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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN RE:	CASE NO. 04-64988
Douglas Keith Roubieu,	CHAPTER 7
Debtor.	JUDGE MASSEY
Pioneer Credit Company,	
Plaintiff,	
v.	ADVERSARY NO. 04-6394
Douglas Keith Roubieu,	
Defendant.	

FINDINGS OF FACT AND CONCLUSIONS OF LAW
AND ORDER CONCERNING PLAINTIFF'S EXHIIBIT 6

In its complaint in this adversary proceeding, Plaintiff, Pioneer Credit Company, seeks a judgment denying the discharge of Defendant and Debtor, Douglas Keith Roubieu, and, alternatively, determining that the debt owed by Debtor to Plaintiff is not dischargeable. The Court conducted a trial in this matter on July 5, 2005. The Court makes the following findings of fact and conclusions of law pursuant to Rule 52 of the Federal Rules of Civil Procedure made applicable by Rule 7052 of the Federal Rules of Bankruptcy Procedure.

The parties stipulated most of the facts relevant to the dispute in the pre-trial order. Based on seven of the eight exhibits admitted without objection (the Court is unable to consider

Plaintiff's Exhibit No. 6 as explained below) and those stipulated facts, Plaintiff contends that it is entitled to a judgment. It did not call a witness. Defendant's counsel called Defendant as a witness.

Plaintiff's Exhibit No. 6 is an audio tape of the meeting of creditors according to the exhibits listed in the pre-trial order. The Court has no means of listening to the tape and cannot be made responsible for the cost of transcribing that tape. Accordingly, if Plaintiff desires that the Court consider any portion of that exhibit not already transcribed in the document marked Plaintiff's Exhibit 7, it may move within ten days of entry of this Order for reconsideration of these findings of fact and conclusions of law and to vacate the judgment so that the trial may be reopened for the purpose of offering the full transcript as evidence. Within ten days after filing such a motion, Plaintiff must file a transcript of the tape marked as Exhibit 6.

In a nutshell, the facts are as follows. On July 30, 2003, Defendant borrowed money from Plaintiff and refinanced an existing loan for a total outstanding debt of $9,377.36. The interest rate was in excess of 27%. The parties entered into a note and security agreement, marked as Plaintiff's Exhibit 1. That two page document granted to Plaintiff to secure the loan a security interest in a 1991 Dodge van and in personal property listed in a schedule that is not attached to the exhibit. The parties agreed that the other personal property consisted of three firearms, two VCRs, one stereo and one pressure washer, all of which Debtor owned as of July 30, 2003. Debtor also executed a financing statement to which there was attached a schedule showing the collateral and the value of each item. The parties agreed that those items of personal property were "valued at $4,125.00." But there was no credible evidence to show in fact what the actual value of those items was. The statement of financial affairs shows Defendant's annual income for the three years prior to the petition to have been approximately $30,000. It is hard to believe that the two VCRs owned by Defendant were in fact worth $1,050.00 as Plaintiff's loan officer wrote on the form attached to the financing statement. Defendant credibly testified that Plaintiff's agent valued the items. True, Defendant went along with that valuation – he wanted the loan – but the values listed do not establish their actual value.

At an unspecified date or dates subsequent to July 30, 2003, the parties agree that Defendant "disposed" of the personal property listed in the attachment to the financing statement. Plaintiff conceded at trial that it does not contend that Defendant transferred the automobile, the certificate of title for which shows Plaintiff as a lienholder. At trial, Defendant testified credibly that the stereo and a pressure washer had been destroyed by fire, that he had traded two firearms and that he sold a firearm for cash. Defendant also testified that he had purchased replacements for the stereo and pressure washer and that he was willing to agree that those replacement items should be considered collateral for the loan.

Defendant testified credibly that he was unaware that he was violating the security agreement with Plaintiff at the time he disposed of the various items of personal property. This is not surprising because the security agreement contains no provision prohibiting the sale of such items or expressly requiring the consent of Plaintiff to sell or exchange collateral. The agreement does provide that "[p]roceeds of collateral are also covered; however, such shall not be construed to mean that Lender consents to any sale of such collateral." The meaning of this provision is not at all clear with respect to whether a sale of collateral would be a breach. It implies that the lender would not quarrel with a sale that produced fair value for the collateral or replacement collateral of equal value but that the lender reserved the right to pursue its collateral in the hands of third parties unless it consented. At best, the agreement is ambiguous with respect to sales or transfers of the collateral, and Plaintiff introduced no evidence to show that Defendant breached the security agreement by trading, selling or substituting collateral.

On March 24, 2004, Defendant filed a petition initiating the above referenced Chapter 7 case. In his statement of financial affairs, Defendant answered "None" to question 10, which asks: "List all other property, other than property transferred in the ordinary course of business or financial affairs of the debtor, transferred either absolutely or as security within one year immediately preceding the commencement of this case." When questioned by the Court about this answer, Defendant credibly testified that he did not "always understand" the question and that he had not remembered that he had granted a security interest to Plaintiff.

