

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW HAMPSHIRE**

In re:

Bk. No. 01-12733-JMD
Chapter 7

George B. Sloane,
Debtor

John Hancock Financial Services, Inc.,
Plaintiff

v.

Adv. No. 01-1213-JMD

George B. Sloane,
Defendant

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MEMORANDUM OPINION

I. INTRODUCTION

The Court has before it a complaint filed by John Hancock Financial Services, Inc. (“John Hancock”) in which it seeks to except from discharge pursuant to section 11 U.S.C. § 523(a)(2)(A) any obligation of George B. Sloane (the “Debtor”) to John Hancock arising out an agreement (the

“Charter Agreement”) for the charter of a 112 foot, two masted, sailing vessel known as the Schooner Roseway (the “Roseway”) during the Sail Boston/Tall Ships festivities in July 2000.¹

This Court has jurisdiction of the subject matter and the parties pursuant to 28 U.S.C. §§ 1334 and 157(a) and the “Standing Order of Referral of Title 11 Proceedings to the United States Bankruptcy Court for the District of New Hampshire,” dated January 18, 1994 (DiClerico, C.J.). This is a core proceeding in accordance with 28 U.S.C. § 157(b).

II. FACTS AND DISCUSSION

John Hancock’s factual allegations have previously been set forth in the Court’s memorandum opinion on the Debtor’s motion to dismiss, see Sloane I, 2002 BNH 010 at 3-5, and will not be repeated here except to the extent that the Court finds it necessary or that the evidence at trial compels different or additional factual findings. In its complaint John Hancock asks the Court to determine the amount of damages it sustained as a result of the Debtor’s failure to produce the Roseway for the Sail Boston/Tall Ships event in July 2000, including interest, costs, punitive damages, and attorneys’ fees, and to except such debt from discharge as a debt incurred by the Debtor’s false pretenses, false representations, or actual fraud.

Section 523(a)(2)(A) requires a creditor to demonstrate by a preponderance of the evidence the following elements:

1. The debtor made a knowingly false representation or one made in reckless disregard of the truth;
2. The debtor intended to deceive;

¹ The Court previously dismissed John Hancock’s claim under 11 U.S.C. § 523(a)(6) when it granted in part the Debtor’s motion to dismiss John Hancock’s complaint. John Hancock Fin. Servs., Inc. v. Sloane (In re Sloane), 2002 BNH 010 (“Sloane I”).

3. The debtor intended to induce the creditor to rely upon the false statement;
4. The creditor actually relied upon the misrepresentation;
5. The creditor's reliance was justifiable; and
6. The reliance upon the false statement caused damage.

Grogan v. Garner, 498 U.S. 279, 291 (1991) (stating the standard of proof under section 523(a) is preponderance of the evidence); Palmacci v. Umpierrez, 121 F.3d 781, 787 (1st Cir. 1997) (same); McCroory v. Spigel (In re Spigel), 260 F.3d 27, 32 (1st Cir. 2001) (citing Palmacci, 121 F.3d at 786 (setting forth elements of section 523(a)(2)(A)). Exceptions to discharge are narrowly construed in order to further the Bankruptcy Code's "fresh start policy" and, for that reason, a creditor must demonstrate that its claim comes squarely within an exception to discharge contained in section 523(a). Palmacci, 121 F.2d at 786 (quoting Century 21 Balfour Real Estate v. Menna (In re Menna), 16 F.3d 7, 9 (1st Cir. 1994)).

In Sloane I, this Court previously held that under Massachusetts law, the law applicable to the Charter Agreement, a plaintiff could recover from an individual corporate officer or employee for the tort of misrepresentation if:

1. The defendant made a false statement with knowledge of the falsity;
2. The false statement concerned a material fact;
3. The false statement was made to induce the plaintiff to act;
4. The plaintiff relied on the false statement; and
5. The plaintiff acted on the false statement to his detriment.

See Sloane I, 2002 BNH 010 at 8 (citations omitted). The testimony at trial established that the Debtor was the president and sole shareholder of Atlantic Shores Packet Company, Inc. d/b/a Yankee Schooner Cruises, owner of the Roseway (the "Owner"), at all relevant times in this

proceeding and was the only employee of the Owner who had any dealings with John Hancock, the Coast Guard and their agents and representatives. The elements required under state law to hold the Debtor individually liable for the alleged misrepresentations are essentially identical to the elements necessary to deny the Debtor a discharge of such obligations under section 523(a)(2)(A). Therefore, for the purposes of this memorandum opinion no distinction will be drawn between the Debtor and the Owner.

