UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW JERSEY

	:	CHAPTER 11
In re:	:	CASE NO.: 96-37009 (WHG)
	:	
ERIC KELLER,	:	
	:	Hearing Date: May 4, 1998; 2:00 p.m.
Debtor.	:	
	:	

ANSWER OF DEFENDANT/RESPONDENT RONALD KELLER TO PROPOSED FINDINGS OF FACTS SUBMITTED BY THE OFFICE OF THE UNITED STATES TRUSTEE, COUNTER-PROPOSED CONCLUSIONS OF LAW, OPPOSITION TO MOTIONS FOR CONTEMPT AND SANCTIONS FILED BY WILSHIRE CREDIT CORPORATION AND FORUM INSURANCE COMPANY, PLEA OF NOT GUILTY TO CRIMINAL CONTEMPT, DEMAND FOR JURY TRIAL, AND DEMAND FOR DISCOVERY

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Respondent/Defendant Ronald Keller ("Defendant"), by and through his attorneys, LoFaro & Reiser, L.L.P., and Flood & Basille, by way of response to the Proposed Findings of Fact and Conclusions of Law submitted by the Office of the United States Trustee ("Trustee") in support of its motion to declare Defendant in civil and criminal contempt, and by way of further response to the corresponding motions of Wilshire Credit Corporation and Forum Insurance Company for the same relief, hereby states as follows:

DEFENDANT'S ANSWER TO PROPOSED FINDINGS OF FACT

In view of the pending charges of criminal contempt, Defendant hereby denies each allegation that pertains to him in each proposed finding of fact raised in the motions for civil and criminal contempt filed by the Trustee, Wilshire Credit Corporation and Forum Insurance Company.

DEFENDANT'S PROPOSED CONCLUSIONS OF LAW

A. Contempt in General

1. The Bankruptcy Court cannot conduct both civil and criminal contempt proceedings in one hearing. *Fed. R. Bankr. P. 9020(b). See In re Alan Baker, 195 B.R. 309, 315 (Bankr. D.NJ. 1996)* (Notice under Bankruptcy Rule 9020 "must state the facts constituting the contemptuous behavior and describe the contempt as **either** criminal or civil"). (emphasis added); *In re Eskay, 122 F.2d 819, 823 (3rd Cir. 1941)*(The Court stated that one of the objects in determining the nature of contempt proceedings is "to inform the accused at the outset with which form of contempt he is charged"). *See also*

Matter of Hipp, 895 F.2d 1503 (5th Cir. 1990), citing *Gomez v. United States*, 109 S.Ct. 2237, 104 L.Ed.2d 923 (1989)("…federal statutes, where they may reasonably be so construed, without violence to their clear meaning, should be given an interpretation that avoids serious questions as to their constitutional validity.").

2. Until a complainant has met the requirements of *Bankruptcy Rule 9020(b)*, the bankruptcy court does not have the power to enter a contempt order. *Alan Baker*, 195 B.R. at 315.

3. Contempt proceedings must be guided by fair procedures affording every person a reasonable opportunity to defend himself. *In re Weeks*, 570 F.2d 244 (8th Cir. 1978). In that regard, the bankruptcy judge must give notice in writing of his intent to hold a hearing on contempt. *In re Finney*, 167 B.R. 820, 823 (E.D.Va. 1994).

4. The correct understanding of the nature of the contempt proceeding is vital, since a person facing criminal contempt is exposed to significant penalties and is entitled to procedural rights not available in civil contempt proceedings. *Universal City Studios, Inc. v. N.Y. Broadway International Corp.*, 705 F.2d 94 (2nd Cir. 1983). Thus, the Court must determine whether a contempt proceeding and the relief sought should be characterized as civil or criminal in nature so as to determine proper applicability of due process protections. *Hicks v. Feiock*, 485 U.S. 624, 105 S.Ct. 1423, 99 L.Ed. 2d 721 (1988).

5. Although the same conduct may result in both civil and criminal contempt charges, *United States v. United Mine Workers of America*, 330 U.S. 258, 67 S.Ct. 677, 91 L.Ed. 884 (1946), however if both civil and criminal relief are imposed in the same

proceeding, then the criminal feature of the order is dominant and fixes its character for purposes of appellate review. *Hicks v. Feiock, supra*.

