In the United States Bankruptcy Court

for the Northern District of Iowa

TERRY D. CAPPS, CYNTHIA M. CAPPS Debtor(s).	Bankruptcy No. 93-20229KD Chapter 7
DUTRAC COMMUNITY CREDIT UNION Plaintiff(s) vs. TERRY D. CAPPS, CYNTHIA M. CAPPS Defendant(s)	Adversary No. 93-2106KD

ORDER

On October 20, 1993, the above-captioned matter came on for trial pursuant to assignment. Plaintiff appeared by Attorney James Trannel. Debtors-Defendants appeared by Attorney Brian Peters. The evidentiary record was submitted pursuant to a Stipulation filed with the Court. Attorney Trannel filed a Brief at trial. Attorney Peters waived the filing of further Briefs as the law in this area is well settled.

FINDINGS OF FACT

The matter before the Court is a complaint filed by Plaintiff Dutrac Community Credit Union asserting that they made a loan to Debtors based on a financial statement which was substantially false. This adversary proceeding is brought under 11 U.S.C. § 523(a)(2)(B).

Plaintiff loaned Debtors $1,500 after Debtors submitted a financial statement which listed $18,000 in debt. Debtors were actually almost $33,000 in debt. Plaintiff ran a credit check in addition to the financial statement. The credit check reflected several additional obligations not disclosed in the financial statement. Plaintiff asserts that it relied upon the financial statement of the Debtors in approving the loan. Plaintiff asserts that the loan was granted on the basis of the debt disclosed and, as it was substantially false, Debtors should be denied discharge on this debt. Plaintiff asserts intent can be inferred from conduct and the intent which should be inferred here is Debtors intentionally gave false financial information in order to obtain this loan.

The loan transaction was completed in November of 1992. Debtors filed for bankruptcy February 16, 1993. They made several payments on this obligation before bankruptcy though the payments were late. The obligation, as of the time of the filing of the bankruptcy, was approximately $1,300 or $1,400.

Debtors assert they incurred this debt in good faith. They say they gave financial information to Plaintiff's loan officer without supporting documentation. The loan officer placed the information on the document and Debtors signed it. Debtors state they intended to pay back the loan when made. However, Cynthia Capps lost her employment after the granting of this loan but before the bankruptcy. Debtors assert this was the precipitating factor preventing them from repaying the loan.

BURDEN OF PROOF

The standard of proof on dischargeability exemptions under 11 U.S.C. § 523 is by a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279, 111 S. Ct. 654, 661, 112 L. Ed. 2d 755 (1991). The preponderance of the evidence standard reflects a fair balance between effectuating the "fresh start" policy of the Bankruptcy Code and limiting the opportunity for a completely unencumbered new beginning to the "honest but unfortunate debtor." Grogan, 111 S. Ct. at 659.

CONCLUSIONS OF LAW

11 U.S.C. § 523(a)(2)(B) states:

a. A discharge under section 727. . . 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--

. . .

B. use of a statement in writing--
   i. that is materially false;
   ii. respecting the debtor's or an insider's financial condition;
   iii. on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and
   iv. that the debtor caused to be made or published with the intent to deceive.

The elements of proof for § 523(a)(2)(B) require that: "(1) the false financial statement be a writing respecting the debtor's financial condition; (2) the financial statement be materially false; (3) the debtor intended to deceive; and (4) there be reliance on the part of the creditor." In re Walderbach, No. L92-00780C, Adv. No. 92-1135LC, slip op. at 7 (Bankr. N.D. Iowa Aug. 31, 1993). For Plaintiff to prevail in its nondischargeability action, it must prove all four elements. In re Bagenstos, No. L-89-00489W, Adv. No. L-89-0112W, slip op. at 3 (Bankr. N.D. Iowa Jan. 4, 1990) ("If any one of the elements of proof is absent, irrespective of how overwhelming the proof as to the others might be, the plaintiff may not prevail in a section 523(a)(2) action.").

The 8th Circuit has concluded that exceptions to discharge must be "narrowly construed against the creditor and liberally construed against the debtor. These considerations, however, 'are applicable only to honest debtors.'" In re Van Horne, 823 F.2d 1285, 1287 (8th Cir. 1987); In re Kerbaugh, No. 92-31237, 1993 WL 409553, slip op. at 4 (Bankr. D.N.D. Sept. 23, 1993).

The fighting issue here is whether Debtors gave false information on their financial statement with the intent to deceive Plaintiff (§ 523(a)(2)(B)(iv)). This Court in Walderbach recently stated that "intent can be gleaned from surrounding circumstances." Slip op. at 8; cf. Van Horne, 823 F.2d at 1287 (concluding that intent in a § 523(a)(2)(A) action can be inferred from the surrounding circumstances).

In a factually similar case, the debtors applied to a credit union for a $1,000 advance. In re Carter, 78 B.R. 811, 812 (Bankr. E.D. Mich. 1987). A loan application, which provided a space for an applicant's outstanding debts, was completed by the loan officer and signed by the debtor. The credit union obtained a credit report showing that the debtor did not list all of his debts on the application. Notwithstanding the omissions, the credit union granted the advance. Id. at 813.

