U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
ENTERED
JAN 15 2003
TAWANA C. MARSHALL, CLERK
BY _____
Deputy

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE:	§	
	§	
GORDON RAY TODD	§	**Case No. 01-39786 HDH-7**
	§	
Debtor	§	

THE CADLE COMPANY	§	
	§	
Plaintiff	§	
	§	
v.	§	**Adversary No. 02-3114**
	§	
GORDON RAY TODD	§	
	§	
Defendant	§	

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Pursuant to Federal Rule of Bankruptcy Procedure 7052, the Court enters the following findings of fact and conclusions of law:

A. Findings of Fact

1. Defendant Gordon Ray Todd ("Todd") is an individual Debtor in the above-captioned Chapter 7 bankruptcy case (the "Case"). Todd has been married for forty-three years to Nancy Todd. Nancy Todd is not a debtor in this, or any other, bankruptcy case.

2. Plaintiff, The Cadle Company ("Cadle"), is an Ohio corporation.

3. Cadle filed two sworn proofs of claim in the Case on or about January 30, 2002 (in the amount of $5,446,341.96, Cadle Ex. 6), and February 1, 2002 (in the amount of $401,172.44,

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Cadle Ex. 7) (collectively, the "Proofs of Claim"). The Proofs of Claim assert claims against Todd pursuant to state court judgments entered against Todd before the filing of his bankruptcy case. Cadle is the assignee of those judgments. Cadle acquired the larger claim after the Case was filed. However, Cadle acquired its interest in the smaller claim evidenced in Cadle Ex. 7, some nine months before the Case was commenced.

4. Todd and Hughes Building, Inc. ("THBI") is a corporation started by Nancy Todd, Debtor's wife, and Melanie Hughes, as 50/50 shareholders. Nancy Todd's part was capitalized by funds received as a gift from her father. Debtor Todd owns no interest in THBI. He was an employee of THBI. THBI has ceased operations.

5. THBI was in the business of residential remodeling and building new custom homes. Todd worked full time for THBI, and was paid $90,000 annually at the time operations and his employment ceased. He received a salary on a monthly basis by a check from THBI.

6. Todd did not work for any other company while employed by THBI. During Todd's employment, THBI increased in value.

7. Todd did not claim a community property interest in THBI in his schedules.

8. Since approximately 1987, Todd has neither maintained nor used a personal checking account.

9. For many years, at least twenty, and perhaps for the entire marriage, Nancy Todd has handled the family's bills and has written checks to creditors. Presently, and at all times relevant to this adversary proceeding, Todd and his wife handle all their financial affairs through two checking accounts held in the name of, and controlled exclusively by, Debtor's wife, Nancy Todd. Todd endorsed his payroll and social security checks directly to Mrs. Todd, or cashed

his checks and Mrs. Todd deposited the proceeds into a bank account at Mercantile Bank from which household bills and expenses were paid. Mrs. Todd deposited her individual checks in the other bank account. Only Mr. Todd's funds were deposited in the Mercantile Bank account. This arrangement was not described in the Debtor's schedules or statement of financial affairs. Mrs. Todd testified that this arrangement was done on advice of counsel who told the Todds to keep Mr. Todd's funds separate from Mrs. Todd's funds. Debtor Todd's testimony was to the same effect. Mrs. Todd stated that this arrangement was solely to protect her assets from the reach of Mr. Todd's creditors.

10. Todd also serves as a trustee for the Juanita Hart Family Trust ("Trust") created by his father-in-law for the benefit of Todd's mother-in-law. Todd has been the only trustee of the Trust since the Trust was created. The Trust is the primary source of support for Todd's mother-in-law.

11. Over the years, the Todd family has made small contributions to the Trust for the support of Todd's mother-in-law. Mrs. Todd testified that she placed Todd's payroll and social security checks into the account at Mercantile Bank, and her salary checks into an account at Legacy Bank. Checks were written by Mrs. Todd from both accounts to the Trust. The amounts were relatively small, usually no more than a few hundred dollars in a single month. Todd and Mrs. Todd testified that those payments were to support Debtor Todd's mother-in-law.

