UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF GEORGIA
WAYCROSS DIVISION

IN RE:	)CHAPTER 7
	)CASE NO. 99-50838-JDW
DANIEL L. O'STEEN III and	)
SUSAN O'STEEN,	)
	)
DEBTORS	)
	)
	)
AGRIBANK, FCB,	)
	)
PLAINTIFF	)
	)
VS.	)ADVERSARY PROCEEDING
	)NO. 99-5035-JDW
DANIEL L. O'STEEN III and	)
SUSAN O'STEEN,	)
	)
DEFENDANTS	)

BEFORE

JAMES D. WALKER, JR.

UNITED STATES BANKRUPTCY JUDGE

<u>COUNSEL:</u>

For Debtors: Andrew A. Taylor
P.O. Box 5010
St. Marys, GA 31558

For Agribank, FCB: David Wolfson
1010 Williams
Valdosta, GA 31601

MEMORANDUM OPINION

This matter comes before the Court on Complaint to Determine the Dischargeability of Debt filed by Agribank, FCB ("Agribank") against Daniel L. O'Steen III and Susan O'Steen ("Debtors") pursuant to 11 U.S.C. § 523(a)(2)(A) and (B).[1]

This is a core matter within the meaning of 28 U.S.C. § 157 (b)(2)(I). The Court held a trial on Agribank's Complaint on January 25, 2001. After considering the pleadings, evidence and applicable authorities, the Court enters the following findings of fact and conclusions of law in compliance with Federal Rule of Bankruptcy Procedure 7052.

Findings of Fact

Debtor is a farmer who in 1998 grew cotton, tobacco, and peanuts. In addition, Debtor raised pigs. However, in the latter part of 1998, Debtor's pig operation began to fail, and he became unable to pay one of his creditors, Agsouth. Subsequently, Debtor met with Agsouth representatives to try and restructure his loan. Out of this meeting, a balance sheet was created dated January 8, 1999, that reflected Debtor's assets, liabilities, and projected income.

Around this time, Johnny Reynolds ("Reynolds"), a branch manager for

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[1] The Court hereafter refers to Daniel L. O'Steen III individually as "Debtor".

Helena Chemical Company ("Helena"), spoke with Debtor about paying a debt he owed to Helena for supplies purchased in 1998. The debt was approximately $135,000, and Debtor informed Reynolds that he would not be able to pay it that month. Reynolds responded by telling Debtor he could apply for a loan through Agribank. Reynolds was familiar with the loan program because he had attended a seminar sponsored by Agribank for the purpose of instructing persons in Reynolds' position on how Agribanks's loan programs worked and how to receive and process loan applications. Manuals and documents were also provided to Reynolds by Agribank. Thereafter, at the urging of Reynolds, Debtor agreed to apply for a loan of $100,000. Later, before the loan was approved, Debtor agreed to give the loan money to Helena to pay his debt

Debtor met with Reynolds on February 1, 1999, and was given a loan application. During that meeting, Debtor filled out part of the application, signed it and gave it back to Reynolds. Debtor did not read the remainder of the application or supply the information necessary to complete the application. After Debtor left his office, Reynolds filled in the rest of the application, including information regarding Debtor's assets and liabilities, based on a prior year's financial statement that Helena had on file in another office. This financial statement was provided to Reynolds by facsimile and was difficult for him to read. As a result, the figures Reynolds put on the loan application were not an accurate reflection of the figures on the financial statement. In addition, the old financial statement did not accurately reflect Debtor's then current

financial status, because it was compiled prior to the failure of Debtor's pig operation.

Subsequently, Agribank processed Debtor's loan application using a score card system. This system is a computerized method of processing loan applications without any manual intervention. Credit evaluations are made based on the information contained in the loan application and the information provided by an independent credit bureau. This information is weighted 54% and 46%, respectively, in determining whether to approve a loan. Based on Debtor's loan application and the information provided by the credit bureau, Debtor received a score of 240. Anyone receiving a score of over 200 was approved for a loan.

After the loan was approved, Debtor attended a closing in April 1999 where he signed loan closing documents, including a document stating his loan application was accurate. However, a copy of the original loan application document was not included with the loan documents for him to review. He never saw the loan application after he signed it in Reynolds' office.

The loan proceeds were transferred to Helena following the closing. Helena used the funds to pay Debtor's debt. Debtor never received any disposable funds. Had Debtor's application accurately reflected his financial status, his score would have been 175, and his loan would not have been approved.

