UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF GEORGIA
NEWNAN DIVISION

IN THE MATTER OF:	:	**CASE NUMBERS**
MARK C. CALLAWAY,	:	BANKRUPTCY CASE NO. 04-14055-WHD
Debtor.	:	
BANCORPSOUTH BANK,	:	
Plaintiff,	:	ADVERSARY PROCEEDING NO. 05-1113
v.	:	
MARK C. CALLAWAY,	:	
Defendant.	:	IN PROCEEDINGS UNDER CHAPTER 7 OF THE BANKRUPTCY CODE

ORDER

Before the Court is the Complaint of Bancorpsouth Bank (hereinafter the "Plaintiff") against Mark Clayton Callaway (hereinafter the "Defendant"). The Complaint objects to the dischargeability of a particular debt pursuant to sections 523(a)(2)(A) and (B) of the Bankruptcy Code. Accordingly, this matter constitutes a core proceeding, over which this Court has subject matter jurisdiction. *See* 28 U.S.C. § 157(b)(2)(I); § 1334.

FINDINGS OF FACT

The Defendant is a financial advisor and, at all times relevant to this proceeding, has been employed by Citigroup Capital Markets, Inc. (also known as Smith Barney). Transcript

of Trial, April 25, 2006 (Docket Number 37) (hereinafter "April 25th Transcript Part 2") at 7, 16. The Defendant and his family lived in Troup County, Georgia until the Defendant separated from his wife and moved to Atlanta, Georgia. The Defendant worked in an Atlanta branch office part time, and while there, lived in a rented condominium in Atlanta. *Id.* At some point, the Defendant and his wife purchased the condominium (hereinafter the "14th Street Condo"). Transcript of Trial, May 18, 2006 (hereinafter "May 18th Transcript) at 47.

In 1999, the Defendant and his wife began considering purchasing a property in La Grange (hereinafter the "Vernon Street Property"), which had previously been owned by members of the Defendant's family, with the intent that the property could be renovated and upgraded to be used as a permanent residence. May 18th Transcript at 52, 62. Prior to purchasing the Vernon Street Property, the Defendant consulted with an architect, an interior designer, and a contractor, Ben Parham, regarding the required renovations and the budget. *Id.* at 57. The Defendant and his wife later agreed to purchase the Vernon Street Property for $735,000 and budgeted $900,000 for the renovation costs. April 25th Transcript Part 2 at 23-24. To acquire the Vernon Street Property, the Defendant sold the family residence on Victoria Drive, used all or a portion of the proceeds to make a down payment of approximately $157,000, and borrowed approximately $570,000 from Frontier Bank. May 18th Transcript at 59-60.

To finance the renovation, the Defendant obtained a construction loan from SunTrust

Bank, which agreed to loan $500,000 to the Defendant with the understanding that the Defendant would put $500,000 of his own money into the Vernon Street Property renovation. May 18th Transcript at 60-62. From the closing of the SunTrust construction loan on June 29, 2001 through January 2002, the Defendant spent the $500,000 of loan proceeds on the Vernon Street Property renovation. April 25th Transcript Part 2 at 28. The SunTrust loan proceeds were completely paid out by January 2002. *Id.* at 27-28. The proceeds were either paid by SunTrust directly to Parham or paid by SunTrust to the Defendant, who then paid Parham. *Id.* at 28. Before the closing of the SunTrust loan on June 29, 2001, the Defendant paid approximately $190,675.49 in connection with the Vernon Street Property project, including the down payment on the home. May 18th Transcript at 109-111; Defendant's Exhibits 78-80, 83. After the SunTrust proceeds had been completely paid out in January 2002, the Defendant wrote checks in connection with the Vernon Street Property that total at least $496,153.19. May 18th Transcript at 111-117; Defendant's Exhibits 67-70, 73, 75, 82, 84-90, 95, 99. Accordingly, in addition to the SunTrust construction loan proceeds, the Defendant invested a total of at least $686,828.68.[1] These non-borrowed funds that the Defendant spent on the project came from his

[1] The Plaintiff has asserted that there is no evidence in the record to substantiate the Defendant's claim that he had invested $689,000 of his own money into the Vernon Street Property by the time he prepared Exhibit 7. The Court disagrees, finding the Defendant's testimony that he paid the checks discussed above, either before the SunTrust loan closed or after the SunTrust loan proceeds had been paid out, to be sufficient evidence upon which to make a finding of fact that the Defendant did in fact make these payments with non-borrowed funds. Additionally, the Plaintiff has introduced no evidence that would dispute the Defendant's contention.

employment and his trust account. April 25th Transcript Part 2 at 63; May 18th Transcript at 108-119; 125.

In January 2002, the Defendant received a statement regarding the progress of the renovation from Parham, which showed that the project was over budget and that the costs had reached $1.1 million. May 18th Transcript at 62-63; April 25th Transcript Part 2 at 29. In April 2002, Parham provided the Defendant with a projected total for the completion of the project. This estimate indicated that the costs would likely be $1.3 million, but would not exceed $1.5 million. May 18th Transcript at 64; April 25th Transcript Part 2 at 30. At that time, the Defendant began seeking permanent financing for the Vernon Street Property. April 25th Transcript Part 2 at 30.

In approximately May and June of 2002, the Defendant contacted various lenders regarding permanent financing, including SunTrust Bank, Commercial Bank and Trust, Community Bank and Trust, and Colonial Bank. May 18th Transcript at 82-83; April 25th Transcript Part 2 at 31-33. At that time, the Defendant anticipated that the Vernon Street Project would require an additional $500,000 of funding, which the Defendant needed to borrow. On May 24, 2002, the Defendant met with John Thompson at Community Bank & Trust regarding a loan and followed up the discussion with a letter. April 25th Transcript Part 2 at 41; Exhibit 25. The letter detailed the Defendant's concern over being able to fund the additional $500,000 of cost overruns that exceeded the $1 million that he had already spent on the project, and also discussed means by which the Defendant could liquidate assets

and reduce his debt service. April 25th Transcript Part 2 at 52, 55-56; Exhibit 25.

At some time after June 30, 2002, the Defendant submitted to each lender a financial package, which included a statement of income, assets, and liabilities, which the Defendant prepared in his own format (hereinafter "Exhibit 7"). April 25th Transcript Part 2 at 33, 41. All of the lenders except the Plaintiff declined to make the loan. May 18th Transcript at 83; April 25th Transcript Part 2 at 37. The Defendant later contacted Robert Williams, a representative of the Plaintiff, about making the $1.65 million loan. Transcript of Trial, April 24, 2006 (hereinafter "April 24th Transcript") at 13; May 18th Transcript at 5. Williams had previously been the originating officer at Frontier Bank who loaned funds to the Defendant to purchase the Vernon Street Property. April 24th Transcript 28; May 18th Transcript at 5. In mid-August, the Defendant met with Williams and Troy Godwin. April 24th Transcript at 13.

Although Godwin claims that the Defendant told him that the renovation project was two weeks from completion, the Court finds that the Defendant actually told Godwin that he and his family would be moving into the property in two weeks, but that significant work remained to be completed on the property.[2] *Id.* at 15, 56; May 18th Transcript at 87-88. At that time, the Defendant also told Godwin that he had already invested $600,000 of his own

[2] In reaching this conclusion, the Court has considered the testimony of the Defendant and Godwin, as well as Godwin's handwritten notes that state "move in 9/4," in addition to "two weeks from completion." *See* Exhibit 113. The Court is persuaded that the Defendant told Godwin that he was planning to move into the home on September 4, and that Godwin simply assumed that the house would be complete by that time.

money into the Vernon Street Property project and disclosed that he planned to recoup $340,000 of this money from the proceeds of the $1.65 million loan, leaving $260,000 of his own funds in the project. April 24th Transcript at 30, 63; Exhibit 114. As to his income, the Defendant told Godwin that his income from his employment with SSB was "in the range of $250,000 to $300,000" per year. April 24th Transcript at 15-16. The Defendant and Godwin did not discuss any of the other properties owned by the Defendant at that initial meeting. *Id.* at 16.

Godwin asked the Defendant to provide him with tax returns for tax years 2000 and 2001, which the Defendant supplied. *Id.* at 18; Transcript of Trial, April 25, 2006 (Docket Number 43) (hereinafter "April 25th Transcript") at 49. After this initial meeting, the Defendant also provided the Plaintiff with Exhibit 7. April 24th Transcript at 24. He did so with the intention of assisting the Plaintiff in making its determination as to whether or not to make the loan. Transcript of Trial, May 17, 2006, at (hereinafter "May 17th Transcript) at 12. In Exhibit 7, the Defendant provided the following information about his income,[3] which he characterized in a cover letter as "[i]ncome statement through June 30, 2002":

-From Wachovia Trust- total in 2002 -	$1,104,062.62
Cash Disbursements	$536,634.11
Stock Disbursements	$547,428.52

-Rental Income

[3] Certain line items that are not relevant to this case have been omitted.

From 14th Street Condo-	$21,000
From Frumious Seaside-	$2,625.47
-SSB Payroll	$149,242.95 Includes Feb bonuses

The Defendant's actual income from his employment was based in part on fees and commissions and varied from month to month. May 18th Transcript at 164. Other than indicating that the figure included bonuses, the Defendant did not condition his disclosure of a specific income figure to further indicate that his income from employment is not fixed. May 18th Transcript at 164.

In the information provided regarding his assets, the Defendant provided the following information:

Real Estate Owned:

Cameron Mill Road -	$ 800,000 (no appraisal)
Vernon Road Property-	$ 2,425,000 (based on appraisal)
14th Street Condo-	$980,000 (based on appraisal)
Frumious Seaside -	$1,900,000 (based on appraisal)
Seaside Lots A&B (½ interest)-	$1,500,000 (no appraisal)
Real Estate held in Wachovia Trust-	$2,078,927 (no appraisal)

The Defendant actually held only a power of appointment over the corpus of the Wachovia trust, which was actually the legal owner of the real estate. May 17th Transcript at 79. Under his power of appointment, the Defendant could appoint property from the trust to his wife or any of his four children. *Id.* at 79. Godwin testified that, based on the classification of the real estate as "owned," as well as his conversations with the Defendant, he was led to believe that the Defendant directly owned the real estate in the Wachovia trust

and could access the property in the trust in "his sole discretion." April 25th Transcript at19-20. Godwin also testified that the Defendant told Godwin and Williams that he was "a ten percent owner of a $200 million trust beneficiary." *Id.* at 19. He further testified that the Defendant told him and Williams that he was a "beneficiary" of three trusts. April 24th Transcript at 115; April 25th Transcript at 52. When asked whether he understood the Defendant's representations regarding the trusts to mean that the Defendant could liquidate, transfer, or encumber the real estate held within the trust upon his whim, Godwin answered in the affirmative on the basis that the Defendant "owned the real estate trust." April 25th Transcript at 52. In Godwin's view, there is no difference between being an owner and being a beneficiary. *Id.* at 52. Godwin admitted that the Defendant did not tell him that he could access the money in the trust at any time he wanted, but testified that the Defendant had told him that he received distributions of $1.1 million in 2002 and that he verbally disclosed to Godwin and Williams that he would be receiving between $400,000 and $500,000 per year in distributions from the trust going forward. April 24th Transcript at 111, 124. The Defendant made no written representations as to his future trust distributions. *Id.* at 111.

