SO ORDERED,

Judge Jamie A. Wilson
United States Bankruptcy Judge
Date Signed: May 3, 2022

The Order of the Court is set forth below. The docket reflects the date entered.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF MISSISSIPPI

IN RE:

JERRY ALVIN HALL,	**CASE NO. 20-02463-JAW**
DEBTOR.	**CHAPTER 7**
CHARTER 3 DEVELOPMENT, LLC	**PLAINTIFF**
VS.	**ADV. PROC. NO. 20-00051-JAW**
JERRY ALVIN HALL	**DEFENDANT**

IN RE:

CHARLES HOWARD WARRINER AND JENNIFER JORDAN WARRINER,	**CASE NO. 20-02444-JAW**
DEBTORS.	**CHAPTER 7**
CHARTER 3 DEVELOPMENT, LLC	**PLAINTIFF**
VS.	**ADV. PROC. NO. 20-00052-JAW**
CHARLES H. WARRINER	**DEFENDANT**

OPINION ON: (1) COMPLAINTS AND OBJECTIONS TO DISCHARGE OF CLAIMS AND (2) OBJECTIONS TO PROOFS OF CLAIM NO. 1 FILED BY CHARTER 3 DEVELOPMENT, LLC

Introduction

This is not a typical debtor-creditor dispute. Charter 3 Development, LLC ("Charter 3") never intended to be a creditor of Castlerock Properties, LLC ("Castlerock"). Only through the acts of Castlerock's owners, Jerry Alvin Hall ("Hall") and Charles H. Warriner ("Warriner"), did Charter 3 become an "involuntary creditor." At bottom, this is a case about two individuals who used funds that did not belong to them.

Procedural History

The consolidated trial of the above-referenced adversary proceedings (the "Adversary Proceedings") took place on December 9, 2021 (the "Trial"), on the Complaint and Objection to Discharge of Claims (the "Hall Adversary Complaint") (Hall Adv. Dkt. #1)[1] filed by Charter 3 and the Response to Complaint and Objection to Discharge of Claims (the "Hall Response") (Hall Adv. Dkt. #9) filed by Hall in adversary proceeding number 20-00051-JAW (the "Hall Adversary"); the Complaint and Objection to Discharge of Claims (together with the Hall Adversary Complaint, the "Adversary Complaints") (Warriner Adv. Dkt. #1) filed by Charter 3 and the Response to Complaint and Objection to Discharge of Claims (together with the Hall Response, the "Responses") (Warriner Adv. Dkt. #9) filed by Warriner in adversary proceeding number 20-00052-JAW (the "Warriner Adversary"); the Objection to Discharge of Claims and Objection to Proof of Claim No. 1 Filed on Behalf of Charter 3 Development (the "Hall Objection") (Hall Bankr. Dkt. #37) filed by Charter 3 in bankruptcy case number 20-02463-JAW (the "Hall Case"); and the Objection to Discharge of Claims and Objection to Proof of Claim No. 1 Filed on Behalf

[1] Citations to docket entries in the Adversary Proceedings are cited as "(Hall Adv. Dkt. #)" in adversary proceeding number 20-00051-JAW and "(Warriner Adv. Dkt. #)" in adversary proceeding number 20-00052-JAW and citations to docket entries in the above-styled bankruptcy cases are cited as "(Hall Bankr. Dkt. #)" in bankruptcy case number 20-02463-JAW and "(Warriner Adv. Dkt. #)" in bankruptcy case number 20-02444-JAW.

of Charter 3 Development (together with the Hall Objection, the "Objections to Proofs of Claim") (Warriner Bankr. Dkt. #60) filed by Charter 3 in bankruptcy case number 20-02444-JAW (the "Warriner Case"). Before Trial, the Court entered an order consolidating the Objections to Proofs of Claim with the Adversary Proceedings. (Hall Bankr. Dkt. #35; Warriner Bankr. Dkt. #61; Hall Adv. Dkt. #36; Warriner Adv. Dkt. #39). At Trial, Clyde X. Copeland, III and William M. Vines appeared on behalf of Charter 3, and Eileen N. Shaffer appeared on behalf of Hall and Warriner.[2] Pretrial Orders (Hall Adv. Dkt. #35; Warriner Adv. Dkt. #38) were entered in the Adversary Proceedings at Trial. Thirty-seven exhibits, marked as Exhibits 1 through 37, were admitted into evidence by stipulation, and one exhibit, marked as Exhibit 38, was admitted into evidence by Charter 3 without objection.[3] (Tr. at 6-7, 85-86).[4] Three witnesses, Jeff Michael Bracken ("Bracken"), Warriner, and Hall testified at Trial. At the close of evidence, the parties requested permission to file post-trial briefs in lieu of closing arguments. Their request was anticipated because the Court had already authorized Charter 3 to include in its post-trial briefs its response to the Objections to Proofs of Claim. (Hall Bankr. Dkt. #35; Warriner Bankr. Dkt. #61; Hall Adv. Dkt. #36; Warriner Adv. Dkt. #39). The Court formally granted their request from the bench. Also, because the parties expressed an interest in providing citations to the testimony, the Court agreed to wait until the transcript of the Trial became available before entering an order setting a thirty-day briefing schedule. On January 20, 2022, a transcript of the Trial was docketed in the Warriner Adversary (Warriner Adv. Dkt. #44), prompting the Court to issue an order setting February 22, 2022 as the

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[2] At a status conference held on December 6, 2021, Eileen N. Shaffer stated that she had explained to Hall and Warriner that a potential conflict may arise between them and assured the Court that they had agreed to joint representation in the Adversary Proceedings. She also represented Hall, Warriner, and Castlerock in their bankruptcy cases, which were filed within days of each other, and Warriner's and Hall's bankruptcy schedules include the same business debts.

[3] The stipulated Trial exhibits, marked as Exhibits 1 through 37, are cited as "(Ex. #)", and Exhibit 38, introduced into evidence by Charter 3, is cited as "(Charter 3 Ex. 38)."

[4] The transcript of the Trial is docketed in the Warriner Adversary. (Warriner Adv. Dkt. #44).

deadline to file post-trial briefs. (Hall Adv. Dkt. #39; Warriner Adv. Dkt. #45). Hall and Warriner thereafter sought an extension of the briefing schedule, which Charter 3 did not oppose. (Hall Adv. Dkt. #40; Warriner Adv. Dkt. #46). The Court entered an order extending the deadline for both parties to file post-trial briefs until March 11, 2022. (Hall Adv. Dkt. #41; Warriner Adv. Dkt. #47). On that day, the Court's case management/electronic case filing ("CM/ECF") system experienced an outage that prevented anyone from electronically filing documents. With the Court's permission, Hall and Warriner filed their post-trial briefs (Hall Adv. Dkt. #42; Warriner Adv. Dkt. #48) in paper format, and Charter 3 filed its post-trial briefs upon restoration of the CM/ECF system that next day. (Hall Adv. Dkt. #43; Warriner Adv. Dkt. #49).

At issue in the Adversary Complaints and in the Objections to Proofs of Claim is whether Hall and Warriner are individually liable to Charter 3 for a debt in the amount of $511,297.36 and, if so, whether the debt is nondischargeable under 11 U.S.C. § 523(a)(2)(A), (4), or (6).[5] Hall and Warriner deny any liability for the debt and any wrongdoing that would render the disputed debt nondischargeable. They seek an award of attorney's fees and costs in the Responses. Having considered the pleadings, exhibits, and testimony presented at Trial, the Court finds as follows:[6]

Jurisdiction

The Court has jurisdiction over the parties to and the subject matter of this proceeding pursuant to 28 U.S.C. § 1334. This is a core proceeding under 28 U.S.C. § 157(b)(2)(I). Additionally, the parties have consented to the entry of a final judgment by this Court. (Hall Adv. Dkt. #35 at 4; Warriner Adv. Dkt. #38 at 4). Notice of the Trial was proper under the circumstances.

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[5] From this point forward, all code sections refer to the Bankruptcy Code found at title 11 of the U.S. Code unless otherwise noted.

[6] Pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure, the following constitutes the findings of fact and conclusions of law of the Court.

Facts

The facts are largely undisputed: Charter 3 and Castlerock entered into joint ventures for the development of certain real estate; the joint ventures were unprofitable; checks representing funds belonging solely to Charter 3 were deposited into Castlerock's general operating account; and Castlerock used the money to pay creditors other than Charter 3. (Hall Adv. Dkt. #35 at 2-3; Warriner Adv. Dkt. #38 at 2-3). With that brief prelude to the undisputed facts, the Court begins with an overview of the two companies and the inception of their business relationship.

Charter 3

Bracken, along with his brother, John Christopher Bracken, and Benjamin Wadlington, formed Charter 3 as a real estate development company in 2005. (Tr. at 9-10). Bracken serves as the sole managing member of Charter 3. (Tr. at 9). In 2018, Charter 3 acquired six vacant lots in the Reunion subdivision in Madison, Mississippi, with the intent of building "spec houses"[7] on the lots. (Tr. at 11; Exs. 15, 22). Bracken knew that Castlerock had built a majority of the homes in Reunion. (Tr. at 11-12, 105, 147).

Castlerock

Castlerock was a limited liability construction company formed in 2003 by Hall and Warriner under Mississippi law. (Tr. at 63-64, 121; Ex. 5). At that time, each owned a fifty percent interest in Castlerock, and they served as co-managers of the company. (Tr. at 64). Both were involved in the daily affairs of the business. (Tr. at 63-64, 121). Hall, who has an associate degree in computer science, handled all of Castlerock's bookkeeping, whereas Warriner, who has a bachelor's degree in business administration, managed the construction of the houses and the company's relationship with realtors and buyers. (Tr. at 103, 146). In short, "Jerry [Hall] ran the office, Charlie [Warriner]

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[7] A "spec house," in contrast to a "custom-built house," is a home built on land owned by the builder in anticipation of selling it on the open market. *United States v. Hanson*, 161 F.3d 896, 898 n.5 (5th Cir. 1998).

ran the field." (Tr. at 33). The houses built by Castlerock sold, on average, for $750,000.00. (Tr. at 105).

Bracken testified that his banker vouched for Hall and Warriner. (Tr. at 12, 23). The banker told him that Castlerock had entered into partnerships with other investors for the construction of homes with some success. (Tr. at 12, 23). Bracken met with Hall and Warriner to pursue a similar deal. (Tr. at 12).

Joint Venture Agreements

After Bracken's meeting with Hall and Warriner, Charter 3 and Castlerock entered into three written joint venture agreements for the development and sale of spec houses on Lots Q-3, Q-5, and Q-8 in July 2018.[8] (Exs. 7-8). Copies of the written joint venture agreements for Lots Q-5 and Q-8 were introduced into evidence at Trial, but Charter 3 was unable to produce a written copy of the joint venture agreement for Lot Q-3. Hall and Warriner, however, do not dispute that such an agreement exists. (Tr. at 107, 121-22).

Hall and Warriner each signed the Joint Venture Agreement for Lot Q-5 in their representative capacity as a "Managing Member" of Castlerock. (Ex. 7). Their signatures are missing from the Joint Venture Agreement for Lot Q-8, but they do not dispute that a signed copy for Lot Q-8 exists or that a signed copy of the missing Joint Venture Agreement for Lot Q-3 exists. (Ex. 8). They emphasize that they signed all three Joint Venture Agreements only in their representative capacities as members of Castlerock.

Hall testified that he "typed" all three joint venture agreements borrowing language from past agreements between Castlerock and other investors. (Tr. at 65, 107). The joint venture agreements

[8] Charter 3 and Castlerock entered into a fourth joint venture agreement regarding a lot in Reunion known as Lot Q-4, but Castlerock did not finish construction of the spec house before filing bankruptcy and rejected the agreement as an executory contract. (Case No. 20-02453-JAW, Bankr. Dkt. #109). These Adversary Proceedings involve only Lots Q-3, Q-5, and Q-8.

are identical except for the reference to the lot number. (Exs. 7-8; Tr. at 65). In each, Charter 3 agreed to contribute a lot to the joint venture and fund the construction of a spec house on that lot. (Ex. 7 ¶ 2(a)-(b); Ex. 8 ¶ 2(a)-(b); Tr. at 19-20, 22-23, 108). For its part, Castlerock agreed to be responsible for "all aspects of the construction of said spec house." (Ex. 7 ¶ 2(c); Ex. 8 ¶ 2(c)). On the day of closing, "a simultaneous conveyance" would occur where Charter 3 would convey the lot to Castlerock and Castlerock, in turn, would convey the lot and newly constructed home to the buyer. (Ex. 7 ¶ 4; Ex. 8 ¶ 4). Charter 3 asked that the conveyance of the lot to the buyer occur in this manner because it believed that it could avoid any warranty obligations under state law by doing so.[9] (Ex. 7 ¶ 6; Ex. 8 ¶ 6; Tr. at 19). This arrangement, however, meant that the buyer of the house issued a check made payable solely to Castlerock at the closing.

