UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
Western Division

In re:	)	Bankr. No. 97-50379
JOHN NICHOLAS BARDONNER Soc. Sec. No. [redacted]-1263	)	Chapter 7
Debtor.	)	
JACK WEAVER, DDS.	)	Adv. No. 98-5016
Plaintiff,	)	
-vs-	)	MEMORANDUM OF DECISION RE: DEFENDANT'S MOTION FOR SUMMARY JUDGMENT
JOHN NICHOLAS BARDONNER	)	
Defendant.	)	

The matter before the Court is Defendant-Debtor's Motion for Summary Judgment. This is a core proceeding under 28 U.S.C. § 157(b)(2). This letter decision and accompanying order shall constitute the Court's findings and conclusions under F.R.Bankr.P. 7052. As set forth below, the Court concludes that summary judgment for Defendant shall be granted as to Plaintiff's non dischargeability claim under 11 U.S.C. § 523(a)(4) and (a)(6) but denied as to Plaintiff's non dischargeability claim under § 523(a)(2)(A).

I.

SUMMARY OF MATERIAL FACTS IN LIGHT MOST FAVORABLE TO PLAINTIFF.

Dr. Jack Weaver entered into an agreement to sell a dental practice to Dr. John N. Bardonner. A letter of understanding was signed by both parties on October 3, 1996. It also set forth a lease option. Bardonner assumed management and control of the dental practice on October 3, 1996 and began paying Weaver as an

associate for services performed after that date. Bardonner made a down payment of $2,500.00. He also was attempting to get financing at that time to complete the purchase. Weaver was aware of Bardonner's need to get financing. He provided American State Bank a letter setting forth the assets he was selling to Bardonner and his valuation of the property.

Closing under the letter of understanding was to be by October 31, 1996. That deadline was not met. The dentists' letter of understanding automatically converted to a month to month tenancy. Bardonner paid rent to Weaver for October, November, and December 1996 and continued the practice.

Bardonner did not obtain financing from American State Bank but he did get a loan from Business Finance Corporation in early November 1996. As security for the loan, Business Finance obtained a factoring agreement related to Bardonner's accounts receivable and a security interest in "goods and inventory." The factoring agreement and related security documents provided that Bardonner could place another security interest on the collateral only with Business Finance's permission. Bardonner did not give Business Finance a copy of the letter of understanding but did give them a copy of the letter that Weaver wrote to American State Bank.

A new Purchase and Security Agreement and a separate Lease Agreement were executed by Weaver and Bardonner on December 3 and 4, 1996. The Purchase and Security Agreement covered the practice and equipment and supplies. The Lease Agreement covered the real property where the practice was located. The Purchase and

Security Agreement incorporated both the letter of understanding and the Lease Agreement. At the time the Purchase and Security Agreement were executed, Bardonner did not inform his own attorney or Weaver about the loan he had obtained from Business Finance and the security agreement Business Finance had taken on assets of the practice.

Under the Purchase and Security Agreement, the parties acknowledged that Bardonner

> has assumed possession and management of the practice as of October 3, 1996, and therefore has assumed all obligation for dental services provided as well as all expenses and obligations for the Dental Practice from and after the said date[,] which is the agreed date of possession for the purposes of this agreement.

However, the transfer of assets and the attachment of Weaver's security interest were not to take place until a $20,000.00 down payment was made. The Purchase and Security Agreement also provided that Bardonner assumed the risk of loss from the date of possession and Bardonner agreed not to dispose of any secured property during the terms of the Purchase and Security Agreement without Weaver's consent.

Bardonner paid Weaver another $17,500.00 in January 1997 to complete the $20,000.00 down payment. He used the funds supplied by Business Finance.

Bardonner filed a Chapter 13 petition in bankruptcy on August 14, 1997. In late December 1997, while the Chapter 13 proceeding was pending, Bardonner and Weaver entered into an Employment Agreement. The Employment Agreement acknowledged that Bardonner had defaulted on the Purchase Agreement and that he

voluntarily surrendered the dental practice to Weaver. The Employment Agreement also recognized the potential impact of state court litigation among the two dentists and Business Finance Corporation regarding who had the superior lien on certain accounts receivable but the Agreement did not clearly set forth the Agreement's contingencies that were dependent on the litigation's outcome. The Employment Agreement was incorporated into two different modified plans that Bardonner proposed but neither plan was ever confirmed and the Employment Agreement was never approved separately by the Court.