As to the value of Cameron Mill Road, the Defendant selected the value of $800,000 by multiplying the then current selling price of one-acre lots ($40,000) by 25 acres and applying a 20% discount. May 18th Transcript at 103. Additionally, the Defendant indicated that the listed value for the 14th Street Condo had been obtained from an appraisal,

when in fact, the Defendant had used his own valuation for the property based on his opinion of square-foot values for similar condominiums, as well as the cash flow of the specific property. May 17th Transcript at 32; May 18th Transcript at 104. The most recent appraisal the Defendant had received in October 1997 valued the property at $575,000. May 17th Transcript at 31. The property later appraised for $810,000 in March 2003. *Id.* at 30. However, the Defendant did disclose in Exhibit 7 that he was trying to sell the 14th Street Condo at an asking price of $799,000. Exhibit 7; April 24th Transcript at 102.

The Defendant provided the following information[4] about his liabilities:

Bank of America	
Credit Line	$69,551
Mortgage on 14th Street Condo	$318,566
Community Bank and Trust	
Unsecured	$100,000
Secured by 14th Street Condo	$473,375
Commercial Bank and Trust	
Seaside Lot purchase	$500,175
Frumious 3rd Mortgage	$197,818
Seaside Construction	$484,848.50
SunTrust	
Revolving Loan	$200,745
Unsecured Revolving Loan	$200,125
Cameron Mill Equity Mortgage	$628,350
Vernon Road Construction Loan	$426,586 (advance of $55,000 in July to Parham)
Checking Line of Credit	$5,000

[4] Certain line items that are not relevant to this case have been omitted.

Wachovia	
Line of Credit	$245,000
Car Loan	$35,218
Wells Fargo	
Frumious Seaside Mortgage	$1,150,000
Frontier National Bank	
Mortgage on Vernon Street	$580,370.06

In Exhibit 7, the Defendant also indicated expected debt reduction as follows:

Frumious Seaside $1,347,818 Paid by sale of property, close 10/15/02
Cameron Mill Road $425,000 Paid by sale of property, close 9/1/02

Although Exhibit 7 anticipates that the debt secured by Frumious will be paid off by the sale of the property in October 2002, the sale actually closed in May 2004. May 17th Transcript at 5. The Cameron Mill Road sale actually closed on or about September 25, 2002. *Id.* at 49.

Finally, the Defendant provided a further summary of his real estate. This section indicates the following debts secured by each piece of real estate owned by the Defendant and his wife, as well as the Defendant's contribution to equity, the value of the property, expected sales, and rental income:

Vernon Street Property		
Frontier National Bank	$580,370	7.04% 5/1 Arm maturing 5/1/2031 Monthly payments $3,911
SunTrust Construction	$481,585	4.75% maturing 9/15/02 Interest only monthly $1725 appx.
Mark Callaway out of pocket	$689,168	

To Ben Parham $521,999

$1,751,123

Appraisals $2.5 million and $2.35 million- average $2,425,000

Total cost of Purchase/Renovation $2,235,000

$ (483,877)

Frumious Seaside

Wells Fargo (1st Mortgage) $1,150,000 5.25% 10/1 ARM maturing 2022
Monthly payments $5,031.25

Commercial Bank & Trust $197,818 6.5% interest payable annually
Renewable annually ----------

$1,347,818

Property generates $70,000 rental income annually
Appraisal $1.9 million
For sale at asking price of $2.65 million
Contract at $2.3 million
$952,182 equity

Despite the fact that the Defendant listed Frumious as generating $70,000 of rental income annually, the actual amount of rental income from Frumious varied from year to year and could swing from as low as zero dollars to as high as $140,000, depending on how many days the property was rented. April 25th Transcript Part 2 at 70; May 17th Transcript at 15. For example, in the year 2000, the rental income from Frumious was $4423.55. May 17th Transcript at 14. The Defendant obtained the $70,000 figure from his 2001 tax return. April 25th Transcript Part 2 at 70. In the income section of Exhibit 7, which is captioned

"[i]ncome statement through June 30, 2002," the Defendant stated that Frumious had generated $2,625.47. This is roughly consistent with the actual income generated year-to-date as of May 31, 2002, as reflected by the statement received from Seaside Development Community (Exhibit 21). May 17th Transcript at 13. The rental income amounts disclosed were gross revenues. In the year 2001, the Defendant spent $121,000 to operate Frumious. *Id.* at 15.

Additionally, although Exhibit 7 disclosed the expected sale of Frumious in October 2002 for $2.3 million, the property was actually sold in May 2004 for $2 million. May 17th Transcript at 5. The Defendant had, in fact, signed a contract in August 2002 for the sale of Frumious for $2.3 million. *Id.* at 27.

Godwin testified that he believed that, at the time Exhibit 7 was prepared, Frumious was encumbered by two additional mortgages that the Defendant had failed to disclose, but he could not identify those mortgages. April 24th Transcript at 93. The Defendant provided Godwin with a copy of the contracts for the sale of Frumious (Exhibit 3) and told Godwin that he expected to clear approximately $600,000 from the sale, which he would use to pay down existing debt. *Id.* at 22.

14th Street Condo		
Bank of America (1st mortgage)	$316,946	6.375% 15-year fixed maturing12/2012 Monthly payments $3,457
Community Bank (2d mortgage)	$473,375	5 1/4% payable quarterly Renewable annually Quarterly payments of $13,250 principal plus interest (appx $17,000

quarterly)
Property generates $42,000 rental income annually -leased through 2004
Appraisal $980,000
For sale at asking price of $799,000

Exhibit 7 listed the 14th Street Condo as generating $42,000 annually in rental income. The Defendant did not state in Exhibit 7 that the rental income listed was a gross figure and did not disclose the costs of operating the 14th Street Condo in Exhibit 7. May 17th Transcript at 28. The costs of operating the 14th Street Condo in 2000 and 2001 were disclosed on the Defendant's 2000 and 2001 tax returns, which the Defendant also provided to the Plaintiff. *Id.* at 29. It was Godwin's practice, based on what he views as the rules of financial statement analysis, to consider any disclosure of rental income as a net figure. April 24th Transcript at 77.

The Defendant listed the second mortgage on the 14th Street Condo as being "renewable annually," when in fact the mortgage was a term note with a three-year term, which was to come due in February 2004. May 17th Transcript at 33. The Defendant also failed to disclose a debt secured by the 14th Street Condo, which was owed to Community Bank and Trust in the approximate amount of $100,125. *Id.* at 34. This debt was disclosed on Exhibit 7, but it was listed as an unsecured debt. *Id.* The debt represented what had been an unsecured line of credit obtained by the Defendant's wife that eventually became collateralized by the 14th Street Condo. *Id.* at 34-35.

Lots 3A and 3B -Seaside

Commercial Bank & Trust

Loan for lot purchase	$500,175	6.5% interest only maturing 9/8/02
Loan for construction	$484,484	7.5% interest only maturing 9/8/02

Appraisal at $3,000,000
Mark Callaway owns 50% interest, Charles Hudson Jr. owns other 50%

Expect to combine to new 10-15 year loan at 5/14% interest only
Payments at that rate would be about $4,307 per month

As to Seaside Lots 3A and B, the Defendant disclosed that he owned a 50% interest in the lots, which had an appraised value of $3 million. He also listed his personal debt of $984,000, which was secured by that property, but he did not indicate that the $984,000 debt was not the only debt encumbering the property or that the co-owner of the property also owed $1 million, which was also secured by the property. *Id.* at 39.

Cameron Mill Road

~~SunTrust $500,000 4 3/4% (Prime) Interest only~~ Cancelled as of Sept 1 2002
Monthly payments $1979
~~SunTrust $128,809 4 3/4% (Prime) Interest only~~
Monthly payments $506

Exhibit 7 indicates the debt secured by Cameron Mill Road was to be paid off on September 1, 2002, but the debt was not in fact paid down until after the sale of Cameron Mill Road, which did not close until September 25, 2002. May 17th Transcript at 49. Although the Defendant valued Cameron Mill Road at $800,000, he initially provided

Godwin with a contract for the sale of Cameron Mill Road for a sales price of $500,000. April 24th Transcript at 131; April 25th Transcript at 9. The sale of Cameron Mill Road did not produce sufficient proceeds to pay off the debt to SunTrust. The deficiency of approximately $200,000 later became secured by Frumious. May 17th Transcript at 5; 20-22. Godwin testified that the Plaintiff would have considered the information on Exhibit 7 to mean that the Defendant was planning to sell Cameron Mill Road and use the proceeds along with funds from another source to pay the entire debt owed on Cameron Mill, such that there would be no future debt service or mortgage on any other property resulting from that debt. April 25th Transcript at 28.

Following the initial August meeting and Godwin's receipt of Exhibit 7, Godwin checked the Defendant's credit through Transunion Credit Report Agency. April 24th Transcript at 19-20. The Plaintiff also commissioned an appraisal of the Vernon Street Property, which was completed by Joyce Trimble on September 9, 2002. *Id.* at 20. The appraised value of the Vernon Street Property was $2.5 million. *Id.* Godwin also personally inspected the Vernon Street Property in September 2002.

Prior to making a recommendation on the Defendant's loan request, Godwin prepared an internal "consumer loan application" (Exhibit 9), an accompanying loan memorandum (hereinafter Exhibit 114), and a "global debt service coverage financial worksheet" (hereinafter Exhibit 123). April 24th Transcript 19, 23, 131; April 25th Transcript at 21. To complete Exhibit 9, Godwin relied on the oral representations made by the Defendant,

as well as the information provided on Exhibit 7. April 25th Transcript at 21.

