NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE TENTH CIRCUIT

IN RE EDWARD PARRA LOPEZ and EVA GONZALES LOPEZ, Debtors.	BAP No. NM-07-064
SOUTHWEST FINANCIAL SERVICES OF LAS CRUCES, INC., Plaintiff – Counter-Defendant – Appellee, v. EVA GONZALES LOPEZ, formerly known as Eva G. Valdez, formerly known as Eva Gonzales Valdez, Defendant – Counter-Claimant – Appellant.	Bankr. No. 05-14734-m7 Adv. No. 06-01078-m Chapter 7 ORDER AND JUDGMENT*

Appeal from the United States Bankruptcy Court
for the District of New Mexico

Before CORNISH, BROWN, and McNIFF, Bankruptcy Judges.[1]

CORNISH, Bankruptcy Judge.

Eva Gonzales Lopez ("Debtor") appeals a summary judgment order against her determining a debt to Southwest Financial Services of Las Cruces, Inc.

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* This order and judgment is not binding precedent, except under the doctrines of law of the case, res judicata, and collateral estoppel. 10th Cir. BAP L.R. 8018-6(a).

[1] The parties did not request oral argument, and after examining the briefs and appellate record, the Court has determined unanimously that oral argument would not materially assist in the determination of this appeal. Fed. R. Bankr. P. 8012. The case is therefore ordered submitted without oral argument.

("Bank") to be nondischargeable pursuant to 11 U.S.C. § 523(a)(2)(A). Having reviewed the record and applicable law, we conclude that with respect to the requirement that Debtor must have intended to deceive Bank, material issues of fact are in dispute. Therefore, although the bankruptcy court correctly ruled that Bank had an enforceable debt against Debtor, summary judgment was not appropriate on the issue of nondischargeability. Accordingly, we affirm in part, reverse in part, and remand for further proceedings.

I. FACTUAL BACKGROUND

In 2001, Debtor secured several loans from Bank. Debtor borrowed the funds at the urging of, and on behalf of, Joseph D. Valdez, her former spouse ("Valdez"). At the time the loans were made, Valdez was president and chief operating officer of Bank. It is undisputed that upon receipt of the loan proceeds from Bank, Debtor immediately gave them to Valdez. The Bank would not have made the loans directly to Valdez because it would have been against policy to lend to an officer of Bank. In addition to Debtor, Valdez also used other "straw persons" to obtain loans for himself from Bank. Valdez made some payments on Debtor's loans, but then became delinquent. The Bank then contacted Debtor to bring the delinquencies current. Debtor informed Bank that she was not responsible for the loans, and advised Bank that it should contact Valdez for payment.

Upon discovery of the improper loans to Debtor and others in September 2002, Bank began negotiating with Valdez regarding repayment of the outstanding balances. This resulted in a Settlement Agreement ("Agreement")[2] entered into on November 3, 2003, by Bank, Valdez, and Gene Lee, another officer of Bank. Debtor was not a party to the Agreement. The Agreement and pay back covered twenty-one sham loans, as well as a shareholder loan that had

[2] Appellant's App. at 11.

been extended by Bank to Valdez.

The total amount of the outstanding loan balances covered by the Agreement plus legal expenses was $144,177. Valdez paid Bank only $71,402 of the total outstanding amount. This amount represented the proceeds of the sale to Gene Lee of his stock in Bank and related organizations, which was required pursuant to the Agreement. The $71,402 payment by Valdez was not allocated to any particular loan balances. Therefore, it is unclear whether Debtor's indebtedness was paid partially or in full. With respect to the remaining $72,775, Valdez's consideration under the Agreement consisted of several promises including the following: (1) a promise that other than the twenty-one loans covered under the Agreement, he was not involved in any other sham loans;[3] and (2) a promise that he would not compete or assist any other person or entity in competing with Bank for a period of three years.[4]

Paragraph 2 of the Agreement, which is critical to the dispute on appeal, provides as follows:

> The remaining balance due [Bank] by Valdez after the payment described in paragraph 1(h) immediately above is $72,775.00. Notwithstanding this remaining balance due [Bank] and Gene Lee promise, while Valdez is not in default of this Agreement, to consider, for purposes of this Agreement, the Accounts as paid in full. It is expressly agreed that [Bank] will not report to any credit reporting agency that the Accounts have been charged off but neither will [Bank] report the Accounts as settled or paid. [Bank] will not provide any additional reports to any credit reporting agency regarding the Accounts.[5]

About one year after the Agreement was executed, Gene Lee uncovered Valdez's involvement in at least one more sham loan which was not disclosed in the

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[3] *Agreement* at ¶ 3(a)-(f), *in* Appellant's App. at 12-13.

