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5 IN THE UNITED STATES BANKRUPTCY COURT
6 FOR THE DISTRICT OF ARIZONA
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8 In Re:

9 PAUL AND NANCY SCHREITER,

10 Debtors.

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13 UNITED STATES TRUSTEE,

14 Plaintiff,

15 vs.

16 PAUL SCHREITER,

17 Defendant.

Chapter 7

Case No. 05-27479

Adv. No. 06-00795

MEMORANDUM DECISION

(Opinion to Post)

18
19 **I. Introduction**

20 The Plaintiff United States Trustee ("U.S. Trustee") commenced an
21 adversary proceeding against Paul Schreiter, the Defendant and Debtor herein, on September 1,
22 2006, to determine whether the Debtor's discharge should be denied pursuant to 11 U.S.C. §
23 727(a)(3). The Defendant filed an Answer on October 2, 2006. The Court conducted various
24 pre-trial hearings in the adversary proceeding, and a trial was held on March 7, 2006. At the
25 conclusion of the trial, the U.S. Trustee requested an opportunity to submit post-trial briefing.
26 The Court granted the request, allowing the U.S. Trustee and the Defendant to file and serve
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1 post-trial memoranda, and thereafter this matter was under advisement.

2 This Decision shall constitute the Court's findings of fact and conclusions of law
3 pursuant to Fed. R. Civ. P. 52, incorporated as Bank. R. P. 7052. The Court has jurisdiction over
4 this matter, and this is a core proceeding. 28 U.S.C. §§ 1334, 157 (West 2007).

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6 **II. Factual Discussion**

7 The Defendant filed a joint petition for relief under Chapter 7 of the Bankruptcy
8 Code on October 14, 2005. His wife, Nancy Schreiter, is not a defendant in this matter. The
9 U.S. Trustee seeks to have the Defendant's discharge denied because of his failure to keep
10 adequate books and records from which the Defendant's "financial condition or business
11 transactions might be ascertained," unless the Defendant's failure to maintain such records "was
12 justified under all of the circumstances of the case."¹

13 The Defendant is well educated, having graduated from college and obtained his
14 doctorate in dentistry, and was licensed as a dentist in Arizona. He operated his own dental
15 practice in Flagstaff, Arizona from approximately 1990 until 1997. The Defendant maintained
16 books and records, as to his dental practice, for a number of years, having filed his tax returns for
17 the years preceding 2003.

18 The Defendant apparently encountered problems when he became a principal in
19 Dr. Paul Smile Design, L.L.C., which employed him in 2004 and 2005. The Defendant also
20 became associated with various other start-up operations at the same time. At the time of trial,
21 the Defendant testified that he undertook the practice of dentistry, but allowed the other principal
22 in Dr. Paul Smile Design, Lenn Friedman, to maintain the books and records of the Defendant's
23 various ventures. The Defendant, for instance, stated that when a new patient came to the Dr.
24 Paul Smile Design practice, he met with the patient to determine what services the patient
25 required. The Defendant then prepared a plan, which outlined the dental services that would

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27 **1.** 11 U.S.C. §727(a)(3).

1 time of trial to support this statement made under penalty of perjury.³ The Defendant presented
2 no records, or other evidence, at the time of trial to establish what he earned in 2003, 2004 or
3 2005.

4 The Defendant also has no personal financial records. As noted above, he has not
5 filed income tax returns for several years. He has no records to establish what payments were
6 made to creditors in the 90 days preceding the filing of his bankruptcy petition, and he does not
7 have or use a check register. The Defendant has no records to establish what is owed to his
8 secured creditors, although the Statement of Financial Affairs, at Question 3, requires that he
9 provide such information to the Court, creditors, and interested parties.

10 The Defendant also lacks records establishing what is owed to many of his
11 unsecured creditors, most of whom were patients of his practice. He does not have addresses for
12 some of these creditors, and, as noted above, has no knowledge regarding, or records
13 establishing, what patients of the dental practice paid or what they might still be owed for
14 services never rendered.⁴ As noted, some of these creditors who were patients of the
15 Defendant's practice paid in full for services never rendered.

16 The Defendant provided no information at the time of trial on any of these issues
17 although he had ample time to gather said information. For instance, he conceded at trial that he
18 could have contacted his financial institutions and obtained information as to when deposits were
19 made to his account reflecting his wages or other compensation. The Defendant could have
20 taken other steps to reconstruct his financial records, yet he took no action.

21 Although the Defendant attempted to place the blame for a failure to keep the
22 records of the various businesses or dental practices with which he was associated on the
23 principal of the practice or even on some of the employees of the practice with whom he worked,
24 the Defendant was not credible. The Defendant is a well educated individual who certainly had

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26 **3.** See Docket Entry. No. 12, page 16.

27 **4.** See Dkt. Entry No. 12, 42; U.S. Trustee's Exhibits 2, 3.

1 the ability to keep copies of the business and the personal records that were important to reflect
2 his financial situation. In fact, the Defendant admitted that he had filed tax returns for a number
3 of years up until 2002. He had no credible explanation as to why he could not retain the
4 appropriate documentation to file his tax returns for the 2003, 2004, and 2005 taxable years.

