NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW JERSEY

IN RE:	:	
WILLIAM R. SCHROEDER, JR. and KATHLEEN A. SCHROEDER,	:	CHAPTER 7
Debtors.	:	CASE NO. 01-14748 (GMB)
GEOFFREY L. STEIERT and PENSCO PENSION SERVICES, INC.,	:	ADVERSARY NO. 01-1273 (GMB)
Plaintiffs,	:	
v.	:	MEMORANDUM OPINION
WILLIAM R. SCHROEDER, JR. and KATHLEEN A. SCHROEDER,	:	
Defendants.	:	

APPEARANCES:

Geoffrey Steiert
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Voorhees, NJ 08043
Appearing Pro Se

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I. INTRODUCTION

The matter was brought before the Court upon the filing of an adversary complaint by Plaintiff, Geoffrey L. Steiert, on September 26, 2001, appearing pro se against Debtors/ Defendants William and Kathleen Schroeder (the "Debtors" or "Defendants") seeking nondischargeability of a debt in the principal amount of $357,150 pursuant to 11 U.S.C. §§ 523(a)(2)(A) and 523(a)(4).[1]

The debt stems from investments in the purchase of promissory notes by the Plaintiff Steiert individually and through several corporate entities. The complaint alleges that these promissory notes were issued by Mata Services, Inc. ("Mata") and sold by the Debtors to the Plaintiff. The Complaint further asserts an investment in the sum of $57,150 in the purchase of a note by PENSCO Pension Services, San Francisco, California ("PENSCO"), as custodian of Mr. Steiert's self-directed IRA account. In addition, Plaintiff Steiert alleges an additional $250,000 investment, bringing his total alleged investment, including $20,000 he claims to have spent in a good faith pursuit of recovery of these funds, to over $357,150.

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[1] By agreement of the parties, Counts IV, V, VI and VII have been dismissed by Stipulations of Dismissal dated September 16, 2002 and June 9, 2003. The following allegations remain to be decided:

> (I) affirmative fraudulent misrepresentations in alleged violation of section 523(a)(2)(A) (Count I);
>
> (ii) intentional omissions of material facts, in alleged violation of section 523 (a)(2)(A)(Count II); and
>
> (iii) defalcations by a fiduciary, in alleged violation of section 523(a)(4) (Count III A).

The record reveals that the Complaint in this matter was amended by the Plaintiff on November 26, 2001 and January 11, 2002. On December 17, 2001, the Court entered an order denying a Motion to Dismiss filed by the Defendants. An answer was filed by the Debtors on December 3, 2001. An answer to the Amended Complaint was filed by the Defendants on January 16, 2002. After a protracted period of discovery and the filing of lengthy pre-trial submissions, as well as the admission of related state court receivership proceedings in lieu of testimony, the Court conducted a trial of this matter on March 27, 2003, April 15, 2003, May 29, 2003, and June 6, 2003, after which time it reserved decision.

II. JURISDICTION

Matters concerning the dischargeability of a debt are core proceedings pursuant to 28 U.S.C. § 157(b)(2)(I). The within Opinion constitutes this Court's findings of fact and conclusions of law pursuant to Fed. R. Bankr. P. 7052.

III. FINDINGS OF FACT

A. Factual Background Concerning Charles McCormick Mata Factoring and Ki-Digital Six Percent Notes

Prior to rendering its specific factual findings in this case, the Court notes for the record that the within matter is in fact the third in a series of three nondischargeability actions filed and tried by various creditors of Debtors William and Kathleen Schroeder relating to the sale of promissory notes in the late 1990's by the Debtors through Mata, and later through its related entity known as Ki-Digital ("Ki-Digital"). The Court rendered its first Opinion orally in the

matter of Robert G. Stevens, Esq. v. William Schroeder, et al., Adv. Pro No. 01-1112 on April 18, 2002,[2] and its second Opinion in written form in V. Thomas Yarnall, Jr. v. William R. Schroeder, Jr., et al, Adv. Pro. No. 01-1270 on March 29, 2006. [3]

At the outset, it is important to note that this Court has repeatedly indicated in the course of these three independent adversary proceedings that the evidence presented in one proceeding has no direct bearing on the factual record in the other two, except as an aid to the Court in its general understanding of the basic factual background common to all three proceedings.

In this regard, since certain of the factual findings as to general factual background in the Stevens and Yarnall matters are directly relevant to the case *sub judice,* they are specifically incorporated by reference as noted below. The Court emphasizes however that the parties to these proceedings have been left to their proofs with respect to establishing a record regarding the section 523 claims and defenses asserted and as argued at trial.[4]

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[2] Adversary Complaint No. 01-1112 was filed on May 17, 2001. In the Stevens matter, the Court entered an Order of Final Judgment in the amount of $100,000.00 in favor of Plaintiff Robert G. Stevens, Esq., Receiver for Ki-Digital and against the Defendants William R. Schroeder and Kathleen Schroeder, on May 8, 2002. On January 2, 2003 the Order was affirmed by the District Court.

[3] For purposes of accuracy, the Court notes the existence of a fourth Adversary Complaint pursuant to § 727 of the Bankruptcy Code, Hai T. Nguyen v. William Schroeder, Adv. No. 01-1192, filed on August 10, 2001. A Stipulation to Dismiss with Prejudice was filed on October 30, 2002.

[4] This Court has previously denied Plaintiff's motion for *res judicata* entitling plaintiff to summary judgment, based on essential factual findings by this Court underlying the judgment in favor of the Receiver granted in Stevens, or seeking in the alternative issue preclusion on some of those basic factual issues. This Court ruled that Plaintiff must establish each of the factual findings based solely on the factual record introduced by the evidence presented in this adversary proceeding. The Court again denied a motion for reconsideration brought at the inception of trial based on the subject of issue preclusion.