[4] *Id.* at ¶ 3(h), *in* Appellant's App. at 13-14.

[5] *Id.* at ¶ 2, *in* Appellant's App. at 12. The "Accounts" refer to the outstanding balances of the twenty-one sham loans and the shareholder loan listed on Exhibit A to the Agreement.

Agreement. The Bank deemed Valdez's failure to disclose this loan to be a breach of the Agreement. Bank gave Valdez written notice of this default in February, 2005.

Debtor filed her voluntary Chapter 13 petition on June 10, 2005. The case was subsequently converted to a Chapter 7 case on November 8, 2005. On February 17, 2006, Bank filed this adversary proceeding seeking to have the bankruptcy court declare nondischargeable Debtor's debt to Bank in the amount $7,702.68, plus interest at 19.99% per annum from December 21, 2003, pursuant to 11 U.S.C. § 523(a)(2), (a)(4) or (a)(6).[6] Debtor responded that any debt to Bank had been satisfied in full under the terms of the Agreement (specifically Paragraph 2 above), and further counterclaimed for declaratory judgment, damages, and attorney's fees and costs.

Based on the Agreement, Debtor filed a motion for summary judgment, claiming she had no enforceable debt to Bank and asking for dismissal of the proceeding. Bank then filed a cross-motion for summary judgment, arguing it was entitled to a judgment that the debt was nondischargeable pursuant to § 523(a)(2) and/or (a)(4).

The bankruptcy court found that the Agreement neither extinguished Debtor's original obligations to the Bank, nor substituted Valdez as the obligor to the Bank.[7] Additionally, the bankruptcy court determined that because Valdez was in default under the Agreement, Debtor's obligations at issue could not be considered paid in full.[8] Therefore, the bankruptcy court denied Debtor's motion for summary judgment and granted Bank's cross-motion for summary judgment.

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[6] Unless otherwise indicated, all future statutory references are to the Bankruptcy Code, Title 11 of the United States Code prior to enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

[7] *Memorandum Opinion* at 10, *in* Appellant's App. at 111.

[8] *Id.*

With respect to the § 523(a)(2) requirements, the bankruptcy court reasoned that it could infer that Debtor intended to trick the Bank into believing it was contracting with her when she was simply a nominal party to the transaction. Additionally, it found that Debtor knowingly falsely represented "herself as borrower to the Bank with intent that the Bank make the loan and without the present intent to repay."[9] The bankruptcy court then concluded that the debt was procured by false representations, false pretenses or actual fraud.[10] As a result, the court held that Debtor's obligations to Bank were nondischargeable pursuant to §523(a)(2)(A) and granted Bank's cross-motion for summary judgment. Debtor now timely appeals.

II. APPELLATE JURISDICTION

This Court has jurisdiction to hear timely-filed appeals from "final judgments, orders, and decrees" of bankruptcy courts within the Tenth Circuit, unless one of the parties elects to have the district court hear the appeal.[11] Neither party elected to have this appeal heard by the United States District Court for the District of New Mexico. The parties have therefore consented to appellate review by this Court.

A decision is considered final "if it 'ends the litigation on the merits and leaves nothing for the court to do but execute the judgment.'"[12] Here, the bankruptcy court determined that Bank's claim against Debtor could not be discharged. Nothing remains for the lower court's consideration. Thus, the order of the bankruptcy court is final for purposes of review.

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9 *Id.* at 14, *in* Appellant's App. at 115.

10 *Id.*

11 28 U.S.C. § 158(a)(1), (b)(1), and (c)(1); Fed. R. Bankr. P. 8002; 10th Cir. BAP L.R. 8001-1(a) & (d).

12 *Quackenbush v. Allstate Ins. Co.*, 517 U.S. 706, 712 (1996) (quoting *Catlin v. United States*, 324 U.S. 229, 233 (1945)).

