ORDER

AND NOW, this **5th** day of **JUNE, 2007**, after consideration of the Motions of the MDC Defendants, Winstead Sechrest & Minick, P.C. ("Winstead"), and Robert J. Naples ("Naples") for dismissal of the Trustee's complaint against them and the Trustee's opposition thereto, it is hereby,

ORDERED that the Motions to Dismiss are **GRANTED** in part and **DENIED** in part; and it is further

ORDERED that the count against the MDC Defendants and Naples for actual fraudulent transfers is **DISMISSED,** with leave to amend the Complaint within thirty days hereof to state fraud with sufficient particularity; and it is further

ORDERED that the constructively fraudulent transfer count against the MDC Defendants and Naples is **DISMISSED**, with leave to amend the Complaint within thirty days hereof to add the required details; and it is further

ORDERED that the preferential transfer count against George McCown, Robert Hellman, and Robert Naples is **DISMISSED;** and it is further

ORDERED that the claim against McCown De Leeuw & Co., Inc. ("MDC") under section 550 for recovery of payments made by the Debtors to TIAA and remitted to MDC is **DISMISSED;** and it is further

ORDERED that the civil conspiracy count against the MDC Defendants, Naples and Winstead is **DISMISSED,** but the Trustee is granted leave to amend the count to add sufficient facts; and it is further

ORDERED that the aiding and abetting a breach of fiduciary duty count against Winstead is **DISMISSED,** with leave to amend the Complaint within thirty days hereof to add more detail; and it is further

ORDERED that the fraudulent transfer count against Winstead is **DISMISSED,** however, the Trustee is granted leave to amend the count to provide sufficient factual allegations; and it is further

ORDERED that the requested declaratory relief claim against Winstead for claim disallowance and subordination is **DISMISSED.**

In the Matter of Clarence Alfred REATH, a/k/a Al Reath, Debtor.

Jill Cochran t/a Cochran & Company, Plaintiff

v.

Clarence Alfred Reath, a/k/a Al Reath, Defendant.

Bankruptcy No. 04–49188/JHW. Adversary No. 05–1493.

United States Bankruptcy Court, D. New Jersey.

April 27, 2006.

Background: In Chapter 7 case, sales repping organization commenced adversary proceeding seeking determination that its claim against debtor for breach of non-compete clause in independent contractor's agreement was nondischargeable. Bench trial was held.

Holdings: The Bankruptcy Court, Judith H. Wizmur, Chief Judge, held that:

(1) organization's claims did not fall within scope of discharge exception for false representations, false pretenses, or actual fraud, and

(2) organization's claims did not fall within scope of discharge exception for willful and malicious injury.

Judgment for debtor.

1. Bankruptcy ⇨3403(1), 3405(13)

Creditor asserting that her claim is non-dischargeable has burden of establishing all elements of exception to discharge by preponderance of evidence. 11 U.S.C.A. § 523.

2. Bankruptcy ⇨3341

Exceptions to discharge are to be construed strictly against creditors and liberally in favor of debtors. 11 U.S.C.A. § 523.

3. Bankruptcy ⇨3372.14, 3372.16, 3372.19

Frauds covered by discharge exception for false pretenses, false representation, or actual fraud are those which in fact involve moral turpitude or intentional wrong; fraud implied in law, which may be established without imputation of bad faith or immorality, is insufficient. 11 U.S.C.A. § 523(a)(2)(A).

4. Bankruptcy ⇨3372.1

For purposes of discharge exception, false representation or false pretense involves (1) knowing and fraudulent falsehoods, (2) describing past or current facts, (3) that were relied upon by other party. 11 U.S.C.A. § 523(a)(2)(A).

5. Bankruptcy ⇨3372.8, 3372.14

For purposes of discharge exception, "actual fraud" consists of any deceit, artifice, trick, or design involving direct and active operation of mind, used to circumvent and cheat another-something said, done, or omitted with design of perpetuating what is known to be cheat or deception. 11 U.S.C.A. § 523(a)(2)(A).

See publication Words and Phrases for other judicial constructions and definitions.

6. Bankruptcy ⇨3372.1

To establish nondischargeability under discharge exception for false pretenses, false representation, or actual fraud, plaintiff must show that (1) debtor made misrepresentations; (2) at that time he knew they were false; (3) he made them with intention and purpose of deceiving creditor; (4) creditor relied on such representations; and (5) creditor sustained alleged loss and damage as proximate result of representations having been made. 11 U.S.C.A. § 523(a)(2)(A).

7. Bankruptcy ⇨3372.1, 3372.17

Sales repping organization's claims against Chapter 7 debtor for breach of non-compete clause and breach of his duties as sales manager did not fall within scope of discharge exception for false representations, false pretenses, or actual fraud, even though debtor's subsequent employer carried product lines organization had previously carried, debtor had contact with same customers, and debtor did not promptly inform organization that sales representatives under his supervision represented competing products, where there was no evidence that debtor caused loss of lines or represented lines for competitor, debtor did not attempt to cause customers to discontinue business with organization or to convince other sales representatives to change employers, debtor informed organization of representative's breaches within two or three weeks, and there was no evidence of intent to deceive. 11 U.S.C.A. § 523(a)(2)(A).

