

# In the United States Bankruptcy Court

## for the Northern District of Iowa

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DANIEL A. HOLMES and  
JUDY A. HOLMES

Bankruptcy No. 99-01961-W

*Debtor(s).*

Chapter 7

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DICK WITHAM FORD - VW

Adversary No. 99-9184-W

*Plaintiff(s)*

vs.

DANIEL A. HOLMES and  
JUDY A. HOLMES

*Defendant(s)*

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### **ORDER RE: APPLICATION FOR AWARD OF ATTORNEY FEES AND COSTS**

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The Court ruled on the underlying Complaint in this adversary proceeding on August 22, 2000. At that time, the Court allowed the parties time to file briefs on Debtors' request for attorney fees and costs under 11 U.S.C. §523(d). The time for filing briefs has now passed and this matter is ready for resolution. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A), (I).

#### **STATEMENT OF THE CASE**

Plaintiff's adversary complaint asserts claims under §§523(a)(2)(A) and (B) arising out of Debtors' purchase of an automobile from Plaintiff. After Plaintiff presented its case at trial on August 22, 2000, the Court granted a directed verdict for Debtors. Debtors request compensation for attorney fees and costs under §523(d).

#### **FINDINGS OF FACT**

Plaintiff Dick Witham Ford-VW asserted in its complaint that Debtors Daniel and Judy Holmes misrepresented the balance due on one of their trade-ins when they purchased a vehicle in September 1998. After Plaintiff presented its evidence at trial, the Court ruled that it had failed to present sufficient evidence to meet its burden of proof under §§523(a)(2)(A) and (B). The Court granted Debtor's Motion for Directed Verdict, dictating its findings of fact and conclusions of law into the record.

To summarize, Plaintiff asserted Debtors committed fraud or misrepresentation in signing a purchase agreement. The agreement stated the amount due on Debtors' loan with Norwest Bank was \$4,053.52. The actual balance on the loan was later discovered to be more than \$10,000. The loan was secured by

a 1997 Ford Escort Debtors traded in for a 1998 Ford F-150. The parties disputed whether Debtors knew the purchase agreement was inaccurate regarding the extent of the lien on the Escort. There was conflicting testimony regarding whether Norwest Bank or Debtors gave Plaintiff the incorrect figure. The Court ruled in favor of Debtors.

### CONCLUSIONS OF LAW

Debtors assert they are entitled to attorney fees and costs under §523(d). That section states:

If a creditor requests a determination of dischargeability of a consumer debt under subsection (a)(2), and such debt is discharged, the court shall grant judgment in favor of the debtor for the costs of, and a reasonable attorney's fee for, the proceeding if the court finds that the position of the creditor was not substantially justified, except that the court shall not award such costs and fees if special circumstances would make the award unjust.

11 U.S.C. §523(d).

In order to receive attorney's fees under this section, the debtor must prove that (1) the creditor requested a determination of dischargeability under §523(a)(2), (2) the debt is a consumer debt, and (3) the debt was discharged. In re Harvey, 172 B.R. 314, 317 (B.A.P. 9th Cir. 1994); FCC Nat'l Bank v. Dobbins, 151 B.R. 509, 512 (W.D. Mo. 1992). Once the debtor meets the burden of proof on these elements, the burden shifts to the creditor to prove that its actions were substantially justified, Dobbins, 151 B.R. at 511, or that special circumstances exist which would make the award unjust. In re Cameron, 219 B.R. 531, 539 (Bankr. W.D. Mo. 1998).

"Substantially justified" means more than frivolous, or undeserving of sanctions. In re Friend, 156 B.R. 257, 262 (Bankr. W.D. Mo. 1993). In order to be "substantially justified", the complaint must have a reasonable basis in law and fact in light of the factors relevant to the claim of nondischargeability. Dobbins, 151 B.R. at 512. Whether a dischargeability complaint has a "reasonable basis in law" is measured against the state of binding legal precedent. In re Stearns, 241 B.R. 611, 628 (Bankr. D. Minn. 1999). Whether it has a "reasonable basis in fact" turns on whether the creditor's evidence arguably meets the elements of its theory of recovery. Id. This can be determined by examining whether the creditor conducted an adequate pre-suit investigation. Id.; Cameron, 219 B.R. at 540.

