

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF INDIANA  
FORT WAYNE DIVISION

IN RE: CASE NO. 07-11441 )  
)  
CHAD MYRDDIN SEYBOLD )  
LAURA REITER SEYBOLD )  
Debtors )  
)  
)  
SALIN BANK AND TRUST COMPANY )  
Plaintiff )  
)  
vs. ) PROC. NO. 07-1255  
)  
)  
CHAD MYRDDIN SEYBOLD )  
LAURA REITER SEYBOLD )  
Defendants )  
)  
)  
CHAD MYRDDIN SEYBOLD )  
LAURA REITER SEYBOLD )  
Counter-Claimants )  
)  
)  
vs. )  
)  
)  
SALIN BANK AND TRUST COMPANY )  
Counter-Defendant )

**DECISION AND ORDER DENYING DEFENDANTS’  
MOTION TO DISMISS OR ABSTAIN**

At Fort Wayne, Indiana on March 5, 2008

This is an adversary proceeding to determine the dischargeability of the debtors’ obligation to the plaintiff. The Seybolds appear to have interests in a number of different businesses. The essence of the plaintiff’s claim is that Mr. Seybold obtained loans for one business entity, representing that it owned or would be acquiring real property upon which the Bank would be granted a mortgage in order to secure the loan. In reality, however, the Bank’s borrower did not own or was not the acquirer of the property in question, with the result that the Bank has received

mortgages upon real estate from someone other than the owner, making them decidedly less valuable than it anticipated. Since Mr. Seybold was allegedly fully aware of the status of the title to the real estate and misrepresented those facts to the Bank, the Bank characterizes his actions as fraud, fraud or defalcation in a fiduciary capacity, and/or a willful and malicious injury which, if accurate, would render his liability to the Bank<sup>1</sup> non-dischargeable under §§ 523(a)(2), (4) and/or (6) of the United States Bankruptcy Code.

In addition to the bankruptcy derived labels for the defendants' conduct, the plaintiff has also given it another name. In Count IV of the amended complaint it labels Mr. Seybold's actions "bank fraud," as defined by I.C. 35-43-5-8,<sup>2</sup> which gives it the opportunity to seek treble damages and attorney fees pursuant to I.C. 34-24-3-1.<sup>3</sup> The defendants have responded with a single motion asking the District Court to withdraw the reference as to Count IV, as well as asking this court to

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<sup>1</sup>That liability is based upon Mr. Seybold's personal guarantee of the obligations in question, as well as the argument that he is personally liable for the torts which he has supposedly committed.

<sup>2</sup>This statute provides: (a) A person who knowingly executes, or attempts to execute, a scheme or artifice:

- (1) to defraud a state or federally chartered or federally insured financial institution;
  - or
  - (2) to obtain any of the money, funds, credits, assets, securities, or other property owned by or under the custody or control of a state or federally chartered or federally insured financial institution by means of false or fraudulent pretenses, representations, or promises;
- commits a Class C felony.

<sup>3</sup>In relevant part, this statute provides: If a person suffers a pecuniary loss as a result of a violation of IC 35-43, IC 35-42-3-3, IC 35-42-3-4, or IC 35-45-9, the person may bring a civil action against the person who caused the loss for the following:

- (1) An amount not to exceed three (3) times the actual damages of the person suffering the loss.
- (2) The costs of the action.
- (3) A reasonable attorney's fee.

dismiss that claim or at least abstain from hearing it.<sup>4</sup> This decision addresses those components of the defendants' motion which may be properly resolved by this court – dismissal and abstention. See, Fed. R. Bankr. P. Rule 5011(c) (motion for withdrawal of reference does not stay the administration of a case or proceeding).

The defendants advance two arguments as to why Count IV of the plaintiff's complaint should be dismissed: res judicata and the lack of subject matter jurisdiction. The first argument is based upon a judgment the plaintiff obtained from the Grant County Superior Court. The second is based upon a mischaracterization of both the nature of this proceeding and the Bankruptcy Court's responsibility or authority in dischargeability litigation.

