

Decision was rendered prior to U.S. Supreme Court's adoption of a preponderance of the evidence standard for the burden of proof in dischargeability determinations. Grogan v. Garner, - U.S. -, 111 S.Ct.654,.112 L.Ed.2d 755 (1991).

UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In the Matter of :
JAY C. DACRE, : Case No. 87-770-C J
Debtor. :
MIDWEST GROCERS CREDIT UNION, Adv. Pro. No. 87-0129
f/k/a Super Valu Employees
Credit Union,
Plaintiff,
JAY C. DACRE, Chapter 7
Defendant

MEMORANDUM OF DECISION

On November 16, 1988, the complaint to determine dischargeability of debt filed by Midwest Grocers Credit Union (Midwest) came on for trial in Des Moines, Iowa. Steven C. Reed appeared on behalf of Midwest. Bryan R. Jennings appeared on behalf of the Chapter 7 debtor and defendant, Jay C. Dacre (Dacre).

This is a core proceeding pursuant to 28 U.S.C. section 157(b)(2)(I). Based on the record including the testimony of the two witnesses, the documents entered into evidence, the trial briefs and the oral arguments, the court makes the following findings of fact and conclusions of law pursuant to Bankruptcy Rule 7052.

FACTS

Dacre filed a petition for relief under Chapter 7 of the Bankruptcy Code on March 24, 1987. He is a former supervisor of inventory accounting at Super Valu. His financial relationship with Midwest began when he commenced working for Super Valu in 1969. Over the course of years, Dacre obtained various loans from Midwest for vehicles, farm related purposes and personal reasons.

A. July 27, 1983 Loan

On July 27, 1983, Dacre approached Bob Gould, the manager and chief financial officer of Midwest, and requested a loan of approximately \$4,000.00. At that time, Dacre had an outstanding loan balance of approximately \$8,700.00. He provided Gould the information needed to complete the loan application. However, Dacre omitted or falsified certain facts regarding his financial condition.

In addition to a 1956 Farmall tractor and a 1973 Chevy pickup, Dacre offered a nonexistent 1972 John Deere 4020 tractor as security for the loan. The phantom tractor also had been the object of a 1981 UCC filing. At times Dacre testified that he intended to use the July 27, 1983 loan proceeds to purchase the tractor; at other times he acknowledged that the UCC filing logically suggested that he represented to Midwest that he had already purchased a tractor. Parenthetically, it should be noted that Gould testified that he crossed out the 1975 John Deere combine

listed as security on the loan application because the debtor disclosed that he did not then own it but intended to purchase it in the future. Gould also testified that his secretary, who processed the application, noted the omission of any loan purpose and inserted "farm equip." at his direction. Read as a whole, Gould's testimony is inconclusive as to the purpose of the new money.

Dacre also failed to disclose to Gould debts he owed Brenton Bank and various credit card issuers. Gould testified that information regarding those additional debts very possibly could have made a difference in determining whether to grant Dacre the loan. Gould would have assessed the amount of money owed and Dacre's repayment structure.

The credit committee, of which Gould was a member, approved the loan application on the next day without any independent verification. That is, the committee did not obtain UCC searches for prior security interests, did not perform credit bureau or insurance checks and did not verify any of the information provided by Dacre.

Although Dacre may have obtained the loan to purchase farm equipment, he actually applied the proceeds to real estate contracts due to the declining farm economy. Dacre ultimately defaulted on the loan. As of November 16, 1988 the amount due under the July 27, 1983 loan totalled \$9,733.80.

B. January 17, 1984 Loan

On January 17, 1984, Dacre approached Gould at Midwest for a loan of \$7,000.00. Dacre again misrepresented his financial condition to Midwest.

First, Dacre offered a nonexistent 1975 John Deere combine as security. Dacre provided a false serial number for the UCC financing statement.¹ Dacre testified that he did not carry out his intent to purchase the combine because of the failing farm economy and his unemployment in March of 1984. Second, Dacre again failed to disclose his Brenton Bank debt and his credit card debts on the loan application. Third, Dacre misrepresented the assets he owned by listing an 80 acre farm valued at \$100,000.00, 44 head of cattle valued at \$20,000.00, a John Deere 4020 tractor valued at \$9,000.00 and a 1975 John Deere combine valued at \$10,000.00 on the back of the loan application. Thus, Dacre's financial condition was overstated by \$139,000.00. Gould testified that it would have been illegal for Midwest to grant the January 17, 1984 loan to Dacre if it had known that he was so overextended. Gould explained that state law governing credit unions limits the unsecured credit that may be extended to one person to \$7,500.00.

