In the United States Bankruptcy Court

for the Southern District of Iowa

GARY SEPELL
Debtor(s).

Bankruptcy No. 04-4939
Chapter 7

UNITED STATES OF AMERICA
Plaintiff(s)

vs.

GARY SEPELL
Defendant(s)

Adversary No. 05-30211-wle

ORDER RE: CROSS-MOTIONS FOR SUMMARY JUDGMENT

The matters before the court are the parties' cross-motions for summary judgment (docs. 27, 37). Hearing on the motions was held December 4, 2006 in Des Moines. Assistant United States Attorney Craig Peyton Gaumer appeared for plaintiff, the United States on behalf of the Social Security Administration (SSA). Attorney Jerrold Wanek appeared for defendant Gary Sepell. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I).

On or about January 23, 1985, Sepell filed an application with the SSA for Child's Insurance Benefits on the record of his father, Nick Sepell. On or about April 9, 1985, Sepell received an award notice from the SSA advising that he would begin receiving benefits. Sepell later became eligible for disability benefits and began receiving such benefits.

On or about April 30, 1996, the SSA sent a letter to Sepell advising him that he had received $23,297.10 in disability benefits to which he was not entitled because of his work activities and earnings. On or about April 19, 1999, the SSA sent another notice of overpayment to Sepell.

On or about February 28, 2001, Sepell was indicted by federal grand jury in the United States District Court for the Southern District of Iowa, Criminal No. 01-38. The indictment, in two counts, charged that Sepell fraudulently concealed information relevant to his right to receive Social Security benefits. He was accused of intentionally withholding information about earnings from employment.

Sepell was represented in the criminal proceedings by Nicholas Drees, Federal Public Defender. On or about March 10, 2003, Sepell entered into a plea agreement. Sepell agreed to plead guilty to Count 2 of the indictment which stated as follows:

> Between in or about March, 1987, and continuing through in or about January, 2001, in the Southern District of Iowa, the defendant GARY SEPELL, having knowledge of the occurrence of an event affecting his continued right to receive Supplemental Security Income Benefits, that is, his continued employment, knowingly concealed and failed to disclose the fact of his employment to the Social Security Administration, with the fraudulent intent to secure payment either in a greater amount than was due or when no payment was authorized. This is a violation of Title 42, United States Code, Section 1383a(a)(3)(A).

Appendix to Motion for Summary Judgment (doc. 27) ("Appdx."), Part A.

The plea agreement further stated that the "offense is punishable by a maximum term of not more than five (5) years, a maximum fine of $250,000, or both. A special assessment of $100.00, and a term of supervised release of not more than three year[s] also may be imposed by the sentencing court." Appdx., Part B, ¶ 4. Sepell agreed "to make full restitution to the Social Security Administration to the extent to which he is financially able, in an amount to be determined by the Court at sentencing." Id., ¶ 11.

At paragraph fourteen of the agreement, the parties agreed that the government was not precluded "from pursuing any civil or administrative matters" against Sepell. The plea agreement included the following stipulation of facts:

> I, Gary Sepell, state as follows:
>
> 1. In 1985, I began receiving Supplemental Security Income (SSI) Benefits from the Social Security Administration. I continued receiving them until approximately April of 2000.
>
> 2. During the time that I received SSI, I also worked for various trucking companies. For example, in 1998, I worked for Diamond F Transportation Co. I did not report the income I received from Diamond F to the Social Security Administration.
>
> 3. I had been told by Social Security that I had to tell Social Security if I worked and received wages. I did not tell Social Security about my return to work. I knew this was wrong and did it so I could continue to receive SSI benefits, even though I was not entitled to them.
>
> 4. This happened in the Southern District of Iowa.

Appdx., Part B, Attachment.

On March 13, 2003, after a sentencing hearing, criminal judgment entered. The court found that the amount of loss to the SSA was more than zero and less than $30,000. Sepell was sentenced to probation for a term of one year. The court waived a special assessment of $100. No fines or costs were imposed; no restitution was ordered.

