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The Holy Grail a/k/a The Bankruptcy Discharge: How to Protect It and How to Get It Denied

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INTRODUCTION

The "principle purpose of the Bankruptcy Code is intended to give a 'fresh start' to the 'honest but unfortunate debtor."[2] Two hurdles a Chapter 7 debtor must overcome on the way to a successful conclusion of his or her case are found in Sections 523 and 727of the Bankruptcy Code. While Section 727 operates to protect the integrity of the bankruptcy process by imposing the denial of discharge for certain acts and omissions of the debtor, Section 523 deals with the dischargeability of individual debts. This article will examine the concepts of discharge and dischargeability for Chapter 7 debtors, beginning first with a review of Section 523.

PART I

EXCEPTIONS TO DISCHARGE IN CHAPTER 7 UNDER 11 U.S.C. § 523

The exceptions to discharge in Chapter 7 cases[3] are found in Section 523 of the Bankruptcy Code.[4] This writing will address some procedural issues and then discusses in turn each of the nineteen paragraphs in Section 523(a).

PROCEDURAL ISSUES

Section 523(c)[5] divides the debts in Section 523(a) into two categories. The first

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[2] *Marrama v. Citizens Bank*, 549 U.S. 365, 367 (U.S. 2007) citing *Grogan v. Garner*, 498 U.S. 279, 286, 287, (1991).

[3] *See* Section 727 (b).

[4] Herein, the word "Section" refers to the associated section in the Bankruptcy Code, 11 U.S.C. 101, et. seq.

[5] Section 523(c) provides:

> (1) Except as provided in subsection (a)(3)(B) of this section, the debtor shall be discharged from a debt of a kind specified in paragraph (2), (4), or (6) of subsection (a) of this section, unless, on request of the creditor to whom such debt is owed, and after notice and a hearing, the court determines such debt to be excepted from discharge under paragraph (2), (4), or (6), as the case may be, of subsection (a) of this section.
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> (2) Paragraph (1) shall not apply in the case of a Federal depository institutions regulatory agency

category includes Subsections 523(a)(2),(4), and (6). The second category includes all of the other Subsections in Section 523(a).

Section 523(c)(1) provides that debts that fall in the first category, Subsections 523(a)(2), (4), and (6), shall be discharged unless the court determines otherwise.[6] If a creditor seeks to except from discharge a debt of the kind described in Sections 523(a)(2), (a)(4), or (a)(6), the creditor must file an adversary complaint.[7]

In a Chapter 7 or Chapter 13 case, with one exception noted in the next paragraph, the deadline for filing a complaint objecting to a discharge of the debts specified in Subsections 523(a)(2), (4), and (6) is the date that is no later than 60 days after the first date set for the meeting of creditors under Section 341(a).[8] The court shall give all creditors no less than 30 days' notice of the time so fixed. If a party in interest files a motion to extend the deadline before the deadline has expired, the court may extend the deadline for cause.[9]

In a Chapter 13 case, the deadline for the filing of a complaint objecting to a discharge under Section 523(a)(6) is different from that described in the preceding paragraph. On motion

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seeking, in its capacity as conservator, receiver, or liquidating agent for an insured depository institution, to recover a debt described in subsection (a)(2), (a)(4), (a)(6), or (a)(11) owed to such institution by an institution-affiliated party unless the receiver, conservator, or liquidating agent was appointed in time to reasonably comply, or for a Federal depository institutions regulatory agency acting in its corporate capacity as a successor to such receiver, conservator, or liquidating agent to reasonably comply, with subsection (a)(3)(B) as a creditor of such institution-affiliated party with respect to such debt.

[6] The only exception occurs when the creditor is a "Federal Depository institutions regulatory agency," as defined in Section 101(21B). See Section 523(c)(2).

[7] F.R.B.P. 7001(6)

[8] F.R.B.P. 4007(c).

[9] *Id.*

by a debtor for a discharge under Section 1328(b),[10] the court shall enter an order fixing the time to file a complaint to determine the dischargeability of any debt under Section 523(a)(6) and shall give no less than 30 days' notice of the time fixed to all creditors.[11] If a party in interest files a motion to extend the deadline before the deadline has expired, the court may extend the deadline for cause.

All other debts described in Section 523(a) are non-dischargeable without a court proceeding. These other Subsections are self-executing; creditors are not required to obtain a judgment from the court for these types of debts to be non-dischargeable. This follows by negative implication from Section 523(c)(1), which requires the filing of an adversary proceeding to establish that a debt is non-dischargeable under Section 523(a)(2), (a)(4), or (a)(6). This does not, however, prevent a debtor from filing a complaint regarding debts described in the Subsections other than Subsections 523(a)(2), (a)(4), or (a)(6) in order to obtain a "comfort" judgment discharging the debt.

TAXES

The rules and tests for the discharge of income taxes in bankruptcy derive from a combination of Bankruptcy Code sections, including Section 523 (exceptions to discharge) and Section 507 (priority claims).[12] Section 523(a)(1)(A) excepts from discharge under Section 727 those priority tax claims covered under Section 507(a)(8).[13]

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[10] The discharge offered under 11 U.S.C. 1328(b) is commonly referred to as a hardship discharge.

[11] F.R.B.P. 4007(d).

[12] While this article focuses on the discharge of federal income taxes, the analysis and the "rules" described herein are the same for state income taxes.

The remaining subsections of Section 523(a)(1) are not related to whether the claim is priority but describe other circumstances where the taxes would be excepted from discharge. Section 523(a)(1)(B) makes nondischargeable a tax for which the return was either not filed or was filed late and less than two years prior to the petition date. Section 523(a)(1)(C) makes a tax nondischargeable if the taxpayer made a fraudulent return or willfully attempted in any manner to evade or defeat such tax.

The two-year period begins when the debtor files a return. A split among the circuits, however, has developed as to whether a late-filed return may be considered a tax return for purposes of dischargeability. While beyond the scope of this outline,[14] the rulings are based on the hanging paragraph to Section 523(a) added by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 and interpret the language to define "return" to exclude any taxpayer filing that does not strictly comply with all return filing requirements, including timeliness.[15]

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[13] Bankruptcy Code § 507(a)(8) assigns 8th priority to income taxes filed or assessed within specified timeframes. Taxes entitled to 8th priority would include: (1) taxes for which the return was last due within three years of the petition date, and (2) taxes assessed within 240 days before the date of the filing of the petition.

[14] For further development of this issue, please refer to the SBLI consumer tax materials from this year's conference.

[15] 11 USC § 523(a) (hanging paragraph), states:

> For purposes of this subsection, the term "return" means a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements). Such term includes a return prepared pursuant to section 6020(a) of the Internal Revenue Code of 1986, or similar State or local law, or a written stipulation to a judgment or a final order entered by a nonbankruptcy tribunal, but does not include a return made pursuant to section 6020(b) of the Internal Revenue Code of 1986, or a similar State or local law.

Bankruptcy Code Section 523(a)(1)(C) excepts from Chapter 7 and 13 discharges any debt for a tax "with respect to which the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat such tax." In determining whether the debtor filed a fraudulent return, courts consider badges of fraud, including (1) large understatements of income made consistently over time; (2) failure to keep adequate records; (3) failure to file tax returns; (4) implausible or inconsistent behavior by the taxpayer; (5) concealing assets; and (6) failure to cooperate with taxing authorities.[16]

FALSE PRETENSES, FALSE REPRESENTATION AND ACTUAL FRAUD

Section 523(a)(2)[17] excepts three categories of debts from the discharge of an individual

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[16] *Berkery v. Commissioner*, 192 B.R. 835, 841 (E.D.Pa.1996).

