IN THE COURT OF APPEALS OF IOWA

No. 6-1013 / 05-2039
Filed January 31, 2007

FIRST SECURITY BANK & TRUST COMPANY,
Plaintiff-Appellant,

vs.

DAVID A. KING and BEATRICE KING, Husband and Wife, ALLMERICA FINANCIAL LIFE INSURANCE & ANNUITY COMPANY, and SCUDDER GATEWAY ANNUITIES,
Defendants-Appellees.

Appeal from the Iowa District Court for Floyd County, James M. Drew, Judge.

A bank appeals from a district court ruling dismissing its petition in an action pursuant to Iowa Code section 630.16 (2003). **AFFIRMED.**

David J. Dutton and Carolyn A. Rafferty of Dutton, Braun, Staack & Hellman, P.L.C., Waterloo, for appellant.

Sarah J. Gayer, Kevin H. Collins, and Theresa C. Davis of Shuttleworth & Ingersoll, Cedar Rapids, for appellee Allmerica Financial Life Insurance & Annuity Company.

Judith O'Donohoe of Ellwood, O'Donohoe, Stochl, Braun & Churbuck, Charles City, for appellee Beatrice King.

Heard by Mahan, P.J., and Vaitheswaran and Eisenhauer, JJ.

MAHAN, P.J.

First Security Bank & Trust Company (First Security) appeals from a district court ruling dismissing its petition pursuant to Iowa Code section 630.16 (2003) seeking to subject certain property to the satisfaction of a judgment against David King. We affirm.

I. Background Facts and Proceedings

David King and Mike Walker formed All-States Quality Foods, Inc. (All-States) in 1984. King's wife, Beatrice King, provided $30,000 of the initial $35,000 needed to start the business. Beatrice did not receive stock or a promissory note for her investment, but she considered the company her "family's business." The business was sold in May 1995.

After the sale of All-States, David became the sole owner of King's Nature Ranch, an ostrich and elk ranch.[1] Beatrice was not involved in the day-to-day operation of the business and knew very little about the business and its finances.

Prior to the sale of All-States, David assured Beatrice that the proceeds from the sale would be invested and owned jointly. David, however, took the $3 million net proceeds and invested it in his own name. He explained to Beatrice that he invested the money in his name alone so he would not have to "bother" her every time he wanted to make a withdrawal.

Beatrice was furious with David when she learned the money was invested in his name only. She had taken over the family's nonbusiness related

[1] David and Mike Walters had started Quality Ostrich Ranch, Inc. in 1992. David bought Walter's interest in the ranch in 1995.

financial responsibilities in 1993, after David suffered a "nervous breakdown" and was hospitalized in a psychiatric ward for one month, and remained concerned about David's unwise financial decisions. The couple continued to fight about the proceeds from the sale of the business for several months.

In April 1996, after hearing rumors of David's extra-marital affairs, Beatrice asked David to leave the family home and gave him an ultimatum: she would divorce him unless he gave her $1 million and the title to their new house. David moved out for approximately four months. In July 1996 David had $1 million transferred from an annuity he owned to an annuity in Beatrice's name. He also promised her the house they were building would be in her name alone. Subsequently, Beatrice told David he could come home.

David did not disclose the $1 million transfer to First Citizens National Bank, his bank at the time. The bank discovered the transfer during a routine periodic inspection a few weeks after the transfer, but did not call any of David's loans or claim he had violated any loan covenant. David still had "significant" other assets after transferring the million dollars to Beatrice.

In April 1999 David approached First Security to discuss a loan for King's Nature Ranch. The bank's vice president, Charles Souder, learned the ranch had experienced big losses in the previous two years and was losing approximately $50,000 per month. He knew the business had never been profitable and repayment of any loan would depend upon the business turning a corner to make a profit.

David applied to First Security for a $150,000 loan on May 11, 1999, and agreed to personally guarantee the full amount of the loan as well as any future

loans. The bank initially requested personal guarantees from Beatrice and David, but was told by David that Beatrice would not be willing to give a personal guarantee. The bank agreed to make the loan with only David's personal guarantee. Its approval on May 11 was contingent on receipt of David's financial statement.