8. Bankruptcy ⇨3374(2)

For purposes of discharge exception for willful and malicious injury, nondischargeability takes deliberate or intentional injury, not merely deliberate or intentional act that leads to injury. 11 U.S.C.A. § 523(a)(6).

9. Bankruptcy ⚿3374(3)

Recklessly or negligently inflicted injuries do not fall within compass of discharge exception for willful and malicious injury. 11 U.S.C.A. § 523(a)(6).

10. Bankruptcy ⚿3374(9)

Sales repping organization's claims against Chapter 7 debtor for breach of non-compete clause and breach of his duties as sales manager did not fall within scope of discharge exception for willful and malicious injury, even though debtor's subsequent employer carried product lines organization had previously carried, debtor had contact with same customers, and debtor did not promptly inform organization that sales representatives under his supervision represented competing products, where debtor's two or three week delay in informing organization was occasioned by his desire to afford sales representatives chance to take up issue directly with organization, and there was no evidence that debtor played role in subsequent employer's acquisition of product lines. 11 U.S.C.A. § 523(a)(6).

John J. Palitto, Jr., Esq., Blackwood, NJ, for Plaintiff.

Debra L. Sherlock, Esq., Reger, Rizzo, Kavulich & Darnall, LLP, King of Prussia, PA, for Defendant.

OPINION

JUDITH H. WIZMUR, Chief Judge.

In this adversary proceeding, the plaintiff, Jill Cochran, trading as "Cochran & Company," (the "Company"), seeks a determination that her claim is nondischargeable under 11 U.S.C. § 523(a)(2)(A) and/or § 523(a)(6). The plaintiff contends that the debtor's actions caused her to suffer a loss that was incurred as the result of the debtor's false representations, false pretenses or actual fraud, and/or the willful and malicious injury he inflicted her and her business.

A trial on this adversary proceeding was conducted on October 18 and 19, 2005. The parties offered only the testimony of Reath and Cochran in support of their positions.[1] I conclude on this record that the plaintiff has failed to meet her burden under either section 523(a)(2)(A) or section 523(a)(6) and that the defendant's unliquidated debt to her, if any, may be discharged.

FACTS AND PROCEDURAL HISTORY

The plaintiff is the sole proprietor of Cochran & Company, a business which represents manufacturers and importers in the gift industry who sell their products to retailers within the Company's territory, the Mid–Atlantic region. The Company utilizes sales personnel who are employed as independent contractors ("sales reps"), each of whom has an assigned local territory in which she or he sells a variety of product lines to retailers. The manufacturers pay the Company, referred to as a "sales repping organization," on a commission basis. The Company, in turn, pays the sales reps a portion of the commissions based upon their sales.

The Company also represents the manufacturers at various gift industry trade shows, primarily at the Philadelphia Gift Show, held in January and July of each year. The Company rents space at the show and hires hourly workers to set up presentation booths to display the manufacturers' products. The commissioned

1. On October 17, 2005, the defendant filed a Motion in Limine to preclude the plaintiff from introducing any documents or witnesses at trial given plaintiff's failure to file a Pretrial Memorandum listing same. I denied this motion without prejudice on the first day of trial.

sales reps then present the Company's lines to retailers during the show.

On May 1, 1995, the defendant, Clarence Alfred Reath, signed an Independent Contractor's Agreement (the "Agreement") with Cochran & Company, in which he was designated as an "I.C." or "Independent Contractor," having the sales territory of southern New Jersey. The Agreement authorized Reath to represent the Company in selling to retailers, and provided for compensation of a commission basis. The Agreement allowed him to terminate his relationship with the Company for any reason, so long as he gave reasonable written notice. Conversely, the Agreement allowed the plaintiff to terminate his employment for "good cause," defined as the "I.C.'s failure substantially to comply with the material and reasonable requirements imposed by Cochran for its accounts." [2]

The Agreement included a non-compete clause, which states:

> *AGREEMENT AGAINST COMPETITION:* In consideration of an initial or continued relationship of I.C. with Cochran, I.C. agrees that during the term of this Agreement, which shall include all extensions and renewals, and for a period of one (1) year after termination of this Agreement, however occasioned, I.C. will not:
>
> a. Cause or attempt to cause any manufacturer, other I.C., or customer of Cochran, with which I.C. worked or whose account I.C. supervised at any time during I.C.'s Agreement with Cochran, to terminate, limit, or in any matter modify or fail to enter into or continue in any actual or potential business relations with Cochran.
>
> b. I.C. shall not represent competing lines without the prior written authorization of Cochran. Such authorization shall not be unreasonably withheld.
>
> c. I.C. covenants and agrees not to represent, either as I.C. or employee of another sales organization, any manufacturer represented by Cochran during the term of this Agreement, which includes all extensions and renewals and for a period of one (1) year after termination of this Agreement, by whatever means. This paragraph shall be deemed to have survived for one (1) year beyond the termination of this Agreement.[3]

The Agreement signed by Reath was substantially the same standard form used for all of the Company's sales reps.[4]

According to the plaintiff, Reath served as a sales rep throughout his employment with the Company, working closely with his daughter, Yvonne Glauner, who was also a sales rep for the Company. The plaintiff explained that Reath was not paid commissions directly by the Company because he was receiving Social Security benefits, and he had asked that his commissions be paid instead to his daughter. Reath acknowledged that he signed the IC Agreement, but denied that he ever functioned as a sale rep for the company.[5] He claimed that he was accustomed to serve as a driver for his daughter to retail stores and to assist her with carrying and displaying product lines. Twice a year, he was hired by the Company to oversee the setup of the Company's booths for the trade shows, for which he was paid by the hour. Reath explained that he had signed

2. Exh. D–1, Independent Contractor's Agreement, ¶ 8.

3. Exh. D–1 at ¶ 10.

4. T14–16 to 17 (10/18/05).

5. T149–13 through 150–9 (10/18/05).

the Agreement at the plaintiff's insistence, given his close working relationship with his daughter.

