

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

---

**In re:**

**JAMES O. YOUNG,**

**Debtors.**

**CASE NO. 97-20967**

**DECISION & ORDER**

---

**RICHARD A. KROLL and  
ERLE W. JACKSON,  
d/b/a EARLY PARK PROPERTIES,**

**Plaintiffs,**

**V.**

**JAMES O. YOUNG,**

**Defendants.**

---

**AP #99-2287**

**BACKGROUND**

On March 19, 1997, James O. Young, d/b/a The Foundation Group (“Young”) filed a petition initiating a Chapter 13 case. On the Schedules and Statements required to be filed by Section 521 and Rule 1007, Young: (1) indicated that he was the owner of real property located at 1349 Culver Road, Rochester, New York (“Culver Road”) which had a current market value of \$80,000.00 and was subject to a first mortgage in favor of Midfirst Mortgage (“Midfirst”) with an outstanding balance of \$42,659.64 (the “Midfirst Mortgage”) and a second mortgage in favor of Erle W. Jackson (“Jackson”) with an outstanding balance of \$37,340.36 (the “Jackson Mortgage”); (2) indicated that he owned a residence on Knickerbocker Avenue, and four parcels of investment real estate, including Culver Road; (3) scheduled unsecured claims in the amount of \$20,293.61; and (4) indicated that

**BK. 97-20967**  
**AP. 99-2287**

he had total monthly income of \$7,025.00, which included his salary at Territory Incorporated and income from investment real estate, and monthly expenses of \$6,060.66, leaving him with excess monthly income of \$964.34.

Along with his petition, Young filed a Chapter 13 plan which provided for: (1) monthly payments to the Chapter 13 Trustee (the "Trustee") of \$810.00 for a period of five years; (2) regular monthly post-petition payments to all mortgage holders outside the plan; (3) the payment through the plan of arrears due on various mortgages; and (4) a one hundred percent (100%) distribution to unsecured creditors.

No party in interest, including Jackson who had notice of the confirmation hearing, objected to the confirmation of Young's plan, and on June 16, 1997, the Court confirmed an amended plan (the "Amended Plan") which increased the monthly payments to \$1,227.00 in order to provide for the payment of an automobile loan.

The Amended Plan provided for the payment through the Plan of mortgage arrears due to Midfirst in the amount of \$4,537.01, but it did not provide for any payments through the Plan on the Jackson Mortgage because Young had advised the Trustee that the Mortgage was current.

On May 5, 1999, the Trustee filed a Motion to Dismiss Young's Chapter 13 case because he had failed to maintain his plan payments. The Motion indicated that Young's last partial payment had been received by the Trustee on March 18, 1998, and that the Amended Plan was currently \$15,819.64 in arrears.

On June 18, 1999, Young filed a Notice which converted his case to a Chapter 7 case.

**BK. 97-20967**  
**AP. 99-2287**

On September 27, 1999, Richard A. Kroll, who had taken an interest in the Jackson Mortgage by assignment, (“Kroll”) and Jackson commenced an Adversary Proceeding against Young which requested that the Court determine that the amount due on the Jackson Mortgage was nondischargeable pursuant to Section 523(a)(2)(A).<sup>1</sup>

The Complaint in the Adversary Proceeding alleged that: (1) Young had purchased Culver Road and assumed the Jackson Mortgage on March 12, 1997, and then filed his Chapter 13 petition seven (7) days later on March 19, 1997; (2) Young had failed to make all of the mortgage payments due on the Jackson Mortgage; (3) during the course of his Chapter 13 case, Young had received rents at Culver Road and used them for purposes other than to maintain the property or pay the Midfirst or Jackson Mortgages; and (4) Young had obtained money and property from Kroll and Jackson by false representations, false pretenses and actual fraud, so that the \$37,354.74 outstanding balance due on the Jackson Mortgage should be determined to be nondischargeable.

On July 27, 2000, the Court conducted a trial at which it heard the testimony of Kroll, Jackson and Young.

---

<sup>1</sup> Section 523(a)(2)(A) provides that:

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt—

(2) for money, property, services, or an extension, renewal, or re financing of credit, to the extent obtained by—

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition[.]