Debtor was indifferent to the consideration of the loan application. The

loan application was made at the insistence of Helena through its representative, Reynolds. The only benefit to approval of the application was Debtor's continuing in good standing with Helena. The Debtor would not have suffered any adverse consequences if the loan had not been approved. Debtor's net worth was not changed by the approval of the application. Neither was there any evidence presented as to any commitment by Helena to provide additional financing for Debtor's farm operations. Instead, the evidence shows that Debtor's prospects for continuing his farming operation were diminished by the failure of his hog operation. In essence, it was Helena, not the Debtor who instigated the loan application, prepared the documentation, and enjoyed the benefit of the proceeds. The requisite "intent to deceive" is lacking in this case as a matter of fact. There remains the question of whether intent can be inferred from these facts as a matter of law.

Some time after the loan closing, Northern Hog Operators filed a lawsuit against Debtor. This was the catalyst for Debtor to file for bankruptcy, and in August 1999, Debtor filed for a Chapter 7 bankruptcy with this Court. Upon reviewing the bankruptcy schedules filed by Debtor, Agribank discovered a discrepancy between the financial information provided to this Court and what was provided to them. They subsequently filed this action to determine the dischargeability of the debt against them under Sections 523(a)(2)(A) and (B).

Conclusions of Law

The purpose of the Code's discharge provisions is to allow insolvent debtors a chance to "make peace with their creditors, and enjoy 'a new opportunity in life with a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.'" Chase Manhattan Bank v. Ford (In re Ford), 186 B.R. 312, 316 (Bankr. N.D. Ga. 1995)(quoting Grogan v. Garner, 498 U.S. 279, 286 (1991)). However, this opportunity is only afforded to the honest, yet unfortunate, debtor. Id. In order to ensure that only honest debtors get the benefit of this fresh start, the Code provides exceptions to its discharge provisions. These exceptions are contained in 11 U.S.C. § 523.

The exceptions relevant to this case are contained in sections 523(a)(2)(A) and (B).[2] Because the fresh start is one of the Code's most important objectives, exceptions to discharge are to be narrowly construed in favor of the debtor.

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[2] Sections 523(a)(2)(A) and (B)provides in pertinent part:

> (a) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt – (2) for . . . an extension . . . of credit, to the extent obtained by – (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's . . . financial condition; (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 . . . credit reasonably relied; and (iv) that the debtor caused to be made or published with intent to deceive[.]

11 U.S.C. § 523(a)(2)(A) and (B).

Ford, 186 B.R. at 316 (citing Schweig v. Hunter (In re Hunter), 780 F.2d 1577, 1579 (11th Cir. 1986), abrogated by, Grogan, 498 U.S. 279 (establishing the standard of proof as preponderance rather than clear and convincing); Chevy Chase Bank v. Briese (In re Briese), 196 B.R. 440 (Bankr. W.D. Wis. 1996). In addition, the creditor objecting to the discharge of a debt has the burden of proving that the debtor is not entitled to have the debt discharged. Murphy & Robinson Inv. Co. v. Cross (In re Cross), 666 F.2d 873, 880 (5th Cir. 1982); Maco Fed. Credit Union v. Adair (In re Adair), 17 B.R. 456, 460 (Bankr. N.D. Ga. 1980).

Section 523(a)(2)(B)

In order for Agribank to prove that Debtors are not entitled to discharge the debt under Section 523(a)(2)(B), Agribank must satisfy four elements. They must show that the debt obtained by a writing is: (1) materially false, (2) respecting the debtor's financial condition, (3) on which the creditor to whom the debt is liable for such money, property, services, or credit reasonably relied, and (4) caused to be made or published by the debtor with the intent to deceive. Equitable Bank v. Miller (In re Miller), 39 F.3d 301 (11th Cir. 1994). The Court will now address each of these elements in turn.

The first element is whether the writing was materially false when it was created. A plaintiff satisfies this requirement in both amount and affect on the creditor receiving the financial statement. Enterprise Nat'l Bank of Atlanta v. Jones (In re Jones), 197 B.R. 949, 955 (Bankr. M.D. Ga. 1996). The falsehood

must affect the creditor's decision-making process. Id.

