

**SO ORDERED.**

**SIGNED this 13th day of October, 2020.**



*Dale L. Somers*

Dale L. Somers  
United States Chief Bankruptcy Judge

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**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF KANSAS**

In re:

Charlene Ann Giles,

Debtor.

James F. Mote and

Lola E. Mote,

Plaintiffs,

v.

Charlene Ann Giles,

Defendant.

Case No. 19-11993-7

Adversary No. 20-5005

**Order Entering Judgment for Defendant/Debtor on Plaintiffs'  
Nondischargeability Complaint under 11 U.S.C. § 523(a)(2)(A)**

Debtor/Defendant Charlene Ann Giles owes Plaintiffs James and Lola Mote more than \$200,000 because of two loans the Motes made to Debtor and her now-deceased husband. The Motes allege that Debtor obtained that

money through “false pretenses, a false representation, or actual fraud,” and object to the discharge of that debt under 11 U.S.C. § 523(a)(2)(A).<sup>1</sup>

The Motes’ claim under § 523(a)(2)(A) proceeded to trial.<sup>2</sup> The Court now concludes the Motes have not met their burden to show the debt is nondischargeable under § 523(a)(2)(A). As a result, the Court enters judgment for Debtor, concluding that the debt owed by Debtor to the Motes is dischargeable.

## **I. Findings of Fact**

Debtor and her husband (Benjamin Giles, who is now deceased) were involved in at least three business entities: Mr. Giles’s accounting firm, MWM Oil Company, Inc., and RAG Oil Co., Inc.<sup>3</sup> For thirty-five years, Debtor worked for her husband at these businesses – preparing financial statements, reconciling bank accounts, tracking accounts receivable and accounts payable, etc. Through her work, Debtors testified that she was intimately aware of all financial details at the oil companies. In February 2013, the Giles became involved in a lawsuit with Jayhawk Pipeline, LLC, concerning

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<sup>1</sup> All future references to Title 11 of the United States Code will be to section number only.

<sup>2</sup> Debtor appears by J. Michael Morris, and the Motes appear by Frank Ojile.

<sup>3</sup> Both MWM Oil Company, Inc. and RAG Oil Co., Inc. have been involved in their own, separate Chapter 11 liquidating bankruptcies: Case No. 19-11404 MWM Oil Company, Inc. and Case No. 19-11405 RAG Oil Co., Inc. Both cases were recently closed, on July 1, 2020.

the valuation of oil and gas reserves on real estate unrelated to the matters discussed herein.

Debtor and Mr. Giles met the Motes many years ago. The parties became friendly – they shared meals, travelled together, and socialized together. At some point in late 2014, Mr. Giles and Mr. Mote began discussing a loan from the Motes to the Giles. Mr. Mote testified that Mr. Giles told him he needed the money to purchase oil pipes; the oil pipes were cheap and it was a good time to buy them. Contrarily, Debtor testified that they needed the money because they were fighting the Jayhawk Pipeline lawsuit and needed cash to keep their business afloat and running. At another point in the trial, Debtor testified that from what she remembers, her husband needed the money because he was trying to get certain oil wells producing. Regardless of the purpose of the loan, Mr. Mote took a mortgage on his life insurance to get the funds and agreed to make the loan to the Giles.

On December 24, 2014, the Giles each signed a promissory note to the Motes for \$150,000, at 8% annual interest. The note required that installments of \$1000 be paid beginning on February 1, 2015, and due monthly thereafter until December 24, 2016, at which time the principal would be due in full. The note is secured by a mortgage on a piece of property

in Butler County, Kansas, and contemporaneously therewith, the Giles executed a mortgage on that property.

Debtor took the signed note to the Motes shortly after Christmas in 2014, at the Motes' vacation property in Mexico. Debtor stayed with the Motes for a few days and then returned home with the money, made out in the amounts Mr. Giles wanted spread over three separate checks. Mr. Mote testified that Mr. Giles wanted at least one of the checks separate so that he could pay off an existing mortgage on the property, and be free to give the mortgage to the Motes.