[17] Section 523(a)(2) provides:

> (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—
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> . . .
>
> (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;
>
> (B) use of a statement in writing—
>
> (i) that is materially false;
>
> (ii) respecting the debtor's or an insider's financial condition;
>
> (iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and
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> (iv) that the debtor caused to be made or published with intent to deceive; or
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> (C)
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> (i) for purposes of subparagraph (A)—
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> (I) consumer debts owed to a single creditor and aggregating more than $500 for luxury goods or services incurred by an individual debtor on or within 90 days before the order for relief under this title are presumed to be nondischargeable; and
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> (II) cash advances aggregating more than $750 that are extensions of consumer credit under an open end credit plan obtained by an individual debtor on or within 70 days before the order for relief under this title, are presumed to be nondischargeable; and
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> (ii) for purposes of this subparagraph—
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> (I) the terms "consumer", "credit", and "open end credit plan" have the same meanings as in section 103 of the Truth in Lending Act; and
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> (II) the term "luxury goods or services" does not include goods or services reasonably necessary for the support or maintenance of the

debtor. First, Section 523(a)(2)(A) provides that a debt is nondischargeable if it is for money, property, services or an extension renewal, or financing of credit to the extent obtained by false pretenses, false representation, or actual fraud, other than a statement respecting the debtor's or other insider's financial condition. Under this paragraph a plaintiff must prove the common law elements of fraud. In *Field v. Mans*, the Supreme Court held: "The operative terms in § 523(a)(2)(A)...'false pretenses, a false representation, or actual fraud,' carry the acquired meaning of terms of art. They are common law terms, and... they imply elements that the common law has defined them to include." [18] The Court further stated, "Then, as now, the most widely accepted distillation of the common law of torts was the Restatement (Second) of Torts (1976), published shortly before Congress passed the Act."[19] The Court continued, "We construe the terms in § 523(a)(2)(A) to incorporate the general common law of torts, the dominant consensus of common-law jurisdictions, rather than the law of any particular state."[20]

In order to prevail on a claim for false pretenses, false representation, or actual fraud, the plaintiff must show that (1) the debtor made a representation, (2) the debtor knew the representation was false, (3) the representation was made with the intent to deceive the creditor, (4) the creditor actually and justifiably relied on the representation,[21] and (5) the creditor

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debtor or a dependent of the debtor;

[18] *Field v. Mans*, 516 U.S. 59, 69, 116 S.Ct. 437, 443, 133 L.Ed.2d 351 (1995).

[19] *Id.*, 516 U.S. at 70, 116 S.Ct. at 443-444.

[20] *Id.*, at footnote 9.

[21] For discussions on justifiable reliance, see *In re Trejo*, 2012 WL 6622617 (9th Cir. B.A.P. 2012) *and In re Sears*, 533 Fed. Appx. 941 (11th Cir. 2013)

sustained a loss as a proximate result of its reliance.[22] Each element must be proved by a preponderance of the evidence.

For purposes of Section 523(a)(2)(A), a debtor's intent to deceive is measured subjectively. This only requires that the debtor knew or should have known that the false representation would induce the creditor to advance goods or services. The debtor's intent to deceive may be inferred from a reckless disregard for the truth or falsity of a statement in light of the magnitude of the misrepresentation.[23]

Fraud by one spouse is not necessarily imputed to the other spouse, regardless of whether the second spouse knew of the fraud.[24] If there are two debtors who are partners and one of them commits a fraudulent act, the act may be imputed to the other partner if it is proved that the innocent partner knew or should have known of his partner's fraud. Reckless indifference on the part of the innocent partner is sufficient evidence to show that the innocent partner should have known of the fraud.[25]

In 2016, the Supreme Court considered the definition of "obtained by actual fraud" under Section 523(a)(2)(A).[26] The Court noted that in 1978, Congress added "actual fraud" to "false pretenses or false representations" and concluded that Congress did not intend that "actual fraud" mean the same thing as the already-statutory "false pretenses." From this, the Court concluded

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[22] *In re Ayesh,* 2011 WL 672289 (Bankr. S.D. Tex. 2011). *Also see, In re Acosta,* 406 F.3d 367 (5th Cir. 2005) and *In re Davis,* 638 F.3d 549 (7th Cir. 2011)

[23] *In re Krupp,* 2013 WL 5745274 (E.D. Mich. 2013). *Also see, In re Johnson,* 477 B.R. 156 (10th Cir. B.A.P. 2011).

[24] *In re Lemke,* 423 B.R. 917 (10th Cir. B.A.P. 2010).

[25] *In re Treadwell,* 637 F.3d 855 (8th Cir., March 9, 2011).

[26] *Husky Int'l Elecs., Inc. v. Ritz,* — S. Ct. —, 2016 WL 2842452 (2016).

that "actual fraud" included fraudulent conveyance schemes even when those schemes do not involve a false representation.

Section 523(a)(2)(B) provides that a debt is nondischargeable if it was obtained by the use of a statement in writing (I) that is materially false; (ii) respecting the debtor's or an insider's financial condition; (iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied;[27] and (iv) that the debtor caused to be made or published with intent to deceive.

Each of the elements of this section must also be met by a preponderance of the evidence for the debt to be non-dischargeable. Minor inaccuracies in a written financial statement will not suffice; a statement in writing that does not describe the debtor's financial circumstances will not result in non-dischargeability.[28] An assignee of a debt may bring a cause of action under Section 523(a)(2)(B) based on misrepresentations made by the debtor to the original assigning creditor.[29] An assignee need not show that it relied on the original misrepresentations in order to prevail, if it can demonstrate that the original creditor did so rely.[30]

The third category, found in Section 523(a)(2)(C), concerns certain consumer debts and

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[27] Under Section 523(a)(2)(B), the standard for reliance is reasonable reliance. *See, e.g., In re Davenport*, 508 Fed. Appx. 937 (11th Cir. 2013).

[28] The phrase "a statement respecting the debtor's or an insider's financial condition" is to be interpreted as used in a commercial context, not as a broadly descriptive phrase intended to include any misrepresentation that pertains vaguely to assets or liabilities of the debtor. *In re Band*, 683 F.3d 671 (5th Cir., June 12, 2012). *Also see, In re Belice*, 461 B.R. 564 (9th Cir. B.A.P. 2011) (The phrase "a statement respecting the debtor's or an insider's financial condition" is to be interpreted narrowly.*)* *And see, In re Kosinski*, 424 B.R. 599 (1st Cir. B.A.P. 2010). (Although a statement of the debtor's or insider's financial condition does not need to be a formal statement, it must provide a statement regarding either a representation of an entity's overall net worth or an entity's overall ability to generate income. A profit and loss statement for a single year does not suffice.)

[29] *In re Pazdzierz*, 718 F.3d 582 (6th Cir. 2013).

[30] *In re Boyajian*, 564 F.3d 1088 (9th Cir. 2009).

cash advances. It provides that (1) consumer debts owed to a single creditor and aggregating more than $675 for luxury goods or services incurred by an individual debtor on or within 90 days before the order for relief, and (2) cash advances aggregating more than $950 that are extensions of consumer credit under an open end credit plan obtained by an individual debtor on or within 70 days before the order for relief, are presumed to be non-dischargeable.[31]

DEBTS OWED TO UNSCHEDULED CREDITORS

Section 523(a)(3)[32] provides two rules regarding nondischargeability, one for each of the two categories that were noted in the earlier discussion concerning Section 523(c), that is, the category that includes the debts described in Paragraphs 523(a)(2), (a)(4) and (a)(6) and the category that includes the debts described in the other paragraphs in Section 523(a).

Section 523(a)(3)(A) provides that an individual debtor is not discharged from the debts described in all paragraphs other than paragraphs (2), (4), and (6) of Subsection 523(a), if the debt is neither listed nor scheduled[33] in time to permit the creditor to timely file a proof of claim

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[31] These dollar amounts were last adjusted pursuant to Section 104(a) on April 1, 2016.