6. If the judge hearing the matter is not sure whether a particular proceeding is civil or criminal in nature, the judge should follow the procedure set forth in *Fed. R. Civ. P. 42* in order to assure that the defendant suffers no prejudice. *See United States v. Powers*, 629 F.2d 619 (9th Cir. 1980).

7. Where there is ground to doubt the wrongfulness of the defendant's conduct, he should not be adjudged in contempt. *Fox v. Capital Co.*, 96 F.2d 684, 685 (3rd Cir. 1938), citing *California Artificial Stone Paving Co. v. Molitor*, 113 U.S. 609, 5 S.Ct. 618, 28 L.Ed. 1106 (1885).

8. Where a defendant properly invokes his Fifth Amendment privilege against compulsory self-incrimination in lieu of answering the averments contained in the pleading of his adversary, the district court should treat his claim as a specific denial and put the plaintiff to his proofs of the matter covered by the denial. *Rogers v. Webster*, 776 F.2d 607 (6th Cir. 1985).

9. In contempt proceedings which have not been committed in the presence of the judge, an evidentiary hearing is required. *See Harris v. United States*, 382 U.S. 162, 86 S.Ct. 352, 15 L.Ed.2d 240 (1965); *In re Finney*, 167 B.R. 820, 821 (E.D.Va. 1994). Summary adjudication of indirect contempts is prohibited. *International Union, United Mine Workers of America v. Bagwell,512 U.S. 821, 114 S.Ct. 2552, 129 L.Ed.2d 642 (1994).*

10. A criminal contempt charge is a separate and independent proceeding at law that is not part of the original action. *See Cooter & Gell v. Hartmarx Corp.*, 110

S.Ct. 2447, 110 L.Ed.2d 359 (1990); *Bray v. United States*, 423 U.S. 73, 96 S.Ct.307, 46 L.Ed.2d 215 (1925). *See also Gompers v. Bucks Stove & R. Co.*, 221 U.S. 418, 31 S.Ct. 492, 55 L.Ed. 797 (1910)(Court held that proceedings for criminal contempt are between the public and the defendant and are not part of the original cause).

11. The Bankruptcy Court has the power to sanction parties for civil contempt, *Alan Baker*, 195 B.R. 309; *In re North Jersey Trading Corporation*, 177 B.R. 814 (Bankr. D.N.J. 1995), *appeal denied*, 66 F.3d 312 (3rd Cir. 1995). However where "the contempt has not been committed in the presence of the court and evidence must be taken to establish contempt, the court's summary powers have been curtained to the extent that the accused must be presumed to be innocent, need not testify against himself and must be found guilty beyond a reasonable doubt." *Eskay*, 122 F.2d 819.

12. Unless the trial court enters an order *in limine* directing the prosecution of a defendant for criminal contempt on behalf of the court and unless papers supporting the process contain a copy of the order or allege its contents correctly, prosecution must be deemed for civil contempt and will support no other than remedial punishment. *Eskay*, 122 F.2d 819.

13. One of the primary due process protections afforded to an alleged contemnor is to inform the accused at the outset which form of contempt he is charged. *Eskay*, 122 F.2d at 823.

14. The stated purpose of the contempt sanction alone is not determinative for establishing whether it is civil or criminal. The court must also examine the character of the sanction. *Alan Baker*, 195 B.R. at 316.

15. "Where there is ground to doubt the wrongfulness of the conduct of the defendant, he should not be adjudged in contempt." *Alan Baker*, 195 B.R. at 316, citing *Quinter v. Volkswagen of America*, 676 F.2d 969, 974 (3rd Cir. 1982).

16. Any ambiguity in the law should be resolved in favor of the party charged with contempt. *Alan Baker*, 195 B.R. at 318. (internal citations omitted); *United States on behalf of I.R.S. v. Norton*, 717 F.2d 767 (3rd Cir. 1983).

