Appeal History:

remanded, No. C90-3011 (N.D. Iowa, September 10, 1990)
Bankruptcy decision after remand (December 10, 1990)

In the United States Bankruptcy Court

for the Northern District of Iowa

ROBERT L. WENTZEL *Debtor(s).*	Bankruptcy No. X86-02596F Chapter 7
FEDERAL DEPOSIT INSURANCE CORP. *Plaintiff(s)* vs. ROBERT L. WENTZEL *Defendant(s)*	Adversary No. X87-0206F

MEMORANDUM OF DECISION AND ORDER

Federal Deposit Insurance Corporation (FDIC) seeks a denial of debtor's discharge under 11 U.S.C. § 727(a)(4) and a determination that the indebtedness of debtor to FDIC is non-dischargeable under 11 U.S.C. § § 523(a)(2) and (a)(6).

Trial was held on June 16, 1989 in Fort Dodge, Iowa.

Having considered the evidence and the arguments of the parties, the court now issues the following memorandum of decision including findings of fact and conclusions of law.

This is a core proceeding under 2 8 U.S.C. § 157(b)(2)(I) and (J).

FINDINGS OF FACT

At the outset of the trial, the parties agreed that the court could consider as undisputed, certain facts set out in their pre-trial stipulation. The court, therefore, adopts as part of its findings the following undisputed facts.

> The Debtor, Robert Wentzel, was a business associate of Rodney Amlie, the former president of the Commercial State Bank of Pocahontas, Iowa (Bank) prior to its closing on June 27, 1986. Rod Amlie has been convicted of federal crimes related to his activities as president of the Bank and is serving a prison term.
>
> In early 1985, the Bank had outstanding loans to the Debtor in excess of its legal lending limit, and the Bank had been directed by regulatory authorities to correct the situation.

Robert Wentzel signed Mr. Schumacher's name to several promissory notes, a security agreement and a financing statement. The Bank advanced funds under one promissory note in the amount of $76,742.09 (Note "A") for the purchase of the Reedy cattle. The Reedy cattle were fed by Ronald Reedy. One loan to pay for feed was obtained with a promissory note using the name of Gerald Schumacher (Note "B").

Funds were also disbursed by the Bank under a third promissory note in the original amount of $55,400.00, which was signed by Wentzel using the name of Gerald Schumacher (Note "C"). FDIC has not been able to identify how these funds were ultimately used, although the funds were initially deposited to an account under the control of Rod Amlie.

The Reedy cattle were sold in July of 1986, and the proceeds were used to pay off notes "A" and "B".

The Commercial State Bank was declared insolvent by the Superintendent of Banking for the State of Iowa on July 29, 1986. The receivership for said Bank was tendered to the FDIC, who accepted said tender. The FDIC, in its receivership capacity, transferred the obligations of debtor sued upon herein to the FDIC, in its corporate capacity, transferred the obligations of debtor sued upon herein to the FDIC, in its corporate capacity, on said date pursuant to and in compliance with 12 U.S.C. Section 1823(e). That the FDIC is currently the holder and owner of said notes and documents.

On November 19, 1986, Robert Wentzel filed a Chapter 7 Bankruptcy and on March 5, 1987, FDIC conducted an examination of Robert Wentzel pursuant to Rule 2004 of the Rules of Bankruptcy Procedure. In his 2004 examination, Robert Wentzel testified that he had obtained a Power of Attorney from Gerald Schumacher "about a year" prior to the 2004 examination. The Power of Attorney was given to Wentzel on or about July 3, 1986.

An outstanding balance of $81,362.85 remains on Note "C", which was signed by Robert Wentzel using the name of Gerald Schumacher, plus interest of $23.53 per day after May 31, 1989.

ADDITIONAL FINDINGS OF FACT

The evidence adduced at trial warrants this court's finding of the following facts:

1. Robert L. Wentzel (WENTZEL) has been a merchant in Pocahontas, Iowa for approximately 30 years. With a partner, he has operated a hardware/farm supply store. He has been involved also in several other business ventures including: a joint venture in the sale of houses; the nursing home business; a restaurant business; a General Motors dealership; miscellaneous investments; and most importantly as it involves this case, the cattle feeding business. Wentzel attended school only through the 9th grade but has obtained a GED degree. He entered the armed services at age 17, served in Korea and was honorably discharged from the service in 1958. At that time, he settled in Pocahontas where he started an automotive parts business with his father. It was that business which was later converted to a hardware and farm store.
2. The Commercial State Bank in Pocahontas, Iowa was owned, for the most part, by the Amlie family. Rodney Amlie (AMLIE) was its chief executive officer and one of its stockholders. Wentzel did business with Amlie's bank. While their relationship was predominantly a business one, Wentzel considered he and Amlie to be friends; they have socialized together and Wentzel

has visited Amlie in prison. Initially, when Wentzel began doing business at the bank, he was helped by others. However, Amlie became more involved in Wentzel's credit transactions when they started feeding cattle. According to Wentzel, "he handled everything I did."

3. In 1984 or 1985, Wentzel began feeding penned cattle at Amlie's suggestion and sometimes in association with him. Wentzel, when he first began feeding cattle, deposited $100.00 in an account at the bank and borrowed from the bank the remaining funds necessary to purchase his first lot. According to Wentzel, Amlie made most of the decisions regarding cattle purchases although Amlie testified he always acted with "some kind of authorization." Wentzel said so many cattle were purchased, fed and sold that he never really knew whether he made or lost money. Wentzel fed approximately $3,000,000.00 worth of cattle over a three-year period. To facilitate the financing of cattle purchases and care, promissory notes and checks were filled out at the bank after Wentzel had already signed them in blank. Wentzel generally would sign twenty-five blank checks and ten blank notes at a time. They were kept by the bank. Amlie or Amlie's secretary, Teri Stover, would fill them out as necessary to conduct Wentzel's cattle business. When a cattle purchase was made, a note was typed up at the bank to fund the purchase price, and a blank check was completed to pay the seller. Signed blank checks in the bank's custody were also filled out and used to pay feeding and yardage costs with regard to the cattle and to repay the loans upon the sale of the cattle. Wentzel never saw the checks used to pay him when he sold the cattle. These were sent directly to the bank and used to pay off outstanding cattle notes.
4. The checking account used at the bank for Wentzel's cattle feeding investments was entitled the "Wentzel cattle venture account". Wentzel received bank statements with regard to this account at month's end along with his cancelled checks. While the statements and checks were always available to Wentzel to examine, Wentzel did not examine the statements or checks and left this chore to his accountant at year's end.
5. Sometime in early 1986, Amlie called Wentzel and a Mr. Dean Holtorf about a "good buy" in cattle available from Ron Reedy, a local cattleman and custom feeder.(fn.1) Amlie wanted to help out the owner of the cattle by facilitating the sale. He believed it would be a good business arrangement for all involved. Amlie deposition, Exhibit M, pages 9, 29). Wentzel and Holtorf agreed to the purchase of the lot on an equal share basis.

