

§ 727(a)(4)(A)

UST v. Chin, Adversary No. 04-3066-rld
Clifford Hom Chin and Gayle Robyne Chin, Case No. 03-40816-rld7

12/17/2004 RLD

Unpublished

In this adversary proceeding opinion decided December 17, 2004, the bankruptcy court denied discharge to chapter 7 debtors pursuant to § 727(a)(4)(A).

P04-5(24)

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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In Re:)	
)	Bankruptcy Case
CLIFFORD HOM CHIN and GAYLE)	No. 303-40816-rld7
ROBYNE CHIN,)	
)	
Debtors.)	
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U.S. TRUSTEE,)	
)	Adv. Proc. No. 04-3066-rld
Plaintiff,)	
)	MEMORANDUM OPINION
v.)	
)	
CLIFFORD HOM CHIN and GAYLE)	
ROBYNE CHIN,)	
)	
Defendants.)	
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The United States Trustee's ("UST") adversary Complaint to deny a discharge to the debtors Clifford Hom Chin and Gayle Robyne Chin (the "Chins") pursuant to 11 U.S.C. § 727(a)(4)¹ (the "Adversary Proceeding") was tried on November 22-23, 2004 (the "Trial"). At the Trial, I also heard the UST's Motion to Dismiss

¹ Hereafter, unless otherwise noted, all statute references are to the federal Bankruptcy Code, 11 U.S.C. §§ 101 et seq.

1 Mr. Chin with whatever work needed to be done at Lucky Produce.

2 In 2001, the Chins refinanced their home and became
3 acquainted with mortgage broker Jeff Johnson. According to
4 Mr. Chin, it was Mr. Johnson who convinced him to enter the real
5 estate investment business, initially through an entity called US
6 Financial Investments LLC ("US Financial"). See Ex. 2, pp. 14-17;
7 Exhibit 3, p. 51. Mr. Chin worked through US Financial to acquire
8 real properties from approximately December 2001 to March 2002. See
9 Ex. 3, p. 51. Later, the Chins worked with C.J. Brigham, who was
10 introduced to them by Jeff Johnson, through an entity called Real
11 Estate Investment Pros LLC ("REIP"), from approximately March 2002
12 to May 2003. See Ex. 2, pp. 17-19; Ex. 3, p. 51.

13 The Chins' career in real estate was spectacular, but
14 ultimately unsuccessful. Between December 2001 and February 2003,
15 the Chins bought a total of 38 properties. See Ex. 1. During the
16 period from approximately December 24, 2001, through February 20,
17 2003, Mr. Chin, Mrs. Chin or both made an approximate total of 46
18 loan applications and borrowed approximately \$10,538,750, secured by
19 their real estate purchases. See Ex. 1, p. 2; Ex. 6.

20 The Chins' real estate acquisitions followed a pattern:
21 Mr. Johnson or Mr. Brigham would locate the properties to be
22 purchased. Each property would be purchased initially by US
23 Financial or REIP, as the case may be, and Mr. Chin, Mrs. Chin or
24 both would buy the property from US Financial or REIP at a greater
25 purchase price. The transactions would close simultaneously in a
26 double escrow. Mr. Chin initially, and later Mrs. Chin, because

1 Mr. Chin's credit was "getting bad," would borrow personally to fund
2 the real estate purchases. US Financial or REIP would receive a
3 distribution from escrow that represented "profit," according to
4 Mr. Chin. Mr. Johnson, from US Financial, and Mr. Brigham, from
5 REIP, would take their profits up front and not return any money to
6 the entities.

7 From approximately April 2002, Mrs. Chin did the bookkeeping
8 for REIP, using a Quickbooks ledger that she maintained on her home
9 computer. The parties are agreed that substantial sums received by
10 the Chins from the escrows and from US Financial and REIP were used
11 to fund loan repayments and repairs/renovations to the purchased
12 properties. According to the Chins, the idea behind both US
13 Financial and REIP was to acquire properties to rehab and sell at a
14 profit. However, the Chins admitted during their testimony that
15 some of the money they received was used to pay their personal
16 expenses.

