

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS**

IN RE:

In Proceedings

Under Chapter 7

DENNIS R. FEURER

ANNA M. FEURER

Case No. 01-34266

Debtor(s).

MASTER TECH AUTOMOTIVE, INC.

Plaintiff(s),

vs.

Adversary No. 02-3069

DENNIS R. FEURER

Defendant(s).

OPINION

In this case, the Court must address the issue of whether a debt arising from a violation of a covenant not to compete is non-dischargeable pursuant to 11 U.S.C. § 523(a)(6) as a “willful and malicious injury.”

The facts of this case are not in dispute. Debtor Dennis Feurer and his wife are the former owners and operators of D & D Automotive, an automotive repair business located at 1006 North Belt West, Swansea, Illinois. On May 17, 1999, the debtors entered into a series of agreements with the plaintiff, Master Tech Automotive, Inc. and its president, Thomas Faitz (“Plaintiff”) regarding the sale of D & D Automotive to Master Tech. As part of this sale, debtor Dennis Feurer executed an Agreement Not to Compete. Section One of that agreement provided, in pertinent part:

1. Restriction. For a period of two (2) years from the date hereof, in consideration

for the sum of Five Thousand (\$5,000.00) Dollars paid to Feurer by Corporation on this date, Feurer, individually and separately hereby warrants, represents, and covenants that he shall not, except on behalf of Corporation, within a fifteen (15) mile radius of Swansea, Illinois, (the "Territory") during the terms of this Agreement:

- (a) Directly or indirectly engage in the automotive repair business in competition with the business of Corporation as an agent, representative, partner, stockholder, or otherwise, of any company, partnership, sole proprietorship, or other entity; or
- (b) directly or indirectly request or advise any clients or customers of Corporation to withdraw, curtail or cancel their business with Corporation; or
- (c) directly or indirectly disclose to any other person, firm, or corporation the names of past, present, or future (if known) clients and customers of Corporation; and
- (d) directly or indirectly induce, or attempt to influence, any employee to terminate his business relationship with Corporation.

Plaintiff's Exhibit 2, Agreement Not to Compete Between Dennis Feurer and Master Tech Automotive, Inc., Para. I(a)-(d), May 27, 1999.

With the proceeds from the sale of his automotive business, the debtor purchased and attempted to operate an amusement park. However, this business was unsuccessful and was permanently closed in the fall of 2000. After the closing of the amusement park, the debtor began operating an automotive repair business called A & D Automotive at 609 South Belt West, Belleville, Illinois, in admitted violation of the covenant not to compete.

Upon learning that the debtor had opened a competing automotive repair business, the plaintiff filed a complaint in the Circuit Court of the Twentieth Judicial Circuit, St. Clair County, Illinois seeking, inter alia preliminary and permanent injunctions enjoining the debtor from violating the terms of the non-compete

agreement.¹ On January 19, 2001, the Circuit Court entered its Memorandum and Temporary Restraining Order granting the plaintiff injunctive relief. This was followed on March 12, 2001 with the court's Memorandum and Permanent Injunction, enjoining the debtor from violating the non-compete agreement and scheduling the matter for hearing on the issue of damages. However, prior to the hearing on damages, the debtors filed their Chapter 7 petition. The plaintiff then filed the instant complaint to determine the dischargeability of its debt, alleging that any damages recovered as a result of the debtor's violation of the non-compete agreement would be non-dischargeable pursuant to 11 U.S.C. § 523(a)(6) as a "willful and malicious injury"

DISCUSSION

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

- (a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title 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). In order for a debt to be determined nondischargeable under this section, a creditor must prove three elements by a preponderance of the evidence: (1) that the debtor intended to

¹

Paragraph 2 of the Agreement provided for the remedy in the event of breach of the covenant not to compete. It states:

- 2. Remedies. The parties hereto acknowledge that a breach of the restrictive covenant or any one of them by Feurer will result in substantial injury and damage to the Corporation for which there is no adequate remedy at law. Therefore, in the event of a breach of the restrictive covenants or any one of them by Feurer, Corporation shall be entitled, in addition to all other remedies, including its right of set-off and recoupment for damages, losses and injuries as provided herein as if fully set forth, to a preliminary restraining order and an injunction to prohibit and restrain the violation of this Agreement by Feurer or by any other person or entity acting for Feurer as agent, representative, or otherwise.

and caused an injury; (2) that the debtor's actions were willful; and (3) that the debtor's actions were malicious. In re Dobek, 278 B.R. 496, 511 (Bankr. N.D. Ill. 2002). Failure by the creditor to establish either willfulness or maliciousness will render the debt dischargeable. In re Longley, 235 B.R. 651, 655 (10th Cir. B.A.P. 1999). The question of whether a debtor acted willfully and maliciously is ultimately a question of fact reserved for the trier of fact. In re Thirtyacre, 36 F.3d 697, 700 (7th Cir. 1994); In re Ardisson, 272 B.R. 346 (Bankr. N.D. Ill. 2001).