A creditor is not substantially justified when it proceeds to trial knowing that it lacks sufficient evidence to sustain its burden of proof and then fails to establish a single necessary element of its claim. Manufacturers Hanover Trust Co. v. Hudgins, 72 B.R. 214, 220 (N.D. Ill. 1987). Attorney fees should be awarded when a plaintiff proceeds with a case past the point at which it knew or should have known it could not carry its burden of proof. Cameron, 219 B.R. at 540.

The purpose of §523(d) is to discourage creditors from commencing actions in an effort to obtain a settlement from an honest debtor who may not be able to pay for an attorney to handle an adversary proceeding. In re Stewart, 91 B.R. 489, 497 (Bankr. S.D. Iowa 1988). It is meant to discourage frivolous objections to discharge. In re Williamson, 181 B.R. 403, 409 (Bankr. W.D. Mo. 1995). "Congress was justifiably concerned that creditors would be able to use the threat of a section 523 nondischargeability proceeding to extract settlements from debtors" who are less able to afford to pay counsel and litigate. Id.

The second of the three elements which debtors are required to prove under §523(d), that the debt is a consumer debt, promotes these purposes. "Consumer debt" is defined in §101(8) as a "debt incurred by an individual primarily for a personal, family or household purpose." This definition was adapted from consumer protection laws which have been construed to exclude debts incurred with a business or profit motive. In re Burns, 894 F.2d 361, 363 (10th Cir. 1990).

Plaintiff requested a determination of dischargeability under §§523(a)(2)(A) and (B). The Court denied Plaintiff's claim in its August 22, 2000 ruling granting Debtors' Motion for Directed Verdict, and concluded that the debt is discharged. Thus, Debtors have met the first two elements of their claim for attorney fees under §523(d).

Plaintiff contests whether the debt in question is a "consumer debt" under §523(d). At the time Debtors filed their bankruptcy petition, Plaintiff's state court action against Debtors for breach of contract, negligence and fraud was pending. Plaintiff argues the debt is thus a legal claim, not a consumer debt. The Court concludes that the debt, arising from a transaction to purchase a family automobile, is a consumer debt under §523(d). Debtors did not purchase the F-150 for a business purpose or with a profit motive. Plaintiff's state court action does not transform the debt into a non-consumer debt.

Debtors have met their burden of proof on all three elements under §523(d). Plaintiff requested a determination of dischargeability under §§523(a)(2)(A) and (B), the debt is a consumer debt, and the Court determined the debt is discharged. As such, Plaintiff has the burden to prove its actions were substantially justified or that special circumstances make the award unjust.

After reviewing the record, the Court concludes that Plaintiff's actions were substantially justified. Plaintiff made pre-suit investigation, as evidenced by its prepetition action against Debtors filed in Iowa District Court. The facts were disputed and Plaintiff ultimately failed in its burden of proof. However, Plaintiff's version of the facts would arguably meet the elements of §523(a)(2)(A) or (B), under fairly well settled legal precedent in the Eighth Circuit.

Under §523(a)(2), the debt would be excepted from discharge if Plaintiff could prove Debtors knowingly provided false information with the intent to deceive. See First Nat'l Bank v. Pontow, 111 F.3d 604, 608 (8th Cir. 1997) (setting out the elements of §523(a)(2)(B)); In re Guske, 243 B.R. 359, 362 (B.A.P. 8th Cir. 2000) (setting out the elements of §523(a)(2)(A)). Plaintiff must prove these elements by a preponderance of the evidence, not by clear and convincing evidence. Grogan v. Garner, 498 U.S. 279, 286-87 (1991). Based on the record, the Court concludes that Plaintiff's action had a reasonable basis in law and fact in light of the factors relevant to the claim of nondischargeability under §§523(a)(2)(A) or (B). As such, Debtors are not entitled to an award of attorney fees and costs under §523(d).

**WHEREFORE**, Debtors' request for attorney fees and costs under §523(d) is DENIED.

**FURTHER**, as set out on the record on August 22, 2000, Plaintiff has failed to meet its burden of proof under §§523(a)(2)(A) and (B).

**FURTHER**, Debtors' obligation to Plaintiff is discharged.

**FURTHER**, this is the Court's final order in this matter for appeal purposes.

**FURTHER**, judgment shall enter accordingly.

**SO ORDERED** this 3rd day of October, 2000.

Paul J. Kilburg  
Chief Bankruptcy Judge