UNITED STATES BANKRUPTCY COURT FOR THE NORTHERN DISTRICT OF IOWA

IN RE:)
) Chapter 7
MARK D. GRITTON)
) Bankruptcy No. 02-03266
Debtor.)
----------) ROBERT HAMDORF)
) Adversary No. 02-9152
Plaintiff,)
)
vs.)
)
MARK D. GRITTON)
)
Defendant.)

ORDER RE COMPLAINT TO DETERMINE DISCHARGEABILITY OF A DEBT

This matter came before the undersigned on February 12, 2003 pursuant to assignment. Plaintiff Robert Hamdorf was represented by Attorney Bradley Norton. Debtor/Defendant Mark Gritton was represented by Attorney Douglas Wolfe. After hearing evidence and arguments of counsel, the Court took the matter under advisement. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I).

STATEMENT OF THE CASE

Plaintiff sold Debtor two riding lawn mowers. Debtor failed to pay for the mowers. Plaintiff asserts the resulting debt is excepted from discharge based on fraud, defalcation and theft.

FINDINGS OF FACT

Plaintiff Robert Hamdorf is retired from employment as a repairman for a John Deere dealership. He is 76 years old and lives at 113 Grant Ave., Lowden, Iowa. Plaintiff has a shop behind his house where he works on small engines and mowers.

Debtor/Defendant Mark Gritton was Plaintiff's neighbor, living at 105 Grant Ave., Lowden, Iowa. He recently moved to a rental house in the country at 786 Yankee Ave., Lowden, Iowa.
Debtor's fiancee, Lori Dibben, is a party to the rental agreement, although it is unclear whether she is Debtor's
landlord or a co-tenant. Ms. Dibben's residence is listed on Schedule G as 110 Grant Ave., Lowden, Iowa.

Plaintiff has known Debtor for 20 years. Approximately 6 years ago, Debtor bought a lawn mower from Plaintiff, paying the full price at the time of purchase. In April 2002, Debtor approached Plaintiff to purchase mowers. Debtor told Plaintiff he wanted the mowers to mow the local cemetery under his contract with the City of Lowden. Plaintiff sold Debtor two riding mowers which he had at his shop. Debtor did not pay for the mowers.
Plaintiff testified Debtor stated he was applying for a loan and would have the money to pay for the mowers in a week or two.

About three weeks after the sale, Debtor told Plaintiff he had failed to get the purchase price from the loan but was trying to correct some paperwork. Debtor stated that he would pay Plaintiff when the paperwork went through and he got the

money.
A few more weeks passed without payment by Debtor. During discussions regarding payment, Debtor told Plaintiff he didn't have the money. Plaintiff testified Debtor indicated he couldn't pay for the mowers until he could get some money from his mowing contract with the City.

After a time, Debtor asked Plaintiff whether he could pay for just one of the mowers. This discussion occurred in August, not long before Debtor filed for bankruptcy. Plaintiff agreed to accept $550 for one of the mowers and return of the other mower. Debtor paid nothing toward the purchase price of the mowers, nor did he return either of the mowers although Plaintiff asked for their return.

Plaintiff later went to Debtor's place in the country about getting the mowers back. Debtor told him he had filed for bankruptcy relief. Plaintiff also attempted to take the mowers back by confronting Debtor at the cemetery when he was mowing.
Plaintiff was accompanied by his son and grandson and brought a trailer to haul the mowers. Debtor and his fiancee's two sons were at the cemetery and the local police were called.

Debtor filed his Chapter 7 petition on September 17, 2002. His statement of affairs discloses that he paid attorney Douglas Wolfe $700 on August 28, 2002 for consultation relating to debt or bankruptcy.

Debtor is a self-employed carpenter, 41 years old. He contracts with the City of Lowden to mow the cemetery for extra income. Debtor agrees with Plaintiff's description of the purchase transaction for the mowers. He testified that his
fiancee, Ms. Dibben, was getting a loan to build a home and he had hoped there would be funds available from the loan to pay the purchase price of the mowers. The loan went through but there was not enough money left over to pay for the mowers. Debtor testified that he did not return the mowers to Plaintiff prepetition because he needed them through October 15 for his mowing contract. He kept the mowers at a locked shed at the cemetery, where he is caretaker.

Debtor's contract with the City is for two years, beginning April 15, 2002 through September 15, 2003. Under the contract, Debtor receives $5,800 per year through monthly payments of $966 per month from April through October. He received five of the six monthly payments for 2002 before he filed his bankruptcy petition in September. Debtor's schedules show he also received
$5,800 from the City Cemetery Board in 2000 and 2001. Debtor testified that he has significant mowing expenses. He hires young people to help with labor, including Ms. Dibben's sons.

Debtor filed a list of business income and expenses with his schedules. The document apparently prorates his income and expenses from the six-month term of the mowing contract over 12 months to report average monthly figures. By extrapolating back to six-month figures, Debtor reports monthly gross income between April and October of $966 and net income of $148. The largest expense reported is $360 for Office Expenses and Supplies. Other significant expenses are $160 for Utilities, $136 for Net Employee Payroll and $90 for Repairs and Maintenance.