A. False Representations

1. Time of Contract and First Payment

In March 2000, George Dow, John Hancock's General Director of Visual Operations, contacted the Debtor regarding the possibility of chartering the Roseway during the Sail Boston/Tall Ships 2000 event. Mr. Dow had arranged for John Hancock to charter ships during prior Tall Ships events and was familiar with the Roseway and sailing in general. The Debtor indicated to Mr. Dow that the Roseway would be available for charter during the period July 7, 2000, to July 13, 2000 (the "Charter Period"), and Mr. Dow tentatively agreed to charter the vessel at a price of \$45,000.00. Kenneth Owens, an independent public relations consultant working for John Hancock, then negotiated the Charter Agreement, with the assistance of William Gottlieb, in-house counsel for John Hancock, with the Debtor. After certain revisions, the parties executed the Charter Agreement, with the Debtor signing the Charter Agreement on behalf of the Owner on April 5, 2000, and Mr. Owens signing the Charter Agreement on behalf of John Hancock on April 6, 2000. Consistent with the terms of the Charter Agreement, Mr. Owens forwarded a check for the first payment of \$22,500.00 payable to "Atlantic Shores Packet Company." At no time prior to the execution of the Charter Agreement did representatives from John Hancock view the Roseway as it was still in the Carribean for the winter season.

During this period, the Debtor was aware that pursuant to an agreement with the Coast Guard dated December 7, 1999, the Owner was responsible for undertaking certain repairs to the Roseway by June 15, 2000. The Debtor also knew that he intended to seek a deferment of the required repairs from the Coast Guard until October 2000, after the conclusion of the summer sailing season and, in fact, made such a formal request of the Coast Guard on behalf of the Owner on April 4, 2000. The Debtor did not share this information with John Hancock and such failure forms the basis for part of John Hancock's complaint.

In determining whether the Debtor made a false statement, false representation, or committed actual fraud, the Court must examine the Debtor's actions and statements in light of the circumstances that existed at the time John Hancock and the Debtor, on behalf of the Owner, entered into the Charter Agreement. If, at the time the Debtor made his statements regarding the future availability of the Roseway, the Debtor actually intended to perform such future action, but the Debtor then later changed his mind or intervening events caused him to act otherwise, the Court must find that the Debtor made no false representation because a debtor's statement of future action is a false representation only if, at the time the statement was made, the debtor did not intend to carry out the stated future action. Palmacci, 121 F.3d at 787.

In the instant case, John Hancock argues that the Debtor made a false statement or misrepresentation when he stated or did the following:

1. The Debtor stated to Mr. Dow in March or April of 2000, that the Roseway would be available for charter during the Charter Period.
2. The Debtor stated in writing in the Charter Agreement that the Roseway would be "in full commission and working order, seaworthy, clean, in good condition throughout and ready" during the Charter Period.
3. The Debtor failed to disclose (A) the extensive repairs to the Roseway required by the Coast Guard, (B) his alleged financial inability to make the required repairs by

June 15, 2000, and (C) his April 4, 2000, request to the Coast Guard to postpone the required repairs.

John Hancock has failed to establish by a preponderance of the evidence that in April 2000 the Debtor did not intend to provide the Roseway during the Charter Period. In fact, the evidence supports a finding that the Debtor actually intended to perform as required under the Charter Agreement. The fact that the Debtor sought to defer the Coast Guard mandated repairs required by June 15, 2000 does not compel the Court to find that the Debtor did not intend to produce the Roseway for the Charter Period and that, therefore, he made a false statement when he indicated in April 2000 it would be available. Rather, the fact that the Debtor sought to defer the repairs is consistent with an intention to continue operating the vessel until some time in October when the repairs would be made. The Debtor apparently wanted to operate the Roseway during the 2000 summer season and do so with minimal capital expenses before the season. Even if the Debtor were unable to obtain the Coast Guard's agreement to defer the repairs as requested by the Debtor on April 4, 2000, under the standing order from the Coast Guard the Owner was required to complete certain repairs by June 15, 2000, which was more than three weeks prior to the Charter Period and more than two months after the Debtor executed the Charter Agreement with John Hancock. Thus, in early April 2000, the Debtor was faced with two possibilities. Either he would have to complete the Coast Guard mandated repairs on or before June 15, 2000, in which case the Roseway would be ready for charter on July 7, 2000; or with Coast Guard approval, the Debtor would be able to defer the repairs until October 2000, in which case the Roseway would also be ready for charter on July 7, 2000.

