

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

IN RE:

DON DISMUKES,

Debtor.

BK #87-28004-WHB
Chapter 7

COMMERCIAL CREDIT CORPORATION,
Raleigh Branch,

Plaintiff,

v.

Adversary Proceeding
No. 88-0066

DON DISMUKES,

Defendant.

MEMORANDUM OPINION AND ORDER

This is a core proceeding pursuant to 28 U.S.C. Section 157(b)(2)(I), and the Court issues the following finding of facts and conclusions of law pursuant to Bankruptcy Rule 7052.

HISTORY OF PROCEEDING

This adversary proceeding was initiated by a complaint filed by Commercial Credit Corporation, Raleigh Branch, asserting that the debt owing to the plaintiff was not dischargeable under Section 523 of the Bankruptcy Code, and the defendant/debtor answered the complaint and filed a counterclaim admitting that this was a core proceeding, and the counterclaim sought recovery for abuse of legal process, attorney's fees, and unspecified damages. The gravamen of the complaint is that the debtor obtained a loan from the plaintiff on September 17, 1987 and that

he filed his bankruptcy petition on December 7, 1987, approximately two and one-half months from the date of the loan. On the loan application, the debtor represented that he was then employed at the Internal Revenue Service, which fact the plaintiff asserts to be a material misrepresentation. Further, the plaintiff asserted that the defendant had no intentions of repaying the loan, was insolvent at the time of the loan, and misled the plaintiff into making a loan to him. Discovery was taken by the parties, including a deposition of the debtor, which deposition was introduced as an evidentiary exhibit to the trial, and the trial of this cause was conducted on July 25, 1988.

Based upon the trial testimony of the debtor, representatives of the plaintiff, exhibits, the debtor's deposition, and the entire record of this proceeding, the court makes the following findings of fact and conclusions of law.

FINDINGS AND CONCLUSIONS

This debtor received a mail solicitation from the plaintiff, inviting him to apply for a loan with Commercial Credit. He completed the written application form and returned it to the plaintiff, the application being dated August 26, 1987. On that written form, he sought a \$3,000.00 loan and stated that he was employed by the Internal Revenue Service as a tax examining clerk since July 8, 1984. The purpose of the loan applied for was "bill consolidation." The application stated that his annual salary, before taxes, was \$17,000.00.

The debtor was actually classified as a seasonal employee with the Internal Revenue Service, meaning that he was subject to temporary layoffs, of unknown duration. The debtor's layoff experience in years prior to 1987 had been that he either had worked for the entire year or had been laid off in 1986 for only two weeks. However, in 1987, he was laid off for a total of

approximately eleven weeks, beginning August 14, 1987. Therefore, at the time of the application to Commercial Credit for a loan, Mr. Dismukes was actually furloughed and was drawing unemployment compensation benefits. On or about August 7, 1987, Mr. Dismukes learned that he was going to be furloughed, but he did not know for how long. During his layoff, he was subject to recall at any time. Therefore, Mr. Dismukes was technically employed by the Internal Revenue Service but he was not working at the time of his loan application.

Mr. Dismukes had other credit at the time of his loan application, and apparently he was in good credit standing with his other creditors. The Commercial Credit representatives testified that they did check the credit references which were satisfactory. Also, Commercial Credit telephoned the Internal Revenue Service and verified the employment of Mr. Dismukes. Unfortunately, the employer did not reveal that Mr. Dismukes was in a layoff status at the time.

Subsequent to the initial loan application, Mr. Dismukes completed a second and more complete written application which he signed on September 17, 1987, which application again listed his employment at the Internal Revenue Service with a gross monthly salary of \$1,420.00 and stated that he had been employed since July, 1984. Again, Mr. Dismukes failed to reveal on this credit application that he was laid off or temporarily unemployed at the time.

Mr. Dismukes went to the Commercial Credit office and executed the loan disclosure and note and other loan requirement forms on September 17, 1987, and from the loan proceeds \$2,007.99 was paid to a Visa Account; \$550.00 was paid to a Master Card Account; \$260.00 was paid to Firestone; and only \$182.02 was given to the borrower directly. Therefore, Mr. Dismukes used, as he testified, the substantial portion of the loan proceeds to pay other prior existing creditors. The loan called for monthly payments of \$110.50 to begin on October 17, 1987. At

the time of the loan closing, Mr. Dismukes was drawing approximately \$128.00 per week in unemployment, and he had nine credit card accounts with total monthly charge payments in the \$800.00 to \$900.00 monthly range. There was testimony both at trial and in the deposition which indicates that Mr. Dismukes had insufficient money from his unemployment income to satisfy all of his monthly living expenses and obligations, including this new loan. However, Mr. Dismukes testified that at the time of making this loan, he anticipated that he would return to employment soon. In fact, Mr. Dismukes testified that he told Mr. Brandon at Commercial Credit on the date of the loan closing that he was unemployed and expected to return to employment in October, 1987. He testified that when he made the loan, he intended to repay it but that his eleven week layoff resulted in an inability to pay this and other creditors. Mr. Dismukes made the first loan repayment on October 15 from his unemployment income but defaulted in other payments.