12. Todd's schedules and statement of financial affairs do not list his service as trustee. However, the contributions or transfers to the Trust are characterized on Schedule J (expenses) as support paid to the mother-in-law. The payments are not listed in the statement of financial affairs as gifts.

13. Todd will be the beneficiary of certain life insurance provided for in his wife's will to be paid to another trust, which is also created in Todd's wife's will. Todd did not disclose an interest in that life insurance policy and testamentary trust in his schedules. The testamentary trust is apparently the beneficiary of the life insurance, and Todd is not a direct beneficiary.

14. Todd was unable to explain the source of a small amount of income disclosed on his tax returns as self-employment income. Todd did explain at trial that the income (a few thousand dollars) was for referral fees. He testified that he did not remember the entities which paid him. He did describe generally the services for which he was paid. Mrs. Todd was unable to explain this income or her own self-employment income.

15. Only Debtor Todd and his wife testified at trial. Cadle invoked the rule and the witnesses testified without hearing each other's testimony. The Todds each appear to this Court to be honest, and their testimony credible. Their testimony was not contradicted by the documents or witnesses offered at trial by Cadle, and in most respects, the documentary evidence offered by Cadle supported the Todds' testimony.

16. Any conclusion of law may also be deemed a finding of fact.

B. Conclusions of Law

<u>The Complaint</u>

1. In this adversary proceeding, Cadle objects to the discharge of Todd, pursuant to 11 U.S.C. §§ 727(a)(2)(A) (transfer with intent to hinder, delay, or defraud), (a)(4)(A) (false oaths), and (a)(5) (inability to explain the loss of assets).

Jurisdiction and Venue

2. This is a core proceeding over which this Court has jurisdiction pursuant to 28 U.S.C. § 157(b)(2). Todd admits subject matter and personal jurisdiction, venue and core proceeding status.

Standing

3. Todd objected to the standing of Cadle, which acquired the claims it seeks to enforce, to bring an action under Bankruptcy Code § 727. Judge McGuire earlier granted a partial summary judgment in favor of Cadle on this point. At trial, Todd's attorney questioned one of the claims of Cadle (Cadle Ex. 6), which was apparently acquired after the Case was filed.

4. Because that claim was acquired after the Case commenced, Debtor argues that Cadle is not a "creditor." In this particular case,[1] Debtor does not win on this issue because Cadle had an interest in a judgment against the Debtor before the Case was commenced. Todd's objection to the standing of Cadle is overruled. Cadle has standing to object to Todd's discharge.

Summary of Claims of Cadle

5. Cadle claims Todd's conduct during the one-year period prior to the petition date, as well as from the course of conduct in concealing his income through transfers to his wife, constitutes intentional conduct to shelter assets from creditors, transfer assets to relatives, and deprive the bankruptcy estate of all non-exempt assets to prevent creditors from recovering anything, such that the estate would be treated as a "no asset" case.

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[1] Some courts have held, and this Court agrees, that, in certain instances, the right to object to a debtor's discharge is not a marketable commodity which may be purchased by one party from another. *See, e.g., Young v. Beugen (In re Beugen)*, 99 B.R. 961 (9th Cir. BAP 1989), *aff'd*, 930 F.2d 26 (9th Cir. 1991). The record here does not support such a finding.

6. More specifically, Cadle further claims that Todd (a) engaged in a course of conduct and pattern with the intent to hinder, delay or defraud creditors, transferred, removed, destroyed, or mutilated, or concealed or permitted to be transferred, removed, destroyed, mutilated, or concealed, certain of his property, thereby preventing it from coming into the hands of his creditors, including Cadle, before his bankruptcy and continuing thereafter; (b) made a false oath with regards to his schedules and statement of financial affairs; and (c) has failed to explain satisfactorily a loss or deficiency of assets, all in violation of 11 U.S.C. § 727(a)(2)(A), (a)(4)(A), and (a)(5).

