

UNITED STATES BANKRUPTCY COURT  
MIDDLE DISTRICT OF NORTH CAROLINA  
GREENSBORO DIVISION

IN RE:

Larry Charles Gates and  
Terry I. Gates,

Debtors.

High Point Bank  
and Trust Company,

Plaintiff,

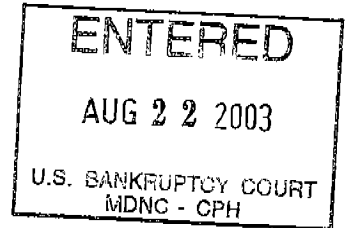
v.

Larry Charles Gates and  
Terry I. Gates,

Defendants.

Case No. 01-12392C-7G

Adversary No. 02-2004



MEMORANDUM OPINION

This adversary proceeding came before the court on March 4, 2003, for trial. Christopher C. Finan appeared on behalf of the plaintiff and J. Brooks Reitzel, Jr. appeared on behalf of the defendants (hereinafter referred to as "Mr. Gates" and "Mrs. Gates" or collectively as "debtors" or "defendants"). The parties submitted stipulations of fact, exhibits and testimony as the evidence to be considered along with the pleadings. Having considered these submissions, the court makes the following findings and conclusions pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure.

#### NATURE OF PROCEEDING

This is a dischargeability proceeding brought under § 727(a)(2), (4)(A) and (5) of the Bankruptcy Code based upon an alleged failure by the defendants to file accurate schedules and statement of financial affairs, intent to defraud creditors and failure to explain the loss of assets. Plaintiff High Point Bank & Trust Company ("Bank") instituted this adversary proceeding on February 11, 2002. The Bank alleged that defendants were not entitled to a discharge of their debts because they knowingly filed schedules that failed to disclose certain financial transactions and certain property owned by the debtors. Based upon such conduct, the Bank alleged that the defendants should be denied a discharge pursuant to § 727(a)(4)(A) for knowingly and fraudulently making a false oath or account. The Bank also objected to the debtors' discharge pursuant to § 727(a)(2) based upon the debtors allegedly having transferred property after filing their petition with an intent to defraud creditors. Finally, the Bank alleged that the defendants should be denied a discharge pursuant to § 727(a)(5) because defendants have failed to explain the disappearance of assets.

#### FACTS

In June of 2000, debtors provided the Bank with a financial statement in connection with their personal guarantee on a loan for B&D Painting Carolina, Inc. ("B&D Painting"). In their financial

statement, debtors showed a total net worth of \$200,536.00 which included personal property valued at \$190,000.00. When debtors filed their Chapter 7 case one year later on August 28, 2001, they listed personal property totaling only \$44,751.84.

Prior to filing their Chapter 7 petition, both debtors were involved in the operations and business of B&D Painting. Mr. Gates was the owner of 100% of the stock of B&D Painting and was an officer and employee of the company. Mrs. Gates also was an officer and employee of B&D Painting, functioning as its bookkeeper and office manager. The debtors continued to work at B&D Painting until it closed in July 2001 and filed a Chapter 7 bankruptcy case. The debtors then went to work for TD Custom Painting, a company that was started in July of 2001 by their son. After closing B&D Painting, debtors had B&D Painting sell TD Custom Painting the painting equipment formerly utilized in B&D Painting for \$5,000.00. This transfer was not disclosed in the original petition for B&D Painting which was filed by the debtors on behalf of B&D Painting. The transfer was later disclosed in an amendment to the statement of financial affairs filed on November 29, 2001. TD Custom Painting performs the same type of work as was performed by B&D Painting using the same equipment as B&D Painting used when it was in business. In effect, TD Custom Painting simply took over the business and customers of B&D Painting as soon as B&D ceased operations.

Mrs. Gates testified that while debtors' Schedule B indicated no cash on hand, the debtors had some cash when they filed. Although debtors' Schedule B indicated "See Exemption Form attached" for a listing of bank accounts, no bank accounts were listed on the exemption form. Mrs. Gates admitted that debtors did in fact have a personal bank account at the time of filing and that there was probably some money in the account although she was not sure how much. Mrs. Gates also admitted that debtors failed to include in their schedules a Kodak camera, computer, wedding rings, watches and costume jewelry which they owned at the time of their Chapter 7 filing. Mrs. Gates further admitted that debtors failed to list life insurance policies owned by them, including one policy with a cash surrender value of approximately \$6,000.00, and debtors also did not disclose in their schedules a 1998 Pontiac Firebird automobile registered in Mr. Gates' name and a farm tractor worth approximately \$2,000.00. Additionally, debtors failed to list in their schedules Mr. Gates' interest in B&D Painting even though he owned 100% of B&D Painting and, on question nineteen of Schedule B, the "none" box was marked for interests in life insurance policies even though Mrs. Gates was the beneficiary of several policies of life insurance insuring Mr. Gates.