Mr. Mote did not record the mortgage upon his return to Kansas; he testified that Mr. Giles told him he did not need to record the mortgage because the Giles would be receiving funds from the Jayhawk Pipeline lawsuit and would pay it off then. Debtor testified that she does not remember her or her husband ever telling the Motes that they did not need to record the mortgage. Debtor also testified that she does not remember any of the meetings leading up to she and her husband signing the note and mortgage. Debtor began making monthly payments on the note as scheduled, in February 2015.

About six months after signing the note and mortgage on the Butler County property, on June 11, 2015, the Giles and Michael Traylor signed a

real estate purchase contract for the sale of that property to Mr. Traylor. Debtor testified that Mr. Traylor approached Mr. Giles about three weeks prior to the sale, seeking to buy the property so he could develop it for his cattle operation. The owner's affidavit, signed by the Giles to induce a title company to issue a title insurance policy, stated there were no "recorded or unrecorded deeds of trust, mortgages, . . . [or] security agreements . . . which affect the real estate." Debtor testified that this statement was, of course, false, but she had simply not remembered the unrecorded mortgage given six months prior, at the end of December 2014.

The Giles did not tell the Motes they sold the Butler County real estate to Mr. Traylor. The sale of the Butler County real estate yielded \$248,230.09 for the Giles. In other words, the Giles received more than enough to repay the Motes; the Giles instead used the funds for their oil and gas business.

Debtor continued to make the \$1000 a month payment to the Motes during this time. About a year after selling the Butler County real estate, on August 18, 2016, the Motes made a second loan to Debtor and Mr. Giles. The Giles signed a promissory note for \$50,000 at 8% interest, to be secured by proceeds from the Jayhawk Pipeline lawsuit, "presently in settlement." This second promissory note also required payments of \$1000 a month, this time beginning in October 2016 and continuing thereafter until either the

settlement of the Jayhawk Pipeline lawsuit or January 1, 2017, whichever came first. Mr. Mote testified that the Giles had come to their home for a social visit, and Mr. Giles ensured him that he would pay the balance due on both notes all at once through the settlement.

Regarding the Jayhawk Pipeline “settlement,” at some point, the parties to the Jayhawk Pipeline lawsuit “settled” their dispute, by agreeing that Jayhawk Pipeline would pay the appraised fair market value of any proved undeveloped oil and gas reserves to the owners of the working interests in the real estate at issue, which included Mr. Giles. The parties also agreed to a procedure for choosing appraisers. But ultimately, the appraisal actually accepted by the state court stated that there were no proved undeveloped reserves, meaning Jayhawk Pipeline would pay nothing to the owners of the working interests.<sup>4</sup> At trial in this Court, the only date given was that the settlement occurred sometime before June 2017, because there was a docket notation in the state court suit that a party filed a motion to enforce the settlement on that date. The Court presumes the August 18, 2016 loan occurred sometime after the parties to the Jayhawk Pipeline suit “settled,” but before the appraisal process was completed. The Court can only

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<sup>4</sup> See *Jayhawk Pipeline, L.L.C. v. MWM Oil Co.*, No. 118,206, 2018 WL 5305686, at \*1 (Kan. Ct. App. Oct. 26, 2018).

conclude that a considerable amount of time passed between the settlement and the filing of the motion to enforce that settlement.

Debtor continued making \$1000 payments to the Motes from the Giles' personal account, until she began writing checks for \$2000 a month in October 2016 – the amount due for both loans. The \$2000 monthly payment was short lived, however. Debtor made only two more \$2000 payments, in November 2016 and January 2017. She then made a \$4000 payment in October 2017, but paid nothing more thereafter to the Motes on the two notes. The \$4000 payment in October 2017 occurred because Mr. Mote was getting pushed by his life insurance to pay his funds back, so he in turn pushed on Mr. Giles to make a payment. Mr. Mote also recorded the mortgage at that point. At the time he recorded the note, he still did not know that the property had actually already been sold by the Giles.