[32] Section 523(a)(3) provides:

> (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—
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> . . .
>
> (3) neither listed nor scheduled under section 521(a)(1) of this title, with the name, if known to the debtor, of the creditor to whom such debt is owed, in time to permit—
>
> (A) if such debt is not of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim, unless such creditor had notice or actual knowledge of the case in time for such timely filing; or
>
> (B) if such debt is of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim and timely request for a determination of dis-chargeability of such debt under one of such paragraphs, unless such creditor had notice or actual knowledge of the case in time for such timely filing and request;

[33] In *In re Meadows*, 428 B.R. 894 (Bankr. N.D. Ga. 2010), the Court held that section 523(a)(3) was not available to the creditor landlord where the debtors listed the landlord as a creditor even though they did not schedule the unsecured debt owed to the landlord.

unless the creditor had notice or actual knowledge of the case in time to timely file a proof of claim. If a debt is neither listed nor scheduled, but the creditor's right to receive a distribution is not affected because the case was a no-asset, no bar date, Chapter 7 case, then the debt is not excepted from discharge.[34]

Courts have adopted two different approaches under Section 523(a)(3)(A) in cases where the creditor receives late notice of the filing of a Chapter 7 asset case. Under the "plain language"[35] approach, the court will conclude that the debt is nondischargeable without further consideration. Under the "distribution" approach,[36] the court will conclude that the debtor is non-dischargeable only if the creditor is unable to receive a pro rata distribution under Section 726(a)(2)(C), which provides for distribution to a creditor that files a late claim.

Section 523(a)(3)(B) provides that an individual debtor is not discharged from the debts described in paragraphs (2), (4), and (6) of Subsection 523(a), if the debt is neither listed nor scheduled in time to permit the creditor to timely file a timely proof of claim and timely request a determination of dischargeability of such debt, unless the creditor had notice[37] or actual knowledge of the case in time to timely file a proof of claim and timely request a determination of dischargeability. In essence, Section 523(a)(3) provides an exception to the deadlines provided by Section 523(c) and Rule 4007. If the creditor benefits from the rule in Section 523(a)(3)(B), and is permitted to file an adversary complaint after the deadline, the creditor must still

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[34] *See, e.g., In re Smolarick,56* B.R. 720, 733 (Bankr. W.D. Va. 1986). *Also See* Judge O'Scannlain's concurring opinion in *In re Beezley*, 994. F.2d 1433 (1993).

[35] *See, e.g., In re Romano*, 59 Fed. Appx. 709 (6th Cir. 2003).

[36] *See, e.g., In re Kuhr*, 132 B.R. 421 (Bankr. E.D. Cal. 1991).

[37] In *In re Herman*, 737 F.3d 449 (7th Cir. 2013), a notice sent to the attorney for the creditor constituted notice to the creditor for purposes of Section 523(a)(3)(B).

successfully prosecute that adversary complaint in order for the debt to be non-dischargeable.

FRAUD, DEFALCATION, EMBEZZLEMENT AND LARCENY

Section 523(a)(4) provides that a discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of the Bankruptcy Code does not discharge an individual debtor from any debt for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.[38] There are four separate grounds on which a debt may be non-dischargeable under Section 523(a)(4): (1) fraud while acting in a fiduciary capacity; (2) defalcation while acting in a fiduciary capacity; (3) embezzlement; and (4) larceny.[39]

"[F]raud or defalcation while acting in a fiduciary capacity" has specific requirements. The debtor must have owed the creditor a fiduciary duty under the first two grounds.

Generally speaking, a fiduciary duty is a legal duty to act solely in another party's interest. Within the context of Section 523(a)(4), however, courts have imposed a more stringent requirement for determining whether the debtor had a fiduciary duty to the injured creditor. In particular, courts have required that the offending debtor must have been the trustee of an actual trust, for there to have been a fiduciary duty that was breached.

The fiduciary relationship that is required under Section 524(a)(4) requires more than just a relationship involving confidence, trust and good faith.[40] "[T]he concept of fiduciary under § 523(a)(4) is narrower than it is under the general common law. Under Section 523(a)(4), 'fiduciary' is limited to instances involving express or technical trusts."[41] The trust giving rise

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[38] 11 U.S.C. 523(a)(4).

[39] *See, e.g., In re Musgrave*, 2011 WL 312883 (10th Cir. B.A.P. 2011)

[40] *See Angelle v. Reed (In re Angelle)*, 610 F.2d 1335, 1338-39 (5th Cir.1980).

[41] *Texas Lottery Comm'n v. Tran*, 151 F.3d 339, 342 (5th Cir.1998).

to the fiduciary relationship must be imposed prior to any wrongdoing; the debtor must have been a "trustee" before the wrong and without reference to it.[42] It does not include constructive, resulting or implied trusts.[43]

In *Bullock v. BankChampaign, N.A.*, the Supreme Court reconciled a split among the Circuit Courts concerning defalcation under Section 523(a)(4) and held unanimously that the element of intent requires a culpable state of mind that includes a knowledge of, or gross recklessness with respect to, the improper nature of the relevant fiduciary behavior.[44]

"Fraud in a fiduciary capacity" is different from "defalcation in a fiduciary capacity." Fraud requires actual fraud with the necessary elements: (1) debtor misrepresented, concealed, or failed to disclose a material fact; 2) the debtor knew that what he said, or failed to say, was false; 3) the debtor intended to induce the plaintiff's reliance by the statement or omission; 4) the plaintiff justifiably relied on the debtor's statement or omission; and 5) the plaintiff suffered damage as a result.

Defalcation requires something less. The primary debate concerning the definition of defalcation focuses or whether mere innocent or negligent conduct can constitute defalcation, or whether defalcation must include some element of wrongdoing.[45] Defalcation under 523(a)(4) is the misappropriation of trust funds or money held in any fiduciary capacity, or the failure to

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[42] *Davis*, 293 U.S. at 333, 55 S. Ct. at 153-54; *In re Pedrazzini (Runnion v. Pedrazzini)*, 644 F.2d 756, 758 (9th Cir. 1981). *Also see Ragsdale v. Haller*, 780 F.2d 794 (9th Cir. 1986)

[43] *Pedrazzini*, 644 F.2d at 759.

[44] *Bullock v. BankChampaign, N.A.*, 133 S.Ct. 1754, 185 L.Ed.2d 922 (2013).

[45] *Id*.

properly account for such funds.[46] It does not have to rise to the level of fraud, embezzlement, or even misappropriation.[47] Even negligence or "an innocent mistake" can result in a finding of defalcation.[48]

Embezzlement and larceny, unlike fraud and defalcation, do not require a fiduciary relationship between the debtor and the creditor. Courts may use the federal common law definition of embezzlement.[49] Embezzlement under Section 523(a)(4) may be defined as the fraudulent appropriation of property by a person to whom such property has been entrusted or into whose hands it has lawfully come. Embezzlement, thus, requires three elements: (1) property rightfully in the possession of a nonowner; (2) nonowner's appropriation of the property to a use other than that for which it was entrusted; and (3) circumstances indicating fraud.[50] Embezzlement can occur regardless of whether the defendant keeps the personal property or transfers it to a third party. A person cannot embezzle funds from oneself, even if a third party has a right to be paid from the funds.[51]

Larceny is the fourth grounds for nondischargeability under Section 524(a)(4). As with embezzlement, there is no requirement that the debtor owe a fiduciary duty to the creditor for

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[46] *In re Niles*, 106 F.3d 1456, 1460 (9th Cir.1997).

[47] *Quaif v. Johnson*, 4 F.3d 950, 955 (11th Cir.1993) (citing *Central Hanover Bank & Trust Co. v. Herbst*, 93 F.2d 510, 512 (2d Cir.1937) (Learned Hand, J.)

[48] *In re Uwimana*, 274 F.3d 806 (4th Cir. 2001).

[49] *See, e.g., Matter of Rose*, 934 F.2d 901 (7th Cir. 1991), *In re Ormsby*, 591 F.3d 1199 (9th Cir. 2010), *In re Jardula*, 122 B.R. 649 (E.D. N.Y. 1990), *In re Ferris*, 447 B.R. 516 (Bankr. E.D. Va. 2011) and *In re Simerlein*, 497 B.R. 525 (Bankr. E.D. Tenn. 2013).

