



SIGNED this 06 day of November, 2008.

A handwritten signature in cursive script, reading "Marcia P. Parsons".

**Marcia Phillips Parsons
UNITED STATES BANKRUPTCY JUDGE**

[This opinion is not intended for publication as the precedential effect is deemed limited.]

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

In re

JEFFERY FOSTER BROBECK and
JANET LAVON BROBECK,

Debtors.

No. 03-21784
Chapter 7

PAUL LEWIS,

Plaintiff,

vs.

JEFFERY FOSTER BROBECK and
JANET LAVON BROBECK,

Defendants.

Adv. Pro. No. 03-2045

MEMORANDUM

Appearances:

James D. Culp, Esq.
207 E. Main Street, Suite 1A
Johnson City, Tennessee 37604
Attorney for Paul Lewis

Robert L. King, Esq.
Post Office Box 4055
Johnson City, Tennessee 37602-4055
Attorney for Jeffery and Janet Brobeck

Marcia Phillips Parsons, United States Bankruptcy Judge. In this adversary proceeding, the Plaintiff Paul Lewis seeks a judgment against Debtors Jeffery and Janet Brobeck and a determination of nondischargeability under 11 U.S.C. § 523(a)(2)(A). Presently before the court is the Debtors' motion for summary judgment, wherein they assert that this action is barred by the doctrine of *in pari delicto* because Plaintiff charged an usurious interest rate on the loans he extended to them. The court concludes that even if the factual basis of the Debtors' argument is correct, the *in pari delicto* defense is inapplicable because Plaintiff was not a participant in the Debtors' alleged fraud. Accordingly, the Debtors' summary judgment motion will be denied. This is a core proceeding. *See* 28 U.S.C. § 157(b)(2)(I).

I.

On May 15, 2003, the Debtors filed a voluntary petition for bankruptcy relief under chapter 7. On August 15, 2003, Plaintiff initiated the present adversary proceeding.¹ In the complaint as amended, the Plaintiff alleges that between July 9, 1998, and August 11, 2000, he loaned the Debtors sums totaling \$274,845 to finance their purchases of used cars for their used car business, which sums were to be repaid as inventory was sold.² According to the amended complaint, the Debtors perpetuated a fraud:

by representing to the Plaintiff that automobiles that had been sold were still in the inventory and failing to repay the Plaintiff for automobiles sold from inventory; by representing to the Plaintiff that automobiles for which the [Debtors] requested funds were purchased for more than the amount actually paid by the Debtors; that the Debtors repaid the Plaintiff for titles or automobiles with worthless checks, representing to the Plaintiff that the sale was not consummated when in fact the sale had been consummated, and failed, neglected or refused to return the title(s) to the Plaintiff; [and] that the debtors induced the Plaintiff to exchange titles on certain automobiles, the Debtors knowing that the title(s) offered in exchange were to automobiles worth less than the value of the automobiles for which they were exchanged.

¹ As is evident from the date that this adversary proceeding was commenced, this action has been pending more than five years without resolution, due in large part to a stay of this proceeding, granted to the Debtors without opposition, pending the conclusion of certain state court criminal proceedings.

² The complaint also sought a determination of nondischargeability under § 523(a)(6), but this court granted summary judgment to the Debtors on this issue in a memorandum opinion and order entered July 27, 2004.

The Plaintiff contends that as a result of the Debtors' fraud, he suffered damages in the principal amount of \$274,845, and that with added fees and interest he is entitled to a nondischargeable judgment of \$671,170.

On July 18, 2008, the Debtors filed their current summary judgment motion, supported by the declaration of B. Scott Cradic CPA, and the Plaintiff's deposition testimony and affidavit previously submitted by him in this case.³ The Plaintiff opposes the motion, but there is no genuine issue as to any material fact because neither the Plaintiff nor the Debtors have objected to the statement of undisputed material facts filed by the other. *See* E.D. Tenn. LBR 7056-1.

