In the United States Bankruptcy Court

for the Northern District of Iowa

DONALD E. MCGRAW ELAINE MARIE MCGRAW *Debtor(s).*	Bankruptcy No. 97-01428-W Chapter 7
IOWA OIL COMPANY *Plaintiff(s)* vs. DONALD E. MCGRAW *Defendant(s)*	Adversary No. 98-9002-W

ORDER

On October 15, 1998, the above-captioned matter came on for trial pursuant to assignment. Plaintiff Iowa Oil Company was represented by Attorney Doug Henry. Debtor/Defendant Donald McGraw was represented by Attorney Michael Dunbar. Evidence was presented and the parties were allowed to submit briefs. The time for filing briefs has now expired and this matter is ready for resolution. This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(I).

STATEMENT OF THE CASE

Defendant/Debtor Donald McGraw (McGraw) filed his Chapter 7 petition on May 9, 1997. On August 22, 1997, Plaintiff/Creditor Iowa Oil Company (Iowa Oil) filed this two count adversary complaint. All facts involved in this adversary proceeding occurred in March of 1997. During that time, Iowa Oil delivered petroleum products to McGraw. Iowa Oil asserts a total claim of $19,082.27 based upon petroleum deliveries. Of this total, $11,716.01 arises out of three separate transactions in which McGraw tendered checks for payment of the previous week's sales. He tendered a check in the amount of $4,064.05 on March 10, a check in the amount of $4,171.82 on March 17 and a check in the amount of $3,480.14 on March 24. All three checks were returned for nonsufficient funds. In addition, Iowa Oil alleges sales occurred between March 24, 1997 and March 31, 1997 in the amount of $7,366.26. Iowa Oil has not been paid for these sales. It, therefore, asserts a total nondischargeable amount of $19,082.27.

Count I of the dischargeability complaint alleges that Iowa Oil was induced to extend credit and deliver petroleum products to McGraw's service station under false pretenses and false representations pursuant to §523(a)(2). Iowa Oil seeks to have the Court determine that the total indebtedness of $19,082.27 is nondischargeable. The three checks represent the $11,716.01 returned for nonsufficient funds. The remaining $7,366.26 represents sales of petroleum products between March 24 and March 31, 1997. Iowa Oil asserts that McGraw accepted the final delivery of petroleum products on March

24 and had no intent to pay for or return the new petroleum products. Iowa Oil claims that McGraw's acceptance of these products and his silence constitutes an implied false representation which prevents discharge of the obligation involving the final delivery. Iowa Oil alleges under Count II that between March 10, 1997 and March 31, 1997, McGraw intentionally converted Iowa Oil's property to his own possession without the intent to pay for the property. Iowa Oil claims that this conversion was a proximate cause of Iowa Oil's damages in the amount of $19,082.27. Iowa Oil states that, as this is a conversion, the obligation is nondischargeable pursuant to both §523(a)(4) and §523(a)(6).

FINDINGS OF FACT

McGraw operated a gas station in Oelwein, Iowa. On December 21, 1995, McGraw entered into a contract with Iowa Oil whereby Iowa Oil would supply McGraw with gasoline and diesel fuel for resale to the public. The business was operated by McGraw and sold primarily petroleum products with a very limited line of other goods. McGraw testified that the business started profitably but competition from more diverse businesses caused his sales to continually decrease. For the last year of its existence, only McGraw and his spouse were employees of the business. McGraw successfully met his contractual obligations until the summer or early fall of 1996. At that time, because of cash flow problems, he began to submit nonsufficient funds checks to Iowa Oil to cover the previous week's sales.

Iowa Oil is in the business of supplying bulk gasoline, diesel fuel and other petroleum products to approximately 38 locations in Iowa. Of these various locations, approximately 25 to 30 are consignment accounts. Under a consignment account, Iowa Oil supplies gasoline or diesel fuel to a particular station. The gasoline remains the property of Iowa Oil until such time as it is sold.

