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UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF WISCONSIN

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U.S. BANKRUPTCY COURT

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In re:

Case Number:

ROBERT ONEAL BOGSTAD  
ARLENE ROSE ALMA BOGSTAD

EF7-83-00354

Debtor.

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PRODUCTION CREDIT ASSOCIATION  
OF RIVER FALLS,

Plaintiff,

Adversary Number:

v.

83-0153

ROBERT ONEAL BOGSTAD and  
ARLENE ROSE ALMA BOGSTAD,

Defendants.  
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FINDINGS OF FACT, CONCLUSIONS OF LAW  
AND  
ORDER DETERMINING DEBT DISCHARGEABLE

Production Credit Association of River Falls (PCA), by Attorney Peter F. Herrell, having filed a Complaint to Determine Dischargeability of Debt; and Debtors Robert Oneal Bogstad and Arlene R. A. Bogstad, by Attorney Mart W. Swenson, having filed an Answer; and a trial having been held; and the matter being appealed and remanded; and additional evidence being received; and PCA appearing by counsel; and the Debtors appearing in person and by counsel; the Court, being fully advised in the premises, FINDS THAT:

1. On March 9, 1983, Debtors Robert Oneal Bogstad and Arlene R. A. Bogstad filed for relief under Chapter 7 of the Bankruptcy Code.

2. In early September, 1980, the Bogstads and Adam Mock, their daughter's beau, signed a loan application, loan agreement and supplementary loan agreement with PCA; said application and agreements related to a loan of up to \$52,225 by PCA to enable Mock to set up a dairy farming operation on the Bogstad farm (Mock has been discharged in an unrelated Chapter 7 proceeding).

3. Contemporaneous to the signing of said application and agreements the Bogstads signed a "Balance Sheet" of their financial condition.

4. Said Balance Sheet was prepared in the following fashion: In late August, 1980, John Wegmann of PCA, using a blank "Balance Sheet" form, interrogated Mr. Bogstad regarding his family's assets and liabilities. Mr. Wegmann's handwritten Balance Sheet was then converted to a typed Balance Sheet by the PCA office staff. Finally, in early September, 1980, both of the Bogstads came into the PCA office and signed the typed Balance Sheet.

5. The following table reflects the Debtors' claimed and actual financial condition as of September, 1980:

Assets

	<u>Claimed</u>	<u>Actual</u>
Life Insurance	\$ 11,000	\$
Livestock	1,200	1,200
Angus Bull	500	500
Heifer	750	750
4 vehicles	2,650	
3 vehicles		2,000
Machinery & Equipment	6,640	6,640
Farm with 30-cow Barn	100,000	
Farm with 20-cow Barn		60,000
10 Acres of Northern Wisconsin Recreational Land	10,000	3,500
TOTAL ASSETS	<u>132,740</u>	<u>74,590</u>

Liabilities

Mortgage (Royal Credit Union)	12,531	12,531
Northern Investment Company	4,000	4,000
Clarence H. Williams (Brother-in-Law)		10,000
TOTAL LIABILITIES	<u>16,531</u>	<u>26,531</u>
TOTAL EQUITY	116,209	48,059

6. Mr. Bogstad told Mr. Wegmann that he was not sure whether the life insurance was whole life or term insurance. Cf. Pl.Ex.4 (Bogstad Balance Sheet line 2, preprinted "Cash Value Life Insurance", is blank).

7. Mr. Wegmann listed the life insurance as "Life Ins. at Place of Employment (Off. farm)" on line 6 of the Balance Sheet.

8. Mr. Bogstad recognized that he owned three unserviceable vehicles.

9. PCA presented the following evidence of the value of the farm: The 1973 purchase price (\$31,500); the March 1983, Bankruptcy Court (Martin, J.) finding of value in a related proceeding (\$60,000); and the March 1983, Bankruptcy Petition claimed value (\$50,000). In addition, PCA showed that no

improvements had been made to the farm since 1973 and that a small pole barn had collapsed during the time the Bogstads owned the farm.

10. Mr. Bogstad testified that he based his August, 1980, valuation on a real estate advertisement for a similar farm which appeared in a local newspaper at the time of the loan application.

11. Mr. Bogstad knew that his barn had room for only 20 cows, that he purchased the farm for \$31,500 in 1973, that he made no improvements to the farm, that a pole barn on the farm was destroyed and that the farm's value was substantially less than \$100,000.

12. PCA presented the following evidence of the value of the northern Wisconsin acreage: The 1968 purchase price (\$100); the March, 1983, Bankruptcy Court (Martin, J.) finding of value in a related proceeding (\$3,500); and the March, 1983, Bankruptcy Petition claimed value (\$3,500).