The evidence reveals that under the parties' business arrangement, each time the Debtors wanted to borrow from the Plaintiff, they would first purchase an automobile and then bring the Plaintiff the certificate of title for the vehicle. The Plaintiff would loan the Debtors the amount they paid for the vehicle, and the Plaintiff would hold the title until the Debtors repaid the loan, although it was understood that each loan was only for thirty days. There was no written agreement between the parties, nor did the Debtors ever sign any promissory notes. Instead, the Plaintiff gave the Debtors a card that set forth his payment terms. The card read as follows:

<u>30-day Advance</u>	<u>Fee</u>	<u>30-Day Depreciation</u> <u>Unit per Single Unit</u>
\$100 - \$1,000	\$100	\$50
\$1,001 - \$1,999	\$175	\$100
\$2,000 - \$4,999	\$200	\$200
\$5,000 - \$6,999	\$225	\$225
\$7,000 - \$10,000	\$300	\$300

Thus, for example, if the amount loaned to the Debtors was between \$100 and \$1,000, the Debtors at the end of thirty days would be required to repay the Plaintiff the amount borrowed, plus

³As referenced in note 2, *supra*, the Debtors previously sought summary judgment in a motion filed April 6, 2004. The court questions why the Debtors did not raise the *in pari delicto* issue in that motion, especially since the current motion is based in part on the Plaintiff's affidavit and deposition testimony that also were the factual basis of their original motion.

a \$100 fee and a \$50 depreciation fee. According to Cradic's affidavit, without taking into account the depreciation fee and assuming that all interest and principal was paid in full on the loans' due dates, the fees charged by the Plaintiff represented interest rates from a low of 34.822% to a high of 1,200.005%.

During the same time that the Plaintiff conducted business with the Debtors, the Plaintiff also conducted transactions with other individuals in the used car business under the same terms and loan rates. The Plaintiff did not hold a state or federal license or registration to conduct a commercial lending business or any other kind of lending business.

Citing Tennessee Code Annotated § 47-14-102(12), the Debtors assert that the Plaintiff charged them an usurious and unlawful rate of interest, and that his conduct is a Class A misdemeanor and implicates Tennessee's RICO statute. According to the Debtors, because of the Plaintiff's wrongdoing, this action is barred by the doctrine of *in pari delicto* and, therefore, must be dismissed. In response, the Plaintiff denies that his fees were usurious. Alternatively, he argues that even if they were, Tennessee law does not preclude recovery of the sums owed to him but rather simply limits the effective rate of interest to the maximum allowable rate, which he assumes is 10%.

II.

Under Tennessee Code Annotated § 47-14-102(12), "usury" is defined as "the collection of interest in excess of the maximum amounts authorized by or pursuant to this chapter or any other statute." According to Tennessee Code Annotated § 47-14-103:

Except as otherwise expressly provided by this chapter or by other statutes, the maximum effective rates of interest shall be as follows:

- (1) For all transactions in which provisions of other statutes fix a maximum effective rate of interest for particular categories of creditors, lenders, or transactions, the rate so fixed;
- (2) For all written contracts, including obligations issued by or on behalf of the state of Tennessee, any county, municipality, or district in the state, or any agency, authority, branch, bureau, commission, corporation, department, or instrumentality thereof, signed by the party to be charged, and not subject to subdivision (1), the applicable formula rate; and
- (3) For all other transactions, ten percent (10%) per annum.

There is no evidence in the record that the Plaintiff has a special license or that he otherwise

qualifies for special statutory rates under paragraph (1) of § 47-14-103(a). And, as previously noted, the parties did not have a written contract, such that paragraph (2) of § 47-14-103 is applicable. Therefore, paragraph (c) of the section would appear to be the applicable provision such that the maximum rate of interest that the Plaintiff could charge the Debtors is 10%.