5 6 **III. Legal Discussion**

7 Under 11 U.S.C. § 727(a)(3),⁵ a court may refuse to grant a debtor’s discharge if
8 the debtor has no “books, documents, records, and papers,”⁶ from which the debtor’s financial
9 condition or business transactions might be ascertained.” “Complete disclosure is in every case
10 a condition precedent to the granting of the discharge,” and if such disclosure is not possible
11 without preserving books or records, a debtor cannot invoke the protection of the Bankruptcy
12 Court without justifying the failure to retain the necessary information. Meridian Bank v. Alten,
13 958 F.2d 1226, 1230-31 (3rd Cir. 1992). A party objecting to a debtor’s discharge must show
14 (1) that the debtor failed to maintain and preserve adequate records, and (2) that such failure
15 makes it impossible to ascertain the debtor’s financial condition and material business
16 transactions. In re Cox, 41 F.3d 1294, 1296 (9th Cir. 1994). Thereafter, the burden shifts to the
17 debtor to prove justification. Id. “Honesty is not enough; the law demands as the condition of a
18 discharge either that the bankrupt shall produce such records as are customarily kept by a person
19 doing the same kind of business, or that he shall satisfy the bankruptcy court with adequate
20 reasons why he was not in duty bound to keep them.” Meridian Bank, 958 F.2d at 1232 (quoting

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22 **5.** 11 U.S.C. § 727(a)(3) requires the court to grant the debtor a discharge, unless:

23 the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or
24 preserve any recorded information, including books, documents, records, and
25 papers from which the debtor’s financial condition or business transactions might
be ascertained, unless such act or failure to act was justified under all of the
circumstances of the case.

26 **6.** These items are referred to collectively herein by the terms “records” or “books and
27 records.”

1 White v. Schoenfeld, 117 F.2d 131, 132 (2nd Cir. 1941)).

2 In determining whether a debtor's failure to keep books and records was justified,
3 the Court must determine whether a reasonable person would have acted similarly, taking into
4 consideration education, experience, and sophistication; the volume or complexity of the
5 debtor's business; the amount of credit extended to the debtor or his business; and any other
6 circumstances that should be fairly considered. Meridian Bank, 958 F.2d at 1231. A
7 sophisticated business person is generally held to a high standard in record keeping. Id.

8 In the decision of In re Cox, the Ninth Circuit examined whether a debtor's
9 reliance on another to keep financial records was sufficient justification for the debtor's failure to
10 keep or preserve any of her own records. 904 F.2d 1399 (9th Cir. 1990). The debtor, Ms. Cox,
11 was a homemaker who relied on her husband to support her and to keep books or records. Ms.
12 Cox signed documents with her husband to become a co-owner of many parcels of real estate, a
13 partner in two or more partnerships, and a director or officer in several corporations, although
14 she had no daily involvement in the various enterprises. After Ms. Cox's husband absconded
15 with the funds from the real estate ventures, an involuntary bankruptcy was filed against her.
16 The trustee objected to Ms. Cox's discharge pursuant to 11 U.S.C. § 727(a)(3). The bankruptcy
17 court held that although Ms. Cox was partly a victim of her husband's actions, she had a duty to
18 keep records. The Bankruptcy Appellate Panel affirmed, and the Ninth Circuit affirmed, in part.
19 It held that although Ms. Cox was not actively involved in her husband's business, she shared his
20 duty to keep records. Id. at 1402. However, it speculated that where business partners were
21 married, and one had significantly more business expertise than the other, reliance of one on the
22 other to keep records might be justified. Id. at 1403. It remanded for the bankruptcy court to
23 consider whether Ms. Cox's reliance was justified, in light of: 1.) Ms. Cox's intelligence and
24 educational background; 2.) Her business experience; 3.) The extent of her involvement in the
25 business matters for which discharge was sought; 4.) Her knowledge as to whether her husband
26 was actually keeping records; 5.) The nature of the marital relationship; and 6.) Any record

1 keeping or inquiry duties imposed on Ms. Cox by state law. Id. at n. 5.

2 In this case, the U.S. Trustee carried her initial burden of showing that the
3 Defendant failed to keep adequate books and records; the Defendant never disputed his lack of
4 records. Although the Defendant had ample time to track down, copy, and reconstruct his
5 business and personal records, he chose not to take the appropriate action. By the time of trial,
6 the Defendant could not present sufficient written evidence to “enable his creditors reasonably to
7 ascertain his present financial condition and to follow his business transactions for a reasonable
8 period in the past.” See In re Horton, 621 F.2d 968, 971 (9th Cir. 1980). The Defendant was
9 able to produce a list of patients and cost estimates given for their dental work; however, he had
10 no documentation or knowledge regarding the amount each patient actually paid or might still be
11 owed for services never rendered.⁷ The Defendant’s failure to keep books and records has made
12 it impossible for his creditors to ascertain the Defendant’s financial condition, see id., and in
13 many instances, to have notice of his bankruptcy proceeding at all.⁸ Although this failure to
14 preserve any books or records would normally preclude the Defendant from receiving a
15 discharge, the Defendant alleges that he has a valid justification excuse.