On May 4, 2001, the Debtors William and Kathleen Schroeder filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code.[5]

As recognized by the Court in Stevens and Yarnall, during the fall of 1996, the debtors became involved in a financial deal with an individual identified as Charles McCormick, a high school friend of the Debtors. Mr. McCormick, who had previously worked as an exterminator and had no college background, advised the Schroeders that he had bought computers at a discount and had an agreement to sell them for a profit, however, he needed financing to complete the transaction and would pay interest for a short term loan.

The Schroeders took an advance on their credit card, loaned the money to McCormick and were repaid with interest. After that transaction was completed, they entered into another. They saw no documentation and had no information regarding the buyers and sellers of the computer equipment. The parties have stipulated that neither Mr. or Mrs. Schroeder had knowledge of the precise payment terms for any of the computer re-sale transactions, including the dollar amount or exact percentage of any down payment or deposit. They told others of the return on their investments and subsequently began handling the collection of funds from investors in return for promissory notes and with respect to which, the Schroeders were paid commissions. In discussing factoring transactions with prospective investors, the Schroeders reiterated the facts and claims included in an undated two page introduction letter ("Introduction Letter"), Exhibit P-3B.

Mrs. Schroeder, who had been working at a hospital at the time of the first McCormick transaction in 1996, left her job in January 1997 in order to work full time handling the

[5] The docket reveals that the Debtors received a discharge on June 18, 2003.

investments. The Court found in Stevens and Yarnall, that neither of the Debtors had any type of education or training in financial management. Neither were licensed security brokers nor investment advisors.

Originally, the investment transactions were arranged through Mata which was an entity controlled by McCormick, and later through Ki-Digital, another entity of McCormick. In this case, Mr. Schroeder has admitted in paragraph 6 of the Debtors' Answer to being an "unregistered agent in the sale of promissory notes issued by Mata." In this regard, the Court notes that Plaintiff's Exhibit P-3B, the undated Introduction Letter, which acted as an investment solicitation, contains at the bottom, the photocopied business card of Mata Services, Inc. ("Wholesale Distribution & Marketing") with the name Bill Schroeder "Investment Manager" listed on the top left hand corner. The Court further notes the large handwritten notation "BILL 435-3441" at the top of the Introduction Letter under the Mata Services, Inc. letterhead.

Also as in Stevens and Yarnall, the Court finds that the number of people investing and the amounts of the transactions grew. The parties have stipulated to the fact that over time, the number of "factoring" deals offered to clients of the Schroeders increased in both the number of investors subscribing and the total dollar amount of notes issued. Mrs. Schroeder would collect money and turn it over to McCormick despite a lack of documentation. Neither of the Debtors ever asked to see documentation of any of the bank accounts or liquid assets of Mata Services or Ki-Digital. It is undisputed that neither of the Debtors ever viewed any financial statements, company books, bank documents, tax filings or other financial documents pertaining to Mata, Ki-Digital or any company affiliated with Mata, Ki-Digital or Charles McCormick.

The Schroeders kept records of all investments for all of their client noteholders, and assigned account numbers to each of their respective clients. After McCormick advised Mrs. Schroeder that the transaction was completed, she would give him a list of the investors who wanted their investment returned with interest. The others would "roll-over" their money to another transaction. The Court found in Stevens and in Yarnall that McCormick never returned all of the profits to the Schroeders, nor did the Schroeders return the profits to all of the investors. The Court has previously found that most investors chose to roll-over their investments, and that only a small percentage of the total number of investors requested their investment or interest returned to them. The history of Mr. Steiert's investments is set forth in detail below. The Court simply notes at this juncture that it is undisputed that the money invested by Mr. Steiert was never returned to him.

In or about May of 1997 the Schroeders incorporated and commenced the business entity known as "Macrophage, Inc." ("Macrophage") in order to handle some of the McCormick-related transactions. The Debtors had developed elaborate computer systems to keep account of the hundreds of investors and millions of dollars of funds they were handling.[6] After June 1997, factoring transactions for clients of the Schroeders were run through or "administered" by

[6] The Answers to Interrogatories supplied by the Debtors in the matter *sub judice* indicate that factoring transactions involving the Schroeders began in 1996 and ended in August 1998. Each transaction was for a period of approximately six (6) weeks. There were a total of five completed factoring transactions in 1996 with total investments of $5, 062,572 consisting of both "new" money and roll over funds. There were a total of eight completed factoring transactions in 1997 with total investments of $24,917, 882. The debtors indicate that the overwhelming majority of the funds in these transactions were roll overs and not new funds. There were a total of nine completed factoring transactions in 1998 prior to August 10, 1998, with total investments of $21,085, 795.

Macrophage such that investors were instructed to make checks payable to Macrophage, Inc. And repayments were made by Macrophage, in whose name the promissory notes were issued.

Significantly, as it relates to the matter *sub judice*, in addition to the Factoring Notes referenced above, the Court finds that in 1997 the debtors began collecting investments in Ki-Digital, a McCormick-owned company located at 15B Kresson Road, Cherry Hill, New Jersey which purportedly specialized in computer animated special effects for the motion picture industry. These investments were also reflected in the issuance of promissory notes which were to pay interest to investors at a rate of six percent per month (the "six percent notes"). These notes were issued directly to the various investor clients of the Schroeders, by Mata as obligor, beginning in June of 1997.