I can readily reconcile the testimony of the plaintiff and Mr. Reath regarding Reath's role with the Company. Reath and Glauner worked as a team, servicing the South Jersey region for the Company since 1995. Reath, a retiree, lived with his daughter, worked in her gift shop, drove her to sales meetings, trade shows and to retailers, and assisted her in transporting her samples. Reath assisted Glauner in securing samples from manufacturers, as evidenced by the "memo bill" invoices accompanying the samples which were addressed to him.[6] While on the road with Glauner or in a booth at a trade show, Reath also assisted his daughter in filling out and processing retailers' orders.[7] Reath's name was also on Glauner's business cards. All commissions arising from their joint efforts were paid to Glauner.

Reath's responsibilities were expanded in March 2002, when he became the plaintiff's Sales Manager. Reath's enhanced role was memorialized in a letter from the plaintiff dated February 25, 2002, with an accompanying "Sales Manager Job Description", both of which were countersigned or initialed by Reath.[8] The letter notes that the defendant would receive "1% of the commissions" received by the Company for sales generated by the supervised sales reps. Generally, as Sales Manager, Reath was responsible to hire, manage and motivate the sales reps.

Because Reath comprised part of a sales team with Glauner throughout his time with the Company, even while he performed his duties as Sales Manager starting in early 2002, Reath remained bound to the terms of the original Agreement until his resignation from the Company in November 2003.

Reath became Sales Manager at a time when the Company's revenues, which had grown every year since the plaintiff started doing business as "Cochran & Company" in 1982, were declining. Revenues declined from 2001 to 2002 and again from 2002 to 2003. From 2002 on, many of the manufacturers represented by the Company were lost, *i.e.*, previously represented wholesalers dropped the Company as their regional sales repping organization. Of the manufacturers who terminated their relationship with the Company, Reath testified that Great Finds, Nature's Own, Center Street Designs and Legacy Publishing represented "A" lines of the company, *i.e.*, large and profitable accounts.[9] By the time Reath left the company in late 2003, Reath estimated that the Company had lost nearly 50% of its business due to the loss of the "A" lines noted.

By letter dated November 16, 2003, Reath resigned from the Company. He wrote:

> Dear Jill,
>
> After receiving a message from Posies and Such, I am aware that you know of Yvonne and Diana repping the line for Sandy Sciria. They are also repping three other lines for Sandy. They are Babba Sox, Twinklers, and Briarpatch. I take full responsibility for keeping this from you.
>
> Having said this, I must also inform you that Yvonne also reps three lines for Van & Co. They are Beanpod, Wongs, and Abdallah Candies.
>
> Now that this has made you aware and that I have been less than truthful about these things, I feel that I should submit

6. Exh. P–4.

7. Exh. P–5.

8. Exh. D–2.

9. T71–2 to 3, 72–4 to 5 (10/19/05).

my resignation from Cochran & Co. effective immediately. I will offer my service to you for the Philadelphia Gift Show in January if you so desire but after the show I will no longer be involved with Cochran & Co.

Thank you,

Al Reath [10]

Sandy Sciria refers to a sales repping organization based in Albany that is a competitor of the Company. Although the Company did not represent Posies and Such, the plaintiff had been trying to acquire the Posies and Such line as a represented wholesaler. Van & Co., another sales repping organization, is also a competitor of the Company. In Reath's letter, "Yvonne" is Yvonne Glauner, his daughter, then the Company's sales rep for southern and central New Jersey. "Diana" is Diana Culbertson, then the Company's sales rep in Delaware and for Maryland's Eastern Shore.[11] Following Reath's resignation, later in November, the plaintiff fired Glauner. It appears that Culbertson and Arrington then resigned.

The plaintiff contends that Reath terminated his relationship with the Company in bad faith, or with malicious intent, as evidenced by the events both preceding and following his resignation. The Company was accustomed to having a sales meeting with all active sales reps twice a year, in the spring and in the fall. According to the plaintiff, Reath insisted on canceling the spring 2003 sales meeting. Instead, in May 2003, he attended a meeting at the home of Pamela J. Noffke, plaintiff's former secretary, who had begun her own competing sales repping organization, Pamela J's Gifts ("Pamela J"), in 2003. The plaintiff characterized the May 2003 session as a "sales meeting". Reath also visited Ms. Noffke's home in October 2003. In the directory for the 2004 Philadelphia Gift Show, which was printed in November 2003, the advertisement for Pamela J's Gifts lists Reath, Glauner, Arrington and Culbertson as the sales reps for Pamela J. Plaintiff submits that these events demonstrate Reath's defection to Pamela J, while he was still working for her Company. The plaintiff believes that Reath and the three sales reps, moving as a team, initially worked for Pamela J when they left her company, and then switched to another sales repping organization, Jack Huisman and Co., when Pamela J ceased to operate.

