



**UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA**

In re

DANIEL SHERIDAN,

Debtor.

BYRON Z. MOLDO, CHAPTER 7
TRUSTEE,

Plaintiff,

vs.

STEPHEN MONTIETH ALBERS, et. al.,

Defendants.

CASE NO. SV 99-17689 KT

CHAPTER 7

ADV. NO. AP 02-01253 KT

**MEMORANDUM ON MOTION TO
DISMISS SECOND AMENDED
COMPLAINT**

On July 21, 2005, Byron Z. Moldo, Chapter 7 trustee of the bankruptcy estate of Daniel Sheridan and plaintiff in Adv. SV 02-01253 (the "Trustee"), filed a second amended complaint (the "2nd Amended Complaint") against defendants Stephen Montieth Albers ("Albers"), Klehr, Harrison, Harvey, Branzburg & Ellers ("Klehr"), Manier & Herod ("Manier"), and Novian & Novian ("Novian").

On October 31, 2005, Albers and Novian filed a motion to dismiss the 2nd Amended Complaint. The matter was set for hearing on March 24, 2006. At or near the time of the hearing on March 24, 2006, the matter was continued to an unspecified date pending the outcome

of a motion to compromise three other adversary proceedings in this bankruptcy case relating to the same set of facts and circumstances. On March 30, 2006, the court entered an order approving the compromise and qualified dismissal of the related adversary proceedings which expressly preserved the Trustee's rights on behalf of the bankruptcy estate.

It has come to the court's attention that the motion to dismiss the 2nd Amended Complaint was not reset for hearing by the court and no request to do so was made by any party thereto. It appears to the court that the matter has been fully briefed except for the impact, if any, of the approval of the compromise of the other adversary proceedings.

The 2nd Amended Complaint

The 2nd Amended Complaint alleges fifteen claims for relief. The 1st, 5th, and 9th claims are against Albers. The 4th, 8th, 12th, and 15th are against Novian. The remaining eight claims are against other parties.

The Motion to Dismiss

The defendants' motion seeks dismissal of the 1st, 4th, 5th, 8th, 9th, 12th, and 15th claims for relief on the grounds of lack of jurisdiction under Federal Rules of Civil Procedure ("FRCP") 12(b)(1) and failure to state a claim upon which relief can be granted under FRCP 12(b)(6).

Previous Settlement of the 4th, 8th, 12th, and 15th Claims for Relief – Against Novian

Albers and Novian allege that the Trustee previously settled his claims against Novian and that the Trustee should have deleted the compromised claims from the 2nd Amended Complaint. The Trustee agrees that the claims against Novian as well as those against Klehr and Manier have been resolved by compromise entered by this court on December 2, 2002. However, the Trustee asserts that it is not proper procedure to delete settled claims.

The court finds that deletion of the settled claims is not required notwithstanding the fact that said claims are no longer at issue. Therefore, the motion is denied in this regard.

Inasmuch as these claims are no longer at issue, it is not necessary for the court to address Novian's further argument that the Trustee lacks standing to prosecute an alleged violation of the discharge injunction.

Based on the foregoing, the court finds that all of the following claims for relief have been resolved: 2nd, 3rd, 4th, 6th, 7th, 8th, 10th, 11th, 12th, 13th, 14th, and 15th.

Remaining Claims – Against Albers

The only claims not resolved by the compromise approved in December 2002 are those against Albers stated in the 1st, 5th, and 9th causes of action for which the Trustee seeks the following relief:

1st – Declaratory Relief

The Trustee seeks judicial determinations of the following:

- (a) Albers had notice of this bankruptcy case in time to file a proof of claim;
- (b) the Debtor's prepetition debts to Albers were discharged upon the entry of the Debtor's discharge;
- (c) the Note, Pledge Agreement and Consent Documents and all acts taken by Albers in his purported capacity as president and/or director of Sheridan Music Group ("SMG") are void ab initio as a matter of law;
- (d) that the funds that were held in the Tennessee State Court Action are and were property of the Debtor's bankruptcy estate;
- (e) that the Debtor's shares of SMG and all rights pertaining thereto, are property of the bankruptcy estate; and
- (f) that the Debtor is and always has been the president and a member of the board of directors of SMG.

5th – Injunction

The Trustee seeks a temporary restraining order, a preliminary injunction, and a permanent injunction enjoining Albers, and his agents, servants, employees, and all persons acting under, in concert with, or for them from taking any actions on behalf of the SMG until further Order of this Court; and from appearing in any Court on behalf of the SMG.

