UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF	)	
	)	
DANIEL J. FRIDRICH,	)	CASE NO. BK90-80096
	)	
DEBTOR	)	CH. 7

MEMORANDUM

Hearing was held on May 16, 1994, on Motion to Convert filed by the debtor. Appearing on behalf of debtor was Douglas Quinn of McGrath, North, Mullin & Kratz, P.C., Omaha, Nebraska. Appearing on behalf of the Internal Revenue Service (IRS) was Loren Mark of Omaha, Nebraska. This memorandum contains findings of fact and conclusions of law required by Fed. Bankr. R. 7052 and Fed. R. Civ. P. 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(A) and (O).

Background

The debtor, Daniel J. Fridrich, filed a petition for Chapter 7 bankruptcy relief on January 19, 1990. In his bankruptcy schedules, the debtor listed the Internal Revenue Service (IRS) as an unsecured priority claim holder with a claim in the amount of $108,789.29. After it was determined that the debtor had no assets, the debtor was released from all dischargeable debts, and the case was closed on April 4, 1990.

After the Chapter 7 case was closed, the IRS proceeded to enforce its claim through levy and execution procedures. The debtor moved to reopen the bankruptcy case to determine the dischargeability of the IRS's claim and the case was ordered reopened. After the case was reopened, the debtor filed two adversary proceedings. The first adversary proceeding, A90-8059, was filed to determine whether the scheduled IRS claim of $108,208.76 was discharged. The second adversary, A93-8021, requested that additional taxes and penalties, which were assessed after the Chapter 7 case was closed, be determined to be dischargeable. Both parties moved for summary judgment in A90-8059. This Court found, as a matter of law, that 11 U.S.C. § 523(a)(1)(C) included willful attempts to evade or defeat the collection or payment of a tax and denied both motions for summary judgment. The Court made no determination of the fact issues concerning the dischargeability of the IRS claims in this case. The Nebraska District Court and the Eighth Circuit Court of Appeals upheld the bankruptcy court's decision on appeal. See Fridrich v. Internal Revenue Service (In re Daniel J. Fridrich), 8:CV92-00385

(D. Neb. April 12, 1993), aff'd, No. 93-2289 (8th Cir. Sept. 7, 1993).

After the Eighth Circuit upheld the bankruptcy court's order denying summary judgment, the debtor moved to dismiss A90-8059 without prejudice and to dismiss A93-8021 without prejudice. Both motions were granted.

On March 4, 1994, the debtor filed a motion to convert from Chapter 7 to a case under Chapter 13. The total amount of the IRS's claim is listed as $81,022.42 in the debtor's schedules, of which $77,822.42 is treated as a priority claim. The IRS objected to the debtor's motion to convert to a case under Chapter 13. The main IRS objections are that the debtor is proposing to convert this case in bad faith, and that the debtor is not eligible for Chapter 13 relief pursuant to 11 U.S.C. § 109(e).

Discussion and Decision

The debtor's right to convert this case from Chapter 7 to a case under Chapter 13 arises under 11 U.S.C. § 706(a), which provides as follows:

> The debtor may convert a case under this chapter to a case under chapter 11, 12, or 13 of this title at any time if the case has not been converted under section 1112, 1307, or 1208 of this title. Any waiver of the right to convert a case under this subsection is unenforceable.

Generally, under Section 706(a), the debtor's right to convert a case from Chapter 7 to a case under Chapter 13 is absolute. In re Martin, 880 F.2d 857, 859 (5th Cir. 1989) ("a debtor's right to convert under section 706(a) is, as indicated by the statute and its legislative history, an absolute one. The courts refuse to interfere in that right in the absence of extreme circumstances." (citation omitted)). Converting a case from Chapter 7 to another chapter under the Bankruptcy Code is permissible after a discharge has been granted in the Chapter 7 case because "[a]n exhaustive review of the legislative history reveals nothing which would indicate that a post-discharge motion to convert should be treated any differently from any other." Id. (permitting the debtor to convert a Chapter 7 case to one under Chapter 13 after a Chapter 7 discharge was granted). See also In re Kilker, 155 B.R. 201, 202 (Bankr. W.D. Ark. 1993); In re Safley, 132 B.R. 397, 399 (Bankr. E.D. Ark. 1991); In re Sieg, 120 B.R. 533, 535 (Bankr. D.N.D. 1990); 4 **Colliers on Bankruptcy** ¶ 706.01, at 706-3 -- 706-4 (15th ed. 1994).