Godwin used the information contained in the Defendant's tax returns, the information contained in Exhibit 7, and the Defendant's credit report to prepare the global debt coverage financial worksheet (Exhibit 123). April 24th Transcript at 131-32. Godwin used all of the information provided by the Defendant through Exhibit 7, the Defendant's tax returns, and the contracts for pending sales to prepare the loan memorandum. April 25th Transcript at 7. It contains several errors. For instance, Godwin stated that the amount of the debt on Cameron Mill Road was $425,000, when Exhibit 7 clearly states in two places that the debt on Cameron Mill Road was $628,000. Exhibit 114. Additionally, Godwin stated that the amount of the debt owed to SunTrust secured by the Vernon Street Property was $730,000, when Exhibit 7 clearly stated that the balance of that loan was $481,585.

When determining whether to approve the $1.65 million loan, Godwin testified that the most important factor for the Plaintiff's consideration was whether the Defendant had the ability to repay the loan. April 24th Transcript at 24. However, he also testified that, of the information provided by the Defendant, the Plaintiff considered all of the items of information "equally important in granting the loan request." *Id.* at 29. In this regard, the Plaintiff considered the primary source of repayment for the loan to be the Defendant's income, including the Defendant's salary, returns on investments, rental income, and trust distributions, and funds generated by the sale of collateral. *Id.* at 23-24. The Plaintiff considered the ability to liquidate the collateral for the loan as a secondary source of

repayment. *Id.* at 24. The Plaintiff also considered the fact that the Defendant had performed in accordance with the loan agreement on the loan acquired from Frontier Bank to purchase the Vernon Street Property and the fact that the Defendant had been "introduced" to the Plaintiff by Williams, who had a previous relationship with the Defendant. *Id.* at 28.

On August 29, 2002, the Defendant signed a document that stated that everything stated in his loan application was correct to the best of his knowledge. Exhibit 10. This statement also authorized the Plaintiff to check the Defendant's credit and acknowledged that the Defendant understood that he "must update credit information" at the Plaintiff's request if his financial condition changed. Exhibit 10. On September 10, 2002, the Defendant borrowed an additional $150,000 from Commercial Bank and Trust of Troup County, which was secured by Frumious. The Defendant did not disclose this fact to the Plaintiff prior to the closing of the $1.65 million loan. May 17th Transcript at 18; May 18th Transcript at 118; Exhibit 27.

The Plaintiff loaned the Defendant $1.65 million, and the loan closed on or about September 17th, 2002. May 17th Transcript at 18; Exhibit 2. Upon the closing of the $1.65 million loan, the Plaintiff paid off the loans to Frontier Bank and SunTrust Bank and disbursed $571,342.64 to the Defendant. April 25th Transcript Part 2 at 69. The Defendant deposited $400,000 of this disbursement into a demand account held by the Plaintiff. May 18th Transcript at 132; Exhibit 2.

In early October 2002, following the closing of the $1.65 million loan, the Defendant received another statement from Parham indicating that the project costs had exceeded his earlier highest estimate of $1.5 million and was currently at $1.8 million. *Id.* at 65. At that point, the Defendant hired an attorney to draft and send a letter to Parham, which demanded that he stop working on the project and leave the premises. *Id.* Work on the project stopped thereafter for several months, with Parham returning to the premises in late 2002 to install weather stripping. *Id.* at 66-67.

In December 2002, the Defendant consolidated several unsecured notes owed to SunTrust, as well as the deficiency balance from the sale of Cameron Mill Road, into one note for $616,970. This note eventually became secured by an additional mortgage on Frumious. May 17th Transcript at 20-22.

At some time in February 2003, the Defendant contacted Godwin to discuss the cost overruns and the possibility of obtaining an additional loan of $350,000 from the Plaintiff. May 18th Transcript at 133. Between the closing of the $1.65 million loan and the Defendant's request to borrow an additional $350,000, the Defendant and his wife had timely made the required payments of the $1.65 million loan. April 24th Transcript at 32. The Defendant told Godwin that he planned to invest an additional $350,000 of his personal funds into the Vernon Street Project. May 18th Transcript at 133. Godwin requested updated financial information from the Defendant, and the Defendant provided Godwin with an updated statement of income and liabilities (hereinafter "Defendant's Exhibit 48") as

follows:

12/31/02
Income Sources 2002

From Wachovia Trust

Total in 2002	$1,104,062.62
Cash Disbursements	$536,634.11
Stock Disbursements	$547,428.52

From Suntrust Trust fbo MCC

Total in 2002	$39,043.17

From Suntrust Trust fbo DCC

Total in 2002	$21,269.33
Trust Withdrawals	**$1,164,375.12**

Rental Income		
14th Street Condo	$42,000.00	
Frumious Seaside	$ 2,625.47	
Director Income- DCC	$4,800	
MAEJIC LP income	$10,000	
Dividends	$11,839.33	
SSB Payroll	$251,541.04	
Earned Income	**$322,805.84**	

The Defendant also attached a "Loan Summary," which was also dated (by hand) December 31, 2002. The Loan Summary disclosed the following information about the Defendant's loans as of the end of 2002.

Bancorpsouth Bank	$1,650,000

mortgage on Vernon Street property

Bank of America		
Credit line -	$69,551	
Mortgage on 14th Street Condo-	$302,493	
Community Bank & Trust		
replaces #60100009	$100,000	Maturity 4/1/2003
second mortgage on 14th Street Condo-	$446,325	
Commercial Bank & Trust		
second mortgage on Frumious Seaside	$605,043.60	Maturity 10/15/2004
Suntrust		
Revolving loan annual renewal	$616,820	Maturity 12/30/2003
Wachovia		
Line of credit	$245,000	Maturity 3/6/2003
Wells Fargo	$1,150,000	
Equity line of credit on Frumious		
Total $4,985,232.60		

The Loan Summary represented the state of the Defendant's liabilities after the debt reductions and loan consolidations that the Defendant had been anticipating at the time he prepared Exhibit 7. May 18th Transcript at 134.

Godwin and his loan processor again created an internal "consumer loan application" (hereinafter "Exhibit 28") using all information previously obtained from the Defendant, including Exhibit 7. April 24th Transcript at 34-35; April 25th Transcript at 7. On March 3, 2003, the Plaintiff checked the Defendant's credit again in connection with the $350,000 loan request. April 24th Transcript at 35; Exhibit 119.

On February 28, 2003, Godwin updated his earlier loan memorandum (hereinafter "Defendant's Exhibit 58"). April 24th Transcript at 145. Defendant's Exhibit 58 also contains several errors. Defendant's Exhibit 58 continues to list Cameron Mill Road (a vacant piece of property) as an asset of the Defendant and states that the Defendant expected to sell it for $500,000, which would pay off the debt of $425,000. However, by that time, the Defendant had sold Cameron Mill Road. Additionally, Defendant's Exhibit 58 lists the rental income for the 14th Street Condo at $65,000, while Defendant's Exhibit 48 discloses rental income of only $42,000. May 18th Transcript at 137. Godwin prepared a subsequent loan memorandum for the $350,000 loan (hereinafter "Exhibit 120"), which is dated March 12, 2003. Exhibit 120 also contains errors, such as the statement that the Defendant earned $350,000 from his employment, rather than the $251,000 figure the Defendant disclosed on Defendant's Exhibit 48. *Id.* at 142; Exhibit 120. Godwin testified that the use of the $350,000 figure was a typographical error, as he had been referencing the number $350,000 several times in the course of writing that memorandum and had mistakenly typed $350,000, when it should have been $300,000. April 24th Transcript at 151. Additionally, Godwin stated that all of the proceeds from the Plaintiff's "loans" had been used in the Vernon Street property. This statement was incorrect, as the Defendant had retained funds from the $1.65 million loan, and Godwin was aware of this fact when he prepared Exhibit 120. May 18th Transcript at 141.

Prior to the closing of the $350,000 loan, the Defendant told Godwin that the

Defendant and Parham had agreed that the cost overruns on the Vernon Street Property would be $750,000, as opposed to the $1 million originally claimed by Parham. April 24th Transcript at 33. The Defendant also told the Defendant that he would use the $350,000 loan to pay the cost overruns and would himself fund the remaining $400,000. *Id.*; May 17th Transcript at 51. The Plaintiff claims that it relied on the Defendant's promise because it ensured that the Defendant would have additional equity in the Vernon Street Property that would "increase the value of the property." April 24th Transcript at 36. Godwin also testified that the Plaintiff would not have made the loan without the representation that the Defendant was putting additional funds into the Vernon Street project. *Id.* at 37.

The Plaintiff agreed to loan an additional $350,000 to the Defendant. It appears that Parham had filed a lien against the Vernon Street Property for amounts owed in connection with the renovation project, or at least that the Plaintiff believed that Parham had done so. The Plaintiff made the loan upon the condition that the lien would be removed from the property. *Id.* at 38. The Plaintiff also contends that the loan was conditioned on the direct payment to Parham of both the $350,000 borrowed funds and the Defendant's portion in order to ensure that the project was completed and that the dispute between the Defendant and Parham was finally resolved and did not result in additional litigation that might distract the Defendant, put a drain on his financial resources, and impair his ability to service the debt owed to the Plaintiff. April 25th Transcript at 30. To this end, the Plaintiff intended that the loan proceeds would be disbursed to an escrow account and held until Parham had

signed a lien waiver *and* the Defendant had paid the additional funds to Parham. April 24th Transcript at 38-39. Godwin testified that the requirement of having the Defendant pay $400,000 to Parham, the requirement of the loan proceeds being released directly to Parham in exchange for the lien release, and the requirement that the project would be completed were verbally discussed with the Defendant and the attorney. The Defendant, however, testified that he never agreed to this arrangement. May 17th Transcript at 51. The terms of the escrow agreement (Exhibit 90) did not require the Defendant to pay Parham $400,000 prior to receiving the loan proceeds. April 25th Transcript at 58; Exhibit 90. Parham did sign a lien release on May 1, 2003 after the closing of the loan and after the Defendant and his wife had received the funds. Exhibit 82; May 17th Transcript at 56.

Godwin testified that the Defendant did not tell the Plaintiff that the settlement amount with Parham had been reduced until the time he told the Plaintiff that he would not be able to make the loan payments. April 24th Transcript at 42-43. The Defendant, however, testified that the Plaintiff clearly knew by April 2003, when the final loan was disbursed, that the settlement amount had been negotiated down to $350,000. May 18th Transcript at 157. When asked whether he had told the Plaintiff that he was not "giving Parham" the entire $350,000 loan proceeds, the Defendant testified that he did not recall "what he told the Bank." May 17th Transcript at 58.