11 U.S.C. § 523(a)(2)(A) (2000).

**BK. 97-20967**  
**AP. 99-2287**

At the trial, Kroll testified that: (1) prior to its purchase by Young, Kroll and Jackson, d/b/a Early Park Properties, owned Culver Road which was subject to the Jackson Mortgage;<sup>2</sup> (2) Kroll and Jackson had placed Culver Road on the market for sale, and in December 1996, Young, with the assistance of a broker (the “Broker”), submitted a purchase offer which provided for the assumption of the Midfirst and Jackson Mortgages; (3) Young received \$4,423.88 in escrows and credits to the buyer from Early Park Properties in connection with the closing of Culver Road; (4) Young never disclosed to Kroll or Jackson that he was contemplating filing a bankruptcy case when he closed on the sale of Culver Road; (5) Kroll and Jackson would not have completed the sale to Young if they knew he was contemplating a bankruptcy; (6) prior to the closing of Culver Road, Young had represented to him that he: (a) was a mortgage broker and property manager; and (b) intended to refinance the Midfirst Mortgage pursuant to an FHA Streamliner Program which would reduce the first mortgage interest rate from twelve percent (12%) to nine percent (9%) and result in positive cash flow at Culver Road, which at the time of the sale was experiencing a negative cash flow; (7) although Young ultimately paid all of the monthly mortgage payments due on the Jackson Mortgage through December 1997, he failed to pay all of the monthly payments due on the Midfirst Mortgage, even though Young represented to him on a number of occasions during his Chapter 13 case that he was paying the Midfirst Mortgage; (8) Kroll and Jackson did not bid in at the foreclosure sale of Culver Road by Midfirst, in order to protect any value in the Jackson Mortgage, because they did not have the approximately \$51,000.00 then due on the Midfirst Mortgage; (9) he believed that because

---

<sup>2</sup> The Jackson Mortgage was granted by a prior owner of Culver Road.

**BK. 97-20967**

**AP. 99-2287**

of the filing of his bankruptcy case, Young was unable to refinance the Midfirst Mortgage under the FHA Streamliner Program; and (10) neither Kroll nor Jackson had run a credit check on Young at the time they accepted his purchase offer for Culver Road, nor did they do any other investigation into his financial condition, they simply accepted the statements of the Broker that Young was a mortgage broker and property manager and should be able to refinance the Midfirst Mortgage.

At trial, Young testified that: (1) he had no contact with Jackson before the closing of Culver Road, and he had never represented to Kroll or Jackson during his Chapter 13 case that he was paying the Midfirst Mortgage; (2) his first discussions with a bankruptcy attorney occurred several months after his purchase offer on Culver Road was accepted; (3) his bankruptcy schedules and statements had been substantially prepared prior to the March 12, 1997 closing of Culver Road, and because of the imminent closing, they reflected that he was the owner of Culver Road; (4) he did not have a specific recollection of representing to Kroll that he was going to “streamline” the Midfirst Mortgage, but acknowledged that he may very well have had a discussion about refinancing, since refinancing the first mortgage to generate additional cash flow made good business sense; (5) at the times when he closed on Culver Road and filed his Chapter 13 petition, he did not believe that a pending Chapter 13 case would prevent a refinance of the Midfirst Mortgage by the FHA or another financial institution; (6) after the filing of his bankruptcy petition he contacted several banks in an attempt to refinance the Midfirst Mortgage, but was unsuccessful; (7) he had used most of the cash he received as escrow and closing adjustments at the closing of Culver Road to pay the Midfirst Mortgage, escrow shortages, property insurance and a substantial water bill; (8) when he offered to purchase Culver Road in December 1996, he knew that it had a slightly negative cash flow, but

**BK. 97-20967**  
**AP. 99-2287**

considered it essentially a break-even property; (9) he had lost the downstairs tenant at Culver Road in April 1997 and the upstairs tenant in August 1997, after which there were no rents received at Culver Road; (10) his Chapter 13 case failed because: (a) in December 1997 he lost his job; and (b) he never received the rents at his investment properties that he had projected when he filed his petition and his Amended Plan was confirmed; (11) in connection with his purchase of Culver Road, neither Kroll nor Jackson had ever asked him whether he was contemplating filing bankruptcy; (12) in connection with his purchase of Culver Road, neither Kroll nor Jackson ever asked him for any financial information whatsoever; and (13) at the times he closed on Culver Road and filed his Chapter 13 petition, he believed that he would be able to pay the Midfirst and Jackson Mortgages in full and never intended on filing a Chapter 13 case with a one hundred percent (100%) plan to obtain a discharge from the indebtedness represented by the Jackson Mortgage.

### **DISCUSSION**

To prevail on a cause of action for false pretenses, Kroll and Jackson must prove that: (1) a false representation was made with the intent to deceive them; (2) they relied on the representation; and (3) they sustained the injury due to the reliance. See *In re Young*, 91 F.3d 1367 (10<sup>th</sup> Cir. 1996); *In re Shaheen*, 111 B.R. 48 (Bankr. S.D.N.Y. 1990). Silence regarding a material fact can constitute a false representation. See *In re Van Horne*, 823 F.2d 1285, 1288 (8<sup>th</sup> Cir. 1987) and the cases cited therein. In addition, the reliance only needs to be justifiable. *Field v. Mans*, 516 U.S. 59 (1995).