17 During the time that the Chins owned real estate investment
18 properties, the properties generated rents totaling \$388,922
19 deposited in REIP accounts. See Ex. 10. However, according to
20 Mr. Chin, the real estate investment business grew too fast, with
21 neither adequate capital nor sufficient income to complete the work
22 required on most of the properties to allow for profitable resale.
23 Mr. Chin testified that he was not really sure but thought that two
24 or three of the properties were sold, with the rest being lost
25 through foreclosure or "short sale." By the end of 2002, the real
26 estate investment business was in trouble, and title to most of the

1 properties was transferred to Mrs. Chin in January 2003. Such
2 transfers were C.J. Brigham's idea, according to Mr. Chin, to give
3 the Chins more time to get new loans or negotiate new payment
4 arrangements with lenders, in order to keep the properties. The
5 Chins' maneuvering was unavailing, and they filed their chapter 7
6 petition in September 2003, on the eve of entry of a substantial
7 default judgment against them.

8 In their Statement of Financial Affairs ("SOFA") filed with
9 their bankruptcy petition, in their response to Item 1, the Chins
10 listed their gross income for the last three years as follows:
11 2001-\$34,384 from Lucky Produce, Inc.; 2002-\$9,000 from Lucky
12 Produce, Inc.; and 2003-\$3,000 from T.P. Produce, Inc. The Chins
13 did not disclose any income from rents or otherwise with respect to
14 US Financial or REIP for any of those years. See Ex. 3, p. 41. In
15 their SOFA, in their response to Item 19d., the Chins responded
16 "None" to the request to list financial institutions or other
17 parties to whom the Chins had issued financial statements during the
18 two years immediately preceding their bankruptcy filing. At their
19 Section 341(a) meeting, the Chins and their counsel advised the
20 trustee that their response to Item 19d. to the SOFA was incorrect
21 and apparently provided to the trustee a list of individuals and/or
22 financial institutions to which financial statements were given.
23 See Ex. 2, p. 9. However, counsel for the Chins also stated at
24 their 341(a) meeting that the Chins' schedules and SOFA would be
25 amended. See Ex. 2, pp. 6 and 9. Thereafter, the Chins never
26 amended their bankruptcy schedules or SOFA.

1 On or about February 27, 2004, the UST filed the Complaint in
2 the Adversary Proceeding and the Motion to Dismiss, based
3 essentially on the inaccurate responses stated by the Chins in Items
4 1 and 19d. of their SOFA.

5 Generally Applicable Legal Standards

6 A primary objective of the Bankruptcy Code is to provide a
7 fresh start to debtors overburdened by debts they cannot pay.
8 Consistent with that social welfare objective, I start from the
9 proposition that the denial of discharge provisions of the
10 Bankruptcy Code are interpreted strictly in favor of debtors. "A
11 denial of a discharge is an act of mammoth proportions, and must not
12 be taken lightly. In light of this gravity, this Court and many
13 others have stated that Section 727 must be construed liberally in
14 favor of the debtor and against the objector." In re Goldstein, 66
15 B.R. 909, 917 (Bankr. W.D. Pa. 1986). See In re Adeeb, 787 F.2d
16 1339, 1342 (9th Cir. 1986); and In re Devers, 759 F.2d 751, 754 (9th
17 Cir. 1985).

18 Nevertheless, the opportunities for a new beginning afforded
19 by the Bankruptcy Code are limited to the "honest but unfortunate
20 debtor." See Cohen v. De La Cruz, 523 U.S. 213, 217 (1998) (citing
21 Grogan v. Garner, 498 U.S. 279, 286-87 (1990)). The dishonest
22 debtor, however unfortunate, does not get the benefit of a discharge
23 in bankruptcy.

24 The party seeking to prevent a debtor's discharge bears the
25 burden of proof. See In re Johnson, 68 B.R. 193, 198 (Bankr. D. Or.
26 1986). Since the United States Supreme Court's decision in Grogan