At trial, Agribank presented evidence that in February, 1999, Debtor submitted a written loan application for $100,000 to Agribank. The application stated that Debtor's net worth was approximately $3,600,000, and his gross income was $1,800,000. Debtor's actual net worth, as reflected in a financial statement generated on January 8, 1999, was approximately $500,000. In addition, Gary Grosgidiar of Agribank testified that had Debtor submitted accurate financial information with his actual net worth, his loan application would have been denied. Based on the extreme discrepancy in the financial information and the testimony that this information had a significant impact on Agribank's decision, the Court finds that the loan application to Agribank was materially false.

As to the second element, the Court finds that the statements in the loan application regarding assets, liabilities, and income, relate to the financial condition of Debtor. Therefore, Agribank has met its burden of proof for the second element of their Section 523(a)(2)(B) claim.

The third element requires Agribank to demonstrate that they reasonably relied on the financial information contained in Debtor's loan application. Reasonable reliance is determined on a case by case basis, and involves a balancing of the principle that the courts should not second guess the decisions of creditors to make loans or set loan policy and the idea that reasonable reliance should not allow creditors to ignore facts readily available

to them. Enterprise Nat'l Bank of Atlanta, 197 B.R. at 961. Several factors may be weighed in this balance. Whether the creditor follows its own established lending procedure can indicate whether the reliance was reasonable. Id. Whether the creditor used other resources, such as credit reports to verify the accuracy of financial information listed by a debtor can also be a factor. Archer, 55 B.R. at 178. Enterprise National Bank of Atlanta notes many other factors as well, such as whether the creditor had a close personal relationship with the debtor or had previous business dealings with the debtor, and whether there were any "red flags" that would have alerted the creditor that the financial information was inaccurate. Enterprise Nat'l Bank of Atlanta 197 B.R. at 961.

In this case, Agribank has a system for processing loan applications such as Debtor's. Agribank assesses applications by reviewing the loan application together with information from a credit bureau. The information is quantified so as to achieve a numeric score. A score over 200 means that the loan is approved, and under 200 means that it is denied. Debtor's application received a score of 240. There was no manual intervention in the system.

If the appropriate financial information been used, Debtor's score would have been 175. In addition, there was no evidence presented that Agribank had any knowledge that Reynolds, rather than Debtor, filled out the application or that Agribank had any knowledge that Debtor was not aware of the financial information provided in the application. Further, Agribank had no prior

relationship with Debtor. Weighing these factors in the balance, the Court concludes that Agribank reasonably relied on the financial information contained in the loan application.

The last element that Agribank must prove to establish its Section 523(a)(2)(B) claim is that Debtor made or published the writing with the intent to deceive Agribank. This is a factual determination in which the court looks at the totality of the circumstances to make its assessment. Miller, 39 F.3d at 305. Under this approach, a debtor's reckless indifference to the accuracy of the financial information in his loan application can be a factor in determining whether a debtor acted with fraudulent intent. Id; Archer, 55 B.R. at 179. However, the case law in this district has been unclear as to whether reckless indifference without more is enough to warrant a finding that the debtor acted with such intent. Because this issue is dispositive of the case before it, some clarification of the case law is necessary.

The Supreme Court has recently addressed the question of whether reckless indifference alone establishes intent under Section 523(a)(6) in Kawaauhau v. Geiger, 118 S.Ct. 974 (1998).[3] There, the Court held that debts

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[3] Sections 523(a)(6)states:

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

11 U.S.C. § 523(a)(6).

arising out of reckless or negligent conduct do not establish that the injury therefrom was willful or malicious and, as a result, do not establish an exception to discharge under Section 523(a)(6). Id. at 978. In arriving at this conclusion, the Court reasoned that the language used in Section 523(a)(6) is that of intentional tort and that intentional torts require a showing of intent as to the consequences of actions, not just intent as to the actions themselves. Id. at 977. The Court went on to note that a "construction so broad [as to include reckless conduct] would be incompatible with the well-known guide that exceptions to discharge should be confined to those plainly expressed." Id.(internal quotation marks omitted). Similarly, Section 523(a)(2) uses the language of intentional tort. Accordingly, reckless conduct under this section should not warrant a finding of intent to deceive because the evidence does not show that the debtor actually intended the misrepresentation that resulted.

In the case at hand, Debtor testified that he did not intend to deceive Agribank, and that the deception was the result of an error made by Reynolds. Debtor further testified that he had no reason to suspect that an error had been made. He thought he had done what he was told to do by Reynolds. Accordingly, Debtor argued that his failure to discover the error or fill out the loan application himself does not amount to intent to deceive.