From the proceeds of the sales of the homes, Castlerock and Charter 3 agreed to evenly split any profits realized "after paying any and all costs associated with the construction of the project." (Ex. 7 ¶ 9; Ex. 8 ¶ 9). "Costs" are defined as including "cost of lot, all interest expenses incurred from construction loan and/or moneys deposited toward the construction of said spec house by Charter 3 Development, LLC, all costs as reflected and actually paid on the Cost Estimate Sheet, any closing cost/attorney fees, and real estate commissions." (Ex. 7 ¶ 9; Ex. 8 ¶ 9). In summary, Charter 3 was entitled to be reimbursed for: (1) the cost of the lot; (2) all interest expenses incurred by Charter 3 to finance the construction of the home; and (3) all money directly contributed by Charter 3 for construction costs.

[9] Under Mississippi's New Home Warranty Act, a "builder" warrants to a new-home purchaser that the home will be free "from any defect due to noncompliance with building standards" subject to either a one-year or six-year limitations period, with the longer limitations period applying to major structural defects. MISS. CODE ANN. §§ 83-58-1 to -17. By conveying the lot to Castlerock rather than to the buyer, Charter 3 hoped to avoid these obligations.

Consistent with the terms of the joint venture agreements, Charter 3 funded the construction of the spec houses on Lots Q-3, Q-5, and Q-8, and Castlerock built and sold them. (Tr. at 28-29, 37, 42-43, 70, 122-23). Prior to each closing, Bracken signed a quitclaim deed conveying the lot from Charter 3 to Castlerock (Exs. 11, 18, 24), and Castlerock signed the deed transferring the lot and home from Castlerock to the buyer.

Closings of the Sales

The closings of the spec houses built on Lots Q-8, Q-5, and Q-3 took place on April 30, 2020, July 9, 2020, and July 24, 2020, respectively. (Exs. 13, 20, 26). Afterwards, checks made payable to Castlerock totaling $511,297.36, which represented reimbursable costs to Charter 3, were deposited into Castlerock's general operating account at BankFirst. At the first closing on April 30, 2020, Warriner signed the paperwork and accepted the check on behalf of Castlerock; at the second and third closings on July 9, 2020 and July 24, 2020, Hall signed the paperwork and accepted the checks. (Tr. at 70, 127). Neither Bracken nor anyone else acting on Charter 3's behalf attended any of the closings. (Tr. at 46-47). After each sale, Hall provided Bracken with a copy of the closing statement. (Tr. at 108).

Unfortunately, the joint ventures were unprofitable. The funds paid to Castlerock at the closings in the total amount of $511,297.36 fell short of the amount of unreimbursed constructions costs totaling $682,437.89. ($312,445.51 + $128,757.29 + $241,235.09 = $682,437.89) (Ex. 3 at Ex. 2; Ex. 4 at Ex. 2; Tr. at 123-24). Castlerock, however, did not remit any of the sales proceeds to Charter 3 even though there was no dispute that the funds belonged to Charter 3. (Tr. at 71). Each sale is discussed in more detail below.

April 30, 2020 Sale of House on Lot Q-8

The house on Lot Q-8 sold first. Fifteen days before the closing, Charter 3 transferred Lot Q-8 to Castlerock by quitclaim deed. (Ex. 11). At the closing on April 30, 2020,[10] the buyer paid $700,000.00 for the house and lot (Ex. 13), but the costs of construction totaled $743,284.36. (Ex. 3 at Ex. 2). These costs included a construction loan of $514,064.36 and cash provided by Charter 3 in the amount of $229,220.00 ($743,294.36 = $514,064.36 + $229,220.00). (Ex. 3 at Ex. 2). Charter 3's unreimbursed costs for the construction totaled $241,235.09. (Ex. 3 at 2). After payment of the balance of the construction loan, closing costs, county taxes, and certain allowances to the buyer, Castlerock, via Warriner, received a check in the amount of $165,870.42. (Ex. 13).

July 9, 2020 Sale of House on Lot Q-5

The house on Lot Q-5 sold next. Charter 3 transferred Lot Q-5 by quitclaim deed to Castlerock on June 29, 2020. (Ex. 18). At the closing on July 9, 2020, the buyer paid $589,800.00. (Ex. 20). The construction costs totaled $595,374.73, including a construction loan of $471,606.73 and cash in the amount of $123,768.00 contributed by Charter 3 ($595,374.73 = $471,606.73 + $123,768.00). (Ex. 3 at Ex. 2). Charter 3's unreimbursed costs for the construction totaled $128,757.29. (Ex. 3 at Ex. 2). Castlerock, via Hall, received a check in the amount of $89,511.30 after payment of the construction loan balance, closing costs, county taxes, and other fees. (Ex. 20).

[10] The Pretrial Orders (Hall Adv. Dkt. #35 at 3; Warriner Adv. Dkt. #38 at 3) and post-trial briefs indicate that the closing occurred on April 20, 2020, but the documents and the testimony at Trial confirm that the closing occurred on April 30, 2020. (Exs. 11, 13; Tr. at 25).

July 24, 2020 Sale of House on Lot Q-3

Finally, the house on Lot Q-3 sold for $669,000.00. (Ex. 26). Charter 3 transferred the lot to Castlerock by quitclaim deed the same day as the closing on July 24, 2020.[11] (Ex. 24). The construction costs totaled $698,895.06, including a construction loan of $469,010.06 and cash provided by Charter 3 in the amount of $229,885.00 ($698,895.06 = $469,010.06 + $229,885.00). (Ex. 3 at Ex. 2). Charter 3's unreimbursed costs for the construction totaled $312,445.51. (Ex. 3 at Ex. 2). Castlerock, via Hall, received a check in the amount of $255,915.64 after payment of the construction loan balance, closing costs, county taxes, and other fees. (Ex. 26).

Summary of Sales & Amounts Due Charter 3

The amount of unreimbursed costs incurred by Charter 3 for each house sold is summarized in a chart attached to the proofs of claim filed by Charter 3 in Hall's and Warriner's bankruptcy cases, as shown below:

Lot/Address	Bank First Constructioin Draw Payments: EX A	Direct construction payments: EX B	Total "Cost" of Construction: A + B	Gross amounts paid "to seller" at closing: From HUD EX C	Net amounts paid "to seller" at closing: From HUD EX C	Amounts due Charter 3 at closing: EX A (-) Pay Off on HUD	Claim amount: Lesser of Net "to Seller" and Amounts Due Charter 3
Q-3 Reunion/315 Lake Village Dr.	$ 469,010.06	$ 229,885.00	$ 698,895.06	$ 669,502.73	$ 255,915.64	$ 312,445.51	$ 255,915.64
Q-5 Reunion/319 Lake Villiage Dr.	$ 471,606.73	$ 123,768.00	$ 595,374.73	$ 590,352.88	$ 89,511.30	$ 128,757.29	$ 89,511.30
Q-8 Reunion/105 Haddington Cv.	$ 514,064.36	$ 229,220.00	$ 743,284.36	$ 700,769.81	$ 165,870.42	$ 241,235.09	$ 165,870.42
TOTAL CLAIM							**$ 511,297.36**

(Ex. 3 at Ex. 2; Ex. 4 at Ex. 2). As reflected in the next-to-last column of the above chart, Charter 3's unreimbursed costs totaled $682,437.89 ($312,445.51 + $128,757.29 + $241,235.09 = $682,437.89). In other words, Charter 3 was entitled to repayment of $682,437.89 but only $511,297.36 was generated from the three sales. No one disputes these figures.

[11] As with the date of the closing of the house on Lot Q-8, the Pretrial Orders and post-trial briefs incorrectly state the date of the closing on Lot Q-3. (Hall Adv. Dkt. #35 at 3; Warriner Adv. Dkt. #38 at 3). The documents and testimony at Trial show that the closing occurred on July 24, 2020, not July 20, 2020. (Exs. 24, 26; Tr. at 43).

Castlerock deposited the checks it received at the closings into its general operating account, did not pay Charter 3 any part of the sales proceeds, and used the money to pay other expenses. (Tr. at 49, 71, 124-25). Except for Castlerock's failure to remit the sales proceeds, Charter 3 agrees that Castlerock performed its obligations consistent with the joint venture agreements. (Tr. at 16-17). For example, Charter 3 does not question the reasonableness of the costs of the construction or the sales prices of the houses.[12] Charter 3's claims instead arise from Castlerock's handling and use of the sales proceeds, which is discussed below.

Sales Proceeds

The checks from the three sales totaling $511,297.36 were deposited into Castlerock's general operating account at BankFirst that Castlerock maintained for all construction projects. (Exs. 14, 21; Tr. at 76). Charter 3 introduced into evidence the bank statements for Castlerock's account at BankFirst for the months of April 2020 through August 2020. (Exs. 14, 21, 28). Although both Hall and Warriner had check-writing authority, only Hall's signature appears on the checks drawn on the account. (Tr. at 74, 76, 79). The bank statements show that Hall signed numerous checks made payable to himself and to creditors of Castlerock other than Charter 3. (Exs. 14, 21, 28). Many of these creditors were later identified by Hall and Warriner as creditors in their individual bankruptcy cases. Some of the debts paid had been personally guaranteed by Hall and Warriner. The bank statements for the months of July 2020 and August 2020 show that Castlerock experienced cash-flow problems before filing bankruptcy in late September 2020.

May 2020 Bank Statement

The statement for May 2020 shows that Castlerock started the month with a balance of $87,796.10. (Ex. 14). The check from the first sale in question was deposited into the account on

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[12] Bracken testified that "the houses had sat quite a while and the interest was eating us alive with our bank and we had just gotten to the point we were ready to cut our losses." (Tr. at 54).

May 1, 2020 in the amount of $165,870.42. (Ex. 14 at 1). Other deposits that month totaled $966,217.48, including a wire transfer from Global Merchant Cash, Inc. ("Global") in the amount of $266,470.00 on May 28, 2020. (Ex. 14 at 2). These funds were the proceeds from a business loan obtained by Castlerock and personally guaranteed by Hall and Warriner.[13] (Tr. at 98-99). The procurement of this loan indicates that Castlerock was experiencing cash-flow problems at this time. Hall wrote checks that month totaling $770,554.53; withdrawals by electronic transfer totaled $75,998.03; and there was a service charge of $16.92. (Ex. 14 at 3). Castlerock ended the month with a balance of $373,314.52.[14] Had Castlerock not deposited into the account the net proceeds from the sale or the proceeds from the Global loan, the balance at the end of May 2020 would have been [-$59,025.90]. ($373,314,52 − $165,870.42 − $266,470.00 = [$59,025.90]). With the deposits of the sale and loan proceeds, the lowest daily balance was $40,012.49 on May 20, 2020. (Ex. 14). As of that date, Castlerock had spent $125,857.93 of the total sales proceeds ($165,870.42 − $40,012.49 = $125,857.93).

An examination of the checks signed by Hall in May 2020 reveals that within a week after the deposit of the $165,870.42 check from the first sale, Hall wrote checks to himself totaling $16,000.00, including a check in the amount of $5,000.00 dated May 1, 2020 (Check #18125, Ex. 14 at 7), $6,000.00 dated May 5, 2020 (Check #18136, Ex. 14 at 8), and $5,000.00 dated May 8, 2020 (Check #18159, Ex. 14 at 10). Hall testified that he was not otherwise employed, and he characterized these payments as "draws" from the business. (Tr. at 112). On May 1, 2020, Hall wrote a check to L&W Supply Corporation, a supplier of sheetrock, in the amount of $13,601.42. (Check #18132, Ex. 14 at 8). That payment is relevant, according to Charter 3, because Hall and

[13] Although the specific date that Warriner executed the personal guaranty is unknown, it is notable that Global funded the loan eight days after Warriner's purported withdrawal from Castlerock. *See infra* p. 15.
[14] $373,314.52 = ($87,796.10 + $165,870.42 + $966,217.50) – ($770,554.53 + $75,998.03 + $16.92). (Ex. 14).

Warriner had signed an agreement in 2019 personally guaranteeing Castlerock's debt to L&W Supply Corporation. (Charter Ex. 38; Tr. at 84-85). Moreover, Hall wrote four checks to Pullen Windows & Doors in the amount of $8,000.00 totaling $32,000.00, including checks dated May 1, 2020 (Check #18090, Ex. 14 at 5); May 8, 2020 (Check #18113), May 15, 2020 (Check #18146, Ex. 14 at 6), and May 22, 2020 (Check #18174, Ex. 14 at 11). According to Charter 3, those payments are relevant because Warriner held an ownership interest in Pullen Windows & Doors. (Ex. 37 at 7; Tr. at 166-67).