Mr. Mote is now retired but worked in management at a local company and also owned and managed rental properties. Ms. Mote, who is a retired teacher, also worked in her husband's rental business and as a real estate agent. Both the Motes, through Ms. Mote's work as a real estate agent and Mr. Mote's work owning rental properties, understand the mortgage and recordation process.

Debtor testified that it became apparent the oil companies were out of money when the Jayhawk Pipeline lawsuit was unsuccessful, and oil started going down in late 2017 and the first part of 2018. During the same approximate time period as the events underlying this suit, the Giles or their business entities borrowed approximately \$1.2 million from friends and associates to help keep them afloat. It was unclear at trial whether Debtor personally carried that debt, or whether only the businesses did so. Debtor testified that she and her husband did not pay off any of the notes when due because they were to be paid off by funds from the Jayhawk Pipeline lawsuit, or from enhanced production at the oil companies which never materialized. As noted above, the Giles did not end up receiving anything from the Jayhawk Pipeline litigation.

Mr. Giles died on September 23, 2018. Debtor has received nothing from his probate estate. Debtor testified that her husband was the driving force behind all of the funds borrowed, because he ran the oil companies and had the accounting practice. Debtor has also received nothing from the liquidating bankruptcy estates of the MWM and RAG oil companies. She currently lives in an apartment and works at a daycare.

Debtor filed her Chapter 7 bankruptcy case on October 16, 2019. On her Schedule F, Debtor listed a \$250,000 debt to James and Lola Mote as



contingent and disputed. The Motes filed their adversary complaint against Debtor in January 2020. The complaint seeks to have the debt owed to them excepted from discharge under § 523(a)(2)(A).

## II. Conclusions of Law

An adversary proceeding to determine the dischargeability of a debt is a core proceeding under 28 U.S.C. § 157(b)(2)(I), over which this Court may exercise subject matter jurisdiction.<sup>5</sup>

Subsection (a)(2)(A) excepts from discharge any debt “for money, property, [or] services . . . obtained by . . . false pretenses, a false representation, or actual fraud.” “Section 523(a)(2)(A), one of the most utilized nondischargeability provisions, prevents the discharge of debts involving a debtor’s dishonesty. Congress concluded that preventing fraud is more important than letting defrauders start over with a clean slate. . . . Thus, § 523(a)(2)(A) encompasses fraudulent representations as well as other forms of actual fraud that can be effected without a false representation.”<sup>6</sup>

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<sup>5</sup> This Court has jurisdiction pursuant to 28 U.S.C. § 157(a) and §§ 1334(a) and (b) and the Amended Standing Order of the United States District Court for the District of Kansas that exercised authority conferred by § 157(a) to refer to the District’s Bankruptcy Judges all matters under the Bankruptcy Code and all proceedings arising under the Code or arising in or related to a case under the Code, effective June 24, 2013. D. Kan. Standing Order 13-1, *printed in* D. Kan. Rules of Practice and Procedure (March 2018).

<sup>6</sup> *Pino v. Jensen (In re Jensen)*, No. CO-18-089, 2019 WL 2403105, at \*4 (10th Cir. BAP June 7, 2019) (internal quotations omitted).

