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OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re: CHARLES V. McCLAIN, III and ARLENE J. McCLAIN, Debtors.	BAP No. WW-06-1191-SPaMo Bk. No. 05-19334 Adv. No. 05-01382
CHARLES V. McCLAIN, III and ARLENE J. McCLAIN, Appellants, v. BOEING EMPLOYEES CREDIT UNION, Appellee.	**MEMORANDUM**[1]

Argued and Submitted on November 16, 2006
at Seattle, Washington

Filed - January 31, 2007

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

Honorable Thomas T. Glover, Bankruptcy Judge, Presiding.

Before: SMITH, PAPPAS and MONTALI, Bankruptcy Judges.

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[1] This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have (see Fed. R. App. P. 32.1), it has no precedential value. See 9th Cir. BAP Rule 8013-1.

Boeing Employees Credit Union ("BECU") filed a non-dischargeability action against debtors under § 523(a)(2)(A)[2]. Debtors counterclaimed with allegations of defamation and malicious prosecution. The bankruptcy court granted summary judgment dismissal in favor of BECU on the counterclaims. A timely notice of appeal was filed on May 18, 2006. We AFFIRM.

I. FACTS

In 2003, Charles McClain ("McClain") sued BECU and certain of its employees in Snohomish County Superior Court alleging wrongful imprisonment, negligent and intentional infliction of emotional distress, and theft of money. BECU counterclaimed that McClain had breached his BECU account agreement and conspired with others to appropriate $40,538.89 from BECU between September and December 2003.

On July 21, 2005, Charles and Arlene McClain (collectively, "Debtors") filed a chapter 7 petition. BECU timely filed an adversary proceeding against Debtors for a determination under § 523(a)(2)(A) that Debtors' indebtedness to it was non-dischargeable (the "complaint"). The complaint asserted that between September 22, 2003, and October 28, 2003, Debtors engaged in a check kiting scheme[3] and that, as a consequence of this

[2] Unless otherwise indicated, all chapter, section and rule references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330, and to the Federal Rules of Bankruptcy Procedure, Rules 1001-9036, as enacted and promulgated pursuant to The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. 109-8, Apr. 20, 2005, 119 Stat. 23.

[3] The facts surrounding the check kiting scheme are as follows. Between October 26 and 28, 2003, McClain received checks from Erik Helmersen, Greg Vaughn, and Roy Veal. Each check was made out to Arlene McClain in the amount of $30,000.
(continued...)

scheme, McClain fraudulently obtained $40,536.89 from BECU.

Debtors denied the check kiting allegations and countersued for pre-petition wrongful acts[4], defamation, and post-petition malicious prosecution based upon the filing of the non-dischargeability proceeding.

In March 2006, BECU entered into a court approved settlement with the chapter 7 trustee that resolved all of Debtors' pre-petition claims against BECU and its employees. As part of the settlement, BECU agreed to dismiss the non-dischargeability

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[3] (...continued)

On October 27, 2003, McClain deposited the $30,000 check from Helmersen in his wife's account at BECU and subsequently telephonically transferred the funds to Debtors' joint account at BECU. Immediately after making the transfer, McClain purchased a $24,500 cashier's check against the joint account. Later that same day, he deposited the cashier's check into an account at a different bank.

The very next day, McClain returned to BECU and attempted to deposit the two remaining checks. McClain endorsed the back of each check with the name "Arlene McClain" and deposited the checks into his wife's account. He then walked from the teller's booth to an internal BECU customer telephone and transferred $51,000 of the $60,000 "deposit" from his wife's account to their joint account. Upon completing the telephonic transfer, he walked outside and withdrew $500 from BECU's automated teller machine.

Less than two hours later, McClain returned to BECU and attempted to purchase a cashier's check for $39,000 (made payable to himself) and to withdraw $6,000 in cash from their joint account. The teller informed McClain that approval was needed for such a large transaction. At that point, the teller contacted BECU's security risk specialist. After some investigation, BECU learned that there were insufficient funds in Helmersen, Veal, and Vaughn's accounts to cover the checks.

[4] The alleged wrongful pre-petition acts revolve around BECU withdrawing funds from the Debtors' bank account on October 28, 2003, November 28, 2003, and December 5, 2003, to offset the amounts that had been lost from the check kiting scheme.

action against Debtors. However, Debtors did not agree to dismiss the counterclaims filed in response to it. As a result, BECU filed its "Motion for a Summary Judgment Dismissal of Charles and Arlene McClain's Counterclaims Against BECU" (the "motion") on March 31, 2006.