   1 Amlie testified that Wentzel contacted him about the purchase.

6. Although Wentzel had agreed to purchase half of the lot of cattle, he was unable to borrow the purchase money from Commercial State Bank because he had already borrowed in excess of the bank's lending limit. The bank's per customer lending limit is determined by a percentage of the bank's capital. The purpose of the lending restriction is to limit the amount of risk to the bank on loan failures by restricting debt concentration.
7. Wentzel's testimony regarding his awareness of being over his borrowing limit was somewhat confusing. He testified that his borrowing limit problem existed at a bank in Webster City. He asserted he was unaware at the time he wanted to buy the cattle of a lending limit problem at Commercial State Bank.

   Amlie's deposition testimony indicates that he told Wentzel of the over-limits problem at the outset of the Reedy cattle purchase. Amlie suggested to Wentzel that the cattle be purchased by using someone else's name (Exhibit M, pages 10, 12). This is corroborated by Wentzel's deposition testimony of September 1, 1988 (Exhibit 0, page 30) and by his oral testimony.

8. The court finds that Wentzel, shortly after his decision to buy half of the Reedy cattle and his authorization to Amlie to make the purchase, became aware of the Commercial State Bank's

inability to lend him the necessary funds because of its lending limit restrictions. Wentzel, therefore, determined that the share of the cattle lot which was to be his would be bought in the name of Gerald Schumacher, his brother-in-law.

9. Having heard the testimony of Wentzel and having observed his demeanor, and by review of the testimony of Amlie and Schumacher, it is this court's finding that the use of Schumacher's name for the Reedy cattle purchase was motivated by Wentzel's desire to fund his purchase commitment and was not made at the request of or with the advance consent of Schumacher, either specifically or generally. The use of Schumacher's name was to circumvent the inability of the bank to lend Wentzel the purchase money because of its lending limit restrictions.
10. Wentzel testified that he had previously talked to Schumacher, who lived in Arizona, about getting involved in cattle feeding. This testimony is at odds with Schumacher's deposition testimony. Schumacher was not advised of any proposed or completed purchase in his name until after the purchase and loan had taken place (Schumacher deposition, Exhibit 0, page 30).

    Schumacher was unaware of the purchasing relationship with Dean Holtorf (Exhibit 0, page 42). Schumacher never knew the specifics about the cattle (Exhibit 0, page 43) and was not involved in any decisions with regard to the care, feeding, or sale of the cattle (Exhibit 0, page 44). Schumacher learned of the transaction made in his name only shortly before he executed a power of attorney for Wentzel in July, 1986 (Exhibit 0, page 43).

    It is clear from the evidence that although Schumacher was not outraged upon learning of the transaction and although he willingly cooperated in providing a power of attorney to Wentzel to shore it up, he had little involvement in or knowledge of any of the transactions. Based on his deposition testimony, his cooperativeness with Wentzel appears to this court to have been based perhaps on his family relationship with Wentzel and upon his respect and admiration for him, especially as he perceived him to be a successful businessman.

11. Once it was determined that Wentzel would use Schumacher's name to purchase the cattle, he executed several blank notes to the bank, using Schumacher's name. It apparently had been decided that the blank-notes-and-checks system by which Wentzel conducted his own cattle financing would also be used for the Reedy purchase using Schumacher's name. Ultimately, three blank but executed notes were filled out (plaintiff's Exhibits A, B, and C). Exhibit A was a note dated March 11, 1986 in the amount of $76,742.09. This was for the purchase of the cattle from Reedy. Exhibit B was a note in the amount of $5,612.98 dated June 2, 1986, showing as signatory "Gerald C. Schumacher by Robert Wentzel." This check was used to pay Reedy for feed and yardage. The third note, plaintiff's Exhibit C, dated April 18, 1986, was in the original principal sum of $55,400.00. It was signed by Wentzel while blank using the name of Gerald C. Schumacher. When later filled out, its purported usage was for the purchase of 170 mixed steers, average weight 584 at a cost of $59.50 per hundredweight.

    Amlie assumes such cattle were bought (Exhibit M, pages 4445). However, there is no evidence to show that such cattle were ever purchased for Schumacher, nor is there evidence that Wentzel specifically authorized such a purchase. Amlie testified that he was involved in the execution of the note (Exhibit M, pages 8-9) and that he most likely provided the notation on the use of the money to buy cattle (Exhibit M, page 21). However, he does not recall the cattle or purchasing them.

12. Wentzel executed a Uniform Commercial Code financing statement in favor of Commercial State Bank in the name of Gerald C. Schumacher to secure debt, which financing statement showed the following types of property: "cattle on feed, feed & supplies therefor". There is no

indication that this was ever filed with the Iowa Secretary of State nor as to whether Schumacher signed the blank UCC form before it was filled out. On the UCC form, Schumacher's address was shown as Route 1, Humboldt, Iowa 50548. Wentzel was not from Humboldt nor was Schumacher.

13. An "Agri-Credit loan agreement" the blanks of which were not filled out, was executed by Wentzel in the name of Gerald Schumacher and provided to the bank. A financial statement for Schumacher was provided to the bank to substantiate the loan. It was completed in Amlie's handwriting. He says some of the information to complete it was given to him by Wentzel. Wentzel denies he had any knowledge of the statement until after the bank closed.

