

# Not Intended for Publication

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF INDIANA  
SOUTH BEND DIVISION

IN RE: CASE NO. 12-34152	)	
	)	
DANIEL THOMAS HENRY	)	
MARGARET JEAN HENRY	)	
	)	
Debtors	)	
	)	
	)	
CAROLYN VENDRAMIN	)	
	)	
	)	
Plaintiff	)	
	)	
vs.	)	PROC. NO. 13-3061
	)	
MARGARET JEAN HENRY	)	
DANIEL THOMAS HENRY	)	
	)	
Defendants	)	

**DECISION**

On April 30, 2015.

The plaintiff and the debtor, Daniel Henry, were shareholders in a closely held corporation – Henry-CAP Construction, Inc. Based on their respective initial investments in the company, Carolyn Vendramin had a one-third ownership interest and Mr. Henry had a two-thirds interest. While successful for a time, the business ultimately failed. During its operations, the plaintiff contends that Mr. Henry used the company’s credit card for personal expenditures, used corporate funds to pay his personal auto insurance coverage, misappropriated corporate opportunities, and engaged in a “freeze out” of the plaintiff from the corporation. After the Henrys filed bankruptcy, the plaintiff filed this adversary proceeding seeking a determination that the defendants’ obligations to her are non-dischargeable due to embezzlement and/or a willful and malicious injury. 11 U.S.C.

§ 523(a)(4), (6). The matter is before the court following trial of the issues raised.

Exceptions to discharge are narrowly construed in favor of the debtor. Ojeda v. Goldberg, 599 F.3d 712, 718 (7th Cir. 2010); Matter of Scarlata, 979 F.2d 521, 524 (7th Cir. 1992); In re Kimzey, 761 F.2d 421, 424 (7th Cir. 1985). The plaintiff bears the burden of proving that the debt should be excepted from discharge by a preponderance of the evidence. See, Grogan v. Garner, 498 U.S. 279, 111 S. Ct. 654 (1991). Yet, before the court considers whether one of the exceptions to discharge has been satisfied, it must first determine that there is a debt which the debtor owes the plaintiff. In the absence of a debt, there is nothing to be discharged. See e.g., In re Sammons, 508 B.R. 426, 430-431 (Bankr. D. Alaska 2014); In re Glenn, 502 B.R. 516, 529 (Bankr. N.D. Ill. 2013); In re Eisaman, 387 B.R. 219, 224 (Bankr. N.D. Ind. 2008); In re Roland, 294 B.R. 244, 249 (Bankr. S.D. N.Y. 2003) (collecting cases); In re Sieger, 200 B.R. 636, 639 (Bankr. N.D. Ind.1996); In re Wilder, 178 B.R. 174, 176-77 (Bankr. E.D. Mo.1995). Cf., Matter of Hallahan, 936 F.2d 1496, 1508 (7th Cir.1991) (“we think it preferable to allow bankruptcy courts ruling on the dischargeability of a debt to adjudicate the issues of liability and damages also.”). The answer to that threshold question is a matter of non-bankruptcy law. Grogan, 498 U.S. at 283-284, 111 S.Ct. at 657-58.

Much of what the plaintiff complains about are not harms to her, but injuries to the corporation of which she was a minority shareholder. The alleged embezzlement, payment of personal expenses and misappropriation of corporate opportunities did not involve her property, her funds or her opportunities, it all belonged to Henry-CAP Construction, Inc. The corporation is the owner of those claims and it must bring them. As a general proposition, shareholders may not bring an action in their own names to redress an injury to the corporation, even if the value of their interest in the corporation was impaired as a result of the alleged harm. Barth v. Barth, 659 N.E.2d 559, 560

(Ind. 1995). Instead, a derivative action is required. Id. at 562.

There is, however, an exception to the general rule; an exception the plaintiff claims to fulfill. The court has the discretion to allow the shareholder of a closely held corporation to bring an action in its own name if it finds that doing so will not: unfairly expose the corporation or the defendants to a multiplicity of actions; materially prejudice the interests of the corporation's creditors; or interfere with a fair distribution of the recovery among all interested persons. Barth, 659 N.E.2d at 562. In this case, the court cannot make these findings. To the contrary, allowing the plaintiff to prosecute this action in her own name will unfairly prejudice the interests of the corporation's creditors.

Henry-CAP Construction, Inc. failed. It was not formally dissolved, but simply withered and died as so many small corporations do. Yet, when it ceased doing business it owed thousands of dollars to its creditors – creditors who have yet to be paid. For the plaintiff to maintain the action in her own name would potentially allow her to gain the benefit of assets that rightly belong to the corporation and the corporation's creditors. Barth, itself, emphasized the importance of remembering the rights of corporate creditors.

