

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF UTAH

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~~UNPUBLISHED~~

In re)
)
DANIEL V. GREENWELL and) Bankruptcy Case No. 84C-02648
DIANE B. GREENWELL,)
)
Debtors.)
)
KAREN P. GREENWELL,) Civil Proceeding No. 85PC-0011
)
Plaintiff,)
)
vs.)
)
DANIEL V. GREENWELL,)
) FINDINGS OF FACT AND CONCLUSIONS
Defendant.) OF LAW

Appearances: Robert A. Echard, Gridley, Echard & Ward, Ogden, Utah, for plaintiff; Frank M. Wells, Ogden, Utah, for debtor/defendant.

BACKGROUND

This adversary proceeding came before the Court for trial on July 11 and 12, 1985 on plaintiff's complaint to determine the dischargeability of a debt pursuant to 11 U.S.C. § 523(a)(2)(A). On September 28, 1984, defendant filed a petition for voluntary relief under Chapter 7 of the Bankruptcy Code. Plaintiff commenced this adversary proceeding on January 7, 1985, alleging fraud by defendant with respect to representations concerning his personal financial condition and the financial condition of two

convenience stores in connection with the parties' divorce proceedings.

The Court, having heard the testimony and observed the candor and demeanor of the witnesses, examined all exhibits received in evidence, and considered the representations, arguments and briefs of counsel, makes the following Findings of Fact and Conclusions of Law as required by Bankruptcy Rule 7052.

FINDINGS OF FACT

1. During the course of their marriage, plaintiff and defendant borrowed money from the Bank of Utah for the purpose of financing two convenience stores. The first loan in the amount of \$35,000.00 was made on March 7, 1979, and was secured by a second mortgage on the parties' residence. A second loan in the amount of \$60,000.00 was made on December 12, 1980, and was secured by a third mortgage on the parties' residence.

2. The first store was located in Washington Terrace, Utah, and the second store was located in Ogden, Utah. Both were operated under the name "Town and Country Market."

3. At the time of the second loan, plaintiff was convalescing from hospital confinement and was taking medication, including muscle relaxers and tranquilizers.

4. Plaintiff hesitated to sign the loan documents for the second loan, but agreed to do so based upon defendant's

representations that the first store was unprofitable due to the small inventory, which precluded him from obtaining large discounts from wholesale suppliers, and that the second store would increase defendant's buying power, thus enabling him to purchase inventory at competitive prices.

5. On October 30, 1981, defendant moved from the marital residence, and approximately one month later commenced divorce proceedings in the Second Judicial District Court in Weber County, Utah.

6. During the pendency of the divorce proceedings, plaintiff brought an order to show cause, seeking to participate in the operation and management of the stores to ensure that sufficient income was generated by them to pay the indebtedness to the Bank of Utah on the second and third mortgages.

7. At that time defendant represented to plaintiff and her attorney that payments on the loans were current and that the stores were profitable.

8. Bank records introduced at the trial of this non-dischargeability proceeding show that no payments were made on the second and/or third mortgages from April 16, 1981 through April 27, 1982.

9. Relying upon defendant's false representations concerning the status of the loans and the financial condition of the stores, plaintiff dismissed her order to show cause and did

not seek to participate in the management and operation of the businesses.

10. During the pendency of the divorce action, defendant borrowed an additional \$44,000.00 from the Bank of Utah, secured by fixtures and accounts receivable.

11. Neither plaintiff nor her attorney were informed of the additional indebtedness incurred by defendant during the pendency of the divorce proceedings when negotiations were being conducted relative to the parties' property settlement agreement.

12. A property settlement agreement was negotiated and a decree of divorce incorporating the terms of the agreement was entered by the Second Judicial District Court on March 31, 1982.

13. Pursuant to the decree of divorce, plaintiff was awarded the marital residence and defendant was ordered to pay off the second and third mortgages thereon within five years. Defendant was further ordered to immediately inform plaintiff if the loans became delinquent or if any action was taken by Bank of Utah to foreclose the mortgages.

14. The decree of divorce reserved to plaintiff the right to petition the state court for such further orders as might be necessary to protect her interest in the marital residence if it was placed in jeopardy by defendant's actions.

15. Shortly after entry of the divorce decree, plaintiff began receiving calls from creditors of the stores who informed

her that they were not being paid for groceries, supplies or gasoline.

16. On May 29, 1982, plaintiff brought an order to show cause in the Second Judicial District Court, seeking to gain control of the stores in order to protect her interest in the marital residence.

17. Based upon the representations of defendant and of James K. Packer, Senior Vice President of the Bank of Utah, that the loans were current, plaintiff dismissed her order to show cause.