The consignment account relationship between McGraw and Iowa Oil began in December of 1995. Mr. Perry Schroeder was credit manager of Iowa Oil and was in charge of collecting accounts. During part of this time, Mr. James McDermott was the collection agent whose job was to collect the weekly proceeds from McGraw. As collection agent, he would go to each consignment account station on a weekly basis and read the meters, measure the supply of petroleum products in the various tanks and determine the existing inventory. Payment was made weekly at the station site. The amount of payment was determined by the amount of petroleum products sold during the previous week. The amount of sales were calculated based on a reading of the meters and measurement of the storage tanks. It was the policy of Iowa Oil to receive timely payment. If payment was not made for the previous week, no further deliveries were to be made until the account was brought current.

It appears that the relationship went reasonably well from December of 1995 until the fall of 1996 when the first NSF checks were written. When this occurred, in lieu of terminating deliveries, the parties reached an agreement whereby the NSF checks were converted into a promissory note. (Plaintiff's Exhibit 2). As of September, 1996, Iowa Oil and McGraw had achieved a zero account balance. Eventually, McGraw paid the promissory note.

McGraw continued to have trouble making timely payments and the writing of NSF checks became more regular. He testified that during the course of the contract, he wrote as many as a dozen NSF checks in order to cover weekly payments. The matter became acute in February and March of 1997. McGraw was required to make a payment each week in order to guarantee delivery of additional petroleum products. He realized he did not have the funds to make payments and, therefore, began to write post-dated checks. This course of conduct was approved by the supervisors for Iowa Oil.

However, even when presented for payment after the posted date, the checks eventually began to be returned for nonsufficient funds.

McGraw began to make good on NSF checks by getting money orders and delivering them to the collection agent to cover past NSF checks while continuing to write post-dated checks for current deliveries of gasoline. Other suppliers also began to receive NSF checks and placed McGraw on a cash basis. Because other suppliers were requiring cash payments for products, McGraw's liquidity became even more impaired. By the 1st of March, 1997, McGraw was paying for his supplies, other than gas, on a cash basis, was providing post-dated checks to Iowa Oil for current obligations, and was delivering money orders to Iowa Oil for past NSF checks.

McGraw decided that he could not continue his business operations in this manner. Nevertheless, he did not discuss his financial problems with Iowa Oil nor did he inform them that he was on a cash basis with other suppliers. McGraw testified that he realized that unless significant changes were made, he could not continue to operate. For a short time, he considered expanding his line of other products, however, this did not occur. He continued to provide post-dated checks to Iowa Oil and continued to inform them that the checks would clear when the posted date occurred. He testified that he did intend to make the checks good and was hopeful that he would have the cash to clear the checks when they were presented for payment on the posted date.

However, business did not improve and in February, 1997, McGraw met with Attorney Michael Dunbar to discuss his business. The date of this meeting is undetermined. They discussed possible liquidation of the business and McGraw testified that, after talking to Mr. Dunbar, he was aware that certain obligations such as lottery payments and sales tax obligations would be nondischargeable in bankruptcy. McGraw testified that he was still hopeful that the business would survive. He scheduled an interview with Magna Bank to see if he could receive additional credit. He met with the Bank on March 27, 1997 but was informed that he was too bad of a risk and no additional funds would be loaned to the business.

During February and March, 1997, Iowa Oil became more adamant about payment upon delivery. The post-dated checks were not clearing the bank. By March 20, 1997, Iowa Oil viewed the problem as acute. It did make a delivery but indicated that other arrangements would have to be made for payment. During this delivery, McGraw informed them that he would be making changes in his business by adding a grocery line and other goods. The delivery was made and a post-dated check was provided which ultimately did not clear the bank. McGraw had some discussions with Iowa Oil concerning another promissory note but McGraw stated that he preferred to go through the bank for a line of credit.

The final delivery was made by Iowa Oil on March 24, 1997. Iowa Oil delivered approximately 1,100 gallons of lead-free gasoline and 1,500 gallons of ethanol blend lead-free gasoline. At the time of delivery, McGraw paid for the previous week's sales with a post-dated check which was eventually returned because of nonsufficient funds. McGraw testified that during the last week he was not thinking clearly and kept hoping that the business would make it. However, after talking to the banker and being denied credit, he knew that he could not continue in business. At that time, he made the decision to drop the prices on existing inventory. He reduced prices by approximately $.03 per gallon which placed his price $.01 per gallon lower than other gas available in town. Between March 24 and March 31, McGraw sold approximately 8,500 gallons of gasoline. Out of this amount, he owed $7,306.17 after adjustment for credit cards.

