UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In re: STEVEN JOHN JOHNSON JILL MARIE JOHNSON, Debtors.	BKY 07-30769 Chapter 7
LLOYD GROBEL, Plaintiff, v.	ADV 07-3115
STEVEN JOHN JOHNSON JILL MARIE JOHNSON, Defendants.	**ORDER FOR JUDGMENT**

This matter came before the Court on defendants' motion to dismiss and for summary judgment. Ryan T. Murphy appeared on behalf of the defendants, debtors Steven and Jill Johnson. Clark Thurn appeared on behalf of the plaintiff Lloyd Grobel. At the close of arguments, the Court took the matter under advisement. Based upon all of the files, records and proceedings herein, the Court being now fully advised makes this Order pursuant to the Federal and Local Rules of Bankruptcy Procedure.

I. FACTUAL BACKGROUND

The plaintiff Lloyd Grobel operated an accounting practice for many years. When he decided to retire, he sold the business for a stream of payments to defendant-debtor Steven Johnson through Johnson's individually held corporation Steven J. Johnson and Associates, Ltd. (SJA). Grobel claims that SJA failed to make payments as required by the terms of the transfer agreement and that, after Grobel filed suit against SJA, Johnson stripped SJA of its assets by selling the business to a third party, Accounting Associates, Inc., by a note in favor of himself personally.

Grobel obtained a default judgment against SJA in the amount of $92,452.60, and separately filed suit against Johnson personally. Grobel claims that Johnson also sold Johnson's right to payments, under the sale of SJA assets to Accounting Associates, to a third party bank for a single payment of $197,000 to himself personally, then spent the funds, and subsequently filed the bankruptcy petition underlying this proceeding, halting the state court litigation pending against him individually. Grobel argues that Johnson is liable on the judgment debt and that it is nondischargeable

pursuant to 11 U.S.C. § 523(a)(6) as a willful and malicious injury.

The Johnsons argue that the complaint must be dismissed for failure to state a claim upon which relief may be granted; that the original transfer agreement and the default judgment are against SJA, not Johnson personally; that the present complaint is precluded because the state court denied Grobel's motion to amend to include Johnson personally as a defendant in the original litigation; and that Jill Johnson is not a valid party in interest and that the complaint should be dismissed against her in any event.

II. DISCUSSION

Claim Preclusion

As a preliminary matter, claim preclusion does not apply in this case. "Under Minnesota law, the doctrine of res judicata is designed to prevent relitigation of causes of action already determined in a prior action." See In re Nielsen, 1998 WL 386384 (Bankr. D. Minn. 1998), citing Beutz v. A.O. Smith Harvestore Prods., Inc., 431 N.W.2d 528, 531 (Minn.1988); In re George A. Hormel Trusts, 543 N.W.2d 668, 671 (Minn. Ct. App. 1996); Beck v. American Sharecom, Inc., 514 N.W.2d 584, 588 (Minn. Ct. App. 1994). "To reach the conclusion that res judicata is applicable, a trial court must be presented with: (1) a final judgment on the merits; (2) a second suit involving the same cause of action; and (3) identical parties or parties in privity." Nielsen, 1998 WL 386384, citing Sautter v. Interstate Power Co., 567 N.W.2d 755, 759 (Minn. Ct. App. 1997); Hormel, 543 N.W.2d at 671-672; Beck, 514 N.W.2d at 588; see also In re Langeslag, 366 B.R. 51, 56-57 (Bankr. D. Minn. 2007); In re Brandl, 179 B.R. 620, 627 (Bankr. D. Minn. 1995); Marshall v. Inn on Madeline Island, 631 N.W.2d 113, 119 (Minn. Ct. App. 2001).

"In this case, the state court lawsuit occurred prior to the filing of the [debtors'] bankruptcy petition, and [the] § 523(a)(6) claim therefore did not yet exist at the time of the state court litigation." Nielsen, 1998 WL 386384, citing Brown v. Felsen, 442 U.S. 127, 135 (1979). "Moreover, a determination of dischargeability under 523(a)(6) could not have been made by the state court in this case because such a determination is within the exclusive jurisdiction of the federal bankruptcy courts." Id.