    Amlie notified Wentzel that the "loan" in Schumacher's name had been approved by the bank's board of directors.

14. Commercial State Bank was closed by the Iowa Department of Banking on June 27, 1986. At the time, Wentzel was out of town. After the bank closed, Wentzel was advised by his counsel to obtain in writing a power of attorney from Schumacher. Wentzel talked to Schumacher by phone two to three days before the power of attorney was executed. It was sent to Wentzel by express mail. The "durable general power of attorney" was executed by Schumacher on July 3, 1986 and was effective the same date.
15. On July 3, 1986, Wentzel opened account number 63-128-0 in the name of Gerald C. Schumacher at Pomeroy State Bank. The initial deposit was $27,691.69. The signature card was executed as "Gerald C. Schumacher by Robert Wentzel." The account was a savings account and the deposit resulted from the sale to Iowa Beef Processors (IBP) of "Schumacher' s" share of the initial cattle purchase. The first IBP check (no. A-898252) was dated July (unreadable), 1986 (Exhibit I) and was in the amount of $27,691.69. It was made payable to Gerald Schumacher and was deposited in the Pomeroy bank on July 3, 1986. The second IBP check (no. A-899641) was dated July 7, 1986 and was made payable to Gerald Schumacher in the amount of $70,785.68 (Exhibit I) . It was deposited at the bank in Pomeroy on July 18, 1986.
16. On July 24, 1986, Wentzel by telephone advice withdrew $85,870.83 from the Pomeroy State Bank savings account and purchased a cashier's check in that amount made payable to Federal Deposit Insurance Corporation. The check was dated July 24, 1986 and the remitter was shown as "Gerald Schumacher." Wentzel picked up the cashier's check at Pomeroy and delivered it to FDIC at Pocahontas. Wentzel had previously called the FDIC to get the specific payoff amount for the March 11, 1986 note.
17. Other withdrawals were made from the account. On July 18, 1986, Wentzel withdrew $818.81 from the Schumacher account at the Pomeroy State Bank and purchased a cashier's check in that amount payable to Point's Trucking. On July 11, 1986, Wentzel withdrew $4,781.31 from the Pomeroy account and purchased a cashier's check to make a feed payment to Ron Reedy. On July 16, 1986, Wentzel deposited $4,781.31 in the account. Wentzel testified that he did not receive the balance of the funds placed in the Pomeroy State Bank in Schumacher's name after bills had been paid. He testified also that Gerald Schumacher did not get any money from the cattle that he knew of. Schumacher also says he did not. The court finds he did not.
18. Sometime after the bank had been closed, Wentzel went through promissory notes which had been due to the bank from Wentzel and from Schumacher. It was then he first learned of the Schumacher note to Commercial State Bank in the amount of $55,400.00 dated April 18, 1986 (hereinafter referred to as "Note C"). Wentzel testified that there were no cattle represented by that note. This was so despite the fact that the promissory note showed the use of the proceeds of the loan to purchase the 170 mixed steers. Wentzel went to the FDIC and the FBI to tell them that there had been no receipt of either the funds or the cattle. 19. Amlie testified that it was

possible that Note C was completed at the bank without Wentzel's involvement (Exhibit M, page 22). The $55,400.00 proceeds of Note C were deposited in an account entitled "delivery account--customer cattle" (No. 131482) which was a checking account at Commercial controlled by Rod Amlie. Wentzel was not a signatory on that account; Amlie was. Amlie testified that it was conceivable that his secretary and the bank's head accountant could also write checks on the account. The bank used the account to handle complicated live cattle and futures transactions for various persons or entities. It is unclear as to whether such deposits became bank funds. Amlie said they were the bank's (Exhibit M, page 23, line 20). The evidence is insufficient so to find. There was no clear evidence as to why the loan proceeds of Note C were placed in this account. There is no evidence as to how the money was disbursed from the account. It could not be traced to Wentzel, and he denies receiving any.

19. As part of the evidence, plaintiff's exhibit G was introduced. It was a record of the account of Robert L. Wentzel, "Wentzel cattle venture." Wentzel examined photocopies of checks from the account and said that the only handwriting on any of the checks which was his was the signature. The balance of the writing on the various documents belonged either to Rod Amlie or his secretary, Teri Stover.
20. The proceeds of the bank loan to "Schumacher" dated March 11, 1988 (Exhibit A) were deposited on March 11, 1986 in the "Wentzel Cattle Venture" account. Two checks drawn on the account explain the use of the funds. Check no. 500 was made payable to Ron Reedy in the amount of $35,939.07 and check no. 501 was made payable to Everett Reedy, Reedy's father, in the amount of $40,803.02. These checks were written on March 4, 1986. Payments were also made to Reedy from the Wentzel account for one-half of the feed and yardage bills.
21. Reedy testified that he had never met Gerald Schumacher and assumed that Wentzel and Dean Holtorf were the buyers of the lot of cattle. Reedy only learned of Gerald Schumacher's ownership interest when they were later sold to IBP. He received the ownership information from the IBP representative.
22. Holtorf is a commodity broker who has fed cattle for approximately twenty years. He began feeding cattle using the bank for the transactions either at the end of 1983 or the beginning of 1984. In the beginning, he would talk to Amlie about buying a pen and would sign a note at the bank. As feeding increased, he began signing blank notes. He would sign ten to fifteen blank notes at a time. Sometimes he would sign blank checks but only once in a great while. Holtorf also bought pens of cattle on the advice of Amlie. Sales of purchase cattle would be handled by Holtorf in conjunction with the feedlot manager. If Holtorf was not available, Amlie would authorize sales. This occurred approximately 25% of the time.
23. With regard to the "Holtorf/Schumacher" lot of cattle, Holtorf testified that Amlie called him around the end of February or first of March. Amlie told him that Reedy had cattle and suggested that he take a look at them for purchase. However, he left it up to Holtorf. Holtorf did go look at the cattle and purchased half of the lot. At the time, he thought the other half was being purchased by Wentzel.
24. While the cattle were being fed, Holtorf learned that the other interest in the cattle was owned by Schumacher. When the cattle were sold, they were sold in the name of Holtorf and Schumacher. Holtorf turned his half of the proceeds over to the FDIC. While the cattle were being fed, Holtorf would receive the feed bills and tell Wentzel so Wentzel could arrange for one-half of the payment. Holtorf arranged for payment of his own one-half expense.
25. An examination of Commercial by the Iowa Department of Banking revealed that Wentzel's "direct and indirect obligations" exceeded the bank's loan limit by $96,414.00. The notation on the written report of examination as of January 31, 1986 stated in pertinent part as follows:

