UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In the Matter of	:	
	:	Case No. 91-1599-D H
STEPHEN R. KRANTZ,	:	Chapter 7
	:	
Debtor.	:	
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A. Fred Berger, Chapter 7 Trustee on Behalf Of:	:	Adv. No. 92-92075
	:	
STEPHEN R. KRANTZ,	:	
	:	
Plaintiff,	:	
	:	
v.	:	
	:	
DARRELL LOAN AND BENTON AGGREGATES, LTD.,	:	
	:	
Defendants.	:	

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ORDER--COMPLAINT TO TURN OVER PROPERTY

A trial on the Plaintiff's Complaint to Turn Over Property was held January 12, 1993. Plaintiff, A. Fred Berger, Chapter 7 Trustee on behalf of Stephen R. Krantz, was represented by Gregory A. Epping. Defendants, Darrell Loan and Benton Aggregates, Ltd. (hereinafter "Loan") were represented by Steven K. Warbase. A briefing deadline was scheduled and the matter was taken under advisement. The parties have file post-trial briefs and the matter is now fully submitted.

The Court has jurisdiction of this matter pursuant to 28 U.S.C. § 157(c). Upon review of the briefs, pleadings, arguments and evidence presented, the Court now enters its

findings of fact and conclusions of law pursuant to Fed.R.Bankr.P. 7052.

FINDINGS OF FACT

1. On October 14, 1988, Steven Krantz entered into a business property lease with Benton County Savings Bank of Norway, Iowa. Krantz leased business property known as the Country Inn, Highway 30 West, Benton County, Iowa. The lease provided for a term of six months beginning November 1, 1988 and ending April 30, 1989 for $300 per month in advance. The lease contained an option to purchase the property during the term of the lease at a purchase price of $40,000.

2. In December 1988, Krantz learned that the property was subject to condemnation by the Iowa Department of Transportation. Subsequently, Krantz went to the Benton County Courthouse and discovered that the assessed value of the property was $67,000. Thereafter, Krantz attempted to obtain financing for the purchase of the property from the Norway Bank. However, the bank refused to loan the money to Krantz.

3. After the Bank refused to finance the purchase, Krantz met with Darrell Loan at his office to determine if Loan was interested in investing in the property. Krantz had become acquainted with Loan while managing the Cedar View Country Club in Cedar Rapids, Iowa and knew that Loan was familiar with condemnation procedures. Krantz met with Loan on

three different occasions in Loan's rural Cedar Rapids office. During these meetings Krantz and Loan entered into an oral agreement regarding the proceeds received as a result of the condemnation. This agreement was memorialized on April 27, 1989 when a contract for distribution, an assignment of purchase, a bill of sale, a promissory note, a warranty deed, and a transmittal document exercising option were executed by Steven R. Krantz and Benton Aggregates, Ltd., which was incorporated to purchase the Country Inn.

4. Essentially, the written agreement called for Krantz to assign the option in the real estate and to sell the business equipment to Loan. Thereafter, Loan would pay $40,000 to the bank for the property and $5,000 to a creditor who held a lien on the business equipment. Loan would take title to the real estate and equipment and lease it back to Krantz until the property was condemned. In return, Krantz signed a promissory note for $5,000 to the order of Darrell A. Loan of which payment was to be made in full upon the sale, condemnation of the Country Inn, or May 1, 1990, whichever came first. The agreement also provided that upon receipt of the condemnation proceeds Loan would be entitled to deduct sums advanced to purchase the real estate and equipment. Any proceeds remaining would then be split with 70 percent to Loan and 30 percent to Krantz.

5. Although a document titled "Bill of Sale" was

executed by the parties which purported to sell the business equipment for the sum of $10,000.00, this sum was never paid to Krantz. Despite this "Bill of Sale", the equipment was, apparently, intended by the parties to be collateral.

6. On May 10, 1989, Benton Aggregates, Ltd. leased the business property to Steve Krantz. The lease specified that the first day of the lease term was May 10, 1989 and the last day of the lease term would be November 30, 1989. The lease provided for rent to be paid at an amount of $300 per month in advance on the first day of each month. The amount of rent was not based on economic considerations related to the property, but was based on the amount of rent charged by the bank to Krantz under the prior lease agreement. At the time that the lease was signed, the first rent payment was not paid, nor was any required by Loan. An addendum was also executed on this date. The addendum contained a forfeiture provision in the event of an uncured default by Krantz. On occasion of such a default, the addendum provided that Krantz would forfeit all of his rights, including his rights to share in condemnation proceeds. The addendum also provided that Krantz was responsible for maintaining and insuring the property.

