IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEBRASKA

In the Matter of CHARLES R. TURNER, Bankrupt.	BK 78-0-854
JOHN GOODKNIGHT, Plaintiff-Appellee, vs CHARLES R. TURNER, Defendant-Appellant.	CIVIL NO. 80-0-130

MEMORANDUM

APPEARANCES: For Plaintiff-Appellee - Martin A. Cannon, Omaha, Nebraska

For Defendant-Appellant - Thomas C. Emery, Omaha, Nebraska

DENNEY, District Judge

This matter comes before the Court on appeal from an order of the Bankruptcy Judge granting the plaintiff-appellee, John Goodnight [hereinafter referred to as "Goodknight"], an $11,000.00 judgment against the defendant-appellant, Charles R. Turner [hereinafter referred to as "Turner"]. The Bankruptcy Judge determined that the judgment was nondischargeable in the involuntary bankruptcy proceedings involving Turner [Filing #90]. Goodknight had objected to the discharge of Turner pursuant to §17a(2) of the Bankruptcy Act (11 U.S.C. §35a(2)) [hereinafter referred to as the "Act"], on the grounds that Turner was liable for willful and malicious conversion of Goodknight's property prior to the bankruptcy proceeding [Filing #51]. The facts of this case are not seriously disputed. In 1977, Goodknight was the owner of an airplane which he was offering for sale. Turner expressed an interest in the airplane and met with Goodknight to inspect the plane. The parties agreed on a $60,000.00 purchase price for the airplane. The initial agreement was that Goodknight would receive $10,000.00 in cash and accept a $50,000.00 six-month note for the balance of the purchase price. Goodknight received a $10,000.00 check at that time. The balance was to be secured by a first mortgage on the airplane to Goodknight. Goodknight did not receive the mortgage or the note at the initial meeting. Turner left his airplane and took Goodknight's plane with him.

At a later time, Goodknight contacted Turner and requested an additional $34,000.00 cash down payment. The reason for this

modification was that Goodknight's banker refused to release a lien on the plane until Goodknight paid off the existing debt. Goodknight proposed to Turner that he receive an additional $34,000.00 and he would accept a $16,000.00 note for the purchase price secured by a second mortgage on the airplane. Turner agreed. Thereafter, Turner gave Goodknight a check for $34,000.00 and executed a note for $16,000.00 and a second mortgage on the airplane.

Turner actually took title to the airplane in the name of Millard Aviation, Inc., a corporation with which he was associated. In fact, unknown to Goodknight, Turner, on behalf of Millard Aviation, Inc., gave a first mortgage to the Bank of Papillion in the amount of $45,000.00. Turner gave the Bank of Papillion a $45,000.00 mortgage instead of one for $34,000.00 because the bank was pressuring him to clear up some other smaller loans as well as infuse additional capital into Millard Aviation, Inc.

Subsequently, Turner and Millard Aviation, Inc., experienced financial difficulties. Turner never paid in full either the $45,000.00 note to the Bank of Papillion or the $16,000.00 note to Goodknight. It was several months after the parties' transaction that Goodknight discovered that Turner had given the Bank of Papillion a first mortgage in the amount of $45,000.00, not $34,000.00. In order to protect his position as second mortgagee, the company which Goodknight controlled bought the $45,000.00 note and mortgage from the Bank of Papillion. Goodknight's company repossessed the plane, but soon realized that the airplane was then worth only about $43,000.00 on the open market. This was approximately the amount due on the Bank of Papillion note which had been assigned to Goodknight's company. Thus, Goodknight's company advised Turner and Millard Aviation, Inc., that it would not proceed to take any action on the defaulted note and first mortgage. But, due to the reduced market value of the airplane, Goodknight personally was prevented from realizing on the security to satisfy the $16,000.00 note and second mortgage that he had obtained from Turner. That is, at the time of the initial transaction, Goodknight operated on the assumption that the airplane worth $60,000.00 would safely allow for the $34,000.00 first mortgage that Turner said he was going to obtain from his banker, the $16,000.00 second mortgage that Turner had given Goodknight, and $10,000.00 of "cushion." The gist of Goodknight's objection to Turner's discharge was that Turner's misrepresentation as to the amount of the first mortgage that he was to obtain from the Papillion bank was willful and malicious and that it caused a conversion of $11,000.00 worth of Goodknight's security interest in the airplane.

On July 17, 1978, Turner was taken into involuntary bankruptcy proceedings by his creditors [Filing #1]. On April 2, 1979, the Bankruptcy Judge entered an order allowing the filing of Goodknight's objection to discharge [Filing #67].

The applicable standards of review for this kind of case are well defined. In determining whether a debt is nondischargeable, the bankruptcy court's factual findings are conclusive unless "clearly erroneous." Carini v. Matera, 592 F.2d 378, 380 (7th Cir. 1979). A presumption exists that the findings below were correct. In re Mascolo, 505 F.2d 274, 277 (1st Cir. 1974); see also Solomon v. Northwestern State Bank, 327 F.2d 720, 724 (8th Cir. 1964). A finding by the bankruptcy court is "clearly erroneous" when, although there is evidence to support it, the reviewing court is left with the firm and definite conviction that a mistake has been committed. Bank of Meeker v. McGinnis, 586 F.2d 162, 164 (10th Cir. 1978).

The Bankruptcy Judge determined that Turner's liability to Goodknight was nondischargeable in bankruptcy under §17a(2) of the Act. He reasoned that Turner, by disregarding Goodknight's assumption that Turner would encumber the airplane with a first mortgage for only $34,000.00, thereby willfully and maliciously converted Goodknight's anticipated secure position as second mortgagee with $10,000.00 of "cushion" to guard against a drop in the value of the security.