The Fifth Circuit is the only circuit court to address whether a case may be converted from Chapter 7 to a case under another

chapter of the Bankruptcy Code after a discharge has been granted in the Chapter 7 case. In the case, In re Martin, the Fifth Circuit held that the debtor had an absolute right to convert its case to Chapter 13 from Chapter 7, but declined to address what the effect of a previous discharge in the Chapter 7 case had on the conversion. 880 F.2d at 859-60. The Fifth Circuit noted that while the right to covert was absolute under Section 706(a), that right did not prohibit courts from prohibiting the conversion on other grounds. Id. at 859.

In the Eighth Circuit, some bankruptcy courts have discussed the question of what happens to the discharge granted in the Chapter 7 upon conversion. In In re Sieg, Judge Hill determined that conversion does not "undo the effect of a previously granted discharge." 120 B.R. 533, 535 (Bankr. D.N.D. 1990). The court noted that neither Section 706(a), which allows for conversion, nor Section 348, which sets forth the effects of a conversion on an estate, provides for the vacation or revocation of an order for discharge. The court opined that under 11 U.S.C. § 727(d) and (e), which is the only section in the Bankruptcy Code that permits revocation of a discharge, a motion to revoke a discharge may only be brought by a trustee or a creditor, and revocation of a discharge may only be granted by a court in three instances: "where obtained through fraud, or [where] the debtor fraudulently secreted estate property or where the debtor failed to obey a court order." Id.

In In re Safley, Judge Scott concluded that orders discharging debtors should be treated with finality, and a discharge received in a Chapter 7 case is not entitled to be set aside automatically when a case is converted to one under another chapter. 132 B.R. 397, 400 (Bankr. E.D. Ark. 1991). In an instance where the debtor has not requested a revocation of a discharge, it is appropriate to reorganize only those debts surviving the Chapter 7 discharge. Id.

Both cases cited In re Tuan Tan Dinh, 90 B.R. 743, 745 (Bankr. E.D. Pa. 1988), for the proposition that discharge orders entered in Chapter 7 cases are treated with finality. The more flexible approach of In re Safley comes from the court's analysis of In re Jones, 111 B.R. 674 (Bankr. E.D. Tenn. 1990). Like In re Sieg, In re Jones noted that Section 727(d) and (e) is the only section in the Bankruptcy Code that permits a discharge to be revoked and does not grant the debtor standing to revoke the discharge. 111 B.R. at 679.

In this case, the debtor has not requested and is not permitted to move to revoke his discharge because Section 727(d) and (e) do not allow debtors to request the revocation of a discharge. The debtor may only reorganize debts that were not discharged in the Chapter 7 case and those debts which arose post-discharge. Since the debtor has only scheduled debts in its Chapter 13 schedules that were not discharged in the Chapter 7

case, or not scheduled, there does not appear to be a dispute over this issue.

Even though no direct dispute exists over the issue of whether the discharge may be revoked upon conversion, the discussion becomes important when considering whether other circumstances exist to prevent the debtor from converting the case from Chapter 7 to one under Chapter 13. The IRS alleges that there are two reasons to deny the debtor's motion to convert: (1) the debtor has not filed its motion to convert in good faith; and (2) the debtor is not eligible for Chapter 13 relief.

(1) Good Faith

Bankruptcy courts in the Eighth Circuit have addressed motions to convert by considering the standards for good faith established by the Eighth Circuit in Handeen v. LeMaire (In re LeMaire), 898 F.2d 1346 (8th Cir. 1990) (en banc). In re Sieg, 120 B.R. at 536; In re Kilker, 155 at 202-04. Even though a motion to convert after a discharge has been granted is not bad faith per se, it is treated as a factor to consider in the "totality of the circumstances" test under LeMaire. In re Sieg, 120 B.R. at 536.