1 v. Garner, the burden of proof standard for actions to deny the
2 debtor a discharge under Section 727 is preponderance of the
3 evidence. See In re Hoblitzell, 223 B.R. 211, 215 (Bankr. E.D. Ca.
4 1998); and Garcia v. Coombs, 193 B.R. 557, 560 (Bankr. S.D. Ca.
5 1996). In addition, once the complaining party has presented a
6 prima facie case for denial of the debtor's discharge, the burden
7 shifts to the debtor to offer a credible justification in defense.
8 See, e.g., In re Devers, 759 F.2d at 754 ("While the burden of
9 persuasion rests at all times on the creditor objecting to the
10 discharge, it is axiomatic that the debtor cannot prevail if he
11 fails to offer credible evidence after the creditor makes a prima
12 facie case."); Chalik v. Moorefield, 748 F.2d 616, 619 (11th Cir.
13 1984); and Montey Corp. v. Maletta, 159 B.R. 108, 112 (Bankr. D.
14 Conn. 1993) ("Where persuasive evidence of a false statement under
15 oath has been produced by a plaintiff, the burden shifts to the
16 defendant to prove that it was not intentionally false [citations
17 omitted] and fraudulent intent may be inferred, if the false
18 statement is not explained.").

19 An essential element required to deny a debtor a discharge
20 under many of the subsections of Section 727(a), including Section
21 727(a)(4), is fraudulent intent. Recognizing the reality that few
22 debtors are likely to break down and confess to fraud on the witness
23 stand, fraudulent intent may be established through circumstantial
24 evidence or evidence of a pattern of conduct consistent with the
25 misconduct alleged. See, e.g., In re Adeeb, 787 F.2d at 1343; In re
26 Devers, 759 F.2d at 754; and In re Johnson, 68 B.R. at 198.

1 The foregoing general principles govern the following
2 analysis of the specific cause of action asserted in the Adversary
3 Proceeding and the evidence presented.

4 727(a)(4)

5 Section 727(a)(4)(A) denies a discharge to a debtor who
6 knowingly gives a false oath or account in connection with his or
7 her bankruptcy case. "Section 727(a)(4)(A) requires the denial of a
8 discharge if: (1) the debtor knowingly and fraudulently made a false
9 oath; and (2) the false oath related to a material fact." In re
10 Ford, 159 B.R. 590, 593 (Bankr. D. Or. 1993), citing In re Aubry,
11 111 B.R. 268, 274 (9th Cir. BAP 1990).

12 In this context, "materiality" is interpreted broadly. To
13 justify denying a discharge to a debtor, the false oath must relate
14 to a fact or facts important to an understanding of the debtor's
15 financial or business affairs, or assets or liabilities. "A false
16 statement is material if it bears a relationship to the debtor's
17 business transactions or estate, or concerns the discovery of
18 assets, business dealings, or the existence and disposition of the
19 debtor's property." In re Wills, 243 B.R. 58, 62 (9th Cir. BAP
20 1999).

21 As noted above, the element of a false oath made with knowing
22 and fraudulent intent may be established by circumstantial evidence
23 and/or evidence of a pattern of conduct representing "a reckless
24 indifference to truth equivalent to fraud." Boroff v. Tully, 818
25 F.2d 106, 108, 112 (1st Cir. 1987). See also Hatton v. Spencer, 204
26 B.R. 477, 484 (E.D. Va. 1997). However, it is important not to lose

1 sight of the requirement under § 727(a)(4) that the complaining
2 party has the burden of proof to establish that the debtor defendant
3 acted with actual intent to defraud.

4 The essential point is that there must be something
5 about the adduced facts and circumstances which
6 suggest[s] that the debtor intended to defraud
7 creditors or the estate. For instance, multiple
8 omissions of material assets or information may well
9 support an inference of fraud if the nature of the
10 assets or transactions suggests that the debtor was
11 aware of them at the time of preparing the schedules
12 and that there was something about the assets or
13 transactions which, because of their size or nature, a
14 debtor might want to conceal....In other words, is
15 there something about the omitted asset or transaction
16 which a debtor might want to avoid disclosing.

17 Garcia v. Coombs, 193 B.R. at 565. [Emphasis added.]

18 A. The UST's Case.

19 Mr. Chin testified on direct examination by the UST that the
20 Lucky Produce business grossed approximately \$50,000 in 2001 and
21 \$9,000 in 2002. While it is unclear from the record why the Chins
22 included the entire gross income for Lucky Produce in 2002 but only
23 a portion of its gross income for 2001 in their response to Item 1
24 on their SOFA, I find that the difference in reporting 2001 gross
25 income for Lucky Produce on the Chins' SOFA is immaterial.