> Wentzel's direct and indirect obligations exceed subject bank's 40% loan limit by 96,414, with this amount held in violation of Section 524.904(2) (a) of the Code of Iowa. Also, total debt less the REM debt and the indirect debt, which qualifies for additional borrowing privileges, exceeds bank's 20% lending limit by 25,498 which is in violation of Section 524.904(2) of the Code of Iowa. Management is requested to correct this infraction by 5-15-86 and notify the Superintendent of Banking of the corrective action taken.

26. With regard to the report of examination, the court finds that the bank did not receive a written copy of the report before March 24, 1986. An exit interview between the examiners and the bank's board of directors (which in March, 1986 included Amlie) may have taken place, but the FDIC was not able to offer any direct evidence of such a meeting.
27. At the time of the Bankr. R. 2004 examination of Wentzel, he was asked when the power of attorney was executed. He responded, "About a year ago." The examination took place on March 5, 1986. A year prior to the examination would have placed the execution of the power of attorney at a date six days prior to the execution of the initial Schumacher note. The power of attorney was actually executed on July 3, 1986 after all three promissory notes (exhibits A, B and C) had come into existence. At his examination, Wentzel also was asked whether he provided a copy to the bank. He answered, "I suppose." A copy of the power of attorney was not provided to FDIC until after the bank had closed.

    Wentzel testified he was confused about when he had received the written power of attorney. Wentzel testified also that it was his understanding when it was decided that the cattle would be purchased in the name of Gerald Schumacher, that a separate account would be opened in Schumacher's name for handling the money arising out of the loans, purchase sales and cattle. This was not done, however, and instead the bank used the Wentzel cattle account. Feed bills for the Gerald Schumacher cattle were apparently paid for out of Wentzells account. Wentzel, in his 2004 examination, testified that the Schumacher cattle were fed through Schumacher's account. Wentzel said it was not until later that he found out that no separate account was set up by the bank for the Schumacher cattle feeding venture. Although Wentzel testified he assumed the bank was opening an account for Gerald Schumacher to handle his cattle transactions, Wentzel admitted he never signed a signature card for such an account. He also never received bank statements for Gerald Schumacher.

28. During the Rule 2004 examination, Wentzel responded in the following ways to questions by FDIC:

    > Q. Were you aware that Mr. Schumacher had loans with Commercial State Bank?
    >
    > A. Yes, I was.
    >
    > Q. How do you become aware of those loans?
    >
    > A. Because I was taking care of them for him, the cattle that he got.
    >
    > Q. So he was involved?
    >
    > A. In this cattle.
    >
    > Q. Through the loans in this cattle buying operation?

A. He would feed his own cattle and not with Hawkeye or any of them, just his own bunches at different places.

(Plaintiff's Exhibit N, page 34, lines 12-24.)

Another colloquy was as follows:

Q. Now what would happen to the proceeds of those notes once they were written?

A. They would go to Jerry Schumacher. You mean the sale of the cattle?

Q. No. There was a note with Gerald Schumacher's name on it. You would sign it, the bank would issue the proceeds on it--that note, and where would they go?

A. They wouldn't go to me, they would go to the feed yard, whoever the cattle were for.

Q. Would the bank issue a check directly to the feed yard or would they be run through someone's ac count? Would you send the money to Gerald Schumacher and he would pay the feed yard?

A. It was usually sent directly to the feedlot. if you bought the cattle you would send the check directly to them.

Q. So none of the proceeds of Mr. Schumacher ever benefitted you?

A. No.

Q. You never received any of the proceeds from any of those notes?

A. I received the ones that were written, you mean?

Q. Uh-huh.

A. No.

Q. None of the proceeds of those accounts ever went into any account that you would have had at the bank?

A. Not that I know of.

(Plaintiff's Exhibit N, page 36 line 25 through page 38 line 1.)

DISCUSSION

Count I asks the court to determine that the indebtedness represented by note Exhibit C be a non-dischargeable debt of Wentzel to FDIC because Wentzel's execution of the Schumacher note constituted obtaining money or credit by false pretenses, false representations or actual fraud under 11 U.S.C. § 523(a)(2)(A). FDIC also contends that that debt should be a non-dischargeable obligation of Wentzel because Wentzel's execution of the note using Schumacher's name was willful and malicious resulting in injury to the bank.

In Count II of its Complaint, FDIC contends that Wentzel's discharge should be denied because he testified falsely three times during his March 5, 1987 Rule 2004 examination.

DISCHARGEABILITY UNDER A 523(a)(2)(A)

In order to be successful on its fraud or misrepresentation Count, FDIC must prove that Wentzel obtained an extension of credit by false pretenses, false representation or actual fraud. 11 U.S. C. S 523(a)(2)(A). This proof must be by clear and convincing evidence. Caspers v. Van Horne (Matter of Van Horne), 823 F.2d 1285, 1287 (8th Cir. 1987) reh'g. denied 1987.

Before the court determines whether the debt is non-dischargeable, it must first determine whether Wentzel is indebted to FDIC on the remaining unpaid note.

Wentzel has not argued that there is no indebtedness owing to FDIC by him. The court concludes that there is such debt arising from promissory Note C even though the note was signed in blank by Wentzel using his brother-in-law's name.