LeMaire states that good faith depends upon the following:

> [W]hether the debtor has stated his debts and expenses accurately; whether he has made any fraudulent misrepresentation to mislead the bankruptcy court; or whether he has unfairly manipulated the Bankruptcy Code.

LeMaire, 898 F.2d at 1349 (quoting Education Assistance Corp. v. Zellner, 827 F.2d 1222, 1227 (8th Cir. 1987)). Specifically, the factors to be considered in the "totality of the circumstances" test that are relevant to this case are: "The type of debt sought to be discharged and whether the debt is nondischargeable in Chapter 7, and the debtor's motivation and sincerity in seeking Chapter 13 relief." In re Kilker, 155 B.R. at 203 (listing factors enumerated in LeMaire, 898 F.2d at 1348-49 n. 4, which are relevant to determine whether the conversion is in good faith). Since the debtor has received a Chapter 7 discharge, the Court must consider, in addition to the factors listed above, whether the debtor is improperly manipulating the Bankruptcy Code by now obtaining the benefits of a Chapter 13 case.

In this case, there is not sufficient evidence before the Court to permit the Court to determine whether the debtor filed its motion to convert in good faith. In the Chapter 7 case, the parties did not resolve whether the IRS's debt was dischargeable because the adversary proceedings were dismissed before findings of fact were made. The issue that was appealed, which was a question

of law concerning the willful evasion of taxes, was not the only basis for the debtor's dischargeability complaint.

The IRS alleges that the time spent on the appeal and then on the dismissal of the adversary proceedings is evidence that the debtor is trying to delay the IRS's collection efforts and therefore, is not acting good faith. At this time, there is no evidence to suggest that the debtor has improperly delayed the IRS. The debtor's adversary proceeding raised a significant question of law in the summary judgment motion, and the debtor was exercising his right under the law to appeal the decision of this Court and the Nebraska District Court to the Court of Appeals. The real cause of the delay appears to be waiting for the courts to rule. The delay in obtaining a final decision is not the fault of the debtor.

The IRS further alleges that the conversion to a case under Chapter 13 is a further ruse to delay and harass the IRS. However, it is legitimate for the debtor, upon losing his summary judgment appeal, to reconsider and change his strategy for dealing with the tax obligation. If the debtor legitimately believed that the IRS's debt would be discharged in the Chapter 7 case, he is entitled to change his strategy once it becomes apparent that his original assessment of how to proceed is questionable.

The IRS takes the position that because the debtor has lost a battle, it must concede the war, but the assertions of the IRS are not sufficient, without further evidence, to convince the Court that the motivation of the debtor is and was to harass the IRS.

What does concern this Court regarding the debtor's behavior are discrepancies between the debtor's Chapter 7 schedules and the debtor's Chapter 13 schedules. On Schedule F of the debtor's Chapter 13 schedules, the debtor lists several unsecured debts that on their face look like they should have been scheduled in the Chapter 7 case, but were not. The unsecured debts in question are the claims of Amoco Oil Company, Dan R. Fridrich, and Thomas J. Fridrich. All three of these debts list as the date the claim was incurred a date before the filing of the Chapter 7 case. If they were incurred or partially incurred before the Chapter 7 case, the debtor's Chapter 7 Schedules should have reflected those debts. This Court is most concerned with the debts to Dan Fridrich and Thomas Fridrich, and whether those claim holders, who are presumably relatives, received favorable treatment by not being discharged in the Chapter 7 case. On the other hand, the discrepancies in the schedules are not sufficient evidence of bad faith on the part of the debtor because the Chapter 13 plan proposed by the debtor will permit a discharge of these newly listed debts with little or no payment.

The final question regarding the debtor's good faith is whether the debtor filed the case solely to avoid the IRS's tax

debt and whether that debt would have been nondischargeable in the Chapter 7 case. An evidentiary hearing is necessary to develop the facts concerning "good faith."