26 Ms. Tammy Combs, the UST's accountant/financial analyst,
27 testified regarding her investigation of the Chins' financial
28 affairs, including review of the Chins' real estate investment
29 activities in conjunction with US Financial and REIP. Ms. Combs
30 reviewed the Chins' personal bank statements and account information
31 and various loan applications signed and submitted by the Chins to
32 potential lenders. In addition, Ms. Combs printed out and reviewed

1 the information contained on the backup disc for the REIP Quickbooks
2 ledger that the Chins delivered to the trustee at their 341(a)
3 meeting, and reviewed REIP bank account information and
4 documentation. See Ex. 9.

5 Based upon Ms. Combs' review and analysis, she testified that
6 a total of \$1,815,522.45, including \$388,922 in rental income, was
7 deposited into REIP bank accounts. See Ex. 10. From those
8 deposits, approximately \$1,604,086 apparently was disbursed directly
9 to pay real estate investment related expenses. See Ex. 35.

10 Ms. Combs testified that \$120,806.70 in checks were written on the
11 REIP bank accounts and deposited into the Chins' personal bank
12 accounts. See Ex. 5, p. 16. Ms. Combs further testified, that
13 giving the benefit of the doubt to the Chins, it appears that
14 \$90,628.55 of personal expenses of the Chins were paid directly with
15 disbursements from the REIP accounts. See Ex. 5, pp. 5-15.

16 Looking at the Chins' personal bank accounts for the period
17 December 2001 through October 14, 2003, the Chins deposited a total
18 of \$318,663.19 into their personal bank accounts from (a) REIP
19 account disbursements, (b) escrow proceeds from real estate
20 investment related loan transactions, and (c) all other sources.
21 See Ex. 8, particularly pp. 1-3. Ms. Combs testified that the Chins
22 deposited \$128,579.95 into their personal accounts from real
23 property closing escrows. Reviewing the disbursements records from
24 the Chins' personal bank accounts, and again giving the benefit of
25 the doubt to the Chins, Ms. Combs testified that disbursements for
26 real estate investment or unknown expenses between December 16,

1 2001, and May 23, 2003, totaled \$139,398.53. See Ex. 11. Ms. Combs
2 further testified that the Chins apparently spent \$176,244 from
3 their personal accounts to pay personal expenses unrelated to the
4 real estate investment business.

5 In summary, based upon her review and analysis of the Chins'
6 financial records and the real estate investment records, including
7 the Quickbooks ledger and bank account information available for
8 REIP, Ms. Combs testified that the Chins deposited \$318,663.19 into
9 their personal bank accounts and used approximately \$266,873 to pay
10 personal expenses during the period when they reported total gross
11 income under penalties of perjury in their response to Item 1 in
12 their SOFA of \$46,384. See Ex. 3, p. 41; Ex. 11, p. 1.

13 Cross examination of Ms. Combs included review of the Chins'
14 Exhibits A through D and L, prepared from the REIP Quickbooks ledger
15 by Mrs. Chin, showing a total of \$893,103 in disbursements for real
16 estate business related expenses. Except for a check written for
17 \$3,500 cash by Mr. Chin, included on Exhibit C, p.36, with respect
18 to which Ms. Combs could not determine the use (see Ex. 5, p. 4),
19 Ms. Combs testified that she had not included any of the expenses
20 listed in the Chins' Exhibits A through D and L in her calculation
21 of the Chins' personal use of cash. In Exhibits A through D and L,
22 the Chins did not include any disbursements to pay their personal
23 expenses from REIP, even though both of the Chins admitted during
24 their testimony at the Trial that some of their personal expenses
25 were paid from the REIP accounts.

26 During the course of his direct examination for the defense,

1 Mr. Chin testified that certain expenses categorized as personal by
2 Ms. Combs at pages 5-14 of Exhibit 5 actually covered business
3 expenses of Lucky Produce and the Chins' real estate enterprises,
4 including the following: Bank of America (credit card), Capital One
5 Services (credit card), \$5,000 cash (\$1,800 to counsel,
6 Mr. Schaller, and \$3,200 to C.J. Brigham), \$2,704 cash (to pay for
7 appraisal services), \$2,000 (to pay for title services), Home Depot,
8 Lucky Produce (\$10,000 loan), Sears, US Bank (credit card), and
9 Wells Fargo (to open account).²

10 In her direct testimony for the defense, Mrs. Chin testified
11 that she agreed with Mr. Chin's characterizations of certain of the
12 "personal expenses" listed in Pages 5-14 of Exhibit 5 as in reality
13 business expenses. In addition, she noted that \$2,704 of cash
14 expenditures and customer withdrawals on pages 6-7 of Exhibit 5 were
15 duplicate entries.