¹ The record does not clarify the discrepancy between the loan application (Exhibit 4), the extension agreement (Exhibit 6) and the UCC financing statement (Exhibit 11). That is, the first two documents indicate that a 1975 John Deere combine is in issue and the latter document refers to a 1974 John Deere combine. The confession of judgment (Exhibit 7) also refers to a 1974 John Deere combine.

Gould approved the \$7,000.00 loan on the spot. There was neither credit committee approval nor independent verification of the financial information Dacre provided. Dacre admitted that he continued to deceive Midwest about the John Deere 4020 tractor because he assumed that Midwest would not grant him another loan if it discovered that he had misapplied the July 27, 1983 loan proceeds.

The record as a whole is inconclusive as to the actual purpose of the loan. However, Dacre applied the loan proceeds to payments on real estate contracts. He eventually defaulted on the loan. As of November 11, 1988, the amount due under the January 17, 1984 note totalled \$9,900.68.

C. February 26, 1985 Loan Extensions

On February 26, 1985, Dacre applied for extensions of the 1983 and the 1984 loans. Dacre continued to misrepresent his financial condition. He failed to inform Midwest that he never owned the John Deere 4020 tractor and the 1975 John Deere combine listed as security on the extension agreements. Dacre admitted that he created a pattern of lying and concealment through February of 1985 because he assumed Midwest would reject his requests for extensions if it knew the truth.

Gould handled the matter for Midwest. He did not require new financial statements at that time. The extensions were approved on the same date in Gould's office. Dacre later defaulted on the extended loans.

Gould approached Dacre about the loan delinquencies in 1986. At that time Dacre admitted that he never owned the tractor or the combine. In November of 1986, Dacre signed a statement confessing judgment to Midwest in the amount of \$10,689.05 with interest at the rate of 15 1/2% per annum (July 1983 loan) and \$8,419.22 with interest at the rate of 14% per annum (January 1984 loan) in exchange for Midwest's forbearance from executing upon the delinquent notes. In the statement, Dacre admitted intentionally misrepresenting to Midwest that he owned or would buy a John Deere 4020 tractor and that the tractor would serve as security for the 1983 loan. He admitted making the same representation as to the combine and the 1984 loan.

Since Dacre's wife co-signed the July 27, 1983 loan application, she signed a confession of judgment as to that debt. She made payments on the confessed amount and credit has been given for the repossession and sale of the Farmall tractor. Dacre has made no voluntary payments pursuant to the confession of judgment.

DISCUSSION

At the outset, the court notes that the complaint, which was filed on June 30, 1987, contains six counts. The first count is based on 11 U.S.C. section 523(a)(2)(A) and refers to the July 27, 1983 loan and the February 26, 1985 extension. In that count, Midwest alleges in part that Dacre misrepresented that he owned a 1972 John Deere 4020

tractor which was to constitute collateral for the loan. The second count is based on 11 U.S.C. section 523(a)(2)(B) and refers to the July 27, 1983 loan only. Midwest claims in part that Dacre provided a financial statement that was materially false in that it left off certain debts he owed. In the third count, Midwest contends that it is entitled to recover on the July 27, 1983 loan under 11 U.S.C. section 523(a)(6) because Dacre allegedly wrongfully disposed of the 1972 tractor or the proceeds therefrom.

The fourth count of the complaint relies upon 11 U.S.C. section 523(a)(2)(A) and refers to the January 17, 1984 loan and the February 26, 1985 extension. In that count, Midwest contends that Dacre misrepresented that he intended to purchase the 1975 John Deere combine with the loan proceeds and that the combine would serve as security for that loan. Midwest further specifies that Dacre misrepresented that he owned the combine at the time of the extension. The fifth count is based on 11 U.S.C. section 523(a)(2)(B) and refers to the January 17, 1984 loan only. Midwest alleges that the statement Dacre provided was materially false in that it omitted some of his debts and set forth assets he in fact did not own. In the sixth count of the complaint, Midwest contends that it is entitled to recover on the January 17, 1984 loan based on 11 U.S.C. section 523(a)(6) insofar as Dacre allegedly wrongfully disposed of the John Deere combine.