13. Mr. Bogstad testified, in effect, that he based his August, 1980, valuation on the price he would set if he were approached by an unsolicited buyer.

14. Mr. Bogstad knew that the recreational land was worth nowhere near \$10,000.

15. In 1962 Mr. Bogstad borrowed approximately \$6,000 from his brother-in-law.

16. Mr. Bogstad has made no payment on said loan and the balance of the brother-in-law loan now exceeds \$10,000.

17. In July, 1982, after PCA started an action against the Bogstads to recover on the debt at bar, Mr. Bogstad gave his brother-in-law a mortgage on the farm property.

18. Mr. Bogstad knew that he owed his brother-in-law in excess of \$10,000.

19. The Bogstads claimed a net worth of \$116,209 and an equity to asset ratio of .875; the Bogstads' actual net worth was \$48,059 and their actual equity to asset ratio was .644. Paragraph 5 supra.

20. PCA would not have made the loan if the Bogstads' net worth was less than \$58,105 or if their equity to asset ratio was less than .6 or .7.

21. PCA actually relied on the Bogstad Balance Sheet to make the loan at bar.

22. Because a man in the PCA office "seemed" to know of the Bogstads' financial condition, PCA required no independent verification of the Bogstad Balance Sheet and made no inquiry of its own.

23. The facts set forth above were established by prior litigation. In re Bogstad, Adv. No. 83-0153 (Bankr.W.D.Wis. Jan. 16, 1984), rev'd and remanded, 84-C-91-S (W.D.Wis. April 9, 1984).

24. At a subsequent hearing, Debtors produced evidence to show that Mr. Bogstad believed the \$10,000 valuation of the recreational land was reasonable.

25. Said evidence relates to Paragraph 14, supra--a fact established by the District Court. Accordingly this Court makes no further findings.

Discussion

26. Under 11 U.S.C. sec. 523:

(a) A discharge . . . does not discharge an individual debtor from any debt--

(2) for obtaining money . . . by--

(B) use of a statement in writing--

(i) that is materially false;

(ii) respecting the debtor's . . . financial condition;

(iii) on which the creditor . . . reasonably relied; and

(iv) that the debtor . . . published with intent to deceive;

27. The party objecting to dischargeability must show all of the elements of proof with clear and convincing evidence. In re Brink, 27 B.R. 377, 378 (Bankr.W.D.Wis. 1983), see In re Kreps, 700 F.2d 372, 376 (7th Cir. 1983).

28. Obtained Money. The Bogstads obtained money from PCA. See 3 L. King, Collier on Bankruptcy para. 523.08[1] (15th Ed. 1984) (the better view is that it is not necessary that the property be procured for the debtor himself).

29. Use of a Published Written Statement of Financial Condition. The Bogstad Balance Sheet was a statement of

financial condition in writing published to Mr. Wegmann and PCA and actually relied upon by them in making the loan at bar.

30. Material Falsehood. PCA has presented clear and convincing evidence that the Bogstad Balance Sheet was false.<sup>1</sup> Paragraph 5 supra. And that the falsehood was material. Paragraphs 19 & 20, see Wolfe v. Tri-State Ins. Co., 407 F.2d 16, 19 (10th Cir. 1969) (under Bankruptcy Act of 1898 section 17(a)(2), 11 U.S.C. sec. 32(c) (repealed): discharge granted where "the bank . . . would have extended such credit regardless of these errors").

31. The discussion set forth above was established by prior litigation. In re Bogstad, Paragraph 23 supra.

32. Reasonable Reliance. Under Section 523(a)(2)(B)(iii), "the creditor must not only have relied on a false statement in writing, the reliance must have been reasonable. This codifies case law construing [section 17(a)(2)]." H.R.Rep. No. 595, 95th Cong., 1st Sess. 364 (1977); S.Rep. No. 989, 95th Cong., 2d Sess. 77-79 (1978). U.S.Code Cong. & Admin. News 1978, pp. 5787, 5864, 6320." In re Kreps, Paragraph 27 supra at 376 (brackets in original).

33. Judge Deitz has identified four situations in which reliance has been held to be unreasonable:

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<sup>1</sup> Because Section 523(a)(2)(B)(iv) is specifically directed toward intent, "false" is used here to mean "untrue". But see 3 L. King, Collier on Bankruptcy para 523.09[2][a] (15th Ed. 1984) ("'false' means more than . . . untrue and imports an intention to deceive").

- (a) the creditor knows that the financial information is not accurate;
- (b) the statement contains obviously inadequate financial information;
- (c) the creditor's investigation of the statement suggests its falsity or incompleteness; and
- (d) the creditor fails to verify information on the statement.