The Motes bear the burden of proof to establish each element of their claim under § 523(a)(2)(A) by a preponderance of the evidence.<sup>7</sup>

**A. Nondischargeability Under § 523(a)(2)(A) based on a False Representation**

To carry their burden of proof under § 523(a)(2)(A) based on a false representation, the Motes must show each of the following elements: “(1) the debtor made a false representation; (2) the debtor intended to deceive the creditor; (3) the creditor relied on the debtor’s conduct; (4) the creditor’s reliance was justifiable; and (5) the creditor was damaged as a proximate result.”<sup>8</sup>

The first element that must be shown is a false representation, and the Motes have failed to carry their burden of proof on this element. “False pretenses’ or ‘representations’ are representations knowingly and fraudulently made that give rise to the debt.”<sup>9</sup> The only false representation alleged by the Motes is that of Mr. Giles, not Debtor. The Motes allege that

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<sup>7</sup> *Grogan v. Garner*, 498 U.S. 279, 287 (1991); see also *Diamond v. Vickery (In re Vickery)*, 488 B.R. 680, 685–86 (10th Cir. BAP 2013) (“Section 523(a) exceptions to discharge must be narrowly construed, and because of the fresh start objectives of bankruptcy, doubt is to be resolved in the debtor’s favor. The creditor bears the burden of proving nondischargeability under § 523(a) by a preponderance of the evidence.” (internal quotations omitted)).

<sup>8</sup> *Ez Loans of Shawnee v. Hodges (In re Hodges)*, 407 B.R. 415, 419 (Bankr. D. Kan. 2009) (citing *Groetken v. Davis (In re Davis)*, 246 B.R. 646, 652 (10th Cir. BAP 2000)).

<sup>9</sup> *In re Jensen*, 2019 WL 2403105, at 5.

Mr. Giles told them they did not need to record the mortgage on the first note, because it would be paid off quickly through the Jayhawk Pipeline lawsuit settlement. There is no testimony to show that Mr. Giles did not in fact believe that a Jayhawk Pipeline settlement was imminent. Even if this statement could rise to the level of a representation knowingly and fraudulently made, how did it give rise to the *making* of the first loan? Let alone the second loan made by the Motes to the Giles over a year and a half later. The statement was given by Mr. Giles *after* the first loan was made, and solely as to recordation of the mortgage. There is no testimony that Debtor made this statement. And obviously, Debtor herself did not make the statement, only Mr. Giles is alleged to have done so. The first element the Motes must prove for a § 523(a)(2) claim based on false representation is that “the debtor made a false statement” – there is no false statement *by Debtor* here.

Because there was no false representation, the Court concludes there could be no reliance thereon.<sup>10</sup> The Motes have not carried their burden as to this claim.

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<sup>10</sup> Reliance on a debtor’s false pretenses or representations must be justifiable “from a subjective standpoint.” *Johnson v. Riebesell (In re Riebesell)*, 586 F.3d 782, 791-92 (10th Cir. 2009) (citing *Field v. Mans*, 516 U.S. 59, 74-75 (1995)). “In order to rely on a misrepresentation,” the party making the nondischargeability claim “necessarily

## **B. Nondischargeability Under § 523(a)(2)(A) based on Actual Fraud**

Actual fraud is “any fraud that involves moral turpitude or intentional wrong” and “anything that counts as ‘fraud’ and is done with wrongful intent is ‘actual fraud.’”<sup>11</sup> “Actual fraud occurs when a debtor intentionally engages in a scheme to deprive or cheat another of property or a legal right. Thus, establishing a prima facie case for actual fraud under § 523(a)(2)(A) requires proof of three elements: 1) fraudulent intent; 2) a fraudulent scheme; and 3) injury caused by the scheme.”<sup>12</sup>

The Motes have a difficult task from the beginning on an actual fraud claim, as they must show Debtor’s fraudulent intent. A debtor’s intent to deceive “may be inferred from the totality of the circumstances.”<sup>13</sup> “The bankruptcy court must consider whether the totality of the circumstances ‘presents a picture of deceptive conduct by the debtor which indicates an intent to deceive the creditor.’”<sup>14</sup> A totality of the circumstances inquiry is

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must first be deceived.” *In re Taylor*, 455 B.R. 799, 802 (Bankr. D.N.M. 2011), *aff’d*, 478 B.R. 419 (10th Cir. BAP 2012), *aff’d*, 737 F.3d 670 (10th Cir. 2013).