At the time of filing, debtors still owed B&D Painting approximately \$75,000.00 on a personal loan from B&D Painting. This debt was not listed in the schedules. Debtors also did not

list indebtedness owed on the 1998 Firebird by Mr. Gates based upon his being a co-signor on the promissory note issued to the Bank when the vehicle was purchased.

Debtors marked the "none" box, on the Statement of Financial Affairs, to question number three which requested a list of all payments over \$600.00 made by the debtors in the 90 days preceding the petition. However, debtors admitted during their testimony that at least six payments over \$600.00 were made during that period of time, including a check made out to "Cash" for \$2,000.00 which they issued. The debtors were unable to provide any information regarding the disposition of this \$2,000.00 payment.

The schedules filed by the debtors listed a Circuit City debt of \$642.00. Although debtors did not list any gifts in their response to the question on the Statement of Financial Affairs regarding gifts in the year prior to the filing of their petition, Mrs. Gates admitted that the \$642.00 Circuit City indebtedness was incurred to purchase gifts.

Debtors also acknowledged filling out and signing the Chapter 7 petition, schedules and statement of financial affairs filed for B&D Painting in B&D's bankruptcy case. In these filings, debtors failed to disclose the debt owed by them to B&D Painting. They also did not disclose that accounts receivable were owned by B&D Painting when it filed for bankruptcy. Debtors also failed to disclose in the B&D filings that more than 30 payments over \$600.00

were made by B&D Painting within the 90 days preceding filing and that at least eight checks payable to "cash" and totaling \$12,784.73 were issued by B&D Painting in the three months prior to filing which the debtors could not or would not explain. B&D Painting also issued checks payable to Mr. Gates totaling at least \$8,510.92 in the month preceding the filing which were not disclosed in the B&D filing or in debtors' bankruptcy filing.

The Bank argues that these omissions and inaccuracies are sufficient to establish that debtors knowingly and fraudulently made a false oath when they executed and filed their schedules and the schedules filed on behalf of B&D Painting. The debtors contend that the omissions were not intentional and were either a simple oversight or that the property and transactions were not listed because they were deemed of insignificant value.

#### DISCUSSION

##### 1. Denial of Discharge Pursuant to § 727(a)(4)(A)

In order for the court to deny debtors a discharge pursuant to § 727(a)(4)(A)<sup>1</sup>, the plaintiff must first establish that the debtors made a false oath or account. The burden of establishing that debtors made a false oath or account may be satisfied by a showing that debtors failed to disclose assets or transactions in their schedules and statement of financial affairs. See In re

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<sup>1</sup> Section 727(a)(4)(A) of the Bankruptcy Code states that a "court shall grant the debtor a discharge, unless the debtor knowingly and fraudulently . . . made a false oath or account."

Downey, 242 B.R. 5 (Bankr. D. Idaho 1999); In re Farouki, 14 F.3d 244 (4th Cir. 1994); In re Krich, 97 B.R. 919 (Bankr. N.D. Ill. 1988); In re Weldon, 184 B.R. 710 (Bankr. D. S.C. 1995); In re Baldridge, 256 B.R. 284 (Bankr. E.D. Ark. 2000). "The recalcitrant debtor may not escape a section 727(a)(4)(A) denial of discharge by asserting that the admittedly omitted or falsely stated information concerned a worthless relationship or holding; such a defense is specious." In re Downey, 242 B.R. at 14 (quoting In re Chalik, 748 F.2d 616, 618 (11th Cir. 1984)). "A 'false oath' sufficient to merit a denial of discharge includes a misrepresentation or an omission in the debtor's bankruptcy Schedules or Statement of Financial Affairs." In re McLaren, 236 B.R. 882, 894 (Bankr. D. N.D. 1999) (citing In re Beaubouef, 966 F.2d 174, 178 (5th Cir. 1992)). The requisite intent to deceive exists where a debtor, in the first instance of filing a petition, schedules or statement of financial affairs, makes statements therein, exceeding honest mistake, which are inconsistent or incompatible with her own knowledge and information. Id. at 895.