Specifically, the Schroeders contend that at the time of the initial six percent note offering in May and June 1997, the Schroeders provided their clients and interested investors with whatever information Charles McCormick instructed them to give. Mr. Schroeder has indicated that he sometimes saw a rough draft of newsletters given to him by Charles McCormick, prior to mailing the original, but that the Schroeders mailed or faxed or otherwise made available to most of their clients, every letter or other written communication that Charles McCormick asked them to make available for client distribution. The Court notes that in this proceeding, this alleged "relaying" of McCormick-generated information by the Schroeders forms a critical component of the Schroeders' section 523 defense.

B. The Civil Enforcement Action, and McCormick's Guilty Criminal Plea to Securities Fraud

Because of its relevance to the matter at hand, the Court further repeats its findings in Stevens and Yarnall that the Attorney General of New Jersey filed a civil enforcement action on behalf of the Chief of the State Bureau of Securities against Ki-Digital, Mata, and Charles McCormick ("the Civil Enforcement Action"). Exhibit D-6 is, inter alia, the June 19, 1998 Consent Order Appointing a Receiver, Robert G. Stevens Esquire, in the Civil Action (Docket No. C-158-98) which was pending in the Superior Court of New Jersey - Chancery Division - General Equity in the County of Essex, before the Honorable Benjamin Cohen.

It is undisputed that on or about March 30, 2000 the Debtors were found to have participated in the sale of unregistered securities in violation of N.J.S.A. 49:3-52(b) and N.J.S.A. 49:3-56(h) by Judge Cohen due to the omission of material facts in dealing with investors and not being properly registered to sell and issue securities. These findings were made despite the fact that during the period in question the Schroeders hired two CPA's Brian Lynn, and Joel Penn and later retained an attorney, David Rubin, Esquire, with respect to a lawsuit in a similar transaction. The Debtors strenuously argue that they had placed their reliance on the McCormick representations and were unaware that their actions violated state law. No criminal charges relating to these transactions were ever brought against the Defendants.

On October 19, 2000, Charles McCormick waived indictment and pled guilty to criminal charges arising from the issuance of the promissory notes including securities fraud. The Court has previously found that the Schroeders acted as agents in connection with the sale of at least 1,567 promissory notes as is further reflected in Exhibit D-6. In the Stevens and Yarnall cases,

the parties stipulated that the debtors realized an aggregate amount of $565,514 from the issuance of factoring notes and $171,281 from the issuance of six percent notes. The record reflects that not until September 1998 when McCormick failed to pay the money due on an outstanding note and the Schroeders were being questioned by State of New Jersey investigators, did they contact an attorney to represent them in the civil enforcement action.

C. The Steiert Investment(s)

Plaintiff Steiert indicates that his section 523 claims against the Debtors originated with the Schroeders' sale to him of the Factoring Notes in 1997. Specifically, it is undisputed that Plaintiff tendered to the Debtors a series of checks totaling $300,000 between June and December 1997, for which the Plaintiff was issued interest-bearing Factoring Notes, many if not most, promising payment of six percent interest per month. In addition, Mr. Steiert transferred his IRA retirement funds to PENSCO, a custodian to whom he was allegedly referred by defendants, so as to enable PENSCO to issue a check to Defendants in the amount of $57,150, for the purchase of a note issued by Mata.

So as to specifically understand the series of monetary transactions that flowed from the Plaintiff to the Defendants, the Court has examined in detail Exhibit P-2 which contains Mr. Steiert's Certification in Support of his Proof of Claim filed on November 23, 2001. Because of its significance to the matter herein, and because the Debtors dispute the total amount ultimately sought by Mr. Steiert with respect to this nondischargeability action, the Court repeats verbatim below, the relevant portions of the Steiert Certification:

Geoffrey L. Steiert, being of legal age and duly sworn according to law, does hereby depose and aver as follows:

1. I am a listed creditor of the Debtors. I make this Certification in support of the attached proof of claim, which is signed by me and submitted on my own behalf.

2. My claims against the Debtors are based on monies which I gave to the Debtors for the purchase of promissory notes issued by Mata Services Inc., a company of which the Debtors claimed to be agents and officers. I purchased a series of notes, not only for myself personally but also for two wholly owned corporations and for my I.R.A. Account. All of the checks were payable to the corporation and were delivered to the Debtors. The total principal dollar amount which I paid to the Debtors is $357,150, allocated as follows:

   Geoff Steiert $249,000.00

   Healing Touch, Inc. $ 45,000.00

   Franklin & McKinley, Inc. $ 6,000.00

   My self-directed I.R.A. account $ 57,150

   ("PENSCO Pension Services, Inc., Custodian FBO Geoffrey Steiert I.R.A. ST 152").

Exhibit P-2.

Mr. Steiert's proofs consist of copies of checks, promissory notes and correspondence substantiating that he invested $249,000 personally, $57,150 from his self-directed IRA held by PENSCO Pension Services, Inc., $47,000 from his wholly-owned corporation Healing Touch, Inc., and $6,000 from his wholly-owned corporation Franklin & McKinley, Inc.

Mr. Steiert also submitted for admission Exhibit P-15B which the Court took under advisement to consider the admissibility. After review, this Court determines that this exhibit, a

Joint Final Pre-trial Order between the Plaintiff herein and counsel for the Debtor-Defendants and other defendants, shall be admitted as it includes their stipulations relating to the same transactions as are the subject of this litigation and were agreed to by the same parties.

This exhibit in paragraph 12 admits the receipt of $300,000 by the Schroeders from Mr. Steiert. The other $57,150 came from his PENSCO pension account and is substantiated by a fax cover letter, and Note authorization form (Exhibit P-1C) and promissory note dated June 2, 1997 (Exhibit P-2).