16 Accepting the Chins' testimony regarding what constituted
17 "business" as opposed to "personal" expenses in the UST's Exhibit 5
18 categorizations at face value³, and adding the \$3,500 check written
19 by Mr. Chin to "cash" on June 27, 2002, included on Exhibit C, a
20 total of \$56,860.62 would need to be deducted from Ms. Combs'

21 ² Ms. Combs previously testified that she assumed most credit
22 card charges did not represent business expenses because the Chins'
23 tended to write checks to cover their business expenses.

24 ³ I have not deducted \$10,255 in payments to Hubert Chin to
25 repay a loan(s), to make a loan and to pay \$80 for computer hookup
26 charges, as testified to by Mr. Chin. Nothing in Mr. Chin's
testimony connects any of those payments to the Lucky Produce
business or the Chins' real estate investment business.

1 estimate of \$266,873 in personal expenditures. However, after
2 deducting that total, the Chins still spent approximately
3 \$210,012.38 for personal expenses during the period when they
4 reported total gross income of \$46,384 in their response to Item 1
5 on their SOFA.

6 The Chins did not include any of the \$388,922 in rental
7 income from their investment properties in their report of gross
8 income in response to Item 1 in their SOFA. Counsel for the Chins
9 argued that excluding the Chins' rental income from their SOFA
10 disclosures was appropriate because any rental income received was
11 offset by expenditures for the investment properties. However, the
12 Chins were not so fastidious with respect to the income information
13 they included in financial statements presented to lenders.

14 From February 15, 2002, through November 19, 2002, one or the
15 other of the Chins, or both, presented approximately 46 loan
16 applications including personal financial statements to potential
17 lenders. See Ex. 6. In the 31 loan applications presented by
18 Mr. Chin individually, he stated his monthly gross income as \$12,000
19 in one application, \$18,000 in one application, \$25,000 in 28
20 applications, and \$37,000 in one application. See Ex. 6 and Ex. 7,
21 pp. 1-9. In his loan applications, Mr. Chin stated his monthly
22 gross rental income as ranging from a low of \$1,200 to a high of
23 \$57,050. See Ex. 6. In the 12 loan applications presented by
24 Mrs. Chin individually, she reported her monthly gross income in a
25 range from \$6,500 to \$18,475. See Ex. 6 and Ex. 7, pp. 10-28. She
26 reported monthly gross rental income ranging from \$0 to \$22,495.

1 See Ex. 6. In two of the three loan applications presented jointly
2 by the Chins, they stated their monthly gross income was \$25,000.

3 See Ex. 6, p. 1. In both of those applications, the Chins reported
4 their monthly gross rental income as \$7,900. See Ex. 6, p. 1.

5 Mr. Chin admitted during direct examination by the UST that
6 he never earned wages of either \$12,000 or \$25,000 a month, although
7 he argued that he might have had rental income in such amounts.

8 Mrs. Chin likewise admitted during cross-examination by the UST that
9 she never earned \$10,500, \$18,000 or \$25,000 a month, either
10 individually or jointly with her husband.

11 Both Mr. and Mrs. Chin testified that C.J. Brigham prepared
12 the Exhibit 6 financial statements that they signed. Mr. Chin
13 testified that he noticed an error in listing a 2002 Mercedes that
14 Mr. Chin did not own on a financial statement that he signed, but
15 Mr. Brigham told him not to worry because he would take care of it
16 later. See Ex. 7, p. 2. Mrs. Chin testified that she brought
17 problems in the financial statements that she and her husband
18 signed, such as listing them as single or unmarried and including
19 inaccurate income information, to Mr. Brigham's attention from the
20 beginning when she started signing financial statements in April
21 2002.