The amount sold during this week was between $3,500 and $4,000 more than sales during a normal week of business. McGraw did not tender any money for the gasoline sold during the final week. The records reflect that there were never sufficient funds in the business account during that time to pay for these sales. During these final days in business, McGraw dropped his sale price from either $\$1.14^{9}$ or $\$1.13^{9}$ to $\$1.10^{9}$. Iowa Oil alleges that this price was below cost. McGraw disputes this and states that he never sold any gasoline during these last days under cost to the best of his knowledge. McGraw testified he closed the doors for business on March 31, 1997. Thereafter, his distributors picked up their remaining goods. Iowa Oil claimed its remaining inventory on April 2, 1997.

McGraw admits that sales were up substantially during the last week in business because he dropped the price $.01 below other gas available in Oelwein. He also admits that during this last weekend, he sold gas knowing that he did not have the ability to pay and, in fact, did not intend to pay Iowa Oil for any gas sold. The revenues generated from these sales were directed elsewhere. McGraw used some of the revenue to pay off the lottery through a money order in the amount of $1,200. He also paid off his sales tax obligations in the amount of $1,400 and used the remaining cash revenue for operating expenses. Upon payment of these obligations, no funds remained to pay for the gas from Iowa Oil.

Iowa Oil asserts that McGraw owes Iowa Oil a total of $19,082.27 for petroleum products which were delivered and not paid for by McGraw. Of this amount, $7,306.17 was accumulated during the final week of the existence of the business between March 24 and March 31, 1997.

BURDEN OF PROOF

Iowa Oil bears the burden to prove the elements of its claim under 11 U.S.C. §523 by a preponderance of the evidence. See Grogan v. Garner, 498 U.S. 279 (1991). Exceptions to discharge must be "narrowly construed against the creditor and liberally against the debtor, thus effectuating the fresh start policy of the Code. These considerations, however, 'are applicable only to honest debtors.'" In re Van Horne, 823 F.2d 1285, 1287 (8th Cir. 1987) (citations omitted).

COUNT I (§523(a)(2))

Iowa Oil relies on § 523(a)(2)(A) in Count I of its complaint as grounds for excepting its claim from discharge. This section states:

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

11 U.S.C. §523(a)(2)(A) (1993). In this Circuit, a creditor proceeding under §523(a)(2)(A) must prove the following elements:

> (1) the debtor made false representations;
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> (2) at the time made, the debtor knew them to be false;
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> (3) the representations were made with the intention and purpose of deceiving the creditor;
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> (4) the creditor justifiably relied on the representations; and,
>
> (5) the creditor sustained the alleged injury as a proximate result of the representations having been made.

Van Horne, 823 F.2d at 1287, as modified by Field v. Mans, 516 U.S. 59, 74-75 (1995) (holding that "§ 523(a)(2)(A) requires justifiable, but not reasonable, reliance"). The Court will analyze each of the elements under § 523(a)(2)(A) as applied to the checks, then the elements will be applied to sales during the final week.

CHECKS

The first and second elements under § 523(a)(2)(A) address false representations and McGraw's knowledge of such representations. These elements can be analyzed together. A split of authority exists whether the delivery of a nonsufficient funds check satisfies the first element. One line of cases holds that a check does not constitute a representation of fact, thereby defeating the first element. The second line of cases treats the act of tendering a check as an implicit representation that the check is good. This Court has discussed these respective theories at length in previous opinions and has concluded that the concept of a passive "false pretense" exists in the context of nonsufficient funds checks. This Court concludes that a debtor's silence as to a material fact, including those involving nonsufficient funds checks, can constitute a false representation actionable under §523(a)(2)(A). See Whitlock v. Rizzio (In re Rizzio), Adv. No. 97-9115-C, slip op. at 6 (Bankr. N.D. Iowa Apr. 7, 1998); Buffalo Bay Grain v. Schuster (In re Schuster), Adv. No. 97-9004-D, slip op. at 4 (Bankr. N.D. Iowa Jan. 6, 1998).

