

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF ILLINOIS

IN RE:)	
)	
JEFFREY L. THORN and)	
DEIRDRE MAY THORN,)	No. 03-80817
Debtors.)	
<hr style="width:50%; margin-left:0;"/>		
)	
STELLA SOLIZ-HOLMES,)	
Plaintiff,)	
)	
vs.)	Adv. No. 03-8086
)	
JEFFREY L. THORN and)	
DEIRDRE MAY THORN,)	
Defendants.))	

OPINION

This matter is before the Court on the motion filed by the Debtors, Jeffrey L. Thorn and Deirdre May Thorn (individually referred to as JEFFREY or DEIRDRE and collectively referred to as the DEBTORS) for summary judgment on the issue of whether the Plaintiff, Stella Soliz-Holmes (STELLA), has standing to seek a determination of the dischargeability of a debt allegedly arising from JEFFREY'S misappropriation of the assets of a corporation of which she is a shareholder.

FACTUAL BACKGROUND

JEFFREY and Daniel Holmes, STELLA'S former husband, each owned fifty percent (50%) of an Illinois corporation known as Buy-Rite Auto Sales (BUY-RITE), a used-car sales business. Subsequent to December, 1999, BUY-RITE was operated exclusively by JEFFREY. Daniel Holmes filed bankruptcy in 2001. At some point during that same year, STELLA and Daniel were divorced and STELLA acquired the stock in BUY-RITE. STELLA sued

both BUY-RITE and JEFFREY in state court. She makes no allegation that a judgment was entered in that proceeding.

JEFFREY and DEIRDRE filed a joint Chapter 7 petition on February 18, 2003. In addition to listing STELLA'S pending lawsuit against BUY-RITE and JEFFREY in their Statement of Financial Affairs, the DEBTORS disclosed a forcible entry and detainer action against BUY-RITE brought by its landlord, which resulted in a surrender of the business property. The DEBTORS did not, however, disclose JEFFREY'S interest in BUY-RITE under Paragraph 18 of the Statement of Affairs. That provision directs the debtor to list specific information about each business in which he was an officer, director, partner, or managing executive within the six years preceding the petition date, including the beginning and ending dates of those businesses. The DEBTORS did list JEFFREY'S 5,000 shares in BUY-RITE on their schedule of personal property, attributing a value of "\$0.00" to the stock and included STELLA on their schedule of unsecured creditors as holding a disputed claim of no value. JEFFREY listed his current employment as a car salesman for Jeff's Car Corner.¹ The Chapter 7 Trustee abandoned his interest in the scheduled property and the DEBTORS were issued a discharge on May 27, 2003. No bankruptcy petition has been filed on behalf of BUY-RITE.²

STELLA brought this action against both DEBTORS under Section 523(a)(6) for willful and malicious injury, alleging that JEFFREY failed to account for and pay over

¹JEFFREY has no ownership interest in that entity. At the time the petition was filed, he had been employed for only one month.

²The DEBTORS asserted this fact in response to STELLA'S discovery request for information regarding BUY-RITE'S credit card accounts.

corporate net profits to either her or her former spouse; used corporate funds for personal and non-corporate expenses; failed to return to her a lift machine which she owns, having continued to use it for corporate business operations; and failed to repay either her or her former spouse for loans made to the corporation.³ STELLA alleges that these acts and omissions injured her “in her capacity as a shareholder.” In their answer, the DEBTORS denied the allegations of the Complaint. The DEBTORS filed a Motion for Summary Judgment, challenging STELLA’S standing to bring this Complaint, based on her failure to allege that she is a creditor of JEFFREY and her inability to quantify her claim.⁴ After a hearing, the Court took the matter under advisement, directing STELLA to file a response to the motion and giving the DEBTORS an opportunity to reply. Neither side filed any authority in support of their positions.

ANALYSIS

Section 523(a)(6) of the Bankruptcy Code provides:

(a) A discharge under Section 727 . . . 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(c)(1), which establishes a standing requirement, provides that “the creditor to whom such debt is owed” must seek a dischargeability determination

³Even though both JEFFREY and DEIRDRE are named as Defendants, the Complaint’s allegations refer only to the conduct of JEFFREY, not DEIRDRE. It thus appears to the Court that the Plaintiff is actually seeking relief only against JEFFREY.