On November 12, 2003, Sepell reapplied for Social Security benefits. In 2005, an Administrative Law Judge determined that Sepell was disabled effective September 10, 2003.

Gary Sepell filed a voluntary Chapter 7 bankruptcy petition on August 6, 2004. He did not list the Social Security Administration in his bankruptcy schedules. On September 22, 2004, Sepell amended his schedule of unsecured priority creditors to add:

> Social Security Administration
> 210 Walnut Street
> Des Moines, IA 50309
> BALANCE: $40,000.00

Appdx. at p. 77. Notice of this amendment was not sent by Sepell to the U.S. Attorney's office, nor was it sent to the SSA's Office of General Counsel in Kansas City. The SSA office in Des Moines has never been the servicing office for Sepell's Social Security benefit claims. The Des Moines office did not have working knowledge of his claim file. When the Des Moines office received notice of Sepell's bankruptcy filing, it forwarded the notice to the SSA processing center in Baltimore, Maryland, which was the custodian of Sepell's case file.

The notice of the filing of the case, sent in August 2004, set November 8, 2004 as the last day to file complaints under § 523(c) of the Bankruptcy Code. Sepell's discharge entered November 9, 2004. SSA issued a letter to Sepell, dated December 14, 2004, stating that "you do not have to pay us back the money paid in error. Based on this, your current overpayment balance is $0.00."

The Creston, Iowa Social Security Field Office is the servicing office for Sepell's Social Security claims. The Creston office learned of Sepell's bankruptcy case on or about December 20, 2004, when Sepell orally informed the office that

he had filed for bankruptcy.

On November 10, 2005, SSA filed the complaint in this proceeding, alleging that the debt arising from Sepell's intentional withholding of information concerning his earnings from employment is nondischargeable under 11 U.S.C. §§ 523(a)(2), 523(a)(6), and 523(a)(3). SSA alleged that the amount of the debt was approximately $24,717.64.

On August 30, 2006, SSA filed a motion for summary judgment that Sepell's debt is nondischargeable under all three of its claims in the complaint. In support of its motion, SSA filed copies of the criminal indictment against Sepell, his plea agreement, the Presentence Investigation Report, court minutes of the sentencing hearing, and the criminal judgment. SSA also filed affidavits of SSA agent Jon Guilford, the lead investigator in the criminal case against Sepell; Stacy Wood, an SSA employee in the Creston field office; Angela Bigley, an assistant manager in the Des Moines office; and Janice K. Reed, an SSA employee in the Kansas City office. Doc. 27 Appdx.; doc. 54. Wood's affidavit states that Sepell's debt as of the date of his bankruptcy filing is $27,724.81.

Sepell resisted the motion for summary judgment and filed a cross-motion for summary judgment. Sepell asks the court to dismiss the SSA's claims under §§ 523(a)(2) and (a)(6) as untimely. He also contends that SSA's complaint should be dismissed in its entirety because the action is barred by the six-year limitation period in 28 U.S.C. § 2415(a). Sepell also moved to strike the affidavit of Jon Guilford on the ground that the affidavit was not made on personal knowledge. The court did not rely on Guilford's affidavit for this decision, so the motion will be denied as moot.

Claims under §§ 523(a)(2) and (a)(6)

The exceptions to discharge described in Bankruptcy Code §§ 523(a)(2), (a)(4) and (a)(6) are not self-effectuating. A creditor must file a complaint with the bankruptcy court for determination of dischargeability of such debts. 11 U.S.C. § 523(c); Palmer v. Nordin (In re Nordin), 299 B.R. 915, 917 (B.A.P. 8th Cir. 2003). Rule 4007(c) of the Federal Rules of Bankruptcy Procedure provides that "a complaint to determine the dischargeability of a debt under § 523(c) shall be filed no later than 60 days after the first set for the meeting of creditors." In Sepell's bankruptcy case, the clerk set November 8, 2004 as the deadline for filing such complaints. Therefore, plaintiff's complaint, filed November 10, 2005, was untimely as to its claims under §§ 523(a)(2) and (a)(6).