Wentzel executed the promissory note while it was in blank form. He did so to make available to bank the wherewithal to conduct Wentzel's cattle purchase operation in the name of Schumacher. It was Wentzel's intent that the promissory note be used to borrow money from the bank for purchases and care of cattle. By his submission to the bank of the blank but executed note form, he authorized the bank, more particularly Amlie, to complete the instrument in accordance with his authorization. At the time Wentzel signed promissory Note C for $55,400.00, it was an incomplete instrument as described in Iowa Code § 554.3115(l). There is insufficient proof to show that anyone at the bank completed the promissory note within the authorization provided to the bank by Wentzel. The court concludes that the completion of promissory Note C was unauthorized by Wentzel within the meaning of Iowa Code § 554.3115(2). The promissory note at issue, while completed in an unauthorized manner, is enforceable by a holder in due course. Iowa Code § § 554.3407(2) and (3). A holder in due course is subject to certain real defenses asserted by a maker, but the court concludes that these real defenses are generally not applicable in this case. Iowa Code § 554.3305(2). The only applicable exception is § 554.3305(2)(d). The FDIC in this case would be subject to the bankruptcy discharge of this indebtedness if the court determines that this obligation is dischargeable.

The rights of the FDIC have been held to be akin to the rights of a holder in due course. 12 U.S.C. § 1823(e), In re Bombard, 59 B.R. 952, 955 (Bankr. D. Mass. 1986). The court, therefore, concludes that despite the lack of proof that Wentzel authorized the completion of promissory Note C, absent a discharge in bankruptcy, he is liable to the FDIC as a holder in due course.

In order to prevent discharge of this obligation under 52 3 (a)(2)(A), the FDIC must prove that Wentzel made a false representation with knowledge of its falsity at the time it was made and that he made such representation with intent to deceive. FDIC must further show that the bank relied upon the misrepresentation and that the misrepresentation was the proximate cause of resultant damage. 11 U.S.C. § 523(a)(2)(A), Federal Deposit Ins. Corp. v. Figge (In re Figge), 94 B.R. 654, 667 (Bankr. C.D. Cal. 1988).

The court finds and concludes that Wentzel in executing the blank promissory notes (Exhibits A, B and C) thereby represented he had actual authority to do so on behalf of Schumacher. Such representation was false and was known to be false by Wentzel at the time he executed the notes. The court furthermore finds that Wentzel executed the notes in blank with Schumacher's name with the intent and purpose of deceiving the bank and the bank examiners. Despite the collusion of Amlie, the

court finds and concludes that the bank relied on the representation of Wentzel in approving the line of credit.

The court cannot find, however, that bank sustained damage in the unpaid amount of Note C as a proximate result of Wentzel's misrepresentation. Plaintiff must prove all of the elements of its case for this court to determine that the indebtedness arising from Note C is non-dischargeable. Wentzel's purpose in making his misrepresentation to the bank was to continue his cattle feeding ventures by preventing the loss of credit due to bank lending limitations. There is no evidence, however, that it was his purpose to steal money from the bank or use it for any other purpose. The evidence shows it was his purpose to purchase, feed and sell cattle using the proceeds of sale to pay off purchase money debt, and to hopefully make a profit. Despite his deception of the bank, this was the authority given the bank, although under a different name. The FDIC has been unable to show that any cattle were bought as a result of the completion of Note C or that any of the money went to Wentzel or benefitted him. FDIC admits that the proceeds of the promissory note for $55,400.00 went into an account controlled by Amlie and could not be traced in any way to Wentzel.

Furthermore, the account was the bank's. FDIC not only cannot show that the money went to Wentzel, it has not dealt with the possibility that the proceeds were used in some way which benefitted the bank.

The other two Schumacher promissory notes were repaid in full (Exhibits A and B). Had they not been, the court believes that Wentzel would have been liable to FDIC for the amounts due under them, and such debt would have been non-dischargeable. This is so because the proof is clear and convincing that Wentzel authorized such advances. Had the bank not been repaid, it would have been damaged as a result of Wentzel's misrepresentations. However, Wentzel did not authorize, or at least there is no proof he authorized, the purchase of steers as shown in Note C. In fact, there is no proof that such steers ever existed.

This court believes that bank may have been damaged to the extent of $55,400.00 by a fraud or theft. However, the court cannot conclude that such damage was the proximate result of Wentzel signing Schumacher's name to a blank note. The guilty party might have just as well used a blank note previously executed by Wentzel, or perhaps Holtorf, or by other customers, trustfully and perhaps stupidly, allowing this method of doing business to take place.

> "The proximate cause element of S 523 requires simply that the action of the debtor was the act, without which the claimant would not have suffered the loss complained of."

Caspers v. Van Horne (Matter of Van Horne], 823 F.2d 1285, 1288 (8th Cir. 1987) reh'g. denied 1987 (citing In re Maier, 38 B.R. at 233).

The court concludes that FDIC has failed to show that Wentzel's misrepresentation was the proximate cause of the damage to bank arising from any unreimbursed disbursement of $55,400.00.

Someone did employ a blank note executed by Wentzel using Schumacher's name to obtain loan proceeds. This use was fraudulent. Such person misrepresented the actual authority to use the note and its purpose. Amlie's testimony leads this court to believe and find that it was Amlie.

If all the elements of fraud exist in the use of the note, would such fraud be imputable to Wentzel for the purposes of 523(a)(2)(A) of the Code? I believe it would.

The Eighth Circuit Court of Appeals has discussed such imputation and when it is permissible in Walker v. Citizens State Bank of Maryville, Missouri (Matter of Walker), 726 F.2d 452 (8th Cir. 1984). There the court said:

> Proof that a debtor's agent obtains money by fraud does not justify the denial of a discharge to the debtor, unless it is accompanied by proof which demonstrates or justifies an inference that the debtor knew or should have known of the fraud. (Citation omitted.) If the debtor was recklessly indifferent to the acts of his agent, then the fraud may also be attributable to the debtor-principal..... The debtor who abstains from all responsibility for his affairs cannot be held innocent for the fraud of his agent if, had he paid minimal attention, he would have been alerted to the fraud.

Id. at 454. (fn.2)

2 There is disagreement as to whether debtor's constructive knowledge of fraud should be a factor in determining whether fraudulent conduct can be imputed to the debtor. The Eighth Circuit Court of Appeals has found it to be a relevant factor in imputation. Other courts have found that it is not. See discussions in American Investment Bank, N.A. v. Hosking (In re Hosking), 89 B.R. 971, 976 (Bankr. S.D. Fla. 1988); Fluehr v. Paolino (In re Paolino), 75 B.R. 641, 648 (Bankr. E.D. Pa. 1987).