McGraw tendered three checks totaling $11,716.01 to Iowa Oil knowing that there were insufficient funds in the account to cover currently dated as well as postdated checks when presented for payment. See In re Kurdoghlian, 30 B.R. 500, 502 (B.A.P. 9th Cir. 1983). It is the conclusion of this Court that in tendering checks to Iowa Oil, McGraw created a false impression that the check was backed by value. This satisfies both the first and second elements of §523(a)(2)(A).

The third element requires that McGraw intended to deceive Iowa Oil. Because actual proof of intent is often difficult to obtain, a creditor may present circumstantial evidence from which intent may be inferred. See Van Horne, 823 F.2d at 1287; see also In re Newell, 164 B.R. 992, 995 (Bankr. E.D. Mo. 1994) (considering the surrounding circumstances when analyzing the third element under § 523(a)(2)(A)); In re Edwards, 143 B.R. 51, 54 (Bankr. W.D. Pa. 1992) (holding that courts must look to the totality of circumstances to establish a debtor's intent). McGraw cannot overcome this inference with an "unsupported assertion of honest intent." In re Simpson, 29 B.R. 202, 211-12 (Bankr. N.D. Iowa 1983). The focus of this third element is on "whether the debtor's actions 'appear so inconsistent with [his] self-serving statement of intent that the proof leads the court to disbelieve the debtor.'" Van Horne, 823 F.2d at 1288 (brackets in original). Relevant factors include the debtor's intent to make good on the insufficient funds check, knowledge of whether the check would clear, attempts to make the check good, and whether the debtor ever had enough funds in the account to cover the check. Edwards, 143 B.R. at 54.

Iowa Oil and McGraw developed a course of conduct over the eighteen month existence of this business relationship. For some period of time, McGraw wrote insufficient fund checks which were eventually made good by promissory notes or money orders. McGraw testified that he intended to make all NSF checks good. In fact, all payments from the beginning of the relationship up to March 10, 1997 were made good in one form or another. However, beginning on March 10, McGraw received a supply of petroleum products and tendered an NSF check for the prior week's receipts in the amount of $4,064.05. On March 17, 1997, McGraw, likewise, submitted a check in the amount of $4,171.82 which was never paid. Finally, on March 24, 1997, McGraw tendered a check in the amount of $3,480.14 which also did not clear the bank.

While McGraw testified that he intended to make all checks good, the record reveals that by March of 1997 McGraw did not have the funds to make these checks good. At no time during this period did he have the resources to pay these checks. McGraw presented in excess of $11,000 in checks knowing that the same would not clear the bank when presented and that he could not make them good upon re-presentation. Under these circumstances, sufficient proof of McGraw's intent to deceive exists to satisfy the third element of §523(a)(2).

The fourth element requires that Iowa Oil relied on McGraw's misrepresentations or false pretenses. See In re Maier, 38 B.R. 231, 233 (Bankr. D. Minn. 1984). The Court must determine whether Iowa Oil was justified in relying on McGraw's misrepresentations that the three checks in question totaling approximately $11,500 was justified. It is the conclusion of this Court that Iowa Oil was not justified in relying upon any representations made by McGraw that these checks would be honored when presented for payment. During the course of this business relationship, McGraw had written approximately twelve checks to Iowa Oil which were dishonored the initial time they were presented for payment. While all of these checks before March of 1997 were eventually made good through promissory notes, re-presentment, or money orders, many checks were accepted by Iowa Oil which were not good at the time they were presented to Iowa Oil or presented after postdating.

Iowa Oil had substantial notice, based on the prior history of the parties' business relationship, that it was as likely as not that any check would not be good when presented for payment. Iowa Oil had no reasonable expectation that any one or all of these checks would be honored the first time that they were presented. In fact, it would have been unusual, based on the history of the parties, to have these checks clear the bank. Iowa Oil relied as much on subsequent payment by promissory notes, re-presentation, or money orders as they did on the fact that these checks would clear.

