

The court incorporates by reference in this paragraph and adopts as the findings and analysis of this court the document set forth below. This document has been entered electronically in the record of the United States Bankruptcy Court for the Northern District of Ohio.



Dated: September 10 2007

Mary Ann Whipple  
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF OHIO  
WESTERN DIVISION

In Re:	)	Case No.: 05-74843
	)	
John A. DeMuth,	)	Chapter 7
	)	
Debtor.	)	Adv. Pro. No. 06-3119
	)	
John Moon and	)	Hon. Mary Ann Whipple
Susan Moon,	)	
	)	
Plaintiffs,	)	
	)	
v.	)	
	)	
John A. DeMuth,	)	
	)	
Defendant.	)	

**MEMORANDUM OF DECISION**

This adversary proceeding is before the court for decision after trial on a complaint filed by Plaintiffs John and Susan Moon (collectively, “the Moons” or “Plaintiffs”) to determine dischargeability of a debt owed to them by Defendant John DeMuth in connection with a settlement agreement entered into by the parties in order to resolve a legal malpractice action brought by Plaintiffs against Defendant. Plaintiffs

allege that the debt should be excepted from discharge under 11 U.S.C. § 523(a)(2)(A).<sup>1</sup>

The court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. §1334(b) and the general order of reference entered in this district. Proceedings to determine dischargeability are core proceedings that the court may hear and decide. 28 U.S.C. § 157(b)(1) and (b)(2)(I). This Memorandum of Decision constitutes the court's findings of fact and conclusions of law under Fed. R. Civ. P. 52, made applicable to this adversary proceeding by Fed. R. Bankr. P. 7052. Regardless of whether specifically referred to in this Memorandum of Decision, the court has examined the submitted materials, weighed the credibility of the witnesses, considered all of the evidence, and reviewed the entire record of the case. Based upon that review, and for the reasons discussed below, the court finds that Defendant is entitled to judgment in his favor on the complaint.

### **FINDINGS OF FACT**

Defendant is an attorney licensed to practice law in the state of Ohio. He represented Plaintiffs in a personal injury action commenced in the Court of Common Pleas in Franklin County, Ohio, claiming damages in the amount of \$600,000. Judgment was entered against Plaintiffs in that action after Defendant failed to oppose a summary judgment motion within the time required by the court's local rules. Thereafter, the Defendants filed a legal malpractice action against Defendant in the Court of Common Pleas in Paulding County, Ohio. Pursuant to a joint request of the parties, that case was referred for mediation. Mediation took place on March 4, 2002. On April 8, 2002, the mediation coordinator filed a report stating that the parties had reached a full and complete agreement in the matter and that "[t]he paperwork resulting from this agreement and the closing of this file will take approximately 120 days to complete. . . ." [Def. Ex. E, unnumbered p. 62]. The parties' agreement was reduced to writing in May 2002. In exchange for Plaintiffs dismissing the malpractice lawsuit with prejudice, Defendant agreed to pay Plaintiffs the sum of \$250,000, with an initial payment of at least \$25,000 and monthly payments thereafter of \$1,000. The agreement does not provide when Defendant was to make the initial \$25,000 payment. Defendant testified, however, that he understood it was to be paid as soon as possible. The agreement also provided terms for naming Plaintiffs as beneficiaries of life insurance policies "in the event that [Defendant] obtains additional life insurance." [Def. Ex. A, ¶ 2]. John Moon testified that it was his understanding that Defendant was to try

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<sup>1</sup> Plaintiffs' complaint also alleges that the debt is nondischargeable under 11 U.S.C. § 523(a)(4). However, the court granted Defendant partial summary judgment on that claim. [Doc. #27].

to obtain additional insurance but, because of a medical condition, was not sure that he would be successful in doing so. Defendant never obtained additional insurance and the record is silent as to whether he ever made any attempt to do so. Finally, Defendant agreed that the debt owed by him to Plaintiffs “shall be secured by a mortgage covering all real estate presently owned by [Defendant] and all future real estate which he may acquire.” [*Id.*, ¶ 3].