In his August 7, 1987 answer, Dacre affirmatively alleges, among other things, that he had intended to purchase the tractor and the combine at the time he applied for the loans and that the creditor did not rely on such representations. He contends that the basis for the extension of credit was the established financial relationship between the parties over a number of years.

On May 13, 1988 Midwest filed a motion for summary judgment with respect to the first and fourth counts of the complaint. In support of the motion, Midwest submitted a statement of facts, the statement confessing judgment, the June 11, 1987 deposition of Dacre with deposition exhibits, the deemed admitted requests for admissions and the affidavit of Gould. Midwest also submitted a brief and memorandum of authorities. In his affidavit, Gould swears that the July 27, 1983 loan was made to the Dacres in reliance that a security interest would be granted to Midwest in a 1972 John Deere 4020 tractor. He further states that Midwest relied upon Dacre's representation of ownership of the tractor at the time of the February 26, 1985 extension. With respect to the January 17, 1987 loan, Gould attests that he relied upon Dacre's representation of ownership of the tractor and Dacre's offer of the John Deere combine as security for the loan. He further states that the loan was extended on February 26, 1985 in reliance upon Dacre's representation that he owned the John Deere combine.

On June 13, 1988, Dacre filed a resistance to the motion for summary judgment. In his supporting affidavit, Dacre swears that he obtained the July 27, 1983 loan with the intention of purchasing the 1972 John Deere 4020 tractor. He further states that after he received the proceeds, he determined that they would be better used on other financial obligations. He attests that Midwest's personnel never indicated to him that the loan applications had to be totally accurate. With respect to the January 17, 1984 loan, he swears that it was his intent to purchase the John Deere combine at the time he sought the loan. Again, after receiving the proceeds he determined that the money would be better applied to other financial obligations. He acknowledges that the representation that he owned the John Deere tractor as of January 17, 1984 was intentional to avoid revealing that he had not yet purchased the tractor. He generally contended that he was not aware and doubted that Midwest ever verified the financial information he provided.

On August 18, 1988 this court entered its order on the motion for summary judgment. It indicated that the following facts were undisputed:

According to the debtor's affidavit, he applied for a \$4,000.00 loan from the Credit Union on July 27, 1983. On that same date, debtor stated to Robert L. Gould, an officer of Credit Union, that his purpose in obtaining the loan was to purchase a 1972 John Deere 4020 tractor. Credit Union loaned the money. Mr. Gould

states in an affidavit that Credit Union made the loan in reliance that debtor would grant Credit Union a security interest in the tractor. Debtor never used the loan proceeds to purchase the tractor. Instead, he applied the money to farm payments. In a statement confessing judgment filed in a state court collection action brought by Credit Union, debtor stated that he "intentionally misrepresented to [Credit Union] he owned or would buy [the tractor] at the time of such loan, for the purpose of procuring such loan."

On January 17, 1984 debtor applied for another loan at Credit Union, this time requesting \$7,000.00. Mr. Gould again handled the loan. Debtor told Mr. Gould he needed the money to purchase a John Deere combine. Debtor further stated that the combine and the John Deere tractor would serve as security for the loan. In his affidavit, Mr. Gould states that this loan was made in reliance upon debtor's representations. Debtor did not use the loan proceeds to purchase the combine. As with the tractor loan, debtor used the proceeds to pay other creditors. In the statement confessing judgment, debtor admitted that to obtain the loan he intentionally misrepresented to Credit Union that he would purchase the combine.

After discussing summary judgment standards, this court set forth the Code section in issue and the applicable case law interpretation:

Section 523(a)(2)(A) provides as follows:

(a) A discharge under section 727... of this title does not discharge an individual debtor from any debt--

....

(2) for money, property, services, or an extension, renewal, or

refinancing of credit, to the extent obtained by--

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

Id. This provision concerns acts or statements, even those made orally, but excludes oral statements regarding a debtor's financial condition. See In re Roberts, 54 B.R. 765, 770 (Bankr. N.D. Iowa 1985). Credit Union's motion for summary judgment does not concern oral statements regarding the debtor's financial condition.