After the parties went to mediation in February and March, at the end of April, the Defendant and Parham reached an agreement that reduced the number owed to Parham to

$350,000. May 18th Transcript at 133; May 17th Transcript at 54, Exhibit 84. The settlement agreement, which was executed on April 30, 2003, obligated the Defendant to pay Parham $350,000, of which he was to pay $50,000 upon the signing of the settlement agreement. Parham agreed to accept a note for $250,000 that obligated the Defendant to make quarterly installment payments. May 17th Transcript at 52; May 18th Transcript at 143. The settlement agreement also required Parham to complete a "punch-list" of items on the project before the Debtor would be obligated to pay the remaining $50,000. May 18th Transcript at 143; Exhibit 84. The Defendant made the $50,000 initial payment to Parham and one or two of the installment payments. May 18th Transcript at 148. The Defendant testified that he did not pay the remaining installment payments because he believed that Parham had defaulted on the settlement agreement by failing to complete the remaining items. May 17th Transcript at 52. Parham sued the Defendant and his wife in October 2003 for breach of the settlement agreement. May 17th Transcript at 88; Exhibit 56.

Parham testified that, during his negotiations with the Defendant, the Defendant discussed the possibility that he may have to file bankruptcy. April 25th Transcript at 66. Godwin testified that the Plaintiff would not have made the $350,000 loan if the Plaintiff had known that the Defendant had threatened to file bankruptcy during his dispute with Parham. Godwin also testified that the fact that the Defendant had filed for divorce from his wife would have been material to the Plaintiff's decision to make the loan, as any child support or alimony awarded could have impacted the Defendant's ability to service his other

obligations. *Id.* at 31. Williams also testified that the fact that the Defendant was having marital problems, which the Defendant did not tell him, would have had an adverse affect on the Plaintiff's decision to make the loan. May 18th Transcript at 7-8. The Defendant had filed for divorce from his wife in January 2003, but dismissed that petition in March 2003, and re-filed the petition in July 2003. April 25th Transcript Part 2 at 19. After the petition was re-filed, the Defendant and his wife reached a settlement of the divorce action. *Id.* at 21.

The Defendant made only one payment on the $350,000 loan on June 12, 2003, and, shortly thereafter, the Defendant ceased making payments to the Plaintiff on either loan. April 24th Transcript at 45; May 18th Transcript at 149. The Plaintiff and the Defendant and his wife attempted to work out a restructuring of the loans, but were unable to do so. April 24th Transcript at 45-46. In October, the Plaintiff proceeded with a foreclosure, from which it purchased the Vernon Street Property for $840,000, and later sold the property to Charles Hudson, Jr., the Defendant's cousin, for $895,000. *Id.* at 47, 50, 170; May 18th Transcript at 24. Between the foreclosure and the sale to Charles Hudson, Jr., the Plaintiff obtained a second appraisal of the property from Joyce Trimble. April 24th Transcript at 48; May 18th Transcript at 16. At that time, the property appraised for $1,050,000. April 24th Transcript at 48; May 18th Transcript at 16.

On approximately April 12, 2004, the Plaintiff obtained a judgment against the Defendant and his wife (Exhibit 238) for the deficiency in the amount of $2,379,180.20, plus

post-judgment interest from the date of entry. April 24th Transcript at 46; May 17th Transcript at 93; May 18th Transcript at 10; Stipulation of Facts, ¶ 12. The Defendant filed a voluntary petition under Chapter 7 of the Bankruptcy Code on December 9, 2004. The current amount owed to the Plaintiff by the Defendant, including post-judgment interest, is $2,050,504.82. May 18th Transcript at 11.

In preparation for this litigation, the Plaintiff hired an expert witness, James Shumaker, to review the loans at issue and the Plaintiff's decision-making process to determine whether the Plaintiff's decision to make the loans to the Defendant was made in accordance with customary lending practices, FDIC regulations, and the Plaintiff's own internal loan policy. Shumaker is a bank examiner and credit analyst employed by the State of Alabama Banking Department with thirty-four years of experience with the Federal Deposit Insurance Corporation. May 17th Transcript at 99; 109. The Court qualified Shumaker as an expert with regard to lending and credit analysis. *Id.* at 110.

In forming his opinion, Shumaker reviewed the Plaintiff's loan policy to determine whether the specific loans were made in compliance with that policy and with the applicable rules and regulations. Shumaker also considered the depositions of the Plaintiff's representatives, including the statements made by Godwin that the Defendant had made certain oral representations to Godwin regarding his income. *Id.* at 113. Additionally, Shumaker reviewed the loan file, which included the credit reports relied upon by the Plaintiff in making its loan decision, the commitment letters, the Defendant's financial

statements, the loan memoranda, the Defendant's settlement agreement with Parham and the lien release, the note from the Defendant to Parham, Exhibit 7, the commitment for title insurance and the title insurance policy for the Vernon Street Property, Goodwin's handwritten notes from his meeting with the Defendant, the loan applications, the Defendant's 2001 tax return, and the appraisal for the Vernon Street Property. *Id.* at 100-01. Shumaker concluded that, based on all of the information available, he would have determined the Defendant to be creditworthy. *Id.* at 113, 117. He also found that the Plaintiff had followed its internal loan policy and had performed a normal and customary degree of due diligence in analyzing the loans, and that the decision to make the loans was consistent with normal and customary practices of lending in the industry. *Id.* at 113-14.

Shumaker agreed that, when looking at Exhibit 7, he could not tell from the Defendant's statement that the 14th Street Condo generated $42,000 income whether that income was net or gross. He opined that he would want to know whether the income was net or gross only if he were analyzing the Defendant's income from Exhibit 7 rather than the "income source statement." *Id.* at 128. He also agreed that determining whether the income stated was net or gross would require further investigation and agreed that one way of investigating further would be to look at the Defendant's tax return. *Id.* at 129. Shumaker testified that the information provided on the tax returns is "kind of the gold standard in credit evaluation because people tend to overstate their income on a financial statement," but are unlikely to overstate their income on their tax returns. *Id.* at 148.

In forming his opinions, Shumaker did look at the Defendant's tax return. *Id.* at 129. He agreed that the tax return showed that, for tax year 2001, the 14th Street Condo and Frumious had negative cash flow. *Id.* at 130-31. Shumaker concurred that the statement in Godwin's 2002 loan memorandum that the 14th Street Condo and Frumious generated enough income to service the debt on the properties was inaccurate based on his review of the 2001 tax return. *Id.* at 132. Shumaker recognized that Godwin's assessment of the Defendant's cash flow was off by $150,000. *Id.* at 132. However, in Shumaker's opinion, the $150,000 error most likely would not have brought the Defendant's cash flow below the acceptable limit such that it would have affected the Plaintiff's decision to make the loan. *Id.* at 135. Shumaker also agreed that, given the knowledge that the Defendant's compensation varies, as evidenced by the disclosure of his receipt of a bonus in February, simply doubling his income from employment as of June 30, 2002 to obtain a yearly income would not be prudent. *Id.* at 155.

As to the second loan memorandum prepared for the $350,000 loan, Shumaker agreed that Godwin had made an additional error of $100,000 per year with regard to the Defendant's income from SSB. *Id.* at 137. Shumaker admitted that the combination of the cash flow errors from the rental properties and the SSB income may have been significant enough to affect the cash flow percentage and lending limits under the Plaintiff' lending guidelines, but stated that the Plaintiff's policies did not even require the Plaintiff to get financial statements on a first mortgage on a principal residence. Therefore, in his opinion,

the Plaintiff was already doing more than it was required to do. *Id.* at 138. However, Shumaker agreed that the Plaintiff's loan policy would have required the Plaintiff to obtain a financial statement signed by the Defendant on a form approved by the Plaintiff's loan administration in connection with the $350,000 loan, as it was a second mortgage. *Id.* at 140.

When asked whether the Plaintiff conducted any investigation above and beyond what the Defendant had provided to the Plaintiff, Shumaker stated that the Plaintiff: 1) obtained credit reports to determine whether the Defendant could service his existing debt; 2) obtained the Defendant's tax returns to determine whether the income levels reported by the Defendant on Exhibit 7 were consistent; 3) obtained an independent appraisal of and title search on the collateral; and 4) relied upon the past experience of its bank officer in having made a previous loan to the Defendant. *Id.* at 148-49.

Lea Coe was the Defendant's personal/administrative assistant and worked for the Defendant for about twenty years. *Id.* at 58. She performed bookkeeping for the Defendant and often signed checks issued from his bank account. Transcript of Trial, May 22, 2006 (hereinafter "May 22nd Transcript") at 5; May 17th Transcript at 58-59.

CONCLUSIONS OF LAW

The discharge of pre-existing debt is one of the most primary tenets of bankruptcy policy. Indeed, "a central purpose of the Code is to provide a procedure by which certain

insolvent debtors can reorder their affairs, make peace with their creditors, and enjoy 'a new opportunity in life with a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.'" *Grogan v. Garner*, 498 U.S. 279, 286 (1991) (citations omitted). At the same time, however, a separate equitable policy mandates that any such mechanism for an unencumbered fresh start only should redound to the benefit of those debtors who are unfortunate, yet honest. *Id.* at 286-87. In light of these competing policy goals, Congress included the following provision in the Bankruptcy Code:

> (a) A discharge under section 722, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor of any debt–
>
> * * * *
>
> (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; [or]
>
> (B) use of a statement in writing . . . that is materially false . . . respecting the debtor's or an insider's financial condition . . . on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied . . . [,] and that the debtor caused to be made or published with intent to deceive.
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> * * * *

11 U.S.C. § 523(a)(2)(B). Thus, through section 523(a)(2), the Code offers a means of denying those individuals who do not qualify as "honest but unfortunate debtors" the

benefits of a fresh start. *Id.* at 287. Like other exceptions to discharge, however, the provisions of section 523(a)(2)(B) warrant narrow construction. *See Gleason v. Thaw*, 236 U.S. 558, 562 (1915); *Schweig v. Hunter (In re Hunter)*, 780 F.2d 1577, 1579 (11th Cir. 1986). The plaintiff bears the burden of establishing non-dischargeability under section 523(a)(2). *Hunter*, 780 F.2d at 1579.