David provided the bank with a personal financial statement dated May 15, 1999. The form indicated it was a "joint" financial statement with Beatrice, but it was not signed by Beatrice, nor did she ever have any contact with the bank. The statement listed assets of $2.9 million and a net worth of $2.7 million. The assets listed included mutual funds, money market funds, and annuities totaling approximately $2.2 million. David listed the name of his financial advisor on the statement. He told Souder the cash and vehicles were Beatrice's but that he owned the remaining assets, including the $2.2 million of stocks. However, David had included the $1 million annuity that was transferred to Beatrice; he actually owned only $360,000 in stocks at that time.

First Security made additional loans in 1999 and 2000. David provided additional personal financial statements and made oral representations as to his investment assets. The bank did nothing to independently verify the information contained in the personal financial statements submitted by David. It never contacted David's financial advisor to verify ownership of investments,[2] nor did it request a copy of a brokerage statement from David to verify ownership. Even after the FDIC "classified" the loans in October 2001 and David indicated to the

[2] Pete Tousignant, David's financial advisor, testified that he is contacted "all the time" by lending institutions to verify the ownership of investments.

bank in March 2002 that he "had no money," the bank did nothing to verify David's assets.

In April 2002 First Security began liquidating King's Nature Ranch. The bank secured an approximate $1.2 million judgment against David in October 2003. An execution was issued and returned unsatisfied in December 2003, and the present action ensued.

First Security filed its petition pursuant to section 630.16, seeking to subject Beatrice's property—namely, the annuity established in 1996—to the judgment against David. The bank named David and Beatrice as defendants and later added Allmerica Life Insurance & Annuity Company and Scudder Gateway Annuities as defendants. The bank claimed fraud under two theories: (1) Iowa Code chapter 684, the Uniform Fraudulent Transfers Act, and (2) equitable fraud. Following a bench trial,[3] the district court filed a ruling dismissing the petition. The court concluded (1) the bank's claim of fraud under chapter 684 was untimely and (2) the bank failed to prove the elements of equitable fraud. First Security filed a motion pursuant to Iowa Rule of Civil Procedure 1.904(2), which was denied by the district court.[4]

The bank appeals, arguing (1) its cause of action for fraudulent transfer pursuant to chapter 684 was timely and (2) it met its burden of proving equitable fraud.

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[3] David did not appear in person or by counsel at trial. The district court entered a default against David pursuant to Iowa Rules of Civil Procedure 1.971 and 1.972.

[4] Appellee Allmerica Financial Life Insurance & Annuity Company argues First Security's appeal is untimely because its motion pursuant to rule 1.904(2) did not toll the time for appeal. *See Bellach v. IMT Ins. Co.*, 573 N.W.2d 903, 905 (Iowa 1998). We assume without deciding that First Security's appeal is timely.

II. Standard of Review

Our scope of review in this equitable action is de novo. Iowa R. App. P. 6.4. We give weight to the fact findings of the district court, but are not bound by them. Iowa R. App. P. 6.14(6)(*g*). "We are especially deferential to the district court's assessment of witness credibility." *Johnson v. Kaster*, 637 N.W.2d 174, 178 (Iowa 2001) (citation omitted).

III. Iowa Code Chapter 684

Transfers by a debtor are fraudulent to a future creditor if made with actual intent to hinder, delay, or defraud any creditor of the debtor. Iowa Code § 684.4(1)(a). A cause of action with respect to a fraudulent transfer under chapter 684 must be brought "within five years after the transfer was made or the obligation was incurred or, if later, within one year after the transfer or obligation was or could reasonably have been discovered by the claimant." *Id.* § 684.9.

The alleged fraudulent transfer—the $1 million transfer in 1996—occurred more than five years before First Security brought this action. Therefore, the issue before the district court was whether First Security filed its petition within one year of when the transfer "could reasonably have been discovered." The district court concluded as follows:

> While ideally every man could be taken at his word, certain business transactions require due diligence. Mr. Souder testified regarding the importance of David's personal guarantee when the bank decided to make the loans. Given the financial track record of King's Nature Ranch there was every reason to believe that the guarantee might come into play. Furthermore, given the amount of money that was ultimately involved there was every reason for the bank to require verification of David's assets. It was certainly feasible to do so as Mr. Tousignant testified that he routinely receives requests from lenders to verify his clients' investments. When one considers how easily the bank could have learned that

> the annuity was not in David's name or, alternatively, been alerted by a refusal to provide such basic information there is little doubt that the bank could have learned of the transfer much earlier than one year prior to filing the petition. Accordingly, the transfer could reasonably have been discovered more than one year prior to filing the petition.