BECU maintained that summary judgment was warranted because 1) the counterclaims which arose out of events that occurred prior to the bankruptcy petition date (July 21, 2005) had been resolved by the March 2006 settlement, 2) the defamation claims stemmed from statements made either in state court or in the bankruptcy court causing them to be absolutely privileged under Washington law, and 3) the malicious prosecution counterclaim was without merit because BECU had probable cause to bring the non-dischargeability action.

Debtors opposed the motion arguing that BECU was not entitled to absolute immunity for the defamatory statements published and spoken during the prosecution of the adversary proceeding because it had been wrongfully initiated. Consequently, BECU was not protected by the absolute privilege because Debtors held a viable defamation claim upon which relief could be granted. In addition, Debtors contended that the inclusion of Arlene McClain in the non-dischargeability action was malicious since there was no evidence that she had engaged in the check kiting scheme. Finally, BECU had violated various Washington banking laws by failing to provide proper notice of the dishonored checks. Thus, Debtors were discharged of any liability relating to the checks.

The matter came on for hearing on April 26, 2006. After both parties were given the opportunity to argue, the bankruptcy court dismissed the counterclaims finding that "[i]ssues of defamation and malicious prosecution don't belong as defenses in a case like [the present], or frankly, very many cases at all."[5]

Debtors appeal.

II. JURISDICTION

The bankruptcy court had jurisdiction under 28 U.S.C. § 1334 and §§ 157(b)(1), (b)(2)(A), and (2)(B). We have jurisdiction under 28 U.S.C. §§ 158(b)(1) and (c)(1).

III. ISSUE

Whether Debtors' counterclaims against BECU were properly dismissed.

IV. STANDARD OF REVIEW

The scope of review on a motion to dismiss for failure to state a claim is limited to the contents of the complaint. Marder v. Lopez, 450 F.3d 445, 448 (9th Cir. 2006). Thus, "if matters outside the pleading are presented to and not excluded by the court, the motion shall be treated as one for summary judgment." Fed. R. Civ. P. 12(b)(6).

A grant of a summary judgment is reviewed de novo. Patterson v. Int'l Bhd. of Teamsters, Local 959, 121 F.3d 1345, 1349 (9th Cir. 1997). If viewing the evidence in the light most

[5] At the hearing, the bankruptcy court briefly addressed the issues surrounding the alleged banking law violations and determined that these issues dealt with the complaint and not the counterclaims, therefore, they should be tested through a separate motion for partial or complete summary judgment as to the complaint. However, by the time of the hearing, BECU had already dismissed the complaint pursuant to the settlement with the trustee rendering these issues moot.

favorable to the nonmoving party, we can see that there is no genuine issue of fact and the applicable substantive law has been correctly applied by the bankruptcy court, then the granting of a motion for summary judgment should be sustained. City of Vernon v. S. Cal. Edison Co., 955 F.2d 1361, 1365 (9th Cir. 1992). The moving party can satisfy its burden of establishing the absence of a genuine issue of material fact by: (1) presenting evidence that negates an essential element of the nonmoving party's case; or (2) by demonstrating that the nonmoving party failed to make a showing sufficient to establish an element essential to the party's case on which that party will bear the burden of proof at trial. Celotex Corp v. Catrett, 477 U.S. 317, 322-23 (1986).

V. DISCUSSION[6]

The motion included evidence outside the four corners of Debtors' counterclaims. As there is no indication that the bankruptcy court excluded this evidence in making its determination, the court's dismissal of the counterclaims must be viewed as a grant of summary judgment. See Fed. R. Civ. P.

[6] In addition to seeking damages for defamation and malicious prosecution, Debtors sought to recover from BECU the funds it withdrew from their account between October 28, 2003, and December 5, 2003. These claims, however, arose prior to Debtors filing for bankruptcy on July 21, 2005, making them pre-petition claims. Pursuant to the settlement agreement entered into between the chapter 7 trustee and BECU, which was approved by the bankruptcy court on March 27, 2006, the trustee agreed to "settle, release, dismiss and waive, with prejudice, all claims" held by the estate against BECU including those "which arose on or before the bankruptcy petition date." Accordingly, these claims were resolved prior to BECU filing the motion. As the parties do not address these claims in their briefs, we deem any argument that the bankruptcy court wrongly dismissed them as waived. See Ellingson v. Burlington N., Inc., 653 F.2d 1327, 1332 (9th Cir. 1981); Fed. R. App. P. 28(a)(2).

