

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE EASTERN DISTRICT OF TENNESSEE

In re

MICHAEL WALTER BROWN,  
  
Debtor.

No. 98-22827  
Chapter 7

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SOUTHEAST FINANCIAL OF  
JEFFERSON CITY, INC.,

Plaintiff,

vs.

MICHAEL WALTER BROWN,

Defendant.

Adv. Pro. No. 99-2005

M E M O R A N D U M

APPEARANCES :

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MARCIA PHILLIPS PARSONS  
UNITED STATES BANKRUPTCY JUDGE

This adversary proceeding is before the court on the motion for summary judgment filed by the plaintiff, Southeast Financial of Jefferson City, Inc. ("Southeast"), on July 30, 1999. As discussed below, the motion will be denied, the court having concluded that genuine issues of material fact remain as to various elements of 11 U.S.C. § 523(a)(2)(B). This is a core proceeding. See 28 U.S.C. § 157(b)(2)(I).

I.

From the facts which can be gleaned from the pleadings, it appears that on or about March 19, 1998, the debtor signed a note and security agreement, promising to pay Southeast the sum of \$3,177.84 over 24 months at the rate of \$132.41 per month.<sup>1</sup> Subsequently, on September 22, 1998, the debtor borrowed the additional sum of \$702.69 from Southeast. This amount plus the balance on the previous loan were consolidated to make a new loan in the amount of \$4,152.00, to be repaid at the rate of \$173.00 per month over 24 months.

On November 9, 1998, the debtor filed for chapter 7 relief, initiating the case underlying the present adversary proceeding.

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<sup>1</sup>The principal amount of the loan was \$2,384.04. Of that amount, only \$777.48 was paid directly to the debtor. Another \$1,291.03 was paid on the debtor's behalf and the remaining \$315.53 went to purchase various types of insurance.

Thereafter, on February 16, 1999, Southeast filed its complaint seeking a determination that the obligation owed Southeast by the debtor was nondischargeable under 11 U.S.C. § 523(a)(2)(B) because the debtor allegedly obtained the September 22, 1998 loan through the use of a false written statement regarding his financial condition. In support of its motion for summary judgment on this issue, Southeast has submitted the affidavit of Peggy Harville, a branch manager of Southeast and the employee of Southeast who dealt with the debtor in connection with the September 22 loan. Southeast has also submitted the debtor's deposition transcript dated June 24, 1999, and the debtor's answers as supplemented to certain interrogatories propounded by Southeast, along with copies of the loan documentation in question.

The written statement concerning the debtor's financial condition which is the crux of Southeast's complaint is the "Renewal Money Request" signed by the debtor in connection with the September 22 loan. According to the affidavit of Ms. Harville, the Renewal Money Request is a Southeast form "specifically designed for existing borrowers to apply for a new or refinance loan." The top third of the one-page form has space to insert personal information on the borrower, including name, address, phone number, employer, length of employment, and

salary. The middle third of the page has a one-line space entitled "Southeast A/C" in which the borrower's current account information with Southeast may be listed, a one-line space to note whether the borrower rents or owns his own home and the monthly payment, and half a dozen lines presumably to list other debts of the borrower. The bottom third of the form has lines for the gross amount of the loan approved, the terms, the amount of the cash advanced, the date approved, the signature of approving officer, and the purpose of the renewal, along with a small computation area which compares the borrower's total monthly net income to his or her monthly payments to determine the debt to income ratio. At the very bottom of the page are lines for the applicants' signatures along with this printed statement: "I hereby authorize the person to whom this application is made, or any credit bureau or other investigative agency employed by such person, to investigate the references herein listed or statements or other data obtained from me or from any other person pertaining to my credit and financial responsibility."

Ms. Harville states in her affidavit that "[i]t is the policy of Southeast Financial of Jefferson City, Inc. to base its determination of whether to approve or deny a Renewal Money Request from an applicant, whose existing loan is in good

standing, primarily on the debt to income ratio of the applicant as stated on the Renewal Request." She additionally states that "[i]t is also the policy of Southeast Financial of Jefferson City, Inc., when reviewing Renewal Money Requests to rely entirely to [sic] information provided by borrowers who have a recent prior loan with Southeast Financial of Jefferson City, Inc.,[,] which loan is in good standing, unless facts become known which indicate additional inquiry is necessary."