<sup>11</sup> *Husky Int’l Elects., Inc. v. Ritz*, 136 S. Ct. 1581, 1586 (2016) (internal quotation marks and alteration omitted).

<sup>12</sup> *In re Jensen*, 2019 WL 2403105, at \*8.

<sup>13</sup> *In re Young*, 91 F.3d 1367, 1375 (10th Cir. 1996).

<sup>14</sup> *In re Davis*, 246 B.R. at 652 (quoting 3 Norton Bankr. Law & Practice 3d § 57:16 (2016)).

fact specific and hinges on the credibility of witnesses.<sup>15</sup> The Motes contend Debtor's intent to deceive can be inferred because Debtor was insolvent at the time she and her husband borrowed the money from the Motes, and that the real property upon which the mortgage was given was sold only six months after giving the mortgage to the Motes.

Again, the Motes problem with this element is that almost none of the evidence supports a finding that Debtor had an intent to deceive. First, regarding Debtor's alleged "insolvency," no proof was offered that Debtor and Mr. Giles were insolvent, and the testimony about the purpose or need for the loan was conflicting. In addition, the evidence concerning the other loans given at the time was also not clear as to whether the businesses took out loans or whether Debtor personally signed the loans. The Motes did establish that Debtor was very involved in tracking and recording the financial matters for the Giles and their businesses, but that is where it ended. Debtor did not negotiate the loans with the Motes; Mr. Giles did. Debtor did not discuss the Jayhawk Pipeline lawsuit with Mr. Mote; Mr. Giles did. Mr. Giles is the one who communicated the need for both the first and second loans to the Motes, and Mr. Giles is the one who negotiated the loans' terms. Mr. Giles was

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<sup>15</sup> See *DSC Nat'l Props., LLC v. Johnson (In re Johnson)*, 477 B.R. 156, 170-72 (10th Cir. BAP 2012).

approached to sell the property upon which he and Debtor had given the mortgage, and Mr. Giles carried out that sale. The only evidence as to the second loan is that Mr. Giles told the Motes the settlement of the Jayhawk Pipeline lawsuit was in progress, and the funds would be quickly in hand. These acts by Mr. Giles are not enough from which the Court could infer an intent to deceive by Debtor.

Yes, Debtor signed a promissory note with the Motes and gave them a mortgage on a piece of property, and then sold that property six months later, without disclosing the unrecorded mortgage thereon. Debtor also signed the second promissory note that indicated a settlement of the Jayhawk Pipeline was in progress, although it turned out the “settlement” needed a lot more steps before it resulted in money for the Giles and the Giles ultimately realized nothing. But there is just no evidence that Debtor’s behavior was fraudulent. Debtor credibly testified that she was not involved in the details of each transaction, and that she was basically just told to come in and sign things by her husband. Debtor at trial was unaware what loans were in her name, versus her husband’s name, or their businesses’ names. She certainly was involved in the financial aspects of the companies, but more as a bookkeeper, not as a decision maker.

The Court concludes that viewing the totality of the circumstances, the Motes have not shown Debtor's fraudulent intent, and therefore, the Motes did not carry their burden to show actual fraud under § 523(a)(2)(A). The Court concludes that the evidence does not support an inference of deceptive conduct *by Debtor*.

### **III. Conclusion**

For a debt to be nondischargeable under § 523(a)(2)(A), there has to be more than just a loan that has gone unpaid. There has to be "false pretenses, a false representation, or actual fraud" in the *making* of the loan, not in acts subsequent to that time.

The Motes have not met their burden to show the debt owed by Debtor to them is nondischargeable under § 523(a)(2)(A) based on "false pretenses, a false representation, or actual fraud." The Court enters judgment for Debtor, and concludes that the debt is dischargeable.

**It is so Ordered.**

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