ORDERED.

Dated: September 01, 2017

Cynthia C. Jackson
Cynthia C. Jackson
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF FLORIDA
ORLANDO DIVISION
www.flmb.uscourts.gov

In re:

WILLIAM W. COLE, JR.,

Debtor.
_____/

Case No. 6:15-bk-06458-CCJ
Chapter 7

PRN REAL ESTATE &
INVESTMENTS, LTD.,

Plaintiff,

v.

WILLIAM W. COLE, JR.,

Defendant.
_____/

Adv. Pro. No. 6:15-ap-00168-CCJ

ORDER GRANTING DEFENDANT'S MOTION FOR FINAL JUDGMENT ON THE PLEADINGS AND GRANTING PLAINTIFF LEAVE TO AMEND

This matter came before the Court on the Defendant William W. Cole, Jr.'s (the "Debtor") Motion for Final Judgment on the Pleadings as to Counts III, IV and V of Second Amended Complaint (the "Motion") (Doc. No. 102); and related responses and replies by Plaintiff PRN Real Estate & Investments, Ltd. ("PRN") (Doc. Nos. 105, 154, 155 and 156), including a request for

leave to amend if the Motion is granted. On April 20, 2017, the Court heard argument on the Motion and related matters and after due consideration of the pleadings and the arguments of counsel, rendered an oral ruling. The parties have requested a written ruling.

For the reasons stated on the record in open court and as supplemented below, the Motion is granted, subject to PRN's leave to further amend its complaint.

Background

The Court assumes the parties' familiarity with the underlying facts. The following summary is based upon the allegations in PRN's Second Amended Complaint, which for purposes of this Order, the Court must accept as true (Doc. No. 49, hereinafter the "Complaint").

From approximately 2000 to 2012, the parties engaged in various business ventures, primarily in real estate development. PRN's principal role was to provide financing, while the Debtor, either personally or through affiliated entities (collectively, the "Cole Entities"), found and managed the projects.

In 2008, the Debtor and the Cole Entities began to experience cash flow problems. To provide additional cash for the development projects, the Debtor, the Cole Entities, PRN and others, entered into an agreement which they later amended on two separate occasions (collectively, the "Memorandum Agreement"). The purpose of the Memorandum Agreement was to allow the Debtor and the Cole Entities to repay existing obligations to PRN while at the same time providing them with new capital. The Debtor personally guaranteed the financing provided by PRN in the Memorandum Agreement.

The Debtor and the Cole Entities defaulted under the Memorandum Agreement. In 2012, the parties entered into an agreement by which PRN agreed not to sue the Debtor or the Cole Entities for existing defaults under the Memorandum Agreement (the "Forbearance Agreement").

In exchange, the Debtor gave additional assurances to PRN, including an agreement to provide PRN with detailed business reports and to give PRN the right of first refusal in any future projects.

More than two years after the parties entered into the Forbearance Agreement, PRN learned that the Debtor had transferred or caused to be transferred millions of dollars in cash and assets from his own accounts or accounts of one of the Cole Entities, into accounts held either by his wife, Terre Cole individually, or accounts he held jointly with Mrs. Cole as tenants by the entireties. PRN claims these transfers were fraudulent insofar as they were intended to place assets beyond PRN's reach and otherwise hinder PRN in its attempts to collect on the debts owed to it by Debtor (collectively, the "Fraudulent Transfer Scheme").

The Debtor filed this chapter 7 case on July 27, 2015. PRN has filed six proofs of claim in the case (Claims 3, 4, 5, 6, 7, and 11), asserting total debts of approximately $50 million arising primarily under either the Memorandum Agreement or the Forbearance Agreement (collectively, the "PRN Debt").

The Adversary Proceeding

PRN originally filed this adversary proceeding in 2015. By its initial Complaint, PRN asked the Court to determine that (i) the PRN Debt is non-dischargeable under Section 523(a)(2)(A) of the Bankruptcy Code[1] and (ii) the Debtor "be declared ineligible for a discharge under Section 727(a)(2), (a)(3), (a)(4) and (a)(5) of the Bankruptcy Code."

As to the non-dischargeability of the PRN Debt, the initial Complaint alleged that Cole made oral misrepresentations (Count I) and written misrepresentations (Count II) upon which PRN had justifiably relied and been damaged. PRN later voluntarily dismissed Count I.

In 2016, after the United States Supreme Court issued its opinion in *Husky International Electronics, Inc. v. Ritz*,[2] PRN amended its Complaint to add Counts III, IV and V (collectively,

the "*Husky* Counts"). By each of the *Husky* Counts, PRN asks the Court to find that the entire PRN Debt "or some undetermined amount" of the debt is non-dischargeable under Section 523(a)(2)(A) of the Code as a result of the Debtor's Fraudulent Transfer Scheme.