Mr. Brandon from Commercial Credit rebutted Mr. Dismukes' testimony and stated that he was not told by the debtor of his unemployment status. The only conversation Mr. Brandon had with the debtor was at the loan closing, which was brief. At that closing, two check stubs of the debtor were submitted to Commercial Credit, one of which checks showed income for the period ending August 15, 1987, but the check for the period ending August 29, 1987 showed zero gross income. (Exhibit 4 to trial). Mr. Brandon testified that he did not know what the zero check indicated, but that it did not strike him as indicating unemployment, since the employment had been verified by Commercial Credit previously and by another Commercial Credit employee. Mr. Brandon stated that Mr. Dismukes made no explanation of the check, and he assumed it could have meant a vacation. Mr. Brandon testified that had the layoff status come

to his attention at the closing, he would not have closed the loan, and he supported this by stating that he had never closed a loan when the borrower was unemployed.

The plaintiff also refers to the fact that the loan application alleges other income of \$1,200.00 monthly to the Memphis State Panhellenic Association for the sale of mace, which income was not realized by the debtor. The debtor testified that he started selling mace in October of 1987, but that the sales did not materialize as he had anticipated. His loan application was based upon "future expectations" (page 26 of deposition). The debtor actually realized net income from the mace sales of approximately \$120.00 (page 4 of deposition).

The obvious factual dispute in this case is that the debtor testified that he advised Mr. Brandon at the loan closing of his layoff status, and Mr. Brandon disputes that testimony. The exhibits introduced do not reveal any indication that Commercial Credit had knowledge of the layoff or any temporary unemployment status. Rather, exhibit 1 introduced at the trial, and consisting of the credit application file, supports the testimony that the employment was verified, and the verification source was a Mrs. Freeman at the Internal Revenue Service, confirming employment since July, 1984, with a salary of \$15,810.00 and indicating that it was permanent employment. Obviously, the debtor may have been considered a permanent employee but still be subject to seasonal layoff.

The court, from the totality of the circumstances and testimony, finds that Commercial Credit did not know of the layoff status of the borrower at the time of his loan application or at the time of the loan closing. While the check stub for no income was some notice to Commercial Credit and perhaps should have caused more inquiry on the part of Commercial Credit, the more compelling evidence is that the debtor misled Commercial Credit on his loan

application forms. The debtor did not indicate in writing at any time that he was on layoff from the Internal Revenue Service, and Commercial Credit, through its credit verification process, was advised that the debtor was employed. The testimony indicated that the actual loan closing was very short in duration, and Mr. Brandon cannot recall any specific facts about the loan closing. However, any statements by Mr. Dismukes that he was not then employed would certainly have been expected to have caught Mr. Brandon's attention. In view of Mr. Brandon's testimony that he had never closed a loan when the borrower was laid off or unemployed, this loan closing would have been unusual had Mr. Dismukes revealed his employment status. The check stubs may not have been reviewed by Mr. Brandon at the loan closing, and they should have been.

However, the debtor cannot evade his responsibility to the lender by placing blame on the lender for not inquiring further. The convincing facts are that the borrower returned a written loan application and then completed a second, more complete application, at no time indicating his actual employment status. The debtor apparently had good credit at the time and his credit history supported the loan. The loan proceeds were used for bill consolidation, and some of the debtor's creditors benefited by receiving payment shortly before the debtor filed a Chapter 7 bankruptcy. Had the debtor not applied for and taken this loan, but defaulted in his existing loans and filed Chapter 7 bankruptcy, the debtor would not be faced with the problem he has in this adversary proceeding. Instead, the debtor obtained a new loan, preferred certain creditors, and quickly defaulted in his new obligation to Commercial Credit. The debtor's intentions no doubt at the time of the loan were to repay the loan; however, the debtor was reckless in applying for a new loan when he was laid off and when he had no way of knowing of his date to

return to work. The court finds that Commercial Credit did rely upon the written loan applications and that the reliance was reasonable under all of the facts and circumstances. A lender is surely entitled to rely upon two written loan applications, both of which reveal permanent employment and which neglect to reveal a layoff status, especially when that lender verified the permanent employment with the employer.