Debtor signed a partially blank loan application with the understanding that Helena's employee, Reynolds, who had Debtor's prior financial statement on file, would fill in the financial information from that statement. Reynolds

was fully aware that the financial information available to him was not current. This fact coupled with the fact that Reynolds solicited the application and received the loan proceeds as payment on the account with Helena is decisive. Debtor was not invited by Reynolds to review the financial information that was provided in the application before the completed application was sent to Agribank. Furthermore, Debtor was not provided with a copy of the completed loan application document to review before being asked to sign the loan closing documents affirming the truth of the application. Perhaps a knowing renewal of the misrepresentation might point to a different result.

The Court finds that Debtor's conduct was reckless. However, applying the reasoning in Geiger and noting that exceptions to discharge are to be narrowly construed in favor of the debtor, the Court does not find that such conduct equates to an exception from discharge under Section 523(a)(2)(B) because Agribank has presented no evidence that Debtor intended the resulting misrepresentation.

In reaching this conclusion, the Court is mindful of the seemingly contradictory holding of Archer. Archer, 55 B.R. at 179. However, in Archer, the debtor's reckless actions were construed as intentional conduct because the debtor signed a blank loan application knowing that the third party filling out the application did not have any financial information on Debtor. As a result, the debtor had no reasonable basis for believing that the financial information provided on his behalf would be accurate. Id. Without such reasonable basis,

the evidence tends to indicate that the debtor intended the misrepresentation that resulted. In contrast, Debtor in this case knew that Reynolds had a financial statement from a prior year with which to fill out the loan application. Accordingly, Debtor had a basis for believing that Reynolds would provide accurate financial information, thereby providing no indication that Debtor intended the injury. The fact that this information was out of date does not appear to have been considered by Debtor. It appears instead to have been an option proposed by Reynolds and accepted by Debtor.

The holding in Archer is distinguishable from this case. The distinction between the cases is subtle but important. In Archer, it does not appear that the court was faced with the dilemma of finding intent as a matter of law where intent as a matter of fact was absent. Agribank having not satisfied the burden of proving its Section 523(a)(2)(B) claim, the Court now turns to Agribank's Section 523(a)(2)(A) claim.

Section 523(a)(2)(A)

To deny the discharge of a debt under Section 523(a)(2)(A), this Court has previously held that three elements must be satisfied: (1) the debtor must have made a false representation with the purpose and intent to deceive the creditor; (2) the creditor must have justifiably relied on the representation of the debtor; and (3) the creditor must have suffered a loss as a result of that reliance. Boyd Gambling Corp. v. Hall (In re Hall), 228 B.R. 483, 488 (Bankr. M.D. Ga. 1998). The burden of proving these elements is on the creditor. Id.

For the reasons stated above, this Court finds that Debtor did not make false representations with the intent to deceive Agribank. Thus, even though creditor satisfies the second and third requirements of this section, its claim must fail.

Conclusion

Accordingly, Agribank has not satisfied the burden of proving its Section 523(a)(2)(A) claim or its Section 523(a)(2)(B) claim, and the Court finds that the debt owed to Agribank is dischargeable.

An order in accordance with this opinion will be entered on this date.

Dated this 11th day of April, 2001.

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James D. Walker, Jr.
United States Bankruptcy Judge

CERTIFICATE OF SERVICE

I, Cheryl Spilman, certify that the attached and foregoing have been served on the following:

Andrew A. Taylor
P.O. Box 5010
St. Marys, GA 31558

David Wolfson
1010 Williams
Valdosta, GA 31601

This 11th day of April, 2001.

____
Cheryl Spilman
Deputy Clerk
United States Bankruptcy Court

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF GEORGIA
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	)
DEFENDANTS	)

ORDER

In accordance with the memorandum opinion entered on this date, it is hereby

ORDERED that Agribank's objection to discharge be DENIED.

SO ORDERED this 11th day of April, 2001.

James D. Walker, Jr.
United States Bankruptcy Judge

CERTIFICATE OF SERVICE

I, Cheryl Spilman, certify that the attached and foregoing have been served on the following:

Andrew A. Taylor
P.O. Box 5010
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This 11th day of April, 2001.

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Cheryl Spilman
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