

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

In re

Case No. 04-33194

ELSA SHANNON SZITO

Debtor

KRISTINA CORBITT

Plaintiff

v.

Adv. Proc. No. 04-3232

ELSA SHANNON SZITO

Defendant

MEMORANDUM

APPEARANCES: JENKINS & JENKINS ATTYS., PLLC
Michael H. Fitzpatrick, Esq.
2121 First Tennessee Plaza
800 South Gay Street
Knoxville, Tennessee 37929-2121
Attorneys for Plaintiff

HAGOOD, TARPY & COX, PLLC
Lynn Tarpy, Esq.
2100 Riverview Tower
900 South Gay Street
Knoxville, Tennessee 37902
Attorneys for Defendant/Debtor

**RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE**

This adversary proceeding is before the court upon the Complaint filed by the Plaintiff, Kristina Corbitt, on September 15, 2004, seeking a determination that a state court judgment against the Defendant/Debtor (Debtor), in the amount of \$3,000.00 plus pre-judgment interest, is nondischargeable under 11 U.S.C.A. § 523(a)(2)(A) (West 2004).

The trial was held on April 6, 2005. The record before the court consists of sixteen exhibits introduced into evidence, along with the testimony of Michael deLisle and the Plaintiff.

This is a core proceeding. 28 U.S.C.A. § 157(b)(2)(I) (West 1993).

I

In May 2002, the Plaintiff was approached by the Debtor regarding a loan to enable the Debtor to make a \$4,000.00 down payment on a modular home. Because the parties were good friends, and in accordance with an oral agreement that repayment was due as soon as the Debtor could do so, but in any event, within one year, the Plaintiff loaned the Debtor \$3,000.00 (Loan) on May 15, 2002. Additionally, the Plaintiff arranged for her estranged husband, Michael deLisle, to loan the Debtor the remaining \$1,000.00, with the understanding that repayment to Mr. deLisle was due on June 5, 2002. The Debtor then used the entire \$4,000.00 as a down payment on a modular home, financing the balance with Vanderbilt Mortgage.

The Debtor did not repay Mr. deLisle by June 5, 2002, but, after he made a demand for payment, the Debtor repaid him the \$1,000.00 a couple of weeks later. The Debtor did not, however, make any

payments to the Plaintiff for her Loan. Thereafter, the Plaintiff filed an action against the Debtor in the Knox County General Sessions Court, and she was awarded a judgment. The Debtor then appealed the General Sessions Court judgment to the Circuit Court for Knox County, Tennessee, and a trial was held on January 28, 2004, at which both parties and Mr. deLisle testified. On January 29, 2004, the state court entered a judgment in the amount of \$3,000.00, plus court costs, against the Debtor (Judgment). *See* TRIAL EX. 22.

Following the Plaintiff's attempts to levy upon her personal property to satisfy the Judgment, the Debtor filed the Voluntary Petition commencing her bankruptcy case under Chapter 7 of the Bankruptcy Code on June 15, 2004. The Plaintiff filed her Complaint initiating this adversary proceeding on September 15, 2004, seeking a determination that the Judgment is nondischargeable under 11 U.S.C.A. § 523(a)(2)(A) (West 2004) and requesting pre-judgment interest. On November 24, 2004, the Debtor filed an Answer, denying the Plaintiff's allegations with respect to repayment of the Loan.

II

The nondischargeability of debts is governed by 11 U.S.C.A. § 523, which provides, in material part:

(a) A discharge under section 727^[1] . . . of this title does not discharge an individual debtor from any debt—

¹ Chapter 7 debtors receive a discharge of pre-petition debts, “[e]xcept as provided in section 523 of this title[.]” 11 U.S.C.A. § 727(b) (West 1993). This accomplishes the goals of Chapter 7 to relieve “honest but unfortunate” debtors of their debts and allow them a “fresh start” through this discharge. *Buckeye Retirement, LLC v. Heil (In re Heil)*, 289 B.R. 897, 901 (Bankr. E.D. Tenn. 2003) (quoting *In re Krohn*, 886 F.2d 123, 125 (6th Cir. 1989) (citing *Local Loan Co. v. Hunt*, 54 S. Ct. 695, 699 (1934)).

....

(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, other than a statement respecting the debtor's or an insider's financial condition[.]

....

(c)(1) Except as provided . . . the debtor shall be discharged from a debt of a kind specified in paragraph (2) . . . of subsection (a) of this section, unless, on request of the creditor to whom such debt is owed, and after notice and a hearing, the court determines such debt to be excepted from discharge under paragraph (2) . . . as the case may be, of subsection (a) of this section.

....