As for the defendants' first argument – res judicata is an affirmative defense. See, Fed. R. Civ. P. Rule 8(c). The function of a motion to dismiss under Rule 12(b)(6) is to test the sufficiency of the plaintiff's complaint and whether it states a claim upon which relief can be granted. As a result, affirmative defenses are not generally the proper subject of a Rule 12(b)(6) motion. See e.g., Xechum, Inc. v. Bristol-Myers Squibb Co., 372 F.2d 899, 901 (7th Cir. 2004); U.S. Gypsum Co. v. Indiana Gas Co., Inc., 350 F.3d 623, 626 (7th Cir. 2003). They are more appropriately raised through a motion for summary judgment, which gives the opportunity to present additional information to the court, rather than focusing solely upon the allegations contained in the complaint. The only exception to this general rule is where the plaintiff has literally pled itself out of court, by making

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<sup>4</sup>This motion fails to comply with the requirements of Local Bankruptcy Rule B-9013-1, which requires that each motion be filed separately. The defendants have made three different requests, which are properly directed to two different courts. Combining all of this in a single filing and single supporting brief makes it a bit difficult to figure out which arguments are directed to which request and to which court. The confusion that is likely to be engendered by such multiplicity amply demonstrates the purpose for this court's local rule. See also, N.D. Ind. L.R. 7.1(b)(also requiring each motion to be filed separately).

allegations in the complaint which demonstrate that it has no right to relief. See, Xechem, 372 F.3d at 901; Early v. Bankers Life and Casualty Co., 959 F.2d 75, 79 (7th Cir. 1992) (citations omitted). In this instance, the court is not prepared to conclude that the Bank has pled itself out of court. Although the court does have the discretion or the opportunity to transform a Rule 12(b)(6) inquiry into one for summary judgment, see, Fed. R. Civ. P. Rule 12(c), it is not inclined to do so here because the parties' arguments concerning the Indiana law of res judicata and the mandatory joinder of claims have not been advanced with sufficient specificity so that they can readily be applied to the facts of this case.

The second argument for the dismissal of Count IV is that the court lacks subject matter jurisdiction over that portion of the plaintiff's claim. See, Fed. R. Civ. P. Rule 12(b)(1). The defendant characterizes it as a state law claim, whose foundation is independent of the provisions of the Bankruptcy Code, the disposition of which will affect neither the property available for distribution to creditors nor the way in which that property might be distributed. Defendants then argue that the claim does not arise under Title 11 – because it is a state law claim – and that it is not related to a case under Title 11 – because of the absence of an impact upon the estate. From this they contend the court lacks the subject matter jurisdiction necessary to determine the issues raised by Count IV.

Jurisdiction is the power to decide, and it must be conferred by Congress. Matter of Chicago, Rock Island and Pacific R. Co., 794 F.2d 1182, 1188 (7th Cir. 1986). Any discussion of the scope of the Bankruptcy Court's subject matter jurisdiction must begin with 28 U.S.C. § 1334. In that portion of the United States Code, Congress conferred upon the District Courts jurisdiction over bankruptcy proceedings. It also established procedures by which that jurisdiction may be exercised.

See, 28 U.S.C. § 157. The District Courts are authorized to refer their bankruptcy jurisdiction to bankruptcy judges, 28 U.S.C. § 157(a), and where that has been done,<sup>5</sup> the statute also describes how the bankruptcy judges may exercise that authority, whether by making a final decision or through proposed finding of facts and conclusions of law. In what have been denominated as core proceedings, the bankruptcy judge is authorized to render a final decision. 28 U.S.C. § 157(b). In proceedings which are only related to the bankruptcy case, absent consent of the parties, the bankruptcy judge is required to submit proposed findings of fact and conclusions of law, for a de novo review by the District Court. 28 U.S.C. § 157(c). Despite this multilayered approach, it is important to remember that jurisdiction itself is always created and defined by § 1334. Jurisdiction must first exist under that statute; if it does, section 157 simply explains how that authority is to be exercised.

In addition to giving the court authority over bankruptcy cases themselves, 28 U.S.C. § 1334(a), the court is also given jurisdiction over “all civil proceedings arising under title 11 or arising in or related to a case under title 11.” 28 U.S.C. § 1334(b). This familiar litany, arising in, under, or related to, describes not discrete and isolated cases, but rather broad and overlapping sets of the different types of disputes that might be associated with a bankruptcy proceeding. Those terms have also come to have well-defined meanings. Proceedings “arising under” title 11 involve a cause of action created by the Bankruptcy Code itself, such as the avoidance of preferences, 11 U.S.C. § 547, the recovery of fraudulent conveyances, 11 U.S.C. § 548(a), or the dischargeability of debt, 11 U.S.C. § 523. See, 1-3 Collier on Bankruptcy ¶3.01[4][c][i] (15th ed. rev.). Proceedings

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<sup>5</sup>In this district the reference has been made through local rule 200.1. See, N.D. Ind. L.R. 200.1(a).