[C]orporate liabilities must be extinguished before any corporate assets can be distributed to the stockholders. Petitioner may not be permitted to circumvent the rights of creditors by maintaining a direct action, the potential benefits of which would inure solely to himself. Barth, 659 N.E.2d at 562 (quoting Maki v Estate of Ziehm, 55 A.D.2d 454, 455-56 (N.Y. 1977)).

Subsequent decisions, in both federal and state courts, continue to recognize that a direct action by a shareholder is not appropriate where corporate creditors remain unpaid. See e.g., Miller v. Up in Smoke, Inc., 738 F. Supp 878, 881-84 (D. N.D. Ind. 2010); In re Arcella-Coffman, 352 B.R. 677, 691 (Bankr. N.D. Ind. 2006) (Klingeberger, B.J.); Hubbard v. Tomlinson, 747 N.E. 2d 69, 72 (Ind.

Ct. App. 2001).

Even if the plaintiff had satisfied Barth's requirements, her claim still fails. To begin with, she has failed to satisfactorily identify, much less prove, the necessary elements of the claims she is trying to prosecute, be it embezzlement, misuse of corporate property or the misappropriation of corporate opportunities; or to put a value on those claims. In other words she has failed to prove both liability and damages. Although she alleges that Mr. Henry used corporate credit cards for personal expenses, she has failed to prove which expenses were of a personal nature. Even at trial she admitted that some of the expenses complained of could have been related to the business. Neither has she satisfactorily proved that other corporate funds were improperly used to pay the debtor's personal expenses. Lastly, which corporate opportunities did he misappropriate and what were they worth? The court simply does not know.

Furthermore, beyond the lack of proof, the plaintiff and the corporation appear to have accepted or acquiesced in the practice of allowing some personal expenses to be paid with the company credit card. Any expenses that could not be attributed to the corporation were booked on the company's records as "due from shareholder" and the balance would fluctuate based upon various debits and credits. In other words, the company kept a running account of the balance due, based upon who had paid what to whom. Indeed, by the time the company ceased doing business, the running total of this account showed it owed the debtor almost two hundred thousand dollars, based upon loans he had made to the corporation in an unsuccessful attempt to keep the business going. Since the claim being prosecuted belongs to the corporation, the court must focus on the account's final balance to determine any amount that might be due and not, as plaintiff would wish, upon some intermediate balance chosen at a date which happens to favor the corporation.

The plaintiff also claims that Mr. Henry engaged in a “freeze out” of her interest as a minority shareholder in the corporation and that this constitutes a willful and malicious injury. Unlike the other claims she has asserted, this one belongs to her; but, like them, it too suffers from a lack of proof. To begin with, although she tries to characterize the defendant’s conduct as a “freeze out,” the plaintiff has never told the court what the elements of such an action might be or tried to demonstrate how the evidence presented at trial might satisfy them. See, In re King, 2006 WL 1994679 \*1 (Bankr. N.D. Ind. 2006) (“A proper legal brief has two components. First, it identifies the law or the rules governing a particular situation; it then advances an argument in which that law, when applied to the facts of the precise matter before the court, demonstrates that the movant is entitled to the relief it seeks.”). While Mr. Henry terminated the plaintiff’s employment as the corporation’s bookkeeper, she nonetheless remained a shareholder and a director. It seems, however, that, after that event, she lost interest in the corporation and chose not to make a meaningful effort to participate in its affairs, while Mr. Henry continued to operate the company in the same informal manner as before. Furthermore, if there was a “freeze out” of the plaintiff’s interest, her damages would be the “fair value” of her interest in the corporation. See, Plaintiff’s Post Trial Brief, filed March 3, 2015, pp. 4-6. But what is the value of a minority interest in a failing business? The court does not know because the plaintiff did not present evidence as to the value of her interest in the company.<sup>1</sup>

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<sup>1</sup>Plaintiff’s post trial brief states she was ready to present an appraisal valuing her shares at \$275,000 in the parties’ state court action, Plaintiff’s Post Trial Brief, filed March 3, 2015, p. 6, but nothing was ever presented to this court.

Plaintiff has failed to prove that defendants owe her any debt under non-bankruptcy law.<sup>2</sup> Absent such a debt, there is nothing to except from discharge. Sammons, 508 B.R. at 430-31; Eisaman, 387 B.R. at 224; Sieger, 200 B.R. at 639. A judgment of dismissal will be entered.

/s/ Robert E. Grant  
Chief Judge, United States Bankruptcy Court

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<sup>2</sup>The co-debtor, Margaret Henry, has also been named a defendant in this action, but the court does not understand why. While she was a named officer of the corporation, she did not actively participate in its affairs and there is no evidence that she misappropriated any corporate opportunities, misused its property or was involved in the alleged freeze out. She may (with Mr. Henry's permission) have used corporate credit cards for some personal expenditures, but the court does not know to what extent. Even if it did, the claim belongs to the corporation, not the plaintiff.