Reath consistently denied that he worked for Pamela J at any time. According to Reath, he and his daughter became friends with Ms. Noffke, having met her while she was the plaintiff's secretary from 2001 to early 2003. They would occasionally visit Pamela and her husband, Steven T. Noffke at their home in Pennsylvania. The Noffkes would reciprocate with visits to the Reath home in New Jersey. Reath recalls that one evening in May 2003, he and his daughter went to visit the Noffkes, and were surprised to see several sales reps at the home. He acknowledges that discussions ensued regarding sales and business matters, but denies that he or Glauner ever worked for Pamela J. He could not explain why his name, his daughter's name, and the names of the two other Company reps appeared in Pamela J's advertisement in the 2004 Philadelphia Gift Show program, but speculated that perhaps Pamela J hoped that he and the other sales reps would come to work for the new company at the 2004 Philadelphia Gift Show in January 2004.

10. Exh. P–1.

11. Not mentioned in Reath's letter was Laurie Arrington, the third Company sales rep, whose territory was Virginia, and who was apparently also involved in selling Posies and Such.

Within six weeks after leaving the Company, Reath began working for Huisman, and represented Huisman at the January 2004 Philadelphia Gift Show. Glauner, Arrington, and Culbertson also worked for Huisman at that show. While Reath believed that working for Huisman did not violate the non-compete clause because Huisman sold "mostly garden center stuff" [12] and did not represent lines that competed with the Company, the plaintiff described Huisman as a direct competitor. She claimed that some of the lines that the Company had lost, such as Nature's Own and Great Finds, took on Huisman as a sales repping organization after Reath joined Huisman. The plaintiff believed that after Reath and the other Company sales reps joined Huisman, Huisman's Philadelphia sales rep approached many of the same retailers serviced by the Company. The plaintiff asserted that the Company not only sold "garden center oriented" lines, but that garden centers, including some big accounts, could and did carry more conventional giftware.[13]

Reath filed his Chapter 7 bankruptcy petition on December 15, 2004, listing the plaintiff, trading as the Company, as an unsecured creditor.[14] On March 21, 2005, the plaintiff filed this adversary proceeding against the debtor. She asserts that, because of the debtor's disloyalty to her and her Company, as well as the debtor's related breaches of the Agreement and his responsibilities as the Company's Sales Manager, any debt due her from Reath is non-dischargeable under 11 U.S.C. §§ 523(a)(2) and (a)(6). That is, the plaintiff claims that Reath's conduct constituted "false pretenses, a false representation, or actual fraud," and that Reath inflicted injuries upon her with the required "willful and malicious" intent.

12. T141–14 to 18 (10/18/05).

13. T15–21 to 25 (10/19/05).

DISCUSSION

The Bankruptcy Code ("Code") is designed to relieve debtors from the weight of oppressive indebtedness and to provide them with a "fresh start." *In re Cohn*, 54 F.3d 1108, 1113 (3d Cir.1995). This "fresh start" is available only to the "honest but unfortunate debtor." *Grogan v. Garner*, 498 U.S. 279, 287, 111 S.Ct. 654, 659, 112 L.Ed.2d 755 (1991); *In re Fegeley*, 118 F.3d 979, 983 (3d Cir.1997); *In re DeBaggis*, 247 B.R. 383, 388 (Bankr.D.N.J.1999).

[1, 2] Not all debts owed by an individual debtor are discharged in bankruptcy. Certain debts, listed in section 523, are excepted from discharge. The plaintiff has the burden of establishing all elements of a section 523 exception to discharge by a preponderance of the evidence. *Grogan*, 498 U.S. at 287–88, 111 S.Ct. at 659–60. Exceptions to discharge are to be construed strictly against creditors and liberally in favor of debtors. *Cohn*, 54 F.3d at 1113.

To assert that her claim is non-dischargeable, the plaintiff relies on sections 523(a)(2)(A) and 523(a)(6) of the Bankruptcy Code.

1. *Section 523(a)(2)(A)*

Debts based upon fraud are nondischargeable pursuant to 11 U.S.C. § 523(a)(2)(A), which provides:

> (a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this

14. Due to the debtor's filing, the state action by the plaintiff against the debtor and others, which is pending in the Court of Common Pleas in Chester County, Pennsylvania, was stayed.

> title does not discharge an individual debtor from any debt—
>
> . . .
>
> (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—
>
> (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition.

Section 523(a)(2)(A) does not define the terms false pretenses, false representation, or actual fraud.[15] Nor does the section expressly refer to elements such as reliance, materiality or intent. Nonetheless, courts have routinely inferred requirements establishing intent, reliance and materiality in applying section 523(a)(2)(A). *See, e.g., In re Menna,* 16 F.3d 7 (1st Cir.1994); *In re Martin,* 963 F.2d 809 (5th Cir.1992); *In re Phillips,* 804 F.2d 930 (6th Cir.1986).

