

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF TENNESSEE

In re:

No. 97-11914
Chapter 7

RANDY BUTLER, fdba Modern
Way Rentals of Winchester

Debtor

CASE CREDIT CORPORATION

Plaintiff

v

Adversary Proceeding
No. 97-1131

RANDY BUTLER, fdba Modern
Way Rentals of Winchester

Defendant

MEMORANDUM

Appearances: Nicholas W. Whittenburg and India Henson, Miller & Martin,
Chattanooga, Tennessee, Attorneys for Plaintiff

Robert S. Peters, Swafford, Peters & Priest, Winchester, Tennessee,
Attorneys for Defendants

HONORABLE R. THOMAS STINNETT
UNITED STATES BANKRUPTCY JUDGE

The complaint filed by Case Credit Corporation (“Case Credit”) alleges that Mr. Butler – the debtor – owes it a debt that can not be discharged in his bankruptcy case. The question now before the court is whether to grant or deny Case Credit’s motion for summary judgment. The complaint relies on Bankruptcy Code § 523(a)(2) and § 523(a)(6). 11 U.S.C. § 523(a)(2) & (6). Section 523(a)(2) excepts from discharge a debt for obtaining credit, services, or various kinds of property by fraud or false pretense. Section 523(a)(6) excepts from discharge a debt for willful and malicious injury to a person or the property of another person; this includes willful and malicious conversion of another person’s property. *Vulcan Coals, Inc. v. Howard*, 946 F.2d 1226 (6th Cir. 1991).

The basic allegations of the complaint can be summarized as follows:

A corporation, Modern Way Rentals of Winchester, bought a used backhoe with financing from the seller.

Modern Way executed an installment contract that granted the seller a security interest in the backhoe to secure payment of the debt. Mr. Butler guaranteed payment of the debt.

The installment contract and Mr. Butler’s guaranty were assigned to Case Credit.

The installment contract provided that the purchaser, Modern Way, could sell the backhoe only with Case Credit’s permission. Modern Way sold the backhoe without Case Credit’s permission.

Neither Modern Way nor Mr. Butler paid the proceeds of the sale to Case Credit. The backhoe was worth more than the amount of the debt.

Case Credit sued Mr. Butler in state court. The complaint in the state court alleged that Mr. Butler “did knowingly, intentionally, fraudulently, and maliciously transfer the Backhoe which proximately damaged Case Credit.”

Mr. Butler’s failure to respond to the complaint resulted in a default judgment for Case Credit and against Mr. Butler in the amount of \$16,000.25.

This debt is not dischargeable under § 523(a)(2) because Mr. Butler committed fraud by selling the backhoe without Case Credit’s permission and not paying the proceeds over to Case Credit.

This debt is not dischargeable under § 523(a)(6) because Mr. Butler willfully and maliciously converted Case Credit’s property, the backhoe and the sale proceeds.

Case Credit’s motion for summary judgment has two parts. The court begins with the second part. It relies on the default judgment by the state court and the doctrine of collateral estoppel. Case Credit contends the judgment is based on fraud or willful and malicious conversion of Case Credit’s collateral by the debtor. Furthermore, according to Case Credit, the judgment collaterally estops the debtor from proving otherwise.

The court applies Tennessee law to determine the effect of the default judgment; under Tennessee law the default judgment may have the effect of collateral estoppel. *Bay Area Factors v. Calvert (In re Calvert)*, 105 F.2d 315 (6th Cir. 1997).

The debtor contends, however, that the judgment does not have collateral estoppel effect because he was never properly served with the summons and complaint in the state court action.

Tennessee follows the rule that a default judgment is not effective against the defendant if he proves that he was not served with the summons and complaint. *Overby v. Overby*, 224 Tenn. 523, 457 S.W.2d 851 (1970); *Hawley v. Lavelle*, 602 S.W.2d 499 (Tenn. Ct. App. 1980); *Johnson v. McKinney*, 32 Tenn.App. 484, 222 S.W.2d 879 (1949).