[50] *In re Littleton*, 942 F. 2d 551, 555 (9th Cir. 1991).

[51] *In re Thompson*, 686 F.3d 940 (8th Cir. 2012) (In *Thompson*, a contractor failed to pay a subcontractor with funds received from the builder. The court held that the subcontractor's right to be paid from the funds did not give the subcontractor an ownership interest in the funds.)

larceny to occur. For purposes of Section 523(a)(4), a bankruptcy court may use the definition of larceny under either state law or federal common law.[52] The plaintiff seeking to demonstrate that a debt is nondischargeable for larceny must show that the debtor committed a wrongful or fraudulent taking and carrying away of another's property with the intent to convert the property to the debtor's use without the consent of the owner.[53] The difference between embezzlement and larceny is that the original taking in embezzlement is lawful and with the consent of the injured person and in larceny the original taking is unlawful and without the consent of the injured person.[54]

ALIMONY, MAINTENANCE, and SUPPORT

Sections 523(a)(5) and 523(a)(15)[55] concern debts arising from domestic support obligations. Section 523(a)(5) provides that a marital debt arising from a DSO[56] ("DSO") is nondischargeable and applies in all individual bankruptcy cases.

Section 523(a)(15) concerns the dischargeability of marital debts other than a domestic

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[52] *In re Ormsby*, 591 F. 3d 1199, 1205 (9th Cir. 2010).

[53] *See, e.g., IMI Factoring, L.L.C. v. McKnew (In re McKnew)*, 270 B.R. 593, 624 (Bankr. E.D. Va. 2001).

[54] *Id. Also see, In re Aman*, 498 B.R. 592 (Bankr. N.D. W.Va. 2013).

[55] Sections 523(a)(5) and (15) provide:

> (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—
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> . . .
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> (5) for a domestic support obligation;
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> . . .
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> (15) to a spouse, former spouse, or child of the debtor and not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, or a determination made in accordance with State or territorial law by a governmental unit;

[56] *See,* Section 101(14A) for the definition of "domestic support obligation."

support obligation ("non-DSOs"). The section concerns any debt "to a spouse, former spouse, or child of the debtor," other than a DSO, "that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, or a determination made in accordance with State or territorial law by a governmental unit."

There are four elements that must be established for a debt to be a domestic support obligation as defined in Section 101(14A)(A)). The debt must be: (1) owed to or recoverable by the debtor's spouse, former spouse, or child (or the child's parent, legal guardian, or responsible relative), or a governmental unit, (2) in the nature of alimony, maintenance, or support (including assistance provided by a governmental unit) of the spouse, former spouse, or child, without regard to whether the debt is expressly so designated, (3) established or subject to establishment before, on, or after the date of the order for relief, by reason of applicable provisions of (i) a separation agreement, divorce decree, or property settlement agreement; (ii) an order of a court of record; or (iii) a determination made in accordance with applicable nonbankruptcy law by a governmental unit, (4) not assigned to a nongovernmental entity, unless that obligation is assigned voluntarily for the purpose of collecting the debt. The party seeking a judgment holding the debt nondischargeable has the burden of proof.[57] As a practical matter, the principal question is whether the debt is in the nature of support of the debtor's spouse, former spouse, or child. The other elements rarely are determinative.

In determining whether an obligation is a DSO-- that is, whether it is in the nature of alimony, maintenance, or support-- courts will conduct a fact-intensive analysis that looks beyond

[57] *See, e.g., In re Sampson*, 997 F.2d 717 (10th Cir. 1993).

the labels the parties have given to a particular debt. Thus, a debt is a DSO if the parties intended it to function as support or alimony, even if they called it something else.

Although the court's decision should be informed in part by state law,[58] other factors are also relevant. They include (1) the agreement's language; (2) the parties' financial positions when the agreement was made; (3) the amount of the division; (4) whether the obligation ends upon death or remarriage of the beneficiary; (5) the frequency and number of payments; (6) whether the agreement waives other support rights; (7) whether the obligation can be modified or enforced in state court; and finally (8) how the obligation is treated for tax purposes.[59] Finally, a debt may be determined to be a DSO even if the parties are not, and never were, married.[60]

WILLFUL AND MALICIOUS INJURY

Section 523(a)(6)[61] provides that a bankruptcy discharge does not discharge an individual debtor from any debt for willful and malicious injury by the debtor to another entity or property of another entity. The use of the phrase "to another entity or to the property of another entity" indicates that the paragraph is applicable to willful and malicious injuries affecting more than just individuals. Under the code, an "entity" includes individuals, partnerships, corporations, and

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[58] *Cummings v. Cummings*, 244 F.3d 1263 (11th Cir. 2001).

[59] *In re McCollum*, 415 B.R. 625 (Bankr. M.D. Ga. 2009).

[60] *See, e.g.*, *In re Rugiero*, 2011 WL 6004576 (E.D. Mich. 2011), aff'd, 502 Fed. Appx. 436 (6th Cir. 2012), and *In re Johnson*, 2012 WL 1933556 (Bankr. D. Utah 2012).

[61] Section 523(a)(6) provides:

> (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—
> . . .
> (6) for willful and malicious injury by the debtor to another entity or to the property of another entity.

even certain governmental entities.[62]

The important words in Section 523(a)(6) are "willful and malicious injury." The Supreme Court has held that nondischargeability requires a deliberate or intentional injury, and not merely a deliberate or intentional act that leads to an injury, because the word 'willful' modifies both the word 'malicious" and the word 'injury.'[63] Intentional torts generally require that the actor intend "the consequences of an act," not simply "the act itself."[64] The Court consequently held that Section 523(a)(6) does not apply to "debts arising from recklessly or negligently inflicted injuries."[65] Intent cannot be inferred, but must be proved as a separate element by a preponderance of the evidence.[66]

FINES, PENALTIES, OR FORFEITURES

Section 523(a)(7)[67] excepts from discharge certain fines, penalties and forfeitures payable to a governmental unit that are not compensation for actual pecuniary loss, other than a tax

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62 *See* 11 U.S.C. 101(41).

63 *Kawaauhau v. Geiger*, 523 U.S. 57, 61 (1998).

64 *Id*., at 61-62.

65 *Id.*, at 61.

66 *See, e.g., St. Paul Fire & Marine, Ins. Co. V. Vaughn*, 779 F.2d 1003 (4th Cir. 1985). Conversion of a creditor's collateral may suffice to support an action for nondischargeability of a debt as a willful and malicious injury.

67 Section 523(a)(7) provides:

> (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—
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> . . .
>
> (7) to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss, other than a tax penalty—
>
> (A) relating to a tax of a kind not specified in paragraph (1) of this subsection; or
> (B) imposed with respect to a transaction or event that occurred before three years before the date of the filing of the petition

penalty with the exception of (1) a tax penalty that does not relate to a nondischargeable tax of a kind in Section 523(a)(1) and (2) a tax penalty imposed with respect to a transaction or event that occurred before three years before the date of the filing of the petition.

Most courts have held that a tax penalty is not a "tax," and that, consequently, the dischargeability of a tax penalty is determined under Section 523(a)(7) rather than Section 523(a)(1).[68] It is important to note that the relevant date for dischargeability under Section 523(a)(7)(B) is that of the "transaction or event giving rise to the penalty," not the date of the imposition of the penalty. Section 523(a)(7)(B) applies even if the tax debt underlying the penalty is nondischargeable.[69] A restitution obligation, imposed upon a criminal defendant in state court as a condition of her probation falls within the ambit of Section 523(a)(7).[70]

EDUCATIONAL LOANS

Section 523(a)(8)[71] excepts from discharge a debt for (1) an educational benefit

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[68] *See, e.g., In re Kuchar*, 298 B.R. 638 (Bankr. D. N.D. 2003).