[3–5] The frauds covered by the terms used in section 523(a)(2)(A) are those which "in fact involve moral turpitude or intentional wrong; fraud implied in law, which may be established without imputation of bad faith or immorality, is insufficient." 4 LAWRENCE P. KING, COLLIER ON BANKRUPTCY ¶ 523.08[1][d] at 523–44.9 (15th Rev. Ed.2006) [hereinafter "COLLIER"]. A false representation or false pretense involves: "(1) knowing and fraudulent falsehoods, (2) describing past or current facts, (3) that were relied upon by the other party." *In re Allison,* 960 F.2d 481, 483 (5th Cir.1992); *RecoverEdge L.P. v. Pentecost,* 44 F.3d 1284, 1293 (5th Cir.1995). " 'As distinguished from false representation, which is an express misrepresentation[,] false pretense involves an implied misrepresentation or conduct intended to create and foster a false impression.' " *In re Brandon,* 297 B.R. 308, 313 (Bankr.S.D.Ga.2002) (quoting *In re Weinstein,* 31 B.R. 804, 809 (Bankr.E.D.N.Y. 1983)). Actual fraud " 'consists of any deceit, artifice, trick, or design involving direct and active operation of the mind, used to circumvent and cheat another-something said, done or omitted with the design of perpetuating what is known to be a cheat or deception.' " *RecoverEdge L.P.,* 44 F.3d at 1293 (quoting COLLIER ¶ 523.08[1][e] at 523–45).

[6] To establish nondischargeability under section 523(a)(2)(A), plaintiff must show that:

> (1) the debtor made the misrepresentations;
>
> (2) that at the time he knew they were false;
>
> (3) that he made them with the intention and purpose of deceiving the creditor;
>
> (4) that the creditor relied on such representations;
>
> (5) that the creditor sustained the alleged loss and damage as the proximate result of the representations having been made.

In re Hashemi, 104 F.3d 1122, 1125 (9th Cir.), *cert. denied,* 520 U.S. 1230, 117 S.Ct. 1824, 137 L.Ed.2d 1031 (1997); *In re Kirsh,* 973 F.2d 1454, 1457 (9th Cir.1992) (quoting *In re Britton,* 950 F.2d 602, 604 (9th Cir.1991)). *See also In re Reynolds,* 193 B.R. 195, 200 (D.N.J.1996); *In re Cohen,* 191 B.R. 599, 604 (D.N.J.1996).

15. In contrast, the text of section 523(a)(2)(B), which addresses materially false statements regarding the debtor's financial condition, specifically requires the debt to be incurred through the use of a written statement: (1) regarding the debtor's financial condition; (2) that was materially false; (3) upon which the plaintiff had reasonably relied; and (4) which the debtor made or published with the intent to deceive the creditor. *See also Cohn,* 54 F.3d at 1114.

[7] The plaintiff has failed to substantiate her contention that either the debtor's alleged breach of the Agreement, or his alleged breach of his duties as a Sales Manager, constituted false representations, false pretenses or actual fraud. As to the Agreement, Reath agreed in the non-compete clause not to represent, either as an Independent Contractor for the Company, or as an employee of another sales organization, any manufacturer represented by the Company during the term of the Agreement, and for a period of one year after termination of the Agreement. He also agreed not to "[c]ause or attempt to cause any manufacturer, other I.C., or customer of Cochran, with which I.C. worked or whose account I.C. supervised at any time during I.C.'s Agreement with Cochran, to terminate, limit, or in any matter modify or fail to enter into or continue in any actual or potential business relationship with Cochran." [16] The plaintiff interpreted these clauses broadly to include selling "similar products, or ... competing for the retailers' time, dollars and store space, all of which are limited." [17]

Reath acknowledged that he commenced his employment with Jack Huisman and Co. two months after he terminated his employment with the Company. Such employment was not proscribed by the agreement between the parties. The plaintiff testified that she believes that the Huisman organization picked up several product lines that had been represented by the Company while Reath was working there, including Great Finds and Nature's Own. However, the plaintiff produced no evidence that Reath caused either of those lines to fail to continue their business relationship with the Company. In fact, one of the lines, Great Finds, was lost by the Company about eighteen months before Reath left, while the other account, Nature's Own, was lost about six months before Reath left.[18] Nor is there direct evidence in the record that Reath actually represented either of these lines at Huisman himself during the one year after he left the Company.

Reath testified that while he was working for Huisman, he had contact with some of the same customers that were serviced by Cochran.[19] He correctly noted that the non-compete clause of the Agreement did not bar him from having any contact with Cochran's customers. The only type of contact that was proscribed was any attempt by the debtor to cause a customer to limit, modify or fail to continue in any actual or potential business relationship with Cochran. No such specific proofs were adduced.

The proofs presented do not substantiate the conclusion that the debtor breached either of these provisions of the Agreement. Even if Reath breached the Agreement through his contact with the plaintiff's customers, post resignation, there is no support for the proposition that such breach constituted false representations, false pretenses or actual fraud.

Further, the plaintiff has failed to establish that the debtor began to work for another sales repping organization, Pamela J's, before he resigned from the Company, or that he solicited the plaintiff's other sales reps to leave the plaintiff, or to cause the other sales reps to solicit product lines that competed with the plaintiff's customers. The plaintiff has established only that:

16. Exh. D–1, ¶ 10.

17. T15–21 to 23 (10/18/05).

18. The Company lost the Great Finds account in June 2002, and lost the Nature's Own line in March 2003.

19. *Id.* at T142–7 to 20.