“arising in” a case under Title 11 involve administrative matters and disputes which could have no existence outside the bankruptcy case, such as proceedings on applications for fees, the approval of a trustee’s final report or resolving a disputed election. 1-3 Collier on Bankruptcy ¶ 3.01[4][c][iv] (15th ed. rev.). The final, and by far the potentially largest, category of disputes the court might encounter are those which are “related to” a case under Title 11. Because this category is so potentially broad and expansive, it should be interpreted narrowly and, in the Seventh Circuit, has come to mean a state law action which will affect either the assets available for distribution to creditors or the way in which those assets will be distributed. Matter of FedPak Systems, Inc., 80 F.3d 207, 213-14 (7th Cir. 1996) (quoting Zerand-Bernal Group, Inc. v. Cox, 23 F.3d 159, 161 (7th Cir. 1994)); Home Ins. Co. v. Cooper & Cooper, Ltd., 889 F.2d 746, 749 (7th Cir. 1989).

It will readily be seen that these categories are sometimes overlapping. For example, an action to recover a voidable preference will clearly have an impact upon the assets available for distribution to creditors, yet it is also a claim that arises out of Title 11 itself. As a result, the basis for the court’s subject matter jurisdiction could be found in both the arising under and the related to portions of § 1334(b). Similarly, proceedings on an application for fees because of the bankruptcy could have no existence without the underlying bankruptcy case; yet, if those fees are to be paid out of the bankruptcy estate, the court’s decision will have an impact upon how the estate is to be distributed. In such a situation, the basis for the court’s subject matter jurisdiction could be found in both the “arising in” and the “related to” portions of §1334(b). There are also proceedings where the source of the court’s authority will be grounded upon only one of the three overlapping categories. Dischargeability litigation is one of them. The ultimate cause of action that the court is determining in a dispute over the dischargeability of debt is created by § 523(a) of the United States

Bankruptcy Code. As a result, the court's authority over it comes from the "arising under" portion of § 1334(b). Admittedly, the underlying claim which plaintiff seeks to except from discharge is a claim created by non-bankruptcy law, yet that will almost always be the case. The vast majority of debts which bankruptcy debtors bring to this court are created, not by federal law, but, by state law. See, In re Donald, 328 B.R. 192, 200 (9th Cir. BAP 2005). It would be quite anomalous for the bankruptcy court to have the exclusive authority to determine whether or not a particular debt is dischargeable, see, 11 U.S.C. § 523(c), and yet have no authority to determine whether or not such a debt exists.

By focusing so exclusively upon the state law origin for the plaintiff's claim and the impact of that claim upon the bankruptcy estate, the defendants have overlooked the essential purpose for this particular litigation and the ultimate relief which the plaintiff seeks from this court. This is a proceeding to determine dischargeability. The first step in determining whether or not a particular debt is dischargeable is to make certain that there is, indeed, a debt owing by the debtor to the creditor. Without such an obligation, there is no debt which could be excepted from the scope of the debtors' discharge. In re Sieger, 200 B.R. 636, 639 (Bankr. N.D. Ind. 1996); In re Wilder, 178 B.R. 174, 176-77 (Bankr. E.D. Mo. 1995). Cf., Matter of Hallahan, 936 F.2d 1496, 1508 (7th Cir. 1991) ("we think it preferable to allow bankruptcy courts ruling on the dischargeability of a debt to adjudicate the issues of liability and damages also."). As a cause of action created by the Bankruptcy Code, dischargeability determinations constitute claims arising under Title 11. Thus, the Bankruptcy Court has subject matter jurisdiction over them and they constitute core proceedings, which it may properly and finally determine without the consent of the parties involved. 28 U.S.C. § 1334; 28 U.S.C. § 157(b)(2)(I). Accordingly, the court holds that it has subject matter jurisdiction over all of

the issues raised by Count IV of Plaintiff's complaint.

Debtors' argument for abstention is based upon the fact that the bank fraud claim being asserted in Count IV of Plaintiff's complaint is a cause of action created by state law, as such it is most appropriately determined by the state courts which are able to offer the debtor the opportunity for a trial by jury.

Abstention is governed by 28 U.S.C. § 1334(c). Section 1334(c)(1) authorizes permissive abstention and gives the court the discretion to abstain from hearing a particular proceeding. Section 1334(c)(2) requires the court to abstain under certain circumstances. Defendant is proceeding under both provisions. It contends both that the court is required to and, in the exercise of its discretion, should abstain from hearing the issues raised by Count IV of plaintiff's complaint.