18. On September 17, 1982, Mr. Packer wrote defendant's attorney informing him that the second and third mortgages were seriously delinquent.

19. On October 29, 1982, in response to an order to show cause hearing commenced by plaintiff, Mr. Packer again wrote defendant's attorney and in his letter indicated that both loans were current and that all of defendant's accounts were being handled in a satisfactory manner. Based upon Mr. Packer's letter and the further representations of defendant that the loans were current, plaintiff dismissed the order to show cause proceeding.

20. The representations contained in Mr. Packer's letter of October 29, 1982 were false as to defendant's true financial status and that of the stores.

21. Upon learning that the loan payments had been delinquent on a number of occasions and that defendant had failed to inform her of the delinquencies, plaintiff brought another order to show cause on September 2, 1983, again seeking to gain control of the stores.

22. A hearing on the order to show cause was held on January 17, 1984, at which defendant testified that the loans were current, that the businesses were profitable and that the stores had made a profit during the preceding year. Each of these statements was false and known by defendant to be false at the time they were made.

23. At the January 17, 1984 hearing, Mr. Packer testified that defendant's relationship with the bank was satisfactory and that the loans were current. Based upon the bank records, these representations were also false.

24. Defendant borrowed additional sums from the Bank of Utah between March 22, 1982 and January 17, 1984, to keep the stores operating: On March 26, 1982, for \$4,000.00; on May 24, 1982, for \$10,000.00; on November 29, 1982, for \$8,291.86; on January 21, 1983, for \$5,000.00; on March 22, 1983, for \$85,000.00; on May 11, 1983, for \$13,000.00; and on June 20, 1983, for \$4,500.00. All of these loans were secured by the store fixtures and accounts receivable. At no time was plaintiff informed of these additional loans.

25. Defendant also borrowed \$56,000.00 from First Security Bank and \$28,000.00 from Moore Financial. Both notes were secured by the stores' equipment. Plaintiff was not informed of these additional obligations, which further eroded whatever equity was available through the businesses to apply toward the second and third mortgages.

26. In July 1984, defendant sold one of the convenience stores and allowed the bank to foreclose on the other store. From the sale of the first store, defendant received \$45,000.00 in cash, and a promissory note in the amount of \$25,000.00, payable over five years.

27. Defendant used all of the sale proceeds to retire his personal and unsecured business debts; none of the proceeds were applied to the loans secured by the second and third mortgages on plaintiff's home.

28. Defendant did not notify the plaintiff of the sale of the first store nor of his disbursement of the proceeds he received.

29. When it liquidated the inventory of the second store, the Bank of Utah received \$1,000.00.

30. On September 5, 1984, the Bank of Utah commenced foreclosure proceedings on the second and third mortgages against plaintiff's home, alleging that principal, interest, costs and

attorney's fees were \$26,966.52 and \$63,178.58 for the second and third mortgages, respectively.

31. As a result of this bankruptcy proceeding, the Bank of Utah has been stayed from foreclosing on its interest in plaintiff's home.

DISCUSSION

I. Did the Defendant Defraud Plaintiff Such as to Render His Debt to Plaintiff Nondischargeable?

Section 523(a)(2)(A) excepts from discharge debts for obtaining money, property, services, or an extension or renewal of credit by false pretenses, a false representation, or actual fraud. The five elements of nondischargeable fraud under § 523(a)(2)(A) are: (1) the debtor made the representations; (2) at the time, the debtor knew the representations to be false; (3) the debtor made the representations with the intent of deceiving the creditor; (4) the creditor reasonably relied on such representations; and (5) the creditor sustained the alleged loss and damage as the proximate result of the representations having been made. See Hatch v. Mason (In re Mason), slip op. No. C82-0440W (D. Utah Aug. 16, 1983) (per Winder, J.); In re Hames, 53 B.R. 868, 871 (Bkrtcy. D. Minn. 1985); Matter of Carpenter, 53 B.R. 724, 729, 13 C.B.C.2d 1158 (Bkrtcy. N.D. Ga.); In re Self, 51 B.R. 686, 690 (Bkrtcy. N.D. Miss. 1985); In re Santore, 51

B.R. 122, 123-24 (Bkrtcy. D. Mass. 1983); In re Schnore, 13 B.R. 249 (Bkrtcy. W.D. Wis. 1981).

A creditor who seeks to have a debt excepted from discharge under Section 523(a)(2)(A) must prove each of these elements by clear and convincing evidence. Hatch v. Mason, at 8.

Plaintiff alleges that defendant made fraudulent representations on three separate occasions between 1981 and 1984. Each instance is discussed below.