Weaver obtained relief from the automatic stay on January 2, 1998. Business Finance Corporation obtained relief from the automatic stay, upon approval of a stipulation with Debtor, on March 26, 1998. Bardonner converted his case from a Chapter 13 to a Chapter 7 on May 29, 1998. Eventually, Weaver's employment of Bardonner was terminated.

On August 31, 1998, Weaver commenced an adversary proceeding against Bardonner seeking a declaration that any sums Bardonner may owe him because of Weaver's lien priority dispute with Business Finance Corporation should be non dischargeable under 11 U.S.C. § 523(a)(2), (4), or (6). Bardonner answered the complaint and subsequently filed a Motion for Summary Judgment on the grounds that Weaver's allegations did not entitle him to recovery under § 523(a)(2) because no fraudulent intent was alleged or can be shown or under § 523(a)(4) because Bardonner was not a fiduciary for Weaver. Bardonner also argued that Weaver had waived any

claims under the Purchase and Security Agreement when he executed the Employment Agreement.

Weaver responded to the summary judgment motion. He highlighted Bardonner's failure to advise either Business Finance or Weaver about the other's actual or intended security interest in the practice assets when Bardonner executed the various agreements with them. He argued that Bardonner's failure to disclose was fraudulent and ultimately put him and Business Finance into yet unresolved state litigation over who had the superior security interest.

II. Summary Judgment

Summary judgment is appropriate when "there is no genuine issue [of] material fact and . . . the moving party is entitled to a judgment as a matter of law." F.R.Bankr.P. 7056 and F.R.Civ.P. 56(c). An issue of material fact is *genuine* if it has a real basis in the record. *Hartnagel v. Norman*, 953 F.2d 394, 395 (8th Cir. 1992)(quotes therein). A genuine issue of fact is *material* if it might affect the outcome of the case. *Id.* (quotes therein). The matter must be viewed in the light most favorable to the party opposing the motion. *F.D.I.C. v. Bell*, 106 F.3d 258, 263 (8th Cir. 1997); *Amerinet, Inc. v. Xerox Corp.*, 972 F.2d 1483, 1490 (8th Cir. 1992)(quoting therein *Matsushita Elec. Industrial Co. v. Zenith Radio*, 475 U.S. 574, 587-88 (1986), and cites therein). Further,

> the plain language of Rule 56(c) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden at trial.

Amerinet, 972 F.2d at 1490 (quoting *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986)). The movant meets this burden if he shows that the record does not contain a genuine issue of material fact and he points out that part of the record that bears out his assertion. *Handeen v. LeMaire*, 112 F.3d 1339, 1346 (8th Cir. 1997)(quoting therein *City of Mt. Pleasant v. Associated Electric Coop*, 838 F.2d 268, 273 (8th Cir. 1988). No defense to an insufficient showing is required. *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 156 (1970) (cite therein); *Handeen*, 112 F.3d at 1346. If the movant meets his burden, however, the non movant, to defeat the motion, "must advance specific facts to create a genuine issue of material fact for trial." *Bell*, 106 F.3d at 263 (quoting *Rolscreen Co. v. Pella Products of St. Louis, Inc.*, 64 F.3d 1202, 1211 (8th Cir. 1995)). The non movant must do more than show there is some metaphysical doubt; he must show he will be able to put on admissible evidence at trial proving his allegations. *Bell*, 106 F.3d 263 (citing *Kiemele v. Soo Line R.R. Co.*, 93 F.3d 472, 474 (8th Cir. 1996), and *JRT, Inc. v. TCBY System, Inc.*, 52 F.3d 734, 737 (8th Cir. 1995)).

III. Dischargeability: Fraud by a Fiduciary

Applicable Law. For a debt to be declared non dischargeable under § 523(a)(4), the debtor must have acted fraudulently or in defalcation of duty while in a fiduciary capacity. The elements for fraud under § 523(a)(4) are the same as for fraud under § 523(a)(2)(A). *McDaniel v. Border (In re McDaniel)*, 181 B.R. 883, 887 (Bankr. S.D. Tex. 1994). The fiduciary capacity must arise from an express, not constructive, trust. *Barclays American/ Business Credit, Inc., v. Long (In re Long)*, 774 F.2d 875, 878-79 (8th Cir. 1985).