Amlie was Wentzel's agent. He had regularly used blank notes previously executed by Wentzel to obtain loans for Wentzel at the bank. Wentzel did not know, but should have known, that the blank notes were being misused or could be misused. He was recklessly indifferent to Amlie's control of these promissory instruments. The whole tenor of the relationship between Amlie and Wentzel manifests that. Wentzel permitted Amlie nearly complete control with regard to Wentzel's cattle ventures. He made no significant attempt to insure that Amlie acted honestly in relation to blank notes. The following are examples of Wentzel's lack of interest in how Amlie handled his affairs:

> Wentzel did not know if he was making or losing money on cattle ventures of great magnitude.
>
> He let Amlie do everything.
>
> He did not balance his statements or examine the checks from his cattle venture account and left that examination to his accountant at year's end. However, there is nothing to indicate that the accountant would have had any way to know of any misuse.
>
> He never followed up on the creation of a checking account for the Schumacher's transactions.
>
> He could have, but did not ask for copies of any notes or checks which were filled out subsequent to his execution of them in blank form.
>
> He allowed Amlie to fill out a financial statement on his behalf and he did not review it before signing it.

(Exhibit N, pages 44, 49).

Wentzel's indifference was reckless. He did not become concerned with regard to how his transactions were being treated until around the time the bank closed. Prior to that time, Wentzel had made no

significant effort to protect himself or the bank from the misuse of the blank, but executed instruments.

Having found that any fraudulent use of Note C may be imputed to Wentzel, the court must still determine whether FDIC has proven all the elements of fraud by clear and convincing evidence. The FDIC has not proven damage by clear and convincing evidence. The money was deposited upon the use of the note in a bank bank-account. FDIC cannot account for its disbursal. Therefore, the court must conclude, despite the misrepresentations of Amlie and Wentzel, that the FDIC has failed to prove fraud.

DISCHARGEABILITY UNDER 11 U.S.C. S 523(a)(6) -- WILLFUL AND MALICIOUS INJURY

Assuming for the purposes of FDIC's complaint under 11 U.*S.C.* § 523(a)(6), that Wentzel's action in executing blank notes with the name of Gerald Schumacher was willful and malicious, FDIC must still show that his actions led to harm in order to prevent discharge of debt under 11 U.S.C. § 523(a)(6). Federal Deposit Ins. Corp. v. Cerar (In re Cerar) , 84 B.R. 524, 530 (Bankr. C.D. Ill. 1988) aff'd. 97 B.R. 447 (C.D. Ill. 1989). On the basis of the court's prior analysis with regard to 11 U.S.C. § 523(a)(2)(A), the court cannot find that the execution of the notes led to damage to the bank. The same must be said as to the use of the note by the bank.

FALSE OATH

FDIC also seeks the denial of Wentzel's discharge on the ground that during his Bankr. R. 2004 examination he made three false oaths. The false testimony has been set out in paragraphs 28 and 29 of the findings of fact.

A. WHEN THE POWER OF ATTORNEY WAS EXECUTED

Wentzel testified on March 5, 1987 that he had executed the power of attorney "about a year ago." This was false. At the time of the Bankr. R. 2004 examination, he had executed the power of attorney almost exactly eight months prior. FDIC argues that such misstatement was material because a year prior would have placed the execution of the power of attorney prior to the execution of any notes in blank.

To prevail under 11 U.S.C. § 727(a)(4), FDIC must prove by clear and convincing evidence that the debtor knowingly and fraudulently made a false oath in connection with the case. Plaintiff must show that there has been an intentional untruth under oath in a matter material to the bankruptcy. Federal Land Bank of Omaha v. Ellingson (In re Ellingson), 63 B.R. 271, 276 (Bankr. N.D. Iowa 1986). The matter said to be material "if it bears a relationship to the debtor's business transactions or estate, or concerns discovery of assets, business dealings or existence or disposition of his property." Id. at 956. An untruth is said to be immaterial where the undisclosed property can have no bearing on the estate's condition or where the matters not disclosed are "so trivial in nature as to have but little effect on the estate and upon creditors."

The court believes the evidence before it does not clearly and convincingly show that the debtor's testimony with regard to when the power of attorney was executed was either a material misstatement or a misstatement knowingly made. Clearly, the debtor's testimony was not exact. However, the importance with which FDIC views the inaccuracy of the statement is not an impact which the court is convinced the debtor understood. The court finds the evidence insufficient to show anything other

than the impreciseness of the statement. Given that objections to discharge are to be construed narrowly in favor of the debtor, this court cannot deny the discharge on the basis of this imprecision.

B. WHERE SCHUMACHER FED CATTLE

Wentzel testified that Schumacher "would feed his own cattle and not with Hawkeye or any of them, just his own bunches at different places." FDIC contends that Schumacher did not own any cattle and that "even if the Reed Cattle could be considered to be Schumacher's cattle, Schumacher never 'fed his own bunches at different places.' The debtor had no reason to believe that Schumacher had any connection with more than one 'bunch' of cattle." (FDIC brief, page 11.) However, Wentzel's statement could have more than one meaning. The testimony of Wentzel can be construed to mean that Schumacher's bunches of cattle were fed separately or at a different location from where Hawkeye or others fed cattle. It is true that the statement is sloppy because it implies that Schumacher may have fed cattle at more than one place. However, later in the examination, Wentzel testifies that Schumacher had only "one bunch" (Exhibit N, page 58). Given the complete testimony of Wentzel, the court cannot find that this misstatement was either knowingly fraudulent or material.

C. LOAN PROCEEDS

Finally, FDIC contends that Wentzel testified falsely by stating that the proceeds of the Schumacher loans were paid directly to the feed yard and not through Wentzel's account and further that the loans did not benefit Wentzel. Based on the colloquy set out on pages 16-17 of the findings of fact, this court cannot find that Wentzel's responses to the FDIC questioning were false or knowingly false. Wentzel's testimony seen in the light most favorable to him, can be construed to mean that he did personally receive the money but the proceeds of the loans were used to pay for the cattle. This was in fact true in spite of the fact that the note proceeds did pass through his cattle account. The proceeds did go to Reedy. Wentzel may well have been talking about the ultimate disposition of the funds and not the route which they took to get there. As to whether the proceeds benefitted him, that is quite a subjective question, the meaning of which was not narrowed or defined at the Rule 2004 examination. It might in large part be a matter of opinion and without more, this court will not deny discharge because of it.