III. STANDARD OF REVIEW

A ruling on summary judgment is reviewed *de novo*, applying the same legal standard used by the bankruptcy court.[13] Summary judgment is appropriate "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law."[14] "In reviewing a summary judgment motion, the court is to view the record 'in the light most favorable to the nonmoving party.'"[15]

IV. ANALYSIS

On appeal, Debtor asserts as follows: (1) the bankruptcy court erred in denying Debtor's motion for summary judgment because the Agreement constituted a novation which extinguished Debtor's obligations to Bank; and (2) the bankruptcy court erred in granting Bank's cross-motion for summary judgment because its finding that Debtor did not have the intent to repay the loans was clearly erroneous. Bank responds that the Agreement did not constitute a novation, and that Debtor admitted in her deposition that she did not intend to repay the debt at the time she entered into the loan transactions. In our view, the bankruptcy court correctly ruled that the Agreement did not constitute a novation, but genuine issues of material fact exist regarding Debtor's intent to deceive Bank. Therefore, Bank is not entitled to summary judgment that the debt is nondischargeable under § 523(a)(2)(A).

A. Debtor's Defense of Novation

As stated by the bankruptcy court, the term "novation" refers to an

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[13] *Kojima v. Grandote Int'l Ltd. Liability Co. (In re Grandote Country Club Co., Ltd.*), 252 F.3d 1146, 1149 (10th Cir. 2001).

[14] Fed. R. Civ. P. 56(c).

[15] *Grandote*, 252 F.3d at 1149 (quoting *Thournir v. Meyer*, 909 F.2d 408, 409 (10th Cir. 1990)).

agreement whereby parties to a contract substitute a new agreement and extinguish an old agreement.[16] Under New Mexico law, a novation requires "'(1) an existing and valid contract, (2) an agreement to the new contract by all parties, (3) a new valid contract, and (4) an extinguishment of the old contract by the new one.'"[17] Further, "there must be a clear and definite intention on the part of all concerned that such is the purpose of the agreement, for it is a well-settled principle that novation is never to be presumed."[18]

In reaching its conclusion that there was no novation and therefore Bank held an enforceable debt against Debtor, the bankruptcy court made three important determinations. First, it determined the second requirement of a novation was not present because Debtor was not a party to the Agreement.[19] Second, the bankruptcy court determined the "Agreement contained no language indicating that the Bank agreed to extinguish [Debtor's] obligations," and therefore the fourth requirement of a novation was not present.[20] And third, the bankruptcy court determined that, even if the Agreement could be construed to mean Debtor's obligations were paid in full, "it is undisputed that Valdez is in default under the [Agreement]; therefore, under the terms of the [Agreement], the obligations at issue cannot be considered paid in full."[21] On appeal, Debtor argues: (1) the law of novation does not require that she be a party to the

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16 *Memorandum Opinion* at 9, *in* Appellant's App. at 110.

17 *Summit Props., Inc. v. Pub. Serv. Co. of N.M.*, 118 P.3d 716, 726 (N.M. Ct. App. 2005) (quoting *Sims v. Craig*, 627 P.2d 875, 877 (N.M. 1981)).

18 *Sims v. Craig*, 627 P.2d 875, 877 (N.M. 1981) (internal quotation marks omitted).

19 *Memorandum Opinion* at 10, *in* Appellant's App. at 111.

20 *Id.*

21 *Id.*

Agreement;[22] (2) the Agreement's "paid in full" language could only mean full extinguishment of her obligations to Bank;[23] and (3) the issue of Valdez's default under the Agreement should be remanded for further factual findings. We believe the bankruptcy court correctly found that Valdez was in default under the Agreement, and that the default nullifies the treatment of the Accounts (Debtor's obligations) as "paid in full." Because this finding is determinative of the novation issue, we need not resolve Debtor's first two arguments above.

Under paragraph 2 of the Agreement, it unambiguously states that the "Accounts" will be considered as "paid in full" only if Valdez is not in default of the Agreement. Pursuant to paragraph 3 of the Agreement, Valdez promised that he had disclosed all improper loans made by Bank in which he was involved. With its motion for summary judgment, Bank tendered evidence of a breach of this promise. According to Gene Lee, in the fall of 2004, he discovered an

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[22] Debtor contends she need not be a party to the new contract because there is a presumption of her consent to an act done for her benefit. We note that although "agreement to the new contract by all parties" is routinely stated in cases as a general requirement of novation, according to the Restatement (Second) of Contracts, "a novation is possible without the assent of the obligor of the original duty or of the obligee of the new duty if that party is an intended beneficiary and does not disclaim." *Restatement (Second) of Contracts* § 280 cmt. c (1981). Bank argues that this section of the Restatement has not been adopted in New Mexico. However, at least two New Mexico appellate opinions cite to § 280. *See Quality Chiropractic, PC v. Farmers Ins. Co. of Ariz.*, 51 P.3d 1172, 1175 (N.M. Ct. App. 2002); *Speer v. Cimosz*, 642 P.2d 205, 208 (N.M. Ct. App. 1982). *See also* 30 *Williston on Contracts* § 76:13 (4th ed. 2007) (the issue of consent of the obligor of the old duty is not likely to arise often because the benefitted debtor is likely to be a donee and its assent can almost always be assumed).