By the Motion, the Debtor argues that the *Husky* Counts fail to state a claim under Section 523(a)(2)(A), and as such, the Debtor is entitled to judgment as a matter of law. The Court agrees.

Standard

A party may move for judgment on the pleadings "[a]fter the pleadings are closed—but early enough not to delay trial . . . ."[3] "Judgment on the pleadings is appropriate where there are no material facts in dispute and the moving party is entitled to judgment as a matter of law."[4]

A court evaluating a motion for judgment on the pleadings applies the same standard as when evaluating a motion to dismiss for failure to state a claim.[5] The Court "must accept the facts alleged in the complaint as true and view them in the light most favorable to the nonmoving party."[6] Based upon those accepted facts, the Court must determine if the complaint states a claim for relief that is "plausible on its face."[7]

Discussion

Section 523(a)(2)(A) excepts from discharge any debt "for money, property, services . . . to the extent obtained by— false pretenses, a false representation or actual fraud . . . ." The narrow issue before the Supreme Court in *Husky* was whether or not a finding of "actual fraud" under Section 523(a)(2)(A) required a misrepresentation. At the time *Husky* was decided, there was a split of authority among the circuits on this issue. Resolving this split of authority, the Court held that no misrepresentation was needed and that a fraudulent conveyance could itself constitute "actual fraud." In so holding however, the Court in no way ignored the clear requirement of Section 523(a)(2)(A) that any such non-dischargeable debt must still be "*obtained by*" fraud. The

Supreme Court recognized that although generally a transferor does not *obtain* anything in a fraudulent conveyance scheme, but that a "recipient of the transfer—who, with the requisite intent, also commits fraud—can 'obtai[n]' assets 'by' his or her participation in the fraud."[8] Thus, the *Husky* Court stated that if "that recipient later files for bankruptcy, any debts 'traceable to' the fraudulent conveyance will be non-dischargeable under Section 523(a)(2)(A)."[9]

The *Husky* Counts fail to state a claim under this analysis. Nowhere in the *Husky* Counts does PRN allege a specific debt owed to it for monies or other assets *obtained by* the Debtor by, or otherwise *traceable to,* the Fraudulent Transfer Scheme. Instead, PRN simply contends that because the Debtor participated in an attempt to hinder PRN's collection of the PRN Debt after it accrued, the PRN Debt is not dischargeable under Section 523(a)(2)(A).

A similar argument was considered and rejected by the bankruptcy court in *In re Vanwinkle*.[10] There, prior to the petition date, the creditor obtained a judgment against the debtor for contract damages. The creditor alleged that the debtor's post-judgment fraudulent transfer scheme resulted in the judgment debt being non-dischargeable under Section 523(a)(2)(A). The *Vanwinkle* complaint, like here, never set forth a separate cause of action for the post-judgment transfers or identified any separate loss resulting from the transfers. The bankruptcy court dismissed the complaint for failure to state a claim holding that "Section 523(a)(2)(A) does not provide a cause of action that simultaneously creates a debt and renders it non-dischargeable."[11] That is exactly what PRN attempts to do here and it fails as a matter of law.

By Counts III – V, PRN simply alleges it was "damaged" by the Fraudulent Transfer Scheme and asks the Court to declare non-dischargeable "the entirety of the amounts owed PRN (or another amount as determined by the Court)."[12] In its post-hearing briefing, PRN conceded that the entire PRN Debt should not be declared non-dischargeable under *Husky*. PRN argues

however, that at least an amount equal to the value of the assets fraudulently transferred and/or conveyed should be deemed non-dischargeable as a specific debt to PRN. PRN cites to no authority which provides for a separate cause of action (or specific debt) to PRN on this basis. At oral argument counsel for PRN argued that PRN should be entitled to such a non-dischargeable, proportional claim for the amount of transfers because the Fraudulent Transfer Scheme was "personal" to PRN's principal, Nancy Rossman. The Court finds the argument without merit.[13]

Rather than being specific or "personal" to PRN, any damages resulting from the Fraudulent Transfer Scheme would affect the whole creditor body of the Debtor. PRN's argument overlooks a critical distinction between Section 523(a)(2)(A) and Section 727(a)(2) of the Bankruptcy Code. As the *Husky* Court explains:

> Although the two provisions could cover some of the same conduct, they are meaningfully different. Section 727(a)(2) is broader than § 523(a)(2)(A) in scope—preventing an offending debtor from discharging all debt in bankruptcy. But it is narrower than § 523(a)(2)(A) in timing—applying only if the debtor fraudulently conveys assets in the year preceding the bankruptcy filing. In short, while § 727(a)(2) is a blunt remedy for actions that hinder the entire bankruptcy process, § 523(a)(2)(A) is a tailored remedy for behavior connected to specific debts.[14]

The *Husky* Counts read more like Section 727(a)(2) claims. The fraud alleged is not behavior specifically connected to debts owed to PRN, instead it is the type of fraud that would hinder all creditors in equal measure. PRN has provided no basis for its novel claim nor could it. There are two ways a bankruptcy court may remedy a fraudulent transfer scheme. Either by denying discharge under Section 727 or by avoiding the transfer under Section 550. Importantly, in either case the remedy must inure to the benefit of *all* of the Debtor's creditors and not just PRN.