As the Debtors assert, “[t]he willful collection of usury is a Class A misdemeanor” under Tennessee law. Tenn. Code Ann. § 47-14-112. Nonetheless, as argued by the Plaintiff, there is no statutory authority under Tennessee law for the proposition that the alleged usurious interest rates charged by the Plaintiff constitute a complete defense under Tennessee law to this action. “A defendant sued for money *may avoid the excess* over lawful interest by pleading usury, setting forth the amount of such excess.” Tenn. Code Ann. § 47-14-110 (emphasis supplied). According to *Riverside Park Realty Co. v. Federal Deposit Insurance Corp.*, 465 F. Supp. 305, 311 (M.D. Tenn. 1978), a debtor who brings an action to have a note declared unenforceable on the ground of usury will be unsuccessful. “[A]lthough he does not have to pay usurious interest, he remains liable on the note for the principal and interest calculated at the legal rate.” *Id.*

Notwithstanding the foregoing, the Debtors assert that this action is barred by the affirmative defense of *in pari delicto*. This doctrine refers to “the plaintiff’s participation in the same wrongdoing as the defendant.” *Terlecky v. Hurd (In re Dublin Sec. Inc.)*, 133 F.3d 377, 380 (6th Cir. 1997) (citing *Bubis v. Blanton*, 885 F.2d 317, 321 (6th Cir. 1989)). The phrase is short for “*in pari delicto potior est conditione defendantis*,” which means “where the wrong of both parties is equal, the position of the defendant is stronger.” *Limor v. Buerger (In re Del-Met Corp.)*, 322 B.R. 781, 818 (Bankr. M.D. Tenn. 2005). “In essence, it prevents one wrongdoer from recovering from another because each should bear the consequences of their wrongdoing without legal recourse against the other.” *Liquidating Tr. of the Amcast Unsecured Creditor Liquidating Trust v. Baker (In re Amcast Indust. Corp.)*, 365 B.R. 91, 123 (Bankr. S.D. Ohio 2007). The doctrine is based on the twin premises that courts should not mediate between wrongdoers and denying judicial relief to a wrongdoer deters illegal conduct. *Id.*

Upon careful consideration of the law in this area, the court concludes that the doctrine of *in pari delicto* provides no defense to the Debtors in this action, even assuming the rate of interest charged by the Plaintiff was usurious as the Debtors claim. “Plaintiffs who are truly *in pari delicto* are those who have themselves violated the law in *cooperation* with the defendant.” *Pinter v. Dahl*,

486 U.S. 622, 636, 108 S. Ct. 2063, 2073 (1988) (emphasis added); *see also Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 307, 105 S. Ct. 2622, (1985) (*in pari delicto* is “limited to situations where the plaintiff truly bore at least substantially equal responsibility for his injury”); *Lawler v. Gilliam*, 569 F.2d 1283, 1292 (4th Cir. 1978) (The doctrine “deals generally with parties whose equal, mutual, and simultaneous fault casts them in the role of conspirators.”). In the instant case, there is no allegation that the parties were co-conspirators in the same wrongdoing or that Plaintiff participated or cooperated in perpetuating the Debtors’ alleged fraud such that the Plaintiff bears equal responsibility for the losses that are the subject of this action. To the contrary, the Plaintiff alleges in the amended complaint that he was the victim of the Debtors’ fraudulent schemes, including the Debtors’ alleged misrepresentation that certain automobiles were still in inventory even though they had already been sold, that cars were represented to have been purchased for more than they actually were in an attempt to induce Plaintiff to lend additional funds to the Debtors, purposely repaying the Plaintiff with checks known to be worthless in order to induce further extensions of credit, and delivering certificates of titles on automobiles that were less valuable than the true automobiles associated with the titles. In contrast, rather than complicity in the Debtors’ alleged fraud, the wrong allegedly committed by the Plaintiff is charging usurious rates of interest on loans extended to the Debtors.