[23] The bankruptcy court concluded there was no novation because the Agreement "contained no language indicating that the Bank agreed to extinguish [Debtor's original] obligations." *Memorandum Opinion* at 10, *in* Appellant's App. at 111. This is true. We note, however, that the law of novation does not require that the new contract *expressly* extinguish the old contract. Rather, it requires that there "be a clear and definite intention on the part of all concerned that such is the purpose of the agreement." *Sims v. Craig*, 627 P.2d 875, 877 (N.M. 1981) (internal quotation marks omitted). This is ordinarily a factual question which should be answered from any written agreements, together with all of the facts and circumstances surrounding the transactions.

additional sham loan in which Valdez participated.[24] Written notice of the default was given to Valdez in February 2005.[25] This evidence regarding default under the Agreement by Valdez was not controverted by Debtor. Accordingly, the bankruptcy court correctly rejected Debtor's defense of novation and concluded that Bank had an enforceable debt.

B. Disputed Facts Exist Regarding Debtor's Fraudulent Intent

In order for the bankruptcy court to declare Debtor's obligations on the loans nondischargeable pursuant to § 523(a)(2)(A), Bank must show by a preponderance of the evidence that "[t]he debtor made a false representation; the debtor made the representation with the intent to deceive the creditor; the creditor relied on the representation; the creditor's reliance was [justifiable]; and the debtor's representation caused the creditor to sustain a loss."[26] To sustain the bankruptcy court's grant of summary judgment on the nondischargeability of the debt, we must be convinced that there is no genuine issue as to any material fact relevant to the foregoing requirements. Here, we think Debtor has sufficiently disputed the issue of her alleged "intent to deceive" so as to prevent summary judgment.

As the bankruptcy court acknowledged, the issue of fraudulent intent is a material issue not easily subject to adjudication by summary judgment.[27] On appeal, Debtor does not dispute that she borrowed the funds from Bank on behalf of Valdez. She does, however, argue that she did not have the requisite intent to

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[24] *Affidavit of Gene Lee* at ¶¶ 7-9, *in* Appellant's App. at 81, attached to *Plaintiff's Motion for Summary Judgment and Memorandum Brief in Support*, *in* Appellant's App. at 66.

[25] *Affidavit of Gene Lee* at ¶ 11, *in* Appellant's App. at 82.

[26] *Fowler Bros. v. Young (In re Young)*, 91 F.3d 1367, 1373 (10th Cir. 1996).

[27] *Memorandum Opinion* at 12, *in* Appellant's App. at 113 (citing *Crossingham Trust v. Baines (In re Baines)*, 337 B.R. 392, 399 (Bankr. D.N.M. 2006)).

deceive Bank because: (1) she didn't know she was doing anything wrong, and (2) she knew that she ultimately would be required to repay if Valdez failed to keep his promise.[28] These arguments are supported by Debtor's deposition testimony.[29] If we take her statements at face value, which we are required to do for purposes of summary judgment, it is difficult to conclude that Debtor had an undisputed intent to deceive Bank when she borrowed the funds. We believe a genuine issue of fact exists with respect to Debtor's intent to deceive. Therefore, the bankruptcy court should not have summarily determined that § 523(a)(2)(A) barred discharge of the debt.

V. CONCLUSION

Viewing the record in the light most favorable to Debtor, Bank is not entitled to judgment as a matter of law. The bankruptcy court correctly ruled that Bank had an enforceable debt against Debtor. However, that portion of the summary judgment order determining Debtor's obligations to Bank to be nondischargeable is reversed and this case is remanded for further proceedings in accordance with this Order and Judgment.

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[28] Brief of Appellant at 15-17.

[29] *See January 22, 2007, Transcript of Deposition of Debtor* at 28, *ll.* 8-12, and 29-30, *ll.* 24-25 and 1-4, *in* Appellant's App. at 93-94.