The district court's conclusions are fully supported by the record, and we adopt them as our own. We affirm the district court on this issue.

IV. Equitable Fraud

Section 630.16 "furnishes means auxiliary to execution by which a creditor may uncover property in which the debtor still holds an interest." *Powell v. Grewing*, 562 N.W.2d 761, 763 (Iowa 1997). In order to prove David still holds an interest in Beatrice's annuity, First Security was required to prove the 1996 transfer to Beatrice was fraudulent.

The elements of fraud, which must be established by a preponderance of clear and convincing evidence, are: (1) representation, (2) falsity, (3) materiality, (4) scienter, (5) intent to deceive, (6) reliance, and (7) resulting injury and damage. *Morton v. Underwriters Adjusting Co.*, 501 N.W.2d 72, 73-74 (Iowa Ct. App. 1993). The rules are not so strict, however, where fraud is alleged in cases of equity. *Id.* at 74. "Equity may grant relief absent a showing of scienter or pecuniary damage." *Id.* In equitable fraud cases "the elements of scienter and intent to deceive are closely related and are shown not only when the speaker has actual knowledge of the falsity of [his or] her representations but also when [he or] she speaks in reckless disregard of whether [his or] her representations are true or false." *Id.*

When determining whether a transaction constitutes a fraudulent conveyance, the court looks for certain "badges or indicia of fraud: inadequacy of consideration, insolvency of the transferor, pendency or threat of third-party creditor litigation, secrecy or concealment, departure from the usual method of business, any reservation of benefit to the transferor, and the retention by the debtor of possession of the property." *Benson v. Richardson*, 537 N.W.2d 748, 756 (Iowa 1995). The existence of a blood relationship strengthens the inference of a fraudulent conveyance, although it is not a per se indication of fraud. *Id.*

We agree with the district court's conclusion that First Security failed to establish fraud in this case. The transfer of $1 million from the proceeds of the sale of All-States to Beatrice was reasonable and supported by consideration, given that Beatrice had provided nearly all the initial investment in All-States. David was not rendered insolvent because of the transfer, and no creditor was threatening litigation at the time of the transfer. David's bank at the time of the transaction, First Citizens National, discovered it within a few weeks, during a routine inspection. To the extent the transfer was a departure from the couple's usual method of managing their finances, such a departure was due to the existing marital discord between the parties, not fraud.

First Security contends that certain transfers of money from Beatrice directly to David, or for his benefit, between 1996 and 2004 are indicative of fraud. We disagree. Rather, the evidence supports the district court's conclusion that

> Beatrice has total control over all the funds and that all disbursements have been made at her discretion. Given the length of the marriage and the dissipation of David's personal wealth,

> Beatrice's use of the funds is not so out of the ordinary as to indicate fraud.

In reaching our conclusion, we are especially deferential to the district court's assessment, which found Beatrice

> to be very credible with respect to the facts surrounding the transfer and the use of those funds. Her testimony was given confidently without any signs of fabrication. While David may have dealt dishonestly with the plaintiff, the court is convinced that the transfer of funds to Beatrice was for the reasons stated and that she did not act in concert with David in perpetrating a fraud.

Finally, First Security failed to prove justifiable reliance. "[T]he test for determining whether a party to a transaction has a right to rely on representations of the other is . . . whether the complaining party, in view of his own information and intelligence, had a right to rely on the representations." *Lockard v. Carson*, 287 N.W.2d 871, 878 (Iowa 1980). The bank could easily have verified David's personal assets by requesting a brokerage statement from David or seeking a release to speak with his financial advisor. As the district court concluded, "[g]iven the minimal effort that would have been required from the bank compared to the importance of the information, the bank's reliance on David's personal financial statements was neither justified nor reasonable."

We affirm the decision of the district court.

AFFIRMED.