The court is not required to abstain from hearing the issues raised by Count IV of Plaintiff's complaint. The opportunity to seek mandatory abstention only exists where the claim in question is "related to a case under title 11." If the claim is one that either arises under title 11 or arises in a case under title 11 mandatory abstention does not apply. 28 U.S.C. § 1334(c)(2). Since this is a dischargeability proceeding and the basis for the court's jurisdiction is the arising under portion of § 1334(b), the court is not required to abstain from hearing it. See e.g., In re Cook, 230 B.R. 475, 477 (Bankr. D. Conn. 1999); In re Mills, 163 B.R. 198, 202-03 (Bankr. D. Kan. 1994). See also, 1-3 Collier on Bankruptcy ¶ 3.05[1] (15th ed. rev.).

As for discretionary abstention, in making that decision, the courts may consider things such as:

(1) the effect or lack thereof on the efficient administration of the estate, the extent to which state law issues predominate over bankruptcy issues, (2) the difficulty or unsettled nature of the applicable law, (3) the presence of a related proceeding

commenced in state court or other nonbankruptcy court, (4) the jurisdictional basis, if any, other than . . . § 1334, (5) the degree of relatedness or remoteness of the proceeding to the main bankruptcy case, (6) the substance rather than form of an asserted ‘core’ proceeding, the feasibility of severing state law claims from core bankruptcy matters to allow judgments to be entered in state court with enforcement left to the bankruptcy court, (7) the burden of [the bankruptcy court’s] docket, (8) the likelihood that the commencement of the proceeding in bankruptcy court involves forum shopping by one of the parties, (9) the existence of a right to a jury trial, and (10) the presence in the proceeding of non-debtor parties. Matter of Chicago, Milwaukee, St. Paul & Pacific R. Co. 6 F.3d 1184, 1189 (7th Cir. 1993).

Here, the court sees no reason that it should abstain from hearing the issues raised by Count IV. To do so will only unnecessarily multiply the time and effort that the parties and the courts – whether state or federal – will be required to devote to this matter. See, Chicago, Milwaukee, St. Paul & Pacific R. Co., 6 F.3d at 1189. See also, In re Colarusso, 382 F.3d 51, 57 (1st Cir. 2004); In re Tucson Estates, Inc., 912 F.2d 1162, 1167 (9th Cir. 1990).

In the first instance, since this is a dischargeability determination, it constitutes a core proceeding under § 157(b)(2)(I). The foundation for plaintiff’s claims of non-dischargeability – § 523(a)(2), (4) and (6) – are the exclusive provenance of the bankruptcy court, 11 U.S.C. § 523(c), and cannot be determined by a state court. Thus, although it is theoretically possible that this court could allow a state court to determine whether or not the debtor has any liability to the plaintiff, should it make that determination, the parties would then be required to come back to this court to seek yet a further determination of whether or not that debt was a dischargeable one. There is already a single proceeding in which both determinations can be made, and the court sees no reason that it should multiply litigation by creating two proceedings – one state and one federal – when a single one will do. Cf., Hallahan, 936 F.2d at 1508 (“we think it preferable to allow bankruptcy courts ruling on the dischargeability of a debt to adjudicate the issues of liability and damages

also.”). This is especially so when one remembers that the facts which the plaintiff relies upon as the basis for its state law bank fraud claim are the same facts that it relies upon for its claims of non-dischargeability – Mr. Seybold’s knowing misrepresentations in connection with obtaining the loans. Bank fraud is simply another label the plaintiff has given those facts. As a result, abstention would require the parties to present to a state court exactly the same evidence they will be presenting here with regard to the first three counts of the complaint. The court sees no reason that it should require such a duplication of efforts, and create the potential for conflicting results, by abstaining from hearing that part of this proceeding. As for the defendant’s claimed right to a trial by jury, the court would only note that he is the one that chose to initiate proceedings in this court and, by doing so has effectively waived or forfeited the right to a trial by jury with regard to any disputes which might subsequently arise in it. Hallahan, 936 F.2d at 1502-06. See also, In re McLaren, 3 F.3d 958, 960-61 (6th Cir. 1993).

Defendants’ motion to dismiss Count IV of plaintiff’s complaint is DENIED and the court will not abstain from hearing the issues raised by it.

SO ORDERED.

/s/ Robert E. Grant  
Judge, United States Bankruptcy Court