On the issue of intent to deceive, the court held that the credit union failed to meet its burden of proof. In support of its ruling the court criticized the application process used by the credit union as follows:

> In many cases, an applicant is asked to fill out an application for credit on the spot. He is told to list all of his current debts, often in a space provided which is woefully inadequate to the task. As is often the case, a

> debtor may truthfully fail to recall every outstanding obligation through any number of reasons. He might focus exclusively on the major debts in his life, (the mortgage and car payment for instance). He might not have given any thought to the question beforehand and so just does not know or remember what debts he owes. Sometimes the stress a debtor undoubtedly experiences from having his finances examined by a stranger, who will render a very personal judgment as to the debtor's worth in life, may cause him to omit some debts by accident. The end result is that instead of having loan applicants take the form home to carefully fill it out, too often the lender has the applicant fill out the form in a matter of minutes, increasing the likelihood of error or oversight. When the errors are discovered, the creditor points to the debtor's signed statement that the information provided is complete and true. Whether intentional or not, such common practices in consumer loan transactions may create errors and thereby give rise to a form of "bankruptcy insurance".

Id. at 817.

In In re Ross, 88 B.R. 805, 805 (Bankr. S.D. Ohio 1988), the debtor, owner of a word processing services company, sought capital for the purpose of financing his entry into computer hardware sales. To obtain a loan, the debtor was required to submit a personal financial statement. Id. at 806. The statement contained several inaccuracies. Id. On the issue of intent, the court focused on the debtor's credibility and good faith, concluding that the evidence failed to establish deceitful intent. Id. at 811. The court expressed its rationale as follows:

> Ross did not impress this Court as a dishonest debtor. He had few financial assets and did not appear to have pretended to be a person of means. He had hopes of succeeding in his new business venture, but the carelessness of his attempts to verify the representations in his financial statement, if typical of his approach to business generally, may partially explain his failure to succeed through Systems. Neither the evidence, Ross' demeanor nor his statements under oath, however, indicated any intent to deceive. No knowing misrepresentation was shown, and the carelessness did not approach a level which could appropriately be equated with fraudulent intent.

Id.

Other cases focus on the financial experience, intellectual understanding, and sophistication of the debtor in determining whether the element of intent to deceive is present. See e.g., In re Breen, 13 B.R. 965, 969 (Bankr. S.D. Ohio 1981) (holding that even if the debtor was of normal intelligence, "it is difficult to understand how he could expect to deceive the Bank, considering the ease with which it could have made a check on this financial condition"); In re Moore, 118 B.R. 64, 67 (Bankr. N.D. Tex. 1990) (finding no intent to deceive where the debtor displayed an "amateurish misunderstanding of the concept of joint and several liability, and a misunderstanding of the correct way to list those type liabilities"); In re Duplessis, 12 B.R. 475, 476 (Bankr. D. Mass. 1981) (attributing the cause of the nondisclosure to the debtor's lack of sophistication in financial matters rather than fraudulent motive.)

In Walderbach, the debtor overstated her household income on a credit card application. Slip op. at 8. At the time, her most recent employment was in an automobile financing department. Id. at 1. Factors the Court considered were whether there was a clear pattern of purposeful conduct, and whether the debtor was intelligent and experienced in financial matters. Id. at 9. The Court concluded that the only rational reason why someone with the debtor's "substantial" financial experience would substantially overstate her income would be to deceive the credit card company. Walderbach, slip op at 9. Similarly, In re Joyner, 132 B.R. 436, 442 (D. Kan. 1991) (discussed the issue of intent as follows:

> The omission of significant contingent liabilities in the financial statement was strong evidence of an intent to deceive. Joyner testified that he was experienced in reviewing and understanding financial statements. Joyner had a substantial amount of experience in business.

See also In re Compton, 97 B.R. 970, 979-80 (Bankr. N.D. Ind. 1989) (finding that given the debtor's job history and supervisory level, the debtor must have realized that she would have been denied the loan had she listed the omitted debts.)

Courts consider a number of factors in determining whether a debtor satisfied the element of intent under § 523(a)(2)(B)(iv). In Carter, the court stressed that the loan application process was rife with potential for accidental oversight or error. 78 B.R. at 817. In Ross, the court focused on the debtor's credibility and good faith. Id. 88 B.R. at 811. In Walderbach, the Court considered the intelligence and financial experience of the debtor and whether there was a pattern of similar conduct. Slip op. at 10.

In this case, numerous factors weigh in favor of Debtors on the issue of intent to deceive. Information supplied by Debtors to the Credit Union was from memory. The potential for inadvertent oversight is substantial. At the time of the loan, Cynthia Capps was employed and little, if any, evidence exists that Debtors were contemplating bankruptcy at the time of the loan. Plaintiff obtained an independent credit check which reflected some irregularities but nevertheless advanced the funds on this loan. Debtors made their first two payments on the loan, albeit late. This suggests good faith on the part of the Debtors at that time. There is little, if any, evidence that Debtors possessed substantial experience in financial matters. At most, the evidence supports a finding that Debtors were careless in omitting indebtedness. Carelessness is not equated with fraudulent intent. Ross, 88 B.R. at 811.

In summary, it is the conclusion of this Court that Plaintiff Dutrac Community Credit Union has failed to establish fraudulent intent by a preponderance of the evidence. As such, Plaintiff Dutrac Community Credit Union's adversary proceeding seeking denial of dischargeability of this debt must be denied.

WHEREFORE, this adversary complaint brought by Dutrac Community Credit Union against Debtors Terry D. and Cynthia M. Capps is not established by a preponderance of evidence and is therefore DENIED.

SO ORDERED this 24th day of November, 1993.

Paul J. Kilburg, Judge
U.S. Bankruptcy Court