CONCLUSIONS UNDER § 727

FDIC's objection to discharge should be overruled. Indebtedness of Wentzel to FDIC arising out of a promissory note dated April 18, 1986 in the principal sum of $55,400.00 is dischargeable. Judgment shall enter accordingly.

SO ORDERED ON THIS 29th DAY OF DECEMBER, 1989.

William L. Edmonds
Chief Bankruptcy Judge

In the United States District Court

for the Northern District of Iowa

ROBERT L. WENTZEL
Debtor.

Bankruptcy No. X86-02596F
NO. C 90-3011

FEDERAL DEPOSIT INSURANCE CORP.
Plaintiff/Appellant

vs.

ROBERT L. WENTZEL
Defendant/Appellee

Adversary No. X87-0206F

ORDER

This matter is before the court on appellant Federal Deposit Insurance Corporation's (FDIC) appeal, filed March 7, 1990, from a decision of the bankruptcy court, entered December 29, 1989, which overruled the FDIC's objections to debtor's discharge. Both parties have filed briefs.

A bankruptcy court's findings of fact will not be set aside on appeal unless clearly erroneous. Bankruptcy Rule 8013. Review of questions of law is de novo. Matter of Newcomb, 744 F.2d 621, 625 (8th Cir. 1984). Appellant's sole assertion on appeal is that the bankruptcy court erred in finding that the FDIC had not been damaged by debtor's actions.

The bankruptcy court's findings of fact and conclusions of law are fully set forth in that court's memorandum of decision, filed December 29, 1989. The court will discuss the bankruptcy court's essential findings and conclusions as necessary.

This matter involves funds disbursed by the Commercial State Bank of Pocahontas, Iowa (Bank) under a promissory note (Note C) which was signed by debtor using the name of Gerald Schumacher. The FDIC has been unable to determine the eventual disposition of these funds, although they were deposited into an account at the bank controlled by Rodney Amlie, the former president of the bank. Appellant objected to the discharge of debtor for liability on this note on the basis of 11 U.S.C. S 523 (a)(2), which prevents the discharge of debts created by the obtaining of money or credit by false pretenses, false representations or actual fraud, and 11 U.S.C. S 523(a)(6), which prevents the discharge of debts arising from willful and malicious injury.

The bankruptcy court stated that, in order to prevent a discharge under § 523(a)(2), the FDIC must prove that the debtor "[1] made a false representation with knowledge of its falsity at the time it was made and that he made such representation with intent to deceive[,] . . . [2] that the bank relied upon the misrepresentation and [3] that the misrepresentation was the proximate cause of resultant damage." Order of the bankruptcy court, at 19-20 (citing 11 U.S.C. S 523(a)(2)(A) and Federal Deposit Ins. Corp. v. Figge (In re Figge), 94 B.R. 654, 667 (Bankr. C.D. Cal. 1988)). The bankruptcy court found that the FDIC had shown elements one and two. See order of the bankruptcy court, at 20. The court found, however, that the FDIC had failed to prove that the FDIC had sustained damage as the proximate result of debtor's misrepresentations. Id., at 20-24.

> The FDIC has been unable to show that any cattle were bought as a result of the completion of Note C or that any of the money went to Wentzel or benefitted him. FDIC admits that the proceeds of the promissory note for $55,400.00 went into an account controlled by Amlie and could not be traced in any way to Wentzel.

> Furthermore, the account was the bank's. FDIC not only cannot show that the money went to Wentzel, it has not dealt with the possibility that the proceeds were used in some way which benefitted the bank.

Order of the bankruptcy court, at 21.

> The FDIC has not proven damage by clear and convincing evidence. The money was deposited upon the use of the note in a bank bank-account. FDIC cannot account for its disbursal. Therefore, the court must conclude, despite the misrepresentations of Amlie and Wentzel, that the FDIC has failed to prove fraud.

Id., at 24. The court reached the same conclusions with respect to 11 U.S.C. S 523(a)(6). Id. at 25.

Appellant argues that it is damaged because the note remains unpaid. Appellant further argues that it is not necessary for the FDIC to prove that the debtor received the proceeds of the note. Appellant cites to In re Bombard, 59 B.R. 952, 954 (B.R. Mass. 1986) ("[I]t is not necessary that the property obtained by false pretenses be actually procured for the debtor himself.") (citing cases). Appellant, however, misses the thrust of the bankruptcy court's conclusions. The bankruptcy court did not merely find that the debtor had received no benefit from the fraudulent conduct. The bankruptcy court found that the proceeds of Note C had been deposited in an account owned by the Bank and that the FDIC had not proven by clear and convincing evidence that the proceeds had gone anywhere other than back to the Bank. In other words, the bankruptcy court found that the FDIC had not been damaged because the proceeds remained with the Bank and, thus, there was no loss to the Bank.

Appellant further argues that there is nothing in the record indicating that the account in which the funds were deposited was an account owned by the Bank. Appellant asserts that the only evidence in the record is that this account was controlled by Rodney Amlie. See record on appeal, at 37 (pretrial stipulation). Appellee asserts that the finding that the money was deposited into an account owned by the Bank is based upon the testimony of the debtor and the deposition testimony of Rod Amlie. The parties have not submitted the transcripts of the debtor's testimony nor Rod Amlie's deposition as part of the record on appeal.

In its findings of facts, the bankruptcy court found:

> The $55,400.00 proceeds of Note C were deposited in an account entitled 'delivery account--customer cattle' (No. 131482) which was a checking account at Commercial controlled by Rod Amlie. . . . The bank used the account to handle complicated live cattle and futures transactions for various persons or entities. it is unclear as to whether such deposits became bank funds. Amlie said they were the bank's (Exhibit M, page 23, line 20). The evidence is insufficient so to find. There was no clear evidence as to why the loan proceeds of Note C were placed in this account. There is no evidence as to how the money was disbursed from the account. It could not be traced to Wentzel, and he denies receiving any.