Debtor testified that prior to filing for bankruptcy, he tried to talk to Plaintiff, on the advice of his attorney, to work out payment for the mowers. Debtor testified he did not intend deceit or fraud or to take the mowers without paying. He asserts the mowers are his property. He testified he intended to pay for the mowers but had no money left over from the loan funds or from the monthly contract payments from the City. When asked why he had not tried to make installment payments, Debtor answered that that was not part of the parties' agreement.

CONCLUSIONS OF LAW

Plaintiff seeks to except the debt from discharge, alleging Debtor committed fraud, defalcation or theft. Fraud, defalcation, and theft are covered in part by 11 U.S.C. § 523(a)(4). Fraud is also covered in part by 11 U.S.C. § 523(a)(2)(A). It is Plaintiff's allegations of fraud by Debtor which form the basis of this complaint and are at issue in the evidence.

Thus, this cause of action arises under § 523(a)(2)(A) and § 523(a)(4), which state as follows:

> (a) a discharge under section 727...of this title 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 –
>
> (A) false pretenses, a false representation, or actual fraud, . . .
>
> . . .
>
> (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.

As the primary goal of the Bankruptcy Code is to provide debtors with a "fresh start," exceptions to discharge are generally construed narrowly. In re Kline, 65 F.3d 749, 751 (8th Cir. 1995). In order to except a debt from discharge under § 523, Plaintiff must prove the elements of the claim by a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279, 286-87 (1991).

SECTION 523(a)(4)

To prevent the discharge of a debt under the initial clause of § 523(a)(4), it is incumbent upon Plaintiff to establish the following two elements: (1) that a fiduciary relationship existed between Debtor and Plaintiff; and (2) that Debtor committed fraud or defalcation in the course of that fiduciary relationship. In re Montgomery, 236 B.R. 914, 922 (Bankr. D.N.D. 1999).

With regard to the first element, whether a relationship is a fiduciary relationship within the meaning of § 523(a)(4) is a question of federal law. In re Cochrane, 124 F.3d 978, 984 (8th Cir. 1997). The fiduciary relationship must be one arising from an express or technical trust. In re Long, 774 F.2d 875, 878 (8th Cir. 1985). A mere contractual relationship is less than what is required to establish the existence of a fiduciary relationship. Werner v. Hofmann, 5 F.3d 1170, 1172 (8th Cir. 1993). The fiduciary relationship of § 523(a)(4) does not encompass ordinary commercial relationships such as debtor-creditor or principal-agent. In re Dove, 78 B.R. 630, 636 (Bankr. M.D. Ga. 1986).

Embezzlement 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 prove embezzlement, Plaintiff must show that (1) Debtor was entrusted with property or lawfully came into possession of property of another; (2) Debtor was under a prior restraint, whether written or verbal, as to the use of the property; and (3) the terms of restraint were violated by Debtor's use of the property. In re Belfry, 862 F.2d 661, 663 (8th Cir. 1988); see also In re Vandaver, Adv. No. 99- 9188-C, slip op. at 6 (Bankr. N.D. Iowa April 10, 2000).

An exception to discharge for larceny under § 523(a)(4) requires proof that the debtor wrongfully and intentionally took another's property. In re Purdy, 231

B.R. 310, 312 (Bankr. E.D. Mo. 1999). The larceny exception cannot apply where the debtor's original possession of the things in question was lawful. Werner, 5 F.3d at 1172.

Based on the foregoing, the Court concludes that Plaintiff's claim is not excepted from discharge under § 523(a)(4). Debtor was not acting in a fiduciary capacity toward Plaintiff. Rather, this is a debtor-creditor relationship. Embezzlement has not occurred. The mowers were Debtor's property after the sale, not Plaintiff's. Thus, Debtor was not entrusted with property of another. Larceny has not been proved as Debtor's original possession of the mowers was lawful.

SECTION 523(a)(2)(A)

Section 523(a)(2)(A) excepts a debt from discharge if it is obtained by "false pretenses, a false representation, or actual fraud." Five elements must be satisfied before a debt will be excepted from discharge under § 523(a)(2)(A). The elements are:
(1) the debtor made false representations; (2) the debtor knew the representations were false at the time they were made; (3) the debtor made the representations with the intention and purpose of deceiving the creditor; (4) the creditor justifiably relied on the representations, Field v. Mans, 516 U.S. 59, 72 (1995); and (5) the creditor sustained the alleged injury as a proximate result of the representations having been made. In re Van Horne, 823 F.2d 1285, 1287 (8th Cir. 1987).

A determination of nondischargeability under § 523(a)(2)(A) requires a finding that Debtor knew that the representations were
false at the time he made them. In re Gramolino, 183 B.R. 565, 567 (Bankr. E.D. Mo. 1995). This standard is derived from the requirement that only actual fraud, and not fraud implied in law, satisfies § 523(a)(2)(A). In re Ophaug, 827 F.2d 340, 342 (8th Cir. 1987).