For a debt to be nondischargeable under section 523(a)(2)(A), the plaintiff must prove that: (1) the debtor made false representations; (2) at the time the representations were made the debtor knew they were false; (3) the debtor made the representations with the intent to deceive the creditor; (4) the creditor relied upon such representations; and (5) the creditor sustained the alleged loss and damages as a proximate result of the false representation. In re Bonefas, 41 B.R. 74, 78 (Bankr. N.D. Iowa 1984), citing In re Houtman, 568 F.2d 651, 655 (9th Cir. 1979). To prevail on a section 523(a)(2)(A) complaint, the plaintiff has the burden of proving each of these elements by clear and convincing evidence. Bonefas, 41 B.R. at 78.

Based upon the record before it and the applicable law, this court denied the motion for summary judgment insofar as it determined that genuine issues of fact did exist as to the first three elements set forth above:

The debtor has submitted an affidavit in
which he states that when he obtained

the loans he intended to purchase the machinery. He further states that it was only after he received each loan that he decided the money could be better spent on other obligations. These statements touch on whether he made false representations, whether he knew they were false at the time they were made, and whether he made the representations with the intent to deceive. The court recognizes that these statements are inconsistent with debtor's statements contained in the confession of judgment. However, giving debtor the benefit of all reasonable inferences made from his affidavit and the record as a whole, the court cannot conclude granting the motion for summary judgment is appropriate. (Emphasis in the original.)

At the outset of the afternoon trial on Midwest's complaint, the court noted that it had previously ruled on the reliance and proximate cause issues with respect to paragraph (A) of section 523(a)(2) and, therefore, would be considering only whether Dacre made false representations, whether Dacre knew the representations were false when made and whether Dacre made the representations with the intent to deceive Midwest.² Neither party questioned the court's

2

At the time of the hearing on the motion for summary judgment, Midwest supported its position with respect to the reliance issue by means of Gould's affidavit. In resisting the motion, Dacre merely speculated that Midwest actually and primarily relied upon the long standing credit relationship between the parties.

Parenthetically, it is noted that Midwest's position was further bolstered by Gould's trial testimony regarding the UCC filings for both the tractor and the combine. Unlike the situation in the companion case tried and decided in the morning of November 16, 1987, Midwest's effort to perfect what it thought were security interests is evidence, under these facts, of its reliance upon the misrepresentations.

characterization of the issues under consideration with respect to the first and fourth counts of the complaint.

Additionally, at the close of the hearing, counsel for Midwest asked the court to take notice of the request for admissions which stood admitted by operation of Bankruptcy Rule 7036. No objections to Midwest's counsel's request were made. By failing to respond to the March 31, 1988 request for admissions, Dacre admitted that: he furnished the information for the financial statements; he intentionally failed to furnish information regarding all his debts; he knew that Midwest would reasonably rely on the information in the financial statements; he intentionally and knowingly misrepresented that he owned the tractor; he intentionally and knowingly misrepresented that he owned the combine; the financial statements materially misrepresented his financial condition; he was in default or not current in payment with respect to the July 27, 1983 loan when he requested an extension; he was in default or not current in payment with respect to the January 17, 1984 loan when he requested an extension; and Midwest reasonably relied upon the financial statement.³

Finally, on the date of the trial, Dacre filed a corrected affidavit in resistance to the motion for summary

³ Although the court questions the weight that can be given an admission by one party regarding reliance by another party, the reliance question was disposed of by the order on the motion for summary judgment--at least with regard to the section 523(a)(2)(A) issue.

judgment. The corrected affidavit states:

I, Jay C. Dacre, the Defendant herein, first being duly sworn on oath, do depose that I made an Affidavit herein that was filed June 13, 1988; in preparing for trial and reviewing other financial documents I have determined that some statements contained in said Affidavit were in error, I hereby correct those statements as follows:

1. As to the 7/27/83 Loan Application the purpose of obtaining the loan was not to purchase a 4020 Tractor. I had represented to the credit union on a prior occasion that I desired to purchase that Tractor. Listing said Tractor on the 7/27/83 loan application was intentional to avoid advising the Plaintiff that I still had not purchased said Tractor. Said Tractor had been listed as security by the Plaintiff on loans dated 2/13/81 and 4/30/82. The stated purpose of the 7/27/83 loan was listed as farm equipment not any specific item.

