

**UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK**

In Re:

STEPHEN T. CALLAWAY,

Debtor.

BK. NO. 94-21815

COMMUNITY BANK, N.A.,

Plaintiff,

A.P. NO. 94-2117

vs.

STEPHEN T. CALLAWAY,

Defendant.

DECISION & ORDER

BACKGROUND

On August 29, 1994, the Debtor, Stephen T. Callaway, (the "Debtor") filed a petition initiating a Chapter 7 case.

On November 29, 1994, Community Bank, National Association ("Community") commenced an adversary proceeding to have an indebtedness guaranteed by the Debtor determined to be nondischargeable pursuant to the provisions of Section 523(a)(2)(A). The indebtedness in question (the "93 Loan") was evidenced by an April 23, 1993 Promissory Note in the original principal amount of \$30,240.48, executed by Ellsworth Thomas Associates #1, a Limited Partnership, (the "Partnership") and guaranteed by the Debtor who was a partner.

After a pretrial conference was conducted by the Court on January 31, 1995, the Debtor made a Motion for Summary Judgment (the "Summary Judgment Motion") which was made returnable on July 12, 1995.

The pleadings filed in connection with the Summary Judgment Motion indicated that on November 29, 1988, Community made a loan (the "88 Loan") to the Partnership in the original principal amount of \$178,000 which was secured by a mortgage on property located on Exchange

Street in Geneva, New York (the "Dove Block Property"). The 88 Loan was also guaranteed by the Debtor and another partner. The City of Geneva had previously commenced an *in rem* real property tax foreclosure proceeding against the Dove Block Property and the time for the Partnership or Community, as a mortgage holder, to redeem the Dove Block Property expired on or about April 23, 1993. To prevent the Dove Block Property from being lost to the Partnership and Community, as a mortgage holder, the 93 Loan was made, the proceeds of which were used to pay the outstanding real property taxes due to the City of Geneva.

The Complaint in the adversary proceeding alleged that the 93 Loan should be determined to be nondischargeable because at the time the 93 Loan was made to the Partnership and guaranteed by the Debtor, the Debtor had failed to list an indebtedness to his mother in the approximately amount of \$400,000 in his January, 1993 financial statement and had otherwise failed to advise Community of the indebtedness and his intention to secure it by a mortgage which: (a) would cover all of his extensive real property holdings except for the Dove Block Property; and (b) was being prepared at the time of the 93 Loan. The Complaint further alleged that on April 28, 1993, five days after the 93 Loan was made by Community and guaranteed by the Debtor, a \$350,000 mortgage was executed in favor of the Debtor's mother which was recorded April 29, 1993 and covered numerous parcels of the Debtor's real property holdings. Community asserted that the 93 Loan by the Partnership was obtained, at least in part, because of the perceived financial strength of the Debtor who the Bank from its long term dealings with him believed had substantial unsecured equity in his real property holdings. By failing to disclose (concealing) his true financial condition to Community (his significant indebtedness to his mother and intention to immediately secure that indebtedness), the Debtor obtained the 93 Loan for himself and the Partnership by false pretenses within the meaning and intent of Section 523(a)(2)(A) because he knew Community believed he had substantial unsecured equity in his real estate holdings and would not have made the 93 Loan if they knew the

mortgage to his mother was to be executed and recorded a few days after the 93 Loan was made.

The ground asserted by the Debtor for granting the Summary Judgment Motion was that Community had suffered no damage as a result of the 93 Loan. The Motion reasoned that by making the 93 Loan, the Dove Block Property, which at the time of the 93 Loan and at the time of the Summary Judgment Motion was worth more than the amount of the 93 Loan, was saved for the Partnership and Community, rather than lost, and that the first monies received by Community from any disposition of the Dove Block Property, whether by a voluntary sale or foreclosure, could and would be applied to repay the 93 Loan. Therefore, there was no damage.

On the July 12, 1995 return date, the Court orally denied the Summary Judgment Motion, directed that discovery be completed and set the matter down for the Court's Trial Calendar on August 16, 1995.

By letter dated July 13, 1995, the attorney for the Debtor requested that the Court reconsider its decision on the Summary Judgment Motion, conduct a short telephonic conference with the attorneys for the parties and issue a decision in support of its denial of the Summary Judgment Motion.

On August 8, 1995, the Court conducted the requested conference and agreed to issue this Decision so that the Adversary Proceeding could be prosecuted within the time frames previously established by the Court.

DISCUSSION

In a Memorandum of Law submitted in opposition to the Summary Judgment Motion, Community cited to the Court the opinion of the United States Court of Appeals for the First Circuit in *In Re Goodrich*, 999 F.2d 22 (1st Cir. 1993) for the proposition that the legislative history of Section 523(a)(2)(B) indicated that a showing of ultimate damage is not required to sustain a cause

of action under that subsection, which deals with financial statements, and that the holding is equally applicable to a Section 523(a)(2)(A) claim where Congress did not specifically make damage a requirement.

Notwithstanding whether damage is or is not a necessary element to a determination of nondischargeability pursuant to Section 523(a)(2)(A), the Court finds that on the pleadings before it on the Summary Judgment Motion, the Debtor has not made a sufficient showing that Community will not suffer damage in the event the 93 Loan is determined by the Court to be dischargeable.

The April 23, 1993 Promissory Note, attached as Exhibit D to the Summary Judgment Motion, specifically stated that it is an unsecured obligation.¹ Therefore, based on the documents before the Court in connection with the Summary Judgment Motion, any proceeds of the Dove Block Property obtained by Community, either by a voluntary sale or a foreclosure, could not properly be applied to the 93 Loan which by its terms was unsecured. Therefore, the Court concluded that unless the 93 Loan is determined to be nondischargeable, and as a result ultimately paid by the Debtor, Community will not be paid the full amount due on the 93 Loan. This is because it was clear that the Dove Block Property was worth significantly less than \$100,000, both as of the date of the Debtor's petition and at the time of the hearing on the Summary Judgment Motion, and the Debtor's

¹ At the telephonic conference conducted on August 8, 1995, it was indicated to the Court that a number of months after April, 1993, additional agreements may have been entered into which secured the 93 Loan by the Dove Block Property, however, those documents were not part of the record when the Court made its decision on July 12, 1995. Even the subsequent securing of the 93 Loan by the Dove Block Property does not necessarily mean that the first proceeds from a disposition of the Property should or would be applied to the 93 Loan or that Community would not have suffered damage if such an application were made. The reasons why the unsecured 93 Loan was later secured by the Dove Block Property may have been for Community's internal bookkeeping purposes or other reasons which might not change the state of the facts which existed at the time of the 93 Loan on April 23, 1993 made on an unsecured basis, or the various determinations that the Court will be required to make under Section 523(a)(2)(A). These are at best issues of fact to be determined at trial.

bankruptcy estate will not otherwise pay his creditors in full. As a result, it appeared from the record before the Court on the Summary Judgment Motion that Community would suffer damage unless the 93 Loan was determined to be nondischargeable.

CONCLUSION

For the foregoing reasons, the Debtor's Motion for Summary Judgment, based on the assertion that Community will suffer no damage as a result of its April 23, 1993 loan, is in all respects denied.

IT IS SO ORDERED.

/s/

HON. JOHN C. NINFO, II
U.S. BANKRUPTCY JUDGE

Dated: August 9, 1995