Creditors' Rights and Bankruptcy Practice Group

GOODSILL ALERT

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SUPREME COURT ADVISES THAT A FALSE STATEMENT ABOUT A SINGLE ASSET CAN RENDER A DEBT NONDISCHARGEABLE

In the case of *Lamar, Archer & Cofrin, LLP, v. Appling, 16-1215 (June 4, 2018)*, the U.S. Supreme Court held that a materially false statement about a single asset can be a "statement respecting the debtor's financial condition," but must be in writing in order for the debt related to the asset to be nondischargeable under 11 U.S.C. §523(a)(2)(B).

BACKGROUND FACTS

The Bankruptcy Code prohibits debtors from discharging debts for money, property, services, or credit obtained by "false pretenses, a false representation, or actual fraud," under 11 U. S. C. §523(a)(2)(A), or, if made in writing, by a materially false "statement . . . respecting the debtor's . . . financial condition," 11 U.S.C. §523(a)(2)(B). Id. at 1.

The question presented to the Supreme Court was whether debtor's false statement about a single asset constitutes a "statement respecting the debtor's financial condition" under Section 523(a)(2)(B) or whether the statement must be about the debtor's overall financial status. Id. The Court explained that "the statutory language makes plain that a statement about a single asset *can* be a "statement respecting the debtor's financial condition," however, if that false statement is not in writing, the associated debt may be discharged. Id.

R. Scott Appling ("Appling") hired Lamar, Archer & Cofrin, LLP ("Lamar"), a law firm, to represent him in a business litigation. Id. at 2. Appling fell behind on his legal bills, and by March 2005, he owed Lamar more than $60,000. Id. at 2.

Lamar informed Appling that if he did not pay the outstanding amount, the firm would withdraw from representation and place a lien on its work product until the bill was paid. Id. Appling told his attorneys that he was expecting a tax refund of

"approximately $100,000," which was enough to cover his owed and future legal fees. Id. Lamar relied on Appling's statement and continued to represent him without initiating collection of the overdue amount. Id. When Appling and his wife filed their tax return, however, the refund they requested was of just $60,718, and they ultimately received $59,851 in October 2005. Id.

Rather than paying Lamar, the Applings spent the money on their business. Id. Appling and his attorneys met again in November 2005, and **Appling falsely told them that he had not yet received the refund**. Id. **Lamar relied on that false statement** and agreed to complete the pending litigation and delay collection of the outstanding fees. Id. In March 2006, Lamar sent Appling its final invoice. Id. Five years later, Appling still had not paid, so Lamar filed suit in Georgia state court and obtained a judgment for $104,179.60. Id. at 2-3. Shortly thereafter, Appling and his wife filed for Chapter 7 bankruptcy. Id. at 3.

Lamar filed an adversary proceeding against Appling arguing that, because Appling made fraudulent statements about his tax refund at the March and November 2005 meetings, his debt to Lamar was nondischargeable pursuant to 11 U.S.C. § 523(a)(2)(A). Appling moved to dismiss the adversary complaint, contending that his alleged misrepresentations were "statement[s] . . . respecting [his] financial condition" and were therefore governed by §523(a)(2)(B), such that Lamar could not block discharge of the debt because the statements were not "in writing" as required for nondischargeability under that provision. Id.

The Bankruptcy Court held that a statement regarding a single asset is not a "statement respecting the debtor's financial condition" and denied Appling's motion to dismiss. Id. After a trial, the Bankruptcy Court found that Appling knowingly made two false representations on which Lamar justifiably relied and that Lamar incurred damages as a result and concluded that Appling's debt to Lamar was nondischargeable under §523(a)(2)(A).

The U.S. District Court affirmed the Bankruptcy Court's decision. Id. However, the Court of Appeals for the Eleventh Circuit reversed, holding that "'statement[s] respecting the debtor's . . . financial condition' may include a statement about a single asset." Id. Because Appling's statements about his expected tax refund were not in

writing, the Court of Appeals held that §523(a)(2)(B) did not bar Appling from discharging his debt to Lamar. Id.

The U.S. Supreme Court granted certiorari to resolve a conflict among the circuits as to whether a statement about a single asset constitutes a "statement respecting the debtor's financial condition." Id. at 4.

THE SUPREME COURT'S DECISION

The Supreme Court started its analysis by explaining that, under 11 U.S.C. §523(a)(2), a discharge under Chapter 7, 11, 12, or 13 of the Bankruptcy Code "does not discharge an individual debtor from any debt . . . for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by" fraud. Id.

In particular, the Court explained, subparagraph (A) bars discharge of debts arising from "false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's . . . financial condition" and subparagraph (B), in turn, bars discharge of debts arising from a materially false "statement . . . respecting the debtor's . . . financial condition" if that statement is "in writing." Id. at 4-5.

The Supreme Court explained that "a statement is 'respecting' a debtor's financial condition if it has a direct relation to or impact on the debtor's overall financial status." Id. at 9. Therefore, it continued:

> A single asset has a direct relation to and impact on aggregate financial condition, so a statement about a single asset bears on a debtor's overall financial condition and can help indicate whether a debtor is solvent or insolvent, able to repay a given debt or not. Naturally, then, **a statement about a single asset can be a "statement respecting the debtor's financial condition.**"

Id. (emphasis added).

The Court therefore affirmed the judgment of the Court of Appeals for the Eleventh Circuit allowing the debt to be discharged.

CONCLUSION

In *Lamar, Archer & Cofrin, LLP, v. Appling*, the U.S. Supreme Court explained that a statement about a single asset can constitute a "statement respecting the debtor's financial condition." The consequence of this ruling is that a debtor's false statements to a creditor regarding assets (or perhaps also liabilities) must be in writing in order to be found to be nondischargeable under 11 U.S.C. § 523(a)(2)(B).

The Supreme Court explained that creditors can protect themselves and benefit from the protections of §523(a)(2)(B) "so long as they insist that the representations respecting the debtor's financial condition on which they rely in extending money, property, services, or credit are made **in writing**." The Court explained, "[d]oing so will likely redound to their benefit, as such writings can foster accuracy at the outset of a transaction, reduce the incidence of fraud, and facilitate the more predictable, fair, and efficient resolution of any subsequent dispute."

This opinion re-emphasizes the importance for lenders and creditors to get financial statements and information from a debtor (including information about assets and liabilities) **in writing** so there is no question that any false information provided will give the lender or creditor the ability to seek a determination that the debts owed to it are nondischargeable under 11 U.S.C. § 523(a)(2)(B).

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