B. Right to Jury Trial in Criminal Contempt Proceedings

17. The Sixth Amendment to the United States Constitution gives defendants a right to a trial by jury in "all criminal prosecutions." *U.S.C.A. Const. Amend. 6*

18. "Petty" contempt like other petty criminal offenses, however, may be tried without a jury. *Taylor v. Hayes*, 418 U.S. 488, 495, 94 S.Ct. 2697, 2701, 41 L.Ed.2d 897 (1974); *Frank v. United States*, 395 U.S. 149, 89 S.Ct. 1503, 23 L.Ed.2d 162 (1969). In determining whether a particular criminal offense can be classified as "petty", the most relevant indication of seriousness of the offense is the severity of penalty authorized for its commission. *Frank v. United States, supra*.

19. For "serious" criminal contempts involving imprisonment of more than six months, constitutional protections afforded an alleged contemnor include a right to jury trial. *International Union, United Mine Workers of America v. Bagwell¸512 U.S. 821, 114 S.Ct. 2552, 129 L.Ed.2d 642 (1994)*; *Bloom v. Illinois*, 391 U.S. 194, 88 S.Ct. 1477, 20 L.Ed.2d 522 (1968). *See also 18 U.S.C. Section 3691*.

20. In determining a right to jury trial in criminal contempt proceedings in which no maximum penalty is authorized, the severity of the penalty actually imposed is

the best indication of the seriousness of the particular offense for purpose of ascertaining whether defense should be categorized as "serious" or "petty", but if the statue creating the offense specifies the maximum penalty than that penalty is relevant. *Id.*

21. *18 U.S.C. Section 401* does not specify a maximum penalty for criminal contempt, nor does it categorized contempts as "serious" or "petty." *Frank v. United States, supra; Goldfine v. United States*, 268 F.2d 941 (1st Cir. 1959); *cert. den.*, 363 U.S. 842, 4 L.Ed. 2d 1727, 80 S.Ct. 1608 (1959).

22. In a prosecution under *18 U.S.C. Section 401*, both a fine and imprisonment cannot be imposed for a single contumacious act, no matter how serious. *See In re Bradley*, 317 U.S. 616, 63 S.Ct. 81 ,87 L.Ed. 500 (1942). However, in a prosecution for contempt which also involves a substantive offense, both a fine and imprisonment may be imposed. *18 U.S.C. Section 402*.

23. If a contempt also constitutes a substantive violation bringing it under the protection of *18 U.S.C. Section 402*, which provides for a maximum sentence of 6 months imprisonment, or a maximum fine of $1,000, or both, then a defendant has a right to a jury trial. *18 U.S.C. Section 402.*

24. *18 U.S.C. Section 3691* provides for a right to a jury trial for contempts involving willful disobedience of court orders where the "act or thing done or omitted also constitutes a criminal offense under any Act of Congress, or under the laws of any state…" *18 U.S.C. Section 3691*.

25. When a defendant charged with an indirect contempt in the Bankruptcy Court and requests a jury trial, the Bankruptcy Court is without power to hear the case. *In*

re Finney, 167 B.R. at 820, citing *In re Stansbury Poplar Place, Inc.*, 13 F.3d 122, 128 (4th Cir. 1993).

C. Civil vs. Criminal Contempt

i. Civil Contempt

26. In order to establish civil contempt, a plaintiff must prove the following three elements by clear and convincing evidence: "(1) a valid order of the court existed; (2) that the defendants had knowledge of the order; and (3) that defendants disobeyed the order." *Roe v. Operation Rescue*, 54 F.3d 133, 137 (3rd Cir. 1995); *Robin Woods, Inc. v. Woods*, 28 F.3d 396, 399 (3rd Cir. 1994), *Quinter v. Volkswagon of America*, 676 F.2d 969, 974 (3rd Cir. 1982); *In re Swanson*, 207 B.R. 76, 80 (Bankr. D.N.J. 1997). Once the petitioner makes out a *prima facie* case of civil contempt, the burden shifts to the contemnor to come forward with evidence to show a present inability to comply. *In re Affairs with Flair, Inc.*, 123 B.R. 724 (E.D.Pa. 1991).