From the debtor's deposition testimony and the affidavit of Peggy Harville, it appears that Ms. Harville interviewed the debtor to obtain the necessary information to complete the Renewal Money Request and, thereafter, the debtor signed the form. In her affidavit, Ms. Harville states that in completing the request, she asked the debtor to provide her with a complete list of all debts owed by him at the time and that in response, he named the creditors listed on the form, namely Heilig-Myers, Fifth Third Bank, and Southern Finance, along with the monthly payments owed to each.<sup>2</sup> Ms. Harville stated that she used this information to compute the debtor's income to debt ratio for the

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<sup>2</sup>In addition to the name of the creditors and monthly payments, the Renewal Money Request form also has space to list the date, amount, date of last payment and balance for each of the various obligations. Except for the debt to Southeast, none of this information was filled in with respect to any of the listed obligations.

purpose of determining whether to grant his application. Based on her calculations that the debtor had an excess income over debt percentage of 51%<sup>3</sup> and the debtor's "apparent steady employment history" as reflected by the fact that he was still employed with the employer he listed on the original loan, Ms. Harville determined that the debtor was qualified for the additional loan.

According to debtor's interrogatory answers, it appears that when the September 22 loan was made, the debtor, in addition to Southeast and the three other creditors listed on the request form, also was obligated to Pioneer Credit, Providian Processing Service, Security Finance, and Credit Store, for monthly payments of \$60.00, \$100.00, \$60.00, and \$100.00, respectively. Ms. Harville states in her affidavit that "[i]f Michael Walter Brown had disclosed the additional four (4) creditors and respective monthly payments as set forth in his Supplemental

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<sup>3</sup>Ms. Harville states in her affidavit that she "arrived at this percentage by dividing the income amount remaining after monthly debt payments (including the payment on the new loan, but excluding the old loan) by the total income." The monthly net income is listed at \$2,320.00 and the monthly payments total \$1,229.00. Using Ms. Harville's formula, the difference between \$2,320.00 and \$1,229.00, *i.e.*, \$1,091.00, would be divided by \$2,320.00, which based on the court's computation, produces a quotient of 47%, rather than 51%. Because Ms. Harville's affidavit does not set forth Southeast's guidelines in extending credit, the court is unable to determine whether the debtor would have still obtained the loan if Ms. Harville's computation had shown 47% rather than 51%.

Answers to Interrogatories, the percentage would have only been 39%, which would not have qualified him for the new loan applied for, despite his employment history."

Based on the foregoing, Southeast contends that the debtor signed a written statement concerning his financial condition, that the statement is materially false, that the debtor made such statement either with intent to deceive Southeast or with reckless disregard for the actual facts, and that Southeast reasonably relied upon the debtor's false statement. Accordingly, Southeast requests summary judgment in its favor. The debtor has not responded to the motion.

## II.

"In order to establish the nondischargeability of a debt [under § 523(a)(2)(B)], the plaintiff must show that the debt was obtained by use of a writing that:

- (1) was materially false;
- (2) respecting the debtor's or an insider's financial condition;
- (3) on which the plaintiff reasonably relied; and
- (4) that the debtor caused to be made or published with the intent to deceive."

*First Nat'l Bank of Centerville v. Sansom*, 1998 WL 57307 at \*\*2

(6th Cir. February 2, 1998)(citing 11 U.S.C. § 523(a)(2)(B)). "Section 523(a)(2)(B) applies not only to documents styled as 'financial statements,' but to any false statements made in written loan applications." *F.D.I.C. v. Lefevre (In re Lefevre)*, 131 B.R. 588, 593 (Bankr. S.D. Miss. 1991). Furthermore, "[a] written statement does not have to be physically prepared by a debtor in order to satisfy the in writing requirement of § 523(a)(2)(B). [Citation omitted.] The in writing requirement ... is satisfied if the existence of the written statement was either signed, adopted and used or caused to be prepared by the debtor." *First Int'l Bank v. Kerbaugh (In re Kerbaugh)*, 162 B.R. 255, 262 n.3 (Bankr. D.N.D. 1993). Accordingly, the Renewal Money Request form signed by the debtor meets § 523(a)(2)(B)'s requirement of a writing respecting the debtor's financial condition.

With respect to the element of material falsity, "[a] materially false statement has been defined as: one that contains an important or substantial untruth. The measuring stick of material falsity is whether the financial institution would have made the loan if the debtor's true financial condition had been known." *First Nat'l Bank of Centerville v. Sansom (In re Sansom)*, 224 B.R. 49, 54 (Bankr. M.D. Tenn. 1998)(quoting *Fleming Co. v. Eckert (In re Eckert)*, 221 B.R. 40,

44 (Bankr. S.D. Fla. 1998)). "[T]he failure to list, concealment or understatement of assets or liabilities is ordinarily a misstatement considered 'material.'" *Id.* (citing *In re Poskanzer*, 143 B.R. 991 (Bankr. D.N.J. 1992)).