Burden of Proof

7. In an adversary proceeding objecting to a debtor's discharge under § 727(a), the trustee or creditor has the burden of proving sufficient facts to sustain the objection by a preponderance of the evidence. *See In re Beaubouef*, 966 F.2d 174 (5th Cir. 1992); *cf. Grogan v. Garner*, 498 U.S. 279, 112 L.Ed.2d 755, 111 S.Ct. 654 (1991) (standard of proof in dischargeability complaints).

Transfers With the Intent to Hinder, Delay, or Defraud

8. In this count, Cadle complains about Debtor Todd's deposit with his wife of Todd's paychecks and Social Security benefits. These funds were placed under the wife's control and used to pay household expenses.

9. Debtor argues that because his wages are exempt under Texas law, the transfer of the exempt wages cannot form the basis of a § 727(a)(2)(A) action. Assuming, *arguendo*, that the wages were exempt once paid, exempt property that is subsequently transferred may be the subject of a § 727(a)(2)(A) denial of discharge, if the requisite intent to hinder, delay or defraud

creditors is shown. *Tavenner v. Smoot (In re Smoot)*, 265 B.R. 128, 143 (Bankr. E.D. Va. 1999); *Saloman v. Kaiser (In re Kaiser)*, 722 F.2d 1574, 1583 (2nd Cir. 1983).

10. Under § 727(a)(2)(A), Cadle bears the burden of establishing that the transfers in question occurred with improper intent. *See Pavy v. Chastant (In re Chastant),* 873 F.2d 89, 90-91 (5th Cir. 1989); *Morton v. Dreyer (In re Dreyer),* 127 B.R. 587, 593 (Bankr. N.D. Tex. 1991). However, to find in Cadle's favor on intent, this Court does not need to find that Todd had the intent to delay *and* hinder *and* defraud. *See Humphries v. Schnurr (In re Schnurr),* 107 B.R. 124, 130 (Bankr. W.D. Tex. 1989) ("all the plaintiff has to prove is that the debtor hindered his creditors, he delayed his creditors, *or* he defrauded his creditors"); *see also NCNB Texas National Bank v. Bowyer (In re Bowyer)*, 916 F.2d 1056, 1059 (5th Cir. 1990) ("the term 'defraud' does not subsume 'hinder or delay'"), *op. on reh'g*, 932 F.2d 1100 (5th Cir. 1991).

11. Nevertheless, the evidence must show that the debtor had actual intent. *Chastant,* 873 F.2d at 91. Actual intent may be established by circumstantial evidence or by inferences drawn from a course of conduct. *Hibernia Nat'l Bank v. Perez (In re Perez)*, 954 F.2d 1026, 1029 (5th Cir. 1992); *Chastant,* 873 F.2d at 91; *Dreyer,* 127 B.R. at 593; *Cullen Center Bank & Trust v. Lightfoot (In re Lightfoot)*, 152 B.R. 141,147 (Bankr. S.D. Tex. 1993).

12. In analyzing the intent necessary to bar a discharge, some courts have identified factors as evidencing the fraudulent intent necessary to deny discharge under § 727(a)(2)(A), including:

    a. the lack or inadequacy of consideration;

    b. the family, friendship or close associate relationship between the parties;

    c. the retention of possession, benefit, or use of the property in question;

d. the financial condition of the party sought to be charged both before and after the transaction in question;

e. the existence or cumulative effect of the pattern or series of transactions or course of conduct after the incurring of debt, onset of financial difficulties or pendency or threat of suits by creditors; and

f. the general chronology of the events and transactions under inquiry.

In re Chastant, 873 F.2d at 91; *Hubbell Steel Corp. v. Cook (In re Cook),* 126 B.R. 261,268 (Bankr. E.D. Tex. 1991).

13. Under certain circumstances, a debtor will be denied a discharge by using the bank account of another to protect the funds from garnishment by creditors. *See, e.g., In re Geter*, No. Civ.A. 3:01-CV-0671, 2002 WL 220059 (N.D. Tex. Feb. 12, 2002) (discharge denied upon showing of a general pattern of concealing assets, including the use of accounts in debtor's mother's and daughter's names).