A. *Section 523(a)(2)(B)*

To succeed under section 523(a)(2)(B), the plaintiff must establish by a preponderance of the evidence that the debtor owes the plaintiff a debt that "was obtained by a writing: (1) that is materially false; (2) respecting the debtor's or an insider's financial condition; (3) on which the creditor to whom the debt is liable for such money, property, services, or credit reasonably relied; and (4) that the debtor caused to be made or published with the intent to deceive. *In re Miller*, 39 F.3d 301, 304 (11th Cir. 1994); *see also In re Izaguirre*, 166 B.R 484 (Bankr. N.D. Ga. 1994) (Massey, J.).

Having considered the evidence and the arguments of counsel, the Court finds that there is no dispute with regard to whether the debtor owes a debt to the creditor that was obtained by a writing respecting the debtor's financial condition. The Defendant clearly owes the Plaintiff a debt for money obtained by the Defendant through the use of Exhibit 7, a written statement concerning the Defendant's financial condition. However, the Court finds, having considered all of the evidence, that the Defendant did not provide a materially

false financial statement to the Plaintiff with the intent to deceive the Plaintiff.

In order to find the first element to have been established, the Court must conclude that the "writing was false at the time it was created, the falsity was material in amount, and the falsity was material in the effect it had on the creditor receiving the writing such that it [a]ffected the creditor's decision making process." *In re Gordon*, 277 B.R. 805 (Bankr. M.D. Ga. 2001); *see also In re Wright*, 299 B.R. 648, 659 (Bankr. M.D. Ga. 2003) ("A falsehood is material if it is 'significant in both amount and effect on the creditor receiving the financial statement'"; the false information must have "'actual usefulness to the creditor receiving the financial statement.'"). Establishing that a representation is false, however, is not sufficient. The creditor must also prove the debtor's intent to deceive the creditor. In determining whether the debtor made a misrepresentation with the intent to deceive the creditor, the court may infer such intent from "'the totality of the circumstances, including the recklessness of a debtor's behavior.'" *Wright*, 299 B.R. at 661 (quoting *In re Miller,* 39 F.3d 301, 305 (11th Cir. 1994)). "'Reckless disregard for the truth or falsity of a statement combined with the sheer magnitude of the resultant misrepresentation may combine to produce the [inference] of intent [to deceive].'" *In re Miller*, 29 F.3d 301, 305 (11th Cir. 1994). "'However, if there is room for an inference of honest intent, the question of nondischargeability must be resolved in the debtor's favor.'" *In re Collier*, 231 B.R. 618 (Bankr. N.D. Ohio 1999) (quoting *In re Druckemiller*, 177 B.R. 859 (Bankr. N.D. Ohio 1994)).

The Plaintiff has alleged that the following representations made in Exhibit 7 were materially false. First, the Plaintiff contends that the Defendant's statements regarding his rental income from the 14th Street Condo and Frumious were materially false. The Defendant stated that the 14th Street Condo generated rental income of $42,000 annually and that Frumious generated $70,000 annually. The Plaintiff complains that the rental income should have been disclosed as a net number rather than a gross number, or that the Defendant should have also disclosed the operating expenses of these properties alongside the rental income figure. Although that may be how the Plaintiff would have liked to have received the information or how the Plaintiff expected and assumed the information was presented, that is not how the Defendant presented the information. The Defendant stated that the property generated a particular amount of income, but no where indicated that it was net of debt service or operating expenses. Accordingly, the Court finds that this statement was not false in that regard.

To the extent that this allegation is viewed as a failure by the Defendant to disclose the existence of the operating expenses, the Court concludes that insufficient evidence was presented to establish whether the Defendant concealed these operating expenses with the intent to mislead the Plaintiff. The Defendant testified[5] that he did not intentionally fail to

[5] In connection with this case, the Plaintiff has moved for the admission of Exhibit 182, which is an e-mail message that appears to have been authored by the Defendant's personal assistant, Lea Coe, and sent to the Defendant. The Defendant objected to the admission of this exhibit due to its lack of relevance to the transaction between the Plaintiff and the Defendant, as well as the fact that the e-mail message was unfairly prejudicial to the Defendant. The Plaintiff asserted that the e-mail message is relevant

state the operating expenses but simply chose to disclose the gross rental income rather than the net income. The Court is inclined to believe that the Defendant would not have intentionally concealed the operating expenses, as he undoubtedly understood that the Plaintiff's representative would have access to his tax returns, which clearly stated the gross income, as well as the principal and interest payments and operating expenses. The Defendant also disclosed elsewhere in Exhibit 7 that the year-to-date gross income of Frumious was substantially less than $70,000 per year, which would have alerted the Plaintiff to the fact that the property would not likely generate $70,000 in 2002, net or otherwise.[6] *See generally In re Collier*, 231 B.R. 618 (Bankr. N.D. Ohio 1999) (the

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because it tends to show that the Defendant and his personal assistant had, in the past, discussed how to present the Defendant's financial information in a manner that would make it look better to a lender. The Court will admit Exhibit 182 over the Defendant's objection, as the e-mail is relevant to this case and the Court does not find that it is unduly prejudicial to the Defendant. That being said, the Court also finds that, even if the Court were to assume that Ms. Coe's statements indicate that she was attempting to "spin" the Defendant's financial information, the e-mail message falls short of establishing that the Defendant encouraged her to do so or that the Defendant did in fact permit her to present, or himself presented, any false information to SunTrust as a result of Ms. Coe's e-mail message. For this reason, the e-mail does not convince the Court that the Defendant previously provided false information to his lenders.

[6] Additionally, even if the omission were intentional, the Court could not find that the Plaintiff established reasonable reliance on the omission of this information, given the fact that the operating expenses for both properties were disclosed in the Defendant's 2001 tax returns, which Godwin testified he reviewed, considered to be part of the Defendant's application, and relied upon in making the loan decisions. At the very least, the disclosure of these expenses created a "red flag" that would have required the Plaintiff to at least ask the Defendant whether his disclosed rental income took into consideration the debt service and operating expenses shown on the tax return. *See In re Harloff*, 272 B.R. 496 (Bankr. M.D. Fla. 2001) ("As concerns the existence of a 'red flag,' '[a] lender cannot claim reasonable reliance on a financial statement that the lender knows is inaccurate or incomplete- particularly where the lender has information in its own files

conclusion that the debtor would not have intentionally omitted a mortgage from his financial statement was supported by the fact that the debtor knew that the lender had access to the debtor's tax returns, which disclosed payment of the interest expense on the mortgage debt).

The Court also notes that the Defendant should have clarified that the rental income for Frumious fluctuates from year to year and can fall within a particular range, or that the rental income for Frumious was $70,000 in 2001, but that it varied from year to year. In this regard, the Court agrees that the Defendant's statement was false. However, the Court finds insufficient evidence to conclude that the Defendant failed to clarify this fact with an intent to deceive the Plaintiff or that he was recklessly indifferent to the truth. The Defendant testified credibly that he took the rental income from his last available tax return and did not intend to mislead the Plaintiff into believing that the amount was or would be the same every year. As noted above, this conclusion is also supported by the fact that the Defendant would have known that his 2000 tax return would have disclosed to the Plaintiff that the income was significantly less than $70,000 in 2000. Additionally, if the Defendant had intended to deceive the Plaintiff into believing that Frumious generated $70,000 each year, it is unlikely

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that confirms the inaccuracies or shows the need for further investigation or confrontation with its customer.'"); *In re Calderone*, 1990 WL 57605, *3 (W.D. Pa. 1990) (finding that the creditor's reliance on a financial statement was not reasonable in light of the fact that "information available to her from 1981 and 1982 tax returns . . . should have prompted her to ask the questions she now raises"). Even the Plaintiff's expert witness agreed that he would not have been able to determine whether the income disclosed on Exhibit 7 was net or gross, and that a person reviewing Exhibit 7 would have had to investigate further.

that he would have disclosed the significantly lower year-to-date income for Frumious elsewhere within Exhibit 7.

Second, the Plaintiff submits that the Defendant's statement of his SSB payroll as $149,242.95 was inaccurate because it did not disclose the fact that the amount varied. The Court finds that this statement was not actually false, as the Defendant did not state that he earned $149,242.95 annually. Additionally, although he did not explicitly state that this income, which was based on fees and commissions, could be expected to fluctuate from year to year, he placed this statement in a section headed "[i]ncome statement through June 30, 2002" and added that the figure included bonuses earned in February 2002, which indicates the Defendant's intent to disclose an accurate, historical figure for his 2002 income, rather than an estimate of his earning potential for the remainder of the year or any following year. Even if one concludes that the Defendant should have clarified further that his salary was not static, the Defendant has failed to prove that the Defendant failed to do so with the intent to deceive the Plaintiff. There is insufficient evidence to support a finding that the Defendant was not making an honest attempt to provide the Plaintiff with the most accurate information regarding his income from employment that he could under the circumstances. It is plausible that the Defendant assumed that the Plaintiff's representative would have understood that salary made by an individual in the brokerage field would not be capable of exact estimation.[7]

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[7] The Court's conclusion is supported by Shumaker's statement that, given the knowledge that the Defendant's compensation varies, as evidenced by the disclosure of

Third, the Plaintiff takes issue with the manner in which the Defendant disclosed his interest in the Wachovia/Synovus trust. Exhibit 7 lists as an asset "real estate held in Wachovia Trust -$2,078,927." The Plaintiff assumed that the Defendant owned the real estate in the trust and that there were no limitations on the Defendant's access to that property. The Court agrees that, technically, the Defendant should have listed the asset held as a power of appointment, which would have clearly put the Plaintiff on notice that the Defendant did not "own" the real estate and could not liquidate or encumber the actual real estate without any restrictions. The Plaintiff has presented sufficient evidence to establish that the failure to clarify the manner in which the trust interest was held was material to the Plaintiff's decision-making process. However, the Court again finds that the failure to clarify the true nature of the ownership of this real estate was not intentional or deceitful. The Defendant appears to have been open and candid with the Plaintiff's representative about the fact that the real estate was owned by the trust. Even Godwin testified that the Defendant told him that he was a beneficiary of a trust. The Defendant clearly assumed that the Plaintiff's representative, an experienced bank officer, would have understood that assets held in a trust, of which one is a beneficiary, are not available to the trust beneficiary without some limitations. If the Defendant had intended to lie about whether he owned the real estate directly, the Court finds it incredible that he would have listed it as being held in a

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his receipt of a bonus in February, simply doubling his income from employment as of June 30, 2002 to obtain a yearly income would not have been prudent. May 17th Transcript at 155.

trust or that he would have told Godwin that he was the beneficiary of a trust.[8]