1. Reath was at Pamela J's home on two occasions, in May and October, 2003;
2. In May, other Company sales reps were at the Noffke home at the same time;
3. Reath and two of the Company's active sales reps, Glauner and Culbertson, were listed as Pamela J's sales reps in a publication that was printed around November 2003;
4. Reath acknowledged in his November 16, 2003 letter of resignation that he failed to inform the plaintiff that several sales reps were repping several product lines for two of the plaintiff's competitors, and
5. Reath and the Company's three active sales reps, including Glauner, Culbertson and Arrington, commenced their employment with Huisman, a competitor of the plaintiff, in January 2004.

Reath testified credibly that he had never worked for Pamela J's, and that he did not know why he was listed as a sales rep in the publication. He also testified credibly that he discovered that Glauner and Culbertson were repping several product lines for competing organizations at the end of October 2003. He failed to inform the plaintiff promptly because he wanted to give the sales reps a chance to inform the plaintiff on their own.[20] He went on vacation in early November, and discovered when he came back that the plaintiff knew about the activities of Glauner and Culbertson. There is no evidence in this record of any sort that Reath solicited the sales reps to represent competing product lines or to join a competing sales repping company.

The plaintiff also contends that the debtor fraudulently breached his obligations as Sales Manager because he represented that "he would manage the sales force [and] [t]he representation at some point became false when his—when he repped other lines while working, while his force was working for others, and he did nothing about it."[21] It is recognized that a debtor's silence regarding a material fact can rise to the level of fraud, where it regards a material fact. *In re Docteroff,* 133 F.3d 210, 216 (3d Cir.1997); *In re Trombadore,* 201 B.R. 710, 714 (D.N.J.1996), *aff'd,* 129 F.3d 1256 (3d Cir.1997). However, the debtor's silence regarding the activities of the sales reps in late October and early November 2003 does not rise to that level. In delaying to impart information about the sales reps to the plaintiff, Reath acted within his discretion as Sales Manager to offer the sales reps the opportunity to seek plaintiff's authorization to represent non-Company lines, as allowed by ¶ 10.b of the Independent Contractor Agreement. Following a brief interval of approximately two to three weeks, Reath informed the plaintiff of the situation.

More broadly, the plaintiff suggests that the debtor conspired to impair the plaintiff's business by working for Pamela J's while he acted as the Company's Sales Manager, solicited or caused the sales reps to represent other product lines and competitors of the Company, and generally violated his duty of loyalty, as Sales Manager, to the Company. The plaintiff has failed to establish these allegations as well. The debtor testified credibly that he never worked for Pamela J's. The only evidence produced regarding such alleged employment was the debtor's presence at Ms.

20. Subsection b of ¶ 10, the non-compete clause of the Independent Contractor Agreement, permits an Independent Contractor to represent competing lines with "the prior written authorization of Cochran ... [which] shall not be unreasonably withheld."

21. T69–12 to 16 (10/19/05).

Noffke's home on two occasions, and his listing as a representative of Pamela J in a publication printed in November, 2003. Nor is there evidence in this record to support the proposition that the debtor solicited or encouraged the other sales reps to violate their non-compete clauses. The fact that the debtor and the three sales reps who were fired or resigned after Reath resigned in November became employed by the same sales repping organization six weeks later does not provide sufficient basis to establish a "deceit, artifice, trick or design" employed by the debtor that would be reflective of actual fraud. *RecoverEdge LP,* 44 F.3d at 1293.[22]

Even if the plaintiff successfully established that the debtor breached his Agreement with the Company in some way, or breached his duty to the Company as a Sales Manager, such breaches would not necessarily constitute false representations, false pretenses, or actual fraud. Without a demonstration of an intent to deceive, proof of a breach of contract cannot support a section 523(a)(2)(A) non-dischargeability finding.

> A bare promise to be fulfilled in the future, which is not carried out, does not render a consequent debt nondischargeable under § 523(a)(2)(A). *Schwalbe v. Gans (In re Gans),* 75 B.R. 474, 486 (Bankr.S.D.N.Y.1987). An unfulfilled promise to perform in the future is actionable only in contract. It is insufficient under § 523(a)(2)(A) simply to show that debtor left unfulfilled a prior oral representation or promise. Were this showing sufficient, virtually every oral obligation would give rise to a nondischargeable debt under § 523(a)(2)(A). A fraudulent promise under § 523(a)(2)(A) requires proof that at the time the debtor made it, he or she did not intend to perform as required. *Seepes v. Schwartz (In re Schwartz),* 45 B.R. 354, 357 (S.D.N.Y.1985). In other words, Plaintiff herein must establish that Defendant had no intention of repaying when he obtained the loan and she has failed to do so. We recognize that fraudulent intent, intent to deceive or scienter can be inferred, since direct proof of state of mind is rarely available. Plaintiff, however, errs in assuming fraudulent intent can be presumed. Fraudulent intent may be inferred; it cannot be presumed.

In re Balzano, 127 B.R. 524, 531 (Bankr. E.D.N.Y.1991).