As support for the proposition that a person with a security interest has a sufficient property interest in property to have it converted, the Bankruptcy Judge correctly cited Davis v. Aetna Acceptance Co., 293 U.S. 328 (1934). In his Memorandum Opinion, though, the Bankruptcy Judge used a somewhat incomplete quotation from Davis, implying that it offered a comprehensive definition of "willful and malicious" in the context of §17a(2) of the Act. Turner points to this flaw in his appellate brief. The language in Davis really only discusses those instances where an innocent or technical conversion does not give rise to an objection to discharge.

Despite the possible error committed by the Bankruptcy Judge in completely relying on Davis for definitional support, the Court agrees with the ultimate conclusion that he reached. The finding that Turner intentionally disregarded the financing assumption under which Goodknight was operating clearly passes muster under the "clearly erroneous" standard of review of factual questions. Turner went so far as to admit this. While the Court is free to reject incorrect legal determinations made by the Bankruptcy Judge, the Court agrees with the conclusion that Turner's disregard of Goodknight's assumption regarding financing amounts to "willful and malicious" conduct.

Recent cases have helped in explaining the meaning of the Davis case. In St. Paul Fire & Marine Ins. Co. v. Elliott, 385 F.Supp. 1194, 1197 (M.D. La. 1979), the court held that "in order for a conversion of another's property to be legally 'willful and malicious' for the purposes of Section 17(a)(2), it must be done without his knowledge or consent, intentionally, without justification and excuse, and to his injury (citing 1A COLLIER ON BANKRUPTCY ¶17.17, p. 1653 (14th ed. 1978) and cases cited therein)." After discussing the Davis case, Judge Campbell, in In re Nance, 556 F.2d 602, 611 (7th Cir. 1977), stated that "[t]here need be no showing of 'special malice' toward the injured party, only that the act 'is done deliberately and intentionally in knowing disregard of the rights of another' (citing Bennett v. W. T. Grant Co., 481 F.2d 664, 664 (7th Cir. 1973))."

As to the Bankruptcy Judge's legal determination that Turner's conduct fits within the "willful and malicious" conversion exception in §17a(2) of the Act, the "clearly erroneous" standard of review is inapplicable. When the issue on appeal is the bankruptcy judge's application of a legal standard to facts which are undisputed or reasonably found, it is enough that the reviewing court is convinced that the result does not jibe with the applicable rule of law. Levin v. City Trust Co., 482 F.2d 937, 939 (2d Cir. 1973). Thus, where the question presented is solely one of law, no presumption of correctness applies, and the bankruptcy judge's legal conclusions may not be approved by the district court without an independent determination of the legal questions. In re Gilchrist Co., 410 F.Supp. 1070, 1074 (E.D. Pa. 1976) (citing 2A COLLIER ON BANKRUPTCY ¶39.28, p. 1532-33 (13th ed. 1974)).

The Court has reviewed the record in light of the applicable law and independently agrees with the Bankruptcy Judge's legal determination that Turner's conduct fits within the "willful and malicious" conversion exception to §17a(2) of the Act. Based on the facts of this case, it is quite clear that Turner's conduct is within the parameters of the rules set forth in the Davis, Elliott, and Nance cases discussed supra. That is, the evidence and facts adduced by the Bankruptcy Judge show plainly that (1) Turner acted without the knowledge of Goodknight, (2) Turner had little if any cognizable justification for disregarding Goodknight's reasonable assumption that Turner would limit the amount of the first mortgage on the airplane to $34,000.00, (3) Goodknight was injured to the extent of $11,000.00 of security that he assumed he would have after the $34,000.00 mortgage to Turner's bank, (4) Turner acted deliberately and intentionally, and (5) Turner knowingly disregarded Goodknight's right to assume

that Turner would abide by his representation that he would encumber the airplane with a first mortgage of $34,000.00. Therefore, Turner's conduct amounted to a "willful and malicious" conversion of $11,000.00 of Goodknight's anticipated second priority in the security.

Appellant Turner argues on appeal that the Bankruptcy Judge's ruling is incorrect because Goodknight failed to prove that he was actually damaged. Here again, this is a factual determination. The Bankruptcy Judge received evidence that perhaps the airplane appreciated in value after the parties' transaction. Still, he was persuaded by the contrary evidence that the airplane had gone down in value, rendering worthless Goodknight's second mortgage. In view of the record, the Court is unwilling to say that this factual determination by the Bankruptcy Judge was clearly erroneous.

As the third and final ground for reversal advocated by Turner, he maintains that Goodknight's company repossessed the airplane and then obtained title without full and proper notification to Turner, thereby depriving Goodknight of any claim to a deficiency judgment. Goodknight is correct in pointing out that the concept of deficiency judgment is totally inapplicable to the facts of this case. Turner's argument on this point is factually and legally without merit.

In sum, the Bankruptcy Judge's factual determinations in this case are supported by the evidence and are not clearly erroneous. Thus, those findings will not be disturbed by the Court. Furthermore, the Bankruptcy Judge's determination of the legal consequences of those facts is correct. For the reasons stated above, the Court affirms the judgment of the Bankruptcy Judge that Turner's liability to Goodknight for the willful and malicious conversion of the latter's property is nondischargeable in bankruptcy.

An order shall issue contemporaneously with this Memorandum Opinion.

Dated this 13th day of August, 1980.