27. A valid order exists if the terms are "specific and definite." *Alan Baker¸195* B.R. at 318, citing *In re Village Craftsman Inc.*, 160 B.R. 740 (Bankr. D.N.J. 1993). *Accord In re Rubin*, 378 F.2d 104 (3d Cir. 1967) (holding that an order claimed to be violated must be specific and definite).

28. Civil contempt has two purposes: one coercive and the other compensatory. *International Union, United Mine Workers of America v. Bagwell, supra*. The paradigmatic civil contempt order is one that allows the contemnor to purge the contempt by committing an affirmative act and who thus, as it were, "carriers the keys of

his prison in his own pocket." *Id.*, quoting *Gompers v. Bucks Stove & Range Co.*, 221 U.S. 418, 442 (1911).

29. The sanction in a civil contempt proceeding must give the contemnor an opportunity to purge himself, and must terminate once he complies. *Lance v. Plummer*, 353 F.2d 585 (5th Cir. 1965), *cert. den.*, 384 U.S. 929, 86 S.Ct. 1885, 16 L.Ed.2d 532 (1965). If the sanction will not compel compliance, it becomes punishment and violates due process. *In re Grand Jury Proceedings*, 877 F.2d 849 (11th Cir. 1989).

30. Neither the Trustee, Wilshire Credit Corporation nor Forum Insurance Company have established the elements of civil contempt as to Defendant by clear and convincing evidence.

ii. Criminal Contempt

31. Criminal contempt implies a crime. *In re Newman*, 196 B.R. 700 (Bankr. S.D.N.Y. 1996). Thus, criminal contempt penalties may not be imposed on someone who has not been afforded protections that the United States Constitution requires of criminal proceedings. *Hicks v. Feiock, supra.*

32. The purpose of criminal contempt is to vindicate offenses against public justice, rather than to enforce the rights of a part, and to compel respect for court orders. *Cook v. United States*, 267 U.S. 517, 45 S.Ct. 390, 69 L.Ed. 767 (1925).

33. In order for a criminal contempt to be found, as with civil contempt, the court must find that there was a clear and definite order of the court, the defendant had knowledge of the order, and that the defendant willfully disobeyed the order. In the Matter of Hipp, Inc., 5 F.3d at 112.

34. However, unlike civil contempt, in order to establish criminal contempt these elements must be proven beyond a reasonable doubt and it must be shown that the defendant willfully disobeyed the court's order. *Id*.

35. Neither the Trustee, Wilshire Credit Corporation nor Forum Insurance Company has not established the elements of criminal contempt as to Defendant beyond a reasonable doubt.

D. Sanctions Should Not Be Imposed Against Defendant And In Favor of Wilshire Credit Corporation

36. Sanctions under *Fed. R. Civ. P. 11* ("*Rule 11*") are reserved only for "exceptional circumstances." *Mary Ann Pensiero, Inc. v. Lingle*, 847 F.2d 90 (3rd Cir. 1988); *In re Kouterick*, 167 B.R. 353 (Bankr. D.N.J. 1994). Generally speaking, *Rule 11* sanctions are not triggered by advocating new or novel theories. *Gaiardo v. Ethel Corp.*, 835 F.2d 479 (3rd Cir. 1987).

37. Further, *Rule 11* is not intended to chill one's enthusiasm or creativity in pursuing factual or legal theories. *Gaiardo v. Ethel Corp.*, 835 F.2d at 484:

> Counsel or client violates the Rule by mounting an attack on existing law not in good faith but rather prompted by such improper considerations as harassment or undue delay. Creativity by itself is not enough. The creativity must be in the service of a good faith application of the law or at least a good faith request for a change in the law.

Id. at 484.

38. Sanctions in bankruptcy proceedings are governed by *Fed. R. Bankr. P. 9011* ("*Rule 9011*"). Under *Rule 9011*, the signer of a pleading has an obligation to make

a reasonable inquiry into the facts and law which support the pleading. *Jones v. Pittsburgh National Corp.*, 899 F.2d 1350, 1359 (3rd Cir. 1990).

