

UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF TENNESSEE

In re:

JAMES McGARRH and  
FLOY McGARRH,  
Debtors.

Case No. 02-37466whb  
Chapter 7

PHILLIP GORMAN and  
SHIRLEY GORMAN,  
Plaintiffs,

v.

Adv. Proc. No. 03-0078

JAMES McGARRH and  
FLOY McGARRH,  
Defendants.

BOB ROSE,  
Plaintiff,

v.

Adv. Proc. No. 03-0097

JAMES McGARRH and  
FLOY McGARRH,  
Defendants.

---

MEMORANDUM OPINION ON COMPLAINTS OBJECTING TO DISCHARGE

---

On October 9, 2003, a joint trial was held on the two complaints objecting to the Debtors' general discharge in this chapter 7 case. The two complaints are based on related facts. Based upon the proof, the Court concludes that the discharge of the Debtor Floy McGarrh will be DENIED but the objection to the discharge of the Debtor James McGarrh was not established by the proof; thus, James McGarrh will be granted his discharge.

This opinion contains the Court's findings of fact and conclusions of law. FED. R. BANKR. P. 7052. This is a core proceeding. See 28 U.S.C. § 157(b)(2)(J).

## **SUMMARY OF COMPLAINTS**

The Gormans' complaint alleges that the Debtors made false oaths in their bankruptcy petition and schedules, that they operated contracting businesses and failed to include in their bankruptcy schedules business income or assets, that Floy McGarrh failed to schedule her income from employment or her business activity and failed to schedule ownership of or transfers of real property, that the Debtors failed to schedule vehicles, and that they failed to keep or preserve financial records of their business transactions. As a result, that complaint seeks denial of both Debtors' general discharge under 11 U.S.C. § 727(a)(2) through (5).

The Rose complaint makes similar allegations, seeking general denial of the Debtors' discharge under the same Code sections.

## **ISSUE**

The issue, of course, is whether the Plaintiffs have sufficiently established one or more statutory grounds for the harsh remedy of denial of either or both Debtors' general discharge.

## **DISCUSSION, FINDINGS AND CONCLUSIONS**

The trial of these complaints was held jointly, by consent of all parties. Obviously, denial of a general discharge can only be done once as to each Debtor, since the result would be a denial as to all creditors. It is irrelevant how these Plaintiffs came to be creditors, but it relates to a house apparently build for the Gormans by one or both of the Debtors. A judgment was entered prior to the bankruptcy filing by the Chancery Court in favor of the Gormans in the amount of \$48,549.55 and in favor of Mr. Rose, who had acted as a special master in the Chancery proceeding, in the amount of \$4,050.00. Except for the Chancery Court Clerk, these Plaintiffs are the only unsecured creditors listed in the bankruptcy Schedule F.

At the trial, only the Debtor Floy McGarrh and Mr. Ted Winestone testified. Exhibits were introduced, and the Court has considered the totality of the evidence in reaching its determination. Essentially, the evidence established that Floy McGarrh, who is past the age of 65, claimed to be retired as a realtor and unemployed at the time of the bankruptcy filing, but she testified that she did do some real estate and improvement work through a

business relationship with Mr. Ted Winestone. Mr. Winestone is an attorney who obviously was motivated to assist Floy McGarrh out of friendship. He is the secured creditor holding a mortgage on the Debtors' home and vehicles. Mr. Winestone permitted Floy McGarrh to assist him in purchasing houses from HUD and to use the checking account of his family corporation, the David and Rebecca Corporation.

For example, Ms. McGarrh would act on behalf of Mr. Winestone in purchasing property from HUD, because only a licensed realtor could deal with HUD on such purchases. She would pay for the property through the David and Rebecca account and use that account, funded by Mr. Winestone, to make required improvements to the HUD properties. Upon a sale of that property, the proceeds would be deposited in the David and Rebecca account. She was an authorized signatory on the account. Unfortunately for Floy McGarrh's discharge purposes, she used that checking account, with Mr. Winestone's permission, to also deposit her social security check and to draw advances for her own personal and family living expenses. The proof established that she owed that account for draws exceeding her social security deposits and any share of the sale proceeds that might be hers. In the one year preceding this bankruptcy filing, she had drawn from the account for personal expenses approximately \$4,000 in excess of her personal deposits. She filed no tax return reflecting this as income, and she testified that this merely represented Mr. Winestone's financial help to her. Mr. Winestone testified that he had not made any gift to the Debtor and that her excess draws represented a loan to her. At a minimum, the proof established that Floy McGarrh had a financial interest in the checking account, and that interest was not scheduled in her bankruptcy petition. Mr. Winestone testified that Ms. McGarrh earned some real estate commissions on some of the HUD acquisitions and that such commissions also went into the David and Rebecca account, presumably offsets against her draws from that account. Based upon the proof, Ms. McGarrh was in fact doing work connected to the acquisition of the HUD properties and improving them, using Mr. Winestone's money. And, she benefitted financially by having freedom to draw income from the corporate account, as well as from any commissions that she earned.

