

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF TEXAS
SHERMAN DIVISION**

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| In re: | § | |
| | § | Case No. 02-45581 |
| ANTHONY FRANCIS ORSINI and | § | Chapter 7 |
| REBECCA LYNN ORSINI, | § | |
| | § | |
| Debtors. | § | |
| <hr/> | § | |
| THE CADLE COMPANY, | § | Adversary Proc. No. 03-4049 |
| | § | |
| Plaintiff, | § | |
| | § | |
| v. | § | |
| | § | |
| ANTHONY FRANCIS ORSINI and | § | |
| REBECCA LYNN ORSINI, | § | |
| | § | |
| Defendants. | § | |

MEMORANDUM OPINION¹

On August 24, 2004, the Court held a trial on this adversary proceeding to determine (i) whether the debtor’s discharge should be denied under sections 727(a)(3) and (5) of the Bankruptcy Code or (ii) whether the debtor’s obligations to the creditor should be excepted from discharge under section 523(a)(2)(B) of the Bankruptcy Code. The Court took the matter under advisement at the conclusion of the trial.

I. JURISDICTION

The Court has jurisdiction to consider this adversary proceeding pursuant to 28 U.S.C. §§ 1334 and 157(b). This adversary proceeding involves objections to discharge as well as determinations as to the dischargeability of a particular debt and, therefore, is a core proceeding

¹ This Memorandum Opinion is not designated for publication and shall not be considered as precedent, except under the respective doctrines of claim preclusion, issue preclusion, law of the case, or as to other evidentiary doctrines applicable to the specific parties in this proceeding.

pursuant to 28 U.S.C. §§ 157(b)(2)(A), (I), (J), and (O) upon which the Court may enter appropriate judgments.

II. FINDINGS OF FACT

The Court makes the following findings of fact:

1. In 1999, Rebecca Lynn Orsini opened a restaurant and gift shop through a corporation, Orsini Family, Inc., which was established for that purpose. Mr. and Mrs. Orsini (the “Orsinis”) have backgrounds involving finance. Mrs. Orsini was at one time a licensed stockbroker and for some period had an Oklahoma real estate license. Mr. Orsini received a degree in finance from Pennsylvania State University.

The Transamerica 12/99 Statement

2. Orsini Family, Inc. applied for a loan from Transamerica Small Business Capital, Inc. (“TSBC”) to supplement working capital in the business. Transamerica collected financial information from Mrs. Orsini through an oral interview and created a one-page document entitled “Personal Financial Statement Dated December 13, 1999” (the “12/99 Statement”).

3. The 12/99 Statement contains the following items: (i) “Cash & Marketable Securities” valued at \$75,000; (ii) “Retirement Assets” valued at \$260,000, (iii) “Real Estate” valued at \$250,000; and (iv) “Autos & Other Personal Assets” valued at \$30,000.

4. In connection with the application, TSBC prepared a document entitled “Deal Portfolio” from the information provided by Mrs. Orsini.² The Deal Portfolio is dated December 19, 1999 and reflects that TSBC independently verified the information provided by Mrs. Orsini. The Deal Portfolio indicates that TSBC was aware that the Orsinis intended to inject \$42,000 in

² The Joint Index of Trial Exhibits and Pre-Trial Order incorrectly label Exhibit 29 as the “SBA Loan Approval Summary.” The document appears to have been prepared by TSBC rather than the SBA.

liquid assets into the business.

5. The loan to Orsini Family, Inc. was approved by TSBC on or before March 7, 2000 [Joint Exhibit 39], but was conditioned upon Small Business Administration (the “SBA”) approval and guaranty of seventy-five (75%) percent of the loan amount.

The SBA 3/00 Statement

6. In connection with the guaranty, the Orsinis filled in the blanks on an SBA form financial statement (the “3/00 Statement”) on or about March 17, 2000. The 3/00 Statement was one of many forms provided by the Orsinis to the SBA in connection with the application, including, among other things, a schedule of collateral, credit reports, and tax returns.

7. The 3/00 Statement valued vehicle(s) at \$20,000.

8. The 3/00 Statement valued personal property described as “stamps, coins and jewelry” at \$20,000. The stamp collection was inherited by Mrs. Orsini from an uncle after the conditional approval of the loan on March 7, 2000, but before March 17, 2000, when the 3/00 Statement was prepared. Mrs. Orsini’s uncle had collected stamps and sold them at auctions or similar market shows. However, neither of the Orsinis had any expertise in valuing stamp collections, coin collections, or jewelry. The value they placed on the stamp collection was an estimate of their value given the large amount of stamps inherited by Mrs. Orsini and her ability to package the stamps as art to sell in the gift shop.