Prior to 1998, there was a split of authority among the Circuit Courts of Appeals regarding the meaning of the terms "willful" and "malicious" within the context of § 523(a)(6). Much of that disagreement centered on whether § 523(a)(6) encompassed acts done intentionally that caused injury or, only acts done with the actual intent to cause injury. See, e.g., St. Paul Fire and Marine Ins. Co. v. Vaughn, 779 F.2d 1003 (4th Cir. 1985); Chrysler Credit Corporation v. Perry Chrysler Plymouth, 783 F.2d 480 (5th Cir. 1986); In re Compos, 768 F.2d 1155 (10th Cir. 1985). This issue was clarified by the United States Supreme Court in 1998, when it rendered its opinion in Kawaauhau v. Geiger, 523 U.S. 57 (1998). In Geiger, the plaintiff sought to hold nondischargeable damages for injuries sustained as a result of the defendant doctor's negligent conduct. In affirming the Eighth Circuit Court of Appeals, the Supreme Court concluded that

"the word 'willful' in subsection (a)(6) modifies the word 'injury,' indicating that nondischargeability takes a deliberate or intentional *injury*, not merely a deliberate or intentional act that leads to injury.

Geiger at 61 (emphasis in the original).

In adopting a more limited reading of subsection (a)(6), the Court explained that to hold otherwise could place within the exception a number of situations not contemplated by Congress. As the Court explained:

[A] more encompassing interpretation could place within the excepted category a wide range of situations in which an act is intentional, but injury is unintended, i.e. neither desired in fact nor anticipated by the debtor. Every traffic accident stemming from an initial intentional act -for example, intentionally rotating the wheel of an automobile to make a left hand turn without first checking oncoming traffic-could fit the description. A 'knowing breach of contract' could also qualify. A construction so broad would be incompatible with the 'well known' guide that exceptions to discharge 'should be confined to those plainly expressed.

Geiger at 62 (citations omitted and emphasis added).²

In its opinion, the Court noted that § 523(a)(6) generally triggers in lawyers' minds those actions which are traditionally characterized as "intentional torts." Id. at 61. This is not to say, however, that actions for breach of contract may never fall within the purview of this section. Contract actions, including actions for breach of non-compete agreements, have been the source of much § 523(a)(6) litigation. However, no *per se* rule has emerged from this litigation for determining whether a violation of a covenant not to compete constitutes a willful and malicious injury for nondischargeability purposes. As the court noted in In re Trammell, 172 B.R. 41, 47 (Bankr. W.D. Ark. 1994), "there are no absolutes in the determination of willfulness and malice. 'In each case, evidence of the debtor's motives, including any claimed justification

²As the court explained in Dorr & Associates v. Pasek, 129 B.R. 247 (Bankr. D. Wyo. 1991):

It is almost always foreseeable in the abstract that a breach of contract will result in some form of economic harm to the other party of the contract. A breach of contract frequently results from an intentional act by the party which chooses not to complete its obligations under the contract for whatever reason.

The focus, for non dischargeability purposes, is not on the wrongfulness of the intentional breach. Instead, the focus for § 523(a)(6) is on the debtor's intent when he took the action.

Id. at 252.

or excuse, must be examined to determine whether the requisite [elements are] present." Id. (quoting Dorr, Bentley & Pecha, C.M.'s, P.C. v. Pasak (In re Pasek), 983 F.2d 1524, 1527 (10th Cir. 1993)).

It is undisputed that the debtor in this case willfully violated the parties' non-compete agreement. See Transcript p. 19-20. However, an intentional or willful act, standing alone, is insufficient to support an action under § 523(a)(6). Instead, the Court must focus on the issue of whether, by his actions, the debtor intended to cause injury to the plaintiff. Based on the testimony and other evidence presented, the Court finds that the debtor did not act with the requisite intent to injure the plaintiff in this case.

The debtor testified that after he sold D & D Automotive to the plaintiff, he purchased an amusement park called Formula One Fun Park. However, that venture was unsuccessful and the debtor lost approximately \$40,000 during its first year of operation. The losses were even greater after the business's second year, leaving the debtor with tremendous debt.³ Not only had the debtor incurred a \$235,000 loan for the purchase of the park, at the time that the business ceased operation, he owed \$74,000 for go-cart leases, \$2,000 to \$3,000 in electric bills, and over \$30,000 in credit card obligations. See Transcript at p. 32-33. In fact, the debtor testified that by the fall of 2000, his monthly bills and expenses exceeded \$11,000. Id. at p. 37.

In an attempt to generate enough income to save the amusement park from foreclosure, the debtor decided to open another auto repair business. He testified that he knew that opening a competing business would violate his agreement with the plaintiff. However, the debtor believed that given his age and occupational skills, there was no other way for him to make enough money to meet his financial

³According to the debtor's testimony, he began the second year of operating with \$135,000. By the end of that year, he "had absolutely nothing." See Transcript p. 32.

obligations.⁴ In October 2000, the debtor and his daughter began operating A & D Automotive in Belleville, Illinois. To advertise this new venture, the debtor mailed flyers to approximately 30-40 persons who had been customers of D&D Automotive. He selected only those persons who he had considered to be friends and did not send a flyer to all of his prior customers. Debtor testified that he had obtained these individuals' names and addresses from old service tickets that he had retained for tax purposes. He further testified that at the time that he mailed out the advertisements, he did not know whether any of these people were customers of the plaintiff. See Transcript at p. 35.