July 2020 Bank Statement

The bank statement for July 2020 shows that Castlerock ended the month of June 2020 with $1,168.43. (Ex. 21 at 1). As of that date, therefore, Castlerock had spent $164,701.99 of the total sales proceeds from the first sale ($165,870.42 − $164,701.99 = $1,168.43). The checks from the second and third sales were deposited on July 9 and 27, 2020 in the respective amounts of $89,511.30 and $255,915.64. (Ex. 21 at 1). During the month of July 2020, other deposits totaled $518,826.00. Hall wrote checks totaling $689,948.59; withdrawals by electronic transfer totaled $91,795.63, and BankFirst charged $72.00 in insufficient funds fees and a service charge of $25.86. (Ex. 21). Castlerock ended the month with a balance of $83,651.29.[15] (Ex. 21 at 1). The lowest daily balance was [-$5,302.20] on July 1, 2020. (Ex. 21 at 3).

During that month, Castlerock paid Global $43,552.96 by electronic transfer in four installments of $10,838.24.[16] (Ex. 21 at 2). According to Charter 3, these withdrawals are relevant because they reduced Hall's and Warriner's personal liability given that they had guaranteed

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[15] $83,651.29 = ($89,511.30 + $255,915.64 + $518,826.00) – ($689,948.59 + $91,795.63 + $25.86).

[16] The chapter 7 trustee in Castlerock's bankruptcy case initiated an adversary proceeding to avoid these payments to Global as well as other payments made by Castlerock in other months as preferential transfers under § 547. *See Henderson v. Global Merch. Cash, Inc*., Adv. Proc. 21-00011-JAW (Bankr. S.D. Miss. Oct. 7, 2021). A default judgment in the amount of $108,382.40 was entered against Global on January 1, 2022, and the adversary has been closed.

repayment of the loan. (Tr. at 99-100). A review of the checks signed by Hall shows that he wrote three checks to himself totaling $700.00 on July 6, 2020 (Check #18361, Ex. 21 at 7), July 14, 2020 (Check #18377, Ex. 21 at 8), and July 21, 2020 (Check #18395, Ex. 21 at 10). On July 6, 2020, he wrote a check in the amount of $16,000.00 to Pullen Windows & Doors, a company in which Warriner held an interest. (Check #18334, Ex. 21 at 5). Hall also wrote a check in the amount of $4,919.97 to L&W Supply on July 24, 2020. (Check #18414, Ex. 21 at 11). As noted previously, Hall and Warriner had personally guaranteed repayment of that debt. Despite beginning the month of August 2020 with $83,651.29, Castlerock ended that month with a balance of [- $1,650.76]. (Ex. 28). Unsurprisingly, Castlerock, Hall, and Warriner filed bankruptcy in late September 2020. Hall admitted at Trial that he spent the net sales proceeds on himself and other creditors during the months of May, June, and July of 2020. (Tr. at 118).

> Q. [I]f you look at how Charter 3's money was spent, what we see here is that you intended to pay a lot of other people with Charter 3's money, including yourself, right?
>
> A. Right.

(Tr. at 118).

Charter 3's Demands for Payment

As to the sale of the first house, Warriner told Bracken the date of the closing and informed him that Hall would contact him later about Charter 3's payment from the net sales proceeds. (Tr. at 33). Bracken signed the deed conveying Lot Q-8 to Castlerock on April 15, 2020. On April 30, 2020, Bracken called and texted Hall on multiple occasions to inquire when Castlerock intended to pay Charter 3. (Tr. at 49). "[T]he less he communicated, the more I tried to reach out to him." (Tr. at 49). Even though Warriner, not Hall, had attended the first closing on the sale of the house on Lot Q-8, Bracken's attempts to obtain the funds were aimed mostly at Hall, not Warriner. (Tr.

at 31, 33). Bracken testified that he spoke with Warriner mostly about the construction of the houses and usually contacted Hall about "the accounting side of" the business. (Tr. at 13-14).

Sometime after the first closing but well before the second closing on July 9, 2020, Warriner informed Hall that he intended to resign as a managing member of Castlerock. (Tr. at 151, 160). Warriner testified that although he and Hall had worked together for roughly 25 years, "it was just time to move [in] a different direction in my life. I was ready to do something else and spend more time with my family because I still have kids." (Tr. at 153, 160). Warriner delivered a typed letter to Hall notifying him that "effective May 22, 2020, I, Charlie Warriner . . . voluntarily withdraw[ ] and cease[] to be a managing member of Castlerock." (Ex. 35). Warriner's signature appears half-way down the page. Hall did not sign the letter or any other document giving his written consent to Warriner's resignation.[17] (Tr. at 95).

On June 18, 2020, Hall filed the Certificate of Amendment with the Mississippi Secretary of State's Office changing Castlerock's registered agent from Warriner to himself and removing Warriner's name as a co-manager of the company. (Ex. 36; Tr. at 151). Warriner, however, knowingly and voluntarily remained as an authorized signatory on Castlerock's account at BankFirst. This fact raises an issue whether Warriner stayed involved in the company after his alleged resignation, which is discussed in more detail later. Neither Hall nor Warriner informed Bracken of Warriner's purported resignation. Because Bracken communicated almost exclusively with Hall about the proceeds from the sales of the houses, he would not have noticed Warriner's absence from the business.

Nearly two months after the closing on Lot Q-8, Castlerock still had not remitted any funds to Charter 3. (Tr. at 35). Bracken began to become impatient with Hall. He nevertheless signed the

[17] Although Warriner purportedly resigned as a "managing member" and not as a "member," Charter 3 does not dispute Warriner's intent to resign as both.

deed conveying Lot Q-5 to Charter 3 on June 29, 2020. On Wednesday, July 8, 2020, the day before the scheduled second closing, Bracken texted Hall, "Hey Jerry, when do you think we can settle up on Q-8?" (Ex. 16, Bates #66).[18] Hall replied by text, "Hey, Jeff, will have it finished up over the weekend. Will get with you Monday." (Ex. 16, Bates #66). That Monday, July 13, 2020, Hall did not contact Bracken. (Tr. at 36). Bracken testified that if Hall or Warriner had informed him that Castlerock did not intend to remit the sale proceeds from the first closing to Charter 3, he would not have moved forward with the second or third closings. (Tr. at 35).

The second closing took place as scheduled on July 9, 2020. Hall, not Warriner, attended that closing on Castlerock's behalf. (Tr. at 70). Castlerock's operating account shows a deposit of $89,511.30 on that date. (Ex. 21). As noted previously, Hall did not contact Bracken on Monday, July 13, 2020, although he had texted him that he would. (Tr. at 36). Two days later, Wednesday, July 15, 2020, Bracken texted Hall, "Hey Jerry, checking in with you about Q-8." (Ex. 16, Bates #65). Hall did not immediately respond.

Bracken became so worried that he delayed signing the quitclaim deed to Lot Q-3. Castlerock's real estate agent told him, "[L]ook man, I've been working with these guys for years . . . .[T]his is just how they roll. You got to stay on them, you got to stay after them. They're going to pay you." (Tr. at 51). On July 24, 2020, the same date as the third closing, Bracken reluctantly signed the deed conveying Lot Q-3 to Castlerock.

More than a week after Bracken's previous text, Hall wrote Bracken on July 24, 2020, "Hey, Jeff, can we meet next Tuesday a[t] 2:30 at your office[?]" (Ex. 16, Bates #65). Bracken replied that same day, "10-4." (Ex. 16, Bates #65). Next Tuesday was July 28, 2020. That meeting in Bracken's office did not occur. (Tr. at 36).

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[18] Because Exhibit 16 consists of several unnumbered pages, citations include the Bates stamp that appears at the bottom of each page.

After the third closing, Bracken became more persistent in demanding payment from Hall who, according to Bracken, "kept kicking the can down the road." (Tr. at 46). At some point, Bracken even attempted to contact Warriner, but Warriner's telephone number had been disconnected. (Tr. at 49). Net sales proceeds of $255,915.64 were deposited into Castlerock's account on Monday, July 27, 2020. (Ex. 21). That same day, Bracken and Hall exchanged the following text messages:

B: Any way you could make 1:30? Chris [Bracken] leaves at 2:00.

H: I think so.

B: 10-4.

(Ex. 16, Bates #65). On Tuesday, July 28, 2020, Hall texted Bracken, "Hey, Jeff, I can't meet at 1:30 today. I can meet at 1:30 Thursday afternoon. I will send you the printout later today so you can look over it." (Ex. 16, Bates #65). On July 29, 2020, the day before their scheduled meeting, Bracken and Hall exchanged the following text messages:

B: Did you get that worksheet done?

H: I will send it this afternoon.

B: 10-4.

(Ex. 16, Bates #64). The meeting scheduled for July 30, 2020 did not take place. (Tr. at 61). Instead, in an email dated that same day, Hall wrote to Bracken, "Good morning Jeff, Lot Q-8 spreadsheet is attached. I will put you a check in the mail. Please send me your mailing address. Jerry." (Ex. 17). Hall sent this email only fifty-five days before he commenced Castlerock's bankruptcy case. (Case No. 20-02453-JAW, Bankr. Dkt. #1). As of July 30, 2020, Castlerock's operating account had a balance of $104,591.15, which was far less than the net sale proceeds of $165,870.42 from the first closing and the total net sales proceeds of $511,297.36 deposited into the account.

(Ex. 21). Simply put, Hall did not have the funds to pay Charter 3 on July 30, 2020, and any pretense that he was going to pay Charter 3 $165,870.42 was false.

Bracken texted Hall his mailing address on August 3, 2020. (Ex. 16, Bates #64). Hall testified that he did not mail the check "because I was still waiting to hear from Jeff [Bracken] to make sure he was okay with the check." (Tr. at 34, 90). According to Hall, Bracken called him asking about the costs shown on the spreadsheet attached to the email dated July 30, 2020. (Tr. at 90). Hall testified that he ended their telephone conversation with a request that Bracken send him a copy of an earlier spreadsheet. (Tr. at 90).

In summarizing his discussions with Hall, Bracken testified, "[H]e never, never said you're not going to get paid. He just would always have some excuse of to why he didn't have everything together or why he couldn't pay me right at that moment, but always assured that we were going to get paid." (Tr. at 42). Bracken also testified that if he had known that Castlerock intended to deposit the sales proceeds into its general business account and use the funds to pay other expenses, he "probably" would not have signed the deeds conveying the lots to Castlerock and "absolutely" would have attended the closings to protect Charter 3's interests. (Tr. at 47-48). It is undisputed that Castlerock should have paid Charter 3 $511,297.36. (Tr. at 49; Exs. 3, 4, 34).

Bankruptcy Filings

On September 22, 23, and 24, 2020, Warriner, Castlerock, and Hall filed separate petitions for relief under chapter 7 of the Bankruptcy Code. (Warriner Bankr. Dkt. #1; Case No. 20-02453-JAW, Bankr. Dkt. #1; Hall Bankr. Dkt. #1). The bankruptcy schedules in all three bankruptcy cases list the same business debts. (Tr. at 157).

Warriner Case—Filed September 22, 2020

Warriner and his spouse (together, the "Warriners") commenced their chapter 7 bankruptcy case first on September 22, 2020. In their bankruptcy schedules, they listed assets of $1,926.636.00 and liabilities of $11,248,714.82, including unsecured debts totaling $9,772,360.34. (Warriner Bankr. Dkt. #48 at 1). Among their unsecured creditors, the Warriners identified 134 individuals/couples who had purchased homes from Castlerock. (Warriner Bankr. Dkt. #53; Cl. #2-3; Cl. #4-1). The Warriners identified Charter 3 as an unsecured creditor with a claim of $511,297.36 and initially did not schedule the claim as contingent, unliquidated, or undisputed. They later amended their bankruptcy schedules to change the status of Charter 3's claim to disputed. (Ex. 1). Charter 3 filed a proof of claim in the amount of $511,297.36. (Ex. 3). The chapter 7 trustee in Warriner's bankruptcy case concluded that no estate property was available for distribution to creditors over and above that exempted by law.

Castlerock Case—Filed September 23, 2020

Hall signed the petition for relief commencing Castlerock's chapter 7 bankruptcy case on September 23, 2020. (Case No. 20-02453-JAW, Bankr. Dkt. #1). In its bankruptcy schedules signed by Hall, Castlerock listed assets of $6,622,081.00 and liabilities of $10,893,603.25, including unsecured debts of $3,036,637.25. (Case No. 20-02453-JAW, Bankr. Dkt. #4 at 2). Castlerock listed its BankFirst account as an asset of the estate having a $0.00 balance. (Case No. 20-02453-JAW, Bankr. Dkt. #4 at 3). Castlerock identified Charter 3 as an unsecured creditor with a claim of $511,297.36 and did not schedule the claim as contingent, unliquidated, or disputed. (Case No. 20-02453-JAW, Bankr. Dkt. #4 at 23). As noted previously, the creditors listed in Castlerock's bankruptcy schedules also appear in the schedules of the Warriners and Hall.