Iowa Oil had no justifiable reason to rely on McGraw's representation that these three checks tendered by him would be honored when presented. It is the conclusion of this Court that these three checks were not justifiably relied upon by Iowa Oil. As such, Iowa Oil has failed to satisfy the fourth element of §523(a)(2)(A).

The fifth element, the proximate cause element of §523, requires "that the action of the debtor was the act, without which the [plaintiff] would not have suffered the loss complained of." Van Horne, 823 F.2d at 1288-89 (quoting Maier, 38 B.R. at 233). Iowa Oil delivered petroleum products to McGraw over a three week period in the amount of $11,716.01. The checks representing payment for these products never cleared the bank and Iowa Oil lost value as a result of the payment of these checks. However, Iowa Oil was not justified in believing these checks would clear. As with other vendors, Iowa Oil could have changed the payment policy at any time to require cash or some other guaranteed form of payment. Iowa Oil continued to accept checks of dubious worth fully knowing the past history of these checks failing to clear the bank. It was not the presentation of the checks by McGraw which caused the loss but rather the acceptance of the checks by Iowa Oil knowing with some certainty that these checks did not represent value when presented. It is, therefore, the determination of this Court that Iowa Oil has failed to satisfy the fifth element of §523(a)(2)(A).

In summary, Iowa Oil has established that McGraw made false representations concerning the three checks dated March 10, March 17, and March 24, 1997 in the amount of $11,716.01. Iowa Oil also has established that, at the time these representations were made, McGraw was aware that the representations were false because he did not have the funds with which to pay the checks when presented. The Court also concludes that, based upon the financial picture of McGraw, he intended to deceive Iowa Oil by presenting these checks. However, the Court concludes that Iowa Oil was not justified in relying on these representations based on the past history of the parties. As a result, the proximate cause of the loss was the unjustified reliance of Iowa Oil and not the misrepresentations of McGraw. Consequently, though Iowa Oil lost value as a result of the misrepresentations of McGraw in the amount of $11,716.01, Iowa Oil has failed to establish all of the requisite elements of §523(a)(2)(A).

FINAL SALES

The second portion of Iowa Oil's claim under Count I involves the sales made by McGraw during the final week of operation. As McGraw never tendered a check for these sales, Iowa Oil's theory of nondischargeability is somewhat different than with the nonsufficient funds checks. Iowa Oil contends that it entered into a contractual relationship with McGraw on a consignment basis. It contends that contractual relationships can be the subject of implied false representations which could form the basis for denying discharge. Specifically, Iowa Oil contends that the final delivery was made at a time when McGraw had no intention to pay for the products delivered. Iowa Oil contends that McGraw's silence on this issue constitutes an implied false representation thereby satisfying the requisite element of §523(a)(2).

Iowa Oil's entire premise under this theory requires that McGraw made a false representation, either actual or implied. While this Court has recognized that an implied promise can, under certain circumstances, satisfy the first element of §523(a)(2), it is the factual conclusion of this Court that no false implied representation was made in this case at the time of delivery of the final petroleum products.

Factually, this Court concludes that the evidence does not support the contention of Iowa Oil that Debtor had no intention to pay for or return the final delivery of petroleum products. It is rather the factual conclusion of this Court that, while McGraw's expectations may have been unrealistic as late as March 27, 1997, he was attempting to stay in business. He had a conference with the Bank on March 27 in an attempt to get additional credit. It was only after being denied credit that McGraw made the final decision that he could not stay in business and he varied from his usual business practices. It was only at that time that McGraw reduced his prices in an attempt to liquidate and turn existing inventory into cash. As such, at the time of the delivery of the final inventory, it is the conclusion of this court that Debtor did not have the intent, either express or implied, to deceive Iowa Oil.