The debtor ceased operation of A&D Automotive in January 2001 after the plaintiff instituted the state court injunction litigation. Between January and May 2001, the debtor complied with the terms of the state court's Temporary Restraining Order and its Order of Permanent Injunction and did not engage in any type of business in competition with the plaintiff. After the expiration of the covenant not to compete on May 26, 2001, the debtor opened his current business, North Belt Automotive.

Based on these facts, this Court finds that the debtor's intent in operating a competing auto repair business was not to harm the plaintiff, but, rather, to try to advert financial failure. As the court explained in KV Pharmaceutical Company v. Harland (In re Harland), 235 B.R. 769 (Bankr. E.D. Pa. 1999)⁵,

⁴Debtor testified that he is 55 years of age and that he has been an auto mechanic since he was 18. He further testified that he attempted to secure employment as a mechanic in other garages prior to opening his own business, but that no one was able to offer him wages sufficient to meet his financial needs. See Transcript at p. 31-2, 37.

⁵In Harland, the debtor had been employed as a chemical engineer by the plaintiff, a drug manufacturer. In his capacity as a manager in the research and development department, the debtor had access to sensitive and lucrative information regarding plaintiff's projects. Because of this, the plaintiff's standard employment contract, which debtor signed, included a confidentiality clause, as well as a non-compete agreement. Upon leaving the plaintiff's employ, not only did the debtor secure employment with one of the plaintiff's primary competitors, he also provided his new employer with over twenty-six (26) lab books containing the plaintiff's trade secrets. The plaintiff brought suit in the state court against

[S]ustaining the plaintiff's § 523(a)(6) cause of action on the basis of its claim for breach of contract would result in precisely the result which the Court, in *Kawaauhau v. Geiger*, stated would attend an erroneous, broad interpretation of § 523(a)(6). Here, the debtor clearly acted intentionally, and his actions clearly resulted in injury to the plaintiff. However, . . . the debtor's intent was focused entirely on maximizing his personal financial interests, not intentionally harming the plaintiff. The injury which resulted flowed from the debtor's breaches of his contract, but there is no finding that it actually was a goal or scheme he pursued, as opposed to the goal of benefitting himself. We must therefore hold that the instant record is insufficient to support the plaintiff's claims under § 523(a)(6).

Id. at 779.

In reaching its conclusion, the Harland court distinguished earlier pre-Geiger cases including In re Hallahan, 936 F.2d 1496 (7th Cir. 1991), which has been cited by the plaintiff in this case. In Hallahan, the Seventh Circuit Court of Appeals affirmed the lower courts' conclusion that a debtor's liability for breach of a covenant not to compete was nondischargeable pursuant to § 523(a)(6). However, the plaintiff's reliance on Hallahan in this case is misplaced for two reasons. First, the Hallahan court did not engage in its own discussion of the requisite standard of willfulness under § 523(a)(6). Rather, the primary focus of its discussion was on the issues of whether the covenant in question was enforceable under Missouri law and on whether the plaintiff was entitled to a jury trial under the Seventh Amendment.⁶ Second, the Appellate

the debtor for breach of contract and fraud. In those proceedings, the state court found that not only did the debtor fail to comply with the terms of his employment contract with the plaintiff, but that he had actually entered into that contract knowing that he had no intention of abiding by it. Specifically, the court found that plaintiff almost immediately began seeking to secure new employment with a company where he could utilize information obtained from the plaintiff. Despite these egregious actions, the bankruptcy court found that the debtor had not acted with the requisite intent to support plaintiff's § 523(a)(6) complaint.

See 235 B.R. at 779.

⁶The only discussion regarding nondischargeability of the debt in Hallahan was as follows:

Because Hallahan concedes that he breached the contract willfully, the bankruptcy

Court did not have the benefit of the Geiger ruling when it rendered its opinion in Hallahan. Since the introduction of Geiger in 1998, the standard for determining nondischargeability under § 523(a)(6) has narrowed, placing the focus not on whether the debtor committed an intentional act, but, rather on whether the debtor intentionally set out to injure the plaintiff by his actions. For the reasons stated in this opinion, the Court finds that the debtor in this case did not act with the necessary intent to render his obligation to the plaintiff nondischargeable under 11 U.S.C. § 523(a)(6). Accordingly, the Complaint to Determine Dischargeability of Debt is DISMISSED.

SEE WRITTEN ORDER.

ENTERED: November 6, 2002

/s/ William V. Altenberger
UNITED STATES BANKRUPTCY JUDGE

court's finding that Hallahan's debt to the plaintiffs in non-dischargeable under Section 523(a)(6) will not be disturbed.

Hallahan, 936 F.2d at 1501.