9. The 3/00 Statement valued interests in “IRA or other retirement accounts” at \$300,000.

10. The 3/00 Statement valued “cash on hand in banks” at \$25,000 and was separate and apart from any amount designated as retirement accounts.

11. The 3/00 Statement valued the Orsinis’ residence at \$250,000, based on the

Orsinis' knowledge of the sale listing of a nearby house. The local tax appraisal district assigned the value of \$185,000 to the home at least one year prior to the bankruptcy filing, but no evidence was presented as to the taxable value of the home in 2000.

12. On June 6, 2000, the SBA authorized the guaranty.

13. On July 21, 2000, TSBC, Orsini Family, Inc. d/b/a Foxglove, and the Orsinis, as personal guarantors, signed a Loan / Security Agreement in the principal amount of \$300,000 (the "Loan"). The Loan was secured by "Personal Property Collateral," which included, among other things, all equipment, machinery, furniture, fixtures, supplies, and accounts receivable held by Orsini Family, Inc.³

Bankruptcy Proceedings

14. On or about February 15, 2002, Orsini Family, Inc. ceased operating the restaurant and gift shop.

15. The Orsinis and Orsini Family, Inc. filed separate petitions for relief under Chapter 7 of the Bankruptcy Code on October 23, 2002 (the "Petition Date"). The chapter 7 petition filed by Orsini Family, Inc. commenced Case No. 02-45571. The chapter 7 petition filed by the Orsinis commenced this case, Case No. 02-45581.

16. The Schedules and Statement of Financial Affairs were also filed on October 23, 2002 (the "Schedules").

17. The total value assigned to the stamps, coins and jewelry in the Schedules was \$525. The difference in value between the 3/00 Statement and the Schedules is attributable to

³ The Loan / Security Agreement defines Orsini Family, Inc. as "Borrower." However, the addendum defining collateral, Exhibit 1.12(a), provides that the "Debtor hereby grants to Secured Party a security interest" in certain property. Neither "Debtor" nor "Secured Party" are terms used or defined in the Loan / Security Agreement. No additional documentation has been provided which indicates the effect intended by the use of inconsistent definitions. Accordingly, the Court assumes "Debtor," as referenced in the addendum, means Orsini Family, Inc.

the fact that the values stated in the 12/99 Statement and the 3/00 Statement were based on the Orsinis' estimate of fair market value at the time the statements were given in 1999 and 2000, and the values in the Schedules were based on the Orsinis' estimate of liquidation value at the time the Schedules were filed in 2002.

18. The stamp and coin collections were turned over to the Trustee for liquidation. The Trustee abandoned such assets by order entered August 2, 2005.

19. The value assigned to the residence in the Schedules was \$200,000. This value is consistent with the informal appraisal conducted by a neighbor and real estate broker, Pat Covington. At some time between March 17, 2000 and the Petition Date, a dump, which is visible from the residence, opened in the Orsinis' neighborhood. Additionally, a highway is being built nearby and seven billboards have been installed on the property behind the residence. These developments in the neighborhood as well as deferred maintenance and repairs account for the reduction in value between the 12/99 Statement and the Petition Date.

20. The value assigned to retirement accounts in the Schedules was \$40,542. On June 2, 2000, Mrs. Orsini faxed a statement to TSBC indicating a \$150,000 decline in the value of such accounts. The Orsinis have not received any distributions from these accounts, nor have they liquidated any of the monies dedicated to these accounts since they were established. The reduction in the value of the retirement accounts reflects natural market fluctuations, not dissipation of assets or misstatements of value of the assets at the time of the 12/99 Statement and the 3/00 Statement.

21. The value assigned to vehicles in the Schedules was \$25,000.

22. The value assigned to cash in the Schedules was \$87.

23. On December 2, 2002, Cadle filed a proof of claim in this bankruptcy case,

asserting an unsecured claim in the amount of \$283,733.13. Cadle's proof of claim indicates that Cadle acquired the Loan on August 22, 2002.