(d) If a creditor requests a determination of dischargeability of a consumer debt under subsection (a)(2) of this section, 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.^[2]

11 U.S.C.A. § 523 (West 2004). The Plaintiff, as the party seeking a determination of nondischargeability, bears the burden of proving each of the above elements by a preponderance of the evidence. *Grogan v. Garner*, 111 S. Ct. 654, 661 (1991). Section 523(a) is construed strictly against the Plaintiff and liberally in favor of the Debtor. *Rembert v. AT&T Universal Card Servs., Inc. (In re Rembert)*, 141 F.3d 277, 281 (6th Cir. 1998); *Haney v. Copeland (In re Copeland)*, 291 B.R. 740, 759 (Bankr. E.D. Tenn. 2003).

² At trial, the attorneys for both parties advised the court that they were representing the parties on a pro bono basis and, therefore, § 523(d) was waived.

To satisfy § 523(a)(2)(A), the Plaintiff must prove that the Debtor obtained the Loan through actual fraud or false pretenses, that the Debtor intended to deceive the Plaintiff, that the Plaintiff justifiably relied on the Debtor's false representations, and that the Plaintiff's reliance was the proximate cause of her losses. *See Copeland*, 291 B.R. at 760 (citing *Rembert*, 141 F.3d at 280).

First, the Plaintiff must prove that the Debtor engaged in conduct that was somewhat "blameworthy," and her fraudulent intent may be "inferred as a matter of fact" based on the totality of the circumstances. *Copeland*, 291 B.R. at 759 (citing *Commercial Bank & Trust Co. v. McCoy (In re McCoy)*, 269 B.R. 193, 198 (Bankr. W.D. Tenn. 2001)). Material misrepresentations, omissions, and actual fraud all fall within the scope of § 523(a)(2)(A). *Copeland*, 291 B.R. at 759; *see also Mellon Bank, N.A. v. Vitanovich (In re Vitanovich)*, 259 B.R. 873, 877 (B.A.P. 6th Cir. 2001) ("Actual fraud as used in 11 U.S.C. § 523(a)(2)(A) is not limited to misrepresentations and misleading omissions.").

"[F]alse pretense" involves implied misrepresentation or conduct intended to create and foster a false impression, as distinguished from a "false representation" which is an express misrepresentation[, while a]ctual fraud "consists of any deceit, artifice, trick, or design involving direct and active operation of the mind, used to circumvent and cheat another - something said, done or omitted with the design of perpetrating what is known to be a cheat or deception."

Copeland, 291 B.R. at 760 (quoting *Ozburn v. Moore (In re Moore)*, 277 B.R. 141, 148 (Bankr. M.D. Ga. 2002), and *First Centennial Title Co. v. Bailey (In re Bailey)*, 216 B.R. 619, 621 (Bankr. S.D. Ohio 1997)); *see also Peoples Sec. Fin. Co., Inc. v. Todd (In re Todd)*, 34 B.R. 633, 635 (Bankr. W.D. Ky. 1983) ("For the purposes of § 523(a)(2)(A), 'false representations and false pretenses encompass statements that falsely purport to depict current or past facts.'").

On the other hand,

a broken promise to repay a debt, without more, will not sustain a cause of action under § 523(a)(2)(A). Instead, central to the concept of fraud is the existence of scienter which, for purposes of § 523(a)(2)(A), requires that it be shown that at the time the debt was incurred, there existed no intent on the part of the debtor to repay the obligation.

EDM Mach. Sales, Inc. v. Harrison (In re Harrison), 301 B.R. 849, 854 (Bankr. N.D. Ohio 2003) (citations omitted). Intent to deceive requires proof that the Debtor made false representations that she knew or should have known would convince the Plaintiff to make the Loan. *Copeland*, 291 B.R. at 765-66. “Fraudulent intent requires an actual intent to mislead, which is more than mere negligence. . . . A “dumb but honest” [debtor] does not satisfy the test.” *Copeland*, 291 B.R. at 766 (quoting *Palmacci v. Umpierrez*, 121 F.3d 781, 788 (1st Cir. 1997)). Fraudulent intent may be inferred by examining the Debtor’s conduct to determine if she presented the Plaintiff with “a picture of deceptive conduct . . . indicat[ing] an intent to deceive.” *Copeland*, 291 B.R. at 766 (quoting *Wolf v. McGuire (In re McGuire)*, 284 B.R. 481, 492 (Bankr. D. Colo. 2002)).

Finally, § 523(a)(2)(A) also requires justifiable reliance by the Plaintiff; i.e., she must prove that she actually relied on the Debtor’s representations and that, based upon the facts and circumstances known to her at the time, such reliance was justifiable. *Copeland*, 291 B.R. at 767. Justifiable reliance can be found even if the Plaintiff “might have ascertained the falsity of the representation had [she] made an investigation.” *Copeland*, 291 B.R. at 767 (quoting *McCoy*, 269 B.R. at 198).