Hall Case—Filed September 24, 2020

Hall commenced his chapter 7 bankruptcy case on September 24, 2020. In his bankruptcy schedules, Hall listed assets of $394,750.00 and liabilities of $9,923,942.25, including unsecured debt of $9,635.942.25. (Hall Bankr. Dkt. #3 at 1). Among his unsecured creditors, he listed 134 individuals/couples who had purchased homes from Castlerock. (Hall Bankr. Dkt. #38; Cl. #2-3; Cl. #4-1). Hall's treatment of Charter 3's claim was similar to that of the Warriners. Hall identified Charter 3 as an unsecured creditor with a claim of $511,297.36 and initially did not schedule the claim as continent, unliquidated, or disputed but later amended his bankruptcy schedules to change the status of the claim to disputed. (Ex. 2). Charter 3 filed a proof of claim in the amount of $511,297.36. (Ex. 4). The chapter 7 trustee in Hall's bankruptcy case concluded that no estate property was available for distribution to creditors over and above that exempted by law.

Adversary Proceedings

Charter 3 filed the Adversary Complaints against Hall and Warriner alleging that they are individually liable for $511,297.36 and that the debt is non-dischargeable in their individual bankruptcy cases under § 523(a). Charter 3 contends that the debt was obtained by false pretenses, a false representation, and/or actual fraud, § 523(a)(2)(A); the debt resulted from fraud or defalcation while acting in a fiduciary capacity, § 523(a)(4); and Hall and Warriner caused "willful and malicious injury" to Charter 3, § 523(a)(6).[19] Charter 3 alleged that Hall and Warriner admitted the amount of the debt in their bankruptcy schedules "as set forth in Charter 3's Proof of Claim." (Hall Adv. Dkt. #1 at 4; Warriner Adv. Dkt. #1 at 4).

[19] Charter 3 did not initiate an adversary proceeding against Castlerock. A corporate chapter 7 debtor is not entitled to receive a discharge. 11 U.S.C. § 723(a)(1).

Hall and Warriner filed the Responses denying individual liability and any wrongdoing that would justify an exception to discharge. (Hall Adv. Dkt. #9; Warriner Adv. Dkt. #9). They seek an award of attorney's fees and costs in the Responses.

Objections to Proofs of Claim

Just before Trial, Hall and Warriner filed the Objections to Proofs of Claim arguing that Charter 3's proof of claim "does not reflect any personal guaranty, or other personal obligation to Charter 3." (Hall Bankr. Dkt. #37; Warriner Bankr. Dkt. #60). At a status conference on December 6, 2021, the parties agreed to consolidate the Objections to Proofs of Claim with the Adversary Proceedings. The Court thereafter entered an order reflecting the consolidation. (Hall Bankr. Dkt. #35; Warriner Bankr. Dkt. #61; Hall Adv. Dkt. #36; Warriner Adv. Dkt. #39).

Discussion

A central purpose of the Bankruptcy Code is to relieve "the honest debtor from the weight of oppressive indebtedness." *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934). This policy of affording relief only to the honest-but-unfortunate debtor is embraced in § 523(a), which excepts from discharge certain debts acquired by the less than honest debtor. *Grogan v. Garner*, 498 U.S. 279, 286-87 (1991). In its post-trial briefs, Charter 3 invokes five of the exceptions to discharge enumerated in § 523(a), including that the debt was obtained by false pretenses, § 523(a)(2)(A), and/or by actual fraud, § 523(a)(2)(A); the debt resulted from a fiduciary defalcation, § 523(a)(4), and/or embezzlement, § 523(a)(4), and/or the debt arose from a willful and malicious injury, § 523(a)(6). Charter 3 need prove the applicability of only one of these exceptions to prevail in its nondischargeability claim. The standard of such proof is a preponderance of the evidence. *Grogan*, 498 U.S. at 291; FED. R. BANKR. P. 4005. Because of the considerable consequences to a debtor who fails to achieve discharge, "exceptions to discharge must be strictly construed against a

creditor and liberally construed in favor of a debtor." *Hudson v. Raggio & Raggio, Inc. (In re Hudson)*, 107 F.3d 355, 356 (5th Cir. 1997).

Charter 3 initiated the Adversary Proceedings against Hall and Warriner prior to any determination of their personal liability. (Hall Adv. Dkt. #42 at 5; Warriner Adv. Dkt. #48 at 5). Before reaching the merits of Charter 3's nondischargeability claims, the Court thus must consider as a preliminary matter their argument that they cannot be held personally liable for a debt owed by Castlerock. *Morrison v. W. Builders of Amarillo, Inc. (In re Morrison)*, 555 F.3d 473, 478-80 (5th Cir. 2009).

A. Personal Liability of Hall and/or Warriner for Castlerock's Debts

Castlerock's liability to Charter 3 for its failure to remit the net proceeds is undisputed; the issue is the personal liability of Hall and Warriner. As Hall and Warriner strenuously point out, they signed the Joint Venture Agreements only in their capacities as members of Castlerock, a limited liability company ("LLC").

LLCs did not exist in Mississippi until 1994 when it was created by statute. *Bluewater Logistics, LLC v. Williford*, 55 So. 3d 148, 159 (Miss. 2011). An LLC is analogous to a corporation but is owned by "members" rather than shareholders and is run by "managers" rather than officers and directors. MISS. CODE ANN. § 79-29-305. It is well settled that an LLC falls within the Bankruptcy Code's definition of a corporation. 11 U.S.C. § 101(9)(A); 2 COLLIER ON BANKRUPTCY ¶ 101.09 (16th ed. 2021) (reasoning that the protection afforded members renders an LLC a "corporation" within the meaning of § 101(9)(A)).

Corporations are treated as "persons" under the law for most purposes but can only act through natural persons, typically the corporation's directors and officers. *See Citizens United v. Fed. Election Comm'n*, 558 U.S. 310 (2010). Those individuals are generally immune from personal liability

for the corporation's obligations and debts, but their immunity is not unlimited. Officers and directors of a corporation may not escape personal liability when they "have some direct, personal participation in the tort, as where the defendant was the 'guiding spirit' behind the wrongful conduct . . . or the 'central figure' in the challenged corporate activity." *Mozingo v. Correct Mfg. Corp.*, 752 F.2d 168, 174 (5th Cir. 1985).

Although corporations and LLCs are different business forms, the liability rules that apply to officers and directors are similar to those that apply to members and managers of LLCs. Mississippi has defined such liability statutorily.

> [T]he debts, obligation and liabilities of a limited liability company, whether arising in contract, tort or otherwise, shall be solely the debts, obligation and liabilities of the limited liability company, and no member, manager or officer of a limited liability company shall be obligated personally for any such debt, obligation or liability of the limited liability company solely by reason of being a member, acting as a manager or acting as an officer of the limited liability company.

MISS. CODE ANN. § 79-29-311(1). Hall and Warriner are thus correct that they cannot be held personally liable for the debts of Castlerock based solely on their status as members of the LLC. (Hall Adv. Dkt. #42 at 5; Warriner Adv. Dkt. #48 at 5). But Charter 3 is equally correct that the statute does not immunize Hall and Warriner from the legal consequences of their own acts or omissions. (Hall Adv. Dkt. #43 at 13-15; Warriner Dkt. #49 at 13-15).

For example, in *Lancaster v. Miller*, 319 So. 3d 1174, 1175 (Miss. Ct. App. 2021), Jan Macko ("Macko") and her daughter Andrea Miller ("Miller") sold a house that was titled in the name of Macko's limited liability company, Magnolia Properties and Remodel LLC ("Magnolia LLC"). Soon after moving into the house, the buyers discovered numerous problems and sued Magnolia LLC as well as Macko and Miller individually for breach of contract and fraud. The trial court granted Macko and Miller summary judgment on the ground they were protected from liability under the LLC's "corporate shield." On appeal, the Mississippi Court of Appeals reversed, ruling

that a member of an LLC can be held personally liable for his own tortious actions, including fraud. *Id*. at 1184.

In short, if the Court concludes that Hall and/or Warriner committed false pretenses or actual fraud, then one or both may be personally liable for the damages resulting to Charter 3. Similarly, to the extent that the Court concludes that Charter 3 has been damaged by a breach of fiduciary duty and defalcation by Hall and/or Warriner, their embezzlement, or their willful and malicious misconduct, one or both may be personally liable to Charter 3. There is one wrinkle in the analysis of Warriner's personal liability—his alleged resignation "as a managing member of Castlerock," the import of which is ironed out below. The Court begins its analysis with Charter 3's claim under § 523(a)(2)(A).

B. § 523(a)(2)(A)

Charter 3 alleges that the debt should be declared nondischargeable because Hall and Warriner falsely represented that Castlerock would reimburse Charter 3 for its costs from the net sales proceeds received at the closings before taking any "profits." (Hall Adv. Dkt. #43 at 17; Warriner Adv. Dkt. #49 at 17). Charter 3 cites § 523(a)(2)(A), which provides that a discharge in a chapter 7 case "does not discharge an individual from any 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." 11 U.S.C. § 523(a)(2)(A).

The post-trial briefs do not address the exception in subparagraph (A) of § 523(a)(2) for "a statement respecting the debtor's . . . financial condition." Whether that exception applies is important because a materially false statement respecting a "debtor's . . . financial condition" is excepted from discharge under § 523(a)(2)(B), not § 523(a)(2)(A), and then only if that statement

was in writing. The U.S. Supreme Court has construed the phrase "a statement respecting the debtor's . . financial condition" in § 523(a)(2)(B) to apply to any statement that has "a direct relation to or impact on the debtor's overall financial status." *Lamar, Archer & Cofrin, LLP v. Appling*, 138 S. Ct. 1752, 1761 (2018). Here, the allegedly false statements of Hall and Warriner are not statements "respecting" Castlerock's "financial condition" but instead are statements about their intent to remit the sales proceeds to Charter 3. Because their alleged fraudulent statements suggest nothing about Castlerock's ability to pay Charter 3, they do not "respect" Castlerock's financial condition, and the dischargeability issue properly focuses on subparagraph (A) of § 523(a)(2).

Subparagraph (A) encompasses three independent but overlapping grounds for non-dischargeability—false pretenses, a false representation, and actual fraud—all of which apply to "debts obtained by frauds involving moral turpitude or intentional wrong." *First Nat'l Bank LaGrange v. Martin (In re Martin)*, 963 F.2d 809, 813 (5th Cir. 1992). A creditor need only prove one of the three grounds to render the debt nondischargeable under § 523(a)(2)(A).

In its post-trial briefs, Charter 3 premises its § 523(a)(2)(A) claim on two prongs of the statute—false pretenses and actual fraud. (Hall Adv. Dkt. #43 at 16-17; Warriner Adv. Dkt. #49 at 16-17). There is a distinction between the elements of proof required for false pretenses and those required for actual fraud. *AT&T Universal Card Servs. v. Mercer (In re Mercer)*, 246 F.3d 391, 402-03 (5th Cir. 2001); *RecoverEdge L.P. v. Pentecost*, 44 F.3d 1284, 1292-93 (5th Cir. 1995). This distinction "appears to be a chronological one, resting upon whether a debtor's representation is made with reference to a future event, as opposed to a representation regarding a past or existing fact." *Barvié v. Broadus (In re Broadus)*, 516 B.R. 378, 386 (Bankr. S.D. Miss. 2014) (citation omitted).

Charter 3 supports its § 523(a)(2)(A) claim for false pretenses and actual fraud with the same factual allegations. In general, Charter 3 asserts that Hall and Warriner falsely and dishonestly represented to Charter 3, both before and after they signed the Joint Venture Agreements, that Castlerock would reimburse it for its costs from the net sales proceeds. In other words, Charter 3 contends that Hall and Warriner knew when they signed the Joint Venture Agreements in 2018 and when Charter 3 conveyed the lots to Castlerock in 2020 that they intended to use the net sales proceeds for purposes other than to pay Charter 3.

1. False Pretenses

A debt is nondischargeable if the creditor shows that the debtor's representations or pretenses were "(1) knowing and fraudulent falsehoods, (2) describing past or current facts, (3) that were relied upon by the other party." *Allison v. Roberts (In re Allison)*, 960 F.2d 481, 483 (5th Cir. 1992). A false pretense involves an implied misrepresentation or conduct intended to create and foster a false impression. *See NextGear Capital, Inc. v. Rifai (In re Rifai)*, 604 B.R. 277, 307 (Bankr. S.D. Tex. 2019). Unlike a false representation, a false pretense does not require an overt misrepresentation and may be based on misleading conduct alone. *Demory v. Martin (In re Martin)*, 630 B.R. 766, 783 (Bankr. S.D. Miss. 2021). "[M]ost times both conduct and explicit statements by the debtor exist, thereby establishing a fraud under both false pretenses and false representation." *Argento v. Cahill (In re Cahill)*, No. 15-72418, 2017 WL 713565, at *6 (Bankr. E.D.N.Y. Feb. 27, 2017). A debtor's silence regarding a material fact may qualify as a false pretense. *Selenberg v. Bates (In re Selenberg)*, 856 F.3d 393, 399 (5th Cir. 2017).