Moreover, no credible evidence has been produced to dispute the amounts claimed by Mr. Steiert. The Debtors argue that the funds from the two wholly-owned corporations should not be included in Mr. Steiert's claim. However, Mr. Steiert was the one who transferred the funds to the Debtors on behalf of these entities and being the sole shareholder, the recovery of these monies would be on his behalf. Therefore, the Court finds that those sums may be included within his claim. The Debtors also ask that the claim be limited by the amount of "alleged" interest received. Because evidence as to the amount of such credit has not been produced, this Court is unable to consider such limitation. Therefore, this Court determines that Mr. Steiert's claim against the Debtors is fixed in the amount of $357,150.00. Although an additional $20,000 for costs is also claimed by Mr. Steiert, insufficient proof has been submitted to support this claim, nor has a legal basis for same been asserted.

As set forth in detail in his Amended Complaint, Mr. Steiert indicates that he was "induced" to invest his funds in the purchase of the Factoring Notes, by what he contends were repeated factual misrepresentations by the Debtors. Specifically, he contends that in 1996 and early 1997, the Debtors representing themselves to be authorized agents and employees of Mata,

solicited and sold to Mr. Steiert promissory notes for participation in the "factoring" of computer equipment.[7] The Plaintiff further alleges that in May and June 1997, Defendants continuing to represent themselves as authorized agents in the employ of Mata, solicited Plaintiff to purchase promissory notes issued by Mata which paid six percent per month and would entitle Plaintiff to an option to purchase stock. In allegedly soliciting the Plaintiff to purchase the six percent notes, the Debtors made numerous representations to Mr. Steiert that he alleges were intended to convince him that purchase of the notes was a "safe" investment and to allegedly "persuade" the Plaintiff to invest a high dollar amount.

The record in this matter reveals that the Plaintiff alleges that these representations included among other statements, claims that:

> a. Mata and its affiliates were fully capitalized and had funded all foreseeable equipment and expense needs;
>
> b. Mata's debt was fully protected by assets of much greater value; and
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> c. Mata maintained liquid cash reserves sufficient to repay all notes in full on demand.

(Amended Complaint filed January 11, 2002, ¶ 9.)

There is no dispute that as noted in his Certification, Exhibit P-2, after initial note purchases in June 1997 individually and through several corporate entities, Mr. Steiert invested

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[7] The Court notes that Exhibit D-6 contains Findings of Fact in the Superior Court Action (C-153-98) that specifically define factoring in this context as follows:

> Factoring has been described as consisting of financing, on a short term basis - - usually a number of weeks - - the sale by distributors or wholesalers of products - - principally computers - - to retailers or dealers, using funds gotten from selling promissory notes to investors.

an additional amount of $57,150, by way of his self-directed PENSCO IRA. Plaintiff asserts that after that time, the Debtors continued to reiterate the above stated factual representations to him with regard to the safety of the notes, with the alleged intention of again "persuading" Mr. Steiert to purchase more notes and to dissuade him from withdrawing any of his invested funds.

Between June 1997 and August 1998, the Defendants allegedly made numerous additional factual representations to Mr. Steiert on several occasions. Mr. Steiert advises that these representations included but were not limited to the following claims:

a. Mata, and its special effects division, Ki-Digital, Inc., were generating many millions of dollars in monthly revenues and profits; and

b. Maintaining investment in the notes was required in order to qualify for an upcoming private stock offering, which was imminent and would be extremely lucrative.

As further reflected in his Certification, Exhibit P-2, with what he contends was "reasonable and justifiable reliance" upon all of the above referenced representations by the Debtors, Mr. Steiert "rolled over" his investments and failed to demand payment of principal or interest on the notes. Mr. Steiert indicates that he has never received payment of any kind, on account of the investments.

In addition to the testimony elicited and exhibits entered during the course of the trial in this matter, Mr. Steiert's position has been set forth in a plethora of pleadings filed with this Court, including, a 52-page post-trial submission filed on August 5, 2003. In his submission, Mr. Steiert sets forth the detailed factual history of the alleged "solicitation" of his initial investment, as well as the subsequent "solicitation" of the investment in the six percent notes. In addition, this factual history includes allegations of false information relating to delays of an

alleged stock offering and related "roll-over" of his investment in the six percent notes. Moreover, detailed information is provided regarding the defendants alleged refusal to honor Mr. Steiert's ultimate request for payment.

With regard to the plaintiff's initial investment, the Court accepts Mr. Steiert testimony that he was initially informed about Mata investment opportunities in a "chance encounter" with an acquaintance, Dennis Taylor, who had invested in several notes issued by Mata. Mr. Taylor, who acknowledged that he did not know Mr. Steiert well until after they both became involved as investors with Mata, testified on April 14, 2003 that he answered an ad in the *Courier Post*, which led him to telephone Mr. Schroeder, in order to inquire about earning additional money. Mr. Taylor testified that Mr. Schroeder, in a phone call to him, and in a subsequent meeting at Mr. Schroeder's home office, proposed to hire Mr. Taylor as a commissioned sales agent to solicit individuals to purchase Mata promissory notes. He testified that he believed the information provided by Bill Schroeder as he had no reason not to believe it.