14. Applying the foregoing, the Court determines that Cadle did not establish intent to hinder, delay, or defraud by a preponderance of the evidence. Mr. and Mrs. Todd testified that the manner of payment to their creditors has essentially been the same for a number of years, perhaps for over the life of their marriage. For many years, Todd gave his wife Nancy Todd his paycheck, or the proceeds of it, and she paid household expenses. (Cadle Ex. 14.) Unlike in *Geter*, the funds in question were earned during the pendency of the Todds' marriage, and, therefore, were community in nature and owned by Mr. and Mrs. Todd. The cancelled checks show the funds were used for community household expenses of Mr. and Mrs. Todd. Further, the funds were not used to purchase substantial assets, nor did they

accumulate. (Cadle Ex. 14.) There is no reliable evidence that funds were secreted to defraud, hinder, or delay Todd's creditors. *Cf. Everspring Enters., Inc. v. Wang (In re Wang)*, 247 B.R. 211 (Bankr. E.D. Tex. 2000) (payment of current living expenses made without intent to defraud, hinder or delay).

False Oath

15. Bankruptcy Code § 727(a)(4)(A) provides that the court shall grant the debtor a discharge, unless the debtor has knowingly and fraudulently, in or in connection with the case, made a false oath or account. 11 U.S.C. § 727(a)(4)(A).

16. Cadle asserts that Todd knowingly and fraudulently made false oaths in this case by executing and causing to be filed with the Bankruptcy Court the allegedly false Schedules and Statement of Financial Affairs, and regarding the disposition of all of his income, the nature of his community interest in THBI, his failure to disclose sources of self-employment income, and his failure to disclose his service as trustee for a trust whose beneficiary is his wife's mother.

17. The bankruptcy system relies on a debtor to deal honestly with his creditors by making full, complete and honest disclosures in his statements and schedules. *Morton v. Dreyer (In re Dreyer),* 127 B.R. 587 (Bankr. N.D. Tex. 1991).

18. However, the failure by a debtor to disclose insignificant or essentially worthless assets is not something that, in and of itself, requires a discharge to be barred. *Cruz v. Topping (In re Topping),* 84 B.R. 840 (Bankr. M.D. Fla. 1988).

19. The question of whether Todd's omissions were made knowingly and fraudulently means that there must have been an intentional, untruthful relationship to the matter material to the

bankruptcy. *In re Schnurr*, 107 B.R. at 128; *Federal Land Bank v. Ellingson (In re Ellingson)*, 63 B.R. 271 (Bankr. N.D. Iowa 1986).

20. In the present case, the Court determines that Cadle has not proved by a preponderance of the evidence that any asset omitted from the schedules was omitted knowingly and fraudulently, as required by the statute. Alternatively, the Court determines that any omissions from the schedules were not material enough to bar Todd's discharge.

21. The funds placed in Nancy Todd's account were community funds and were used for community household purposes. Cadle even argues that Mr. Todd maintained control over this; therefore, it is unclear that Cadle ever established a "transfer" which was omitted.

22. The evidence at trial established that Debtor Todd has no financial stake in the Trust, and never has.

23. No evidence established a community interest by Debtor Todd in his wife's stock in THBI. The only evidence was that Mrs. Todd's interest in THBI was her separate property, obtained with separate property funds. Cadle argues that "[t]he bankruptcy estate may have a community estate reimbursement claim for the value of Todd's time, toil, and effort which contributed to an increase in the value of his wife's separate property interest in THBI." (Pl.'s Trial Br.) Todd was fairly paid for the work he did at THBI. Under Texas law, Mr. Todd's separate estate, or Mr. Todd's share of the community estate, has a claim for economic contribution against Mrs. Todd's separate estate when Mr. Todd makes an economic contribution to Mrs. Todd's separate property. TEX. FAM. CODE ANN. § 3.403(a) (Vernon Supp. 2002). TEX. FAM. CODE ANN. § 3.402(b)(2) (Vernon Supp. 2002) clearly states that economic contribution does not include the contribution of time, toil, talent or

effort during the marriage. Furthermore, TEX. FAM. CODE ANN. § 3.404(b) (Vernon Supp. 2002) states that a potential claim for economic contribution does not create an ownership interest in the separate property of the other spouse and only matures on the dissolution of the marriage or the death of either spouse. Thus, Mr. Todd has no present interest in any economic contribution claim as alleged by Cadle. Mr. Todd's individual claim for community estate reimbursement, if any, is not ripe under Texas law and cannot be even a contingent claim required to be disclosed in his schedules.