24. After the Petition Date, Cadle served the Orsinis with a five-page, blanket discovery request seeking, among other things, any and all documents relating to any account at any financial institution for the past five years. The Orsinis responded by providing Cadle with all the documents in their actual possession (which consisted of several boxes of documents). When Cadle requested additional documents, the Orsinis obtained the requested documents from their financial institutions and provided them to Cadle. It is not the Orsinis' general practice to maintain their personal credit card and bank statements after such statements have been reviewed, verified, and reconciled.

25. On February 14, 2003, Cadle filed its ORIGINAL COMPLAINT OBJECTING TO DISCHARGE, commencing this adversary proceeding in which Cadle objects to the Orsinis' discharge and to the dischargeability of the Orsinis' obligation to Cadle.⁴ On March 14, 2003, the Orsinis' filed their RESPONSE TO ORIGINAL COMPLAINT OBJECTION TO DISCHARGE, MOTION TO STRIKE, AND MOTION FOR SANCTIONS.

26. Neither TSBC nor the SBA appeared at the trial of this adversary proceeding. Cadle did not present any testimony, live or through deposition, of a representative of TSBC or the SBA in the prosecution of this matter.

III. DISCUSSION AND CONCLUSIONS OF LAW

Cadle objects to the Orsinis' discharge under sections 727(a)(3) and 727(a)(5) of the

⁴ In addition to the instant adversary proceeding, Cadle filed a similar complaint in the bankruptcy case filed by Orsini Family, Inc. (Adversary Proceeding No. 03-4048). Cadle eventually dismissed the Complaint after Orsini Family, Inc. pointed out that corporate debtors do not receive a discharge under the Bankruptcy Code and that sections 727 and 523 of the Bankruptcy Code do not provide for the relief requested by Cadle.

Bankruptcy Code. Alternatively, Cadle requests that the obligation to Cadle be excepted from discharge under section 523(a)(2)(B) of the Bankruptcy Code. The Court will address each of Cadle's claims in turn.

A. Nondischargeability under Section 727

Section 727 of the Bankruptcy Code provides that the Court must grant a discharge to a chapter 7 debtor unless one or more of the specific grounds for denial of a discharge listed in paragraphs (1) through (10) are proven to exist. The provisions governing denial of a debtor's discharge are construed liberally in favor of the debtor and strictly against the party challenging the debtor's right to a discharge. *Friendly Finance Discount Corp. v. Jones (In re Jones)*, 490 F.2d 452 (5th Cir. 1974). Under Rule 4005 of the Federal Rules of Bankruptcy Procedure, the burden of proof is on the party objecting to discharge.

In this case, Cadle has objected to the Orsinis' discharge pursuant to sections 727(a)(3) and (5). In particular, Cadle sought to establish at trial that the Orsinis' discharge should be denied because the Orsinis failed to maintain bank and credit card statements, which prevented creditors such as Cadle from ascertaining the Orsinis' pre-petition financial condition. Cadle also sought to establish at trial that the Orsinis' discharge should be denied because the Orsinis failed to explain the loss of certain assets.

1. Section 727(a)(3): Failure to Keep or Preserve Records

Section 727(a)(3) requires debtors to maintain records in order to obtain a discharge in bankruptcy. *See, e.g., In re Esposito*, 44 B.R. 817 (Bankr.S.D.N.Y.1984). Section 727(a)(3) specifically provides as follows:

The court shall grant the debtor a discharge, unless . . . the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or preserve any recorded information, including books, documents, records, and papers, from which the

debtor's financial condition or business transactions might be ascertained, unless such act or failure to act was justified under all of the circumstances of the case.

11 U.S.C. §727(a)(3).⁵ Thus, in this case, Cadle must establish by a preponderance of the evidence that *either* the Orsinis failed to keep or preserve recorded information, including books, documents, records and papers, *or* they engaged in an act of destruction, mutilation, falsification or concealment of such recorded information. If Cadle's burden is satisfied, the burden of proof shifts to the Orsinis to prove that the inadequacy in keeping or maintaining records is justified under the circumstances of this case. *See Robertson v. Dennis (In re Dennis)*, 330 F.3d 696, 703 (5th Cir. 2003) (the debtor's explanation for inadequate books and records must be satisfactory).