As a false representation is the cornerstone of §523(a)(2)(A), Iowa Oil has not met its burden of proof. Though Iowa Oil lost value during this last week of operation in the amount of $7,306.17, it has failed to establish that Debtor made an implied false representation at the critical point in time. It is the conclusion of this Court that Iowa Oil has failed to establish the first element of false representation under §523(a)(2) as it applied to this final delivery.

COUNT II

Iowa Oil has defined two separate theories under Count II. Iowa Oil asserts a breach of both §523(a)(6) and §523(a)(4). The Court will first address Iowa Oil's theory of nondischargeability under §523(a)(6).

§523(a)(6)

While the language of Count II appears to encompass not only the final delivery but also the earlier deliveries in the month of March, 1997, the evidence and the post-trial briefs seem to focus on the final delivery. Iowa Oil seeks to apply §523(a)(6) to the facts as established in this case. This section states in applicable part:

> (a) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt -
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> . . .
>
> > (6) for willful and malicious injury by the debtor to another entity or to the property of another entity.

Recent decisions by the United States Supreme Court and other courts have established high standards to hold an obligation nondischargeable under this section. Kawaauhau v. Geiger, 118 S. Ct. 974 (1998). To satisfy the willfulness component of §523(a)(6), the conduct in question must be an intentional act traditionally defined as an intentional tort. Intent, as used in the Restatement (Second) of Torts, refers to the consequences of a tortious act rather than the act itself. The Restatement (Second) of Torts defines intent as follows: "The word 'intent' is used throughout the Restatement of this Subject to denote that the actor desires to cause consequences of his act, or that he believes that the consequences are substantially certain to result from it." Restatement (Second) of Torts §8A (1964).

If the record establishes that the conduct complained of is an intentional tort, the willfulness component of §523(a)(6) is satisfied. Something additional is necessary, however, above and beyond the willfulness component to satisfy the maliciousness component of §523(a)(6). The Eighth Circuit strongly suggests that in order to satisfy the maliciousness component, it must be established that the tortious conduct was "targeted at the creditor". In re Long, 774 F.2d 875, 881 (8th Cir. 1985). This Court has concluded that if an intentional tort is established and it is established that the conduct was targeted at the creditor, the requirements of §523(a)(6) are satisfied. Hobson Mould Works, Inc. v. Lease (In re Lease), Adv. No. 98-9002-W, slip op. at 9 (Bankr. N.D. Iowa July 21, 1998).

Iowa Oil, in its brief, asserts that McGraw diverted the proceeds from the sale of the petroleum products. In other words, the proceeds of the sale were to be paid to Iowa Oil for the goods delivered.

Iowa Oil states that the diversion of proceeds is clearly an intentional act. The Court agrees that diversion of proceeds would constitute an intentional act. The current standards for §523(a)(6), however, require an intentional tort. Under this factual record, Iowa Oil has not established such an intentional tort.

The business arrangement between Iowa Oil and McGraw did not require that the funds, after sale, be segregated in a separate account. At all times, McGraw was authorized to utilize the proceeds of the sale in any appropriate business manner. During the entire course of McGraw's business, there was no targeting of sale proceeds from the gas to Iowa Oil. Therefore, the claim that the diversion of proceeds in inappropriate is not established by the record.

Secondly, the factual record establishes that until the last weekend of McGraw's business, it was his desire and intent to continue in business. It was only after he was denied credit by the Bank that his business conduct journeyed outside the ordinary course of business. It is the conclusion of this Court that until that time McGraw intended to conduct his sales in a legitimate business manner. Therefore, Iowa Oil has failed to establish the willfulness component of §523(a)(6).

Even if the Court were to conclude that the willfulness component of §523(a)(6) is satisfied, Iowa Oil must satisfy the extremely high standard to establish the maliciousness component of §523(a)(6). To satisfy this component, Iowa Oil must establish that the conduct in question was targeted at Iowa Oil. There is no evidence in this record to establish that McGraw held any ill will toward Iowa Oil. His conduct, if inappropriate in any manner, was designed to allow him to remain in business or to protect his own financial interests. There is nothing in this record to establish that his conduct was targeted at Iowa Oil in such a manner as to cause damage or injury to Iowa Oil. As such, it is the conclusion of this Court that Iowa Oil has failed to establish and satisfy either of the two elements under §523(a)(6).