[69] *See, e.g., In re Hosack*, 282 Fed. Appx. 309 (5th Cir. 2008); McKay v. U.S., 957 F.2d 689 (9th Cir. 1992) and *In re Roberts*, 906 F.2d 1440 (10th Cir. 1990).

[70] *Kelly v. Robinson*, 479 U.S. 36, 107 S.Ct. 353, 93 L.Ed.2d 216 (1986).

[71] Section 523(a)(8) provides:

> 523(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—
> . . .
> (8) unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents, for—
> (A) (I) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or
> (ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or
> (B) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual;

overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or (2) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or (3) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual, unless the exception from discharge would impose an undue hardship on the debtor and the debtor's dependents.

The two tests that are used to determine whether the discharge of an educational loan would impose an undue hardship on the debtor and the debtor's dependents are the *Brunner*[72] test and "totality-of-the-circumstances" test. The *Brunner* test is the most widely used test.

Under the *Brunner* test, the debtor must satisfy a three-pronged test. The debtor must demonstrate (1) that the debtor cannot currently maintain a "minimal" standard of living for herself and her dependents if forced to repay the loans; (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and (3) that the debtor has made good faith efforts to repay the loans.[73] The Third, Fourth, Fifth, Sixth, Seventh, Ninth, Tenth, and Eleventh circuits have adopted the *Brunner* test.

The Eighth Circuit declined to adopt the *Brunner* test and reaffirmed the "totality-of-the-circumstances test.[74] The Eighth Circuit adopted the totality-of-the-circumstances test over the *Brunne*r test because it was less restrictive and because,

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[72] *Brunner v. New York State Higher Educ. Servs. Corp.*, 831 F.2d 395 (2d Cir. 1987).

[73] *Brunner* at 396.

[74] *In re Long*, 322 F.3d 549 (8th Cir. 2003)

the court believed, the *Brunner* test would diminish the inherent discretion contained in Section 523(a)(8)(B). The Court further reasoned that fairness and equity required bankruptcy courts to examine the unique facts and circumstances of each case when determining whether denying the dischargeability of the student loan debt would impose an undue hardship on the debtor and the debtor's dependents.[75]

The Eighth Circuit further held that in evaluating the totality of the circumstances, bankruptcy courts should consider: (1) the debtor's past, present, and reasonably reliable future financial resources; (2) the amount of the debtor's and her dependent's reasonable necessary living expenses; and (3) any other relevant facts and circumstances necessary to determine whether the debtors' reasonable future financial resources can sufficiently fund payment of the student loan debt, while still allowing for a minimal standard of living or the debtor and the debtor's dependents. The Supreme Court has held that under certain circumstance a debtor may discharge a portion of his or her student loan debt if the creditor fails to object to the confirmation of a plan that adversely affects the creditor's rights.[76]

DEATH OR PERSONAL INJURY CAUSED BY THE DEBTOR WHILE DRIVING UNDER THE INFLUENCE

Section 523(a)(9)[77] excepts from discharge a debt for a death or personal injury caused by

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[75] *Id.*, at 554-555

[76] *United Student Aid Funds, Inc. v. Esponosa*, 130 S.Ct. 1367 (2010).

[77] Section 523(a)(9) provides:

> 523(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—
> . . .
> (9) for death or personal injury caused by the debtor's operation of a motor vehicle, vessel, or aircraft if such operation was unlawful because the debtor was intoxicated from using alcohol, a drug, or another substance;

the debtor while unlawfully operating a vehicle, boat or aircraft because the debtor was unlawfully under the influence of a drug or alcohol. Whether the debtor was legally intoxicated at the time is to be determined under state law.

The three elements that must be proven under Section 523(a)(9) are (1) the existence of a debt for death or personal injury; (2) caused by the operation of a motor vehicle, vessel or aircraft; (3) being operated unlawfully under state law due to the debtor's intoxication. It is not necessary that the debtor's intoxication caused the injury; it is sufficient that the injury was caused by the debtor's unlawful operation of the motor vehicle, vessel or aircraft when that operation was unlawful because the debtor was intoxicated.[78]

WAIVER OR DENIAL OF DISCHARGE IN PRIOR CASE

Section 523(a)(10)[79] excepts from discharge debts owed by a debtor before he or she filed a prior bankruptcy petition under Title 11 or under the Bankruptcy Act, in which prior case the debtor waived discharge, or was denied a discharge under section 727(a)(2), (3), (4), (5), (6), or (7) of Title 11, or under section 14c(1), (2), (3), (4), (6), or (7) of the Bankruptcy Act. If the debtor reaffirmed a debt in a prior case, then this paragraph does not except the reaffirmed debt from discharge.

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[78] *In re Owen*, 2011 WL 4007861 (Bankr. E.D. La. 2011).

[79] Section 523(a)(10) provides:

> 523(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—
> . . .
> (10) that was or could have been listed or scheduled by the debtor in a prior case concerning the debtor under this title or under the Bankruptcy Act in which the debtor waived discharge, or was denied a discharge under section 727(a)(2), (3), (4), (5), (6), or (7) of this title, or under section 14c(1), (2), (3), (4), (6), or (7) of such Act;

FRAUD OR DEFALCATION AGAINST DEPOSITORY INSTITUTIONS AND INSURED CREDIT UNIONS

Section 523(a)(11)[80] excepts discharge any debt provided for in a final judgment or order issued by a Federal depository institutions regulatory agency or contained in any settlement agreement between the debtor arising from an act of fraud or defalcation while acting in a fiduciary capacity committed with respect to any depository institution or insured credit union.

MALICIOUS OR RECKLESS FAILURE TO FULFILL A COMMITMENT TO A FEDERAL DEPOSITORY INSTITUTIONS REGULATORY AGENCY

Section 523(a)(12)[81] excepts discharge any debt arising from the debtor's malicious or reckless failure to fulfill a commitment to a Federal depository institutions regulatory agency to maintain the capital of an insured depository institution, unless the commitment would otherwise be terminated due to any act of such agency.

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[80] Section 523(a)(11) provides:

> 523(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—
> . . .
> (11) provided in any final judgment, unreviewable order, or consent order or decree entered in any court of the United States or of any State, issued by a Federal depository institutions regulatory agency, or contained in any settlement agreement entered into by the debtor, arising from any act of fraud or defalcation while acting in a fiduciary capacity committed with respect to any depository institution or insured credit union;

[81] Section 523(a)(12) provides:

> 523(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—
> . . .
> (12) for malicious or reckless failure to fulfill any commitment by the debtor to a Federal depository institutions regulatory agency to maintain the capital of an insured depository institution, except that this paragraph shall not extend any such commitment which would otherwise be terminated due to any act of such agency;

RESTITUTION ORDERS

Section 523(a)(13)[82] excepts from discharge any payment of an order of restitution issued under the Federal Criminal Code. This exception does not apply to restitution orders issued under state law.

DEBTS INCURRED TO PAY NON-DISCHARGEABLE TAXES, FINES, AND PENALTIES

Section 523(a)(14)[83] excepts from discharge any debt incurred to pay a tax to the United States or other governmental unit that would be nondischargeable pursuant to Section 523(a)(1), and any debt incurred to pay fines or penalties imposed under Federal election law.

The purpose of Section 523(a)(14) and (14A) is to prevent a debtor from substituting a nondischargeable tax debt for a dischargeable debt. Two elements must be met: (1) the debt must have been incurred to pay a tax, and (2) that tax must have been nondischargeable under Section 523(a)(1).[84]

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[82] Section 523(a)(13) provides:

> 523(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—
> . . .
> (13) for any payment of an order of restitution issued under title 18, United States Code;

[83] Section 523(a)(14) provides:

> 523(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—
> . . .
> (14) incurred to pay a tax to the United States that would be nondischargeable pursuant to paragraph (1);
> (14A) incurred to pay a tax to a governmental unit, other than the United States, that would be nondischargeable under paragraph (1);
> (14B) incurred to pay fines or penalties imposed under Federal election law;

[84] *In re Barton*, 321 B.R. 869 (Bankr. N.D. Ohio 2004).