39. The purpose of *Rule 9011* is equivalent to that of Rule 11 and the same standard of review is applied under both rules. *Kouterick*, 167 B.R. at 362, citing *Landon v. Hunt*, 977 F.2d 829, 833 n. 3 (3rd Cir. 1992); *Cinema Services Corp. v. Edbee Corp.*, 774 F.2d 584 (3rd Cir. 1985). *Accord In re Haardt*, 77 B.R. 480 (Bankr. E.D.Pa. 1987) (*Rule 9011* is intended to discourage, in bankruptcy proceedings, the same type of conduct which *Rule 11* proscribes). Therefore, it is not surprising that Rule 9011 tracks the language of *Rule 11* with only such modifications as are appropriate to reflect differences between bankruptcy cases and ordinary civil actions. *Id.* at 480.

40. The Third Circuit has summarized the essence of *Rule 11* as follows:

> The rule imposes an obligation on counsel and client analogous to the railroad crossing sign, Stop, Look and Listen." It may be rephrased, "Stop, Think, Investigate and Research" before filing papers whether to initiate a suit or to conduct the litigation. These obligations conform to those practices which responsible lawyers have always employed in vigorously representing their clients while recognizing the court's duty to serve the public efficiently. It bears repeating that the target is abuse—the Rule must not be used as an automatic penalty against an attorney or a party advocating the losing side of a dispute.

Gaiardo, supra.

41. The certification embodying *Rule 11* "is directed at the three substantive prongs of the Rule; its factual basis, its legal basis, and its legitimate purpose. *Haardt*, 77 B.R. at 480. In the context of *Rule 9011* the existence of "bad faith" is determined by an examination of the totality of the factors at issue. *In Matter of Elsub Corp.*, 66 B.R. 183, 189 (Bankr. D.N.J. 1986).

42. The Third Circuit has acknowledged that the standard for testing conduct under *Rule 11* is an objective one of reasonableness under the circumstances. *Kouterick*, 167 B.R. at 363, citing *Ford Motor Co. v. Summit Motor Products, Inc.*, 930 F.2d 277, 298 (3rd Cir. 1991)(other internal citations omitted).

43. The term "reasonableness" is defined as "an 'objective knowledge or belief at the time of the filing of a challenged paper' that the claim was well-grounded in law and fact. *Business Guides, Inc. v. Chromatic Communications Enterprises, Inc.*, 498 U.S. 533, 111 S.Ct. 922, 112 L.Ed.2d 1140 (1991).

44. The objective reasonableness standard "seeks to discourage pleadings 'without factual foundation, even though the paper was not filed in subjective bad faith,'" and to ensure that pleadings are not made for improper purposes such as delay, harassment or to increase litigation expenses. *Kouteric*, 167 B.R. at 363 (quoting *Lony v. E.I. Du Pont De Nemours & Co.*, 935 F.2d 604, 615 (3rd Cir. 1991). The proper analysis requires the court to focus on the circumstances that existed at the time counsel filed the challenged paper.

45. There are five factors which the Court should consider in applying the objective reasonableness standard under *Rule 11*; namely:

a). the amount of time available to the signer for conducting the factual and legal investigation;
b). the necessity for reliance on a client for the underlying factual information;
c). the plausibility of the legal position advocated;
d). whether the case was referred to the signer by another member of the bar; and
e). the complexity of the legal and factual issues implicated.

Kouteric, 167 B.R. at 363 (citing *Pensiero*, 847 F.2d at 95 (other internal citations omitted).

46. Bankruptcy Courts in the Third Circuit have generally expressed a distaste for imposing Rule 9011 sanctions. *See, e.g., In re Smith*, 111 B.R. 81 (Bankr. E.D.Pa. 1990); *In re Arena*, 81 B.R. 851, 856-857 (Bankr. E.D.Pa. 1988); *Gaiardo*, 835 F.2d at 482-485; *In re Geller*, 96 B.R. 564 (Bankr. E.D.Pa. 1989). As the Third Circuit in *Gaiardo* cautioned:

> The use of *Rule 11* as an additional tactic of intimidation and harassment has become part of the so-called "hardball" litigation techniques espoused by some firms and their clients. Those practitioners are cautioned that they invite retribution from courts which are far from enchanted with such abusive conduct. A court may impose sanctions on its own initiative when the Rule is invoked for an improper purpose.