At the time the parties entered into the settlement agreement, Defendant was in the process of refinancing his home in order to obtain the \$25,000 he intended to use to make the initial payment under the agreement. However, before the agreement was reduced to writing in May 2002 [Def. Ex. E, unnumbered p.67 (Memorandum of Understanding of Parties’ Agreement, Ex. A to Plaintiffs’ Motion to Enforce Settlement and Request for Hearing)], Defendant was approached by his former father-in-law regarding purchasing twenty-two acres of land owned by his trust. The twenty-two acres is situated contiguous to a one-acre parcel of land owned by Defendant on which his home is located and which was previously a part of twenty-three acres comprised of Defendant’s one acre and his father-in-law’s twenty-two acres. Defendant testified that this real estate is rural property and that, at the time the one-acre parcel was conveyed to him, the legal description was never confirmed by survey and the parcel was not platted. Rather, Defendant and the previous owner used a measuring tape to map one acre of land out of the twenty-three acres. Defendant also testified that a septic tank located on his property drains into a tile field across the twenty-two acres. Although never a problem between Defendant and his former father-in-law, Defendant had no easement to drain his septic tank across the twenty-two acres. Defendant believed it important to purchase the twenty-two acres in order to avoid potential issues regarding the legal description and lack of an easement in the event the property was sold to a stranger. He further testified that he believed the purchase of the twenty-two acres would enhance the value of his one-acre parcel. The court credits Defendant’s testimony that it was for these reasons that he used the money obtained from refinancing his home to purchase the twenty-two acres instead of immediately making the initial \$25,000 payment to Plaintiffs.

The purchase of the twenty-two acres was closed on July 31, 2002, which is the date upon which the deed was executed. Defendant then sought refinancing of the twenty-two acres in order to satisfy his obligation to make the \$25,000 initial payment to the Moons. Defendant obtained the refinancing in December 2002 and used the proceeds to pay Plaintiffs both the initial payment and the first \$1,000 monthly payment. At this time, the deed to the twenty-two acres was recorded. [Plf. Ex. 8].

Defendant did not grant Plaintiffs a mortgage in the twenty-two acres that he purchased. Nor did he grant Plaintiffs a mortgage on any other real property in which he had an interest, including his home and a commercial building. He testified that had he granted Plaintiffs a mortgage in the twenty-two acres at the time of the purchase, he would not have been able to obtain the financing that allowed him to make the initial payment to Plaintiffs.

In the meantime, on October 11, 2002, Plaintiffs had filed in the state court a motion to enforce the parties' settlement agreement. The motion was set for hearing on December 6, 2002. However, Defendant testified that when the court inquired as to whether the hearing should proceed, he informed the court that a hearing was not necessary and that Plaintiffs were entitled to judgment in accordance with the judgment entry that had been prepared and submitted by Plaintiffs' counsel. The judgment entry mirrored the provisions of the settlement agreement with one exception. It did not include the provision that the debt owed by Defendant to Plaintiffs be secured by a mortgage covering all real estate owned by Defendant. Defendant testified that he had discussed this provision with Plaintiffs' counsel at that time and that the mortgage provision was not included in the judgment since Defendant's debt to Plaintiffs could be secured by a judgment lien. The judgment, for some unexplained reason, was not actually entered until November 12, 2003, at which time the malpractice action was dismissed with prejudice. Defendant never executed a mortgage in favor of Plaintiffs, and neither Plaintiffs nor their counsel ever requested that he do so after the motion to enforce the settlement was filed. A certificate of judgment, however, was never filed. *See* Ohio Rev. Code § 2329.02.

On October 27, 2003, Defendant and his wife executed a deed to themselves that included the legal description of the entire twenty-three acres that they now owned and Defendant's business property on which his law office was located. Defendant did not do a title search at that time.

After making the initial \$25,000 payment and the first \$1,000 monthly payment, Defendant continued to make monthly payments of \$1,000 during every month thereafter, for a total of thirty-four months, until October 2005 when, aware that the bankruptcy law was changing, he filed his bankruptcy petition on the eve of the effective date of most of the amendments of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. In February 2005, Defendant had taken the bench in the Paulding County, Ohio Probate/Juvenile Court, which resulted in a decrease in his monthly income. Defendant testified that during his first six to eight months on the bench, he was still collecting income from the accounts receivable of his law practice and was, therefore, able to and did continue making the \$1,000

monthly payments to Plaintiffs. However, realizing that his income would no longer permit him to do so, he sought advice from bankruptcy counsel. Defendant testified that he researched the Paulding County records at that time and only then learned that a judgment lien in favor of Plaintiffs had never attached to his property.