Southeast alleges that the Renewal Money Request was false because it did not list all of the debtor's liabilities and that the falsity is material because the debtor would not have qualified for the loan if all of his debts had been disclosed. Although the evidence certainly establishes that all of the debtor's liabilities were not included on the request form, it is not clear that all of the liabilities were required to be listed. There is no heading on the form that directs the applicant to list all debts or other such language mandating such a listing. *See, e.g., In re Kerbaugh*, 162 B.R. at 262 (application required applicants to provide "true and complete" information regarding their monthly income, monthly rental payments and credit information); *Community Nat'l Bank & Trust Co. of New York v. Aycott (In re Aycott)*, 54 B.R. 578, 579 (Bankr. E.D.N.Y. 1985)(application form states "List all debts including those accounts on which you are a co-maker, guarantor or endorser"). Instead, on Southeast's form there is only a graph: along the left are three lines with headings for information concerning an existing Southeast account, the

borrower's rental or mortgage payment, and an automobile loan; across the top are columns labeled "ARTICLE, DATE, AMOUNT, TERMS, DATE LAST PAYMENT, BALANCE, and HOW??" ; and there are two subheadings under the word "TERMS" labeled "NO. MOS." and "NO. PYMTS." There is no language located anywhere on the form whereby the applicant must certify or state that the information contained therein is complete or that it represents a full and accurate picture of the applicant's financial information. See, e.g., *Horowitz Finance Co. v. Hall (In re Hall)*, 109 B.R. 149, 154 (Bankr. W.D. Penn. 1990)(application was sworn to on its face as being accurate). Ms. Harville does state in her affidavit that in completing the form, she instructed the debtor to provide a complete list of all debts owed by him at the time. However, the debtor testified to the contrary during his deposition. In response to the question, "You've listed quite a few people there that weren't listed on your application for the loan. Any reason for that?" the debtor responded:

I guess at the time, they just cut me short. They said that's enough, you know, because I feel that as anxious I am to get the money, they're even more anxious to give me the money, because I guess I was a good payer. That's the way I felt, you know. Besides that, if I remember that application, it's not long enough to list everybody you know...everybody you owe.

At the another point in the deposition, the following exchange took place:

Question: But you weren't behind on your payments to the other creditors? There wasn't a reason that you didn't disclose those to Southeast Financial at the time you were getting the loan?

Answer: No, sir. Like I said earlier, I think they actually just cut me short, like that's enough, you know. It was like...like I said, as anxious as I was to get the money, they were just as anxious to give me the money.

Question: So, you're saying that you think that they told you "That's enough, I don't need to know anymore of your creditors"?

Answer: No, they just more or less said that's good enough. That's enough, you know.

Question: That's enough, when you were telling them who you owed, they said, "That's enough I don't need to know anymore"?

Answer: Really, I guess when I was giving them a list of my big time creditors, I guess, you know, they were like that's good enough, you know. So I guess I was in good standing, you know.

Because the debtor's deposition testimony contradicts Ms. Harville's affidavit, a genuine issue of material fact exists on the issue of whether the Renewal Money Request was in fact false. The completed form is false only if the debtor was directed or understood that he was required to reveal all of his liabilities to Ms. Harville. Otherwise, the form is not false since there is no representation thereon that all of the debtor's obligations are listed.

The above colloquy also tends to cast doubt on Southeast's assertion that it actually and reasonably relied on information

given it by the debtor in making the loan. See *Bank One, Lexington, N.A. v. Woolum (In re Woolum)*, 979 F.2d 71, 75-76 (6th Cir. 1992)(there are two components to the reliance element in a § 523(a)(2)(B) action: actual reliance and reasonable reliance). The United States Supreme Court explained in *Field v. Mans*, 516 U.S. 59, 76-77, 116 S. Ct. 437, 446-447 (1995), that Congress may have placed the reasonable reliance requirement in § 523(a)(2)(B) because it was concerned that consumer finance companies were encouraging borrowers to submit false or incomplete loan applications for the purpose of insulating the lender in the event of the applicant's bankruptcy. See *Redburn v. Armbrustmacher (In re Redburn)*, 202 B.R. 917, 927 n.24 (Bankr. W.D. Mich. 1996). The Supreme Court quoted the following passage from the House Report on the 1978 Act:

It is a frequent practice for consumer finance companies to take a list from each loan applicant of other loans or debts that the applicant has outstanding. While the consumer finance companies use these statements in evaluating the credit risk, very often the statements are used as a basis for a false financial statement exception to discharge. The forms that the applicant fills out often have too little space for a complete list of debts. Frequently, a loan applicant is instructed by a loan officer to list only a few or only the most important of his debts. Then, at the bottom of the form, the phrase "I have no other debts" is either printed on the form, or the applicant is instructed to write the phrase in his own handwriting.