16 The Defendant argues that he was justified in failing to keep books and records
17 for his dental practice because he relied on his business partner, Mr. Friedman, to do so. The
18 Defendant testified at trial that the business duties were delegated between the partners: the
19 Defendant was Dr. Paul Smile Design’s primary dentist, and Mr. Friedman took care of the
20 business aspects of the practice. When Mr. Friedman absconded with the funds of the dental
21 practice, the Defendant stated that he was left with no books or records, and was unable to access
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25 ^{7.} See Amended Schedule F, listing patient-creditors with amounts owing set forth as
“Treatment Plan estimate/Otherwise unknown;” U.S. Trustee’s Exhibit 3.

26 ^{8.} See Id., listing a number of patient-creditors with addresses “unknown;” U.S.
27 Trustee’s Exhibit 3.

1 any records inside the business premises.⁹ The Court did not find the Defendant's testimony
2 credible; but even if it had, the Defendant was not justified in relying solely on Mr. Friedman to
3 keep the books and records. See In re Cox, 904 F.2d 1402, 1403, n.5. Rather, given the
4 Defendant's substantial involvement in the dental practice as a principal, the Defendant shared
5 the duty to keep the books and records of the dental practice or practices. See Id. at 1402.

6 The Defendant's reliance on Mr. Friedman was also not justified because the
7 Defendant had extensive business experience. See In re Cox, 904 F.2d at 1402. He had owned
8 his own dental practice for many years, and had worked for several other dental practices prior to
9 working at Dr. Paul Smile Design. He conceded at trial that he knew he was required by law to
10 keep certain records, and file certain tax forms. The Defendant testified that he had kept records,
11 such as articles of incorporation, for other corporations he owned, some in conjunction with Mr.
12 Friedman, that are not at issue here. The Defendant was heavily involved in Dr. Paul Smile
13 Design on a day-to-day basis. Yet despite his business acumen; knowledge of the importance of
14 record keeping; high level of educational attainment; daily involvement in the business; shared
15 duty to keep records; and apparent ability to keep records, the Defendant testified that he did not
16 keep records for his dental practice and never checked to ensure that Mr. Friedman was doing so.
17 See In re Cox, 904 F.2d 1402. The Defendant testified that he did not know whether any
18 financial statements were ever prepared for the business; what the business's revenue was for
19 any operating quarter; what happened to the money paid to the practice by patients; or even what
20 his actual salary was. The Court does not find the Defendant's justification excuse to be
21 credible.

22 Furthermore, unlike the debtor in In re Cox, the Defendant was not married to his
23 business partner. See 904 F.2d at 1403. Thus, apart from the Defendant's assertions that he
24 relied on Mr. Friedman to keep his business records, the Defendant's failure to keep any

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26 **9.** At trial, the Defendant testified that he was later able to access restored data on a
27 portion of a hard drive, from which he derived the list of patients and Treatment Plan estimates
28 on his Amended Schedule F.

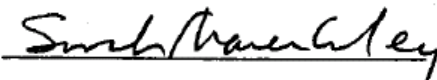
1 personal financial records remains utterly unexplained. Although the Defendant had previously
2 employed certified public accountants to assist with his personal finances, and regularly filed
3 income tax returns, he abruptly ceased to do so after 2002. The Defendant testified that he
4 received no documentation from Dr. Paul Smile Design regarding his earnings, was paid
5 irregularly by the practice, and was behind on personal bills, facing possible eviction and
6 foreclosure at times. The Defendant is a highly educated, articulate person. However, it seems
7 that the Defendant never questioned Mr. Friedman regarding the business's financial condition
8 or its failure to provide him with any personal payroll information. Even at trial, the Defendant
9 failed to present any recent bank or other records pertaining to his personal financial condition
10 from which his yearly income, at least, could have been deduced. The Defendant did not
11 undertake to keep even minimal records. See Meridian Bank, 958 F.2d at 1231 (requiring a
12 higher standard of record-keeping for sophisticated parties). The Defendant has not carried his
13 burden of proving justification for his lack of financial records.

14 15 **IV. Conclusion**

16 Although the Defendant argues that his failure to keep books and records was a
17 mistake, a Court does not examine intent in determining whether a debtor has preserved
18 adequate books and records of his financial affairs. Rather, the Court must determine whether
19 creditors could ascertain the debtor's financial condition and material business transactions from
20 the records the Defendant presents. In re Cox, 41 F.3d 1294, 1296 (9th Cir. 1994); Meridian
21 Bank v. Alten, 958 F.2d 1226, 1230-31 (3rd Cir. 1992). In this case, the Defendant has no books
22 or records, relating to his personal life or his business practice, from which creditors could
23 reasonably determine his financial situation or his material business transactions. As the
24 Defendant has presented no plausible justification for this failure to preserve such necessary
25 information, the Court concludes that the Defendant's discharge must be denied pursuant to 11
26 U.S.C. § 727(a)(3). The Court will execute a separate order incorporating this decision.

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DATED this 19th day of June, 2007.


Honorable Sarah Sharer Curley
U. S. Bankruptcy Judge

BNC to Notice