Even though Mr. Dismukes testified that he did reveal his layoff status at the loan closing, and even if the court could find that to be true, the debtor should not be able to divert attention from the fact that the debtor's initial misrepresentation is the cause for Commercial Credit's loss. Commercial Credit did not force the debtor to apply for a \$3,000.00 loan; rather, it was a voluntary act of the debtor, and borrowers should know that lenders are going to rely upon credit information.

Even though the debtor also misrepresented his income from sales to the Memphis State Panhellenic Association, the testimony of Commercial Credit is that they did not rely upon this income in making the loan; therefore, this representation is irrelevant but not condoned by this Court.

This loan had no co-signers and there is no collateral securing the loan. Therefore, Commercial Credit only had the debtor's repayment ability to look to, and the debtor misrepresented that critical source of repayment.

This debtor is certainly a sophisticated debtor, holding a Bachelor of Business Administration degree from Memphis State University and holding employment as a tax examining clerk. He certainly was a knowledgeable person, in a position to know of the seriousness of his representations to Commercial Credit. The very fact that the borrower knew

when he signed the applications that he was not gainfully employed and that he did not know how long he would be laid off is evidence which overcomes any good faith intentions on the part of the debtor at the time to repay the loan. The behavior of the debtor even though not rising to actual intentional fraud was such a reckless disregard of the accuracy of his credit information and of the risk imposed upon Commercial Credit as to constitute grounds for exception from discharge under Section 523(a)(2)(B), which section provides as follows:

Section 523(a)(2)(B):

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt -

(2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by -

(B) use of a statement in writing -

(i) that is materially false;

(ii) respecting the debtor's or an insider's financial condition;

(iii) on which the creditor to whom the debtor is liable for such money, property, services or credit reasonably relied; and

(iv) that the debtor caused to be made or published with intent to deceive; or

The court finds that the debtor's representation in writing of his employment status was materially false, that the representation did respect the debtor's financial condition, that the creditor reasonably relied upon the representation, and that the debtor's reckless behavior constitutes an intent to deceive the creditor.

As the Sixth Circuit observed in In re Martin, 761 F. 2d 1163 (6th Cir. 1985), the purpose of reasonable reliance under this Code section is to assure that a creditor does not act in bad

faith. This court does not find any bad faith on the part of Commercial Credit. Rather, Commercial Credit did use efforts and sources to verify the information provided by the debtor, which verification supported the debtor's representations. The fact that the debtor gave a check stub showing no income does not overcome the debtor's misrepresentations. Further, the Martin case illustrates that intent to deceive may be satisfied by gross recklessness of the debtor, and the Court has found that the debtor's actions in this proceeding were grossly reckless and in disregard of the reliance which he knew or should have known would be placed upon his representations.

The general discharge granted under Section 727 is designed to protect the honest but unfortunate debtor. The gross recklessness of this specific debtor prevents the debtor from being entitled to a discharge of this debt, even though the balance of his debts are dischargeable.

This objecting creditor has satisfied the requirement of proving an exception from discharge by clear and convincing evidence. Knoxville Teachers Credit Union v. Parkey, 790 F.2d 490, 491 (6th Cir. 1986).

Therefore, the court finds and concludes that the debt owing to Commercial Credit is excepted from discharge pursuant to Section 523(a)(2)(B) of Title 11, and that pursuant to Section 523(d), the plaintiff is entitled to its costs and reasonable attorney's fees. No proof of attorney's fees has been presented, and if the parties are unable to agree upon a reasonable attorney's fee, the plaintiff's attorney may move for an allowance, and after notice and hearing, the court will establish the same. Judgment is rendered for the plaintiff for the non-dischargeable balance of the loan, plus costs and attorney's fees, the latter to be determined, plus statutory post-judgment interest.

As a result of the Court's decision, the counterclaim of the defendant is denied and no basis for the said counterclaim is found in law or in fact.

SO ORDERED this 25th day of August, 1988.

William Houston Brown
United States Bankruptcy Judge

cc:

Don Dismukes, Debtor
3482 Mediterranean Drive
Apartment 1
Memphis, Tennessee 38118

Commercial Credit
Raleigh Branch
3274 Austin Peay Highway
Post Office Box 28677
Memphis, Tennessee 38128

Mr. W. Ray Jamieson
Attorney for Commercial Credit
150 East Court
Second Floor
Memphis, Tennessee 38103

Mr. Patrick Johnson, Jr.
Attorney for Debtor
4425 Faronia Road
Memphis, Tennessee 38116

Mr. Richard T. Doughtie, III
Attorney at Law
239 Adams Avenue
Memphis, Tennessee 38103
(Published)