Cadle did not complain that records were destroyed, mutilated, falsified or concealed. Rather, Cadle sought to establish at trial that the Orsinis failed to keep books or records from which their financial condition and material business transactions could be ascertained for the period preceding the bankruptcy filing. *See In re Juzwiak*, 89 F.3d 424, 427 (7th Cir. 1996). Cadle also argued at trial that the Orsinis failed to maintain sufficient documentation to account for an alleged loss in the value of the Orsinis' retirement accounts, residence and stamp and coin collections. Since the failure to justify or document a "loss in value" is more properly reviewed with respect to an objection to discharge under section 727(a)(5), which follows in the next section, rather than subsection (a)(3).

The Court agrees that, although Federal Rule of Bankruptcy Procedure 4005 places the burden of proof on the party objecting to discharge, this rule does not alter a debtor's initial obligation to produce records from which his or her financial condition can be ascertained. *See*

⁵ Section 727(a)(3), unlike the other subsections of section 727, does not require a showing of intent or that the complained of act or acts were knowing and fraudulent. *See, e.g., In re Potter*, 88 B.R. 843, 848 (Bankr. N.D.Ill. 1988) ("The question is not why doesn't the debtor have adequate books and records but rather simply does the debtor have adequate books and records").

In re Greene, 81 B.R. 829, 833 (Bankr. S.D.N.Y. 1988). As another bankruptcy court has explained, the chapter 7 trustee and other creditors “are entitled to honest and accurate signposts on the trail showing what property passed through the debtor’s hands during the period prior to his bankruptcy.” *In re Dreyer*, 127 B.R. 587, 594 (Bankr. N.D.Tex. 1991). An individual debtor, however, generally “is not required to keep an immaculate set of books and records of his personal financial transactions.” *Id.* The true inquiry is whether the level of recordkeeping employed by a particular debtor is appropriate given the nature of his or her particular circumstances. *In The Matter of Bartolotta*, 485 F.2d 227 (5th Cir. 1973) (the Fifth Circuit indicated that the lower court should have considered if there were any special circumstances relevant to the case); *Texas National Bank of Beaumont v. Edson*, 100 F.2d 789 (5th Cir. 1939) (a failure to keep books and records must be justified under all the circumstances of the case).

Here, the Orsinis produced a number of records to Cadle; Trial Exhibit 39, which lists the records originally produced by the Orsinis to Cadle, reflects that the Orsinis retained, or were able to produce, extensive personal and business records.. The documents which Cadle complained were not provided consisted mainly of certain bank account and credit card statements. Mr. Orsini testified that, with respect to personal financial matters, he kept bank statements for approximately two years and credit card statements until they were verified and reconciled. The failure of an individual debtor to maintain cancelled checks and credit card receipts for consumer purchases does not, standing alone, warrant denial of discharge. *In re Peterson*, 296 B.R. 766, 789 (Bankr. C.D.Ill. 2003) (an office manager’s failure to maintain credit card receipts for consumer purchases did not bar his discharge); *Ledbetter v. Zaidan (In re Zaidan)*, 86 B.R. 296 (Bankr. S.D.Fla. 1988) (an individual debtor who customarily disposed of cancelled checks and similar documents but maintained bank statements and recent tax returns

should not be denied a discharge); *In re Irely*, 172 B.R. 23 (Bankr. N.D. Ohio 1994) (maintenance of bank statements without check stubs or cancelled checks is sufficient record-keeping for an individual non-business debtor).

While there are gaps in the information retained by the Orsinis for the five years prior to Cadle's document request, the Orsinis provided Cadle with every record they had in their possession and took action to obtain additional documentation from third parties. The Orsinis, as individuals, are not under any duty to keep any more detailed records than that of any other individual taxpayer. *In re Rowe*, 81 B.R. 653, 657 (Bankr. M.D.Fla. 1987) (holding that the debtor's checking account statement was sufficient for ascertainment of his financial condition). The particular types of records that Cadle complains the Orsinis failed to produce would not have provided any further explanation regarding the alleged losses in value with respect to the Orsinis' retirement accounts, residence, or stamp and coin collections. There were no transactions, dispositions, sales, conveyances, or transfers which should have been documented or which could have provided creditors additional evidence of the Orsinis' financial picture. Furthermore, it was clear from the quality of the evidence and arguments presented at trial that the Orsinis provided sufficient information from which creditors could reconstruct and understand the Orsinis' financial condition in the years leading up to the bankruptcy filing.