SSA concedes that its complaint was not filed within the time provided. It argues, however, that the court should equitably toll the deadline because the government did not receive proper notice of the case. In his bankruptcy schedules, Sepell did not list the SSA office that had actively handled his Social Security case, nor did he list the SSA's Office of General Counsel. He did not give the U.S. Attorney's office notice that the SSA was a bankruptcy creditor. SSA argues that Sepell's failure to properly schedule its claim was misleading conduct warranting application of the docrine of equitable tolling, citing Zerilli-Edelglass v. New York City Transit Authority, 333 F.3d 74 (2d Cir. 2003), and In re Albini, 2004 WL 943908 (Bankr. D. Conn. 2004).

In Zerilli-Edelglass, an employment discrimination case, the Second Circuit observed that equitable tolling may be appropriate when the plaintiff is not aware of its cause of action due to "misleading conduct of the defendant." 333 F.3d at 80. In In re Albini, the court found that the debtor's conduct was "sufficiently troubling and misleading" to equitably toll the deadline for filing a dischargeability complaint. 2004 WL 943908 at *6. Hartford Insurance Company, as subrogee of Albini's employer, had filed a civil action against debtor pre-petition for her embezzlement from the insured employer. When debtor filed her Chapter 7 petition, although she listed Hartford in her schedule of unsecured creditors, she did not list Hartford's litigation attorney. The court suspected that the debtor's schedules were an effort to increase the chances that Hartford would miss the deadline for filing a dischargeability complaint. Id. at *5.

The Bankruptcy Appellate Panel for the Eighth Circuit has held that the deadline for filing a dischargeability complaint may be extended if there are equitable grounds for doing so. Landmark Community Bank, N.A. v. Perkins (In re Perkins), 271 B.R. 607, 612 (B.A.P. 8th Cir. 2002). However, "equitable tolling is only appropriate in rare and exceptional circumstances." Zerilli-Edelglass, 333 F.3d at 80. In In re Perkins, the bankruptcy clerk of court affirmatively misled the creditor as to the bar date for complaints and the creditor reasonably relied on information from the clerk. In this situation, equity required the court to extend the filing deadline. 271 B.R. at 614. Absent such an exceptional circumstance, the bankruptcy court lacks authority to extend the deadline once it has passed. Fed.R.Bankr.P. 4007(c), 9006(b)(3). If the reason for missing the deadline is failure to receive adequate notice, the creditor's remedy is a

claim under Bankruptcy Code § 523(a)(3). LeGrand v. Harbaugh (In re Harbaugh), 301 B.R. 317, 320 (B.A.P. 8th Cir. 2003); In re Nordin, 299 B.R. at 917. As the court discusses below, the SSA will be allowed to proceed with its claim under § 523(a)(3)(B). Therefore, the court will grant summary judgment on Sepell's motion to dismiss SSA's claims under §§ 523(a)(2) and (a)(6).

Claim under § 523(a)(3)

Bankruptcy Code § 523(a)(3)(B) provides that a Chapter 7 discharge does not discharge a debtor from any debt-

> neither listed nor scheduled . . . with the name, if known to the debtor, of the creditor to whom such debt is owed, in time to permit . . . if such debt is of a kind specified in paragraph (2), (4), or (6) of this subsection, . . . timely request for determination of dischargeability of such debt under one of such paragraphs, unless such creditor had notice or actual knowledge of the case in time for such timely . . . request.