Motion to Dismiss/Summary Judgment

A court "considering a motion to dismiss under Rule 12(b)(6) accepts all factual allegations in the complaint as true." See McAuley v. Federal Ins. Co., 500 F.3d 784, 787 (8th Cir. 2007), citing Botz v. Omni Air Int'l., 286 F.3d 488, 490 (8th Cir. 2002). "The motion will 'succeed or fail based upon the allegations contained in the face of the complaint.'" McAuley, 500 F.3d at 787, citing Gibb v. Scott, 958 F.2d 814, 816 (8th Cir. 1992). *See also*, Fed. R. Bankr. P. 7012.

"Rule 12(b)(6) itself provides that when matters outside the pleadings are

presented and not excluded by the court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56." McAuley, 500 F.3d at 787, citing Hamm v. Rhone-Poulenc Rorer Pharm., Inc., 187 F.3d 941, 948 (8th Cir. 1999). "Such 'matters outside the pleadings' include both statements of counsel at oral argument raising new facts not alleged in the pleadings, id., and 'any written or oral evidence in support of or in opposition to the pleading that provide some substantiation for and does not merely reiterate what is said in the pleadings.'" Id., citing Gibb, 958 F.2d at 816 (quoting 5C Wright & Miller, Federal Practice and Procedure § 1366).

In this matter, the parties filed various materials supplemental to the complaint and answer pleadings and basic motion to dismiss, including party affidavits, copies of the transfer agreement, and copies of pleadings and decisions in the related state court proceedings. While the Court need not consider the additional materials in order to determine the motion to dismiss, the supplemental documents were nevertheless presented and not excluded. Therefore, the Court will treat the motion as one for summary judgment.

"Summary judgment is proper 'if the pleadings, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.'" See Acton v. City of Columbia, Mo., 436 F.3d 969, 975 (8th Cir. 2006), citing Fed. R. Civ. P. 56(c). Viewing the facts as pleaded in the light most favorable to the nonmoving plaintiff, in this case and for the purposes of this motion construing the complaint to be a true and uncontested factual account of the controversy, there is no genuine material factual issue in dispute with respect to a claim against the defendants under 11 U.S.C. § 523(a)(6), and no claim upon which relief may be granted. Defendants are entitled to judgment as a matter of law.

Section 523(a)(6)

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.

See 11 U.S.C. 523(a)(6).

"Generally, debts for breach of contract are not excepted from discharge under section 523(a)(6)." See In re Glatt, 315 B.R. 501, 511 (Bankr. D.N.D. 2004), citing Cutler v. Lazzara (In re Lazzara), 287 B.R. 714, 722 (Bankr. N.D.Ill. 2002). "This is true even in the case of an intentional breach of contract." Glatt, 315 B.R. at 511, citing Petralia v. Jercich (In re Jercich), 238 F.3d 1202, 1205 (9th Cir. 2001), cert. denied,

Jercich v. Petralia, 533 U.S. 930 (2001). "Simple breach of contract ... is not included in the limited exceptions to discharge in bankruptcy." See In re McDowell, 299 B.R. 552, 555 (Bankr. N.D. Iowa 2003). "The exception to discharge in § 523(a)(6) sounds in tort, not breach of contract." See In re Jeffries, 2007 WL 3046649 (Bankr. W.D. Mo. 2007), citing In re Howard, 6 B.R. 256, 257 (Bankr. Fla. 1980). *See also*, In re Rickabaugh, 355 B.R. 743, 758 (Bankr. N.D. Iowa 2006); Integrated Practice Management, Inc. v. Olson (In re Olson), 325 B.R. 791, 801 (Bankr. N.D. Iowa 2005), citing Sandak v. Dobrayel (In re Dobrayel), 287 B.R. 3, 24-25 (Bankr. S.D.N.Y. 2002).

Section 523(a)(6) requires "a deliberate or intentional invasion of the legal rights of another." See Geiger v. Kawaauhau, 113 F.3d 848, 852 (8th Cir. 1997). "[T]he correct rule is that a judgment debt cannot be exempt from discharge in bankruptcy unless it is based on what the law has for generations called an intentional tort, a legal category that is based on 'the consequences of an act rather than the act itself.'" Id., citing Restatement (Second) of Torts § 8A, comment a, at 15 (1965). Under alternative construction, there would be "no reason that a knowing breach of contract would not result in a judgment that would be exempt from discharge." Geiger, 113 F.3d at 852. "Surely this proves too much." Id. "A construction so broad would be incompatible with the 'well-known' guide that exceptions to discharge 'should be confined to those plainly expressed.'" See Kawaauhau v. Geiger, 523 U.S. 57 (1998), citing Gleason v. Thaw, 236 U.S. 558, 562 (1915).