With regard to Cadle's complaint that the Orsinis failed to maintain documentation to support the "loss in value" of their retirement accounts, residence and stamp and coin collections, Cadle failed to establish that any additional records or documents actually exist, should have been maintained, or are necessary to ascertain the Orsinis' financial history. The Orsinis kept and produced a significant number of statements with respect to the retirement accounts and, as discussed below, the loss in value of those accounts was a result of natural market fluctuations,

not due to transfers, distributions, liquidations or dissipation of assets. With respect to the loss in the value of the Orsinis' residence and the stamp and coin collections, there were, again, no transfers, conveyances, or liquidations, documentation of which would have assisted creditors in understanding the Orsinis' financial history. Additional credit card statements and bank statements would not have shed any light on the loss in value of these assets, particularly where such "losses" are due to market fluctuations or the Orsinis' estimation of value at different points in time and for different purposes.

Accordingly, the Court concludes that Cadle failed to sustain its burden of showing under section 727(a)(3) that the Orsinis failed to keep or preserve records sufficient to ascertain their pre-petition financial condition and business transactions. To the extent that Cadle could be determined to have made a *prima facie* case under subsection (a)(3), the Court finds that the Orsinis have shown that the records and documents they maintained were sufficient, under the particular circumstances of this case, to allow their creditors to properly understand their financial history prior to the bankruptcy filing.

2. Section 727(a)(5): Failure to Explain Loss of Assets

Section 727(a)(5) states that a debtor will be denied a discharge when "the debtor has failed to explain satisfactorily, before determination of denial of discharge under this paragraph, any loss of assets or deficiency of assets to meet the debtor's liabilities." 11 U.S.C. §727(a)(5). The initial burden of proof under this subsection is on the objecting creditor, who must identify assets of the debtor that are no longer available to creditors. If the disappearance of substantial assets or of unusual transactions is established, the debtor has the burden of explaining the loss or disappearance of an asset. *See In re Reed*, 700 F.2d 986, 992-993 (5th Cir. 1983).

A "satisfactory" explanation means more than a vague, indefinite, and uncorroborated

assertion by the debtor. The Court must be convinced of the truth of the debtor's explanation as to what happened to his assets. *In the Matter of D'Agnese*, 86 F.3d 732, 735 (7th Cir. 1996); *Great American Ins. Co. v. Nye (In re Nye)*, 64 B.R. 759, 762 (Bankr. E.D.N.C. 1986) (the debtor's explanation need not be meritorious to be satisfactory). As stated by the Fifth Circuit:

The word 'satisfactorily,' as contained in [section 727(a)(5)] may mean reasonable, or it may mean that the court, after having heard the excuse, the explanation, has that mental attitude which finds contentment in saying that he believes the explanation -- he believes what the bankrupts say with reference to the disappearance or the shortage. He is satisfied. He no longer wonders. He is contented.

In re Shapiro & Ornish, 37 F.2d 403, 406 (N.D.Tex. 1929) *aff'd*. 37 F.2d 407 (5th Cir. 1929); *see also In re Martin*, 145 B.R. 933, 950 (Bankr. N.D.Ill. 1992) (the explanation should be sufficient to eliminate the Court's need to speculate as to what happened to the assets). The ultimate burden of persuasion is on the creditor to overcome a credible explanation by the debtor, if such explanation is given.

In this case, as noted *supra*, Cadle sought to establish a loss in the value of the following assets: (i) the Orsinis' residence, (ii) the Orsinis' retirement accounts, and (iii) the Orsinis' stamp and coin collections. Cadle did not complain of any "missing" asset, only the loss of value in these particular assets.⁶ Thus, the issues before the Court are whether there was a loss in the value of the Orsinis' assets and, if so, whether the explanation given by the Orsinis was satisfactory and, if so, whether Cadle properly rebutted the Orsinis' explanation.

Value of Residence

First, Cadle objected to the Orsinis' alleged failure to explain the decline in the value of their residence. The residence was valued at \$250,000 for purposes of the 12/99 Statement and

⁶ Mrs. Orsini testified that she physically lost a pair of diamond earrings, but this loss is not complained of by Cadle.

the 3/00 Statement. The Orsinis valued their residence at \$200,000 for purposes of their Schedules, which were filed in 2002. Mr. Orsini testified that immediately prior to the bankruptcy filing, a real estate broker, who is a neighbor, informally appraised the residence at \$200,000. He also testified that, given the need for deferred maintenance repairs, including paint, appliances upgrades, and carpet replacement, along with the installation of seven billboards on the property behind theirs and the construction of a waste dump, which is visible from their property, the value of \$200,000 seemed proper. The Court finds that Mr. Orsini's testimony was credible, and the Court is satisfied with his explanation as to the diminution in the value of the Orsinis' residence. While Cadle may not agree with this explanation, Cadle offered no evidence to contradict it.