Here, there is no support for either the proposition that the debtor did not intend to perform his duties as an Independent Contractor or as the Sales Manager for the Company when he agreed to act in those capacities, or that he intended to deceive the plaintiff in any way by his activities. While Reath may have had a "continuing obligation" to abide by his employment agreements as a matter of contract law, any breach by the debtor of his contractual obligations to the plaintiff does not give rise to the necessary intent to deceive by the debtor which is required under section 523(a)(2)(A). Plaintiff has failed to meet her burden to show that the defendant's debt to her, if any, should be declared non-dischargeable under 11 U.S.C. § 523(a)(2)(A).

2. *Section 523(a)(6)*

[8, 9] Section 523(a)(6) provides that:

> (a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this

22. In fact, plaintiff's counsel acknowledged at trial that the "actual fraud" standard would not apply: "I believe I must concede under both New Jersey and Pennsylvania law for actual fraud, there must be a representation which was false at the time that it was made, and I don't think we can show that." T65–11 to 15 (10/19/05).

> 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.

11 U.S.C. § 523(a)(6). Section 523(a)(6) requires an act that is both "willful" and "malicious". "Willful" is generally understood to mean voluntary, intentional or deliberate. *Kawaauhau v. Geiger,* 523 U.S. 57, 61 n. 3, 118 S.Ct. 974, 977 n. 3, 140 L.Ed.2d 90 (1998). "The word 'willful' in (a)(6) modifies the word 'injury,' indicating that nondischargeability takes a deliberate or intentional injury, not merely a deliberate or intentional act that leads to injury." *Id.* at 61, 118 S.Ct. at 977. "[R]ecklessly or negligently inflicted injuries do not fall within the compass of § 523(a)(6)." *Id.* at 64, 118 S.Ct. at 978. *See also In re Hawkins,* 231 B.R. 222, 228 (D.N.J.1999).

The Supreme Court did not specify the precise mental state necessary to rise to the level of "willful and malicious." *In re Conner,* 302 B.R. 509, 514 (Bankr.W.D.Pa. 2003) (citing to *In re Jercich,* 238 F.3d 1202, 1207 (9th Cir.), *cert. denied,* 533 U.S. 930, 121 S.Ct. 2552, 150 L.Ed.2d 718 (2001)). "As a result, appellate courts have taken both an objective and subjective approach to the inquiry." *In re Peterson,* 332 B.R. 678, 682 (Bankr.D.Del.2005) (citing *Conner,* 302 B.R. at 514). "Under the subjective approach, an injury is willful and malicious if the debtor caused harm through a deliberate action *with the belief that there was a* substantial certainty of injury. In contrast, under the objective approach, an injury is willful and malicious if the debtor caused harm through a deliberate action *with an objective* substantial certainty of injury." *Peterson,* 332 B.R. at 682–83 (emphasis in original) (citing *Conner,* 302 B.R. at 515 n. 4).

The Third Circuit has not revisited the issue since *Geiger.* In *In re Conte,* 33 F.3d 303 (3d Cir.1994), decided before *Geiger,* the Third Circuit arguably endorsed an objective approach. *In re Conner,* 302 B.R. at 515 n. 4. In *Conte,* the Third Circuit held "that actions are willful and malicious within the meaning of § 523(a)(6) if they either have a purpose of producing injury or have a substantial certainty of producing injury." *Conte,* 33 F.3d at 307. Quoting the *Restatement (Second) of Torts,* the Third Circuit found that the word " 'intent . . . denote[s] that the actor desires to cause consequences of his act, or that he believes that the consequences are substantially certain to result from it.' " *Id.* at 308 (emphasis in original) (quoting RESTATEMENT (SECOND) OF TORTS § 8A (1979)). Thus,

> Intent is not . . . limited to consequences which are desired. If the actor knows that the consequences are certain, or substantially certain, to result from his act, and still goes ahead, he is treated by the law as if he had in fact desired to produce the result. As the probability that the consequences will follow decreases, and becomes less than substantial certainty, the actor's conduct loses the character of intent and becomes mere recklessness.

Id. (quoting RESTATEMENT (SECOND) OF TORTS § 8A cmt. B (1979)). *See also In re Reynolds (Starr v. Reynolds),* 193 B.R. 195, 203 (D.N.J.1996); *In re Casini,* 307 B.R. 800, 820 (Bankr.D.N.J.2004) (the exception requires an actual intent to cause injury); *In re Groff,* 301 B.R. 644, 650 (Bankr.D.N.J.2003).

"[R]ecklessly or negligently inflicted injuries do not rise to the level of 'willful and malicious.' " *Peterson,* 332 B.R. at 682 (citing *Geiger,* 523 U.S. at 64, 118 S.Ct. at 978). As such, a knowing breach of contract will not ordinarily rise to the level of "willful and malicious." *Id.* at 62, 118 S.Ct. at 977. *See also In re Lazzara,* 287

B.R. 714, 722 (Bankr.N.D.Ill.2002) (stating that debts for intentional "breach of contract are not excepted from discharge").