To prevail on a cause of action for false pretenses, Kroll and Jackson must prove that there was a series of events, activities, or communications which created a false and misleading set of

**BK. 97-20967**  
**AP. 99-2287**

circumstances or understanding of a transaction, by which Young wrongfully induced them to extend credit. *In re Reid*, 237 B.R. 577 (Bankr. W.D.N.Y. 1999); *In re Luppino*, 221 B.R. 693 (Bankr. S.D.N.Y. 1998).

After having heard the testimony of the witnesses at trial, observed the witnesses and their demeanor, formed an opinion as to the credibility of the witnesses, and reviewed the documentary evidence admitted at trial and the post-trial submissions, I find that: (1) Kroll and Jackson have not met their burden under Section 523(a)(2)(A) to prove by a preponderance of the credible evidence that Young obtained credit or property from them by false representations, false pretenses or actual fraud; (2) at the times Kroll and Jackson accepted Young's offer to purchase Culver Road and closed on the transaction, they did not ask Young about his financial condition or request that he provide them with any written information concerning his financial condition; (3) at the times when Kroll and Jackson accepted Young's offer to purchase Culver Road and closed on the transaction, Young did not make any actual representations to Kroll and Jackson, orally or in writing, concerning his financial condition; (4) at the times he closed on Culver Road and filed his Chapter 13 petition, Young intended to pay the Midfirst and Jackson Mortgages in full, and had a reasonable belief that he would be able to do so; (5) Young's reasonable belief at the time he filed his Chapter 13 bankruptcy petition that he would be able to pay the Midfirst and Jackson Mortgages in full, as well as all of his other existing creditors, even if he filed a Chapter 13 case, was confirmed by the recommendation of the Trustee that his Amended Plan was filed in good faith and was feasible; (6) the failure of Young to pay the Midfirst and Jackson Mortgages in full according to their terms, as assumed by him at the closing of Culver Road, was not due to the filing of his Chapter 13 case, but

**BK. 97-20967**  
**AP. 99-2287**

was primarily the result of his job loss and his investment properties not performing as projected;

(7) Kroll and Jackson did not believe that the filing of a Chapter 13 case by Young, seven days after he closed on Culver Road, was in bad faith, or made it unlikely that the Midfirst and Jackson Mortgages would be paid in full according to their terms as assumed by Young at the closing, because they failed to take any steps in Young's Chapter 13 case to: (a) object to the confirmation of the Amended Plan as being proposed in bad faith or not being feasible; (b) monitor the Debtor's operation and management of Culver Road during the Chapter 13 case to insure that the property was being properly maintained and that Young was making his plan payments and the mortgage payments on the Midfirst Mortgage; or (c) insist that the order confirming the Amended plan include a provision that in the event that any plan payments or regular monthly post-petition mortgage payments due to Midfirst were not paid, the automatic stay would terminate so that Kroll and Jackson could foreclose on the Jackson Mortgage; (8) an individual's failure to disclose that he is contemplating the filing of a Chapter 13 case with a plan which appears to be feasible and provides for full payment to all creditors is not a false representation per se because it is always a material fact in connection with a credit transaction, but is only one factor a Court should consider in determining whether credit has been obtained by false representations, false pretenses or actual fraud under Section 523(a)(2)(A); (9) based upon all of the facts and circumstances presented in this case, the failure of Young to advise Kroll and Jackson at the time of the closing of Culver Road that he was contemplating filing a Chapter 13 case was not sufficiently misleading as to either his financial condition or ability to pay the Midfirst and Jackson Mortgages in full as assumed by him at the closing to warrant the indebtedness evidenced by the Jackson Mortgage being determined to be



**BK. 97-20967**  
**AP. 99-2287**

nondischargeable under Section 523(a)(2)(A); (10) any misrepresentation that Young may have made to Kroll post-petition that he was paying the Midfirst Mortgage was not a false representation that resulted in Young obtaining money, property, services or credit from Kroll or Jackson within the meaning of Section 523(a)(2)(A); (11) any statement that Young may have made in connection with the closing of Culver Road that he intended to refinance the Mortgage, whether through an FHA Streamliner Program or otherwise, was not a materially false representation in connection with the transaction within the meaning of Section 523(a)(2)(A); and (12) Culver Road was a troubled property that Kroll and Jackson hoped that Young could operate it in a manner which would result in the repayment of the Midfirst Mortgage and possibly the Jackson Mortgage, in whole or in part, and in closing on Culver Road they relied upon their second mortgage position and the representations of the Broker that Young could effectively manage the property to those ends.

### **CONCLUSION**

Young's obligation on the Jackson Mortgage was discharged by the Discharge Order entered by the Bankruptcy Court on October 1, 1999.

**IT IS SO ORDERED.**

\_\_\_\_\_/s/\_\_\_\_\_  
**HON. JOHN C. NINFO, II**  
**CHIEF U.S. BANKRUPTCY JUDGE**

**Dated: September 1, 2000**