Order of the bankruptcy court, at 11-12. There is inconsistency between these findings of fact and the bankruptcy court's statements in its conclusions of law that "the account was the bank's," id., at 21, and "[t]he money was deposited upon the use of the note in a bank bank-account." Id. at 24. Due to this inconsistency, the court will remand this matter to the bankruptcy court for reconsideration of this matter, for resolution of this inconsistency, and for the taking of further evidence in the bankruptcy court's discretion. Bankruptcy Rule 8013.

ORDER:

Accordingly, It Is Ordered:

Pursuant to Bankrupty Rule 8013, this matter is remanded to the bankruptcy court for further proceedings in accordance with the above text.

Done and ordered this 10th day of September 1990.

David R. Hansen, Judge
UNITED STATES DISTRICT COURT

In the United States Bankruptcy Court

for the Northern District of Iowa

ROBERT L. WENTZEL *Debtor(s).*	Bankruptcy No. X86-02596F Chapter 7
FEDERAL DEPOSIT INSURANCE CORP. *Plaintiff(s)* vs. ROBERT L. WENTZEL *Defendant(s)*	Adversary No. X87-0206F

SUPPLEMENTAL ORDER

This adversary proceeding has been remanded to the Bankruptcy Court by the United States District Court for reconsideration of this court's ruling of September 10, 1990 and for resolution of an inconsistency pointed out therein by the District Court. The matter was remanded on September 10, 1990. The parties filed additional briefs and presented oral argument. The court having considered the record and the additional arguments of counsel, now issues this supplemental order.

The District Court called attention to an apparent inconsistency in the undersigned's findings and conclusions as to the nature of a particular bank account located at Commercial State Bank. The District Court stated as follows:

In its findings of fact, the bankruptcy court found:

> The $55,400.00 proceeds of Note C were deposited in an account entitled "delivery account--customer cattle" (No. 131482) which was a checking account at Commercial controlled by Rod Amlie . . . . The bank used the account to handle complicated live cattle and futures transactions for various persons or entities. It is unclear as to whether such deposits became bank funds. Amlie said they were the bank's (Exhibit M, page 23,

> line 20). The evidence is insufficient so to find. There was no clear evidence as to why the loan proceeds of Note C were placed in this account.
>
> There is no evidence as to how the money was disbursed from the account. It could not be traced to Wentzel, and he denies receiving any.

Order of the Bankruptcy Court, at 11-12. There is inconsistency between these findings of fact and the bankruptcy court's statements in its conclusions of law that "the account was the bank's," Id., at 21, and "[T]he money was deposited upon the use of the-note in a bank bank-account." Id. at 24.

By its findings and conclusions, the bankruptcy court intended to distinguish between the ownership and control of the account, and the ownership of the money within the account. From the court's review of the record, it is believed that this distinction is appropriate. Wentzel testified that Rod Amlie owned or controlled the account. Trial Transcript p. 69, 11. 20-21. This testimony is not inconsistent with other evidence in the case. Deborah McGee of the FDIC testified that Amlie had the sole signature authority over the account. Trial Transcript p. 114, 1. 23 through p. 115, 1. 2. In his deposition, Amlie testified that he had "control of the account." Exhibit M, p. 23, 1. 25. But he referred to the account as a "bank function" and said it was owned by Commercial State Bank. Exhibit M, p. 48, 1. 4-6.

Although the court believes that the evidence supports a factual determination that the account belonged to the bank, it did not necessarily follow that the money within the account was owned by the bank. Amlie himself made this distinction in his deposition testimony. He was asked:

> Q: You have indicated that the funds in your delivery cattle account were under your control. Were those your funds or were those funds that other people also had an interest in?
>
> A: Possibly a combination thereof.

Amlie testified, however, that the money in the account "would be the bank's." Exhibit M, p. 23, 1. 18-22.

The court, having re-examined the record, still finds that the evidence is insufficient to permit a determination of who owned all or any part of the money within the account.

II.

In its prior memorandum, the court found that "[t]here is no evidence as to how the money was disbursed from the account. It could not be traced to Wentzel, and he denies receiving any." Order, p. 12, p. 19.

FDIC has taken issue with this finding. It points out that the debtor testified as to his belief that Rod Amlie had taken the $55,400.00 proceeds from the note; he said that Amlie had admitted that to him on more than one occasion. The pre-trial stipulation of the parties provided that "the Debtor claims that Rod Amlie, rather than the Debtor, received the proceeds of Note 'C'." FDIC argues out that there was no contrary evidence as to who received the proceeds of note C and therefore the bankruptcy court must conclude that Rod Amlie received the proceeds of the note.

It may be true that Wentzel believes Amlie took the proceeds. But notwithstanding that belief and notwithstanding the stipulation, evidence at trial was not convincing. Ms. McGee, the FDIC

representative, testified that from her review of bank records, she could not determine who "ultimately ended up with this money." Trial Transcript, p. 113, 11. 14-22. In his deposition, Amlie was unable to testify as to where the funds in the "customer cattle" account went. Exhibit M, p. 47, 11. 5-11.

Contrary to Wentzel's deposition testimony, Amlie denied having discussions with Wentzel on the Shumacher transactions after Amlie's removal from the bank. Exhibit M, p. 35, 1. 18 through p. 37, 1. 5. From a review of the record, the court believes that the evidence is still inconclusive as to the disbursement of the proceeds of note C from the "delivery account."

Having reconsidered the matter in light of the District Court's Order of Remand,

IT IS ORDERED that the findings of fact and conclusions of law of the Order of December 29, 1989, as explained and amplified herein, are reaffirmed.

IT IS ORDERED that FDIC's objection to discharge is overruled. The indebtedness of Wentzel to FDIC arising out of a promissory note dated April 18, 1986 in the principal sum of $55,400.00 is discharged. Judgment shall enter accordingly.

SO ORDERED ON THIS 10th DAY OF DECEMBER, 1990.

William L. Edmonds
Chief Bankruptcy Judge

To the Top