⁴Because standing is a jurisdictional issue and not an affirmative defense, it is not waived by failure to raise it in the answer to the complaint. *Native American Arts, Inc. v. The Waldron Corp.*, 253 F. Supp. 2d 1041 (N.D.Ill. 2003).

for debts based on fraud and tort, including debts for willful and malicious injury under Section 523(a)(6). The Bankruptcy Code defines a “creditor” as an entity that has a claim against the debtor that arose at the time of or before the order for relief” 11 U.S.C. § 101(10)(A). A “claim” is defined as a “right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.” 11 U.S.C. § 101(5)(A). Whether a creditor holds a valid claim in bankruptcy is determined by applicable state law or federal nonbankruptcy law. *Butner v. U.S.*, 440 U.S. 48, 54-55, 99 S.Ct. 914, 59 L.Ed.2d 136 (1979); *Grogan v. Garner*, 498 U.S. 279, 111 S.Ct. 654, 112 L.Ed.2d 775 (1991).

When a shareholder of a corporation is bringing a claim against a corporate officer, the determination of the shareholder’s standing can be a tricky proposition. Some claims may be personal to the shareholder and may be asserted directly in the shareholder’s own name. Other claims that seek compensation for an injury to the corporation may only be brought derivatively on behalf of the corporation. It is important, at the outset, to draw the proper distinction between those two categories of claims.

Under Illinois law, it is well settled that an action for injury to a corporation must be brought in the corporate name. *Frank v. Hadesman and Frank, Inc.*, 83 F.3d 158 (7th Cir. 1996). A shareholder seeking relief for an injury to the corporation must bring his or her suit derivatively on behalf of the corporation. *Kamen v. Kemper Financial Services, Inc.*, 500 U.S. 90, 111 S.Ct. 1711, 114 L.Ed.2d 152 (1991). *Spillyards v. Abboud*, 278 Ill.App.3d 663, 662 N.E.2d 1358, 215 Ill.Dec. 218 (Ill.App. 1 Dist., 1996). The direct beneficiary of the action is the corporation that initially possessed the right to bring the suit. It is a vehicle to insure

corporate accountability. *March v. Miller-Jesser, Inc.*, 202 Ill.App.3d 148, 559 N.E.2d 844, 147 Ill.Dec. 504 (Ill.App. 1 Dist. 1990). This rule applies even in the context of closely-held corporations, where shareholders perceive that they have been personally wronged by corporate actions. *See, In re DeMert & Dougherty, Inc.*, 271 B.R. 821 (Bankr.N.D.Ill. 2001). A derivative claim may be limited, however, to wrongs committed after the complaining shareholder acquired his stock. 805 ILCS 5/7.80(a).

In order for a shareholder to sue individually, the shareholder must allege a special injury, either one that is unique to that shareholder alone or one that arises from a contractual right of a shareholder, such as the right to vote or to assert majority control. *Spillyards v. Abboud, supra*. The determination of whether the action being brought by the shareholder is derivative or direct requires a strict focus on the nature of the alleged injury. *Sterling Radio Stations, Inc. v. Weinstine*, 328 Ill.App.3d 58, 765 N.E.2d 56, 262 Ill.Dec. 230 (Ill.App. 1 Dist. 2002). Both a derivative and an individual claim may be asserted together in the same action. *Levy v. Markal Sales Corp.*, 268 Ill.App.3d 355, 643 N.E.2d 1206, 205 Ill.Dec. 599 (Ill.App. 1 Dist. 1994); *see, also, In re Beeber*, 239 B.R. 13 (Bankr.E.D.N.Y. 1999) (50% shareholder of corporation could bring Section 523 and 727 actions both individually and on behalf of the corporation against other shareholder).

The DEBTORS' Motion for Summary Judgment is premised upon STELLA'S failure to allege, in her Complaint, that she is a creditor of JEFFREY. The DEBTORS suggest that her only relationship to JEFFREY is as a shareholder of BUY-RITE and that BUY-RITE is not even a creditor of the DEBTORS. STELLA'S response is that as a shareholder of BUY-RITE,

she has a right to a portion of the amounts alleged to be owed by JEFFREY to BUY-RITE. Her claims alleging improper corporate expenditures and misapplication and waste of corporate assets are derivative in nature. *See, Kleban v. S.Y.S. Restarurant Management, Inc.*, 929 F.Supp. 294 (N.D.Ill. 1996). STELLA'S claims alleging a failure to account to her and to pay her one-half of the net profits, as well as the failure to return to her equipment owned by her, are personal claims. The alternative allegations in paragraphs 6.A and B of the Complaint, asserting a failure to account to and pay Daniel Holmes his share of the profits are claims that are personal to Daniel, not STELLA.