> It is the substance of a transaction, rather than the labels assigned by the parties, which determines whether there is a fiduciary relationship for bankruptcy purposes.

Long, 774 F.2d at 878 (citing *Davis v. Aetna Acceptance Co.*, 293 U.S. 328, 333 (1934)). The fiduciary relationship to which § 523(a)(4) applies does not cover trusts imposed on transactions by operation of law or as a matter of equity. *ITT Life Insurance Co. v. Haakenson (In re Haakenson)*, 159 B.R. 875, 887 (Bankr. D.N.D. 1993).

Whether a party is a fiduciary under § 523(a)(4) is a question of federal law. *Kunzler v. Bundy (In re Bundy)*, 95 B.R. 1004, 1013 (Bankr. W.D. Mo. 1989). However, state law is relevant when deciding whether an express trust relationship exists. *Ragsdale v. Haller*, 780 F.2d 794 (9th Cir. 1986); *Bundy*, 95 B.R. at 1013.

Discussion. Plaintiff Weaver has not offered any evidence that Bardonner was a fiduciary for Weaver. Their relationship arose only from the sale, lease, and employment agreements between them, none of which imposed any kind of formal trust. Hence, summary judgment shall be entered for Defendant Bardonner regarding Plaintiff's count under § 523(a)(4).

IV. Dischargeability: Wilful and Malicious Debt

Applicable Law. A debt for a willful and malicious injury to another or to the property of another is excepted from discharge under 11 U.S.C. § 523(a)(6). For § 523(a)(9) to apply, the injury or the consequences of the act must be deliberate or intentional; the section does not apply if there was merely a deliberate or intentional act that led to injury. *Kawaauhau, v. Geiger*, 118 S.Ct. 974, 977 (1998). Debts arising from reckless or negligent torts are not excepted from discharge. *Id.*

Discussion. Weaver has offered no evidence that Bardonner acted with the intent of financially harming Weaver. While Weaver may be able to show that Bardonner intentionally withheld relevant information to foster his deal with Weaver, Weaver has not set forth any evidence that Bardonner's intent in making this deal was ultimately to harm Weaver financially. Hence, Weaver cannot meet the narrow definition of "wilful injury" required by § 523(a)(6) as interpreted by *Kawaauhau*, 118 S.Ct. at 977. Summary judgment for

Defendant Bardonner shall be entered on that count.[1]

V. Dischargeability: General Fraud

Applicable Law. A debt for money, property, services, or an extension or renewal of credit is excepted from discharge under § 523(a)(2)(A)[2] to the extent is was obtained by "false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition." As § 523(a)(2)(A) is interpreted by case law, the party opposing discharge must show that:

1. the debtor made the false representation;
2. at the time made, the debtor knew them to be false;
3. the representations were made with the intention and purpose of deceiving the creditor;
4. the creditor justifiably relied on the representation; and
5. the creditor sustained the alleged injury as a proximate result of the representations having been made.

Field v. Mans, U.S., slip op. 94-967 (Nov. 28, 1995); *Caspers v. Van Horne (In re Van Horne)*, 823 F.2d 1285, 1287 (8th Cir. 1987); *Thul v. Ophaug (In re Ophaug)*, 827 F.2d 340 (8th Cir. 1987).

Evidence of the surrounding circumstances may be presented from which intent may be inferred. *Van Horne*, 823 F.2d at 1287

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[1] Neither party briefed § 523(a)(6) but it was pled by Plaintiff Weaver.

[2] Section 523(a)(2)(B) is not considered because Dr. Bardonner did not give Dr. Weaver a financial statement or other statement in writing regarding his financial condition.

(cites therein). The debtor may be required to overcome the circumstantial evidence with more than unsupported assertions of honest intent. *Id.* at 1287-88 (cites therein). However,

> A fraud case cannot be won by a showing of broken promises and unrealized business potential. [The plaintiff must] show not only that the defendants did not keep their promises, but also that they did not intend to keep them when they made them (or that they knew they could not keep them).