Her statement of financial affairs states that the McGarrhs had no income in 1990 through 2001, except for social income, and this is not true. She may very well be indebted

to Mr. Winestone for her excess draws but the practical effect of her free use of the David and Rebecca account is that she had business income that was not disclosed in the bankruptcy. Moreover, based upon Mr. Winestone's testimony, Ms. McGarrh earned some real estate commissions that were not revealed in her schedules. It is not clear to the Court when she would have earned these commissions, but Ms. McGarrh denied earning any income at all within the one year of the bankruptcy filing. Although she admitted continuing to hold a real estate license, she would have the Court believe that she had no earnings from that license, and that does not comport with the totality of the evidence.

The critical question is whether Ms. McGarrh's failure to schedule in any way her income or interest in the David and Rebecca account, as well as her business activity, establishes a basis for the harsh remedy of denial of her discharge.

Section 727(a)(2) requires a showing of actual intent to "hinder, delay, or defraud a creditor," when a debtor has "concealed" the debtor's property within one year of the bankruptcy filing. Ms. McGarrh's activity in the David and Rebecca account was on-going throughout 2002. Her bankruptcy was filed October 18, 2002; thus, the Court finds that she concealed her income and her interest in that account within one year of the bankruptcy filing. Was this concealment with fraudulent intent? Of course, Ms. McGarrh did not admit any fraudulent intent. "[C]ourts have identified several objective indicia that, taken together, strongly indicate fraudulent intent." *Groman v. Watman (In re Watman)*, 301 F.3d 3, 8 (1st Cir. 2002) (a fraudulent transfer case, discussing a non-exclusive list of indicia, including "retention of possession, benefit or use of the property in question;" "the existence or cumulative effect of the pattern or series of transactions or course of conduct...;" "the general chronology of the events and transactions under inquiry;" and "an attempt by debtor to keep the transfer a secret").

Notwithstanding Mr. Winestone's apparent good motive of wanting to assist the Debtors, the Court can find no reason for Ms. McGarrh to use the David and Rebecca account for the commingled deposit of real estate transactions and her social security income other than a purpose of concealing her financial transactions from her creditors. Since it is obvious that her only creditors, other than Mr. Winestone, are related to the Gormans' suit against her, the Court can only infer that Ms. McGarrh used the concealed

account to avoid the Gormans' efforts to collect from her. Ms. McGarrh's testimony about the account conflict, somewhat, with the documentary proof and with Mr. Winestone's testimony about the account, further indicating that her personal draws from the account were income in nature. Mr. Winestone testified that the purpose of permitting Ms. McGarrh to use the account was to allow her to remodel the HUD houses for resale purposes and to make advances for herself, with the advances to be repaid with the social security checks and sales of the HUD properties. He further stated that any profits from the HUD houses would have belonged to Ms. McGarrh and Mr. Winestone's daughter. There was, in fact, a profit of \$7,500 on one house that was credited against Ms. McGarrh's draws from the account. In essence, Ms. McGarrh was in business, remodeling and selling houses with Mr. Winestone's financing and with the hope of making a profit. Her business activity was not scheduled in her bankruptcy.

From the totality of the facts in this case, the Court concludes that Ms. McGarrh concealed her income, including business income, from her creditors within one year of the bankruptcy filing and that the concealment was done with fraudulent intent under § 727(a)(2)(A).

Ms. McGarrh's failure to be candid in her bankruptcy schedules, at least disclosing her interest in the David and Rebecca account and her business transactions with the HUD properties amounts also to a false oath under § 727(a)(4)(A).

As a result, Ms. McGarrh's general discharge must be DENIED.

As to her spouse, there was no proof from which the Court can determine his intent. Unlike Ms. McGarrh, James McGarrh was not called as a witness. Although it may be argued that he benefitted financially from the checking account transactions, the only proof was that this was Ms. McGarrh's activity. There was some indication that Ms. McGarrh may have used her spouse's contractor's license in doing some work on the HUD properties, but that suggestion provides no proof of Mr. McGarrh's actions or intent. Lacking proof, the Court will deny the relief sought against James McGarrh. He shall be allowed his chapter 7 discharge.

## **CONCLUSION**

Based upon a finding and conclusion of sufficient proof under § 727(a)(2)(A) and (a)(4)(A), the discharge of Floy McGarrh will be **DENIED**. The practical effect of a denial of discharge may be questionable, since Floy McGarrh is beyond age 65 and largely dependent on social security income, which is exempt from creditors' reach, but what happens after the conclusion of this bankruptcy is beyond this Court's influence or jurisdiction. James McGarrh shall be permitted his chapter 7 discharge. A separate order will be entered, consistent with this opinion.

This 30th day of October, 2003.

---

William Houston Brown  
United States Bankruptcy Judge

cc:

Debtors  
Ronald T. Riggs, attorney for Debtors  
Scott A. Frick, attorney for Gormans  
Ted Hayden, attorney for Rose  
United States Trustee  
Norman P. Hagemeyer, Chapter 7 Trustee