9th – Violation of Discharge Injunction, Turnover, and Sanctions

The Trustee seeks judicial determinations that (a) Albers is in violation of the discharge injunction pursuant to 11 U.S.C. §524(a)(2) and that such acts taken by Albers amount to a willful violation; (b) the Note, Pledge Agreement, Consent Documents and all other acts taken by Albers in his purported capacity as president and/or director of SMG are void ab initio; (c) Albers must turnover the Debtor's shares in SMG; and (d) sanctions.

Partial Resolution of 1st Claim for Relief

On April 8, 2005, a Memorandum of Decision (the "MSJ Memorandum") was entered on the Trustee's renewed motion for summary adjudication on the Trustee's 9th claim for relief in the First Amended Complaint ("MSJ") in which this court made certain limited findings and conclusions:

(1) Albers had actual knowledge of the bankruptcy case in time to file a POC;

(2) All prepetition claims of Albers against Sheridan are subject to the discharge in Sheridan's bankruptcy case; and

(3) Actions taken by Albers in violation of the discharge in this case resulted in the exercise of control over property of the bankruptcy estate, i.e., Sheridan's interest in SMG. The Trustee has standing to preserve, protect and pursue assets of the bankruptcy estate. The Trustee has standing to challenge the wrongful and unenforceable exercise of dominion over property of the estate.

The first and second findings and conclusions set forth in the MSJ Memorandum resolve two of the determinations sought in the Trustee's 1st claim for relief in the 2nd Amended Complaint.

Technical Abandonment of SMG Stock

The prepetition asset which is at the heart of this controversy is the Debtor's stock in SMG. The Debtor's Schedules filed on June 24, 1999, disclose: "Debtor and his wife are the sole shareholders of The Sheridan Music Group, Inc. The company's liabilities exceed its assets, therefore it has no value."

The complicated, multi-suit, multi-venue controversy of which this adversary proceeding is a part is, at the most basic level, a dispute over the value of the Debtor's interest in the SMG stock and whether the Trustee can capture any of that value for the benefit of creditors at this time.

Underlying Allegations

In Paragraph 15 of the 2nd Amended Complaint, the Trustee alleges that, as of the petition date, the Debtor was the president and member of the Board of Directors of SMG and was acting as the authorized representative of SMG. In Paragraph 20, the Trustee alleges that the Debtor testified at the §341(a) meeting of creditors that SMG had no value. The Trustee further alleges that the Debtor's testimony was based on information provided to the Debtor by Albers, "who the Debtor stated was responsible for preparing and maintaining SMG's books and records." In Paragraph 21, the Trustee alleges that the Debtor failed to disclose the fact that SMG was entitled to royalties or the right to collect royalties. In Paragraph 22, the Trustee states that he filed a No Asset Report in the case "in light of the misrepresentation made by the Debtor upon the information provided by Albers." On December 29, 1999, the court entered the Debtor's discharge, and on January 6, 2000, the bankruptcy case was closed.

Thereafter, the Trustee learned of litigation in Tennessee over music royalties claimed by SMG. In September 2001, the Trustee moved to reopen the case to administer assets of the estate. The Debtor filed a non-opposition to the reopening and, on December 27, 2001, an order

was entered vacating the order closing the case and reopening the case “so that the Trustee can administer the newly discovered asset; and that the Trustee’s Report of No Asset filed on December 27, 1999, be withdrawn.”

The Contentions of the Parties

Albers asserts that the court has no jurisdiction to hear this dispute because the SMG stock was abandoned by operation of law when the case was closed and that this abandonment is not revoked merely by reopening the case. The Trustee counters that the reopening order set aside the abandonment. The Trustee further argues that the court has denied Albers’ argument on this issue on three previous occasions, i.e., when the court heard the Summary Judgment motion on the 9th cause of action and granted the Trustee’s motions to file the 1st and 2nd Amended Complaints.

Presently, there is no court ruling that states, specifically, that the technical abandonment accomplished by Section 554(c) was revoked or withdrawn in this case. However, revocation of abandonment is implied in the MSJ Memorandum in which the court stated:

“Actions taken by Albers in violation of the discharge in this case resulted in the exercise of control over property of the estate, i.e., Sheridan’s interest in SMG. The Trustee has standing to challenge the wrongful and unenforceable exercise of dominion over property of the estate.”

In light of the fact that the issue continues to arise, it is appropriate to address it now with specificity.

Discussion of Withdrawal of Technical Abandonment

Section 554(c) states: “Unless the court orders otherwise, any property scheduled under section 521(1) of this title not otherwise administered at the time of the closing of a case is abandoned to the debtor and administered for purposes of section 350 of this title.”