Coenco, Inc., v. Coenco Sales, Inc., 940 F.2d 1176, 1178 (8th Cir. 1991). Intentional non disclosure of a material fact can be actual fraud under § 523(a)(2)(A). *Van Horne*, 8223 F.2d at 1288.

Under a recent Supreme Court ruling, the creditor must have *justifiably* relied on the debtor's representations. *Field v. Mans*, 116 S.Ct. 437, 444-46 (1995). Justifiable reliance requires the Court to consider the particular plaintiff - - his knowledge and his intelligence -- and the circumstances of the particular case. *Id.* at 444. The Court must ask whether the plaintiff had knowledge of facts that should have warned him that he is being deceived and that he needs to make further investigation. *Id.* However, a person is justified in relying on a factual representation without conducting an investigation, so long as the falsity of the representation would not be patent upon cursory examination. *Id.* A community standard of reasonableness is no longer the sole consideration. *Id.* at 444-46. Reasonableness, however, is still relevant as it goes to the probability of actual reliance. "[T]he greater the distance between the reliance claimed and the limits of

the reasonable, the greater the doubt about reliance in fact." *Id.* at 446.

Discussion. The Court concludes that summary judgment on this general fraud count pursuant to § 523(a)(2)(A) should not be entered. Plaintiff has come forward with some evidence that Bardonner knowingly failed to disclose to Weaver his financial arrangement with Business Finance and that Weaver relied on that non disclosure to his detriment. At trial, Weaver will need to carefully address each element of § 523(a)(2)(A) as set forth above.

This Court, however, will not go forward with a trial at this time. The state court litigation among Business Finance and Drs. Bardonner and Weaver will determine what harm, if any, Weaver suffered because of the security interest Bardonner gave Business Finance before the Purchase and Security Agreement with Weaver was executed. Until then, Weaver does not have a debt against Bardonner. Further, some of the evidence at the state court trial will duplicate what this Court needs to receive. There is no need for the parties to present it twice. Since the state court's inquiry appears to be broader, it should proceed first.

Finally, the Court's conclusions here are not premised on Weaver and Bardonner's January 1, 1998 Employment Agreement. That agreement was never approved by this Court, as it should have been since Bardonner was in Chapter 13 at the time. *See* F.R.Bankr.P. 9010. At the time the agreement became a part of the record, the

Court also understood that it resolved all claims between the parties. Since it was not noticed for objections and approved, however, and since any *de facto* approval or recognition of it now may adversely effect the Chapter 7 estate, the Court has not and will not consider it a material part of this adversary proceeding.

An order granting in part and denying in part Bardonner's Motion for Summary Judgment will be entered. The Court will conduct a telephonic status conference with counsel to determine the status of the state court litigation and reschedule the trial date from December 21, 1998, if possible.

Dated this 17th day of December, 1998.

BY THE COURT:

Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:
Charles L. Nail, Jr., Clerk
By: M. Kay Rieck
Deputy Clerk

UNITED STATES BANKRUPTCY COURT ★ SEAL

NOTICE OF ENTRY
Under F.R.Bankr.P. 9022(a)
Entered

DEC 17 1998

Charles L. Nail, Jr., Clerk
U.S. Bankruptcy Court
District of South Dakota

I hereby certify that a copy of this document was mailed, hand delivered, or faxed this date to the parties on the attached service list.

DEC 17 1998

Charles L. Nail, Jr., Clerk
U.S. Bankruptcy Court, District of South Dakota
By M. Kay Rieck

Case: 98-05016 Form id: 122 Ntc Date: 12/17/1998 Off: 3 Page : 1
Total notices mailed: 5

Intereste Bardonner, John Nicholas 429 N. Ellsworth Rd., Box Elder, SD 57719
Intereste Bihlmeyer, Lawrence Robin 1750 Dorothy Drive, Rapid City, SD 57701
Aty Frederick, Elizabeth M. 2902 W. Main St #4, Rapid City, SD 57702
Aty Martin, Robert A. PO Box 484, Rapid City, SD 57709
Intereste Whetzal, Dennis PO Box 8285, Rapid City, SD 57709