Gaiardo, 835 F.2d at 485. Notwithstanding, the imposition of sanctions is mandatory if Rule 9011 has been violated. *In re Gioiso*, 979 F.2d 956 (3rd Cir. 1992); *Haardt*, 77 B.R. 480.

47. The power of federal courts to impose sanctions are not limited by *Rules 11* or *9011*. As explained by the Third Circuit in *Fellheimer, Eichen & Braverman, P.C. v. Charter Technologies, Inc.*, 57 F.3d 1215 (3rd Cir. 1995), federal courts have the inherent power to impose sanctions for bad faith. Thus, the mere fact that no sanction may be imposed under *Rules 11* or *9011* does not preclude federal courts from assessing sanctions in exercise of its inherent power. *Id.*

48. The United States Supreme Court addressed the nature and scope of the federal courts' inherent power to control the conduct of those who appear before them,

including attorneys, in *Chambers v. NASCO, Inc.*, 501 U.S. 32, 111 S.Ct. 2123, 115 L.Ed.2d 27 (1991). As explained by the Supreme Court in *Chambers*, the types of sanctionable conduct are those cases where:

> a party has " 'acted in bad faith, vexatiously, wantonly, or for oppressive reasons.' " … The imposition of sanctions in this instance transcends a court's equitable power concerning relations between the parties and reaches a court's inherent power to police itself, thus serving the dual purpose of "vindicat[ing] judicial authority without resort to the more drastic sanctions available for contempt of court and mak[ing] the prevailing party whole for expenses caused by his opponent's obstinacy."

Id. at 45-46, 111 S.Ct. at 2133 (internal citations and quotations omitted).

E. Piercing Corporate Veil

49. Defendant cannot be held in contempt or sanctioned in his individual capacity with respect to the filing of the bankruptcy proceeding of Gallup House Properties, Inc. in the United States Bankruptcy Court for the District of New Jersey, Newark Vicinage, Case No.: 97-44015, the very filing which the Trustee proffers as being violative of the Court's August 14, 1997 Order in the case at bar. Neither the Trustee, Wilshire Credit Corporation nor Forum Insurance Company have demonstrated the requisite proof to pierce the corporate veil of Gallup House Properties, Inc. in order to establish personal liability as to its President - the Defendant.

50. A corporation is a separate entity from its shareholders. *State v. Dept. of Environmental Protection v. Ventron Corp.*, 94 N.J. 473, 500 (1983). The primary reason for incorporation is insulation of shareholders from liability of the corporate enterprise. *Id.*

51. "Except in cases of fraud, injustice or the like, courts will not pierce the corporate veil. *Lyon v. Barrett*, 89 N.J. Super 294, 300 (1982). The purpose of the doctrine of piercing the corporate veil is to prevent an independent corporation from being used to defeat the ends of justice, *Telis v. Telis*, 132 N.J.Eq. 25 (E. & A. 1942), to perpetrate a fraud, to accomplish a crime, or otherwise to evade the law. *Trachman v. Trugman*, 117 N.J. Eq. 167, 170 (Ch. 1934)." *State v. Dept. of Environmental Protection v. Ventron Corp., supra*. *Accord In re HSR Associates*, 162 B.R. 680 (Bankr. D.N.J. 1994)(Under New Jersey law, corporate veil will be pierced only in cases of fraud or injustice).

52. Under New Jersey law, the fact that a corporation consists of a sole shareholder is not sufficient, in and of itself, to disregard the corporate identity. *Matter of Velis*, 123 B.R. 497 (D.N.J. 1991), *aff'd in part, reversed in part sub nom Velis v. Kardanis*, 949 F.2d 78, *rehearing denied* (3rd Cir. 1991). A corporate identity will be deemed a fiction and disregarded where the corporation is an alter ego of its shareholders to the extent that the shareholders' disregard of the corporate entity made it a mere instrumentality of their own affairs, that there was such unity of interest and ownership that separate personalities of corporation and its owners no longer exist, and adherence to doctrine of corporate entity would promote injustice or protect a fraud. *Id.*

53. The fact that a closely held corporation is owned by one or more shareholders or family members is not sufficient, in and of itself, to undermine the corporate identity. *Coppa v. Taxation, Division Director*, 8 N.J. Tax 235 (N.J. Tax 1986).