7. On May 11, 1989, Steve Krantz received a letter from Loan regarding relocation opportunities offered by the state following condemnation. The letter informed Krantz that these opportunities were conditioned upon Krantz not being in

default under the contract. At this time Krantz was already in default for not making the payment due on May 10, 1989.

8. In October of 1989, the Iowa Department of Transportation advised Krantz that they were ready to present an initial offer to purchase the property and would do so at a meeting on October 6, 1989. Krantz informed Loan of the meeting date and time. On October 6, 1989, the Iowa Department of Transportation made an offer to purchase this property to Benton Aggregates, Ltd. and Steven Krantz. Krantz was present at this meeting, however, Loan was not. Krantz signed the Iowa Department of Transportation papers at this meeting and was advised that the Iowa Department of Transportation would contact Loan for his signature. Krantz closed his business on that day and turned off the electricity.

9. On October 16, 1989, Krantz saw Loan at the Country Inn. Krantz was advised by Loan that he was closing the business and changing the locks on the building. Krantz protested because no notice of default had been given.

10. On October 17, 1989, a notice of default of leased business property was mailed to Steven Krantz by Benton Aggregates, Ltd. The notice alleged that there had been a failure to make rental payments in a total of $1,700. The notice also charged that there was a failure to pay utilities, and to maintain insurance, and that Krantz had closed the business. This notice provided that the lease would be

canceled and forfeited after the giving of the notice unless the defaults were remedied within a five-day period.

11. On February 26, 1990, a revised offer to purchase was made to Benton Aggregates, Ltd. and Steven Krantz for $79,400. This offer superseded the previous offer. Eventually, Loan received $78,000 from the condemnation award. Krantz received nothing.

12. On May 3, 1991, Krantz filed a voluntary petition for relief under Chapter 7, listing the action against Loan as an asset of the bankruptcy estate. The order of discharge was entered on August 27, 1991. This adversary proceeding was filed as an action for turnover of property based on fraudulent misrepresentation.

DISCUSSION

To prevail on a claim for fraudulent misrepresentation under Iowa law, the Plaintiff must prove the following elements by a preponderance of clear, satisfactory, and convincing evidence:

> 1) a false material representation; 2) made knowingly (scienter); 3) with the intent to deceive; 4) upon which plaintiff justifiably relied; and 5) which is the proximate cause of injury or damages.

American Family Service Corp. v. Michelfelder, 968 F.2d 667, 672

(8th Cir. 1992).

Loan and Krantz entered into an agreement drawn up by Loan's attorneys whereby Krantz would lose all rights to share in any condemnation proceeds upon a default of the lease. Krantz testified that Loan told him that the rental payment due under the lease agreement need not be paid until the proceeds from the condemnation were received. Loan denies this allegation.

Fraud must be proved by a preponderance of clear, satisfactory and convincing evidence. However, direct evidence of fraud is rarely obtainable and, therefore, usually must be proven by circumstantial evidence. Production Credit Association v. Shirley, 485 N.W.2d 469, 472 (Iowa 1992). The lease provided that the first rental payment was to be paid on the date on which it was executed. However, it is clear that no payment was made at this time. The evidence also shows that a letter was sent from Loan to Krantz the day after the lease was signed informing Krantz that his right of relocation was contingent upon not being in default. This letter fails to mention the fact that Krantz was already in default at this time for failure to make the first rental payment. In addition, although Krantz had never made a rental payment and had been in violation of the written terms of the lease since May 1989, Loan only notified Krantz of his default after an initial offer to purchase was made by the Iowa Department of Transportation in October, 1989. The Court finds that based on

this evidence, the testimony, and credibility of the respective parties, that Krantz has met the required standard of proof. Loan did, in fact, represent to Krantz that the rental payments need not be made until after receipt of the condemnation proceeds, thereby inducing Krantz to violate the terms of the lease.

Scienter and intent to deceive may be shown when the speaker has actual knowledge of the falsity of his representations or speaks in reckless disregard of the truth. Beeck v. Aquaslide 'N' Dive Corp., 350 N.W.2d 149, 155 (Iowa 1984). The Court finds that Loan knew at the time when he induced Krantz to delay rental payments that to do so was a default of the lease provisions. Loan's own attorneys drafted the document. The subsequent notification of default alleged nonpayment of rent as a cause for default. These actions show actual knowledge of the falsity of his misrepresentation and are evidence that Loan knowingly made the misrepresentation intending to deceive Krantz.