The Eighth Circuit B.A.P. has stated that "a false representation made under circumstances where a debtor should have known of the falsity is one made with reckless disregard for the truth, and this satisfies the knowledge requirement" of
§ 523(a)(2)(A). In re Moen, 238 B.R. 785, 790 (B.A.P. 8th Cir. 1999). This Court has found that a false representation or misrepresentation may be established by a showing of fraudulent intent or reckless disregard for the truth which is tantamount to a willful misrepresentation. In re Frye, No. 85-0064F, slip op. at 3 (Bankr. N.D. Iowa March 10, 1987) (Melloy, J.). Fraud is proved if it is shown that a false representation has been made recklessly, careless of whether it is true or false, and evidencing more than mere negligence. Palmacci v. Umpierrez, 121 F.3d 781, 788-89 (1st Cir. 1997). The court's focus should be on whether the surrounding circumstances or the debtor's actions appear so inconsistent with self-serving statements of intent that the proof leads the court to disbelieve the debtor. Id. at 789; see, e.g., In re Cook, 263 B.R. 249, 257-58 (Bankr. N.D. Iowa 2001) (finding the debtor had no intention to repay a loan, based on the circumstances, including his lack of credibility and his knowledge that he could not repay).

In weighing the credibility of witnesses, the Court must examine the evidence presented and evaluate the testimony, including variations in demeanor as well as changes in the tone of voice. Anderson v. City of Bessemer, 470 U.S. 564, 575 (1985). The Court can assess credibility based upon the content of the testimony as well as the Court's own experience with the way people act. In re Carrigan, 109 B.R. 167, 170 (Bankr.
W.D.N.C. 1989). Where two permissible views of the evidence exist, it is the responsibility of the Court to weigh the evidence presented including the credibility of the witnesses and make a choice between them. In re Waugh, 95 F.3d 706, 712 (8th Cir. 1996); In re Dullea Land Co., 269 B.R. 33, 36 (B.A.P. 8th Cir. 2001) (discussing bankruptcy court's evaluation of evidence and credibility of

witnesses).

Debtor repeatedly testified that the mowers are his and he always intended to pay for them. The Court finds that the surrounding circumstances are inconsistent with Debtor's statements of intent. Debtor initially represented to Plaintiff that he was getting a cash loan to pay for the mowers. The record establishes instead that Debtor's fiancee was getting the loan to do work on a home. Debtor was not a party to the loan and had no right to the proceeds. There was nothing to indicate Ms. Dibben's loan would produce sufficient funds to cover payment of the mowers. Debtor's purported reliance on this possible chance to obtain the funds to pay Plaintiff constitutes a misrepresentation by Debtor of his intent and ability to pay.

Debtor had at least three years of experience with the mowing contract with the City. He represented to Plaintiff that he would pay for the mowers after he got his contract payments. However, his own testimony reflects that he knew his net income from the contract would be insufficient to pay the $1,100 due. According to his bankruptcy schedules, Debtor nets only $888 per mowing season. This is insufficient to pay his debt to Plaintiff.

Based on the circumstances established by the evidence, Debtor's schedules in his bankruptcy case, and the Court's observations of Debtor's demeanor on the witness stand, the Court concludes Plaintiff has met his burden under § 523(a)(2)(A). The Court had the opportunity to observe Debtor's attitude and demeanor on the witness stand. Debtor affirmatively represented that he would have the funds available to pay for the mowers.
However, Debtor’s assertions that he intended to pay are belied by testimony indicating a complete inability to pay.

Debtor needed the mowers to satisfy his mowing contract. To obtain the mowers, he misrepresented his ability to pay to Mr.
Hamdorf. It is the conclusion of this Court that Debtor obtained the mowers under false pretenses. Plaintiff has established that Debtor intended to keep the mowers without payment through the mowing season. Having filed his Chapter 7 petition prior to the end of his mowing contract, he now intends to keep the mowers and discharge Plaintiff's claim for payment. The Court concludes Debtor never intended to pay Plaintiff for the mowers. Rather, he intended to possess the mowers without the ability to pay for them.

Debtor knowingly made false representations of his intent and ability to pay for the mowers with the intention of deceiving Plaintiff into letting him take the mowers without payment.
Plaintiff justifiably relied on Debtor's misrepresentations and was injured in the amount of $1,100 which Debtor agreed to pay. Plaintiff has met all the elements of § 523(a)(2)(A) by a preponderance of the evidence.

WHEREFORE, Plaintiff Robert Hamdorf's claim in the amount of $1,100 is excepted from discharge pursuant to § 523(a)(2)(A).

FURTHER, judgment shall enter accordingly.

SO ORDERED this 13th day of March, 2003.

PAUL J. KILBURG
CHIEF BANKRUPTCY JUDGE