FEES AND ASSESSMENTS FOR MEMBERSHIP ASSOCIATIONS REGARDING CONDOMINIUMS AND COOPERATIVES

Section 523(a)(16)[85] excepts from discharge fees and assessments that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a unit that has condominium ownership, in a share of a cooperative corporation, or a lot in a homeowners association, for as long as the debtor or the trustee has a legal, equitable, or possessory ownership interest in such unit, such corporation, or such lot, but does not except from discharge a debt for a membership association fee or assessment for a period arising before entry of the order for relief in a pending or subsequent bankruptcy case.

A Chapter 7 debtor remains liable for condominium fees even if he or she surrenders the property[86] even if he or she has stipulated to relief from the stay in order to permit the creditor to foreclose.[87]

FILING FEES, COURT COSTS, AND EXPENSES

Section 523(a)(17)[88] excepts from discharge a debt arising from a fee imposed on a

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[85] Section 523(a)(16) provides:

> 523(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—
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> . . .
>
> (16) for a fee or assessment that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a unit that has condominium ownership, in a share of a cooperative corporation, or a lot in a homeowners association, for as long as the debtor or the trustee has a legal, equitable, or possessory ownership interest in such unit, such corporation, or such lot, but nothing in this paragraph shall except from discharge the debt of a debtor for a membership association fee or assessment for a period arising before entry of the order for relief in a pending or subsequent bankruptcy case;

[86] *In re Langenderfer*, 2012 WL 1414301 (Bankr. N.D. Ohio 2012)

[87] *In re Burgueno*, 451 B.R. 1 (Bankr. D. Ariz. 2011)

[88] Section 523(a)(17) provides:

prisoner by any court for the filing of a case, motion, complaint, or appeal, or for other costs and expenses assessed with respect to such filing, regardless of an assertion of poverty by the debtor or the debtor's status as a prisoner.

DEBTS OWED TO PENSION OR OTHER EMPLOYEE BENEFIT PLAN

Section 523(a)(18)[89] excepts from discharge any debt owed to a pension, profit-sharing, stock bonus, or other plan arising from a loan permitted under ERISA or a loan from a thrift savings plan. Nothing in paragraph (18) may be construed to provide that any loan made under a governmental plan under section 414(d), or a contract or account under section 403(b), of the Internal Revenue Code of 1986, constitutes a claim or a debt under the Bankruptcy Code.

> 523(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—
> . . .
> (17) for a fee imposed on a prisoner by any court for the filing of a case, motion, complaint, or appeal, or for other costs and expenses assessed with respect to such filing, regardless of an assertion of poverty by the debtor under subsection (b) or (f)(2) of section 1915 of title 28 (or a similar non-Federal law), or the debtor's status as a prisoner, as defined in section 1915(h) of title 28 (or a similar non-Federal law);

[89] Section 523(a)(18) provides:

> 523(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—
> . . .
> (18) owed to a pension, profit-sharing, stock bonus, or other plan established under section 401, 403, 408, 408A, 414, 457, or 501(c) of the Internal Revenue Code of 1986, under—
> (A) a loan permitted under section 408(b)(1) of the Employee Retirement Income Security Act of 1974, or subject to section 72(p) of the Internal Revenue Code of 1986; or
> (B) a loan from a thrift savings plan permitted under subchapter III of chapter 84 of title 5, that satisfies the requirements of section 8433(g) of such title;
>
> but nothing in this paragraph may be construed to provide that any loan made under a governmental plan under section 414(d), or a contract or account under section 403(b), of the Internal Revenue Code of 1986 constitutes a claim or a debt under this title;

VIOLATION OF FEDERAL OR STATE SECURITY LAWS

Section 523(a)(19)[90] excepts from discharge a debt that is (i) for the violation of any of the Federal securities laws, any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or (ii) for common law fraud, deceit, or manipulation in connection with the purchase or sale of any security. The debt must result from either (i) a pre-petition judgment, order, consent order, or decree entered in any Federal or State judicial or administrative proceeding; or (ii) a pre-petition settlement agreement entered into by the debtor; or (iii) a pre-petition court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor.

Under Section 523(a)(19), a debt may be excepted from discharge even if the debtor has not violated securities laws, if the debtor has innocently received a monetary return from a Ponzi scheme operated by another person.[91]

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[90] Section 523(a)(19) provides:

> 523(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—
> . . .
> (19) that—
> (A) is for—
> (I) the violation of any of the Federal securities laws (as that term is defined in section 3(a)(47) of the Securities Exchange Act of 1934), any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or
> (ii) common law fraud, deceit, or manipulation in connection with the purchase or sale of any security; and
> (B) results, before, on, or after the date on which the petition was filed, from—
> (I) any judgment, order, consent order, or decree entered in any Federal or State judicial or administrative proceeding;
> (ii) any settlement agreement entered into by the debtor; or
> (iii) any court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor.

[91] *Oklahoma Dept. of Securities ex rel. Faught v. Mathews*, 691 F.3d 1171 (10th Cir. 2012). (The

EXCEPTIONS TO DISCHARGE IN CHAPTER 13

Section 1328(a)[92] provides the list of debts that are non-dischargeable in Chapter13.

Section 1328(a)(1) excepts debts as described in Section 1322(b)(5). Section 1322(b)(5) provides that the Chapter 13 plan may, while the case is pending, provide for the curing of any default on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due.

Section 1328(a)(2) excepts from discharge under Chapter 13 any debt of the kind specified in Section 523(a) (1)(B), (1)(C), (2), (3), (4), (5), (8), or (9) of section 523(a). It also excepts from the future discharge debts that give rise to claims under section 507(a)(8)(C). These are unsecured governmental claims for taxes "required to be collected or withheld and for which the debtor is liable in whatever capacity." These taxes are the so-called trust fund taxes for which a debtor might be a responsible person.

Court, in reversing the bankruptcy court, reasoned that the purpose of Section 523(a)(19) is to protect investors and hold accountable those who violate securities laws. The Court reasoned that the paragraph must be broadly construed to achieve both of these purposes.)

[92] Section 1328(a) provides:

> (a) Subject to subsection (d), as soon as practicable after completion by the debtor of all payments under the plan, and in the case of a debtor who is required by a judicial or administrative order, or by statute, to pay a domestic support obligation, after such debtor certifies that all amounts payable under such order or such statute that are due on or before the date of the certification (including amounts due before the petition was filed, but only to the extent provided for by the plan) have been paid, unless the court approves a written waiver of discharge executed by the debtor after the order for relief under this chapter, the court shall grant the debtor a discharge of all debts provided for by the plan or disallowed under section 502 of this title, except any debt—
>
> (1) provided for under section 1322(b)(5);
>
> (2) of the kind specified in section 507(a)(8)(C) or in paragraph (1)(B), (1)(C), (2), (3), (4), (5), (8), or (9) of section 523(a);
>
> (3) for restitution, or a criminal fine, included in a sentence on the debtor's conviction of a crime; or
>
> (4) for restitution, or damages, awarded in a civil action against the debtor as a result of willful or malicious injury by the debtor that caused personal injury to an individual or the death of an individual.

Section 1328(a)(3) excepts from discharge any debt for restitution, or a criminal fine.

Section 1328(a)(4) excepts from discharge any debt "for restitution, or damages, awarded in a civil action against the debtor as a result of willful or malicious injury by the debtor that caused personal injury to an individual or the death of any individual."