The Plaintiff contends that the Debtor never intended to repay the Loan and that she took every possible route to avoid repaying the Plaintiff. The Plaintiff argues that the Debtor first admitted that she

owed the Loan but claimed that she did not have the resources to pay it. Then, the Debtor denied even taking a loan from the Plaintiff, and later still, the Debtor argued that the Plaintiff owes her money because her son assisted with the Plaintiff's son, who is handicapped.

The Debtor, however, contends that the Loan was made on an oral promise to pay, but that she has not had the resources to do so. In support of her argument, the Debtor offered into evidence an August 15, 2002 letter in which she assured the Plaintiff that "you will be paid as soon as I am able." TRIAL EX. 1 (August 2002 Letter). The Debtor also argues that the Plaintiff knew that she was disabled and, because of her inability to earn extra money, she struggled to pay her bills and support her children. With her only income being from social security, the Debtor contends that the Plaintiff was fully aware of the risk that she would not be repaid, but there is no evidence of fraud on the Debtor's part.

The Plaintiff has not met her burden of proof under § 523(a)(2)(A). Central to the issue in this case is the Debtor's intent at the time the Loan was made. All of the evidence, and in fact, the Plaintiff's own testimony, reflects that in May 2002, when she accepted the Plaintiff's Loan, the Debtor intended to repay it. The Plaintiff testified that when she accepted the Loan, the Debtor said that she would repay it, but that she would have to make periodic payments, and it would take some time. This testimony is consistent with Trial Exhibit 1, the August 15, 2002 Letter, which expressly admits owing the Loan and needing time for repayment, as follows:

As far as money I borrowed, I have already returned the \$1,000 I agreed to do by June, and I intend to repay the remainder by the end of the year or shortly thereafter. At the time the money was loaned you indicated there was no rush, other than the \$1,000 and I must hold you to this with the assurance you will be paid as soon as I am able.

TRIAL EX. 1.

The Plaintiff urges the court to look beyond this letter and into the totality of the Debtor's conduct in the months that followed. To that end, she introduced into evidence ten letters sent by the Debtor to the Plaintiff, Mr. deLisle, and the General Sessions Court, in which the Debtor denies owing any money to the Plaintiff and consistently changes her story with respect to the Loan and whether she is actually owed money from the Plaintiff. In addition, Mr. deLisle and the Plaintiff testified that during the trial in the Knox County Circuit Court case, the Debtor testified that the money was actually hers, never having belonged to the Plaintiff at all.

All of these letters do present inconsistent statements with respect to the nature of the parties' relationship, that of their children, and to whom what amount of money is owed. Nevertheless, in order to satisfy § 523(a)(2)(A), the Debtor must have accepted the Loan with no intention whatsoever to repay it. The fact of the matter is that these parties were good friends at the time the Loan was made and remained friends until the Plaintiff took the Debtor's son on a trip to Florida later in May 2002. At sometime after that trip, the Debtor began making assertions of improprieties regarding the conduct of some adults on the trip, and the parties' relationship thereafter soured. Nonetheless, as late as August 15, 2002, the Debtor acknowledged the Loan and stated her intention to repay it. *See* TRIAL EX. 1.

Based upon the evidence, it appears to the court that there was no fraud in the inducement, and therefore, there was no fraud upon which a determination of nondischargeability can be based. The fact

that the Debtor later decided that she was not going to pay, and even the Debtor's inconsistencies and lack of complete honesty after the fact, cannot form the basis for finding the Judgment nondischargeable.

Accordingly, because the Plaintiff has not met her burden of proof under § 523(a)(2)(A), the court finds that the Judgment entered on January 29, 2004, in favor of the Plaintiff and against the Debtor in the Circuit Court for Knox County, Tennessee, in the amount of \$3,000.00 plus court costs is discharged.

A judgment consistent with this Memorandum will be entered.

FILED: April 18, 2005

BY THE COURT

s/ Richard Stair, Jr.

RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE

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J U D G M E N T

For the reasons set forth in the Memorandum filed this date containing findings of fact and conclusions of law as required by Rule 52(a) of the Federal Rules of Civil Procedure, made applicable to this adversary proceeding by Rule 7052 of the Federal Rules of Bankruptcy Procedure, it is ORDERED, ADJUDGED, and DECREED that the Complaint filed by the Plaintiff on September 15, 2004, is DISMISSED and the Plaintiff's claim against the Defendant is discharged.

ENTER: April 18, 2005

BY THE COURT

s/ Richard Stair, Jr.

RICHARD STAIR, JR.
UNITED STATES BANKRUPTCY JUDGE