2. As to the 1/17/84 loan application the purpose of the loan was listed as "downpayment". I do not now specifically recall what the "downpayment" was to be on. I listed the 1975 John Deere Combine on that application to avoid disclosing to the Plaintiff that I did not own a combine as I recall having previously represented to Plaintiff that I did so own.

3. To the extent that my previous affidavit is at variance with the foregoing I amend and correct said affidavit.

Due to the procedural posture of the case, Midwest now clearly prevails. The three elements in issue with respect to the section 523(a)(2)(A) cause of action regarding both loans and extensions have been established. That is, Dacre

misrepresented to Midwest that he owned the tractor on July 27, 1983 and the John Deere combine on January 17, 1984. Dacre admitted that at the time he made such representations he knew they were false. Dacre admitted that he intended to deceive Midwest--to avoid disclosing that he had not purchased such items earlier. When he was in default on both loans and requested extensions on both loans, he knowingly continued the misrepresentation of ownership so that Midwest would grant him the extensions. Accordingly, the amount due and owing on both notes as extended is nondischargeable pursuant to 11 U.S.C. section 523(a)(2)(A).⁴

Having disposed of the case under section 523(a)(2)(A), it is not necessary for the court to analyze the record under section 523(a)(2)(B)⁵ or under section 523(a)(6).

⁴ In light of the record viewed as a whole, Dacre fails to persuade the court that only \$4,000.00 of the amount loaned in 1983 should be in issue. Clearly Midwest was considering both the total loan amount and the security interest in the tractor when it approved the loan in 1983 and when it extended the loan in 1985.

⁵ Much of the questioning of Gould focused upon whether Midwest's reliance was actual and reasonable. Had Midwest not prevailed on the section 523(a)(2)(A) cause of action, the court would have analyzed reliance under section 523(a)(2)(B). However, it might have been impossible for Midwest to establish reasonable reliance upon the financial statement. That is, the court did not find that there was a factual issue with regard to reliance and proximate cause in ruling upon the motion for summary judgment. Based on Gould's affidavit, the actual reliance was upon the existence or purchase of the tractor and the combine which, in turn, would serve as collateral for the loans. Moreover, the careless lending practices, over which the court expressed concern in the companion case, would have made Midwest's burden under paragraph (B) difficult.

As a final matter, the court addresses the request for attorney fees made by Midwest's counsel at the close of the hearing and in its post-trial brief. Bankruptcy Rule 7056 incorporates Federal Rule 56 of Civil Procedure. Paragraph (g) of that Rule provides:

Affidavits Made in Bad Faith.

Should it appear to the satisfaction of the court at any time that any of the affidavits presented pursuant to this rule are presented in bad faith or solely for the purpose of delay, the court shall forthwith order the party employing them to pay to the other party the amount of the reasonable expenses which the filing of the affidavits caused him to incur, including reasonable attorney's fees, and any offending party or attorney may be adjudged guilty of contempt.

In light of what the court views as a very garbled record attributable to both witnesses and to the less than model paperwork of Midwest, the court does not find that Dacre's first affidavit was presented in bad faith or solely for the purpose of delay. The request for relief under Rule 7056(g) will be denied.

CONCLUSIONS

WHEREFORE based on the foregoing analysis, the court finds with respect to the July 27, 1983 loan and the January 17, 1984 loan and the February 26, 1985 extensions that:

1. Dacre made false representations with regard to ownership of the John Deere 4020 tractor and the John Deere combine;
2. At the time Dacre made the representations he

knew they were false;

3. Dacre made the representations with the intent to deceive Midwest;

4. Midwest relied upon Dacre's representations; and

5. Midwest sustained the alleged losses as a proximate result of the false representation.

Additionally, the court finds that Dacre's first affidavit in resistance to the motion for summary judgment was not made in bad faith nor filed solely for the purpose of delay.

Order and judgment shall enter accordingly.

Signed and filed this 6th day of February, 1989.

LEE M. JACKWIG

CHIEF U.S. BANKRUPTCY JUDGE