24. The testamentary trust established by Todd's wife only goes into effect under her will and when she dies. Debtor Todd has no interest now in that testamentary trust or in the life insurance policy for which that Trust is a beneficiary.

Failure to Explain

25. Cadle finally argues that Todd's discharge should be barred under Bankruptcy Code § 727(a)(5). Cadle claims Todd also has failed to explain satisfactorily, before determination of denial of discharge, a loss of assets or deficiency of assets to meet the Debtor's liabilities.

26. The Bankruptcy Court has a duty to deny discharge where the debtor fails to adequately explain shortage, loss, or disappearance of estate assets. *In re D'Agnese,* 86 F.3d 732 (7th Cir. 1996). However, when a debtor's wages are no more than enough to cover his reasonable living expenses for himself and his family, the debtor's inability to account for his wages is not sufficient grounds to deny a discharge. *In re Hale*, 274 F.Supp. 813, 816 (W.D. Va. 1967).

27. Fraudulent intent is not required to deny a discharge based on loss or deficiency of assets. *In re Gannon,* 173 B.R. 313 (Bankr. S.D.N.Y. 1994); *In re Bell,* 156 B.R. 604 (Bankr. E.D.

Ark. 1993). The discharge statute requires a satisfactory explanation for the whereabouts of the debtor's assets, which must consist of more than vague, indefinite, and uncorroborated assertions by the debtor. *In re D'Agnese,* 86 F.3d 732 (7th Cir. 1996); *In re Lordy,* 214 B.R. 650 (Bankr. S.D. Fla. 1997) (denying discharge based on assertion that funds were used on undocumented living expenses); *In re Dupree,* 197 B.R. 928 (Bankr. N.D. Ala. 1996) (denying discharge on vague and indefinite explanation that "monies were spent").

28. On this count, Cadle fails as a matter of fact and of law. Cadle wants Todd's discharge barred because Todd did not explain his self-employment income. Also, Cadle claims the omission of the mother-in-law's trust should be enough to bar Todd's discharge.

29. In his testimony, Todd explained his extra income as referral fees. He did not disclose that he was a trustee for a trust set up for his mother-in-law; however, such disclosure was not material because Todd is neither a settlor nor a beneficiary of that trust. He has no stake in the Trust, and, therefore, the Trust is not an asset of Todd which needs further explanation.

30. Cadle claims Todd has enjoyed a high salary and other income for many years, but cannot satisfactorily explain why none of this money was in his hands at the time of the filing of the case. However, the Debtor's wife testified, and the checking account records (Cadle Ex. 14) satisfactorily indicate, that the funds placed into the accounts were used to pay household expenses of Debtor Todd and his wife. The records suggest that the funds on a monthly basis were about a "wash" – mostly speaking, the deposits and checks were approximately equal. (Cadle Ex. 14.) The funds placed in that account were used mostly for household bills, without much accumulation each month. (*Id.*) Given that Debtor's expenses generally equalled his income, Debtor's inability to explain why he has not accumulated any wealth

is not sufficient grounds for denial of discharge. *See In re Hale*, 274 F.Supp. at 815-16.

31. Cadle also claims Debtor was not able to explain the source of much of this income, as reflected in his tax returns. Debtor did explain the nature of the income, but could not remember the party who paid him. That income is relatively minor. In addition, past "income" is not an "asset." For these reasons, the discharge of the Debtor will not be denied under 11 U.S.C. § 727(a)(5).

32. Any finding of fact may also be deemed a conclusion of law.

Signed: 1/13/03

Harlin D. Hale
United States Bankruptcy Judge