Mr. Steiert alleged that prior to investing, in at least two telephone conversations, he asked many questions of Bill Schroeder, which he indicated were based in large part on the factual claims set out in Exhibit P-3, the Mata Introduction Letter referenced earlier herein. At a follow-up meeting, the Plaintiff agreed to initially invest $2,500 in what defendants termed a "factoring note" which they represented to be a secured financing of a bulk sale of computer hardware, in which MATA acted as "middleman." [8] It is undisputed that after one "roll-over" of this initial investment, Plaintiff withdrew his money with MATA. The Schroeders then opened

[8] In this regard, the Court notes from its review of Exhibit P-3, the Introduction Letter, that it contains a handwritten notation on the top right hand corner, reflecting the $2,500 investment as "Acct. #351."

an account for the Plaintiff at their Stratford Office, where they testified that they maintained all the records of Mata investments made by their "subscribers."[9]

The thrust of Mr. Steiert's position is that he repeatedly "focused" on the safety of his invested funds and the Schroeders' "assurances of Mata's ability to repay the loan as promised," through his repeated requests for verification of the claims made in the Introduction Letter. In this regard, both Debtors testified that they relied primarily on the facts included in the Introduction Letter, in explaining Mata and answering questions from their subscribers and prospective investors. Specifically, the testimony of both Debtors was that all of their statements to clients and prospective clients reiterated or were consistent with the representations in Exhibit P-3B, and that they did not contradict any of the facts asserted therein.[10]

Mr. Steiert contends that by way of an example of his adopting a somewhat cautious approach to his investment strategy with the Schroeders, he did not attend a May 1997 "demonstration session" with regard to investment opportunities relating to the opening of a new division of Mata. Mr. Steiert testified that only after a series of detailed discussions with Mr. Schroeder was he persuaded to examine the offering documents. Again, Mr. Steiert contends that he engaged in "several substantial question and answer" sessions with Mr. Schroeder regarding the safety of the investment and the assured ability of the company to timely repay his promissory notes, supplemented once again by his confirming of the specific

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[9] Exhibit P-3B also includes the notation "Acct.#351 and P.O. Box 211 Stratford."

[10] The Court notes that Exhibit P-3B includes the following information/representations:

> We are proud members of the Better Business Bureau of South Jersey, Dunn & Bradstreet, The New Jersey Customer Assistance Program and The National Directory of America's Professionals and executives. We enjoy an A-1 track record in doing business.

details made in the offering documents.[11] This testimony was further supported by the testimony of Dennis Taylor who indicated that he was provided with information about what he described as "mind-boggling profits."

The Court finds that these "offering" documents consist of primarily four mailings from the Schroeders' Stratford Office to the Plaintiff, which were marked for the trial record as Exhibits P-4, subparts A through D. As they had with regard to the Introduction Letter used in soliciting clients to subscribe to the factoring offerings, the Debtors acknowledged that they never on any occasion contradicted or even qualified the claims asserted in the offering documents which were distributed to their subscribers between April 1997 and June 1998.

The Court finds compelling the fact that the record supports the finding that the primary individuals available for information or any other purpose on Mata's behalf were the Schroeders and not Charles McCormick. The record supports Plaintiff's assertion that Mr. Steiert never

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[11] Exhibit P-3, The Introduction Letter states:

> "The greatest and most important difference with our company compared to others who buy in bulk lots, is that we only purchase when we have locked-in buyers from whom we secure a deposit (usually about 20%) for the equipment they wish to acquire. We will then order and fill our customers with as many units that we can supply at our profitable mark-up (usually 15% to 30%). Investors are then secured to float the cost price of the equipment. This is known, in the banking business, as Factoring Commission Paper. Most of the transactions are completed within a 4 to 5 week period, at which time all original investments and profits are paid.
>
> You'll be informed by Fax or Phone every week to ten days of each offering that is secured by buyers so you may select, from the offering sheet, the product(s) you wish to fund by investment and the amount of that participation. You are not obligated to re-invest and can stop at any time. Obviously the greatest financial gain is realized when you roll-over the investment."

specifically asked about Charles McCormick. The record is replete with offering documents distributed to the Plaintiff by the Debtors advising the potential subscribers to contact only their "rep" at 435-3441 (the Debtors' phone number)[12] with any questions or to follow-up on any additional note purchases as opposed to any inference of potential investor contact with Charles McCormick. The Court further finds support in this record for the Plaintiff's contention that the subscribers regarded the Debtors' Stratford home as the "Stratford Office for Mata" and the Schroeders as the agents for the sale of notes.

The Court further specifically finds that the record further supports the fact that the six percent note offering was associated with the opportunity to reserve the option to participate in the future investment projects of Mata, and that the intended "vehicle" for this participation was stock ownership. The Court accepts the Plaintiff's contention that the May 1997 investor meeting was initially advertised as a "presentation" for ownership of stock in Mata's new division (Exhibit P-4A). Mr. Steiert strenuously contends that it was not until after the Debtors explained to Mr. Steiert that the stock offering was being postponed in order to allegedly prepare a prospectus and to comply with S.E.C. regulations, did the Plaintiff consider the resulting short term investments.[13] This information reinforced the contention of the Plaintiff that he trusted that his funds could not be risked in a new business venture, and that the funds could only be committed if, after viewing the prospectus, he agreed to buy stock.

In support of the above, the Court has examined in detail Plaintiff's Exhibit P-1E, a December 26, 1997 hand-written letter to the Schroeders from Mr. Steiert. It states as follows:

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[12] Exhibit P-3.

[13] The Court notes that the six percent notes have maturity dates of either three or six months.

Hi, Bill and Kathy,

Enclosed are my 2 checks for $200,000. As we discussed, you now have most of my savings - plus my PENSCO IRA.

I continue to rely, of course, on assurance that the company maintains enough liquid funds to repay ALL lenders upon demand.

I'll need to withdraw most of my monies by April, because of the Roth IRA threshold we talked about. Please remember: If there is a stock offering, I'd need at least 3 to 4 weeks to review the company's financials.