The affidavit of the process server states that he served the complaint and summons by leaving copies at the debtor's dwelling house or usual place of abode with a person of suitable age and discretion, specifically the debtor's wife. Under Tennessee law, service can be made in this way, but only when the defendant is evading or attempting to evade service. *Tenn. R. Civ. P.* 4.04(1). The affidavit does not state that the debtor was evading or attempting to evade service. Thus, the affidavit does not establish effective service of process as required by Tennessee law.

The debtor, however, may not be allowed to raise this question. Paragraph 20 of Case Credit's complaint in this court alleges valid service of process in the earlier state court action. Paragraph 20 the Mr. Butler's answer admits this allegation. The debtor is bound by this admission unless the court allows him to amend the answer to change the admission to a denial. Mr. Butler has not filed a motion to amend as required by the rules. *Fed. R. Bankr. P.* 7015; *Fed. R. Civ. P.* 15(a).

The facts presently before the court do not reveal any reason why the court would not allow such an amendment if the defendant files a motion. Rule 15(a) provides that leave to amend “shall be freely given when justice so requires.” *Fed. R. Bankr. P.* 7015; *Fed. R. Civ. P.* 15(a).

Though this proceeding is near to trial, there has been no long delay by Mr. Butler in raising the issue. There could be no long delay in light of how quickly this matter has progressed toward trial. Case Credit filed its complaint on July 8. Mr. Butler filed his answer on July 30. The court entered an order and notice of trial on August 8. It set the trial for December 2. Case Credit filed its motion for summary judgment on October 3. Mr. Butler filed his response on November 18. The response was later than required by the order and notice of trial; it required a response within 20 days. Nevertheless, the court does not think this delay was significant. Delay is a cause for not allowing an amendment only if it results in prejudice to the opposing party. *Security Ins. Co. v. Kevin Tucker & Associates, Inc.*, 64 F.3d 1001 (6th Cir. 1995).

The court does not see any substantial prejudice to Case Credit as a result of the delay. The factual issues raised by Mr. Butler’s response are simple. An insignificant amount of additional work by Case Credit should reveal whether the issue is worth pursuing. Allowing the amendment does not mean that Case Credit will lose at trial. It only means there is a factual issue as to whether Case Credit obtained valid service of process on Mr. Butler in the state court case. Amendments are freely allowed so that the outcome of a lawsuit will be determined by the true facts, not gamesmanship. 6 Charles

A. Wright, *et al.*, *Federal Practice and Procedure* § 1471 at 505-507 (2d ed. 1990). A mistake by the defendant or his lawyer may give the plaintiff the prospect of easy victory. The court may take away that prospect by allowing the defendant to amend his answer and requiring the plaintiff to prove the true facts instead. This is not the kind of prejudice to the plaintiff that should usually lead the court to disallow such an amendment. *Cf. Beeck v. Aquaslide 'N' Dive Corp.*, 562 F.2d 537 (8th Cir. 1977); *Adkins v. International Union of Electrical, Radio and Machine Workers*, 769 F.2d 330 (6th Cir. 1985).

Furthermore, the record reveals that both parties have prepared for a trial to determine the facts. Case Credit has not assumed the state court judgment would automatically entitle it to summary judgment, if only there is no dispute as to service of process in the state court action. Finally, the record at this point does not show any dilatory motive or bad faith by Mr. Butler or his counsel.

In this situation, an amendment should be allowed under the standards set down by the Supreme Court in *Foman v. Davis*, 371 U.S. 178, 83 S.Ct. 227, 230, 9 L.Ed.2d 222 (1962); *see also General Electric Co. v. Sargent*, 916 F.2d 1119 (6th Cir. 1990); *Estes v. Kentucky Utilities Co.*, 636 F.2d 1131 (6th Cir. 1980). Two other Sixth Circuit cases can be distinguished on the ground that allowing the amendment to the answer would have created substantial prejudice to the plaintiff. *United States v. Midwest Suspension and Brake*, 49 F.3d 1197 (6th Cir. 1997); *Hayden v. Ford Motor Co.*, 497 F.2d 1292 (6th Cir. 1974).