Defendant listed Plaintiff as a secured creditor in Schedule D and reflected there the security interest in the vehicle. In Schedule B, Defendant showed that he owned household goods and furnishings, including audio and video equipment, that he valued at $4,500. Plaintiff made no effort at trial to show that the household items disclosed in Schedule B did not include proceeds of any disposition of its collateral.

Based on these facts, Plaintiff contends that the Court should deny Defendant's discharge pursuant to 11 U.S.C. § 727(a)(2) and (a)(4). The burden of proving the facts necessary to establish the elements of a section 727 claim is on Plaintiff. Fed. R. Bank. P. 4005.

Section 727(a)(2) provides in relevant part:

(a) The court shall grant the debtor a discharge, unless -

> . . .
>
> (2) the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed,

> destroyed, mutilated, or concealed, or has permitted to be transferred, removed, destroyed, mutilated, or concealed -
>
> > (A) property of the debtor, within one year before the date of the filing of the petition; or
> >
> > (B) property of the estate, after the date of the filing of the petition[.]

"Section 727(a)(2)(A)'s bar to discharge comprehends four elements of preponderant proof: (1) the debtor transferred, removed, concealed, destroyed, or mutilated, (2) his or her property, (3) within one year of the bankruptcy petition's filing, [and] (4) with the intent to hinder, delay, or defraud a creditor. *In re Hayes,* 229 B.R. 253, 259 (1st Cir. BAP 1999) (footnote omitted.).

The first three elements are satisfied by the parties' stipulation of facts. But there is no evidence that in selling certain items of personal property, Defendant subjectively intended to hinder, delay or defraud a creditor or an officer of the Court. Although Defendant testified at the meeting of creditors (Plaintiff's Exhibit 7) that he was aware at that meeting that items sold were collateral for his loan from Plaintiff, that awareness does not prove that Defendant in fact intended at the time of each such sale or transfer to hinder, delay or defraud Plaintiff or a trustee in any future bankruptcy case. As we have seen, the security agreement did not unambiguously bar Defendant from selling those items. Even if the agreement is so interpreted, the most the evidence can be said to show is a breach of contract. Defendant's conduct resulted in proceeds that continued to secure the loan so long as they were identifiable, and nothing in the record shows that Plaintiff did not end up with the cash proceeds. Indeed, Plaintiff's Exhibit 8 shows payments from Defendant to Plaintiff in October, November and December 2003, which contradicts the notion that Defendant was trying to defraud Plaintiff. Defendant credibly testified that at least one transaction involved a swap of items, thereby preserving Plaintiff's interest in proceeds.

In proposed findings of fact and conclusions of law submitted to the Court on July 5, 2005, Plaintiff relies on *Walton v. Staub (In re Staub)*, 208 B.R. 602 (Bankr. S.D.Ga. 1997) as support for its contention that "Defendant sold its collateral in contravention of section 727(a)(2)." There, the U.S. Trustee moved to revoke the debtor's discharge on the ground that Debtor had committed acts justifying denial of his discharge under section 727(a)(4), not section 727(a)(2). The U.S. Trustee alleged and proved that the debtor had concealed substantial assets of the estate from creditors and the case trustee. As a result, the Court denied that debtor's discharge. Section 727(a)(2) does not punish a debtor's unauthorized sale of collateral; it provides for denial of a discharge if the plaintiff can show by a preponderance of the evidence that a debtor transferred his property with intent to hinder, delay or defraud a creditor or court officer within one year of the petition date. Not every sale of collateral securing a debt is done with the intent of harming the creditor. Here, Debtor testified he sold a few items without remembering the security interest at the time for the purpose of raising money to pay debts. As the parties understand, one can prove fraud by circumstantial evidence. It is not enough, however, to point to an ambiguous security agreement and an admission that collateral was sold and in some instances replaced with similar items to prove fraudulent intent. In short, Plaintiff failed to carry its burden of proving facts to show that Defendant's discharge should be denied under section 727(a)(2).

Section 727(a)(4) provides in relevant part:

(a) The court shall grant the debtor a discharge, unless -

. . .

(4) the debtor knowingly and fraudulently, in or in connection with the case -

(A) made a false oath or account[.]

The elements that a plaintiff must prove under section 727(a)(4)(A) are that "(1) the debtor made a statement under oath, (2) the statement was false, (3) the debtor knew the statement was false, (4) the debtor made the statement with fraudulent intent, and (5) the statement related materially to the bankruptcy case." *In re Kressner*, 206 B.R. 303, 316 (Bankr. S.D.N.Y.1997) (quoting *In re Emery*, 170 B.R. 777, 783 (Bankr. E.D.N.Y. 1994)). Section 727(a)(4) overlaps with section 727(a)(2) to the extent that a debtor transfers or conceals property before or after the petition date with intent to hinder, delay or defraud a creditor or the trustee and then knowingly and fraudulently makes false oaths concerning that property.