11 U.S.C. § 523(a)(3)(B).

The court first addresses whether SSA's debt was "listed or scheduled" within the meaning of § 523(a)(3). The purpose of listing creditors in the bankruptcy schedules, and including them in the mailing matrix, is to provide creditors with notice. See Krakowiak v. Lyman (In re Lyman), 166 B.R. 333, 336-37 (Bankr. S.D. Ill. 1994) (creditors on schedule but not included on mailing matrix are not "listed or scheduled" under §523(a)(3)). Listing a creditor "requires the proper deliverable address where the creditor is destined to receive appropriate notice." Beverly Lumber Co. v. Nicholson (In re Nicholson), 170 B.R. 153, 155 (Bankr. W.D. Mo. 1994). The adequacy of notice to a federal agency requires review of special procedures applicable to the government. See United States v. Bridges, 894 F.2d 108, 111 (5th Cir. 1990) (meaningful notice to large, "cumbersome" government agencies is subject to special procedures).

Federal Bankruptcy Rule of Procedure 2002(j) governs bankruptcy notices to the United States and provides:

> Copies of notices required to be mailed to all creditors under this rule shall be mailed . . . (4) if the papers in the case disclose a debt to the United States other than for taxes, to the United States attorney for the district in which the case is pending and to the department, agency, or instrumentality of the United States through which the debtor became indebted.

Fed.R.Bankr.P. 2002(j)(4). Proper notice to the United States requires notice both to the U.S. attorney for the appropriate district and to the appropriate agency address. Miller v. Farmers Home Administration (In re Miller), 16 F.3d 240, 243 (8th Cir. 1994). Sepell does not dispute that the U.S. Attorney for the Southern District of Iowa was not included in his schedules or the creditor mailing matrix. The court finds and concludes that the SSA was not properly "listed or scheduled" within the meaning of § 523(a)(3).

The SSA may proceed with its dischargeability claim under § 523(a)(3)(B) unless it had "notice or actual knowledge of the case" in time to file a timely complaint. Sepell bears the burden of proving that SSA had such notice or actual knowledge. United States v. Bridges, 894 F.2d at 111; In re Harbaugh, 301 B.R. at 320-21.

Notice of Sepell's bankruptcy filing was not sent to the U.S. Attorney's office that was familiar with his criminal case, nor was it sent to the Creston SSA office that was familiar with his Social Security claims. The SSA office in Des Moines received notice of Sepell's bankruptcy filing on or about September 24, 2004. The Des Moines office has never been a servicing office for Sepell's Social Security claims. It had no working knowledge of his claim file or of legal issues presented by his bankruptcy filing. Affidavit of Angela Bigley, ¶¶ 4, 5. A United States agency should not be charged with notice or actual knowledge of a bankruptcy case "unless the agency particularly responsible for and familiar with the claims against the debtor has notice or actual knowledge of the debtor's bankruptcy case." United States v. Bridges, 894 F.2d at 113; see also Miller v. Farmers Home Administration, 16 F.3d at 243& n.3 (mailing to agency office "least likely to provide adequate notice" does not satisfy rules).

SSA's Creston office had actual knowledge of Sepell's bankruptcy case on or about December 20, 2004, well past the deadline for filing a timely dischargeability complaint. Therefore, SSA may proceed to trial on its claim under § 523(a)(3)(B).

Binding Effect of Presentence Investigation Report

In order to establish its claim under § 523(a)(3)(B), SSA must prove the underlying elements of §§ 523(a)(2) or (a)(6). Sepell contends that SSA has not established all the elements of its claim under § 523(a)(2), because the plea agreement and criminal judgment do not establish justifiable reliance on a false statement or the damages proximately caused thereby. SSA argues that these elements are established in part by facts set out in the Presentence Investigation Report, also called the Presentence Report, or "PSR." SSA contends that Sepell's failure to object to facts in the PSR in the criminal case has a preclusive effect in this adversary proceeding.