§523(a)(4)

As a second part of Count II, Iowa Oil seeks to apply the elements of §523(a)(4) to McGraw's conduct in this case. Under this theory, Iowa Oil limits its application of §523(a)(4) to the final week of sales by McGraw. In its brief, Iowa Oil states that "if the contract between the parties was a true consignment and the conversion occurred after delivery, when the Debtor had lawful possession, the question would be embezzlement." Therefore, Iowa Oil is relying on a theory of embezzlement of property to satisfy one of the requisite elements of §523(a)(4) concerning the conduct of McGraw during the last days of the business existence.

Section 523(a)(4) states in applicable part:

> (a) A discharge under §727 . . . of this title does not discharge an individual debtor from any debt
> . . .
>
>> (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.

This section addresses three different types of conduct for which discharge can be denied. However, Iowa Oil only asserts that discharge should be denied under the embezzlement clause of §523(a)(4). It is the position of Iowa Oil that embezzlement occurred because McGraw was lawfully in possession of Iowa Oil's property but used the property in derogation of Iowa Oil's rights in the property.

Embezzlement for purposes of §523(a)(4) is the "fraudulent appropriation of property of another by a person to whom such property has been entrusted or into whose hands it has lawfully come." In re Phillips, 882 F.2d 302, 304 (8th Cir. 1989). In order to establish the elements of embezzlement, Iowa Oil must establish that: (1) McGraw was entrusted with or lawfully came into possession of property of another; (2) McGraw was under prior restraint as to the use of the property; and (3) McGraw's use violated the terms of the restraint. In re Belfry, 862 F.2d 661, 663 (8th Cir. 1988).

The evidence establishes that during the last week of operation of this business, McGraw sold $7,366.26 in petroleum products. During a portion of this time, he reduced the prices of these petroleum products to $.01 less than any other competitor in Oelwein, Iowa. The Court is satisfied, after considering the record, that McGraw sold a portion of the petroleum under cost and sold the remainder for no profit. Certainly, during the last several days of the existence of this business, McGraw was not selling his products for the purposes of making a profit, but was attempting to sell large volumes of petroleum products to convert petroleum into cash. This was a consignment account and the products remained the property of Iowa Oil until sold. This arrangement was established on December 21, 1995 when Iowa Oil and McGraw entered into a Contract Dealer Agreement. (Plaintiff's Exhibit 1). Paragraph 2 of this agreement states in relevant part:

> IOCO retains the option to accept payment for gasoline and diesel fuel delivered hereunder or the return of the gasoline and diesel fuel as provided herein. Dealer is authorized to sell the gasoline and diesel fuel to his customers in the ordinary course of his business, and it is agreed that title to said gasoline and diesel fuel shall pass on to the dealer at the meters on the pumps.

McGraw admits that from March 27, 1997 until the business closed on March 31, 1997, he lowered the prices intentionally to increase volume of sales and that he intended to sell products without the intent to pay Iowa Oil. In fact, the cash generated by the sales outside of the usual course of business was paid to several creditors whose claims would have been nondischargeable.

Applying these factual determinations to the elements of embezzlement, the first element requires proof that McGraw was entrusted with or lawfully came into possession of the property of another. The facts establish that pursuant to the consignment agreement between Iowa Oil and McGraw, the ownership of the property remained with Iowa Oil until ownership passed at the time of sale at the pumps. Until the time of sale, McGraw was lawfully in possession of Iowa Oil's property under the terms of their agreement.

Secondly, Iowa Oil must establish that McGraw was under a prior restraint as to the use of the property. The agreement entered into between Iowa Oil and McGraw provides that ownership would remain with Iowa Oil until the sale of the petroleum products. However, the sale was to be conducted using ordinary business practices. Therefore, McGraw was under a restraint as to the use of the property to the extent that he was not at liberty to sell the products in a manner inconsistent with good business practices. He was required to sell the products in the ordinary course of this type of business.