A court may infer a false oath or intent to conceal assets from the sheer number of errors on schedules. *E.g.*, *In re Dulock*, 250 B.R. 147, 152 (Bankr. N.D.Ga. 2000) ("A series or pattern of errors or omissions may have a cumulative effect giving rise to an inference of an intent to deceive."). Nonetheless, "the misstatement or omission must be made with the requisite fraudulent intent . . . ." *In re Parnes*, 200 B.R. 710, 714 (Bankr. N.D. Ga. 1996).

> Fraudulent intent must be shown by actual, not constructive fraud. 4 L. King, Collier on Bankruptcy, para. 727.02 at 727-15 (15th ed. 1990); *In re Sawyer*, 130 B.R. 384 (E.D.N.Y.1991). Scienter and fraudulent, wilful intent are essential elements. *In re Irving*, 27 B.R. 943, 945 (Bankr.E.D.N.Y.1983). Thus, the party objecting to discharge must show that the information was omitted for the specific purpose of perpetrating a fraud and not simply because the debtor was careless or failed to fully understand his attorney's instructions. *In re Seablom*, 45 B.R. 445, 449 (Bankr.D.N.D.1984). As a debtor will rarely admit actual intent to defraud creditors, fraudulent intent may be established by circumstantial evidence or by inferences drawn from a course of conduct. *In re Glaser*, 49 B.R. 1015, 1019 (Bankr.S.D.N.Y.1985).

In re Kelly, 135 B.R. 459, 461-62 (Bankr. S.D.N.Y. 1992).

Plaintiff is in effect asking the Court to conclude that Defendant committed fraud because his answer to question 10 on his statement of financial affairs was wrong. Such a conclusion would be based purely on a finding of constructive fraud based solely on the error in the statement of financial affairs. It is not supported by any other evidence to show that Defendant acted deliberately in omitting to disclose the transfers and not as result of carelessness, forgetfulness or ignorance. As noted earlier, Defendant testified that he did not "always understand" the question. When asked whether he recalled having granted a security interest to Plaintiff, Defendant testified that when he executed his statement of financial affairs, he had forgotten about the security interest he gave to Plaintiff and then added, "it was not my intent to do that." The Court infers from his answer that he found the language of bankruptcy confusing. Many honest debtors do. The Court further understands his answer as denying that he deliberately misstated his answer to question no. 10.

Providing complete and honest information is the duty of every debtor. Only honest debtors are entitled to a discharge. Nonetheless, proving that a debtor provided incorrect information does not prove that the debtor was dishonest in doing so. The fact of the matter is that many, if not most, debtors make errors on their bankruptcy filings. It is therefore a factually intensive exercise to distinguish the con artist from the honest debtor. In this case, the Court, having closely observed Mr. Roubieu's demeanor, finds that he was telling the truth.

As was the case with section 727(a)(2), Plaintiff has failed to offer any evidence of fraudulent intent in answering question 10 in the negative. Defendant was not trying to hide his relationship with Plaintiff as evidenced by his Schedule D. Plaintiff did not establish a motive impelling Defendant to lie on his bankruptcy papers. Because there is no credible evidence to show that Defendant had a fraudulent intent in marking "None" as his answer to question 10 on his statement of financial affairs, Plaintiff failed to carry its burden of proving facts sufficient to warrant denial of discharge under section 727(a)(4).

Defendant could have proceeded on a different theory and, if it had proper proof, might have succeeded. Under section 523(a)(6), a sale of a secured party's collateral that is forbidden by the security interest may constitute a "willful and malicious injury" to the secured party, giving rise to a nondischargeable debt equal in amount to the value of the mishandled collateral. To have succeeded on such a theory, Plaintiff would have had to show that Plaintiff understood not only that Plaintiff had a security interest in the collateral but also that sale of the collateral without Plaintiff's permission was forbidden. The security agreement standing alone is not up to that task, as we have seen. It would also have had to show the value of the collateral sold on the date of sales. If the sales were unauthorized, Plaintiff could have proceeded against its collateral in the hands of others. Defendant has now obtained reconveyances of most of the collateral. Although that fact would not constitute a defense to the claims tried on July 5, it would mitigate any damages that Plaintiff might have claimed had it sued under section 523(a)(6).

Instead, Plaintiff contended it its complaint that the Court should determine the debt to be non-dischargeable because Defendant obtained the loan "by false pretenses, or, alternatively, by actual fraud and misrepresenting to the Plaintiff his financial status, ability to repay, and his intention to repay the funds to Plaintiff." Plaintiff elected not to present any additional evidence on the section 523 count at trial. Because there is no evidence concerning any fraud or misrepresentation by Defendant in obtaining the loan from Plaintiff, Defendant is entitled to a judgment on that count.

IT IS SO ORDERED.

Dated: July 6, 2005.

James E. Massey

JAMES E. MASSEY
U.S. BANKRUPTCY JUDGE