Krantz provided persuasive evidence to this Court that he acted in reliance on Loan's statement. However, Krantz must also show that this reliance was justified. Loan argues that Krantz's reliance was not reasonable in this case. Reasonableness of reliance is measured by a subjective standard. Sedco Int'l, S.A. v. Cory, 683 F.2d 1201, 1207 (8th Cir. 1982). In Sedco, the 8th Circuit found that the test for

justifiable reliance is "whether the complaining party, in view of his own information and intelligence, had a right to rely on the representations." Id. (quoting Lockard v. Carson, 287 N.W.2d 871, 878 (Iowa 1980)). In the case at hand, the lease agreement and the addendum clearly stated the rental terms and the consequences in the event of a default. Despite these documents, Loan did not require Krantz to pay the initial lease payments when the documents were signed and reassured him that they need not be paid until after the condemnation. Additionally, evidence shows that the letter on May 11, 1989 failed to mention the current default and Krantz did not receive notification of default until October. The Court, taking into consideration Krantz's information, Loan's actions, and the respective positions and business experience of the parties, finds that Krantz's reliance on Loan's representation was reasonable in these circumstances.

Krantz must next show that his reliance on Loan's representation proximately caused his damages. It is clear that Krantz suffered injury in that he failed to receive a portion of the condemnation proceeds as he bargained for. However, proximate cause is a more difficult question in this case as Loan argues that the failure to pay rent was not the only instance of default.

Loan alleges that Krantz failed to pay insurance premiums as required in the addendum to the lease. Krantz produced

sufficient evidence which showed that the property was, in fact, insured. Therefore, the Court finds that the allegation of failure to provide insurance on the property is entirely without merit.

Loan also contends that Krantz's nonpayment of utilities and failure to keep the business open were part of the default. Krantz closed the business and turned off the utilities on October 6, 1989, after he met with the Iowa Department of Transportation and signed papers regarding the real estate property. Loan was not liable for payment of utilities, nor was the closing of the business of any economic consequence to Loan as the parties had agreed that Krantz was to keep any relocation award from the condemnation of the property. The Court, therefore, finds that the misrepresentation regarding rental payments was the cause of the default and the proximate cause of the injury to Krantz.

Successful plaintiffs in fraudulent misrepresentation cases are generally entitled to benefit-of-the-bargain damages. Robinson v. Perpetual Services Corp., 412 N.W.2d 562 (Iowa 1987). Accordingly, Krantz is entitled to actual damages in the amount of $9390.00. This amount is equal to 30% of the total of the condemnation proceeds less the land purchase price, the equipment purchase price, and the back rent. Krantz also seeks punitive damages in this case. Punitive damages may be awarded in cases of fraud despite the fact that the fraud

grew out of representations made when the parties entered into contractual agreements. Steckelberg v. Randolph, 448 N.W.2d 458, 462 (Iowa 1989). Iowa Code § 668A.1 requires that in a trial for a claim involving a request for punitive or exemplary damages the court shall make findings as follows:

> 1.(a) whether, by a preponderance of clear, convincing and satisfactory evidence, the conduct of the defendant from which the claim arose constituted willful and wanton disregard for the rights or safety of another.
>
> (b) whether the conduct of the defendant was directed specifically at the claimant, or at the person from which the claimant's claim is derived.

The Court finds that the evidence shows by a preponderance of clear, convincing and satisfactory evidence that Loan's conduct constituted a willful and wanton disregard for the rights of Krantz. The conduct was deliberate, certain to cause Krantz injury, and directed specifically at Krantz. Accordingly, the Court orders punitive damages in the amount of $1,000.00.

Proceeds of this action are property of the estate pursuant to 11 U.S.C. § 541(a). Outside of exceptions irrelevant in this case, 11 U.S.C. § 542(a) provides that an entity in possession, custody, or control, during the case, of property the trustee may use sell, or lease under § 363, or that the debtor may exempt under § 522, shall deliver to the

trustee, and account for, such property or the value of such property. Therefore, the recovery is subject to turnover pursuant to 11 U.S.C. § 542(a).

ORDER

IT IS THEREFORE ORDERED that the Plaintiff is entitled to judgment against the Defendants in the amount of $9390.00 in actual damages and $1,000.00 in punitive damages.

IT IS FURTHER ORDERED that the Trustee is authorized to recover, for the benefit of the estate, the judgment ordered herein.

Dated this 23rd day of August, 1993.

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RUSSELL J. HILL
U.S. BANKRUPTCY JUDGE