In a case including an employee who breached a covenant not to compete and took proprietary information with him, Judge Scholl of the Eastern District of Pennsylvania held that the plaintiff employer demonstrated nondischargeability under 11 U.S.C. § 523(a)(4) on the ground of embezzlement, but not under section (a)(6). *In re Harland*, 235 B.R. 769, 775–82 (Bankr.E.D.Pa.1999). About section 523(a)(6), he stated:

> We believe that sustaining the Plaintiff's § 523(a)(6) cause of action on the basis of its claim for breaches of contract would result in precisely the result which the Court, in *Kawaauhau v. Geiger*, stated would attend an erroneous, broad interpretation of § 523(a)(6). Here, the Debtor clearly acted intentionally, and his actions clearly resulted in injury to the Plaintiff. However, by the very terms of State Court's findings, the Debtor's intent was focused entirely on maximizing his personal financial interests, not intentionally harming the Plaintiff. The injury which resulted flowed from the Debtor's breaches of his contract, but there is no finding that it actually was a goal of the scheme he pursued, as opposed to the goal of benefitting himself. We must therefore hold that the instant record is insufficient to support the Plaintiff's claims under § 523(a)(6).

Id. at 779.

A more expansive view of *Geiger* and section 523(a)(6) was taken in the *Butler* case from the Central District of Illinois, in which an ophthalmologist violated a covenant not to compete with the medical association with which he had been associated, violated a series of state court injunctions and was ruled in civil contempt. The court concluded that the record amply demonstrated the debtor's willfulness and maliciousness for purposes of section 523(a)(6) nondischargeability. *In re Butler*, 297 B.R. 741, 745–49 (Bankr.C.D.Ill. 2003). *See also In re Sarff*, 242 B.R. 620, 623–27 (6th Cir.BAP2000) (affirming bankruptcy court's determination that debtor's violation of covenant not to compete had been intentional, and his debt non-dischargeable). "The willfulness and malice required by 11 U.S.C. § 523(a)(6) is demonstrated by [the state court trial judge's] finding that Debtor repeatedly and purposefully engaged in acts which he knew to be in violation of the covenant not to compete and the trial court's preliminary injunction orders." *Butler*, 297 B.R. at 748. The *Butler* court noted that,

> Debtor may dispute that he subjectively intended to injure Plaintiff by intentionally violating the covenant not to compete, thereby breaching the Employment Contract. However, Debtor does not (and could not) seriously dispute the fact that he had subjective knowledge that injury to Plaintiff was substantially certain to result from his intentional acts. He clearly knew that violating the covenant not to compete would cause financial harm to Plaintiff, yet he knowingly violated the covenant anyway. As indicated above and as established by precedent, that is all that is required to meet the standard of nondischargeability set forth in *Geiger*.

Id. at 749 (citations omitted).

[10] Whether the *Harland* or the *Butler* approach is taken, there is no basis in this record to conclude that Reath inflicted a deliberate and intentional injury, with malice, upon the plaintiff or her Company in any way. His failure to promptly inform the plaintiff about the competing product lines being represented by the Company's sales reps was occasioned by his desire to afford the sales reps the

chance to take up the issue directly with the plaintiff. The competing product lines were not large accounts. The record does not reflect when the sales reps began to sell these lines, or whether the debtor had any involvement at the outset of their representation of the competing lines. The debtor's resignation did not violate the agreement between the parties. We do not know how it happened that the debtor and three of the sales reps all went to work for Huisman in January 2004. The lines acquired by Huisman in January 2004 had been lost by the Company in 2002 and March 2003. Huisman picked up one line formerly represented by the plaintiff, Spin Shades, in November 2003, but no evidence was offered that Reath had any involvement in that arrangement. These facts do not support the conclusion that the debtor either caused harm to the plaintiff through a deliberate action with the belief that there was a substantial certainty of injury, or that the debtor caused harm through a deliberate action with an objective substantial certainty of injury. *See Peterson,* 332 B.R. at 682–83.

I conclude that the plaintiff has failed to establish the requisite elements of either section 523(a)(2)(A) or 523(a)(6). Judgment in favor of the defendant shall be entered. The defendant's counsel shall submit a form of order.[23]

23. The defendant's motion for sanctions against the plaintiff for FED.R.BANKR.P. 9011 violations is denied. The complaint was not presented for an improper purpose, such as to harass or a cause delay. R. 9011(b)(1). The claims of the plaintiff seeking nondischargeability of the debt allegedly due to her from the debtor were warranted under existing law. R. 9011(b)(2). The plaintiff's factual contentions had evidentiary support, but were simply insufficient to establish the elements of non-dischargeability asserted by the plaintiff. R. 9011(b)(3).

In re GATEWAY ACCESS SOLUTIONS, INC., Debtor.

Gateway Access Solutions, Inc., Movant,

v.

Andrew C. Nester, Benjamin C. Steele, David F. Wiesner and Anchor Bay Corp., Respondents.

No. 5–07–50051RNO.

United States Bankruptcy Court, M.D. Pennsylvania.

May 17, 2007.

Background: Chapter 11 debtor moved to reject its executory contract granting third party an option to acquire debtor's leases from the Federal Communications Commission (FCC), and creditors whose claims were secured by any lease conversion payments that debtor might receive in future in event that third party exercised its option objected to proposed rejection and asserted right to adequate protection or, in alternative, to superpriority claim.

Holdings: The Bankruptcy Court, Robert N. Opel, II, J., held that:

(1) debtor's rejection of option that it had granted to third party to acquire debtor's FCC leases was not proposal to "use, sell or lease" the contingent interest granted to creditors in any lease conversion payments that this third party made, such as might trigger creditors' right to adequate protection;

(2) debtor's rejection of option was not Fifth Amendment "taking" of the con-