Value of Retirement Accounts

Cadle also objected to the Orsinis' failure to explain the decline in the value of their retirement accounts. These accounts were valued at \$260,000 and \$300,000 in the 12/99 Statement and 3/00 Statement, respectively. In their bankruptcy schedules, the Orsinis valued their retirement accounts at \$40,542.40.

Mr. Orsini testified, credibly, that the pre-petition decline in the value of the retirement accounts was simply due to market fluctuation and depreciation in the underlying investment securities. Mr. Orsini also testified that no distributions, liquidations, or withdrawals had been made from any of the retirement accounts since they were established (other than rollover-type transactions to other retirement investment accounts). While the Orsinis did not produce every statement they received regarding these accounts from 1999 through the Petition Date, they did provide statements for a significant portion of this period. These statements supported Mr. Orsinis' testimony.

Cadle provided no evidence that the loss in value of the retirement accounts is supported by any explanation other than that provided by the Debtor. Cadle, however, appeared to interpret section 727(a)(5) as requiring the Orsinis to explain the stock market and all the forces that have affected the value of their securities for the five-year period preceding the bankruptcy filing. The Court does not adopt that interpretation of the statute. The Court finds that the explanation given by the Orsinis as to the decrease in value of the retirement accounts is satisfactory.

Value of Stamp / Coin Collections

Finally, Cadle objected to the Orsinis' failure to explain the difference in value placed on the jewelry, stamp and coin collections in the Orsinis' financial statements and the Schedules. Mrs. Orsini inherited the stamp collection after the 12/99 Statement was prepared. Accordingly, there was no valuation made with respect to this asset in that financial statement. However, in the 12/99 Statement, the Orsinis' valued their vehicles and "other personal assets" at \$30,000, which, presumably, included their jewelry and the coin collection. In the 3/00 Statement, the vehicles were valued at \$20,000, "other personal property" was valued at \$20,000, and "jewelry, stamps and coins" were valued at \$20,000. In the Schedules, the Orsinis valued vehicles at \$25,000, the coin collection at \$325, the stamp collection at \$125, jewelry at \$75, and other personal property at \$3,335.

Cadle's burden under section 727(a)(5) is to demonstrate that there is a discrepancy between the assets identified by the Orsinis' in the Schedules and the assets that exist or did exist at one time. *In re Lee*, 309 B.R. 468, 478 (Bankr. W.D.Tex. 2004) (a creditor objecting to discharge must prove assets are missing); *In re Isles*, 297 B.R. 910, 916 (Bankr. S.D.Fla. 2003). In this case, the stamp and coin collections were not sold, transferred or otherwise dissipated. Rather, as the Court has described in detail in the preceding paragraph, the Orsinis expressed

different opinions regarding the value of these assets at different points in time. *See In re Batcher*, 289 B.R. 205, 219 (Bankr. M.D.Fla. 2003).

With respect to the stamp collection, Mrs. Orsini testified that, for purposes of the 3/00 Statement, she valued the stamp collection based on the volume of stamps she had inherited and her belief that, if her uncle had willed them to her, they must have had some value. In addition, Mrs. Orsini testified that she had seen framed stamps for sale as pieces of art and that she intended to attempt to sell some of the stamps in this manner in her gift shop. It also is noteworthy that the Orsinis had very little time to assess the true value of the stamp collection, which Mrs. Orsini inherited only a week or two prior to preparation of the 3/00 Statement. Mr. Orsini testified that most of the \$20,000 value they placed on the stamp and coin collection in the 3/00 Statement was attributable to the stamp collection and that he felt the coin collection might be worth approximately \$1,000. Mr. Orsini testified that he had reviewed his coin collection and knew roughly what he had spent over the years to acquire the coins.