PART II

DENIAL OF DISCHARGE UNDER 11 U.S.C. § 727

Generally, the primary reason debtors file bankruptcy is to receive a discharge. However, receiving a discharge is not guaranteed merely by filing a petition. Debtors are required to follow the rules, make full disclosure, and act in good faith if they expect to cross the finish line and receive their discharge.[93] Some frank discussions between attorney and client, diligence on the part of the debtor in providing information and on the attorney in reviewing it (and probably looking behind what is provided) are all key plays necessary for reaching the goal line! Otherwise, a severe penalty will be imposed – denial of the discharge.

A judge's perception of the debtor plays a pivotal role in deciding whether the debtor deserves a discharge under Section 727. If the debtor appears to be honest and generally acting in good faith in his dealings with his creditors, the judge will more likely minimize or view in a more favorable light the facts offered as supporting the parameters of Section 727. If the debtor appears less than credible and does not give the appearance of or act like an "honest but unfortunate debtor," a bankruptcy judge may give more weight or credence to seemingly less significant acts sufficing to deny a discharge.[94]

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[93] "The veracity of the bankrupt's statements is essential to the successful administration of the Bankruptcy [Code]." *Chalik v. Moorefield (In re Chalik)*, 748 F.2d 616, 618 (11th Cir. 1984).

[94] Two examples are *Chalik v. Moorefield (In re Chalik)*, 784 F.2d 616 (11th Cir. 1984) and *Future*

In order to successfully object to a debtor's discharge under §727, there are specific elements that an objecting party must prove by a preponderance of the evidence. The burden is on the objecting party and ALL of the elements of the specific provision must be proven in order to successfully carry the burden. The debtor, on the other hand, will be arguing to the judge that the objecting party failed to meet the burden of proof in establishing ALL of the elements required to prevail under Section 727(a)(2), (3), (4), (5), (6) and/or (7), whichever section alleged to be at issue. These specific provisions of Section 727 and the elements needed to be established are discussed herein with pertinent cases referenced or included in the materials.

TRANSFER, DESTRUCTION AND CONCEALMENT OF PROPERTY

Under Section 727(a)(2), the court shall grant the debtor a discharge unless "the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with the 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 the petition; or (B) property of the estate, after the date of the filing of the petition…."

Question: Did the debtor intentionally hinder, delay or defraud a creditor or trustee by transferring, removing, destroying or concealing property of the debtor within 1 year of filing the bankruptcy or property of the estate after filing bankruptcy?

If a creditor, trustee, or the U.S. Trustee is proceeding under this section of 727 in objecting to the debtor's discharge, they must prove 4 elements: (1) the transfer, destruction or concealment of property; (2) belonging to the debtor or the estate; (3) within 1 year prior to the

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Time, Inc. v. Yates, 26 B.R. 1006 (M.D. Ga. 1983), aff'd mem., 712 F.2d 1417 (11th Cir. 1983).

bankruptcy filing; and (4) the intent to hinder, delay, or defraud a creditor(s) or the trustee.[95] The intent to defraud must be actual not constructive.[96]

Courts typically look for the presence of certain factors to indicate fraudulent intent. For example, the Fifth Circuit uses a six-factor test to evaluate evidence of actual intent to defraud under Section 727(a)(2)(A): (1) the lack of inadequacy of consideration; (2) the family, friendship or close associate relationship between the parties; (3) the retention of possession, benefit or use of the property in question; (4) the financial condition of the party sought to be charged both before and after the transaction in question; (5) the existence or cumulative effect of the pattern or series of transactions or course of conduct after the incurring of debt, onset of financial difficulties, or pendency or threat of suits by creditors; and (6) the general chronology of the events and transactions under inquiry.[97]

CONCEALMENT, DESTRUCTION, FALSIFICATION AND FAILURE TO KEEP BOOKS AND RECORDS

Under Section 727(a)(3), the court shall grant the debtor a discharge unless "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…."

Courts generally have a two-fold test for denial of discharge under Section 727(a)(3) for failure to maintain records: (1) did the debtor fail to maintain and preserve adequate records; and,

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[95] *Cadle Co. v. Pratt*, 411 F. 3d 561, 565 (5th Cir. 2005) referring to decision in *Pavy v. Chastant (In re Chastant)*, 873 F. 2d 89, 90 (5th Cir. 1989).

[96] *Id.*, citing *Pavy v. Chastant* at p. 91. See also, e.g., *Future Time, Inc. v. Yates*, 26 B.R. 1006 (M.D. Ga. 1983), aff'd mem., 712 F.2d 1417 (11th Cir. 1983); *In re Davis*, 911 F.2d 560 (11th Cir. 1990).

[97] *In re: Duncan*, 562 F.3d 688 (5th Cir., March 11, 2009) (case no. 07-41024).

if so (2) did the failure make it impossible for the plaintiff to ascertain the debtor's financial condition for a reasonable period past to present. Section 727(a)(3) does not require any showing of intent, and once the objecting party proves each prong of this test by a preponderance of the evidence, then the burden shifts to the debtor to justify his failure to maintain and preserve adequate records under the circumstances.[98]

Factors that courts consider when analyzing the sufficiency of the debtor's justification include: (1) the debtor's education; (2) the debtor's sophistication; (3) the volume of the debtor's business; (4) the complexity of the debtor's business; (5) the amount of credit extended to the debtor in his business; (6) any other circumstances that should be noted in the interest of justice.[99]

Cases under this section generally involve debtors who have destroyed records that could lead the trustee to property the debtor has not disclosed or simply is unable to back up assertions about finances contained in the bankruptcy schedules. In *Bozeman v. Sullivan (In re Sullivan)*, the court stated that in order to prove a case for failure to keep records, it must be shown that the debtor failed to maintain and preserve adequate records and that the failure made it *impossible* to ascertain the financial condition and *material business* transactions of the debtor in the case.[100]

What is material? The court in *Chalik* gives guidance when discussing materiality in the context of a false oath under Section 727(a)(4), discussed in the next paragraph.[101]

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98 *See*, *Meridian Bank v. Alten*, 958 F.2d 1226 (3d Cir. 1992).

99 *In re Liberatore*, 503 B.R. 23 (Bankr. E.D. Pa., Sept. 30, 2013), appeal withdrawn, Case No. 2:13-cv-06688 (E.D. Pa., Feb. 19, 2014) (case no. 2:11-bk-16408; adv. proc. no. 2:12-ap-289) (Bankruptcy Judge Jean K. FitzSimon).

100 492 B.R. 348, 354 (Bankr. M.D. Ga. 2013). The court cited: *Gullickson v. Brown (In re Brown)*, 108 F. 3d 1290, 1295 (10th Cir. 1997) (citing *In re Folger*, 149 B.R. 183, 188 (D.Kan.1992)) (emphasis added by 10th Circuit).

101 *Chalik v. Moorefield (In re Chalik)*, 748 F.2d 616, 618 (11th Cir. 1984).

FALSE OATH OR ACCOUNT

Under Section 727(a)(4), the court shall grant the debtor a discharge unless "the debtor knowingly and fraudulently, in or in connection with the case— (A) made a false oath or account; (B) presented or used a false claim; (C) gave, offered, received, or attempted to obtain money, property, or advantage, or a promise of money, property, or advantage, for acting or forbearing to act; or (D) withheld from an officer of the estate entitled to possession under this title, any recorded information, including books, documents, records, and papers, relating to the debtor's property or financial affairs…."

Question: Did the debtor knowingly and fraudulently, in or in connection with, the bankruptcy case make a false oath or account?

If proceeding under this section to object to the debtor's discharge, the objecting party must show (1) the debtor made a statement under oath; (2) this statement was false; (3) the debtor knew the statement was false; (4) the debtor's intent when making the statement was the intent to defraud; and (5) the statement made related to the bankruptcy case in a material way.[102] To prove a false oath, the objecting party must show that the debtor made a material false oath with fraudulent intent.[103] Under Section 727(a)(4), a false oath is material "if 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."[104]

Can the debtor amend errors or omissions in his petition and schedules to correct

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[102] *In re Chavin*, 150 F3d 726, 728 (7th Cir. 1998)("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"); *Hunt v. O'Neal (In re O'Neal)*, 436 B.R. 545, 560-61 (Bankr. N.D. Ill. 2010).