Several bankruptcy courts have recognized that in the context of a closely held corporation with only two shareholders, one shareholder's malfeasance may cause direct injury to the other shareholder, in which case that shareholder has standing to sue for damages from that injury. *In re Phillips*, 185 B.R. 121, 127 (Bankr.E.D.N.Y. 1995); *In re Beeber*, *supra*; *In re Pomainville*, 254 B.R. 699 (Bankr.S.D.Ohio 2000). The *Phillips* court reasoned as follows:

Where, as in this case, the matter concerns a closely held corporation in which all ownership is vested in the two parties to the lawsuit, there can be little doubt that any injury to the corporation caused by one fifty percent owner is in fact a direct injury to the other owner. Therefore, Plaintiff's injury is direct whether he sues directly as an individual or as a shareholder.

185 B.R. at 127. This Court agrees with that reasoning in the context of a two-shareholder corporation where each owns fifty percent (50%).

Accordingly, it is this Court's opinion that STELLA has standing to sue not only for harm she alleges to have suffered in her individual capacity, but also for harm to the corporation, to the extent that it caused her a financial loss in her capacity as a fifty percent

(50%) shareholder. The fact that she has standing to sue for what might otherwise be brought as a derivative action, however, does not moderate her burden of proof. This remains an action under Section 523(a)(6) in which STELLA must prove that the actions taken by JEFFREY were done with an intent to injure *her*. See, *Kawauhau v. Geiger*, 523 U.S. 57, 118 S.Ct. 974, 140 L.Ed.2d 90 (1998). It would be insufficient if she was only able to prove, for example, that JEFFREY intended to harm her former husband, Daniel Holmes, or creditors of the corporation.

STELLA must also clear a second significant hurdle if she is to prevail on the quasi-derivative claims. The purpose of derivative actions is to protect the corporation and its creditors. Damages for harm to a corporation may only be recovered for the benefit of the corporation in a derivative suit. Since shareholders stand behind creditors in the line for distribution of a defunct corporation's assets, damages realized from a successful derivative suit would only flow to shareholders if all creditors are first paid. It follows, in a case such as this where STELLA is bringing a nondischargeability claim for debts allegedly owed to her, individually, that she must prove not only that JEFFREY dissipated corporate assets, but that *she* would have received the value of those assets, most likely in the form of a dividend or upon dissolution of the corporation. If the corporation was insolvent, it is not easy to see how that burden could be met. If she is unable to directly link the harm to the corporation to a quantifiable financial loss that she, as a fifty percent (50%) shareholder, suffered, her quasi-derivative claims will fail.

At this stage, however, the focus is only on whether the Complaint states a claim for relief under Section 523(a)(6) that is properly brought by STELLA, individually, as a person

with standing to bring such a claim. For the reasons stated herein, except as to those claims that are personal to Daniel Holmes, the Court determines that she does have standing.

Finally, as this Court indicated to the DEBTORS at the hearing on their Motion for Summary Judgment, that the debt is disputed by the DEBTORS and remains unliquidated does not affect STELLA'S right to pursue a nondischargeability claim. *Beeber, supra*. Accordingly, DEBTORS' Motion for Summary Judgment will be denied. However, the phrase "or her predecessor, Daniel Holmes," will be stricken from paragraphs 6.A and B of the Complaint, since STELLA does not have standing to bring claims that are personal to Daniel Holmes.

This Opinion constitutes this Court's findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052. A separate Order will be entered.

Dated: September 14, 2004.

THOMAS L. PERKINS
UNITED STATES BANKRUPTCY JUDGE

Copies to:

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ORDER

For the reasons stated in an Opinion filed this day, IT IS HEREBY ORDERED that:

1. The Motion for Summary Judgment filed by the DEFENDANTS is GRANTED, in part, with respect to those claims which are personal to Daniel Holmes.
2. The phrase "or her predecessor, Daniel Holmes," is stricken from paragraphs 6.A and B of the Complaint.
3. In all other respects, the Motion for Summary Judgment is DENIED.
4. The Clerk is directed to schedule a Final Pretrial Conference.

Dated: September 14, 2004.

THOMAS L. PERKINS
UNITED STATES BANKRUPTCY JUDGE

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James L. Neppel
U.S. Trustee