A debtor's promise related to a future action cannot be defined as a false pretense unless it depicts a current or present fact. *Bank of La. v. Bercier (In re Bercier)*, 934 F.2d 689, 692 (5th Cir. 1991). Even if a debtor's subsequent breach of contract is unjustified, a promise related to a future

action cannot qualify as a false pretense. 4 COLLIER ON BANKRUPTCY ¶ 523.08[1][d] (16th ed. 2021). A misrepresentation of the debtor's intention to perform contractual duties, however, may be a false pretense if the debtor had no intention of performing any of the obligations under the contract at the time it was made. *Allison*, 960 F.2d at 484.

Moreover, a false pretense must have been relied upon by the creditor. The creditor's reliance need only be justifiable. *Field v. Mans*, 516 U.S. 59, 77 (1995). The creditor is justified in relying on a false pretense even if he might have ascertained the truth through further investigation "unless its falsity is obvious or there are 'red flags' indicating such reliance is unwarranted." *In re Mercer*, 246 F.3d at 417-18.

a. When Joint Venture Agreements Were Signed in 2018

As one would expect, both Hall and Warriner testified that they did not intend to deceive Bracken into signing the Joint Venture Agreements in 2018. (Tr. at 91, 159). A debtor's testimony, however, is not the only way to establish his fraudulent intent. Here, Charter 3 relies on proof of Castlerock's worsening financial condition as circumstantial evidence that Hall and Warriner deliberately misled Bracken about their intent to reimburse Charter 3 for its costs. To that end, Charter 3 points to Castlerock's bankruptcy schedules listing liabilities of $10,893,603.25 and assets of only $6,622,081.00. (Case No. 20-02453-JAW, Bankr. Dkt. #4).

A review of the docket, however, reveals that Castlerock filed its petition for relief and its schedules on September 23, 2020, more than two years after Bracken signed the Joint Venture Agreements on Charter 3's behalf. (Case No. 20-02453-JAW, Bankr. Dkt. #1). The Court, therefore, finds that the schedules are not necessarily illustrative of Castlerock's financial condition when Bracken signed the Joint Venture Agreements.

The Court also rejects the suggestion raised by Charter 3 at Trial, but not in its post-trial briefs, that Hall and Warriner purposely structured the joint ventures so that the checks were made payable only to Castlerock rather than to both Castlerock and Charter 3. Bracken testified that he, not Hall or Warriner, requested that Charter 3 quitclaim the lots to Castlerock "in a simultaneous conveyance" to avoid any warranty obligations under state law. (Tr. at 20, 108).

Finally, the proof at Trial regarding the alleged wrongdoing of Hall and Warriner focused mostly on events that occurred contemporaneously with the closings of the sales. Except for testimony regarding how the parties met, why Charter 3 chose Castlerock to build the spec houses, and the terms and conditions of the Joint Venture Agreements, there was no evidence suggesting that either Hall or Warriner entered into a business relationship with Charter 3 in 2018 with the intent of depriving Charter 3 of the net sales proceeds in 2020. Hall's and Warriner's promise to perform the obligations in the Joint Venture Agreement is not a false representation merely because they later breached that promise. *See Allison*, 960 F.2d at 484. Moreover, assuming that Charter 3 is correct that Hall and Warriner duped Bracken in 2020, such evidence does not support an inference that Hall and Warriner never intended to comply with the Joint Venture Agreements in 2018. A promise to perform later does not constitute a false pretense unless at the time the promise was made, the debtor knew full well that he had no intention of performing the future act. *Mercer*, 246 F.3d at 407-08.

The Court, therefore, finds that Charter 3 has not met its burden of proving that either Hall or Warriner fraudulently induced Bracken to sign the Joint Venture Agreements in 2018. In the absence of an intent to deceive, it is unnecessary for the Court to consider whether Charter 3's reliance was justifiable. Charter 3's nondischargeability claim against Hall and Warriner based on the

assertion that it was induced to sign the Joint Venture Agreements by false pretenses fails without evidence of fraudulent intent.

b. When Lots Were Conveyed in 2020

Bracken alleges that after Castlerock finished building the spec houses, Hall and Warriner lied to him about their intent to remit the sales proceeds to Charter 3 to induce him to sign the quitclaim deeds. Bracken signed the quitclaim deeds a few days or weeks before the closings of the houses on Lots Q-8, Q-5, and Q-3 on April 30, July 9, and July 24, 2020, and the net proceeds from the sales were deposited into Castlerock's operating account in the amounts of $165,870.42 on May 1, 2020; $89,511.30 on July 9, 2020; and $255,915.64 on July 29, 2020. It is undisputed that the joint ventures were not profitable, that Castlerock should have remitted the net sales proceeds in their entirety to Charter 3 to reimburse it for its costs, and that Castlerock used the proceeds for other purposes without Bracken's knowledge or consent. The speed at which the funds were spent indicates that Hall and Warriner intended to do so all long. The bank statements from Castlerock's operating account are circumstantial evidence that they had no intent to remit the funds when the closings took place. (Exs. 14, 21, 28).

Castlerock's bank statements show that when the first sale occurred on April 30, 2020, the business was struggling to pay its expenses and never regained its financial footing. In their post-trial briefs, Hall and Warriner attributed Castlerock's financial problems to "market conditions" without further elaboration. (Hall Adv. Dkt. #42 at 4; Warriner Adv. Dkt. #48 at 4). The exact reasons for Castlerock's demise are unknown, but if the sales of the spec houses are any indication, the business simply was not profitable. A comparison of the estimated costs of construction versus the actual costs suggests either that the construction costs, including the price of the lots, were too high or the sales prices were too low. For example, the estimated construction costs for the house

built on Lot Q-8 were $588,972.34 (Ex. 12, Bates, #161-68), but the actual costs were $755,284.00 (Ex. 3 at Ex. 2) and the house sold for $700,000.00 (Ex. 13). Similarly, the estimated costs for the houses built on Lots Q-5 and Q-8 were $578,793.34 (Ex. 19, Bates #126) and $582,893.34 (Ex. 27, Bates #89), respectively, but the actual costs were $595,374.73 and $698,895.06 (Ex. 3 at Ex. 2) and the houses sold for $589,800.00 and $669,000.00 (Exs. 20, 26). By July 1, 2020, Castlerock's operating account had a balance of [-$5,302.20]. (Ex. 21). There was a pattern of overdraft and returned-item charges beginning in June 2020. In all, Castlerock incurred seventeen insufficient fund charges totaling $612.00 through August 2020. (Ex. 28). Castlerock ceased operations and filed bankruptcy on September 23, 2020. (Case No. 20-02453-JAW, Bankr. Dkt. #1; Hall Adv. Dkt. #42 at 4). Against this backdrop of Castlerock's downward financial spiral, the Court considers the conduct of Hall and Warriner separately.

i. Hall

Charter 3 points to Hall's text messages to Bracken as circumstantial evidence of his fraudulent state of mind. (Tr. at 87). Bracken's demands to Hall via text messages to turn over the proceeds began on July 8, 2020, between the first and second closings. Prior to that first text message, Bracken signed the deed conveying Lot Q-5 to Charter 3 on June 29, 2020 in anticipation of the second closing on July 9, 2020. On July 8, 2020 Bracken sent Hall a text message inquiring about "settl[ing] up" the sale proceeds from the first closing. (Ex. 16, Bates #66). Unbeknownst to Bracken, those sales proceeds of $165,870.42 had already been spent. Although net sales proceeds of $165,870.42 had been deposited into Castlerock's operating account on May 1, 2020, Castlerock's operating account had a balance of [-$5,302.20] on July 1, 2020. (Ex. 21 at 3). On July 8, 2020, the date of Bracken's text message, the account had a balance of only $19,869.06, which was still far less than the deposited funds from the first closing necessary to pay Charter 3. (Ex.

21). Hall responded to Bracken's text message, "Hey, Jeff, will . . . get with you on Monday." (Ex. 16, Bates #66). That Monday was July 13, 2020, and according to the bank statements, Charter 3's money had already been spent.

The second closing took place on July 9, 2020 as scheduled, and $89,511.30 in net proceeds from the sale of the house on Lot Q-5 were deposited into Castlerock's operating account that same day. With that second deposit, Castlerock should have remitted total net sales proceeds of $255,381.42 to Charter 3 but did not. Hall did not "get with" Bracken on Monday, July 13, 2020. On that date, the operating account had a balance of only $42,321.03. On Wednesday, July 15, 2020, Bracken texted Hall, "Hey Jerry, checking in with you about Q-8." (Ex. 16, Bates #65). A week passed without any response from Hall. Then, early on the morning of July 24, 2020, Hall responded, "Hey, Jeff, can we meet next Tuesday a[t] your office[?]" (Ex. 16, Bates #65). Later that same day, Bracken signed the deed conveying Lot Q-3 to Castlerock, and the third closing took place as scheduled. On July 27, 2020, net sales proceeds of $255,915.64 were deposited into the account from the third closing. (Ex. 21). After that third deposit, Castlerock should have re-mitted total net proceeds of $511,297.36 to Charter 3 but did not. The meeting on Tuesday, July 28, 2020 did not occur.

These text messages between Bracken and Hall reveal a course of evasive conduct by Hall which Bracken aptly described at Trial as "kicking the can down the road." (Tr. at 46). Hall never revealed to Bracken that Castlerock had spent the net sales proceeds and there was no evidence that Hall attempted to replenish any of the spent funds from his own sources. Then, on July 30, 2020, Hall sent Bracken an email stating, "I will put you a check in the mail." (Ex. 17). On that date, the operating account had a balance of $104,591.15, but Charter 3 was entitled to

$511,297.36. (Ex. 17). As Hall admitted at Trial, Charter 3 did not receive "one red cent" of the net sales proceeds. (Tr. at 118).

Hall was Castlerock's accountant; he reconciled its operating account; and he signed all checks drawn on the account. In May 2020, Hall and Warriner personally guaranteed a business loan over the internet from Global. A bank statement shows a wire transfer from Global of $266,470.00 on May 28, 2020. (Ex. 14 at 2). Without those loan proceeds, Castlerock would have ended the month of May 2020 with a balance of $106,844.52, which is $59,025.90 less than the amount of the net sale proceeds from the first closing. ($373,314.52 − $266,470.00 = $106,844.52 and $106,844.52 − $165,870.42 =[-$59,025.90]) (Ex. 28). In other words, Castlerock had already spent $59,025.90 of Charter 3's funds. Each month's lowest daily balance shows a steady decline in funds in the account: $40,012.49 on May 20, 2020; $1,168.43 on June 30, 2020; [-$5,302.20] on July 1, 2020; and [-$1,737.72] on August 17, 2020. (Ex. 28). For certain, without the use of Charter 3's funds, these amounts would have been significantly less, and the account would have reached a negative balance sooner.

Although Hall testified on cross-examination that "we fully intended to" pay Charter 3, he did not explain why Castlerock was entitled to use the funds for its own purposes or how Castlerock planned to pay Charter 3 if not from the sales proceeds. (Tr. at 87). Hall's admission that he made no effort to safeguard any of the funds to remit to Charter 3, supports an inference that he had no intention of ever turning over any portion of the net sales proceeds to Charter 3. His actions "appear so inconsistent with [his] self-serving statement of intent that the proof leads the court to disbelieve [him]." *Caspers v. Van Horne (In re Van Horne)*, 823 F.2d 1285, 1288 (8th Cir. 1987).

Moreover, his testimony that he intended to pay all of Castlerock's creditors, not just Charter 3, shows that he viewed Charter 3's right to the sales proceeds as a "payment" rather than a

"remittance," no different than any other creditor's right. (Tr. at 87, 108). Hall was flippant in his testimony at Trial that any reimbursement to Charter 3 of its costs depended entirely upon the availability of funds in Castlerock's operating account. His testimony is totally inapposite to the duties and terms set forth in the Joint Venture Agreements that he drafted himself. There was simply no contingency under the Joint Venture Agreements where Castlerock could reasonably claim any of the funds without Charter 3's consent in the absence of any profit. Castlerock has not asserted any claim for setoff, arguing that Charter 3 was not entitled to the full amount.