A. EXECUTION OF THE THIRD MORTGAGE

Plaintiff has shown that defendant made certain representations to plaintiff to induce her to sign loan documents secured by a third mortgage on the marital residence at a time when she was convalescing from hospital confinement and was taking medication. The evidence does not support a finding that such representations were false or that defendant made those representations with the intent to deceive plaintiff.

B. DIVORCE PROPERTY SETTLEMENT AGREEMENT

Plaintiff contends that her claim is nondischargeable under Section 523(a)(2)(A) because defendant's representations at the time of the divorce property settlement negotiations were fraudulent. The evidence presented supports this contention.

During those negotiations, defendant told plaintiff and her attorney that both stores were profitable and would generate

sufficient income to retire the home mortgages within five years. The evidence presented clearly shows that the stores were not profitable at that time. Bank records indicate defendant was incurring substantial debt in the form of additional loans to meet operating expenses.

Having personally borrowed the additional funds, defendant knew his representations to plaintiff were false. Defendant knew the significance of the misrepresentations and intended to dissuade plaintiff from taking any action to secure her interest in the stores.

Plaintiff reasonably relied on defendant's representations and negotiated the property settlement agreement. At the time of the negotiations the stores apparently had a going concern value. By the time plaintiff learned of defendant's misrepresentations, the stores had been sold or liquidated and nothing was left to apply toward the home mortgages. A proximate result of defendant's misrepresentations was the diminution in value of plaintiff's interest in the stores.

C. POST-DIVORCE PROCEEDINGS

Plaintiff next alleges that defendant intentionally misrepresented the financial condition of the stores in testimony at an order to show cause hearing on January 17, 1984. This is fully borne out from the evidence.

At that hearing, defendant testified that the stores were doing well and that it was unnecessary for plaintiff to be given control of the stores to protect her interests. Defendant's testimony was corroborated by testimony from James K. Packer of Bank of Utah, who also testified that the loans were current and that defendant had a satisfactory relationship with the Bank of Utah.

From testimony at the trial and the bank records admitted into evidence, it is clear that both of these representations were false. It is also clear that defendant intentionally represented to plaintiff that the stores were doing well so that plaintiff would not exercise her rights under the divorce decree to gain control of the stores. These intentional misrepresentations stalled plaintiff's actions and allowed defendant time to secretly sell and liquidate the assets of the business without her knowledge.

Based upon defendant's testimony and the declaration of Mr. Packer regarding the financial status of the stores, the Court finds that plaintiff's reliance was reasonable under the circumstances and that a proximate result of defendant's fraudulent misrepresentations was the diminution in value of plaintiff's interest in the stores.

II. Damages.

Another element of proof which must be established under Section 523(a)(2)(A) is evidence that loss or damage was the proximate result of the debtor's representations. Matter of Eaton, 41 B.R. 800, 803, 11 C.B.C.2d 292 (Bkrctcy. E.D. Wis. 1984). In this case, plaintiff has shown that the debtor's representations in the divorce proceeding amounted to a fraud against her and against the state court. Plaintiff has also shown that she was prevented by the debtor's fraud from exercising her remedies under the divorce decree. But she has failed to establish the fifth element -- that she sustained loss or damages as proximate result of the false representations.

Although the evidence shows that, but for the representations of the debtor, she might have obtained an order from the state court authorizing her to participate in the management of the convenience stores, there was no evidence that she could have operated them profitably or that they could have been liquidated for enough money to satisfy the secured and unsecured business debts and pay off the second and third mortgages on her home. In fact, the only evidence presented which was even remotely related to this point was testimony as to the \$70,000.00 sale price of one store in July 1984 --approximately six months after the debtor's false testimony at the order to show cause hearing. Thus, in the absence of sufficient proof that

plaintiff's damages are the proximate result of the debtor's deceit, this Court reluctantly concludes that plaintiff is not entitled to judgment under Section 523(a)(2)(A).

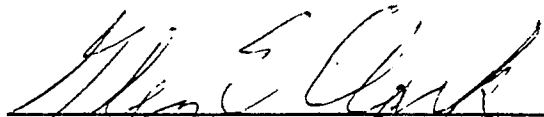
CONCLUSION

Having carefully considered the testimony of the witnesses and the arguments of counsel, and having examined the exhibits and applicable law, this Court concludes that the plaintiff has failed to establish an essential element of her claim for nondischargeability under Section 523(a)(2)(A), the element of damages. Plaintiff is not, therefore, entitled to judgment under Section 523(a)(2)(A).

Counsel for defendant will prepare and submit an appropriate order and judgment under Local Rule 13.

DATED this 28 day of July, 1986.

BY THE COURT:



GLEN E. CLARK
UNITED STATES BANKRUPTCY JUDGE