### LAW AND ANALYSIS

Plaintiffs seek a determination that the debt owed to them by Defendant is nondischargeable under 11 U.S.C. § 523(a)(2)(A). A creditor must prove exceptions to dischargeability for individual debts under § 523(a), including the exception for fraud, by a preponderance of the evidence. *Grogan v. Garner*, 498 U.S. 279, 291(1991). Exceptions to discharge are to be strictly construed against the creditor and liberally in favor of the debtor. *Rembert v. AT&T Universal Card Servs. (In re Rembert)*, 141 F.3d 277, 281 (6th Cir. 1998).

Section 523(a)(2)(A) excepts from discharge a debt “for money, property, services, or an extension, renewal, or refinancing 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. . . .” In order to except a debt from discharge under this section due to false pretense or false representation, a plaintiff must prove the following elements by a preponderance of the evidence: (1) the debtor obtained money, property, services or credit through a material misrepresentation, either express or implied, that, at the time, the debtor knew was false or made with gross recklessness as to its truth; (2) the debtor intended to deceive the creditor; (3) the creditor justifiably relied on the false representation; and (4) the creditor’s reliance was the proximate cause of loss. *Rembert*, 141 F.3d at 280-81. A debtor’s intent to defraud a creditor is measured by a subjective standard and must be ascertained by the totality of the circumstances of the case at hand. *Id.* at 281-82. “If there is room for an inference of honest intent, the question of nondischargeability must be resolved in favor of the debtor.” *ITT Fin’l Servs. v. Szczepanski (In re Szczepanski)*, 139 B.R. 842, 844 (Bankr. N.D. Ohio 1991).

For purposes of § 523(a)(2)(A), “false representations and false pretenses encompass statements that falsely purport to depict current or past facts.” *Peoples Sec. Fin. Co., Inc. v. Todd (In re Todd)*, 34 B.R. 633, 635 (Bankr. W.D. Ky. 1983). “‘False pretense’ involves implied misrepresentation or conduct intended to create and foster a false impression, as distinguished from a ‘false representation’ which is an express misrepresentation.” *Ozburn v. Moore (In re Moore)*, 277 B.R. 141, 148 (Bankr. M.D. Ga. 2002)(quoting *Sears Roebuck & Co. v. Faulk (In re Faulk)*, 69 B.R. 743, 750 (Bankr. N.D. Ind. 1986)).

In addition, § 523(a)(2)(A) also addresses “actual fraud” as a concept broader than misrepresentation. See *McClellan v. Cantrell*, 217 F.3d 890 (7<sup>th</sup> Cir. 2000); *Mellon Bank, N.A. v. Vitanovich (In re Vitanovich)*, 259 B.R. 873 (B.A.P. 6<sup>th</sup> Cir. 2001). “Actual fraud has been defined as intentional fraud, consisting in deception intentionally practiced to induce another to part with property or to surrender some legal right, and which accomplishes the end designed. It requires intent to deceive or defraud.” *Vitanovich*, 259 B.R. at 877 (quoting *Gerad v. Cole (In re Cole)*, 164 B.R. 951, 953 (Bankr. N.D. Ohio 1993)). A debtor’s intent to defraud a creditor under § 523(a)(2)(A) is measured by a subjective standard and must be ascertained by the totality of the circumstances of the case at hand. *Id.*; *Rembert*, 141 F.3d at 281-82. A finding of fraudulent intent may be made on the basis of circumstantial evidence or from the debtor’s “course of conduct,” as direct proof of intent will rarely be available. *Hamo v. Wilson (In re Hamo)*, 233 B.R. 718, 724 (B.A.P. 6<sup>th</sup> Cir. 1999).

In this case, Defendant’s negotiation of the agreement to settle Plaintiffs’ malpractice action resulted in a benefit received by him, that is, he received an enforceable contract right to require Plaintiffs to dismiss the malpractice lawsuit against him with prejudice and the right to satisfy a debt owed to Plaintiffs over time. *Cf. Brady v. McAllister (In re Brady)*, 101 F.3d 1165, 1172 (6<sup>th</sup> Cir. 1996) (assuming that a plaintiff proceeding under § 523(a)(2)(A) must show “that the debtor directly or indirectly obtained some tangible or intangible financial benefit as a result of his misrepresentation”). Plaintiffs contend that he received such rights through a material misrepresentation.<sup>2</sup> Specifically, Plaintiffs argue that, from its inception, Defendant did not intend to perform under the terms of their settlement agreement and that such intent is demonstrated by Defendant’s post-agreement conduct. While a mere breach of a promise to pay will not support a finding of fraud, “any debtor who does not intend to perform a contract from its inception has knowingly made a false representation.” *Stifter v. Orsine (In re Orsine)*, 254 B.R. 184, 188 (Bankr. N.D. Ohio 2000).