The Sixth Circuit Court of Appeals decision in *Dublin Securities* is illustrative of the narrow applicability of the *in pari delicto* doctrine to instances where there was cooperation by the defendant and plaintiff in the same wrongdoing. *In re Dublin Sec. Inc.*, 133 F.3d 377. In that case, the chapter 7 trustee sued the attorneys who had represented and allegedly assisted the debtor in connection with its fraudulent public stock offering. The court of appeals upheld the district court’s dismissal of the action based on *in pari delicto* principles, because the trustee in bringing the action was standing in the shoes of the debtor that admittedly was at least as culpable as the defendants in perpetrating the fraud. *Id.* at 381. *See also Nisselson v. Lernout*, 469 F.3d 143 (1st Cir. 2006) (doctrine of *in pari delicto* barred trustee’s claims brought on behalf of the estate where debtor itself was implicated in the alleged fraud asserted against the defendants); *Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co. Inc.*, 267 F.3d 340 (3rd Cir. 2001) (action by unsecured creditors committee on behalf of debtor corporation against sole shareholder of corporation was barred by *in pari delicto* doctrine since both debtor and the defendant were engaged in the fraudulent Ponzi scheme); *Luzinski v. Peabody & Arnold LLP (In re Gosman)*, 382 B.R. 826 (S.D. Fla. 2007) (claim

brought by trustee standing in the shoes of the debtor was barred by *in pari delicto* where trustee alleged in the complaint that the debtor had participated with the defendant in the alleged fraudulent transfer).

In contrast with these cases is the case of *Interpublic Group of Cos. v. Fratarcangelo*, No. 00 Civ.3323, 2002 WL 31720355 (S.D.N.Y Dec. 4, 2002), wherein the purchaser of the stock of a corporation brought suit against the seller and its owner, alleging that they committed securities fraud during the course of the sale by misrepresenting the corporation's viability. The defendants raised the *in pari delicto* defense, asserting that the plaintiff had engaged in similar fraud by inflating its own stock price through accounting irregularities that were ongoing at the time of the transaction. The court refused to apply the doctrine, explaining that the mere allegation that the plaintiff had also engaged in collateral wrongdoing was insufficient. For the *in pari delicto* doctrine to apply, the court held, the plaintiff must have been an active, voluntary participant in the unlawful activity for which the plaintiff seeks damages. *Id.* at *2. *See also Food Lion, Inc. v. Capital Cities/ABC, Inc.*, 951 F. Supp. 1233, 1235 (M.D.N.C. 1996) (*in pari delicto* defense could not be utilized where each party may have acted wrongfully at some point, but "did not act wrongfully in conjunction with one another during the same act").

Similarly, in the present case, regardless of whether the Plaintiff charged the Debtors a usurious rate of interest, his action in this case is based on the allegation that the Debtors defrauded him in the procurement of the loans. By definition, the Plaintiff could not have been a co-conspirator with the Debtors in this fraud. As such, the *in pari delicto* defense does not apply.

III.

Federal Rule of Civil Procedure 56, as incorporated by Rule 7056 of the Federal Rules of Bankruptcy Procedure, mandates the entry of summary judgment if the pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits, if any, show there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. *See* Fed. R. Civ. P. 56 (c). In ruling on a motion for summary judgment, any inferences to be drawn from the underlying facts contained in the record must be viewed in the light most favorable to the party opposing the motion. *See McCafferty v. McCafferty (In re McCafferty)*, 96 F.3d 192, 195 (6th. Cir. 1996) (citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S.

574, 587 (1986)). Summary judgment is appropriate for deciding whether *in pari delicto* defense may be asserted as a matter of law. See *OHC Liquidation Trust v. Credit Suisse First Boston (In re OakwoodHomes Corp.)*, 389 B.R. 357 (D. Del. 2008) (granting summary judgment on *in pari delicto* grounds in favor of attorney who had been sued for malpractice); *Food Lion, Inc. v. Capital Cities/ABC, Inc.*, 951 F. Supp. at 1235 (holding as a matter of law that *in pari delicto* defense could not be utilized where parties were not in the role of joint conspirators). Accordingly, an order will be entered in accordance with the foregoing, denying the Debtors' motion for summary judgment.

###