The general rule, as stated in Collier on Bankruptcy, ¶554.02[3], is: “Abandonment, once accomplished, cannot be revoked simply because it is subsequently discovered that the property had greater value than previously believed.” However, Collier goes on to acknowledge that some courts, including the Court of Appeals for the Tenth Circuit, have held that abandonment can be revoked for equitable reasons. 5 Collier on Bankruptcy ¶554.02[3] (Alan N. Resnick & Henry J. Sommers eds., 15th ed. rev). In In re Bruckner, 224 B.R. 760 (Bank. E.D. Mo. 1998), the bankruptcy court held that abandonment may be vacated when trustee’s decision to abandon was caused by debtor’s incomplete disclosure of assets. This discretion was recognized by the Ninth Circuit in Cusano v. Klein, 264 F.3d 936, 946 (9th Cir. 2001).

In Sheridan’s case, the case was reopened by order entered December 27, 2001, “so that the Trustee can administer the newly discovered asset.” The motion to reopen, filed on

September 21, 2001, described the grounds for reopening as follows:

“ In the past two weeks, the Trustee has learned of pending litigation and possible fraudulent transfers involving the rights to collect certain music royalties. The Debtor’s new counsel believes the Debtor may be entitled to the royalties, which were previously signed away to a relative. The Trustee has determined that it would be in the best interest of the estate to reopen the case and withdraw the Report of No Asset so that he might use the additional weight of the bankruptcy proceeding to further investigate this matter.”

Although not defined in the order, “the newly discovered asset” can only be the value of SMG’s stock, ownership of which was disclosed by the Debtor in his bankruptcy schedules. On at least one occasion in later pleadings, the Trustee states that he “reopened the case to administer royalties.”¹ However, it appears to be undisputed that the royalties in question were assigned to SMG, not the Debtor, and are not direct assets of the bankruptcy estate. In any case, the order reopening the case to deal with “the newly discovered asset” can only apply to assets of the bankruptcy estate and would make no sense if the abandonment, if any, of the asset was not also revoked or withdrawn.

While there may be a dispute about who is responsible for failure to disclose potential value in SMG stock represented by the assignment of music royalties, the bankruptcy judge then assigned to the Sheridan case must have considered the effect of Section 554(c) and exercised his discretion to revoke or withdraw the abandonment in this case. The order reopening the case “vacated” rather than withdrew the closing of the case and “withdrew” the trustee’s no-asset report.

Conclusion on Technical Abandonment

In light of the foregoing and the time this matter was pending and litigated before Judge Greenwald without challenge or clarification on this point, the court finds that the abandonment of the Debtor’s interest in SMG was revoked or withdrawn pursuant to the court’s order of December 21, 2001.

The Trustee’s Standing to Sue For Violation of Section 524

This court has clarified its view that the order reopening the case was sufficiently express to revoke the abandonment of the estate’s interest in the Debtor’s interest in SMG. (See above.) The court has also ruled, on summary adjudication, that actions by Albers taken in violation of the discharge injunction resulted in exercise of control over property of the estate and that the Trustee has standing not only to preserve, protect, and pursue assets of the bankruptcy estate but

¹ Reply In Support of Motion for Leave to Amend First Amended Complaint, page 3: “There is no merit to the claim that because the Trustee reopened the case to administer royalties, he cannot administer the Debtor’s interest in SMG.”

also to challenge the wrongful and unenforceable exercise of dominion over property of the estate.

However, as set forth in the MSJ Memorandum, the court did not make any findings on the scope of the Trustee's standing or his entitlement to recover monetary damages, whether compensatory or punitive.² The issue of standing is now squarely before the court.

Contentions of the Parties

Albers argues, as he did in his opposition to the MSJ and the Trustee's motions to amend the complaint, that the Trustee lacks standing to bring an action for violation of the discharge injunction because such a claim, if any, belongs solely to the Debtor and is not property of the bankruptcy estate. Albers points out that the Debtor brought suit against Albers on the same grounds in another adversary proceeding. Albers also asserts that neither the Trustee nor the Debtor can maintain a private right of action to enforce an alleged violation of the discharge injunction, citing Walls v. Wells Fargo Bank, N.A., 276 F.3d 502, at 506 (9th Cir. 2002); Cort v. Ash, 422 U.S. 66, 78 (1975); and Ramirez v. General Motors Acceptance Corporation (In re Ramirez), 273 B.R. 620, 623 (Bankr. C.D. Cal. 2002).