Thanks,

Geoff Steiert

Enc.: 2 checks to Ki-Digital:
$175, 000 Individual;
$25,000 Healing Touch

The Court further accepts Mr. Steiert's contention that the maturity dates of the six percent notes were repeatedly extended by "roll-overs" due to the alleged postponements of the promised stock offering. In this regard, Mr. Steiert contends that the original accrual date of the Plaintiff's six percent notes was the second of December 1997, six months after issuance. As evidence of the company's purported belief in the near term expectation for the proposed private stock offering (based on estimated time required to comply with SEC regulations and issuance of an approved prospectus),[14] the Plaintiff advises that the the date was extended one month, to the second of January 1998. When that brief extension was not enough, Mata issued new, three month notes, due April 2, 1998. That date was later extended to June 2, 1998.

The Plaintiff testified specifically that he felt compelled to maintain his investment in the six percent notes due to the fact that he was advised:

[14] See Exhibit P-5E, Ki-Digital Newsletter advising of SEC regulations and guidelines.

a.) That funds withdrawn could not be re-invested;

b.) The less invested in the six percent notes, the less stock would be made available;

c.) That the private stock offering was imminent; and that

d.) through "repeated boasts" of increasing company profits, to be reaped upon the exercise of the stock options.

(Exhibit, P-5, Mata correspondence and related newsletters).

It is undisputed that Plaintiff never asked for payment of principal or interest, for the ten months extending from June 2, 1997 through April 2, 1998. At that time however, Plaintiff asserts that he requested the return of his funds via telephone call to the Schroeders. In this regard, Plaintiff submits that the reasons for this decision to request a "payout' included the following:

a.) The original purpose of the six percent notes had been to reserve for a few months the option to participate in an imminent private stock offering, and the ten months had transpired;

b.) The plaintiff had forewarned the debtors that this plans to transfer his IRA to a new "Roth" IRA required that he limit his investment earnings to comply with the Roth laws; and that

c.) On April 2, 1998, Plaintiff emerged from the hospital with what he describes as permanent injuries of his cervical nerve roots and spinal cord that he suspected would be disabling.

(Steiert Post Trial Submission dated August 1, 2003, page 23).

The Court notes that the Defendants have consistently disputed this last point insofar as they have stated that investors could have obtained a return of funds at any time through early August of 1998 and that Mr. Steiert willingly agreed to continue to roll-over his six percent notes for a period of two months until June 2, 1998.

D. The Debtors' Position

The chief defense of the Defendants Bill and Kathy Schroeder essentially focuses on the first and fourth elements of a section 523(a)(2)(A) cause of action, arguing that the Plaintiff's objection to dischargeability should be denied as Defendants did not receive Plaintiff's funds, and that there was no justifiable reliance on the part of the Plaintiff. (Debtor's Post Trial submission dated June 26, 2003).

With regard to the former element, the Schroeders contend that the documents moved into evidence by Mr. Steiert show that all funds related to his investments in six percent notes, and which form the basis of his claims against the Debtors, were made payable to either Ki-Digital or Mata and deposited into Mata Services/Ki-Digital Accounts. That is, the Schroeders testified, that they had no access to these accounts. (Exhibit P-1B). The Schroeders argue that the Plaintiff has presented no evidence which would directly trace the funds he invested in his personal name or in the name of PENSCO Pension Services, for the benefit of Geoffrey Steiert, to those funds received by the Schroeders and deposited into their personal accounts. Based upon an anticipated commission of one percent per month from the time of the initial investment in June 1997 and January 1998, the Defendants allege a maximum total commission earned, but not shown to have been received by the Schroeders, as $16,865.00. Therefore, they argue that this amount would be the maximum judgment that Plaintiff should be entitled to if the Court should find in his favor.

As to the second element, the Schroeders contend that the Plaintiff has not proved by a preponderance of the evidence that he reasonably relied on the statements of the Defendants in making his decision to invest. Instead, they argue that testimonial and documentary evidence

produced at trial indicates that he in fact relied heavily on other sources. The position of the Debtors is that the Schroeders were "information relayers." In support of their position the Debtors contend that the Plaintiff would often contact Dennis Taylor and not Bill Schroeder, when he had a question about his investments. Additionally, the Schroeders argue that the Correspondence identified as Exhibits P-4 and P-5 cited earlier herein, indicate that the Plaintiff was aware of the existence of Charles McCormick and his statements cited within. As to Exhibit P-3, the Debtors argue that Mr. Steiert relied on the statements contained in this Exhibit, which he received from Dennis Taylor, but that he never contacted any of the references provided including Dunn and Bradstreet and the Better Business Bureau.

IV. DISCUSSION

The issues before the Court are first, whether the Debtors obtained money from the Plaintiff by false representations within the meaning of 11 U.S.C. § 523(a)(2)(A)[15]; and/or whether the discharge exception for fiduciary debts pursuant to 11 U.S.C. § 523(a)(4)[16] applies.

As to section 523(a)(2)(A), in order to prevail under this section, the creditor must show:

---

[15] 11 U.S.C. § 523(a)(2)(A) provides in relevant part:

> (A) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt
> (2) for money. . . , to the extent obtained by-
> (A) false pretenses, a false representation or actual fraud.

[16] 11 U.S.C. § 523(a)(4) provides in relevant part:

> (A) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt
>
> (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.