The Orsinis turned over both the stamp and coin collection to the Trustee for liquidation, and the Trustee abandoned the estate's interest in such assets after due investigation of their worth. Based upon the abandonment and the lack of any contrary evidence presented by Cadle, it appears that the value attributed to the stamp and coin collections in the Schedules was an accurate assessment of their value when the Schedules were filed in 2002. The difference in the values in the 12/99 Statement, the 3/00 Statement and the Schedules is attributable to the fact that the values in the financial statements were based on the Orsinis' estimate of fair market value, and the values in the Schedules were based on the Orsinis' estimate of liquidation value. Under these circumstances, the Court finds that there was no loss of assets within the meaning of section 727(a)(5), and, to the extent a loss could be said to have occurred, the Orsinis have

satisfactorily explained the loss.

B. Nondischargeability under section 523(a)(2)(B): False Written Statements

A creditor who is owed a debt that may be excepted from discharge under section 523(a)(2) must initiate a proceeding in this Court seeking an exception to discharge. The creditor has the burden of proof under a preponderance of the evidence standard. *Grogan v. Garner*, 498 U.S. 279, 286 (1991). “Intertwined with this burden is the basic principle of bankruptcy that exceptions to discharge must be strictly construed against a creditor and liberally construed in favor of a debtor so that the debtor may be afforded a fresh start.” *Hudson v. Raggio & Raggio, Inc. (In re Hudson)*, 107 F.3d 355, 356 (5th Cir. 1997); *In re Whitaker*, 225 B.R. 131, 139 (Bankr. E.D.La. 1998). Thus, without satisfactory proof of each element of the cause of action, judgment must be entered for the debtor.

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

[A] discharge under §727 . . . of this title does not discharge an individual debtor from any debt for money, property, or services, . . . to the extent obtained by 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 or made to be published with the intent to deceive.

11 U.S.C. §523(a)(2)(B). In this case, Cadle sought to establish at trial that the Orsinis’ obligations under the Loan are not dischargeable in bankruptcy, because the Orsinis had obtained the Loan by intentionally submitting materially false financial statements upon which the TSBC and/or the SBA relied. In particular, Cadle complained that the Orsinis made misrepresentations regarding the value of the following assets: (i) cash in hand; (ii) the stamp and coin collections; and (iii) their residence.⁷

⁷ Cadle originally objected to the Orsinis’ failure to identify certain debts or obligations in the amount of

“In Writing” Requirement

To come within the exception of section 523(a)(2)(B), the statement must be either written by the debtor, signed by the debtor, or written by someone else but adopted and used by the debtor. *Engler v. Van Steinberg*, 744 F.2d 1060 (4th Cir. 1984) (affirming discharge where allegedly false financial statements were oral); *Bellco First Federal Credit Union v. Kaspar (In re Kaspar)*, 125 F.2d 1358 (10th Cir. 1997) (computer generated form produced from debtors’ oral statements did not satisfy ‘in writing’ requirement).

Cadle acknowledged that the 12/99 Statement was prepared internally by TSBC – not by the Orsinis. *See* Pre-Trial Order [Docket No. 62] Section 2(d). Additionally, the Court finds that the 12/99 Statement was prepared from the oral representations made by Mrs. Orsini and TSBC’s own verification of that information. There is no evidence before the Court that the Orsinis knew of the 12/99 Statement at the time it was prepared or that they reviewed and had an opportunity to verify its contents. Accordingly, it does not constitute a statement that was written, signed, or adopted and used by the Orsinis and cannot form the basis for a denial of discharge under section 523(a)(2)(B).

The 3/00 Statement is a written document prepared by the Orsinis. Thus, in contrast to the 12/99 Statement, the 3/00 Statement satisfies the “in writing” requirement of section 523(a)(2)(B). The Court will review the remaining elements of section 523(a)(2)(B) in the context of the 3/00 Statement only.

Materiality Requirement

As stated in section 523(a)(2)(B), Cadle must show not only that the 3/00 Statement was

\$150,000. However, the parties represented to the Court, at trial, that this portion of the claim had been resolved and was being withdrawn.

factually incorrect, but that it was materially false. “Materiality” in this context has been interpreted to mean that the misrepresentation or false statement presents a substantially untruthful picture of the debtor’s financial condition *and* concerns a matter which affected or influenced the creditor’s decision to extend credit. *See Investors Credit Corp. v. Batie (In re Batie)*, 995 F.2d 85 (6th Cir. 1993); *In re Jones*, 197 B.R. 949, 955 (Bankr. M.D.Ga. 1996); *In re Bailey*, 145 B.R. 919 (Bankr. N.D.Ill. 1992).

