NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE TENTH CIRCUIT

IN RE MARILYN J. ANDARAKES, also known as Lyn Andarakes, Debtor.	BAP No. WO-04-062
SOUTHEASTERN MEDICAL LABORATORIES, INC., Plaintiff – Appellant, v. MARILYN J. ANDARAKES, Defendant – Appellee.	Bankr. No. 03-14764-BH Adv. No. 03-01236-BH Chapter 7 ORDER AND JUDGMENT*

Appeal from the United States Bankruptcy Court
for the Western District of Oklahoma

Before CLARK, NUGENT, and BROWN, Bankruptcy Judges.

PER CURIAM.

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.

Southeastern Medical Laboratories, Inc. (SML) timely appeals a final Judgment entered by the United States Bankruptcy Court for the Western District

* This order and judgment is not binding precedent, except under the doctrines of law of the case, res judicata, and collateral estoppel. 10th Cir. BAP L.R. 8018-6(a).

of Oklahoma dismissing its nondischargeability Complaint against the Chapter 7 debtor, Marilyn J. Andarakes (Debtor).[1] The parties have consented to the jurisdiction of this Court because they have not elected to have this appeal heard by the United States District Court for the Western District of Oklahoma.[2] For the reasons stated below, the bankruptcy court's Judgment is AFFIRMED.

I. Background

The Debtor owns a 50% interest in an Oklahoma limited liability company, operating as "Horses First, L.L.C." (HF). Lance Graves (Lance) owns the other 50% interest in HF. Lance's father, Jim Graves (Graves), is the Chief Financial Officer of SML.

The Debtor owned a horse named "Tammy Leo," and both she and Lance jointly owned three other horses. Tammy Leo and the other jointly-owned horses were insured under a "Mortality Policy" owned by the Debtor, and the Debtor paid all premiums on this Policy. The horses were kept on the Debtor's property, and the Debtor incurred the costs of feeding and caring for them.

HF was formed by the Debtor and Lance to breed Tammy Leo with a stallion that appeared in the movie "Black Beauty," and to promote the offspring for sale. HF sold "Beanie Baby" horse dolls to promote the horse and to generate funds during the period that the horse was being shown for sale.

On Graves's suggestion, HF borrowed $32,200 from SML to have the Beanie Baby horse dolls manufactured. This loan is evidenced by a six-month Promissory Note. The Debtor and Lance personally guaranteed HF's debt under the Promissory Note in a Guaranty Agreement. The Promissory Note states that HF's payment is secured pursuant to a Security Agreement, under which HF purported to grant SML a security interest in the Debtor and Lance's four horses

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[1] 28 U.S.C. § 158(a)(1); Fed. R. Bankr. P. 8002(a).

[2] 28 U.S.C. § 158(b)-(c); Fed. R. Bankr. P. 8001(e).

and the Beanie Baby horse dolls. The Security Agreement makes no reference to an interest in sale proceeds from either the horses or the dolls.

SML extended the six-month term of the Promissory Note several times. HF made several interest payments to SML under the Promissory Note.

Tammy Leo died in September 1999, just prior to the time that the Promissory Note initially became due. The Debtor thus filed an insurance claim on Tammy Leo under her Mortality Policy. The insurer honored the claim by issuing a check payable to the Debtor in the amount of $10,000 (the "Proceeds"). The Debtor contacted Graves and asked him what to do with the Proceeds. On Graves's advice, the Debtor invested the Proceeds in a Certificate of Deposit (CD). The CD was obtained in the Debtor's name at a different bank than the one where HF had its account. While Graves and the Debtor's initial discussions about the CD assumed that the CD funds would be used to make a payment on the Promissory Note when it became due at the end of its extended term, the Debtor liquidated the CD and used the funds therefrom to pay her debts.

In July 2000, Lance took possession of the three jointly-owned horses that had previously been located on the Debtor's property without notifying the Debtor or obtaining her consent. In September 2000, SML commenced an action in state court for breach of contract against HF and the Debtor. It was after these events, sometime in 2001, that Debtor used the CD funds to pay her bills. She testified that the money was used to pay horse-related expenses.

On April 30, 2003, the Debtor filed a Chapter 7 petition. SML claims that the Debtor owed it approximately $21,000 as of the petition date. SML commenced an adversary proceeding against the Debtor pursuant to 11 U.S.C. § 523(a),[3] seeking to except a portion of her debt to it from discharge. It alleged

[3] All future statutory references in the text are to title 11 of the United States Code.

that the Debtor improperly used the Proceeds and, therefore, $10,000 of the Debtor's debt to it was nondischargeable under § 523(a)(4) and (a)(6).

The bankruptcy court conducted a trial on SML's Complaint, at the conclusion of which it stated its findings of fact and conclusions of law on the record. It refused to except the Debtor's debt to SML from discharge. The bankruptcy court's findings of fact and conclusions of law are incorporated by reference in its separate Judgment in favor of the Debtor.

This appeal followed.

II. Discussion

Section 523(a) states, in relevant part, that:

> (a) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt–
>
> . . . .
>
> (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny;
>
> . . . .
>
> (6) for willful and malicious injury by the debtor to another entity or to the property of another entity[.][4]

To except a debt from discharge under these provisions, SML was required to prove each element by a preponderance of the evidence.[5] For the reasons stated below, the bankruptcy court did not err in concluding that SML failed to prove nondischargeability under § 523(a)(4) or (a)(6).