Fourth, the Plaintiff claims that the Defendant inflated the values of Cameron Mill Road and the 14th Street Condo. The Defendant valued Cameron Mill Road at $800,000, notwithstanding the fact that he had a contract for the sale of that property for $425,000, and he valued the 14th Street Condo at $980,000, notwithstanding the fact that he was asking $799,000 for the property. The Court does not have sufficient evidence to value these properties at the time the Defendant prepared Exhibit 7. The Defendant may have been correct in his valuations. If the Defendant had more time to market the properties, he may have received more from their sale. The only evidence presented by the Plaintiff as to the property's actual value is the fact that the Defendant, who appears to have been under a compunction to sell the properties, was willing to sell the properties for less than the listed value. This does not necessarily tell the Court what a willing seller, who is not under a compunction to sell, would have been willing to pay. As it is the Plaintiff's burden to prove that the statements made were false, the Court finds that the Plaintiff has failed to meet that

[8] Further, the Court has considerable reservations as to whether the Plaintiff could establish that it reasonably relied on the Defendant's failure to clarify his ownership of the real estate. In Exhibit 7, the Defendant clearly stated that this property was "Real Estate held in Wachovia Trust," which should have put the Plaintiff on at least inquiry notice that he did not own the real estate directly and that some form of trust arrangement stood between the Defendant and these assets. Godwin testified at various times that the Defendant told him that he was a "beneficiary" of the trust, which is directly contrary to any statement that he actually "owned" the real estate. At the very least, if the Defendant's characterization of his interest in the real estate held in the trust were contrary or confusing to Godwin, and he were relying on the Defendant having free access to the assets, Godwin should have inquired further or seek clarification from the Defendant as to what he intended by including the trust under Real Estate Owned.

burden as to the Defendant's valuations of these properties. Additionally, if the Court were to find that the values were false, the Court would conclude that the Debtor did not inflate the values with an intent to deceive the Plaintiff. If he had intended to mislead the Plaintiff as to the values, it would have made little sense for him to do so at the same time that he disclosed the fact that he was selling the properties for less than the inflated values and to provide the Plaintiff with copies of a sale contract for Cameron Mill Road.[9]

Fifth, the Plaintiff asserts that the Defendant failed to disclose an additional mortgage on Frumious of $503,000 owed to Commercial Bank and Trust. Exhibit 7 discloses a mortgage on Frumious held by Commercial Bank and Trust in the amount of $197,818 and a mortgage in favor of Wells Fargo in the amount of $1,150,000. The Plaintiff has presented insufficient evidence to establish the existence of an undisclosed mortgage on Frumious at the time the Defendant prepared Exhibit 7. The only evidence submitted was Godwin's testimony that he believes that two additional mortgages existed, but he could not identify those mortgages. Additionally, the Defendant has explained that the $503,000 note reference by the Plaintiff, which was executed on September 11, 2000, was eventually refinanced by a mortgage in favor of Commercial Bank and Trust in the amount of $563,023.85 and paid down to $197,818. May 18th Transcript at 44-45. The $197,818

[9] Alternatively, the fact that the asking and contract prices were less than the value provided by the Defendant would have been a sufficient "red flag" to alert the Plaintiff to question the actual value. The Plaintiff's failure to even ask the Defendant about his values would result in this Court's conclusion, if necessary, that the Plaintiff did not reasonably rely on these values.

mortgage to Commercial Bank and Trust was in fact disclosed on Exhibit 7.

Sixth, the Plaintiff points to the Defendant's failure to disclose the fact that he borrowed an additional $150,000 from Community Bank and Trust of Troup County, which was secured by Frumious, between the time the Defendant requested and received the proceeds of the $1.65 million loan. The Defendant asserts that his failure to disclose this transaction cannot be a false statement for purposes of Exhibit 7 because he had not obtained the mortgage at the time he prepared Exhibit 7 and did not have a duty to update the financial information provided to the Plaintiff unless asked to do so by the Plaintiff. The Court agrees, as there is no evidence that the Plaintiff ever requested updated financial information from the Defendant prior to the time the Defendant provided such information in connection with the $350,000 loan.

Seventh, the Defendant listed the second mortgage on the 14th Street Condo as being "renewable annually." This statement was false, as the mortgage was a term note with a three-year term, which was to come due in February 2004. Also, the Plaintiff claims that the Defendant failed to disclose a debt owed to Community Bank and Trust that was secured by the 14th Street Condo in the approximate amount of $100,125. The Defendant acknowledged that he failed to disclose this as a secured debt, but noted that the debt was disclosed on Exhibit 7 as an unsecured debt. The Court does not find that the Defendant made either of these misstatements with the intent to deceive the Plaintiff. First, the Court simply finds no reason why the Defendant would have been motivated to falsely characterize

the three-year term note as renewable annually, when the term of the note was not in fact due for renewal until February 2004 and he was expecting to sell the 14th Street Condo and pay off the loan early. Under those facts, the Defendant would have assumed that the nature of this loan would have little impact on the Plaintiff's loan decision and would have had no reason to lie about it. As to the mischaracterization of the $100,125 debt as unsecured rather than secured, the Court is persuaded that the Defendant made an unintended error in not placing the debt in the proper place, most likely due to the fact that the debt was originally an unsecured line of credit obtained by his wife.

Eighth, the Plaintiff contends that the Defendant made a false statement regarding the extent of the liabilities encumbering Seaside Lots 3A and 3B. In Exhibit 7, the Defendant stated that he was liable for a loan in the amount of $500,175 for the purchase of the lots and a loan in the amount of $484,484 for the construction of the lots. He stated that he owned only a 50% interest in the lots and that Charles Hudson, Jr. owned the other 50% interest. However, the Defendant did not disclose that the lots themselves were encumbered by an additional $1 million in debt personally owed by Charles Hudson, Jr. The Plaintiff takes issue with the fact that, although the Defendant correctly disclosed his personal liability for the debt secured by Frumious, the Defendant did not accurately reflect the fact that his 50% interest in the Seaside Lots was encumbered by additional debt for which the co-owner was personally liable. Accordingly, the Plaintiff appears to have believed that the total equity in the property was approximately $2,000,000, and that the Defendant's one-half share of

that equity was $1,000,000. In actuality, considering the total debt on the property, the equity was $1,100,000. In the Defendant's view, his interest in the property was worth $1.5 million, and his share of the debt encumbering the property was $984,659, leaving him $515,000. While the Court agrees that information concerning the entire debt placed on the Lots would have been relevant to the Plaintiff's loan decision, the Court finds insufficient evidence to support the conclusion that the Defendant concealed this information with the intent to deceive the Plaintiff. The Defendant testified that he believed he was disclosing his true financial condition when he reported that he was a 50% owner of the lots, that the lots were worth $3 million, and that he was personally liable for only approximately $1 million in connection with the property.

Ninth, as to Cameron Mill Road, the Plaintiff contends that the Defendant falsely claimed that the debt encumbering Cameron Mill Road would be fully paid to SunTrust when the sale of Cameron Mill Road closed. The means by which the Defendant listed the debts to SunTrust, marked them through, and wrote "Cancelled as of Sept 1 2002" next to them, does appear to be a statement that the debt would be fully paid off in September 2002. This statement was false at the time it was made, as the Defendant knew at that time that Cameron Mill Road would not produce sufficient funds to pay off the entire debt. Again, the Court's consideration of the Defendant's testimony persuades the Court that the Defendant did not state that the debt would be canceled or fail to disclose that he would continue to owe SunTrust some amount as a deficiency following the sale of Cameron Mill

Road with the intent to deceive the Plaintiff. The Defendant clearly stated the amount of the debt secured by Cameron Mill Road, as well as the expected sale price for the property. If he truly intended to mislead the Plaintiff into believing that the entire debt secured by Cameron Mill Road would be paid following the sale of the property, it is difficult for the Court to believe that he would have been so obvious about the fact that the sale of the property would leave a significant deficiency.

For the reasons stated above, the Court concludes that the Defendant did not provide the Plaintiff with a materially false financial statement with the intent to deceive the Plaintiff.[10] Accordingly, the Court cannot conclude that the debt owed to the Plaintiff is nondischargeable under section 523(a)(2)(B).

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[10] The Plaintiff has made much of the fact that the Defendant seemed to be more candid in his correspondence with John Thompson at Community Bank & Trust regarding his financial situation than he was with the Plaintiff's representatives. From the letter, it appears that the Defendant disclosed no information to Thompson that he did not disclose to the Plaintiff during the process of applying for the $1.65 million loan. The Defendant told the Plaintiff that the Vernon Street Property was costing more than he had originally budgeted, that he had several options for raising the extra money, such as selling his interest in Seaside Lots 3A and 3B, selling Cameron Mill Road, and selling the 14th Street Condo. The fact that the Defendant used the phrase "between a rock and a hard place" in his letter to Thompson but never said these words to the Plaintiff does not convince the Court that the Defendant was less candid with the Plaintiff. The Defendant was conveying to Thompson the fact that he had encountered unexpected costs in renovating the Vernon Street Property and that he was concerned about whether the property would appraise for more than $1.4 million and about how he would raise the additional $500,000 that he had not expected to need. By the time the Defendant was working with the Plaintiff, the Vernon Street Property had appraised for $2.5 million. Therefore, there would have been no need for the Defendant to voice that concern to the Plaintiff. Additionally, it should have been obvious to the Plaintiff that the Defendant could not fund the additional $500,000, as he was seeking to borrow that amount for the completion of the property. The Court cannot see how the Thompson letter proves that the Defendant withheld information from the Plaintiff, intentionally or otherwise.

B. *Section 523(a)(2)(A)*

The Plaintiff also seeks a determination that the debt owed by the Defendant to the Plaintiff is nondischargeable under section 523(a)(2)(A). Here, there is no dispute that the Defendant owes the Plaintiff a debt "for money, property, services, or an extension, renewal, or refinancing of credit." To establish that this debt is excepted from discharge under section 523(a)(2)(A), a plaintiff must prove by a preponderance of the evidence that:

> (1) the debtor made a false representation, other than an oral statement respecting the debtor's financial condition, with intent to deceive the creditor;
> (2) the creditor actually relied on the misrepresentation;
> (3) the creditor's reliance was justifiable; and
> (4) the misrepresentation caused a loss to the creditor.

See In re Bilzerian, 100 F.3d 886, 892 (11th Cir. 1996); *In re Johannessen,* 76 F.3d 347 (11th Cir. 1996); *Grogan v. Garner,* 498 U.S. 279, 287(1991).