Indeed, were judgment rendered as requested by PRN, once the Court determined the "amount" that would be deemed non-dischargeable, how would the Court apportion any such

amount among a debtor's creditors? Would apportionment be governed by the Bankruptcy Code's priority scheme? Would secured creditors whose claims might be satisfied by their own collateral be excluded? Or, would the creditor who takes up the mantle and prosecutes the adversary reap all the rewards?

As explained in *Husky*, Section 523(a)(2)(A) is a "*tailored remedy for behavior connected to specific debts*."[15] This is not to say that the debt must be liquidated. But to state a claim, the allegations in the complaint must detail a debtor's liability to the plaintiff-creditor on an enforceable obligation resulting from or traceable directly to the alleged fraudulent transfer.[16]

Leave to Amend

At oral argument and in its pleadings, PRN requests leave to amend should the Court grant Debtor's motion. It is true that the purpose of a motion for judgment on the pleadings "is not to clarify vague pleadings but rather to dispose of cases where the material facts are undisputed and a judgment on the merits may be rendered by examining the substance of the pleadings and any judicially noticed facts."[17] It is equally true, however, that a Court should grant leave to amend a complaint "freely . . . when justice so requires."[18]

PRN has relied on an erroneous interpretation of *Husky*. The *Husky* Counts fail as a matter of law, and should be dismissed. The Court, however, will not enter final judgment in Debtor's favor and instead will permit PRN a final opportunity to correct the deficiencies identified in the Complaint.

In granting leave to amend, the Court is guided by the procedural history of this particular proceeding and the relative recentness, as of the filing of the Complaint, of the Supreme Court's decision is *Husky*.

Therefore, it is **ORDERED**:

1. Defendant's Motion for Final Judgment on the Pleadings as to Counts III, IV and V of Second Amended Complaint is **GRANTED**.

2. Plaintiff is granted leave to amend. Plaintiff shall have fourteen (14) days from entry of this Order to file a third amended complaint.

Service of this Order other than CM/ECF service is not required as all parties in this proceeding are represented by counsel. Local Rule 9013-1(b).

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[1] Sectional references are to 11 U.S.C. §§ 101–1532 ("Code" or "Bankruptcy Code"), unless indicated otherwise.
[2] 136 S. Ct. 1581 (2016).
[3] Fed. R. Bankr. P. 7012 (incorporating Fed. R. Civ. P. 12(c)).
[4] *Cannon v. City of W. Palm Beach*, 250 F.3d 1299, 1301 (11th Cir. 2001).
[5] *See Young v. City of Houston*, 599 F. App'x 553, 554 (5th Cir. 2015); *Sampson v. Wash. Mut. Bank*, 453 F. App'x 863, 865 n.2 (11th Cir. 2011).
[6] *Cannon*, 250 F.3d at 1301.
[7] *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007).
[8] *Husky Int'l Elecs., Inc.*, 136 S. Ct. at 1589.
[9] *Id.* (citation omitted). The *Husky* Court recognized that the circumstances in which a debt resulting from a fraudulent transfer scheme could be declared non-dischargeable "may be rare", yet clarified that such schemes were not "wholly incompatible with the 'obtained by' requirement." *Id.*
[10] *Crawford v. Vanwinkle (In re Vanwinkle)*, 562 B.R. 671 (Bankr. E.D. Ky. Dec. 27, 2016).
[11] *Id.* at 678.
[12] Compl. ¶¶ 68, 73, 79.
[13] To be clear, the Court has not been called to decide, nor does it decide, whether the PRN Debt may be non-dischargeable under Count II of the Complaint.
[14] *Husky Int'l Elecs., Inc.*, 136 S. Ct. at 1589.
[15] *Id.* (emphasis added).
[16] *See Husky Int'l Elecs., Inc.*, 136 S. Ct. at 1589–90; *Norton v. Wilson (In re Wilson)*, No. 16-30782, Adv. Pro. No. 16-3068, 2017 WL 1628878, at *9 (Bankr. N.D. Ohio May 1, 2017); *In re Vanwinkle*, 562 B.R. at 678.
[17] *Material Prods. Int'l, Ltd. v. Ortiz (In re Ortiz)*, 441 B.R. 73, 82 (Bankr. W.D. Tex. 2010) (internal quotation omitted).
[18] Fed. R. Bankr. P. 7015 (incorporating Fed. R. Civ. P. 15(a)(2)).