John Hancock argues that the Debtor did not have the financial ability to make the repairs and therefore the Debtor's beliefs regarding his ability to produce the Roseway for charter was

unreasonable and reckless. John Hancock focuses on the fact, however, that the total repairs under the five year plan agreed upon with the Coast Guard were going to cost between \$400,000.00 to \$500,000.00, and the Debtor did not have the ability to generate cash or raise such a large amount of capital by October 2000. However, by focusing on the total five year repair costs, John Hancock ignores the fact that the repairs required to be made by June 15, 2000, would cost and, in fact, did cost substantially less. John Hancock argues that the Debtor had no intention of completing the required repairs and that he simply wanted to defer the date of reckoning with the Coast Guard. Even if this argument were correct, such motivation is not inconsistent with the ship being available for the Charter Period. If the Coast Guard had agreed to the deferment, the ship would have been licensed to carry passengers during the Charter Period. If the Coast Guard did not agree to the deferment, the Owner would have been required to complete some, but not all, of the five year repair schedule. No evidence was presented concerning the cost of the repairs required by June 15, 2000. However, the evidence did disclose that the repairs were in fact completed to the Coast Guard's satisfaction between June 22 and July 14, 2000. See Ex. 27. Therefore, John Hancock has not established that the Debtor's beliefs were unreasonable and reckless in April 2000.

John Hancock argues further that the Debtor's omissions (i.e., his failure to disclose the Coast Guard order and his request to defer repairs) constitute false statements. The Court is unable to make such findings for several reasons. First, John Hancock has not convinced the Court that the Debtor had any obligation to make such disclosures. Second, despite John Hancock's assertions that such information was important to it, John Hancock presented no evidence that its representatives, either Mr. Dow or Mr. Owens, ever asked the Debtor about the need for any

repairs to the Roseway, asked whether there were outstanding orders from the Coast Guard mandating repairs, or requested a copy of the most recent annual Coast Guard inspection report.

The evidence established that John Hancock utilized Mr. Dow as its agent during this process because of his knowledge and experience with sailing ships as well as his previous service to John Hancock in chartering sailing ships for various corporate events. Mr. Dow testified that he would have carefully considered any Coast Guard mandated repairs in his decision to recommend the charter of the Roseway because of his involvement in other charters where there were problems completing such repairs. He also testified that he initially inquired about the availability of the Roseway, a seventy-five year old wooden sailing ship, based upon his knowledge of the ship's size and suitability for John Hancock's purposes. Despite the fact that the ship was not available in New England for an inspection, no evidence was presented that Mr. Dow ever asked the Debtor about the condition of the ship or whether the Roseway needed to undergo any repairs or was under any Coast Guard order to do so. The evidence did establish that the Roseway was required to pass an annual Coast Guard inspection in order to maintain its certification to carry passengers. The evidence also established that such annual inspections, especially those involving older wooden sailing ships, usually result in a list of repairs and work which must be completed to the Coast Guard's satisfaction. Notwithstanding Mr. Dow's knowledge of sailing vessels and his prior experience in chartering such ships, no evidence was offered that any representative of John Hancock asked the Debtor about such inspections or any scheduled yard work prior to the execution of the Charter Agreement.

Accordingly, John Hancock has failed to present any evidence that the Debtor intended to misrepresent the condition or availability of the Roseway to John Hancock or had a duty to volunteer information on the ship's maintenance schedule. For these reasons, the Court holds that

John Hancock has not met its burden of establishing that the Debtor made a false statement or misrepresentation in March or April 2000. John Hancock did not establish that the Debtor knew or should have know in April 2000 that he would be unable to provide the Roseway during the Charter Period because of the need to make Coast Guard mandated repairs. As explained above, a debtor does not make a false representation if the debtor intends to perform an action in the future but that action does not occur because the debtor later changes his mind or intervening events cause him to act otherwise. The Court finds that the \$22,500.00 deposit paid by John Hancock in April 2000 should not be excepted from discharge pursuant to section 523(a)(2)(A).

2. Time of Second Payment

After the parties entered into the Charter Agreement and before John Hancock made its second payment, additional events transpired. On May 10, 2000, the Coast Guard denied the Debtor's request to defer the June 2000 repairs until October 2000. A few days later, the Roseway arrived in Gloucester, Massachusetts, from the Carribean where it had spent the winter season. On or about May 23, 2000, Mr. Dow and Mr. Owens met with the Debtor in Gloucester to view the ship. Mr. Dow testified that at that meeting he raised with the Debtor his concerns regarding whether the Roseway would be ready for the Charter Period. According to Mr. Dow, the vessel was unkept, appeared generally to be in ill repair and the bowsprit was broken. The Debtor indicated that the Roseway would be available but that repairs needed to be undertaken. The Debtor stated further that the repairs would not be undertaken in Gloucester as originally planned, but that the Roseway would be moved to Boothbay Harbor, Maine, in order to complete them. John Hancock offered no evidence that after this initial inspection Mr. Dow, or any other representative of John Hancock, ever asked the Debtor for a list of repairs or a copy of the most recent annual Coast Guard inspection.

Under the Charter Agreement, John Hancock was obligated to make a second deposit of \$11,250.00 on or before June 6, 2000. Despite knowing that the Roseway needed to be repaired (although not knowing that such repairs were required by the Coast Guard) and knowing that such repairs would be undertaken in Boothbay Harbor, not Gloucester, John Hancock issued a check on May 31, 2000, for the second deposit, payable to “Yankee Schooner Cruises.” The Debtor negotiated the check on or about June 12, 2000.