In order to establish the first element, the creditor must prove that the debtor made a "false representation," other than an oral statement regarding the debtor's financial condition with the intent to deceive the creditor. Additionally, a statement made with "reckless indifference to the truth is sufficient to bar a discharge" under section 523(a)(2)(A). *See Birmingham Trust Nat. Bank v. Case*, 755 F.2d 1474 (11th Cir. 1985). "[F]raud may consist of silence, concealment or intentional non-disclosure of a material fact, as well as affirmative misrepresentation of a material fact." *Id.*; *see also Matter of Thomas*, 12 B.R. 765, 768 (Bankr. N.D. Ga. 1981) (Norton, J.). However, a statement of intent to perform an act in the future will not generally form the basis of a false representation that

is actionable under section 523(a)(2)(A) unless the creditor can establish that the debtor lacked the subjective intent to perform the act at the time the statement was made. *See In re Allison,* 960 F.2d 481 (5th Cir. 1992); *In re Bullock,* 317 B.R. 885 (Bankr. M.D. Ala. 2004); *Matter of Turner*, 12 B.R. 497 (Bankr. N.D. Ga. 1981) (Norton, J.). "'Actual' fraud precluding discharge consists of any deceit, artifice, trick or design, involving the direct and active operations of the mind used to circumvent or cheat another; something said, done or omitted with the design of perpetrating what is known to be a cheat or deception." *In re Butler*, 277 B.R. 843, 848 (Bankr. M.D. Ga. 2002); *see also McClellan v. Cantrell*, 217 F.3d 890 (7th Cir. 2000); *In re Cassel*, 322 B.R. 363 (Bankr. C.D. Ill. 2005). "As distinguished from false representation, which is an express misrepresentation[,] false pretense involves an implied misrepresentation or conduct intended to create and foster a false impression . . . and [i]t is well recognized that silence, or the concealment of a material fact, can be the basis of a false impression which creates a misrepresentation actionable under § 523(a)(2)(A).'" *In re Brandon*, 287 B.R. 308 (Bankr. S.D. Ga. 2002) (internal citations omitted).

Obviously, the debtor is unlikely to admit that he made a promise without the intent to perform or that he made a false statement or omission with the intent to deceive the creditor. Therefore, the court is permitted to infer such fraudulent intent from the facts and circumstances of the case. *See Bullock,* 317 B.R. at 890; *In re Hall*, 228 B.R. 483 (Bankr. M.D. Ga. 1998) (when determining whether debtor had intent to perform a promise, a

subjective test is used, which considers all the circumstances of the case).

The Plaintiff asserts that the Defendant made several false representations and intentional omissions. First, the Plaintiff contends that the Defendant told the Plaintiff's representatives, Godwin and Williams, that he would receive between $400,000 and $500,000 per year in distributions from the Wachovia/Synovus trust going forward. Having considered the testimony of Godwin, Williams, and the Defendant, the Court concludes that there is insufficient evidence to determine that the Defendant made this statement. Williams and Godwin have testified that the Defendant made the statement during their initial meeting, but the Defendant denies making the statement at any time. The Court finds that all three witnesses have sufficient personal motivation to render self-serving testimony. The Defendant's motivation is obvious, and Williams and Godwin were, at the time of the trial, still employed by the Plaintiff and were responsible for making the loans that resulted in the Plaintiff's loss.

If the Defendant did make the statement, it could explain why Godwin relied upon the $400,000 figure in his loan memorandum for the $1.65 million loan and on the $500,000 figure in the second loan memorandum. On the other hand, if the Defendant made the statement, the Court would have expected Godwin's handwritten notes of his initial meeting with the Defendant to include at least some mention of a discussion of the trust, if not some discussion of the future income to be derived from it. The Court also finds it curious that, despite the fact that the Defendant never made any written statement regarding the future

trust income, Godwin apparently never questioned the Defendant's omission of this information from Exhibit 7. Finally, the Court would not have expected the Defendant to make this statement, while at the same time disclosing the fact that the value of his interest in the trust was only approximately $2 million. It seems incredible that the Defendant, an experience financial planner, would have expected Godwin and Williams, experienced bank representatives, to believe that his interest in the trust could have produced that kind of income going forward. In any event, the Court simply cannot conclude from the evidence presented whether the Defendant did or did not tell the Plaintiff that he could expect to receive $400,000-$500,000 per year going forward from the Wachovia/Synovus Trust. As it is the Plaintiff's burden of proof to establish that the Defendant made a false representation, the Court must find that the Plaintiff has failed to meet that burden with respect to this allegation.

Alternatively, assuming the Court could conclude that the Defendant made this statement, the Court would find that the statement was "an oral statement respecting the debtor's financial condition" that would not be actionable under section 523(a)(2)(A). The Court recognizes a trend in the case law toward a narrow construction of the term "oral statement respecting the debtor's financial condition." *See In re Joelson*, 427 F.3d 700 (10th Cir. 2005), *cert. den.* 126 S. Ct. 2321 (2006). These cases have adopted a strict interpretation that requires statements excluded from the reach of section 523(a)(2)(A) to be "financial-type statements including balance sheets, income statements, statements of

changes in financial position, or income and debt statements that provide what may be described as the debtor or insider's net worth, overall financial health, or equation of assets and liabilities." *Id.* at 711-712. The *Joelson* case involved a debtor who persuaded the plaintiff to loan her $50,000 by misrepresenting that her brother would give her money to repay the debt and that she would provide assets, including real estate and antique cars, to be used as collateral for the loan. The Bankruptcy Appellate Panel affirmed the bankruptcy court's holding that the statement regarding the fact that her brother would give her money to repay the loan was an oral statement respecting the debtor's financial condition, but that the statements regarding the particular assets to be used as collateral were not broad enough to be considered statements regarding her overall financial health. It appears that the only issue before the Tenth Circuit was the bankruptcy appellate panel's decision that the debtor's misrepresentation as to the ownership of the assets did not constitute a statement respecting the debtor's financial condition. The Tenth Circuit affirmed that decision, but did not have the opportunity to address the panel's decision that the statement regarding the debtor's ability to obtain money from her brother to repay the debt was an oral statement respecting her financial condition. At to that issue, the panel had concluded that this statement was a statement respecting financial condition because it involved her ability to generate income and "[e]ven the narrow interpretation includes statements of 'ability to generate income.'" *In re Joelson*, 307 B.R. 689, 696 (10th Cir. BAP 2004).

In this case, the Plaintiff alleges that the Defendant orally represented that he would

be receiving a substantial amount of income from the Wachovia/Synovus Trust each year. The Plaintiff additionally presented the testimony of Williams, who contends that the Defendant even stated that he would "more than likely pay [the $1.65 million loan] off through lump sum distributions" obtained from the Trust. May 18th Transcript at 22. Although the Court concurs with the reasoning of the Tenth Circuit Court of Appeals in the *Joelson* case and also agrees that a strict approach is preferable to an overly broad approach, the Court finds that a statement that a debtor will receive a substantial amount of income from which a loan would be repaid is "unequivocally a statement concerning [the debtor's] financial condition." *In re Sharpe*, __B.R. __, 2006 WL 2817463 (Bankr. N.D. Tex. Sept. 28, 2006) (finding that the debtor's oral statement to the plaintiff that he had money stashed away that he would use to repay the plaintiff was a statement respecting the debtor's financial condition).

As to the Plaintiff's allegation that the Defendant told Godwin and Williams that he had an interest in two other trusts -- the Callaway Land Trust, which is a generation-skipping trust, and the Q-Tip trust -- the Court finds that the Defendant did not disclose the existence of these trusts to the Plaintiff. April 24th Transcript at 16; May 18th Transcript at 170. The Defendant had no access to the assets in these two trusts and had no expectation of receiving any distributions from either trust. May 18th Transcript at 170. Godwin's handwritten notes from the original meeting with the Defendant do not reflect any discussion of these trusts. April 24th Transcript at 60. *See* Exhibit 113. It appears to the Court that Godwin may have

learned of the existence of these trusts after the loan was made, perhaps during discovery connected with this case or during negotiations between the Plaintiff and the Defendant as to the disposition of the loans and their collateral.

The Plaintiff attempted to introduce Exhibit 149 as evidence that the Defendant disclosed the existence of the other two trusts to the Plaintiff. The Defendant objected to the admission of Exhibit 149 on the basis that the document contained unidentified handwriting that had not been authenticated, but did not object to the statement itself, which the Defendant identified as one of several account statements that he routinely received regarding the Wachovia/Synovus Trust. May 22nd Transcript at 23. The Defendant admitted that his initials are on the corner of the statement, but he testified that the handwriting in the middle of the first page of the document was not his handwriting. May 22nd Transcript at 14. No testimony was presented as to who wrote the notes on the statement or when they were written. The Defendant testified that he did not provide the information regarding the three trusts, which forms the basis of the handwritten notes, to any of the Plaintiff's representatives. May 22nd Transcript at 15. The Court will admit Exhibit 149 for only the limited purpose of establishing the account status and activity for the Wachovia/Synovus Trust as reflected in the statement. The Court will not consider the handwritten notes on the basis that they have not been authenticated. Even if the Court were to consider the handwritten notes, the notes would not persuade the Court that the Defendant disclosed the existence of the other two trusts to the Plaintiff prior to the Plaintiff's making

its loan decision. The statement is dated June 1, 2003 through June 30, 2003. Accordingly, it would have been impossible for the Defendant to have provided this document to the Plaintiff or for a representative of the Plaintiff to have written the information on the document before the Plaintiff made its loan decisions in August 2002 and March 2003. Even if the Court were to conclude that the handwritten notes tend to prove that the Defendant did disclose this information to the Plaintiff's representative at a later time, that fact would not convince the Court that the Defendant made the same statements earlier in order to persuade the Plaintiff to make either loan. Therefore, the Court could not conclude that the Defendant made such a statement with intent to deceive the Plaintiff or that the Plaintiff actually relied on any statement regarding the other two trusts in granting the Defendant either loan.