The Trustee responds that the 2nd Amended Complaint has dropped his previous requests for compensatory and punitive damages and, instead, the Trustee now seeks turnover of the Debtor's shares in SMG and sanctions for civil contempt in such amount as the court deems appropriate. (See 9th claim for relief.) The 2nd Amended Complaint repeats the Trustee's prior requests to enjoin Albers from taking any actions on behalf of SMG (5th claim for relief). The 2nd Amended Complaint also repeats his requests for the following: (1) that all acts taken by Albers on behalf of SMG are void ab initio; (2) that the funds that were held in the Tennessee state court action are and were property of the bankruptcy estate; (3) that the Debtor's shares of SMG and all rights pertaining thereto are property of the bankruptcy estate; and (4) that the Debtor is and always has been president and a member of the board of directors of SMG. The Trustee further asserts that sanctions for violating the discharge injunction are equivalent to those available for violation of the automatic stay of Section 362, including compensatory damages and attorneys' fees.

In summary, the 2nd Amended Complaint seeks (1) declaratory relief as to the estate's interest in the Debtor's shares in SMG, the consequences flowing from the estate's interest in the Debtor's shares in SMG including rights to benefit from the assets of SMG, and the estate's interest in the Debtor's authority to act as an officer and director of SMG; (2) turnover of the Debtor's shares in SMG; and (3) civil contempt sanctions for violation of the Debtor's discharge.

² The Ninth Circuit addressed whether punitive damages are recoverable for civil contempt of the automatic stay under Section 362 and concluded that they are not if they constitute anything more than "relatively mild" noncompensatory fines." In re Dyer, 322 F.3d, 1178, 1193 (9th Cir. 2003).

Standing under Section 524

Under Ninth Circuit law, no private right of action under Section 524 can be brought by the Debtor, the Trustee, or any other party in interest who may be aggrieved by violations of the discharge injunction. Walls v. Wells Fargo, at 510 (9th Cir. 2002). The only remedy for such violations is the civil contempt remedy provided by §105(a). In re Dyer, at 1191.

In the years before the court approved the settlement between the Debtor and Albers in March, 2006, the Debtor was pursuing claims against Albers for violating the discharge injunction which were administratively consolidated with the Trustee's claims in this adversary proceeding. If successful, the remedies available to the Debtor and the Trustee were intertwined. When the settlement was approved, the Trustee lost the benefit of the Debtor's position. Therefore, the issue of whether the Trustee has an independent right to seek sanctions for violation of the Debtor's discharge injunction must be decided.

Neither the Trustee nor Albers has brought to the court's attention any case in which a trustee pursued remedies for violation of the discharge injunction. Both Walls and Bennett involved the debtor as the enforcing party. Although the pursuing party in Dyer was the Chapter 7 trustee, the injunction at issue was the automatic stay under Section 362.

The court concludes that the Trustee does not have standing to seek civil contempt remedies for violation of the Debtor's discharge injunction.

The discharge injunction of Section 524 is for the benefit of the debtor, not third parties. The discharge protects the debtor against attempts to pursue prepetition, discharged claims as a personal liability of the debtor. Section 524(e) makes clear that the discharge does not affect the liability of any other entity or the property of any other entity for a debt that has been discharged. Nothing in Section 524 suggests that any third party potentially aggrieved by a violation of the discharge injunction can raise its protections at all, let alone when the debtor chooses not to do so. In the absence of clear direction otherwise from Congress or the appellate courts, this court does not see a direct remedy for the Trustee in this case under Section 524.

Notwithstanding the absence of a direct remedy under Section 524, acts in violation thereof may be relevant facts in considering other remedies including, if applicable, remedies for violation of the automatic stay and turnover of estate property.

Standing to Pursue Turnover and Related Remedies

The 9th cause of action seeks turnover of property of the estate. This remedy is not foreclosed by the court's conclusion that the Trustee has no independent remedy under Section 524. Whether property of the estate is limited to the Debtor's interest in SMG or includes the right to control SMG and its assets are issues that remain undecided.

CONCLUSION

Based on the foregoing, the Motion to Dismiss is granted in part and denied in part. The cause of action for violation of the discharge injunction is dismissed. Otherwise, the motion to dismiss the 1st, 5th, and 9th claims for relief are denied.

IT IS SO ORDERED.


Dated: NOV 9 2006

/s/
KATHLEEN THOMPSON
U.S. BANKRUPTCY JUDGE

CERTIFICATE OF MAILING

I hereby certify that copies of the **MEMORANDUM ON MOTION TO DISMISS
SECOND AMENDED COMPLAINT** were mailed to the following parties in interest:

DATED: **NOV 13 2006** JON D. CERETTO
CLERK OF COURT

By: 
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