A prior criminal conviction can preclude relitigation of issues resolved in the criminal case, but the preclusive effect extends only to questions "distinctly put in issue and directly determined" in the criminal prosecution. Emich Motors Corp. v. General Motors Corp., 340 U.S. 558, 568-69, 71 S.Ct. 408, 414 (1951). Such preclusion may also be based on a criminal judgment after a plea of guilty, but the party relying on the preclusive effect of the criminal judgment has the burden of proving that the issues to be precluded were "distinctly put in issue and directly determined" by the guilty plea in the criminal case. Hyslop v. United States, 261 F.2d 786, 790 (8th Cir. 1958).

Four elements must be established in order to apply issue preclusion:

(1) the issue sought to be precluded must be the same as that involved in the prior action;
(2) the issue must have been litigated in the prior action;
(3) the issue must have been determined by a valid and final judgment; and
(4) the determination must have been essential to the prior judgment.

Stoebner v. Parry, Murray, Ward & Moxley, 91 F.3d 1091, 1094 (8th Cir. 1996) (citing In re Miera, 926 F.2d 741 (8th Cir. 1991)).

Criminal judgments have been used to preclude litigation of bankruptcy discharge and dischargeability issues. In Gargula v. Petersen (In re Petersen), 315 B.R. 728 (Bankr. C.D. Ill. 2004), the U.S. Trustee filed a complaint to deny debtor's discharge for false oath and concealment of assets. Plaintiff moved for summary judgment and submitted a transcript of the hearing in prior criminal proceedings in which debtor pleaded guilty to four counts of bankruptcy fraud. The bankruptcy court determined from the criminal hearing transcript that the judgment on the guilty plea established the elements of the claims to deny discharge. In U.S. Bank National Association v. Young (In re Young), 323 B.R. 484 (Bankr. W.D. Mo. 2005), several creditors filed dischargeability complaints under §§ 523(a)(2), (a)(4), and (a)(6) of the Bankruptcy Code. Plaintiffs moved for summary judgment by application of issue preclusion based on the outcome of a criminal case against the debtor. Debtor did not resist the merits of the motion. The court granted summary judgment based on matters in the plea agreement and judgment in the criminal proceedings.

SSA has not cited authority for using facts recited in a PSR as a basis for preclusion in a subsequent civil case. In a defendant's criminal case, a "fact in a PSR to which the defendant has not specifically objected is a fact admitted by the defendant." United States v. White, 447 F.3d 1029, 1032 (8th Cir. 2006). It appears that this proposition arises at least in part from Federal Rule of Criminal Procedure 32, and may not apply outside the context of criminal sentencing proceedings. See Fed.R.Crim.P. 32(i)(3)(A) (district court at sentencing "may accept any undisputed portion of the presentence report as a finding of fact"); United States v. Milam, 443 F.3d 382, 385-86 (4th Cir. 2006) (discussing Rule 32); United States v. McCully, 407 F.3d 931, 933 (8th Cir. 2005) (same).

Issue preclusion arises from a valid, final judgment. Not all facts recited in a PSR are necessarily essential to the criminal judgment. Applying issue preclusion on the basis of facts in a PSR would be particularly unfair if the defendant lacked the incentive to litigate such facts. See Raiford v. Abney (Matter of Raiford), 695 F.2d 521, 524 (11th Cir. 1983) (finding defendant had sufficient incentive to litigate).

In Sepell's criminal case, the court sentenced him to probation but imposed no fines and ordered no restitution. There were numerous facts in the PSR that were not essential to the decision. Moreover, there is a serious question whether Sepell had an incentive to litigate these facts. He agreed to pay restitution to the extent he was financially able. Being aware of his own financial situation, it may have made no difference to him whether SSA's claimed damages were one

amount rather than another. The court concludes that facts recited in the PSR are not binding in this proceeding.

