisfactorily . . . any loss of assets or deficiency of assets to meet the debtor's liabilities. . . ." 11 U.S.C. § 727(a)(5). "Section 727(a)(5) is broadly drawn and clearly gives a court broad power to decline to grant a discharge in bankruptcy where the debtor does not adequately explain a shortage, loss, or disappearance of assets." Martin, 698 F.2d at 886 (citations omitted). There are two stages of proof with respect to § 727(a)(5). Banner Oil Co. v. Bryson (In re Bryson), 187 B.R. 939, 955 (Bankr. N.D. Ill. 1995). First, the party objecting to discharge has the burden of proving that the debtor at one time owned substantial and identifiable assets that are no longer available for his creditors.

Id. (citation omitted). Second, if the party objecting to the discharge meets its burden, then the debtor is obligated to provide a satisfactory explanation for the loss. Id. (citation omitted).

What constitutes a "satisfactory" explanation for § 727(a)(5) purposes is left to the discretion of the Court. Baum v. Earl Millikin, Inc., 359 F.2d 811, 814 (7th Cir. 1966); Olson v. Potter (In re Potter), 88 B.R. 843, 849 (Bankr. N.D. Ill. 1988). The debtor's explanation, however, must consist of more than "a vague, indefinite, and uncorroborated hodgepodge of financial transactions." Baum, 359 F.2d at 814. Instead, "it must be a good faith explanation of what really happened to the assets in question." Potter, 88 B.R. at 849. "To be satisfactory, the explanation must demonstrate the debtor has exhibited good faith in conducting his affairs and explaining the loss of assets." Martin, 141 B.R. at 999 (citations omitted). A debtor "cannot abuse the bankruptcy process by obfuscating the true nature of his affairs and then refusing to provide a credible explanation." Johnson, 98 B.R. at 366 (quoting Martin, 698 F.2d at 888).

The Court finds in favor of the Debtor on this theory. He testified that he was living from day to day teetering on the edge of insolvency for quite some time due to the nature and risks attendant to his construction businesses. The Debtor turned over substantial documents to the Trustee pursuant to her request. There was no convincing testimony or documentary evidence to establish that the Debtor's past and present business activities were not fully explored by the Plaintiffs or explained. Indeed, it was from the materials furnished by the Debtor to the Trustee that the Creditor was able to unearth and later prove the material deficiencies and omissions in the original Schedules and Statement of Financial Affairs,

which have given rise to the successful objections based on §§ 727(a)(2)(A) and (a)(4)(A). There has not been a requisite showing by the Plaintiffs that the Debtor at one time owned substantial assets that are no longer available for his creditors, nor is the Court convinced that the Debtor has not adequately explained his inability to pay his debts.

V. CONCLUSION

For the foregoing reasons, the Court hereby grants judgment, in part, in favor of the Plaintiffs. The Debtor's discharge is denied and the objections thereto pursuant to § 727(a)(2)(A) and § 727(a)(4)(A) are sustained. The objections under § 727(a)(3) and § 727(a)(5) are overruled. The Court denies the Debtor's motion for directed findings.

This Opinion constitutes the Court's findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052. A separate order shall be entered pursuant to Federal Rule of Bankruptcy Procedure 9021.

ENTERED:

DATE: _____

John H. Squires
United States Bankruptcy Judge

cc: See attached Service List