[103] *Bozeman* at 353.

[104] *Chalik* at 618.

mistakes? Some courts have allowed amendments to correct mistakes so long as the original mistake, error or omission was not made with the fraudulent intent and does not form the basis for the denial of a discharge.[105]

FAILURE TO EXPLAIN LOSS OF ASSETS

Under Section 727(a)(5), the court shall grant the debtor a discharge unless **"**the debtor has failed to explain satisfactorily, before determination of denial of discharge under this paragraph, any loss of assets or deficiency of assets to meet the debtor's liabilities…."

Question: Did the debtor fail to explain satisfactorily any loss or deficiency of assets to meet his liabilities?

In order to proceed under Section 727(a)(5), the objecting party must prove (1) the debtor at one time owned a substantial, identifiable asset; (2) not too remote in time from the filing of the case; (3) that on the day of filing the petition the debtor no longer had the particular asset; and (4) the debtor is not able to explain his loss or lack of possession of the asset.[106] The objecting party "must introduce more than merely an allegation that the debtor has failed to explain losses, e.g., the objector must produce some evidence of the disappearance of substantial assets or of an unusual transaction which disposed of assets."[107]

The objecting party has the initial burden of showing that the debtor at one time had the assets but that thereafter they were no longer available for the debtor's creditors. Once the creditor

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[105] *In re Wines*, 997 F. 2d 852, 856-857 (11th Cir. 1993); But see *In re* Parnes, 200 B.R. 710 (Bankr. N.D. Ga. 1996) and *In re* Mitchell, 496 B.R. 625 (Bankr. N.D. Fla. 2013).

[106] *Libertore v. Walden (In re Walden)*, 380 B.R. 883, 894 (Bankr. M.D. Fla. 2008); *Menotte v. Hahn (In re Hahn)*, 362 B.R. 542, 548 (Bankr. S.D. Fla. 2007).

[107] *Riehn v. Park (In re Park*), 272 B.R. 323, 332 (Bankr. D. N.J. 2001) (quoting *In re Ishkhanian*, 210 B.R. 944, 953 (Bankr.E.D.Pa.1997)).

has introduced some evidence of the disappearance of substantial assets, the burden shifts to the debtor to explain satisfactorily the loss.[108]

"The Bankruptcy Code does not require a debtor seeking a discharge specifically to maintain a bank account, nor does it require an impeccable system of bookkeeping. Nevertheless, the records must "'sufficiently identify the transactions [so] that intelligent inquiry can be made of them.' The test is whether 'there [is] available written evidence made and preserved from which the present financial condition of the bankrupt, and his business transactions for a reasonable period in the past may be ascertained.'"[109] Thus, in order to invoke the protection of the bankruptcy court, the debtor must maintain and preserve adequate records. If the debtor fails to do so, there must be some justification.[110]

FAILURE TO OBEY LAWFUL ORDER

Under Section 727(a)(6), the court shall grant the debtor a discharge unless "the debtor has refused, in the case—(A) to obey any lawful order of the court, other than an order to respond to a material question or to testify; (B) on the ground of privilege against self-incrimination, to respond to a material question approved by the court or to testify, after the debtor has been granted immunity with respect to the matter concerning which such privilege was invoked; or (C) on a ground other than the properly invoked privilege against self-incrimination to respond to a material question approved by the court or to testify…."

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[108] *In re Brien*, 208 B.R. 255 (1st Cir. B.A.P. 1999). *In re Joslin*, 499 B.R. 47 (Bankr. D. Mass., Sept. 30, 2013) (case no. 1:11-bk-10171; adv. proc. no. 1:11-ap-1289) (Chief Bankruptcy Judge Frank J. Bailey).

[109] *Meridian Bank v. Alten*, 958 F.2d 1226, 1230 (3d. Cir. 1992) (quoting *In re Decker*, 595 F.2d 185, 187 (3d Cir.1979).

[110] *Id*.

Question: Did the debtor refuse to obey a lawful order of the court for which there is no justification? The debtor's refusal must not be merely a mistake or due to an inability to comply or perform but rather, the refusal must be willful and intentional.[111] If a debtor is ordered to produce a specific, known, identifiable document pursuant to an order requiring that the debtor submit to a Rule 2004 examination and refuses to do so, and without justification, the debtor may lose his discharge under this section.

The majority position is that the word "refused" in Section 727(a)(6)(A) is more than a simple failure to comply. The plaintiff must show some degree of volition or willfulness on the part of the debtor in failing to comply with the order."[112] Refusal requires a degree of scienter, that is, knowledge of the order and a decision not to abide by it.[113]

CONDUCT IN AFFILIATED CASE

Under Section 727(a)(7), the court shall grant the debtor a discharge unless **"**the debtor has committed any act specified in paragraph (2), (3), (4), (5), or (6) of this subsection, on or within one year before the date of the filing of the petition, or during the case, in connection with another case, under this title or under the Bankruptcy Act, concerning an insider…."

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[111] *Smith v. Jordan (In re Jordan)* 521 F.3d 430 (4th Cir. 2008)("The term used in § 727(a)(6)(A) is 'refused' not 'failed'" at 433); *Ring v. Swan (In re Swan)*, 506 B.R. 47 (Bankr. W.D.N.Y. 2014 ("It does not seem… that all Chapter 7 debtors who are not fully compliant with an Order of the Court should be denied discharge. Denial of discharge is reserved for dishonest people…." at p. 51); *In re Prevatt*, 261 B.R. 54, 60-61 (Bankr. M.D. Fla. 2000) (concluding refusal under section 727(a)(6) must be willful and not merely inadvertent); *In re Barman*, 237 B.R. 342, 349 (Bankr. E.D. Mich. 1999)("Failure to comply with a court order, standing alone, is not the equivalent of "refusal" under § 727(a)(6).").

[112] *In re Lipp*, 2009 WL 2032127 (Bankr. D. Mass., July 6, 2009); *In re Tougas*, 354 B.R. 572 (Bankr. D. Mass. 2006); *In re Jordan*, 521 F.3d 430 (4th Cir. 2008).

[113] In re Fatsis, 435 B.R. 814 (Bankr. D. Mass., Sept. 21, 2010) (case no. 1:03-bk-19121; adv. proc. no. 1:09-ap-1059) (Bankruptcy Judge Frank J. Bailey).

Question: Has the debtor committed one of the acts specified in sections (a)(2)-(6) of Section 727 within 1 year of the filing date of his bankruptcy case or during his bankruptcy case, in connection with another bankruptcy case, concerning an insider?

Most often this situation arises when a debtor (an individual) files a petition under Chapter 7 and an entity under his control (an "insider" – see, Section 101(31) for definitions) files a petition under Chapter 7 or 11. If, in connection with the insider's bankruptcy case, the debtor commits an act in the insider's case that would result in a denial of his discharge under Section 727 if it had occurred prior to or during his own case, then, if proven, he will be denied his discharge in his own case. The act in question could include the following: (a) participation in the fraudulent concealment, destruction or transfer of the insider's property; (b) the failure to produce the insider's books and records; (c) making a false oath while testifying in the insider's case; (d) failure to explain the insider's losses; or (e) refusal to obey a lawful order to produce documents or to answer a material question in the insider's case.[114]

[114] *In re Kane*, 755 F.3d 1285 (11th Cir. 2014); *Giant Eagle Inc. v. Monus (In re Monus)*, 294 B.R. 707 (Bankr. N.D. Ohio 2003); *In re Moore*, 559 B.R. 243 (Bankr. M.D. Fla. 2016); *in re Breedlove*, 545 B.R. 359 (Bankr. M.D. Ga. 2016); *In re Lewiston*, 537 B.R. 808 (Bankr. E.D. Mich. 2015).