54. Under New Jersey law, the party seeking to pierce the corporate veil bears the burden of persuasion. *Matter of Velis, supra*; *In re HSR Associates, supra*. *Accord Local 397, International Union of Electronic Elec. Salaried Mach. And Furniture Workers, AFL-CIO v. Midwest Fasteners, Inc.*, 779 F.Supp. 788 (D.N.J. 1992).

55. Under New Jersey law, fraud justifying piercing the corporate veil can be legal or equitable. *In re HSR Associates, supra.*

56. Under New Jersey law, "legal fraud" is defined as a material misrepresentation of a presently existing or past fact, made with knowledge of its falsity and with intention that the other party rely thereon, resulting in reliance by that party to his detriment. *Diaz v. Johnson Matthey, Inc.*, 869 F.Supp. 1155 (D.J.J. 1994. *See also Lightening Tube, Inc. v. Witco Corp.*, 4 F.3d 1153, 1183 (3rd Cir. 1993) (Reliance must be reasonable).

57. To sustain a claim for legal fraud, a plaintiff must prove his case by a preponderance of the evidence. *Lightening Tube, Inc., supra*.

58. Unlike legal fraud, equitable fraud does not require the elements of scienter, knowledge of the falsity, and an intent to obtain an undue advantage. *Baldasarre v. Butler*, 254 N.J. Super. 502 (App. Div. 1992), *certif. den.*, 130 N.J. 10, *aff'd in part, rev'd in part*, 132 N.J. 278 (1992). The elements of equitable fraud are a material misrepresentation of fact; upon which a party relied; and to its damage. *Matter of Baby M*, 217 N.J. Super. 313, 379 (Ch. Div. 1987), *certif. granted*, 107 N.J. 140 (1987), *on remand*, 225 N.J. Super. 267 (Ch. Div. 1988).

59. In an action for equitable fraud, only equitable relief may be obtained, such as rescission or reformation of an agreement, but not monetary damages. *Enright v.*

Lubow, 202 N.J. Super. 59 (App. Div. 1985), *on reconsideration*, 215 N.J. Super. 306 (App. Div. 1987), *certif. den.*, 108 N.J. 193 (1987); *Foont-Freedenfeld Corp. v. Electro-Protective Corp.*, 126 N.J. Super. 254 (App. Div. 1973), *aff'd*, 64 N.J. 197 (1974).

60. To sustain a claim for equitable fraud, a plaintiff must prove his case by clear and convincing evidence. *Lightening Tube, Inc., supra.*

F. Gallup House Properties, Inc. Is A Necessary and Indispensable Party Who Should Be Joined In This Action

61. Pursuant to *Fed. R. Bankr. P. 9014* which governs "contested matters," "unless the court otherwise directs, the following rules shall apply: 7021, 7025, 7026, 7028-7037, 7041, 7042, 7052, 7054-7056, 7062, 7064, 7069, and 7071. The court may at any state in a particular matter direct that one or more of the other rules in Part VII shall apply." *Fed. R. Bankr. P. 9014.*

62. In view of the magnitude of the civil and criminal charges being sought by the moving parties, Defendant respectfully submits that the Court apply *Fed. R. Bankr. 7019* (mandatory joinder), and *Fed. R. Bankr. P. 7021* (misjoinder and non-joinder of parties).

63. Gallup House Properties, Inc. is a necessary and indispensable party to the motions filed by the Trustee, Wilshire Credit Corporation and Forum Insurance Company pursuant to *Fed. R. Civ. P. 19* and *Fed. R. Bankr. P. 7019.* Accordingly, Gallup House Properties, Inc. was entitled to receive notice of the motions filed by the Trustee, Wilshire Credit Corporation and Forum Insurance Company in accordance with *Fed. R. Bankr. P. 2002* and *Fed. R. Bankr. P. 9014.*

64. The Trustee, Wilshire Credit Corporation and Forum Insurance Company's motions must be denied for failure to join Gallup House Properties, Inc., a necessary and indispensable party. Alternatively, Gallup House Properties, Inc. should be joined as a party to these contempt proceedings in accordance with *Fed. R. Bankr. P. 7019* and *Fed. R. Bankr. P. 7021*.