> (1) the debtor obtained money through a material misrepresentation;
>
> (2) the Debtor, at the time, knew the representation was false or made with gross recklessness as to its truth;
>
> (3) the debtor intended to deceive the creditor;
>
> (4) the creditor justifiably relied on the debtor's false representations; and
>
> (5) the creditor sustained a loss and damages as a proximate result of the debtor's material false representations. (Emphasis added)

In re Cohen, 191 BR 599, 604 (D.N.J. 1996)(citing In re Poskanzer, 143 B.R. 991, 999 (Bankr. D.N.J. 1992), affirmed 106 F.3d 52 (3rd Cir. 1997), affirmed 118 S.Ct. 1212 (1998); see also In re Trombadore, 201 B.R. 710, 713 (D.N.J. 1996).

The creditor bears the burden of proving each of the elements by a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279, 287, 288 (1991).

Based upon a thorough review of the record in this matter, including inter alia, the testimony of the parties, the exhibits submitted into evidence and the relevant case law, the Court finds for the reasons that follow that Plaintiff Geoffrey Steiert has in fact met his burden of proving the elements of his claim by the requisite preponderance of the evidence and that therefore the $357,150 debt as to the Schroeders is nondischargeable pursuant to 11 U.S.C. § 523(a)(2)(A). Having so found, the Court declines to undertake analysis of the elements of nondischargeability of a fiduciary debt pursuant to 11 U.S.C. § 523(a)(4).

A. Nondischargeability Pursuant to 11 U.S.C. § 523(a)(2)(A)

With respect to the first element of obtaining money or property by false representation, it has been recognized that most courts have held that it is not necessary that the property actually be gained for the direct benefit of the debtor. Even an indirect benefit to the debtor may constitute "obtaining property" within the meaning of section 523(a)(2)(A). Collier on Bankruptcy, § 523.08 [1][a] (citing Brady v. McAllister (In re Brady), 101 F.3d 1165 (6th Cir. 1996); Hssn#7 Limited Partnership v. Bilzerian (In re Bilzerian), 100 F.3d 886 (11th Cir. 1990)).

As applied to the facts herein, the Court rejects the threshold defense of the Debtors' counsel as set forth in its post trial submission of June 26, 2003, that Plaintiff's objection to dischargeability based on his investments in Mata, under 11 U.S.C. § 523(a)(2)(A) should be denied as Defendant Debtors "did not receive Plaintiff's funds." (Debtors' Post Trial Submission June 26, 2003, page 3).

The Court finds that based upon the totality of the record before it, there was, at a minimum, an indirect benefit to the Debtors stemming from the Steiert investments, as part of an overall investment scheme through which the Schroeders obtained hundreds of thousands of dollars in commissions. In this regard, the Court finds any argument based upon a lack of direct benefit to the Debtors stemming from these transactions, with respect to which Mata and Ki-Digital undeniably defaulted, is not enough to defeat the Plaintiff's 523(a)(2)(A) claim. By his own representations (Exhibit P-3), Mr. Schroeder was acting as an "Investment Manager" and later as a "Executive Marketing Director "of Mata. (Exhibit P-4). Both of these corporate entities obtained millions of investor dollars from which they and their "agents" gained. Exhibits D-15

and D-16, the 1099 Miscellaneous Income Statements of the Internal Revenue Service, indicate income from Mata to William Schroeder in 1996 of $79, 676.55 and in 1997 of $348, 363.20.

Moreover, Mr. Steiert delivered the funds to the Schroeders, as directed by them, and numerous documents submitted in evidence which direct all contact to the agents of Mata and Ki-Digital.[17] The Debtors received these funds and transmitted, deposited or transferred them. It was their determination as to what happened to the funds, not Mr. Steiert's. They received the funds for their own benefit, acquiring significant commissions on the receipt of these and other funds. The Court finds that whether or not they actually received a commission on each particular transaction is immaterial because they obtained the funds for their own financial benefit.

As to the second element of the section 523(a)(2)(A) claim, to except a debt from discharge, the false representations giving rise to the debt must have been knowingly and fraudulently made. Century 21 Balfour Real Estate (In re Menna), 16 F.3d 7 (1994). This Court has previously recognized that in this Circuit, reckless representations may in some cases be sufficient to except a debt from discharge. In re Cohn, 54 F3d 1108 (3rd Cir. 1995). A material fact is one touching upon the essence of the transaction. Collier, § 523.08[d]. It is basically undisputed herein, that a litany of factual representations too numerous to recount in detail but fully supported by the record, including inter alia, the offering documents and other pieces of correspondence distributed by the Schroeders to Mr. Steiert, ultimately proved to be false. Like the Bankruptcy Court in In re Wholly, 145 B.R. 830, 834 (Bankr. E.D. Va. 1991), this Court

[17] Exhibits P-3 and P-4.

finds that the statements and actions of the Debtors were "reckless and in conscious indifference to the consequences."

As in Stevens, and again in Yarnall, the Court finds that with respect to Mr. Steiert, the Schroeders had an obligation to satisfy themselves and the investors that they had made a reasonable investigation into the legitimacy of the enterprise regarding which they were collecting from the investing public, millions of dollars. The Court has found before and finds again here that the fact that they hired professionals who did not reveal these problems, is of little weight when balanced against the fact that they undertook this enterprise without training, education or license and had the potential to inflict devastating harm to investors and their pension funds. As to this last point, the Court particularly notes the postscript to Exhibit P-4D which states:

> PENSCO Pension Services, Inc. (San Francisco, CA) - Handles self-directed IRA's. Has unlimited transaction limit. For more information on this manner of investing, feel free to contact Bill Schroeder at (609) 435-3441.

Kathleen Schroeder testified on March 27, 2003 that neither she nor her husband Bill took any courses in financial management as she did not think any were necessary.