22 I find the Chins' attempts to lay all of the inaccuracies in
23 the income information included in their financial statements at the
24 doorstep of Mr. Brigham not credible in light of the fact that the
25 Chins apparently kept signing multiple, clearly inaccurate financial
26 statements over a period of at least ten months, without ever making

1 any effort to correct the misinformation that was being communicated
2 to their lenders. In particular, Mrs. Chin testified that she
3 recognized the inaccuracy of the income information included in the
4 first financial statements that Mr. Brigham prepared for her to
5 sign. Yet, when confronted with inaccurate income information in a
6 financial statement that she signed four months later, her first
7 reaction was to lie and testify that she did not recall whether her
8 gross income was \$10,500 per month, before admitting that she never
9 made that much.

10 The evidence presented by the UST tends to establish that the
11 Chins engaged in a pattern of misrepresenting their income in
12 financial statements during the heady period of their participation
13 in the real estate game, that the UST goes on to argue was carried
14 over into misrepresentations of their income in their response to
15 Item 1 in their SOFA.

16 The UST argued that the discrepancies between the Chins'
17 actual income and the income reported in response to Item 1 of their
18 SOFA were material to an appropriate examination of the Chins'
19 financial affairs. I agree, and I find that the UST presented a
20 sufficient prima facie case to establish that the Chins knowingly
21 and fraudulently made a false oath when they signed off on
22 inaccurate income information in their SOFA.

23 B. The Case for the Defense.

24 The Chins raised a number of defenses to the UST's claims.
25 First, while the Chins testified that they read their bankruptcy
26 schedules and SOFA before signing them and thought they were

1 accurate, Mr. Chin testified that the Chins were under the stress of
2 a deadline to file their bankruptcy petition before a default
3 judgment could be taken against them. He testified that he just
4 "skimmed" the schedules and SOFA and later recognized that they
5 contained errors. He further testified that errors were brought to
6 the attention of the trustee at the Chins' 341(a) meeting.

7 At the outset, this court does not take lightly the
8 obligations of debtors to list their assets and liabilities and give
9 a report of their affairs accurately in their bankruptcy schedules
10 and statements of financial affairs under penalties of perjury.

11 ...[T]he very purpose of certain sections of the law,
12 like 11 U.S.C. § 727(a)(4)(A), is to make certain that
13 those who seek the shelter of the bankruptcy code do
14 not play fast and loose with their assets or with the
15 reality of their affairs. The statutes are designed
to insure that complete, truthful, and reliable
information is put forward at the outset of the
proceedings, so that decisions can be made by the
parties in interest based on fact rather than fiction.

16 Boroff v. Tully, 818 F.2d at 110.

17 The fact alone that a debtor, through ignorance or otherwise,
18 takes a casual approach to the process of preparing and signing his
19 or her bankruptcy schedules and statement of financial affairs may
20 not be dispositive to establish that the debtor knowingly and
21 fraudulently made a false oath. However, if such schedules and/or
22 statements of financial affairs prove to be materially inaccurate,
23 evidence of such inaccuracies may establish such reckless disregard
24 for the truth or fit within a pattern of providing false
25 information, as to justify denying a discharge to the debtor. See,
26 e.g., Hatton v. Spencer, 204 B.R. 477 (E.D. Va. 1997); and Mosley v.

1 Sims, 148 B.R. 553, 557 (Bankr. E.D. Ark. 1992) (“...Willie Sims
2 asserts that he merely ‘glanced over’ the petition but ‘didn’t
3 really understand it.’ However, the Bankruptcy Code requires more
4 than a ‘glance over’ in reporting assets and transactions. Indeed,
5 a mere ‘glance over’ constitutes a cavalier and reckless disregard
6 for truth which is inconsistent with the relief to be afforded the
7 honest debtor.”).

8 In this case, based upon the foregoing review of evidence
9 submitted by the UST, there is substantial evidence that the Chins
10 under-reported their income in their response to Item 1 in their
11 SOFA. In addition, the Chins reported “None,” in response to the
12 request in Item 19d. of their SOFA to list parties to whom the Chins
13 had issued financial statements during the two years preceding their
14 bankruptcy filing. At their 341(a) meeting, counsel for the Chins
15 apparently delivered to the trustee a list of parties to whom the
16 Chins had given financial statements. However, despite a commitment
17 to the contrary by counsel for the Chins at their 341(a) meeting,
18 the Chins never amended their schedules or SOFA. Accordingly, the
19 Chins never amended their report of gross income in their response
20 to Item 1 in their SOFA, and there is nothing in the evidentiary
21 record to establish what the Item 19d. list delivered to the trustee
22 contained. If Exhibit 6, with its listing of 46 loan applications
23 with financial statements, is any indication, the list must have
24 been lengthy. Yet, it was delivered in the context of the following
25 statement by Mr. Chin in response to the trustee’s question: “To the
26 best of your knowledge is the information contained in the

1 petitions, schedules, statements and related documents true and
2 correct?" Mr. Chin: "Some of it was just a little bit off." Ex. 2,
3 p. 5.