It is true that Defendant did not make the initial \$25,000 payment until December 2002, after Plaintiffs had filed their motion to enforce the settlement agreement, and never granted Plaintiffs a mortgage in property owned by him as required under the settlement agreement. However, the court finds

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<sup>2</sup> On summary judgment, Plaintiffs argued that the debt was obtained through misrepresentations at two points in time as the parties entered into two separate contracts – one, for Defendant to represent Plaintiffs in the personal injury action and the other to settle the malpractice action. The court granted Defendant partial summary judgment as to Plaintiffs’ claim under § 523(a)(2)(A) with respect to his engagement as Plaintiffs’ attorney in their personal injury action.

Defendant's testimony explaining the delay to be credible and does not find that his post-agreement conduct demonstrates that he never intended to perform under the agreement. The twenty-two acre deal did not arise until after the parties had negotiated the settlement agreement. Although Defendant clearly acted in his own self-interest in using funds from the refinancing of his home to purchase the twenty-two acres, he did so still intending to carry out the provisions of the agreement. After the purchase, he applied for refinancing of the twenty-two acres in order to obtain the \$25,000 initial payment. He did not receive the refinancing funds until December 2002, at which time he paid Plaintiffs both their initial payment and the first monthly payment as required under the settlement agreement. Although this occurred after Plaintiffs filed their motion to enforce the settlement agreement, the court credits Defendant's testimony that he began the refinancing process immediately after the twenty-two acre purchase. The court finds that the timing of the payments were the result of the refinancing timetable, not just because the motion to enforce had been filed.

The court also credits Defendant's testimony regarding his failure to grant Plaintiffs a mortgage on the twenty-two acres at the time he purchased the land. Had he done so, he would not have been able to obtain financing in order to pay the \$25,000 initial payment. By the time Defendant received the funds from refinancing in December 2002, he believed he was no longer required to provide a mortgage to Plaintiffs. The judgment entered on Plaintiffs' motion to enforce the settlement agreement did not include the mortgage provision and, in effect, modified the settlement agreement by eliminating that requirement. The court credits Defendant's un rebutted testimony regarding a discussion with Plaintiffs' counsel at the time of the hearing on the motion that the mortgage provision was not included in the judgment entry because Defendant's debt would be secured by a judgment lien. Defendant's testimony is buttressed by the fact that Plaintiffs' counsel prepared the judgment entry and, after entry of judgment, Defendant did not execute a mortgage and neither Plaintiffs nor their counsel ever asked Defendant to do so. Under Ohio law, a judgment lien on real property is effected by filing a certificate of judgment in the common pleas court. Ohio Rev. Code § 2329.02. The filing of a certificate of judgment was within the sole control of Plaintiffs, as "[s]uch certificate shall be made by the clerk of the court in which the judgment was entered, under the seal of said court, upon the order of any person in whose favor such judgment was rendered..." *Id.*

The court also credits Defendant's testimony that he assumed the judgment lien had in fact been filed at the time he and his wife executed the deed to themselves in October 2003 that included the legal description for the entire 23 acres that they then owned. He had not refinanced or sold any property since December 2002 and there had been no reason for him to do a title search that would have confirmed the attachment of a judgment lien with respect to any property owned by him. While no certificate of judgment was actually ever filed, that was not the result of any action or omission to act by Defendant.

Finally, the court does not find Defendant's failure to obtain additional life insurance naming Plaintiffs as beneficiaries to be evidence of an intentional misrepresentation. The settlement agreement did not expressly require Defendant to obtain additional insurance, providing only that Plaintiffs were to be named as beneficiaries "[i]n the event" additional insurance is obtained. [Def. Ex. A, ¶ 2]. To the extent that the parties' agreement required Defendant to at least attempt to obtain additional insurance, the record is silent as whether such attempt was ever made.

### **CONCLUSION**

In light of the foregoing, the court finds that Plaintiffs have not met their burden of proving an intentional misrepresentation, either express or implied, or that Defendant's conduct demonstrates actual fraud. Defendant is, therefore, entitled to judgment on Plaintiffs' claim brought under 11 U.S.C. § 523(a)(2)(A) with respect to the settlement agreement. A separate judgment in accordance with this Memorandum of Decision and the Memorandum of Decision and Order Re Cross Motions for Summary Judgment will be entered by the court.