*Field v. Mans*, 516 U.S. at 77, 116 S. Ct. at 447 n.13 (quoting H.R. REP. NO. 95-595, at 130-131, reprinted in 1978 U.S.C.C.A.N. 5787, 6091.

Nevertheless, the court does not conclude that a consumer finance company such as Southeast can never establish actual and reasonable reliance with respect to an application such as the one in question as some courts have held. See *In re Redburn*, 202 B.R. at 927 n.24 ("[A] finance company that claims it relied solely upon a debtor's written loan application in extending a loan will have failed to show reasonable reliance."). Rather, the reasonableness of the reliance will be judged by this court based on the totality of the circumstances. See *In re Sansom*, 224 B.R. at 55.<sup>4</sup> Relevant considerations in this regard include:

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<sup>4</sup>In the case of *Security Federal Credit Union v. Carter (In re Carter)*, 78 B.R. 811, 818 (Bankr. E.D. Mich. 1987), the court stated the following:

It is appropriate ... that bankruptcy judges look with a jaundiced eye upon plaintiffs' claims of being deceived by false financial statements when: (a) the proofs indicate that the financial statement is unduly restrictive with respect to size and completion requirements, (b) the loan officer completes the application in his or her own handwriting, giving the loan applicant no time to go home and carefully prepare a list of his debts, but instead requires him to dictate them "off the cuff" in the rush of the application process, or (c) a financial statement purports to require information (like addresses and account numbers, etc.), but the creditor disregards the applicant's failure to provide it, thus leading

(continued...)

1. The existence of prior business dealings between the parties;
2. Whether any warnings would have alerted a reasonably prudent person to the debtor's misrepresentations;
3. Whether minimal investigation would have uncovered the inaccuracies; and
4. The creditor's standards for evaluating creditworthiness and the standards or customs in the industry.

*Id.* (citing 4 COLLIER ON BANKRUPTCY ¶ 523.08[2][d](15th ed. 1998)).

Furthermore, "[r]easonable reliance is not a rigorous standard" and "operates to bar a discharge only where the creditor's reliance was so unreasonable as to negate the existence of actual reliance." *In re Sansom*, 224 B.R. at 55.

To support its assertion that Southeast reasonably relied upon the application, Ms. Harville states in paragraphs 11 and 12 of her affidavit that:

Mr. Brown's previous loan with Southeast Financial of Jefferson City, Inc. was in good standing on September 22, 1998, and the records of Southeast Financial of Jefferson City, Inc. indicated that he had been honest and forthcoming with regard to his previous disclosure of debt and his promises to repay. In my judgment, as manager and loan officer, based on the information available on September 22, 1998, no other inquiry seemed necessary, nor was it required by the normal business policies, practices and procedures of

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<sup>4</sup>(...continued)

the borrower to believe that the form's requirements need not be seriously considered. Moreover, if a credit bureau report can be feasibly obtained, the trier of fact may fairly expect that it would be obtained unless good reason exists not to.

Southeast Financial of Jefferson City, Inc.

In light of the assertions by the debtor during his deposition that in deciding whether to make the loan, Southeast was more interested in the debtor's payment history than a full picture of his financial condition, a genuine issue of material fact also exists with respect to whether Southeast actually and reasonably relied on the "representations" in the application. Similarly, the debtor's deposition testimony raises a genuine issue as to whether the omissions from the application were made with the intent to deceive or with gross recklessness. See *In re Sansom*, 224 B.R. at 57 n.11 ("gross recklessness is not characterized by inadvertence" but means "flagrant, indicating mental attitude of the debtor that would be the evidentiary equivalent of intent to deceive").

### III.

Fed. R. Civ. P. 56, as incorporated by Fed. R. Bankr. P. 7056, mandates the entry of summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." In ruling on a motion for summary judgment, the inference to be drawn from the

underlying facts contained in the record must be viewed in a light most favorable to the party opposing the motion. See *Schilling v. Jackson Oil Co. (In re Transport Assoc., Inc.)*, 171 B.R. 232, 234 (Bankr. W.D. Ky. 1994)(citing *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 106 S. Ct. 2505 (1986)). See also *Street v. J.C. Bradford & Co.*, 886 F.2d 1472 (6th Cir. 1989). Because genuine issues of material fact remain in this proceeding, summary judgment is inappropriate. Accordingly, an order will be entered in accordance with this memorandum denying Southeast's motion for summary judgment.

FILED: September 2, 1999

BY THE COURT

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MARCIA PHILLIPS PARSONS  
UNITED STATES BANKRUPTCY JUDGE