Finally, Iowa Oil must prove that McGraw used the property in a manner which violated the terms of the prior restraint. Iowa Oil has established that McGraw violated the terms of the prior restraint because he sold products during the final three or four days of the business at a price which was not intended to derive a profit. At best, it can be concluded that McGraw sold the petroleum products at cost but more than likely he sold much of this gasoline at less than cost. Whether it was sold at cost or less is not of critical significance. The critical point is that McGraw had determined that he was going to sell as much petroleum as possible during the remaining days of the existence of this business in order to turn these petroleum products into ready cash which he could use for his own purposes in derogation of the rights of Iowa Oil. This conduct was clearly in violation of the prior restraint placed upon the use of this property which required that McGraw use ordinary business judgment and sell these products in the ordinary course of business. Artificially reducing the price was in derogation of the rights of Iowa Oil and was designed for no other purpose than to turn the property of Iowa Oil into cash.

It is the conclusion of this Court that Iowa Oil has established the requisite elements of embezzlement and that the conduct of McGraw from March 27, 1997 until March 31, 1997 in selling these petroleum products constituted embezzlement. As such, that component of Iowa Oil's claim deriving from this conduct is nondischargeable.

DAMAGES

The final issue for determination is the amount of damages caused by McGraw's conduct. From March 24 through March 31, McGraw had sales of approximately $7,300. McGraw's business records reflect that on an average business week he sold between $3,500 and $4,000 worth of gasoline. McGraw began to sell gas at an accelerated rate after March 27. The increase in sales was caused by the significant decrease in prices at the pump.

It is difficult to compute the amount of damages incurred by Iowa Oil with mathematical precision. However, the law does not require mathematical precision in the determination of damages so long as there is satisfactory evidence that damages were incurred and the damages can be measured with some degree of certainty. In this case, it is fair to conclude that if Debtor had not dramatically decreased his prices during the week of March 24 through March 31, 1997, he would have sold petroleum products in an amount nearly identical to that sold during an ordinary week, or between $3,500 and $4,000. However, on this last week of the existence of this business, sales increased dramatically to $7,300. It is fair to conclude, therefore, that the difference between the $7,300 in sales and an ordinary week's sales was proximately caused by McGraw's dramatic decrease in prices.

Based on the Court's conclusions in this opinion, if Debtor had not decreased the gasoline prices and had continued to sell gas in the usual course of business at ordinary competitive prices, McGraw would have had an ordinary week of sales; McGraw would have committed no acts which would support nondischargeability of any obligation to Iowa Oil; and Iowa Oil would have been able to reclaim the unsold portion of McGraw's inventory thereby incurring no loss. However, the decrease in price caused an increase in sales and a commensurate decrease in inventory. It is this difference between average sales and this particular week's sales which constitutes the damages incurred by Iowa Oil. Again, while not capable of mathematical precision, the damages are the difference between what would have been sold and what was actually sold during this week.

The only basis for determining what would have been sold is a comparison to an ordinary week's sales. It is the conclusion of this Court that an ordinary week's sales is approximately $3,750. Therefore, it is the conclusion of this Court that Iowa Oil has incurred damages as a result of McGraw's conduct in the amount of $3,550.

CONCLUSION

Iowa Oil has failed to establish the requisite elements of §523(a)(2)(A) of the Code and, therefore, the obligation owing by McGraw to Iowa Oil is not excepted from discharge under this theory. Further, Iowa Oil has failed to establish the requisite elements of §523(a)(6). Iowa Oil's claim of nondischargeability under this theory is denied. Further, Iowa Oil has established the requisite elements of §523(a)(4) against McGraw for conduct occurring between March 27 and March 31, 1997. The Court determines that the amount of damages caused by McGraw's conduct during this period of time is $3,550 and it is this amount which will be nondischargeable.

WHEREFORE, Plaintiff Iowa Oil's claim of nondischargeability against Debtor Donald E. McGraw under 11 U.S.C. §523(a)(4) is granted in the amount of $3,550.

FURTHER, judgment shall enter accordingly.

SO ORDERED this 3rd day of December, 1998.

PAUL J. KILBURG

Paul J. Kilburg
U.S. Bankruptcy Judge