"Essentially, the facts of this case are not distinguishable from any other ordinary breach of contract case, where the debt is dischargeable and the creditor has an unsecured claim in the bankruptcy." See In re Glossip, 331 B.R. 871, 876 (Bankr. W.D. Mo. 2005). "Absent a finding that [the plaintiff] has a property interest ... which could have been injured by the Debtors' actions, the Court cannot, as a matter of law, find that the debt is excepted from discharge pursuant to § 523(a)(6)." Id.

The claim for nondischargeability as advanced by Grobel is not actionable under 11 U.S.C. § 523(a)(6). The pleaded facts demonstrate a breach of contract claim, not an intentional tort. Grobel sold his accounting business to SJA pursuant to a transfer agreement providing a stream of payments from SJA. Johnson, as the sole shareholder of SJA, represented SJA's intention to comply with the terms of the sale. He made a promise to pay, and apparently satisfied that obligation for a relatively brief initial period time. However, Grobel did not retain a secured interest in, for example, SJA's accounts receivable, equipment, or proceeds from sale or assignment of SJA or its assets.

The complaint centrally claims, among other related facts and allegations:

> Defendant Steven J. Johnson, personally made the conveyances set forth and described in sections above with willful and malicious intent to harm Plaintiff in that he personally stripped the corporation of all its assets and abandoned it with malicious and willful intent to deprive Plaintiff of the fruit of his lifelong labor, the value of the accounting practice he spent his life

building and dependent upon in retirement.

Complaint, ¶ 15.

Having failed to secure collateral as part of the transfer agreement, Grobel released his interest in the business in exchange for a promise of a stream of payments. He did not negotiate and obtain a personal guaranty from Johnson. He ultimately did not protect the value and "the fruit of his lifelong labor," and § 523(a)(6) does not operate as a remedy under such circumstances.

Grobel cites many cases in support of the complaint, but all involve secured creditors and one variety or another of conversion of collateral. See In re Clark, 50 B.R. 122 (Bankr. D.N.D. 1985); In re Giffen, 195 B.R. 951 (Bankr. M.D. Fla. 1996); In re Thiara, 285 B.R. 420 (9th Cir. BAP 2002); Randall Bank v. Melhus, 117 B.R. 648 (D. Kan. 1990); In re Smith, 302 B.R. 530 (Bankr. N.D. Miss. 2003); Matter of Brinsfield, 78 B.R. 364 (Bankr. M.D. Ga. 1987); In re Littleton, 942 F.2d 551 (9th Cir. 1991).

The transaction underlying the factual basis of the complaint was unsecured, and therefore the record is devoid of conversion or other allegations of an intentional tort. Grobel cannot assert a right in property and injury by Johnson to such a right. The claim is for breach of contract, and accordingly must fail under § 523(a)(6) at the outset. The fundamental failure under § 523(a)(6) being determinative, the Court need not address the remaining arguments regarding the propriety of naming Jill Johnson as a defendant or piercing the corporate veil to reach Steven Johnson personally.

III. DISPOSITION

IT IS HEREBY ORDERED:

1. Defendants motion for summary judgment is GRANTED;

2. Any debt owing by Steven John Johnson or Jill Marie Johnson to Lloyd Grobel, arising from the facts alleged in the complaint filed in this adversary proceeding, is not excepted pursuant to 11 U.S.C. § 523(a)(6) from the debtors' discharge.

LET JUDGMENT BE ENTERED ACCORDINGLY.

BY THE COURT:

DATED: November 14, 2007

/e/Dennis D. O'Brien
United States Bankruptcy Judge

NOTICE OF ELECTRONIC ENTRY AND
FILING ORDER OR JUDGMENT
Filed and Docket Entry made on 11/14/07
Lori A. Vosejpka, By DLR