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**What Is a Misrepresentation “With Respect to” a Debtor’s  
“Financial Condition” that Must Be in Writing to Render a Claim  
Nondischargeable?**

Marshall E. Tracht

## What Is a Misrepresentation “With Respect to” a Debtor’s “Financial Condition” that Must Be in Writing to Render a Claim Nondischargeable?

### CASE AT A GLANCE

A basic purpose of bankruptcy law is to provide a fresh start to the “honest but unfortunate” debtor. The bankruptcy discharge is therefore not generally available for debts incurred by “false pretenses, a false representation, or actual fraud.” However, if the false statement alleged by the creditor is one “respecting the debtor’s or an insider’s financial condition,” it is only nondischargeable if the creditor can show that it was in writing and that the creditor reasonably relied on it. The question in this case is whether a statement by the debtor regarding a single asset, rather than its overall net worth or solvency, is a statement respecting the debtor’s financial condition and, thus, subject to this higher standard for nondischargeability.

### *Lamar, Archer, & Cofrin v. Appling* Docket No. 16-1215

**Argument Date: April 17, 2018**  
**From: The Eleventh Circuit**

by Marshall Tracht  
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### INTRODUCTION

Bankruptcy law permits an individual to discharge many but not all debts so that a person can recover from misfortune. However, debtors can be denied discharge altogether on account of some types of misconduct, such as hiding assets from the bankruptcy court or carrying specific debts based on various public policies. For example, child support payments, many tax debts, and debts arising from malicious torts are not dischargeable. This case concerns an exception from discharge for debts arising from “false pretenses, a false representation, or actual fraud.” Regardless of whether the false statements are oral or written, such debts are generally not dischargeable provided the creditor justifiably relied on them. Some unscrupulous creditors developed the practice of having debtors provide credit information on forms making it difficult to be complete and accurate, specifically to make the debts nondischargeable on the claim that they were secured by misrepresentations. Congress therefore tightened the standard for nondischargeability where the creditor is claiming a misstatement with respect to the debtor’s financial condition, requiring not only that the statement be in writing, but that the creditor prove that it reasonably relied on that information. This case addresses the scope of representations covered by this higher standard: whether a statement by the debtor about a particular asset is a statement “with respect to” the debtor’s “financial condition.”

### ISSUE

Does a false statement about a single asset fall within the general standard for nondischargeability of debts arising from false representations or fraud, or is it instead covered by the specific provision for false statements “respecting the debtor’s or an insider’s financial condition,” which imposes additional

requirements on the creditor seeking to have the claim held nondischargeable?

### FACTS

In 2004, R. Scott Appling (respondent) retained Lamar, Archer & Cofrin, LLP (Lamar or petitioner) to represent him in commercial litigation. By 2005, he had paid \$135,000 in fees and owed another \$60,000. Although the testimony is in conflict, the bankruptcy court apparently concluded that, during a meeting in March 2005 to discuss the growing balance, Appling told Lamar that his accountant said he would be able to file amended tax returns and recover a refund of more than \$100,000. Lamar knew that Appling had no other unencumbered assets, but continued to work on the case based on this representation. In a meeting that November, according to Lamar, Appling said that the accountant had made an error on the return and Appling had not yet received the refund. In fact, he had received the refund, of \$59,000, the month before. In early 2006, the litigation settled, and soon thereafter Lamar learned that Appling had already received the tax refund and it was not available to pay the firm’s fees. In 2012, Lamar sued Appling for the unpaid fees, obtaining a judgment for over \$104,000. Appling and his wife then filed for bankruptcy, and Lamar asserted that its claim was not dischargeable because the debt was a result of Appling’s “false pretenses, a false representation, or actual fraud.”

### CASE ANALYSIS

Section 523(a)(2)(A) of the Bankruptcy Code provides that an individual cannot discharge a debt “for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by... false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor’s or an insider’s

financial condition.” If the false statement regards “the debtor’s or an insider’s financial condition,” then Section 523(a)(2)(B) provides that the debt can be discharged, but only if the creditor can show that the statement was in writing, materially false, and made with intent to deceive, and that the creditor reasonably relied on the statement.

The Bankruptcy Court held that Appling’s comments about the tax refund were not statements respecting his financial condition because they did not address his “overall financial condition or net worth” and were therefore not subject to the higher standards of Section 523(a)(2)(B). In other words, these statements justified denying the discharge of his debt to Lamar even though the statements were not in writing. The district court agreed, but the Eleventh Circuit Court of Appeals reversed, holding that a statement about a single asset can be a statement respecting the debtor’s financial condition and thus Section 523(a)(2)(B) applied. The court explained that the statute was “unambiguous” and that while “financial condition” likely refers to net worth, a statement about an asset is one “respecting” financial condition because it is related to or affects the debtor’s net worth. A contrary reading, the court held, would give no meaning to the word “respecting.”

The Eleventh Circuit’s decision was consistent with *Engler v. Van Steinburg*, 744 F.2d 1060 (4<sup>th</sup> Cir. 1984), in which the court held that a debtor’s statement that he owned a property free and clear of liens was a statement respecting his financial condition. However, these decisions are in conflict with *In re Joelson*, 427 F.3d 700 (10<sup>th</sup> Cir. 2005) (holding that statements about specific assets that could serve as collateral for a loan were not statements respecting the debtor’s financial condition because they did not purport to address her “overall financial health”) and *In re Bandi*, 683 F.3d 671 (5<sup>th</sup> Cir. 2012), cert. denied, 568 U.S. 1086 (2013) (holding that representations that the debtor owned certain real estate were not statements respecting the debtor’s financial condition).