In the same vein as his testimony that "we fully intended to" pay Charter 3, Hall's testimony that he handled the sales proceeds no differently than proceeds from other construction projects misses the point. (Tr. at 76, 82).

> Q. [I]nstead of paying Charter 3 whose money that was, you all started paying other creditors with that money, correct?
>
> A. That's correct.
>
> Q. And you knew what you were doing when you wrote those checks, didn't you?
>
> A. We were doing exactly what we have always done for the past 17 years. Nothing different.

(Tr. at 81-82). At the inception of their business relationship, Charter 3 was a partner, not a creditor of Castlerock. By using the funds that he knew belonged to Charter 3, Hall transformed Charter 3 into an "involuntary creditor."

As the manager in charge of Castlerock's financial affairs, Hall should have segregated the net sales proceeds. Because there were no profits, there was no reason to co-mingle the funds in the general operating account. Hall could have simply endorsed the checks over to Charter 3 and avoided depositing the funds altogether. Instead, he deliberately chose to turn Charter 3 into an "involuntary creditor" by using Charter 3's funds as he pleased while placating Bracken with

empty promises to meet with him. Such evidence supports an inference that Hall intended to deceive Charter 3, which Hall has not overcome with his glib testimony that "we fully intended to pay" Charter 3. *See Van Horne*, 823 F.2d at 1287.

In his post-trial brief, Hall contends that there was no proof at Trial that he received any personal benefit from the checks he wrote after the net sales proceeds were deposited into the operating account. (Hall Adv. Dkt. #42 at 6). For example, as to the checks that he wrote to himself on May 1, 5, and 8, 2020 and on July 6, 14, and 21, 2020, he argues that Charter 3 did not trace the source of those withdrawn funds to the sales proceeds in question. But as of July 1, 2020, the operating account had reached a negative balance, so at that point, all sources of funds had been depleted, including the sale proceeds from the first closing. The account again reached a negative balance at the end of August 2020 after the sales proceeds from the second and third closings had been deposited into the account.

The Court finds that Charter 3, although not required to do so, presented evidence that Hall personally benefitted from the net sales proceeds deposited into the company's operating account. Castlerock provided him his livelihood, and he admitted at Trial that he had no other employment. Such evidence explains the motive behind his actions but was otherwise unnecessary because proof that Hall obtained *any* personal benefit is not a required element of Charter 3's § 523(a)(2)(A) claim. The Fifth Circuit in *Deodati v. M.M. Winkler & Assocs. (In re M.M. Winkler & Assocs.)*, 239 F.3d 746, 749 (5th Cir. 2001), expressly rejected the line of cases in other jurisdictions imposing a "receipt of benefit" requirement. To the extent that any of its past rulings could be interpreted as adopting such a requirement, the Fifth Circuit held that they had been overruled by the U.S. Supreme Court's decision in *Cohen v. de la Cruz*, 523 U.S. 213, 220 (1998). In *Cohen*, the U.S. Supreme Court concluded that all liabilities arising out of a debtor's fraudulent conduct are

nondischargeable without regard to whether the debtor benefitted in some way. *Id*. "Once it is established that specific money or property has been obtained by fraud . . . 'any debt' arising therefrom is excepted from discharge." *Winkler*, 239 F.3d at 749 (citing *Cohen*, 523 U.S. at 218-19); *Hancock Bank v. Harper (In re Harper)*, 475 B.R. 540, 549 (Bankr. S.D. Miss. 2012).

A false pretense is conduct by a debtor that implies or promotes a fraudulent scheme such as when a debtor, with the intent to mislead a creditor, engages in "a series of events, activities or communications which, when considered collectively, create a false and misleading set of circumstances, or . . . understanding of a transaction, in which a creditor is wrongfully induced by the debtor to transfer property . . . to the debtor." *Sterna v. Paneras (In re Paneras)*, 195 B.R. 395, 406 (Bankr. N.D. Ill. 1996). The Court finds that Hall's deception fits within this description of a false pretense. He never disclosed to Bracken in any of his communications that he intended to immediately use the proceeds from the sales for other purposes. Hall engaged in this deception knowing that the express terms of the Joint Venture Agreements required Castlerock to turn over the proceeds to Charter 3. Hall, after all, not only signed the Joint Venture Agreements on Castlerock's behalf but also drafted them. Moreover, because of the text messages from Bracken demanding remittance, it is inconceivable that Hall could have believed that Charter 3 consented to Castlerock's use of the funds. Such evidence shows that Hall fraudulently induced Bracken and, thus, Charter 3, to sign the quitclaim deeds.

Turning to the element of justifiable reliance, the Court notes that before he signed the Joint Venture Agreements, Bracken discussed Castlerock with his banker who told him that other investors had entered into similar deals with Castlerock and "did pretty well with them." (Tr. at 23). Just before the third closing, he spoke with Castlerock's realtor who assured him that Hall and Warriner would eventually pay Charter 3. (Tr. at 50-51). Bracken testified that he did not fully

realize until August 2020 that Castlerock never intended to pay Charter 3. (Tr. at 52). Bracken had not seen Castlerock's bank statements and was unaware of its declining financial condition.

Justifiable reliance is a less exacting standard than reasonable reliance and does not impose a duty to investigate unless there are "red flags" indicating that reliance is unwarranted. *Field*, 516 U.S. at 71. Here, there were no "red flags." If, for example, Hall or Warriner had notified Bracken of Warriner's purported resignation from Castlerock, such notice might have raised a "red flag," but neither did so. The evidence shows that Bracken justifiably relied upon Hall's deceptive conduct and that Hall's actions deprived Charter 3 of the net sales proceeds paid at the closings.

In summary, Hall is subject to personal liability because he engaged in false pretenses to induce Bracken to sign the quitclaim deeds from which Charter 3 incurred damages. Accordingly, the Court finds that Charter 3 has established the elements of a § 523(a)(2)(A) non-dischargeability claim against Hall in the amount of $511,297.36. The Court turns next to Warriner.

ii. Warriner

Warriner's defense differs from Hall's because it rests largely on his purported resignation as Castlerock's manager on May 22, 2020, before the second and third closings. (Tr. at 154-55; Warriner Adv. Dkt. #48 at 6). Warriner apparently contends that as of the date of his resignation, he was legally incapable of making any financial decisions relating to Castlerock. In other words, Warriner views as irrelevant any evidence of his conduct after May 22, 2020. Charter 3 argued at Trial, but not in its post-trial briefs, that Warriner's attempted resignation fell short of the requirements of Mississippi law.

The withdrawal of a member from an LLC is governed by section 79-29-303 of the *Mississippi Code*.[20] Under that statute, a member in an LLC has no unilateral right to resign his membership before the dissolution of the company but may cease to be a member only by obtaining the written consent of all members or by complying with the provisions of the LLC's written operating agreement.

> Notwithstanding anything to the contrary under applicable law, unless the certificate of formation or a written operating agreement provides otherwise, a member may not withdraw from a limited liability company prior to the dissolution and winding-up of the limited liability company without the written consent of all of the members of the limited liability company.

MISS. CODE ANN. § 79-29-303 (Rev. 2011).

Hall testified that he accepted Warriner's resignation but did not sign Warriner's resignation letter or otherwise indicate his consent in writing. Copies of Castlerock's certificate of formation and operating agreement were not introduced into evidence,[21] and there was no testimony that either document allowed Warriner to withdraw his membership unilaterally. Because Warriner's purported resignation did not conform to Mississippi law, the Court rejects Warriner's defense that he was legally incapable of making financial decisions on Castlerock's behalf as of May 22, 2020. Simply put, Warriner's attempt to withdraw from the LLC did not relieve him of his obligations under the Joint Venture Agreements. Having ironed out this wrinkle in the analysis of Warriner's personal liability, the Court next examines evidence of his direct, personal participation in the alleged wrongdoing.

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[20] The Mississippi Limited Liability Act was revised in 2010. Pursuant to section 79-29-1309 of the *Mississippi Code*, the revised version of the Mississippi Limited Liability Act applies to Warriner's purported resignation in 2020.

[21] None of Castlerock's organizational documents were offered as evidence at Trial. MISS. CODE ANN. § 79-29-201 (requiring LLCs to enter into a certificate of formation).

Warriner signed the Joint Venture Agreements and was in charge of the construction of the spec houses. Text messages between Warriner and Bracken show that Warriner routinely contacted Bracken requesting construction draws while the spec houses were under construction. (Ex. 23; Tr. at 13). As construction neared completion, Warriner communicated with Bracken about potential buyers. After the first house sold, Warriner told Bracken the date of the closing and informed him that Hall would contact him later about Charter 3's payment from the net sales proceeds. (Tr. at 33). Warriner then attended the first closing on April 30, 2020. He signed the deed conveying the house to the buyer, and in return, he received a check in the amount of $165,870.42. He did not endorse and tender that check to Charter 3. The check instead was deposited into Castlerock's operating account on May 1, 2020. Warriner could not recall whether he, Hall, or one of the "young ladies at the desk" deposited the check, but he admitted that he either deposited it himself or handed it over to someone else to do so. (Tr. at 128-29, 151). Warriner was an authorized signatory on the account but did not sign any checks. He delegated that responsibility to Hall. According to both Warriner and Hall, Warriner's active role in the daily affairs of the business ended shortly after the first closing. Bracken testified that except for his conversation with Warriner that took place before the first closing, he "really didn't mess with Mr. Warriner over trying to collect money." (Tr. at 33).

Recognizing, perhaps, that Warriner's handling of the net sales proceeds after the first closing was more limited than Hall's, Charter 3 asks the Court in its post-trial briefs to impute Hall's fraud to Warriner. (Warriner Adv. Dkt. #49 at 16). The Court addresses Charter 3's vicarious liability argument first. *See Tower Credit, Inc. v. Gauthier (In re Gauthier)*, 349 F. App'x 943, 945 (5th Cir. 2009) (recognizing that a debt may be nondischargeable when actual fraud is imputed to the debtor under agency principles).

In support of holding Warriner vicariously liable for Hall's alleged fraud, Charter 3 cites the Fifth Circuit's decision in *In re Luce*, 960 F.2d 1277, 1282 (5th Cir. 1992). There, a wife who was business partners with her husband attempted to discharge debts that she and her husband had personally guaranteed. The bankruptcy court entered judgments against the husband and wife declaring the debts nondischargeable under § 523(a)(2) and (4). In declaring the debt nondischargeable against the wife, the bankruptcy court imputed the husband's fraud to the wife, who appealed the decision. The Fifth Circuit agreed with the bankruptcy court's analysis, holding that the wife was vicariously liable regardless of her knowledge of or involvement in the fraudulent scheme because: (1) she was a partner in the business; (2) the debts were obtained by her husband on behalf of the partnership; and (3) the husband's fraud benefitted the partnership.[22] The Fifth Circuit rested its holding in *Luce* on *Strang v. Bradner*, 114 U.S. 555 (1885), where the U.S. Supreme Court ruled that a partner's fraudulent actions, even when conducted without the knowledge or direction of his innocent partners, may be "imputed . . . to all members of his firm" when state partnership law mandates such liability. *Id*. at 561.

The facts in *Luce* are distinguishable from those here because Warriner was not Hall's partner but a member of an LLC. The only partnership relationship was between Charter 3 and Castlerock as joint venturers, but Castlerock is not a defendant in the Adversary Proceedings and its liability is not at issue. Under Mississippi law, Castlerock's business form as an LLC shields Warriner from the imputation of Hall's alleged fraud. *See* MISS. CODE ANN. § 79-29-311(1). As noted previously, to establish Warriner's personal liability for Castlerock's debt, Charter 3 must present evidence of his "direct, personal participation" in the alleged fraud. *Mozingo*, 752 F.2d at 174.

[22] The Fifth Circuit later clarified in *Winkler* that it did not intend for its decision in *Luce* to create a "receipt of benefit" requirement. *Winkler*, 239 F.3d at 749.

Returning to that question, Warriner testified that it was unreasonable for Bracken or any other investor to expect payment the same day as a closing “because there’s always expenses coming in.” (Tr. at 130). But there was no evidence in the record of any post-closing expenses incurred in connection with the spec houses. Even if there were any such post-closing expenses, it would not have entitled Hall to spend the net sales proceeds for other purposes. Castlerock and Charter 3 had agreed to split any profits realized only “after paying any and all costs associated with the construction of the project.” (Ex. 7 ¶ 9; Ex. 8 ¶ 9).