With respect to the element of intent, the debtors' defense is that they did not know that the representations were false when they passed them on to their clients and that they did not intend to deceive them. They assert here once again that they were misled by Charles McCormick just like the creditors of their estate. They point to the fact that some of the client/investors were sophisticated business people and argue that if they could be deceived, so could the Debtors. This Court has previously rejected this defense stating that the problem with it is that while the creditors only invested their own funds into a risky investment, the debtors

made a business of soliciting investors and collecting funds to invest in these entities, based on the false representations they were passing on to the public. It is uncontested that they earned hundreds of thousands of dollars based on these false representations. The losses they claim are merely the lost commissions they thought they would earn as part of the fraudulent McCormick scheme and the cost and expense of defending themselves in Court proceedings relating to their improper conduct. [18]

Moreover, the Debtors, without question, solicited individuals to invest substantial sums with them. Despite their knowledge that Mr. Steiert was investing his settlement proceeds and retirement income and knowing his seriously disabled condition, they never cautioned him or other investors as to the risks involved, never verified any information they passed on, and focusing on their own greed, solicited, assisted and perpetuated this fraudulent scheme. Therefore, based upon the voluminous record before it, that by failing to take the appropriate steps to register the securities and be licensed, and failing to adequately investigate exactly what they were soliciting for their clients to invest in, the debtors were "grossly reckless." This reckless indifference to the truth is also sufficient to find that they intended to deceive the creditors of Mata and Ki-Digital, and in this case, Mr. Steiert. In re Cohn, 191 B.R. 605 (determining that intent to deceive may be inferred from the totality of the circumstances which includes the debtor's reckless disregard of the truth.")

[18] The Court has reviewed Exhibit P-10, an August 23, 2001 letter from Bill and Kathy Schroeder regarding their lost investment. It provides an overview of the Schroeders' financial situation since 1997, including monies invested in MATA through Macrophage.

As to the fourth element of justifiable reliance, In Field v. Mans, 516 U.S. 59, 116 S.Ct. 437, 133 L.Ed. 351 (1995), the Supreme Court settled a conflict among courts of appeals about the level of reliance that must be demonstrated for a false representation to be nondischargeable.

> The Supreme Court held that the other party's reliance on the false representation must be "justifiable" under the circumstances. The inquiry will thus focus on whether the falsity of the representation was or should have been readily apparent to the individual to whom it was made. This is a less exacting standard than "reasonable" reliance, which would focus on whether reliance would have been reasonable to the hypothetical average person.

Collier, § 523.08[d].

Mr. Steiert testified that he believed the debtors and relied upon their representation which this Court finds to be justified. In support of this finding the Court looks to several circumstances.

First, the Court cites the various pieces of correspondence and corporate newsletters replete in this case, entered as exhibits, and cited herein, that direct and require investors to rely on their representative, in this case Mr. Schroeder, for information. These same documents also discourage independent inquiry by investors. In particular, the Court has examined Exhibit P-5E, the November 1997, Ki-Digital Corporate Newsletter, signed by Charles McCormick and issued by the Debtors to Mr. Steiert. It states in pertinent part:

> As a whole, our current set-up with investors has gone really well. Although I have stated in past newsletters that I would like phone calls and faxes from investors to be handled through our representatives, we still receive a few calls each week requesting information, progress, future plans, etc. We have set this investment format up in a way that will allow us to handle these types of questions in a more confined manner.
>
> Direct calls to the office end up passed to people who should be concentrating and completing their workload. This is what I

> consider "Non-Productive Time." Please use your rep as a liaison to us. I can not emphasize this enough.(Emphasis Added).

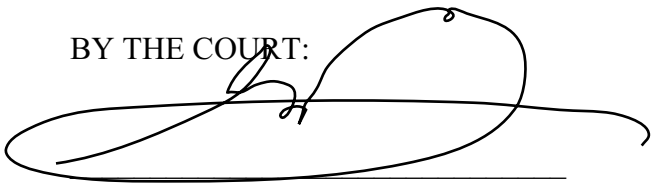
In sum, the record herein, (including both Exhibits and witness testimony), supports the finding that investors were primarily to talk to with the Debtors regarding any questions, and that the Schroeder's phone number and address were the ones provided.

Moreover, Mr. Steiert offered detailed testimony recounting his conversations with the Debtors regarding his financial needs and investment concerns, and correspondence to the Schroeders (Exhibit P-1E) supporting the Plaintiff's position that he relied upon false representations made by the Debtors, to his detriment.

V. CONCLUSION

For the reasons set forth herein, this Court finds that the Plaintiff Geoffrey Steiert has satisfied each of the elements of Section 523(a)(2)(A) by a preponderance of the evidence. A judgment shall be granted in his favor in the amount of $357,150.00 as a non-dischargeable debt.

BY THE COURT:



HONORABLE GLORIA M. BURNS
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW JERSEY

IN RE:	:	
WILLIAM R. SCHROEDER, JR. and KATHLEEN A. SCHROEDER,	:	CHAPTER 7
Debtors.	:	CASE NO. 01-14748 (GMB)
GEOFFREY L. STEIERT and PENSCO PENSION SERVICES, INC.,	:	ADVERSARY NO. 01-1273 (GMB)
Plaintiff,	:	
v.	:	CERTIFICATE OF SERVICE
WILLIAM R. SCHROEDER, JR. and KATHLEEN A. SCHROEDER,	:	
Defendants.	:	

I, Nicole A. Ramos, hereby certify that on this 31st day of March, 2006, I have caused a true and correct copy of the foregoing Memorandum Opinion and Order in the above-referenced adversary proceeding to be served on the following by placing same in the United States Mail, addressed as follows:

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/s/ Nicole A. Ramos
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Honorable Gloria M. Burns, U.S.B.J.