Application of 28 U.S.C. § 2415

Sepell argues that SSA's complaint should be dismissed because its claim is barred by 28 U.S.C. § 2415(a). This statute provides in relevant part that--

> every action for money damages brought by the United States . . . which is founded upon any contract express or implied in law or fact shall be barred unless the complaint is filed within six years after the right of action accrues or within one year after final decisions have been rendered in applicable administrative proceedings . . . whichever is later.

28 U.S.C. § 2415(a); see also 28 U.S.C. § 2415(b) (three year period to bring action for damages founded upon a tort). Sepell argues alternatively that SSA has waived its claim. Doc. 51, Brief at 19.

The court concludes that Sepell's motion to dismiss SSA's complaint should be denied. Section 523(a) of the Bankruptcy Code specifies the types of "debt" that are nondischargeable. Section 101(12) defines debt as liability on a claim. The term "claim" is broadly defined to mean--

> (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; or
> (B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment, fixed, contingent, matured, unmatured, disputed, undisputed, secured, or unsecured.

11 U.S.C. § 101(5).

SSA's complaint is not an action for money damages but for a determination of dischargeability. Even assuming that 28 U.S.C. § 2415(a) would apply to an action to collect overpayments resulting from Social Security fraud, the running of the limitations period does not extinguish the government's claim. Thomas v. Bennett, 856 F.2d 1165, 1169 (8th Cir. 1988). Section 2415 expressly provides that the six-year period does not prevent the United States from asserting its claim as a counterclaim or from collecting its claim by means of administrative offset. 28 U.S.C. § 2415(f), (i). On the date of Sepell's bankruptcy filing, the United States had an enforceable claim against Sepell, and SSA may proceed with its complaint to determine whether Sepell's liability on the claim is excepted from his discharge.

Sepell argues that SSA has waived its claim by its failure to assert the claim at various times and particularly by issuance of the letter of December 14, 2004 stating that no overpayment was owed. Sepell's claim of waiver is without merit. The letter was issued by SSA's Baltimore office as an automated response to the order granting Sepell's bankruptcy discharge. It was not an intentional relinquishment of a known right. In re Estate of Warrington, 686 N.W.2d 198, 202 (Iowa 2004).

Issues Remaining for Trial

SSA argues that the same conduct which makes Sepell's debt excepted from his discharge under § 523(a)(2) as debt for fraud also establishes it as debt for willful and malicious injury under § 523(a)(6). Although SSA cites United States v. Foust (In re Foust), 52 F.3d 766 (8th Cir. 1995), for this position, the case does not support the argument. In Foust, it appears that debtor's conduct causing willful and malicious injury, conversion of grain, was distinct from his false representations about his farm operation.

The court does not need to decide if SSA's allegations, if proven, would satisfy the elements of both §§ 523(a)(2) and 523(a)(6). Deciding the point would not eliminate any issues for trial, because there are material facts in dispute under both theories of nondischargeability. In SSA's claim under § 523(a)(2), there are disputed facts relating to the separate instances of fraud, whether SSA justifiably relied on false representations by Sepell, and the amount of damages caused by fraud. See Merchants National Bank v. Moen (In re Moen), 238 B.R. 785, 790 (B.A.P. 8th Cir. 1999) (elements of § 523(a)(2)(A)). In the claim under § 523(a)(6), there are factual issues in regard to Sepell's alleged intent to cause harm.

See Kawaauhau v. Geiger, 523 U.S. 57, 118 S.Ct. 974 (1998) (definition of "willful and malicious" injury); Barclays American/Business Credit, Inc. v. Long (In re Long), 774 F.2d 875, 881 (1985) (same).

IT IS ORDERED that the motion to strike the affidavit of Jon Guilford is denied as moot.

IT IS FURTHER ORDERED that plaintiff's claims under 11 U.S.C. § 523(a)(2) and § 523(a)(6) are dismissed.

IT IS FURTHER ORDERED that the clerk shall set a scheduling conference to select a trial date.

DATED AND ENTERED _March 12, 2007_

William L. Edmonds
U.S. Bankruptcy Judge