Warriner contends that his resignation on May 22, 2020 marked the end of his active participation in the business. It is undisputed that Warriner did not attend the second and third closings and did not receive the checks at those closings. Several facts, however, suggest that Warriner remained involved in the business to some extent. For example, after Warriner’s alleged withdrawal from Castlerock, Global funded the loan that Warriner had personally guaranteed, he voluntarily agreed to remain a signatory on the operating account, and he retained the same counsel as Castlerock and Hall in his bankruptcy case and in these Adversary Proceedings. Also, the timing of his attempted resignation raises an inference that Warriner may have tried to distance himself from Castlerock when he became aware of the company’s dire financial condition and its mishandling of the sales proceeds from the first closing. *See Farmers & Merchants State Bank v. Perry (In re Perry)*, 448 B.R. 219, 226 (Bankr. N.D. Ohio 2011) (“‘[W]illful blindness’ does not provide a defense to an action brought under § 523(a)(2)(A), and may instead be used as a factor indicative of fraud.”). Warriner testified that he resigned because he wanted to spend more time with his family and described Hall as “one of the best men I know, a very Godly man, and hard worker” for whom he ”would do anything.” (Tr. at 153). Based on Warriner’s testimony and demeanor, the

Court is suspect of Warriner's hasty retreat from a twenty-five-year-plus business relationship while Castlerock teetered on the brink of bankruptcy.

Although Warriner did not fully end his involvement in the business after the first closing, the evidence does not indicate that he communicated with Bracken about the proceeds from the second or third closings. He did, however, provide assurances to Bracken regarding the proceeds from the first sale and caused the funds to be deposited in Castlerock's account. The Court, therefore, finds that Warriner is personally liable for the proceeds from the first sale in the amount of $165,870.42 as a debt incurred through false pretenses. That finding also leads the Court to conclude that this amount is a nondischargeable obligation. Although Charter 3 need prove only one exception, the Court reaches the same conclusions under the "actual fraud" prong of § 523(a)(2)(A) for the reasons explained below.

2. Actual Fraud

In support of its claim under § 523(a)(2)(A) for "actual fraud," Charter 3 alleges that Hall and Warriner committed actual fraud by knowingly receiving, depositing, and then spending funds that they admitted at Trial did not belong to them. (Hall Adv. Dkt. #43 at 21; Warriner Adv. Dkt. #49 at 21). According to Charter 3, Hall and Warriner should have immediately endorsed and delivered the checks to Charter 3 or, at the very least, should have deposited them into an escrow account.

In general, actual fraud "consists of any deceit, artifice, trick or design involving direct and active operation of the mind, used to circumvent and cheat another—something said done or omitted with the design of perpetrating what is known to be a cheat or deception." *RecoverEdge*, 44 F.3d at 1293. Distilled, a § 523(a)(2)(A) claim for actual fraud requires knowledge of the falsity and an intent to deceive, both of which may be inferred by examining the totality of the circumstances.

In support of its nondischargeability claim, Charter 3 relies on the U.S. Supreme Court's decision in *Husky International Electronics, Inc. v. Ritz*, 578 U.S. 356 (2016). There, a debtor deliberately transferred the assets of a closely held corporation to other entities he controlled to prevent a creditor from collecting its debt. *Id.* at 357-58. The creditor challenged the dischargeability of the debt under the "actual fraud" prong of § 523(a)(2)(A). The bankruptcy court, and then on appeal, the district court and the Fifth Circuit, held that the debtor did not commit "actual fraud" because of the absence of any misrepresentation by the debtor to the creditor. The U.S. Supreme Court, however, concluded that "actual fraud" within the meaning of § 523(a)(2)(A) encompasses forms of fraud like fraudulent conveyance schemes "even when those schemes do not involve a false representation."[23] *Ritz*, 578 U.S. at 366.

Charter 3 does not allege that Hall and Warriner engaged in a fraudulent conveyance scheme like the one at issue in *Ritz*. Charter 3 nevertheless argues that *Ritz* applies because debtors like Hall and Warriner who knowingly receive money embezzled from a creditor exhibit the same level of deception as the knowing recipient of a fraudulent conveyance. (Hall Adv. Dkt. #43 at 20; Warriner Adv. Dkt. #49 at 20). Charter 3's contention stems from the U.S. Supreme Court's rejection of the argument that a debtor who fraudulently conveys property does not "obtain[ ] money, property, services, or credit" from his participation in the fraud within the meaning of § 523(a)(2)(A). *Ritz*, 578 U.S. at 364-65. Although recognizing that the transferor does not "obtain" debts in a fraudulent conveyance, the U.S. Supreme Court noted that "the recipient of the transfer . . . can 'obtai[n]' assets 'by' his or her participation in the fraud. . . . Thus, at least sometimes a debt 'obtained by' a fraudulent conveyance scheme could be nondischargeable under § 523(a)(2)(A)."

[23] The U.S. Supreme Court did not decide whether the creditor prevailed in its attempt to deny the debtor a discharge of its debt but remanded the case to the Fifth Circuit for that determination. *See Husky Int'l Elecs., Inc. v. Ritz (In re Ritz)*, 832 F.3d 560 (5th Cir. 2016).

Ritz, 578 U.S. at 365 (citations omitted). Likewise, Charter 3 contends that Hall and Warriner "obtained" the sales proceeds as a result of their embezzlement and the debts traceable to their embezzlement are nondischargeable. Charter 3 points out that the Mississippi bankruptcy court in *Mid-South Maintenance, Inc. v. Burk (In re Burk)*, 583 B.R. 655, 667 (Bankr. N.D. Miss. 2018), concluded that a debtor who knowingly receives embezzled money commits fraud and the debt is nondischargeable.

Charter 3 entrusted Castlerock with the net sales proceeds of $511,297.36. Warriner received the check from the first closing in the amount of $165,870.42, and Hall received the checks from the second and third closings totaling $345,426.94. All three checks were deposited into Castlerock's operating account, and both Hall and Warriner had access to that account. Hall and Warriner were fully aware that the funds belonged to Charter 3, but the funds were used for other purposes while Hall falsely assured Bracken otherwise. The Court finds that such behavior evinces "moral turpitude or intentional wrong" and constitutes actual fraud within the U.S. Supreme Court's expanded definition. *See Ritz*, 578 U.S. at 364 (rejecting argument that § 523(a)(2)(A) applies only when fraudulent conduct occurs at the inception of the debt). The Court also finds that Charter 3 proved justifiable reliance for the reasons previously discussed.[24] Accordingly, Warriner and Hall are jointly and severally liable to Charter 3 for $165,870.42 of the sale proceeds from the first closing since that debt can be traceable to a fraudulent scheme that involved them both, and Hall is individually liable for an additional $345,426.94 of the sales proceeds from the second and third closings. Because there was insufficient evidence of Warriner's personal involvement as to the use of the sales proceeds after the first closing, the debts attributable to the second

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[24] The U.S. Supreme Court in *Ritz* left open the question whether there is a reliance requirement for frauds not premised on a false pretense or false representation. *See Ritz*, 578 U.S. at 365. Even if not a required element, justifiable reliance exists under these facts.

and third closings are not traceable to Warriner. The Court further finds that all of these amounts are nondischargeable as debts arising from actual fraud.

C. § 523(a)(4)

As an alternative basis for denying Hall and Warriner a discharge of the debt, Charter 3 alleges that Hall and Warriner either committed defalcation while acting in a fiduciary capacity or embezzled the net sales proceeds. Section 523(a)(4) provides that a discharge in a chapter 7 case "does not discharge an individual debtor from any debt . . . for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." 11 U.S.C. § 523(a)(4). The phrase "while acting in a fiduciary capacity" only modifies fraud and defalcation; therefore, a debt for embezzlement may be nondischargeable without regard to whether the debtor was a fiduciary. *Miller v. J.D. Abrams Inc. (In re Miller)*, 156 F.3d 598, 602 (5th Cir. 1998).

1. Fiduciary Fraud or Defalcation

Charter 3 alleges that Hall and Warriner owed it fiduciary duties of loyalty, honesty, and good faith and breached their fiduciary duties by fraudulently converting Charter 3's funds and refusing to tender those funds to Charter 3. (Hall Adv. Dkt. #1 at 6; Warriner Adv. Dkt. #1 at 6). In construing this exception to discharge, the Fifth Circuit has held that § 523(a)(4) was "intended to reach those debts incurred through abuses of fiduciary positions and through active misconduct whereby a debtor has deprived others of their property by criminal acts; both classes of conduct involve debts arising from the debtor's acquisition or use of property that is not the debtor's." *Boyle v. Abilene Lumber, Inc. (In re Boyle)*, 819 F.2d 583, 588 (5th Cir. 1987), *superseded by statute as recognized by Ratliff Ready-Mix, L.P. v. Pledger (In re Pledger)*, 592 F. App'x 296, 300 (5th Cir. 2015).

"Determining whether a debtor committed fraud or defalcation while acting in a fiduciary capacity is a two-step process." *Interstate Plywood Co. v. Blankenship (In re Blankenship)*, 525 B.R. 629, 640 (Bankr. N.D. Miss. 2015) (citation omitted). The first step is proof of the existence of a fiduciary relationship. *Id*. (citing *Murphy & Robinson Inv. Co. v. Cross (In re Cross)*, 666 F.2d 873, 879 (5th Cir. 1982)). "Second, some type of fraud or defalcation must have occurred during the fiduciary relationship." *Id*. at 641 (citing *In re Chavez*, 140 B.R. 413, 422 (Bankr. W.D. Tex. 1992)). Charter 3's claim under § 523(a)(4) requires the Court to examine whether Hall and Warriner owed a fiduciary duty to Charter 3 and whether a defalcation occurred during the course of the fiduciary relationship.

a. Fiduciary Capacity

There is no definition of "fiduciary capacity" in the Bankruptcy Code. The Fifth Circuit has construed the "fiduciary capacity" requirement as applying to technical trusts or to traditional fiduciary relationships involving trust-type obligations imposed by statute or common law. *Tex. Lottery Comm'n v. Tran (In re Tran)*, 151 F.3d 339, 342 (5th Cir. 1998). There need not be a formal, written agreement creating the express-trust arrangement, however, because the definition includes fiduciary relationships established by law, so long as the fiduciary relationship existed prior to the alleged wrongdoing. *LSP Inv. P'ship v. Bennett (In re Bennett)*, 989 F.2d 779, 784 (5th Cir. 1993). Although the question of fiduciary capacity under § 523(a)(4) is governed by federal common law, state law is relevant in determining whether a trust relationship exists. *FNFS, Ltd. v. Harwood (In re Harwood)*, 637 F.3d 615, 619-20 (5th Cir. 2011). Mindful that relationships that are characterized as fiduciary in nature under state law do not necessarily amount to a fiduciary capacity under § 523(a)(4), the Court turns to Mississippi law. *Shcolnik v. Rapid Settlements, Ltd. (In re Shcolnik)*, 670 F.3d 624, 628 (5th Cir. 2012).

In Mississippi, fiduciary relationships can arise in a variety of contexts. "Traditional fiduciary relationships are found in cases of trustee and beneficiary, *partners*, principal and agents, guardian and ward, managing directors and corporation." *Robley v. Blue Cross/Blue Shield of Miss*., 935 So. 2d 990, 994 (Miss. 2006) (citation omitted) (emphasis added). Under Mississippi law, members of a joint venture are fiduciaries. *Scruggs v. Wyatt*, 60 So. 3d 758 (Miss. 2011). Joint venturers "owe each other a duty of utmost good faith and scrupulous honesty in their mutual endeavor." *Deauville Corp. v. Fed. Dep't Stores, Inc.*, 756 F.2d 1183, 1194 (5th Cir. 1985).

Hall and Warriner assert that they did not owe Charter 3 a fiduciary duty because they were not joint venturers with Charter 3. This assertion is a variation of their argument, rejected previously, that Castlerock's business form shields them from personal liability for its debts. As held previously, however, managing members of an LLC may be found liable for their own misconduct. Moreover, where a business entity such as an LLC owes a fiduciary duty, the individuals charged with carrying out the fiduciary duty on behalf of the LLC can act in a fiduciary capacity sufficient to fall within the parameters of § 523(a)(4). *Miller*, 156 F.3d at 602. As a joint venturer, Castlerock owed a fiduciary duty to Charter 3 under state law. *Wilson v. Scruggs*, 371 F. Supp. 2d 837 (S.D. Miss. 2005).