Neither TSBC nor SBA were called to testify regarding their reliance on the 3/00 Statement, reasonable or otherwise. The value attributed to the stamp and coin collections in the 3/00 Statement may have been overstated, but, in terms of materiality, the Court finds that Cadle has failed to prove that this discrepancy materially affected the TSBC or SBA’s analysis of the Orsinis’ financial condition -- particularly in light of the total net worth of the Orsinis, which exceeded the amount of the Loan by 200% without including the value of the stamp and coin collections, and in light of the fact that TSBC conditionally approved the loan prior to the 3/00 Statement (which is the only statement referring to the stamp collection). Accordingly, the Court finds that Cadle has failed to sustain its burden under section 523(a)(2)(B), and the Loan is an obligation which is properly dischargeable. While it is unnecessary to discuss the remaining elements of section 523(a)(2)(B), the Court will briefly review the remaining issues relevant to nondischargeability under this section in the interest of providing a complete discussion.

“Reasonable Reliance” Requirement

The reasonable reliance requirement of section 523(a)(2)(B)(iii) is a factual determination. *See, e.g., Coston v. Bank of Malvern (In re Coston)*, 991 F.2d 257, 260-261 (5th Cir. 1993). The Fifth Circuit has stated that “[t]he reasonableness of a creditor's reliance, in our view, should be judged in light of the totality of the circumstances.” *Id.* at 261. One factor the

Court may consider is whether minimal investigation would have uncovered the inaccuracies in the financial statement. *Id.*

In this case, as discussed above, TSBC conditionally approved the Loan based on the 12/99 Statement. The 3/00 Statement the Orsinis provided to the SBA showed a few additional assets. However, in light of TSBC's conditional approval of the Loan based on the 12/99 Statement, the lack of any basis for TSBC's acceptance of a layman's estimation of the value of a recently inherited stamp collection, and the lack of any inquiry by TSBC regarding the Orsinis' valuations in the 3/00 Statement, the Court finds that TSBC did not reasonably rely on the 3/00 Statement.

“Intent to Deceive” Requirement

Cadle's argument regarding the Orsinis' intent relied on the premise that the discrepancies in value between the 12/99 Statement, the 3/00 Statement and the Schedules are so great that the financial statements must have been prepared with the intent to defraud. However, the passage of time and the different purposes of the valuations (*i.e.*, fair market value vs. liquidation value) constitute plausible and valid explanations for the differences in value of which Cadle complains. With regard to the value of the Orsinis' residence, the different valuations also reflected changes in the neighborhood and deferred maintenance, and were not knowingly false. With regard to the stamp collection, although the Orsinis' valuation in the 3/00 Statement was, in retrospect, incorrect, their estimate of the value of the stamp collection in the 3/00 Statement was made in good faith. Finally, with regard to the Orsinis' retirement accounts, their declining value was evidenced by the statements provided to the Orsinis from their various investment management groups.

The intent to deceive requirement is also judged in light of the totality of the

circumstances. *See, e.g., In re Slonaker*, 269 B.R. 595 (Bankr. N.D.Tex. 2001); *In Re Barron*, 126 B.R. 255, 260 (Bankr. E.D Tex. 1991). Having observed the Orsinis when they testified, the Court finds that their estimates of value were all made in good faith and that the Orsinis lacked any intent to deceive.

IV. CONCLUSION

For the foregoing reasons, the Court finds that there has been no failure of record keeping which would justify the denial of a discharge. The Court also finds that there was no loss of assets or, alternatively, that the Orsinis satisfactorily explained any loss in assets which occurred prior to the filing of the bankruptcy case. The Orsinis are entitled to their discharge, and the Loan is an obligation that is properly dischargeable. The Court, therefore, concludes that Cadle's objections to discharge and the dischargeability of debt should be denied. Judgment will be granted in favor of the Orsinis. This opinion constitutes the Court's findings of fact and conclusions of law as required by Rule 7052 of the Federal Rules of Bankruptcy Procedure, made applicable herein by Rule 9014 of the Federal Rules of Bankruptcy Procedure and disposes of all issues pending before the Court.

Signed on 3/31/2006

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HONORABLE BRENDA T. RHOADES,
UNITED STATES BANKRUPTCY JUDGE