John Hancock argues that the Debtor made a false representation by failing to inform it that the Coast Guard was the one requiring the repairs, that the Debtor’s request for a deferral of those repairs was denied, and that the real reason for not conducting repairs in Gloucester was that the Debtor was continuing to seek a deferral until October 2000. At the time that John Hancock made the second payment it knew, because its representatives had seen the condition of the ship and the Debtor had told such representatives, that the Roseway needed to be repaired and that such repairs would take place in Maine. However, the Debtor did not tell John Hancock that the Coast Guard had rejected the Debtor’s request to defer the repairs scheduled for June to October. John Hancock asserts that it would have made other charter arrangements if it had been informed that the Debtor was continuing to attempt to defer such repairs. Even if that were true, that does not make the Debtor’s statements or omissions misrepresentations. As long as the Debtor reasonably believed on May 23, 2000, that the Roseway would be available for the Charter Period, his statements on that date regarding availability or any failure to disclose the repair requirements were not false or misleading.

John Hancock’s witnesses testified that after the second deposit was paid they continued to follow up with the Debtor regarding the status of the repairs to be made to the Roseway and that the Debtor became less certain over time that the ship would be available for the Charter Period.

The evidence establishes that the Roseway proceeded to Boothbay Harbor and was hauled out of the water sometime prior to June 22, 2000. By June 22, 2000, planking had been removed from the starboard quarter of the hull, ceiling panels had been removed at the transom and the Coast Guard had conducted its initial inspection. See Ex. 27. The shipyard manager and the shipwright working on the Roseway testified that the Debtor authorized overtime work in order to complete the job in time for the beginning of the Charter Period on July 7, 2000. Mr. Dow also visited the shipyard and was unable to receive assurances from the Debtor that the Roseway would be available for the Charter Period. In fact, he testified that the Debtor advised him that John Hancock should not count on the Roseway's availability during the first day or two of the Charter Period. On June 27, 2000, Mr. Dow advised the Debtor in a telephone conversation that John Hancock was canceling the charter due to concerns over the vessel being ready on time. See Exs. 4 and 5. The shipwright testified that sometime in late June the Debtor eliminated overtime work because there was no longer a reason to expedite the work. The work was completed and the final in-the-water Coast Guard inspection occurred on July 14, 2000. See Ex. 27.

The evidence establishes that sometime in mid-to-late June 2000 the Debtor was concerned about his ability to meet the commitments in the Charter Agreement and that John Hancock was similarly concerned. John Hancock pressed the Debtor for assurances and he became increasingly unwilling to provide the level of assurance that John Hancock was seeking. Notwithstanding these concerns, the Debtor authorized overtime and an expedited repair schedule in an apparent attempt to have the Roseway available for the Charter Period. However, no evidence was presented which suggested that as of May 23, 2000, or as of the delivery of the second deposit in early June that the Debtor knew, or should have reasonably known, that the work on the Roseway could not have been completed in time to fulfill the Charter Agreement. The Court finds it unlikely that the

Debtor with admitted financial problems and a history of trying to minimize repair expenses would authorize an expensive schedule of overtime work if he had no intention to fulfill the Charter Agreement.

Given the evidence before it, the Court cannot conclude that as of the date of the receipt of the second deposit, or immediately before such date, the Debtor did not intend to, or reasonably believe that he could, fulfill the terms of the Charter Agreement. John Hancock has failed to establish by a preponderance of the evidence that the Debtor made a false statement in May 2000 prior to John Hancock making its second payment of \$11,250.00 in accordance with the terms of the Charter Agreement. Accordingly, John Hancock has not met its burden of proof regarding the first element of its claim under section 523(a)(2)(A).

B. Remaining Elements under Section 523(a)(2)(A)

Because John Hancock has not established by a preponderance of the evidence that the Debtor either made a knowingly false representation or a representation made in reckless disregard of the truth, the Court need not address the other elements of John Hancock's claim under section 523(a)(2)(A). Therefore the Court need not determine the amount of damages that John Hancock may have sustained as a result of the Roseway not being available during the Charter Period as such debt is dischargeable.

III. CONCLUSION

The Court concludes that John Hancock did not satisfy its burden under section 523(a)(2)(A) of proving that the Debtor obtained money by false pretenses, a false statement, or actual fraud. Accordingly, Count I of John Hancock's complaint is denied. This opinion constitutes the Court's findings of fact and conclusions of law in accordance with Federal Rule of

Bankruptcy Procedure 7052. The Court will issue a separate judgment consistent with this opinion.

DATED this 29th day of November, 2002, at Manchester, New Hampshire.

/s/ J. Michael Deasy
J. Michael Deasy
Bankruptcy Judge