4 Whether or not the income information included in their SOFA
5 was inaccurate, the Chins further argue that any income, including
6 rental income, generated by their real estate investment ventures
7 was offset by expenses for the properties. Consequently, in the
8 Chins' view, such income did not need to be reported in their
9 response to Item 1 in their SOFA, in spite of the fact that the Item
10 1 request for information refers to "gross income." See Ex. 3,
11 p. 41. The Chins also contend that money received from their real
12 estate investment enterprises was not income because it consisted of
13 loan proceeds.

14 There is a line of authority, as cited by counsel for the
15 Chins in argument at the Trial, to the effect that loan proceeds
16 generally are not included in gross income for tax purposes. See,
17 e.g., Oliver v. United States, 193 F. Supp. 930, 934 (E.D. Ark.
18 1961); Stayton v. Commissioner, 32 B.T.A. 940 (1935); and Dilks v.
19 Commissioner, 15 B.T.A. 1294 (1929), aff'd, 69 F.2d 1002 (7th Cir.
20 1934.)

21 However, even within the line of authority cited by counsel
22 for the Chins, the Supreme Court has characterized income as
23 including "undeniable accessions to wealth, clearly realized, and
24 over which the taxpayers have complete dominion." Commissioner v.
25 Glenshaw Glass Co., 348 U.S. 426, 431 (1955). See also Eisner v.
26 Macomber, 252 U.S. 189, 206-07 (1920). The definition of "gross

1 income" in the Internal Revenue Code of 1986, as amended,
2 specifically includes "rents" as an example. See 26 U.S.C.
3 § 61(a)(5).

4 In bankruptcy, the concept of "income" or "gross income" is
5 flexible. "The term 'gross income' should not convey the same
6 definite and inflexible significance under all circumstances and
7 wherever used. It is a term whose construction and meaning depends
8 on the context of the subject matter." Shelley v. Kendall, 184 B.R.
9 356, 359 (9th Cir. BAP 1995), aff'd, 109 F.3d 639 (9th Cir. 1997).

10 The factual evidence presented at the Trial tends to vitiate
11 the effectiveness of the Chins' legal arguments that funds they
12 received from their real estate investments should not be considered
13 income. On direct examination by the UST, Mr. Chin testified with
14 regard to a number of specific transactions that funds paid to REIP
15 from the double closings represented profits. He further testified
16 that Jeff Johnson and C.J. Brigham took their profits from the US
17 Financial and REIP transactions up front and paid nothing for
18 maintenance, improvements or service of indebtedness with respect to
19 any of the investment properties. See Ex. 2, pp. 16, 18-19, 100-01.
20 Mr. Johnson and Mr. Brigham clearly realized "income" out of the
21 loan proceeds generated in relation to the real estate investment
22 transactions.

23 The UST established through admitted exhibits and the
24 testimony of Ms. Combs, as clarified by the testimony of Mr. and
25 Mrs. Chin, that the Chins paid personal expenses that exceeded the
26 income they reported in their response to Item 1 in their SOFA by a

1 range of from \$150,000 to \$200,000 for the subject time period. By
2 paying those personal bills, the Chins exercised "complete dominion"
3 over those funds and effectively realized income.

4 A primary source of information regarding the Chins' receipt
5 of funds and their payment of personal expenses was their personal
6 bank account records. See Exs. 5 and 8. Bank deposits can be
7 considered as evidence of income in appropriate circumstances. See
8 Mills v. Commissioner, 399 F.2d 744, 749 (4th Cir. 1968) ("In the
9 absence of records kept by the taxpayer showing the source of his
10 cash receipts the Commissioner may look to other sources of
11 information to establish income, and may take into account, as prima
12 facie evidence of income, bank deposits made by the taxpayer during
13 the years in question." [Emphasis added.]). See also Ruark v.
14 Commissioner, 449 F.2d 311 (9th Cir. 1971).