(2) Chapter 13 Eligibility

11 U.S.C. § 109(e) provides:

> [O]nly an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than $100,000 and noncontingent, liquidated, secured debts of less than $350,000 ... may be a debtor under chapter 13 of this title.

A party may not convert a case from Chapter 7 of the bankruptcy code to one under Chapter 13 if the debtor is not eligible for Chapter 13 relief under Section 109(e). In re Safley, 132 B.R. at 399.

In this case, the debtor listed on his Chapter 7 schedules that the IRS held a priority unsecured claim in the amount of $108,789.29, and at the time the adversary proceeding was brought, the debtor alleged that the same claim was worth $107,789.92. In addition to the scheduled amount, the debtor's second adversary proceeding alleged approximately $58,160.20 in additional claims of the IRS. Clearly, the amount of unsecured debt of just the IRS, which was disclosed by the debtor in the Chapter 7 case, would preclude the debtor from Chapter 13 relief because the debtor's unsecured debts were not less than $100,000.

In the debtor's Chapter 13 schedules, the debtor alleges in Schedule E that the IRS's claim is much lower because the IRS's total claim is for $81,022.42, of which $77,822.42 is listed as an unsecured priority claim. All of the debtor's unsecured priority claims added together amount to $99,202.42. In addition to the unsecured priority claims, the debtor also lists on Schedule F $5,979.53 in general unsecured claims that have arisen since the debtor's discharge. Together, all unsecured claims amount to $105,181.95, which is not less than the $100,000 ceiling for Chapter 13 eligibility. Therefore, based on the debtor's schedules, the debtor is not eligible for Chapter 13 relief.

The debtor has alleged, however, that the IRS's claim may not be accurate. Since this is a question of fact, it is necessary to set a hearing to determine whether the debtor is eligible for Chapter 13 relief. Other than the debtor's schedules, the only evidence that suggests the amount of the IRS's claim is a Declaration submitted by the IRS. (Declaration: Robert Wilson, Def. Ex. 3). (The IRS did not file a claim in the Chapter 7 case.) If the debtor has a valid legal or factual objection to the IRS

claims, he should be allowed to present such objection to counter his apparent ineligibility for Chapter 13 relief.

Conclusion

The clerk is directed to set a hearing concerning the following fact issues: (1) Whether the debtor is acting in good faith by moving to convert his Chapter 7 case to one under Chapter 13; and (2) Whether the debtor is eligible for Chapter 13 relief under 11 U.S.C. § 109(e).

Separate journal entry to be entered.

DATED: June 17, 1994.

BY THE COURT:

/s/ Timothy J. Mahoney
Timothy J. Mahoney
Chief Judge

CC: Movant, Debtor(s) Atty. and all parties appearing at hearing
[ ] Chapter 13 Trustee [ ] Chapter 12 Trustee [ ] U.S.Trustee

Movant is responsible for giving notice of this journal entry to any parties in interest not listed above.

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF	
DANIEL J. FRIDRICH,	CASE NO. BK90-80096 A
DEBTOR(S)	CH. 7
	Filing No.
Plaintiff(s) vs.	JOURNAL ENTRY
Defendant(s)	DATE: June 17, 1994 HEARING DATE: May 16, 1994

Before a United States Bankruptcy Judge for the District of Nebraska regarding Motion to Convert filed by the debtor.

APPEARANCES

Douglas Quinn, Attorney for debtor
Loren Mark, Attorney for IRS

IT IS ORDERED:

The clerk is directed to set a hearing concerning the following fact issues: (1) Whether the debtor is acting in good faith by moving to convert his Chapter 7 case to one under Chapter 13; and (2) Whether the debtor is eligible for Chapter 13 relief under 11 U.S.C. § 109(e). See memorandum entered this date.

BY THE COURT:

/s/ Timothy J. Mahoney
Timothy J. Mahoney
Chief Judge

CC: Movant, Objector/Resistor (if any), Debtor(s) Atty. and all parties appearing at hearing
[ ] Chapter 13 Trustee [ ] Chapter 12 Trustee [ ] U.S.Trustee

Movant is responsible for giving notice of this journal entry to all other parties if required by rule or statute.