A. The bankruptcy court did not err in refusing to except the Debtor's debt to SML from discharge under § 523(a)(4)

Section 523(a)(4) makes a debt nondischargeable for three reasons: (1) fraud or defalcation while acting as a fiduciary; (2) embezzlement; or (3) larceny. SML did not assert that the debt it is seeking to except from discharge is for fraud

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[4] 11 U.S.C. § 523(a)(4) & (a)(6).

[5] Grogan v. Garner, 498 U.S. 279 (1991).

while acting in a fiduciary capacity.[6] Thus, the only issue is whether the bankruptcy court erred in refusing to except the Debtor's debt to SML from discharge as arising from embezzlement or larceny.

"[E]mbezzlement is defined under federal common law as 'the fraudulent appropriation of property by a person to whom such property has been entrusted or into whose hands it has lawfully come.'"[7] While the definition of "larceny" under § 523(a)(4) is not settled, under any definition of the term, it must be shown that the debtor took property belonging to another person or entity.[8] Thus, for a debt to arise from embezzlement or larceny, the debtor must take property belonging to another.

SML admits that only the Debtor owned Tammy Leo and the Mortality Policy. As a result, the Debtor owned the Proceeds, and her use of them did not amount to embezzlement or larceny because she did not take something that she did not own.

Furthermore, embezzlement did not occur as a result of HF's pledge of Tammy Leo as collateral under the Security Agreement. HF did not own Tammy Leo and, therefore, it could not pledge the horse as collateral or claim an interest in the Proceeds. Even if HF could have pledged Tammy Leo, the Security Agreement does not give SML an interest in the Proceeds. SML, therefore, has no interest in Tammy Leo or the Proceeds, and the Debtor had no legal obligation to give the Proceeds to SML. The Debtor simply did not appropriate funds in which SML held an interest.

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6 Transcript at 5, Appellant's Appendix at 33.

7 Klemens v. Wallace (In re Wallace), 840 F.2d 762, 765 (10th Cir. 1988 (further quotation omitted); Driggs v. Black (In re Black), 787 F.2d 503, 507 (10th Cir. 1986), *abrogated on other grounds*, Grogan, 498 U.S. at 279; Cousatte v. Lucas (In re Lucas), 300 B.R. 526, 531 (10th Cir. BAP 2003).

8 *See*, e.g., 52A C.J.S. *Larceny* § 1(1) (1968).

SML disputes the conclusion that it lacked an interest in the Proceeds. While it admits that the Debtor, not HF, owns Tammy Leo and the Mortality Policy, it claims that the Promissory Note and Security Agreement were actually made by the Debtor and Lance, not HF. SML points out that both documents are signed by the Debtor and Lance without any statement as to their representative capacity, and other statements in the documents are confusing.

This argument is deemed waived because it was not raised below.[9] But, even if it had not been waived, it is without merit because the record shows that HF, not the Debtor and Lance, incurred the debt.

The Promissory Note states that the "undersigned" promises to pay . . . .[10] At the bottom of the Note, is the following:

> HORSES FIRST, LLC
>
> By:
>
> /s/ The Debtor
> /s/ Lance[11]

The Security Agreement states "Horses First, LLC" was the pledging party.[12] It is signed in the same way as the above-quoted Promissory Note. A Guaranty Agreement was given by the Debtor and Lance to secure the debt of the "Borrower" "Horses First, LLC."[13] Graves testified that he advised the Debtor and Lance to set up a LLC to protect themselves. Finally, at trial, SML assumed that the Debtor executed the Promissory Note and Security Agreement "on behalf

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[9] *See, e.g.*, Tele-Communications, Inc. v. Comm'r, 104 F.3d 1229, 1233 (10th Cir. 1997) (appellate court will not consider issues not raised below); Walker v. Mather (In re Walker), 959 F.2d 894, 896 (10th Cir. 1992) (same).

[10] Promissory Note at 1, Appellant's Appendix at 168.

[11] *Id.*

[12] Security Agreement at 1, Appellant's Appendix at 169.

[13] Guaranty Agreement at 1, Appellant's Appendix at 172.

of" HF, and the Debtor testified that she had done so.[14] Based on the entire record, the debt was incurred by HF, not the Debtor.

B. The bankruptcy court did not err in refusing to except the Debtor's debt to SML from discharge under § 523(a)(6)

It is well-established that a cause of action under § 523(a)(6) requires proof that a debtor deliberately or intentionally injured the plaintiff-creditor, "not merely a deliberate or intentional act that leads to injury."[15] The bankruptcy court concluded that there was no evidence that the Debtor deliberately and intentionally intended to injure SML by using the Proceeds. Our review shows that this conclusion is fully supported by the record.

A § 523(a)(6) action such as the present one typically involves a debtor's improper use of collateral. For the reasons discussed above, the Debtor did not use SML's collateral. SML, having no right to the Proceeds, cannot complain because the Debtor used them in a way that was contrary to its expectations.

III. Conclusion

The bankruptcy court's Judgment is AFFIRMED.

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[14] Transcript at 47 & 49, Appellant's Appendix at 130 & 132.

[15] Kawaauhau v. Geiger, 523 U.S. 57, 61 (1998).