Second, the Plaintiff alleges that the Defendant misrepresented the fact that the Vernon Street Property was two weeks away from being complete. The Court has already determined, having considered the evidence, that the Defendant actually told Godwin that he and his family planned to move into the Vernon Street Property in two weeks, but did not make a representation that the renovations on the home were two weeks from being completed. This finding is consistent with Parham's testimony that the Defendant and his family moved into the property at some time in September and early October, at which time the interior of the house was approximately 80-85% complete and the outside was about

75% complete. April 25th Transcript at 63.[11]

Third, the Plaintiff claims that the Defendant falsely stated that he had invested $600,000 of his own money into the purchase and renovation of the Vernon Street Property. The Plaintiff asserts that the funds spent on the renovation were all borrowed. The Court has already found, as part of its findings of fact, that the Defendant had invested at least $686,828.68 of non-borrowed funds into the Vernon Street Property at the time he made this representation. In making this finding of fact, the Court considered the Defendant's testimony, as well as the checks submitted into evidence by the Defendant. The checks by which these payments were made were issued and paid either before the closing of the SunTrust construction loan or after all of the loan proceeds had been spent on the project in January 2002, but prior to the date upon which the Defendant prepared Exhibit 7. Although Godwin testified that he personally believed that the Defendant never put any of his own money into the Vernon Street Property, the Court finds sufficient evidence, including the Defendant's testimony and the checks written that appear to have been for payment of renovation expenses, as well as the fact that the Defendant appointed out over $600,000 in

[11] Even if the Defendant had told Godwin that the property was two weeks from being complete, the Court agrees with the Defendant that Godwin did not actually or justifiably rely on the Defendant's statement. Godwin personally inspected the Vernon Street Property in September 2002. May 18th Transcript at 154. At that time, the property had no landscaping or driveway, the guest house had only been framed without finished walls, the main house was missing approximately 40 lighting fixtures, and the downstairs' bathroom had no sink. April 24th Transcript at 55-56; May 18th Transcript at 154-55. Godwin also testified that, even when he inspected the property in March 2003, it was still not complete and was in fact never completed while the Defendant owned it.

distributions to his wife's account in the first six months of 2002, to overcome Godwin's bare speculation as to how the funds were obtained. April 25th Transcript at 88, 91. In any event, it is the Plaintiff's burden to establish that a statement made by the Defendant was false. Despite the Plaintiff's contention that there is no evidence in the record to substantiate the Defendant's claim that he spent at least $600,000 of his own money on the project, the Court finds that there is evidence to suggest that he did and no evidence to prove that he did not. Accordingly, the Plaintiff has failed to carry its burden of establishing that the Defendant made a false statement with regard to this issue.

Fourth, the Plaintiff points to the Defendant's representation to the Plaintiff that he would use the proceeds from the $350,000 loan to pay one-half of the settlement amount of $700,000 owed to Parham and that he would pay the remaining amount with his own funds, therefore settling the dispute with Parham in a final manner. The Court finds that this representation was true at the time the Defendant initially made it. The Defendant had negotiated the amount owed to Parham down to $700,000. There is no dispute that he disclosed this information to Godwin, as the $700,000 figure appears in Godwin's loan memorandum. At some time after first making this statement to Godwin, the Defendant mediated his dispute with Parham, and a $350,000 figure was reached. The Court recognizes that Parham did not actually sign the settlement agreement until after the loan closing. Nonetheless, the Court finds, from considering the totality of the circumstances and the Defendant's own testimony, that he knew prior to the loan closing that Parham had

agreed to the reduced settlement amount of $350,000 and that the Defendant knew that Parham would accept a note, such that the Defendant had no intention of using the $350,000 loan proceeds to pay Parham at the time he accepted the loan proceeds from the Plaintiff. The Defendant testified that the Plaintiff was aware at the time of the loan closing that the settlement figure had been reduced to $350,000, which establishes that the Defendant was also aware of this fact. The Court does not believe, however, that the Defendant shared this information with Godwin. In this regard, Godwin testified that the Plaintiff did not become aware of the reduced settlement amount until the time the Defendant and his wife informed the Plaintiff that they could no longer make the payments on the loans, and, considering the circumstances at the time of the loan closing, the Court finds Godwin's testimony on this issue to be more credible.

The Court's conclusion that the Defendant intentionally remained silent as to this change in the stated purpose of the loan and his intent to use the loan proceeds for that purpose is supported by evidence that the Defendant's personal and financial situation, as well as his ability to maintain payments on his debt load, had deteriorated by March 2003 to an extent that the Defendant became willing to intentionally withhold what he knew or should have known was material information from the Plaintiff in order to obtain the second loan. This conclusion is supported by the fact that the Defendant was having marital difficulties that prompted him to file for divorce from his wife; the fact that he had depleted and liquidated substantially all of his assets in order to pay for the Vernon Street Property

renovation, and the fact that he was contemplating filing bankruptcy as an alternative to paying the full amount of his obligation to Parham. The nature of the Defendant's financial situation is confirmed by the fact that he and his wife made only one payment on the $350,000 loan and, shortly after the closing of the $350,000 loan, also ceased making payments on the $1.65 million loan. From this, the Court infers that the Defendant knew full well in March 2003 that his financial situation was dire and finds that this knowledge was enough to motivate him to conceal material facts from the Plaintiff in an effort to obtain the $350,000 loan.

Having considered all of the evidence available, the Court finds that the Defendant knew prior to the loan closing and intentionally withheld from the Plaintiff the fact that the settlement figure had been reduced to $350,000, as well as the fact that he subjectively did not intend to use the loan proceeds for the stated purpose. The Defendant, therefore, borrowed the $350,000 from the Plaintiff under false pretenses within the meaning of section 523(a)(2)(A). *See In re Kahler*, 187 B.R. 508 (Bankr. E.D. Va. 1995) ("[O]missions or a failure to disclose by the debtor can constitute misrepresentations for the purposes of nondischargeability where the circumstances of the case are such that omissions or failure to disclose creates a false impression which is known by the debtor.").

Alternatively, the Court finds that the Defendant closed the $350,000 loan without the intention of repaying the debt, and therefore, the $350,000 loan was incurred through actual fraud. As noted above, this conclusion is supported by the totality of the

circumstances surrounding the loan closing and the Defendant's deteriorated financial condition. The Court is persuaded that the Defendant submitted his updated financial information to the Plaintiff and requested a second loan from the Plaintiff with the knowledge that he would not be able to and would not repay the $350,000 loan being sought.

As to the requirement of justifiable reliance, the court applies a subjective test to determine whether the creditor *justifiably* relied on a debtor's false statements or false pretense. This requirement is not as exacting as the requirement of *reasonable* reliance. *See Field v. Mans*, 516 U.S. 59 (1995); *In re Vann*, 67 F.3d 277, 283 (11th Cir. 1995). Accordingly, the Court need not consider what a reasonable man would do or "apply a community standard of conduct" to each case. *Field v. Mans,* 516 U.S. at 70-71. In conducting this analysis, the "court examines the 'particular qualities and characteristics of the plaintiff and circumstances of the particular case.'" *In re Simpson*, 319 B.R. 256, 261 (Bankr. M.D. Fla. 2003) (quoting *In re Vann*, 67 F.3d 277, 283 (11th Cir. 1995)).

In this case, the Court concludes that the Plaintiff *justifiably* relied on the false impression created by the Defendant that he would use the $350,000 and his own funds to pay off Parham. The Plaintiff was clearly motivated to make this loan to the Defendant because of his representation that it was necessary to complete the project, obtain a lien waiver from Parham, and to completely settle the dispute between Parham and the Defendant. Accordingly, the Plaintiff actually relied on the Defendant's earlier statements as to the purpose of the loan. The Plaintiff justifiably relied on these statements, as the

Plaintiff had no basis to know that the Defendant had persuaded Parham to take less money or that the Defendant intended to pay Parham through a note, rather than paying the funds to Parham directly. Nothing alerted the Plaintiff that it should not trust the Defendant's statement of the loan purpose or that it should investigate whether the Defendant actually intended to use the loan proceeds to achieve a final settlement of the Parham dispute.

Additionally, to the extent that the Court must find justifiable reliance by the Plaintiff on the Defendant's actual fraud in accepting the $350,000 without the subjective intent to repay the loan, *see, e.g., In re Cassel*, 322 B.R. 363 (Bankr. C.D. Ill. 2005) (noting that a creditor's reliance is only relevant when the fraud complained of takes the form of a misrepresentation and that, when actual fraud is involved, reliance is subsumed within the determination as to whether the debtor tricked the creditor into extending credit), the Court finds that the Plaintiff justifiably relied on the impression created by the Defendant that he intended to repay the $350,000 loan. The Plaintiff was not aware that the Defendant was contemplating bankruptcy or that he had threatened his contractor with a bankruptcy filing. The Plaintiff relied on the Defendant's good character and the previous banking relationship between Williams and the Defendant. The Plaintiff also knew that the Defendant had performed in accordance with the terms of the loan from Frontier Bank and that he had performed in accordance with the terms of the $1.65 million loan since the inception of that loan in September 2002. The Plaintiff had no reason to question whether the Defendant had a subjective intention of repaying the $350,000 loan.

The possibility that Godwin made certain miscalculations with regard to the Defendant's income does not alter the fact that, had the Defendant disclosed the fact that he did not intend to use the $350,000 loan proceeds to pay Parham in full settlement of Parham's claims or that he did not intend to repay the $350,000 loan, the Plaintiff simply would not have made this second loan to the Defendant, and the Plaintiff's loss would have been limited to the funds extended through the original $1.65 million loan. *See Sanford Institution for Sav. v. Gallo*, 156 F.3d 71 (1st Cir. 1998) (creditor's contributory negligence does not prevent justifiable reliance on misrepresentation; banks failure to conduct title search did not prevent bank from justifiably relying on debtor's misrepresentation, as the statement was consistent with debtor's conduct, and the debtor had previously been known to the bank as "an honest, trustworthy, and reliable businessman").

For the above reasons, the Court concludes that the Defendant's intentional creation of a false impression as to the purpose of the loan proceeds and the Defendant's acceptance of the $350,000 loan proceeds without the intention of repaying the debt constitute false pretense and actual fraud under section 523(a)(2)(A). The Court also finds that the Plaintiff justifiably relied on such false pretense and actual fraud and that this fraud resulted in a total loss to the Plaintiff of the funds extended through the second loan of $350,000.

CONCLUSION

In accordance with the foregoing reasoning, the Court finds that the portion of the

debt arising in connection with the $1.65 million loan is dischargeable, but that the portion of the debt arising from the $350,000 loan is nondischargeable under section 523(a)(2)(A). The parties are **DIRECTED** to attempt to stipulate the amount of the total debt attributable to that loan. If the parties cannot reach such a stipulated amount, the parties shall file a joint request to have the matter determined by the Court following a further hearing. If the parties submit a stipulation, the Court shall enter a final judgment in accordance with Rule 7054.

IT IS ORDERED.

At Newnan, Georgia, this 28 day of November, 2006.

W. HOMER DRAKE, JR.
UNITED STATES BANKRUPTCY JUDGE