G. The Principles of *Res Judicata* and Collateral Estoppel As To Facts and Conclusions Of Law Established against Co-Defendant Eric Keller Are Not Binding On This Defendant

65. *Res Judicata* or "claim preclusion" is an ancient judicial doctrine which contemplates that when a controversy between parties is once fairly litigated and determined it is no longer open to relitigation. *Lubiner v. Board of Alcoholic Beverage Control for City of Paterson* , 33 N.J. 428 (1966).

66. The doctrine of r*es judicata* applies to decisions of bankruptcy courts, *Katchen v. Landy*, 382 U.S. 323, 334, 86 S.Ct. 467, 475, 15 L.Ed.2d 391 (1966). "Under the modern transactional view of claim preclusion, a plaintiff is not permitted to raise issues in the second action which could have been raised under the pleadings in the first action. *In re Graham*, 131 B.R. 275, 278 (Bankr. E.D.Pa. 1991), *vacated and remanded*, 973 F.2d 1089 (3rd Cir. 1992), *on remand sub nom, Graham v. I.R.S.*, 74 A.F.T.R.2d 94-5887 (Bankr. E.D.Pa. 1994). "The principle that the previously unlitigated claim could and should have been brought in the earlier litigation is the heart of the doctrine. *In re Fonda Group, Inc.*, 108 B.R. 962, 969 (Bankr. D.N.J. 1989).

67. Successful application of *res judicata* requires a showing that there has been: (i) a final judgment on the merits in a prior matter; (ii) involving the same parties

or their privies; and (iii) a subsequent matter based on the same cause of action. *In re Glenn*, 124 B.R. 195, 199 (Bankr. W.D.Pa. 1991).

68. Collateral estoppel is a branch of the broader law of *res judicata* that bars relitigation of any issue actually determined in a prior action between the parties, and is somewhat narrower concept that claim preclusion, which is normally associated with *res judicata*. *Suarez v. Camden County Bd. of Chosen Freeholders* , 972 F.Supp. 269 (D.N.J. 1997). Collateral estoppel precludes relitigation of an issue that has been put in issue and directly determined adversely to the party against whom estoppel is asserted. *Kitces v.* Wood, 917 F.Supp. 338 (D.N.J. 1996).

69. Neither the elements of *res judicata* nor collateral estoppel have been established against Defendant by virtue of this Court's prior Orders entered in this case on April 8, 1998 holding Co-Defendant Eric Keller in civil and criminal contempt.

PLEA OF "NOT GUILTY"

Defendant hereby enters a plea of "not guilty" to the charge of criminal contempt.

JURY DEMAND

Defendant demands a right to a jury trial pursuant to *Fed. R. Bankr. P. 9020(d), 18 U.S.C. Section 3691,* and in accordance with *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989) as to all issues so triable as to the charges of civil and criminal contempt. Defendant does not consent to a jury trial in the Bankruptcy Court pursuant to *28 U.S.C. Section 157 (e).*

DEMAND FOR DISCOVERY

In accordance with *Fed. R. Bankr. P. 9014* and *Fed. R. Bankr. P. 7026*, defendant demands discovery from the Trustee of the following:

1. All documents which refer or relate to the investigation performed by the Office of the U.S. Trustee at the directive of the United States Bankruptcy Court for the District of New Jersey, in connection with this and all other proceedings in which the Trustee is alleging the Defendant's conduct constitutes civil and/or criminal contempt.

2. The names and addresses of all witnesses who may have knowledge of facts relevant to the subject matter of the Trustee's motion for civil and criminal contempt against Defendant.

3. The names and addresses of all witnesses whom the Trustee intends to call to testify at the trial with respect to its motion against Defendant for civil and/or criminal contempt.

4. Any and all documents which may exculpate the Defendant from civil and/or criminal contempt charges.

Respectfully submitted,

LOFARO & REISER, L.L.P.
-and-
FLOOD & BASILLE
Co-Counsel for Defendant/Respondent,
Ronald Keller

By:_____
Glenn R. Reiser
Raymond T. Flood

Dated: April ____, 1998