In re Duncan, 35 B.R. 323, 325 (Bankr.W.D.Ky. 1983) (cases collected at footnote 7). See In re Garman, 643 F.2d 1252, 1255-1256 (7th Cir. 1980) (Bankruptcy Act of 1898 section 17(a)(2), 11 U.S.C. sec. 35(a)(2) (repealed), cases collected), cert. denied sub nom. Garman v. Northern Trust Co., 450 U.S. 910 (1981).

34. It is the fourth situation which has been argued in the case at bar. Has PCA presented clear and convincing evidence that it verified the Bogstad Balance Sheet?

35. An atmosphere of mutual trust established during an ongoing relationship may eliminate any need to investigate the veracity of a financial statement which is regular on its face. See In re Garman, Paragraph 33 supra, at 1257 & 1259 (at 1259: discharge denied where the debtor "was a longtime customer of the bank"), In re Kreps, Paragraph 27 supra, at 373 & 376 (at 376: discharge denied where the bank creditor "wished assurance that its long-time customer had sufficient resources").

36. Neither one of the conditions are present in this case: There is no evidence of any prior dealings between PCA and the



Bogstads. And, to a sophisticated agricultural lender, see 12 U.S.C. sec. 2001, 2091 et seq. (production credit associations are a part of the federal farm credit system), with apparent knowledge of the Bogstad operation, Paragraph 22 supra, a financial statement containing a 65% overvaluation of the Bogstads' only farm and principal asset would not be regular on its face.

37. Arguably, the Seventh Circuit decisions in Garman, Paragraph 33 supra, and Kreps, Paragraph 27 supra, preclude judicial inquiry into the sufficiency of creditor investigation of debtor financial statements. However, this is not to say that a creditor may "'assume the position of an ostrich with its head in the sand and ignore facts which were readily available to it'." In re Blatz, 37 B.R. 401, 404-405 (Bankr.E.D.Wis. 1984) (at 405: discharge denied where "the Bank made at least some effort" to investigate); see In re Ardelean, 28 B.R. 299 (N.D.Ill. 1983) (discharge denied where bank investigation followed normal banking practice); cf. In re Eaton, 41 B.R. 800 (Bankr.E.D.Wis. 1984) (discharge granted under Section 523(a)(2)(A) where bank knew that debtor's collateral belonged to others).

38. Here, the only step taken by the PCA lending officer to verify the Debtors' financial statement was a conference with a fellow officer who seemed to know the Bogstad's financial condition but who evidently did not notice that the farm was substantially overvalued. Paragraph 22 supra.

39. This Court is of the opinion that PCA did not "investigate" the veracity of the Bogstad Balance Sheet.

40. Accordingly, PCA's reliance upon the Bogstad Balance Sheet was not reasonable.

41. Intent. In view of the findings of the District Court, Paragraphs 5, 11, 14 & 18 supra, this Court must rule that Mr. Bogstad intentionally published the Bogstad Balance Sheet with intent to deceive PCA. See In re Kreps, Paragraph 27 supra, at 1260-1261 ("'where, as here, a person knowingly or recklessly makes a false representation which the person knows or should know, will induce another to make a loan, intent to deceive may logically be inferred'").

42. However, Ms. Bogstad appears to be an "innocent spouse", see Paragraph 4 supra, and should be free of the taint of her husband's knowing representations. See In re Dee, 6 B.R. 784, 788 (Bankr.W.D.Pa. 1980) (under 11 U.S.C. sec. 727(a)(2): wife's "delegation of financial matters to her husband was not done with 'reckless indifference'"); cf. In re Conti, 42 B.R. 122 (Bankr.E.D.Va. 1984) (under 26 U.S.C. sec. 6013(e)).

#### CONCLUSIONS OF LAW

1. PCA has presented clear and convincing evidence that the Debtors obtained money by the use of a materially false written statement respecting their financial condition.

2. PCA has not presented clear and convincing evidence that its reliance on said statement was reasonable.

3. PCA has presented clear and convincing evidence that Mr. Bogstad published said statement with an intent to deceive.

4. PCA has not presented clear and convincing evidence that Ms. Bogstad published said statement with an intent to deceive.


5. The Debt owed by the Debtors to PCA should be found dischargeable.

ORDER

IT IS ORDERED THAT the debt owed by Robert Oneal Bogstad and Arlene R. A. Bogstad to Production Credit Association of River Falls and evidenced by loan agreements dated September 9, 1980, should be, and the same hereby is, dischargeable.

Dated: December 4, 1984.

BY THE COURT:

  
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William H. Frawley  
U. S. Bankruptcy Court