Both parties agree that “financial condition,” as used in the statute, refers to the aggregate of the debtor’s assets and liabilities, or the debtor’s overall financial health or net worth. The disagreement arises over the meaning of “respecting...financial condition.” Appling argues that “respecting” is consistently used in law as a broadening term, like “related to.” Thus, he argues, the First Amendment prohibition on any law “respecting the establishment of religion” extends beyond statutes that would actually establish a national religion. In interpreting the Civil Rights Act, Appling notes, the Court has said that “with respect to voting” means having a “direct relation to, or impact on, voting.”

Lamar argues that “respecting” is an ambiguous term that can mean “about” or “concerning” or “regarding” and, in light of the history of the Bankruptcy Code, should not be read expansively. Congress intended to limit Section 523(a)(2)(B) to statements about the debtor’s overall financial health. Statements “respecting” financial condition are more than “statements of financial condition,” which might have been read to be limited to formal financial statements or balance sheets, but should not be read to sweep in every statement about an asset or a debt. The Section covers a statement like “Don’t worry, I am above water,” as it is about the debtor’s overall financial condition, Lamar argues. But

Lamar asserts reading Section 523(a)(2)(B) to cover any statement that can have an effect on net worth ignores Congressional intent in limiting the provision to statements about “financial condition.”

Appling disagrees, noting that while statements about assets or liabilities are statements respecting the debtor’s financial condition, there are still a wide range of misrepresentations that fall outside the limits of Section 523(a)(2)(B). Reported cases include misrepresentations by debtors of their professional qualifications, skills, or experience; the intended use of borrowed funds; and the costs of materials, for example. Thus, the limitation to statements respecting “financial condition” has meaning even if it covers all statements about individual assets.

Moreover, Appling argues, the statute must be read in light of pre-Code law. Under a 1903 statute, the Bankruptcy Act denied discharge to a person who made materially false statements in writing to the creditor. Courts held, however, that false representations to credit rating agencies, like Dun’s, were not “made to” the creditor and thus did not block the debtor’s discharge. In 1926, Congress closed this loophole, barring discharge where a person obtained credit “by making or publishing, or causing to be made or published in any manner whatsoever, a materially false statement in writing respecting his financial condition.” In interpreting this statute, courts held that statements regarding specific assets were covered by the language “respecting his financial condition.” Appling argues that Congress was aware of this interpretation when it adopted the nondischargeability provisions in Section 523.

Lamar’s rebuttal is based on the premise that bankruptcy is intended to provide a discharge to the honest but unfortunate debtor, not to those who commit fraud, and the broad reading given to “respecting his financial condition” under the pre-Code statute worked against those who had committed fraud. Under the current statute, a broad reading makes it *easier* for a person who committed fraud to get a discharge. Thus, he argues, it cannot be assumed that Congress intended the pre-Code cases to govern.

## SIGNIFICANCE

The case presents a direct circuit split on an issue that regularly arises. The National Federation of Independent Business filed an amicus brief arguing that the Eleventh Circuit’s ruling would create a tremendous burden on small businesses that often extend credit based on oral representations and would, under its ruling, often be unable to raise these oral misrepresentations as a basis for nondischargeability. While there might be some truth to this, the number of cases involved is likely modest, particularly given the costs of contesting dischargeability and the fact that the discharge provisions apply only to debts owed by individuals, not those owed by business entities like corporations or LLCs.

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## AMICUS BRIEFS

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In Support of Respondent R. Scott Appling  
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Law Professors Richard Aaron, Laura Bartell, et al. (John Collen,  
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United States (Noel J. Francisco, Solicitor General, 202.514.2217)

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## In This Issue

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### APPOINTMENTS CLAUSE

#### *Lucia v. SEC*

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### BANKRUPTCY

#### *Lamar, Archer, & Cofrin v. Appling*

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### CRIMINAL RESTITUTION

#### *Lagos v. United States*

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### DORMANT COMMERCE CLAUSE

#### *South Dakota v. Wayfair*

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### ELECTION LAW

#### *Abbott v. Perez*

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### FEDERAL SENTENCING GUIDELINES

#### *Chavez-Meza v. United States*

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### IMMIGRATION

#### *Trump v. State of Hawaii*

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### IMMIGRATION LAW

#### *Pereira v. Sessions*

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### INTERNATIONAL CIVIL PROCEDURE

#### *Animal Science Products v. Hebei Welcome Pharmaceutical Co.*

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Courts," 34 *Journal of Maritime Law & Commerce* 97 (2003); and *Transnational Litigation* (Lexis Law 1999). She can be reached at lteitz@rwu.edu or 401.254.4601. Professor Teitz joined in one of the amicus curiae briefs filed in this case, that of the Professors of Conflict of Laws and Civil Procedure (March 1, 2018).

### PATENT LAW

#### *WesternGeco LLC v. ION Geophysical Corporation*

Kean DeCarlo is a Partner with Womble Bond Dickinson (US) LLP. His practice encompasses all areas of IP prosecution and counseling, with particular emphasis on patent and trademark prosecution, licensing, and counseling. Mr. DeCarlo's patent and trademark experience includes both domestic and international patent and trademark prosecution, portfolio and competitor analysis, strategic due diligence guidance, and trade secret and misappropriation guidance, to companies, universities, and investors. Mr. DeCarlo is also an adjunct professor of law in Intellectual Property at Georgia State University College of Law and Mercer University College of Law. He may be reached at 404.962.7536 or by email at kean.decarlo@wbd-us.com.

### TAX LAW

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#### *Washington v. United States*

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2017-18 Wrap-Up

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OF UNITED STATES SUPREME COURT CASES