The exhibits as well as the testimony of the debtors establish that the debtors did not disclose their interests in various assets and financial transactions that occurred in the months preceding debtors' bankruptcy filing. Plaintiff therefore has met the burden of proving that the debtors made a false oath or account when they signed the schedules and statement of financial affairs and

represented that their schedules and statement of financial affairs were accurate. Moreover, such failure to disclose was inconsistent with debtors' own knowledge and information and, given the number and nature of the property interests and financial transactions that were not disclosed, cannot be passed off as an honest mistake or innocent oversight but, instead, establish an intent to deceive.

It follows that the Gates are not entitled to a discharge of their debts because they knowingly made a false oath by signing schedules and statements of financial affairs which they knew did not accurately reflect their financial transactions or their interests in property owned at the time the bankruptcy petition was filed and did so with an intent to deceive.

2. Denial of Discharge Pursuant to § 727(a) (2)

Pursuant to 11 U.S.C. § 727(a) (2) the court may deny a debtor a discharge if:

the debtor with, intent to hinder, delay or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be transferred, removed destroyed, mutilated or concealed -

(A) property of the debtor, within one year before the date of the filing of the petition; or

(B) property of the estate, after the date of filing of the petition.

In order to prevail under this provision, the plaintiff must establish an intent to hinder, delay or defraud creditors or the estate. A simple showing of a transfer of property is not



sufficient. See In re Nazarian, 18 B.R. 143, 150 (Bankr. D. Md. 1982). However, intent to defraud can be inferred from circumstantial evidence including conduct by the debtor that is replete with one or more badges of fraud, such as concealed transfers without consideration to insiders. See In re Hooper, 247 B.R. 210 (Bankr. D. S.C. 2001).

The exhibits and testimony in this case established that the debtors knew that the male debtor was a co-signor on the promissory note on the Firebird. The debtors also knew that his name was on the title to the Firebird. Nevertheless, no mention of the Firebird or the indebtedness appeared in the debtors' schedules or statement of financial affairs. After filing the petition in this case, debtor transferred the vehicle to his son for no consideration and without making any disclosure of such transfer. Once this case was filed, the male debtor's interest in the vehicle became property of the estate pursuant to § 541 of the Bankruptcy Code and when he transferred the Firebird to his son he transferred a property interest of the bankruptcy estate. These circumstances are sufficient to carry the burden of establishing that the male debtor transferred property of the estate after the filing of the petition and that he did so with intent to hinder, delay or defraud creditors. Thus, § 727(a)(2) provides an additional ground for

denying the discharge of Mr. Gates.<sup>2</sup>

In accordance with the foregoing findings and conclusions, a judgment will be entered contemporaneously herewith denying the debtors a discharge pursuant to § 727(a)(2) and § 727(a)(4)(A) of the Bankruptcy Code.

This 22nd day of August, 2003.

~~William L. Stocks~~

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WILLIAM L. STOCKS  
United States Bankruptcy Judge

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<sup>2</sup>The Bank also contends that the debtors should be denied a discharge pursuant to 11 U.S.C. § 727(a)(5) which provides that a debtor may be denied a discharge if they have "failed to explain satisfactorily . . . any loss of assets." The Bank argues that the debtors have not satisfactorily explained how their personal property which was listed at \$195,000.00 on a financial statement provided to the Bank in June 2000 was worth only \$44,751.84 on the petition date in August of 2001. The Bank further contends that the debtors have not explained what happened to the \$8,510.92 paid to the male debtor from B&D Painting in the month prior to filing nor accounted for the \$12,784.73 paid out by B&D Painting by checks made payable to cash shortly before the B&D filing. Since the Bank has established that both debtors should be denied a discharge pursuant to § 727(a)(4)(A) and that Mr. Gates also is barred from receiving a discharge pursuant to § 727(a)(2), the court need not address these contentions.

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ENTERED

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U.S. BANKRUPTCY COURT  
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JUDGMENT

In accordance with the memorandum opinion filed contemporaneously herewith, the relief sought by the plaintiff is granted and Larry Charles Gates and Terry I. Gates are denied a discharge pursuant to §§ 727(a)(2) and 727(a)(4)(A) of the Bankruptcy Code.

This 22nd day of August, 2003.

William L. Stocks

WILLIAM L. STOCKS  
United States Bankruptcy Judge