Another Sixth Circuit case says that an amendment to an answer to change an admission to a denial should be allowed only when the defendant proves “exceptional circumstances.” *Ferguson v. Neighborhood Housing Services of Cleveland, Inc.*, 780 F.2d 549, 551 (6th Cir. 1986). This seems to be inconsistent with the direction in Rule 15 that leave to amend should be “freely given when justice so requires.” *Fed. R. Bankr. P.* 7015; *Fed. R. Civ. P.* 15(a). It may also be inconsistent with the Supreme Court’s decision in *Foman v. Davis*, 371 U.S. 178, 83 S.Ct. 227, 230, 9 L.Ed.2d 222 (1962). Thus, the court takes the *Ferguson* decision to mean only that substantial prejudice to the plaintiff will often be the obvious result of allowing the defendant to change an admission to a denial. In this proceeding, the facts do not lead to that conclusion.

The court will not direct Mr. Butler to file a motion to amend, but without a motion to amend, the court will deal with the summary judgment motion based on the record as it now stands.

The court turns now to the first part of Case Credit’s motion for summary judgment. It deals with the debtor’s defenses to the complaint in this court. The complaint alleges that Case Credit did not know the debtor sold the backhoe until long after the fact. The debtor’s answer denies this allegation; the answer in effect asserts that Case Credit knew of the sale. The answer also denies that the debtor’s intent was malicious or fraudulent; the answer states that the debtor always intended to pay the debt. Finally, the debtor denies the amount of damages asserted by Case Credit.

In support of its motion for summary judgment, Case Credit submitted the affidavit of Richard A. Miller. Mr. Miller states that he is a legal account specialist for Case Credit, that he has knowledge of the records relating to the accounts of the debtor and Modern Way Rentals of Winchester, Inc., and that the records are in his care, custody and control. Mr. Miller also states that he has personal knowledge of the facts stated in his affidavit.

In his affidavit Mr. Miller states that Case Credit first learned of the transfer of the backhoe at the meeting of creditors in the debtor's earlier Chapter 13 case. Mr. Miller also states that Case Credit was not notified of the transfer and did not consent to it. Mr. Miller's affidavit does not state that he has investigated and found no employee or agent of Case Credit who had prior notice of the transfer or who consented to it. Thus, Mr. Miller's affidavit means two things: (1) Mr. Miller was not notified of the transfer and did not consent to it on behalf of Case Credit, and did not learn of the transfer until the meeting of creditors in the earlier Chapter 13 case; (2) the records of Case Credit do not reveal that it was notified of the transfer or that it consented to the transfer, but they do reveal that Case Credit learned of the transfer as a result of the meeting of creditors in the debtor's earlier Chapter 13 case. This is not sufficient to overcome the debtor's claim that Case Credit had knowledge of the transfer.

Of course, this raises the question of whether mere knowledge of the transfer by Case Credit would prevent it from being fraudulent or willful and malicious. But the court will not delve into that question. The debtor's answer raises the question of his intent

in general. It also raises the question of whether the damages alleged by Case Credit are the correct amount. Furthermore, the trial date is only one week away. The court will deny summary judgment under the first part of Case Credit's motion. There appears to be a genuine issue of material fact. *Fed. R. Bankr. P. 7056; Fed. R. Civ. P. 56(c)*. Even if a careful review should show that there is no genuine issue of material fact, at this late date the court has discretion to deny the summary judgment motion in favor of hearing the evidence. This is particularly appropriate in this case. The issues are few, they are simple, and they should not take long to try. On the other hand, granting summary judgment at this point would be likely to prolong this proceeding beyond the date currently set for trial. *Lisle Mills, Inc. v. Arkay Infants Wear*, 90 F.Supp. 676, 678 (E. D. N. Y. 1950).

This Memorandum constitutes findings of fact and conclusions of law as required by Fed. R. Bankr. P. 7052.

At Chattanooga, Tennessee.

BY THE COURT

entered 11/25/1997

R. THOMAS STINNETT
UNITED STATES BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
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Defendant

ORDER

In accordance with the court's Memorandum Opinion entered this date,

It is ORDERED that the plaintiff's Motion for Summary Judgment is DENIED.

ENTER:

BY THE COURT

entered 11/25/1997

R. THOMAS STINNETT
U.S. BANKRUPTCY JUDGE