15 I have found that the UST presented sufficient evidence to
16 establish a prima facie case that the Chins' substantially
17 understated their gross income in their response to Item 1 in their
18 SOFA. If the Chins intended to rely on a technical "tax" definition
19 of income to defend against the UST's case, the best evidence to
20 support their position probably would include copies of their
21 federal income tax returns filed for the years 2001, 2002, and 2003.
22 However, the Chins did not submit their tax returns for those years
23 as exhibits.

24 Based on the foregoing review of the evidence, I find that
25 the Chins substantially under-reported their gross income for 2001,
26 2002, and 2003 in their response to Item 1 in their SOFA. I further

1 find that an accurate statement of their income for the periods in
2 question was material to an understanding of their perpetuation
3 financial affairs, particularly regarding their real estate
4 investing activities.

5 C. Knowing and Fraudulent.

6 Based on the evidentiary record, I find that the Chins were
7 substantially inaccurate in stating their gross income in their
8 response to Item 1 in their SOFA. Their disregard for the truth in
9 disclosing income is consistent with the pattern of grossly
10 inaccurate statements as to their income included in the many
11 financial statements delivered to potential lenders in 2002. See
12 Ex. 6. However, with the Garcia v. Coombs standard in mind, the
13 evidence in this case further presents a compelling motive for
14 knowing nondisclosure.

15 I find that the real estate investment enterprises conducted
16 in the names of US Financial and REIP were real estate scams. The
17 Chins apparently were used by Jeff Johnson and C.J. Brigham as front
18 people to extract money from transactions with a surface legitimacy.
19 The Chins assumed all of the liabilities as ultimate borrowers in
20 the US Financial and REIP real estate purchases, and they were left
21 holding the bag when real estate prices and rents did not rise fast
22 enough to compensate for the inadequate capitalization of their
23 enterprises. However, the Chins were in too deep and stayed in too
24 long to play the roles of innocent dupes credibly. After all, the
25 Chins began signing off on financial statements that they knew were
26 materially incorrect in early 2002 and continued to put their

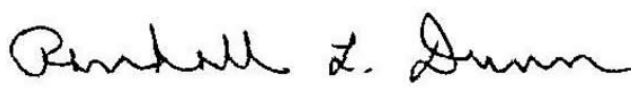
1 signatures and initials on dozens of such financial statements
2 through November 2002. See Ex. 6. In addition, Mrs. Chin began
3 doing the bookkeeping for REIP in April 2002 and continued keeping
4 the REIP accounts through the end in May 2003, making decisions
5 about disbursements of REIP funds with Mr. Chin and C.J. Brigham.

6 I find that the Chins had and have an interest in keeping the
7 records of US Financial and REIP transactions obscure, particularly
8 with respect to disbursements made to pay the Chins' personal
9 expenses. I understand and do not discount from the evidence
10 presented that the Chins made very large expense payments with
11 respect to their real estate investments from REIP and from their
12 personal accounts. However, I find that the Chins appropriated
13 substantial sums in excess of their income from Lucky Produce and TP
14 Produce from the REIP and US Financial transactions to fund their
15 personal expenses. I further find that the Chins did not include
16 such substantial sums in their reported gross income in their
17 response to Item 1 in their SOFA and that they knowingly and
18 fraudulently failed to report said income. Accordingly, I find that
19 the UST has met the burden of proof required to deny the Chins a
20 discharge pursuant to Section 727(a)(4)(A) in their chapter 7 case.
21 Since the denial of discharge remedy provides all the relief that
22 the UST otherwise seeks through the Motion to Dismiss, I do not need
23 to decide the Motion to Dismiss, and I decline to do so.

24 Conclusion

25 In summary, I find in favor of the UST on her cause of action
26 to deny a discharge to the Chins pursuant to Section 727(a)(4)(A) of

1 the Bankruptcy Code. Counsel for the UST should submit a form of
2 judgment consistent with this Memorandum Opinion.

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5 RANDALL L. DUNN
6 Bankruptcy Judge

7 cc: M. Vivienne Popperl
8 James R. Schaller
9 Michael B. Batlan, Trustee

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