As to Hall's and Warriner's fiduciary capacity, the Court notes that they were the sole members and co-managers of Castlerock, each held a fifty-percent ownership interest in the business, and both signed the Joint Venture Agreements as members of Castlerock. Beyond those basic facts, the Court considers Hall's and Warriner's fiduciary capacity separately.

i. Hall

Hall was Castlerock's accountant and exercised control over Castlerock's financial affairs. His signature appears on all checks drawn on the business account. Given his ownership interest and

role in the company, the Court concludes that Hall was charged with carrying out Castlerock's fiduciary duties to Charter 3 and was acting in a fiduciary capacity.

ii. Warriner

Warriner was just as involved in the day-to-day affairs of the business as Hall until mid-May 2020. (Ex. 35; Tr. at 113). He did not sign any of the checks drawn on the business account but delegated that task to Hall. He nevertheless had check-writing authority during the relevant events. Based on Warriner's responsibility as a co-manager, his participation in the day-to-day operations of Castlerock, his fifty-percent ownership in the business, and his authority to write checks from Castlerock's operating account which did not end after his attempted resignation, the Court finds that Warriner was also charged by Castlerock with carrying out its fiduciary duties to Charter 3 and was acting in a fiduciary capacity. His attempt to withdraw his membership in Castlerock in May 2020 did not alter his fiduciary duties to Charter 3 under the Joint Venture Agreements. *Sledge v. Grenfell Sledge & Stevens, PLLC*, 263 So. 3d 655 (Miss. 2018). Having determined that a fiduciary relationship existed as to both Hall and Warriner, the Court considers whether a defalcation occurred during the course of the fiduciary relationship.

b. Defalcation

Defalcation under § 523(a)(4) requires a culpable state of mind involving "knowledge of, or gross recklessness in respect to, the improper nature of the relevant fiduciary behavior." *Bullock v. BankChampaign, N.A.*, 569 U.S. 267, 269 (2013). Defalcation includes "not only conduct that the fiduciary knows is improper but also reckless conduct of the kind that the criminal law often treats as the equivalent." *Id.* at 274. "Where actual knowledge of wrongdoing is lacking," there may be a defalcation "if the fiduciary 'consciously disregards' (or is willfully blind to) 'a substantial and unjustifiable risk' that his conduct will turn out to violate a fiduciary duty." *Id.* That risk

must involve "*a gross deviation* from the standard of conduct that a law-abiding person would observe in the actor's situation." *Id*. (citations omitted).

i. Hall

Applying *Bullock*'s "reckless conduct" standard to the facts presented in the Adversary Proceedings, the Court finds that Hall committed a defalcation within the meaning of § 523(a)(4). Hall testified that he was aware that the funds from all three closings belonged to Charter 3. Despite this knowledge, Hall wrote checks to creditors other than Charter 3 while ignoring Bracken's demands for payment.

Hall's conduct did not involve simple or even inexcusable negligence—which would not give rise to the level of culpability required by the standard of recklessness—but an extreme departure from the standard that a law-abiding person would follow. His own testimony establishes his awareness of the situation that he helped to create. Given Castlerock's poor financial condition, there was a "substantial and unjustifiable" risk to Charter 3 that his co-mingling of the net sales proceeds would violate his fiduciary duty and he committed defalcation when he wrote checks to other creditors. Hall's testimony that he had no specific intent to misappropriate funds belonging to Charter 3 is not a proper defense because specific intent is not a requirement. *See Bullock*, 569 U.S. at 269. Accordingly, the Court finds that the debt in the amount of $511,297.36 should be excepted from discharge in the Hall Case as a debt for a fiduciary defalcation under § 523(a)(4).

ii. Warriner

Like Hall, Warriner was aware that the net sales proceeds from the closings belonged to Charter 3, not Castlerock, under the Joint Venture Agreements. Unlike Hall, however, Warriner was not directly involved in the accounting of those funds. The timing of his attempted resignation raises an inference that he was aware of Castlerock's poor financial condition and Hall's

comingling of the net sales proceeds. Still, he was only actively involved in the affairs of the business before the second and third closings. As to the first closing, the Court finds that his presence there, his acceptance of the check, and his delegation of authority to Hall over those funds without any supervision or controls in place constitutes reckless conduct, especially given his knowledge of Castlerock's financial problems. Those funds in the amount of $165,870.42 should be excepted from discharge in the Warriner Case as a debt arising out of a fiduciary defalcation under § 523(a)(6).

2. Embezzlement

Next, Charter 3 seeks a declaration that the debt is nondischargeable under the embezzlement prong of § 523(a)(4). Embezzlement for purposes of § 523(a)(4) requires proof that the creditor entrusted the debtor with his property, that the debtor appropriated the property for a use other than for which it was entrusted, and that the debtor intended to defraud the creditor. *Miller*, 156 F.3d at 603. Nondischargeability may rest on embezzlement without requiring proof of a fiduciary relationship. *See Cross Point Church v. Andrews (In re Andrews)*, 560 B.R. 429, 444 (Bankr. S.D. Miss. 2016).

The checks from the closings were entrusted to Castlerock, the proceeds from the checks belonged to Charter 3, the checks were deposited into Castlerock's operating account, and the proceeds were used to pay obligations unrelated to the spec houses built under the Joint Venture Agreements. For the reasons discussed previously in connection with Charter 3's nondischargeability claim for actual fraud under § 523(a)(2)(A), the Court finds that Charter 3 has proved Hall's fraudulent intent as to all of the closings and Warriner's as to the first closing. As the Court made clear in that same discussion, this is not a situation where a debtor merely mis-used loan proceeds or where the creditor incurred loses simply because of a bad business decision. Here, Charter 3

never agreed to loan money to Castlerock, and Castlerock knew that the funds belonged solely to Charter 3 when it converted the funds to its own use. Accordingly, the Court finds that $165,870.42 of Charter 3's claim against Warriner is nondischargeable and that the entire amount of its claim against Hall, $511,297.36, is nondischargeable as debts arising from embezzlement under § 523(a)(4).

D. § 523(a)(6)

Finally, Charter 3 seeks a determination that the debt is non-dischargeable under § 523(a)(6). Section 523(a)(6) excepts from discharge any debt "for willful and malicious injury by the debtor to another entity or to the property of another entity." 11 U.S.C. § 523(a)(6). The U.S. Supreme Court in *Kawaauhau v. Geiger*, 523 U.S. 57 (1998), established guidelines for determining whether a debt results from a willful and malicious injury. The U.S. Supreme Court concluded that nondischargeability under § 523(a)(6) requires a deliberate or intentional injury, rather than a deliberate or intentional act that leads to an injury. *Id*. at 61; *see also Chrysler Credit Corp. v. Perry Chrysler Plymouth, Inc*., 783 F.2d 480, 486 (5th Cir. 1986). Following *Kawaauhau*, the Fifth Circuit condensed the test for a "willful and malicious injury" into a single inquiry of whether there is either (1) an objective substantial certainty of harm or (2) a subjective motive to cause harm on the part of the debtor. *See Williams v. Int'l Bhd. of Elec. Workers (In re Williams)*, 337 F.3d 504, 509 (5th Cir. 2003) ("a debtor must commit an intentional or substantially certain injury in order to be deprived of a discharge" under § 523(a)(6)); *Raspanti v. Keaty (In re Keaty)*, 397 F.3d 264, 273-74 (5th Cir. 2005). "Because debtors generally deny that they had a subjective motive to cause harm, most cases that hold debts to be non-dischargeable do so by determining whether [the debtor's] actions were at least substantially certain to result in injury." *Berry v. Vollbracht (In re Vollbracht)*, 276 F. App'x 360, 361-62 (5th Cir. 2007) (citation omitted) (unpublished).

The Court has already determined that the acts of Hall and Warriner constituted embezzlement as to all or part of the funds. Under § 523(a)(6), however, acts that constitute embezzlement still require proof of a subjective motive or an objective substantial certainty of harm. *Miller*, 156 F.3d at 606. The Court examines the conduct of Hall and Warriner separately to determine if Charter 3 met its burden of proof.

1. Hall

The evidence presented to the Court shows that Hall used the net sales proceeds knowing, with substantial certainty, that Charter 3 would be harmed. Hall was the co-manager of Castlerock and personally handled its financial affairs. Yet he failed to take any steps whatsoever to safeguard these funds during the company's financial crisis. Instead, he paid himself as well as select and preferred creditors of Castlerock, including Global and L&W Supply whose debts he had personally guaranteed. *See Herman v. White (In re White)*, 519 B.R. 832, 840 (Bankr. N.D. Okla. 2014) (holding that a willful injury may be established indirectly by evidence of the debtor's knowledge of the creditor's rights and knowledge that his conduct will cause a particularized injury). Hall spent the funds while sending Bracken text messages agreeing to "settle up" and meet with him knowing he had no intent to turn over the net sales proceeds to Charter 3. (Ex. 16, Bates #65, #66).

Hall's actions were willful and malicious because his use of the net sales proceeds were substantially certain to cause Charter 3 injury. He was in control of Castlerock's finances and chose to injure Charter 3's interest in the sales proceeds in order to satisfy other creditors and protect his personal interests. There was no evidence that Hall made any effort to ensure that Charter 3 received the funds. To the contrary, he immediately began to use the funds after each closing. Accordingly, the Court finds that Charter 3 has met its burden of proving by a preponderance of the

evidence that the debt in the amount of $511,297.36 is nondischargeable under § 523(a)(6) as a willful and malicious injury inflicted by Hall.

2. Warriner

Warriner was actively involved in the disposition of Charter 3's net sale proceeds in the amount of $165,870.42 received at the first closing. Warriner knew that depositing these funds into the general operating account would jeopardize Charter 3's interest in the net sale proceeds, especially given the decline in Castlerock's finances. Warriner had the legal ability to control Castlerock's finances during the events in question but delegated that task to Hall. His willful blindness is no defense to the disposition of those funds that he allowed Hall to distribute. No evidence, however, established that he played any role in diverting the net sales proceeds from the second and third closings. Accordingly, the Court finds that Charter 3 has proved that the debt in the amount of $165,870.42 is nondischargeable under § 523(a)(6) as a willful and malicious injury inflicted by Warriner.

E. Attorney's Fees & Costs

In the post-trial briefs, Hall and Warriner do not seek an award of attorney's fees and costs against Charter 3. Their request for payment of their attorney's fees and costs appears only in the Responses, which they did not support with any legal authority. The Bankruptcy Code permits an award of attorney's fees and costs when a creditor seeks but is denied a determination that a consumer debt is nondischargeable under § 523(a)(2). 11 U.S.C. § 523(d); *Carthage Bank v. Kirkland*, 121 B.R. 496, 499-500 (S.D. Miss. 1990). Because the debt in question is not a consumer debt, § 523(d) does not apply. *See* 11 U.S.C. § 101(8); *In re Booth*, 858 F.2d 1051, 1055 (5th Cir. 1988) (holding that a "consumer debt" for purposes of § 707(b) is a debt acquired for a personal, family, or household purpose in contrast to a business debt that is a "debt incurred with an eye toward

profit"). Here, the debt owed Charter 3 arose from a failed joint venture for the development of certain real estate incurred "with an eye toward profit." *Booth*, 858 F.2d at 1055. Because § 523(d) does not apply and because Hall and Warriner have not identified any other legal authority, the Court finds that their request for attorney's fees and costs should be denied.

Conclusion

Hall and Warriner insist in their post-trial briefs that if this Court "follow[s] the logic of Charter 3's argument, no debt would ever be dischargeable in a bankruptcy proceeding as the debtor has generally always received a service, materials or funds from a third party that has not been paid." (Hall Adv. Dkt. #42 at 8; Warriner Adv. Dkt. #48 at 9). Although it is true that most debtors in bankruptcy have unpaid debts and most debts are discharged, Hall and Warriner fail to appreciate that Charter 3 was a partner, not a creditor, at the inception of their business relationship. Charter 3 became a creditor only because Castlerock failed to turn over the net sales proceeds. If the checks had been handed over to Bracken, Charter 3 would not be a creditor or have a claim against Hall and Warriner. The logic of Charter 3's argument is wholly consistent with the purpose behind § 523(a), which is to limit the discharge of debts to the honest but unfortunate debtor. Hall and Warriner used Charter 3's funds without their consent when they had no right to do so, intentionally putting Charter 3 at risk.

Based on the foregoing, the Court concludes that Hall and Warriner should be held jointly and severally liable for the debt owed to Charter 3 in the amount of $165,870.42 from the first sale and that Hall should be held individually liable for the debt owed to Charter 3 from the second and third sales in the total amount of $345,426.94. These respective amounts should be excepted from discharge in the Hall Case and in the Warriner Case on the alternative grounds that the debts were either obtained by false pretenses and/or actual fraud under § 523(a)(2)(A), resulted from fraud or

defalcation while acting in a fiduciary capacity and/or embezzlement under § 523(a)(4), and/or were caused by a willful and malicious injury to Charter 3 under § 523(a)(6).

As to the Objections to Proofs of Claim, the Hall Objection should be overruled in the Hall Case as to the full amount of Charter 3's claim of $511,297.36, and the Warriner Objection should be sustained only to the extent Warriner is jointly and severally liable with Hall in the amount of $165,870.42 in the Warriner Case. All other relief requested, including Hall's and Warriner's request for attorney's fees and costs, should be denied. Separate final judgments will be entered in the Adversary Proceedings, the Hall Case, and the Warriner Case in accordance with Federal Rules of Bankruptcy Procedure 7058 and 9021.

##END OF OPINION##