12(b)(6).

A. Defamation[7]

A defamation claim requires proof of (1) a false statement, (2) an unprivileged statement, (3) fault, and (4) damages proximately caused by the statement. Kauzlarich v. Yarbrough, 20 P.3d 946, 950 (Wash. Ct. App. 2001). Defamatory "statements, spoken or written by a party or counsel in the course of a judicial proceeding, are absolutely privileged if they are pertinent or material to the redress or relief sought, whether or not the statements are legally sufficient to obtain that relief." McNeal v. Allen, 621 P.2d 1285, 1286 (Wash. 1980). An absolute privilege absolves the defendant of all liability for defamatory statements. Kauzlarich, 20 P.3d at 951.

Debtors complain that the bankruptcy court erred in dismissing their defamation claim because their actions did not satisfy the legal definition of check kiting. Thus, BECU defamed them by accusing them of such in the complaint. While there is no disagreement that the complaint includes allegations of check kiting, BECU has presented evidence sufficient to establish that its statements were both absolutely privileged and not defamatory.

BECU sought a determination that Debtors' debt to it should be excepted from discharge under § 523(a)(2)(A). Under

[7] The counterclaim does not specify what defamatory statements were made. It simply states that "Plaintiff has defamed Defendants." In reviewing Debtors' opposition to the motion and their opening brief, it can be inferred that the defamatory comment was that "[Debtors] engaged in a check kiting scheme." When the counterclaim was filed, the only place this defamatory statement could be found was in the non-dischargeability complaint.

§ 523(a)(2)(A), a debtor may be denied a discharge from any debt for money obtained by "false pretenses, a false representation, or actual fraud." 11 U.S.C. § 523(a)(2)(A). In this regard, BECU alleged the following facts:

> 4. Between September 22, 2003 and October 28, 2003 Defendants engaged in a check kiting scheme by depositing bad checks, obtaining provisional credit from BECU, then immediately transferring the funds to another BECU account and subsequently withdrawing the funds in cash.
>
> 5. During the above dates, 3 bad checks totalling [sic] $44,000.00 were deposited to Defendant, Arlene J. McClain's account, BECU provisionally credited her account, the funds were transferred to Defendant Charles V. McClain's account and the funds were subsequently withdrawn. . . .
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> 6. The bad checks were subsequently returned to BECU as non-sufficient funds ("NSF") and the provisional credit revoked resulting in a negative balance in the account.
>
> 7. After all appropriate offsets and credits there remains a balance due and owing to BECU in the sum of $40,538.89.

The above facts are material to obtaining the relief under § 523(a)(2)(A) since they describe the actions Debtors took to defraud BECU. Because the statements were made in the course of a judicial proceeding and were pertinent to the relief sought, the statements are privileged. Whether they were legally sufficient to obtain relief under § 523(a)(2)(A) or establish check kiting is irrelevant for the purpose of determining their privileged status. See McNeal, 621 P.2d at 1286.

By establishing that its statements were privileged, BECU satisfied its burden of proving the absence of a genuine issue of material fact by negating an essential element of Debtors' defamation claim. Thus, for Debtors to defeat the summary

adjudication of this claim, they needed to present evidence sufficient to establish the existence of a genuine issue of material fact as to whether the statements are privileged. Celotex, 477 U.S. at 324. As Debtors failed to do this, dismissal of the defamation claim was warranted.

B. Malicious Prosecution

In order to maintain an action for malicious prosecution based on a civil proceeding, the plaintiff needs to prove

> (1) that the prosecution claimed to have been malicious was instituted or continued by the defendant; (2) that there was want of probable cause for the institution or continuation of the prosecution; (3) that the proceedings were instituted or continued through malice; (4) that the proceedings terminated on the merits in favor of the plaintiff, or were abandoned; . . . (5) that the plaintiff suffered injury or damage as a result of the prosecution . . . (6) arrest or seizure of property[; and] (7) special injury (meaning injury which would not necessarily result from similar causes of action).

Clark v. Baines, 84 P.3d 245, 248-49 (Wash. 2004). Although a plaintiff must prove all the required elements, "malice and want of probable cause constitute the gist of a malicious prosecution action." Id. at 249; Hanson v. City of Snohomish, 852 P.2d 295, 297 (Wash. 1993). An absolute defense to a malicious prosecution claim is proof of probable cause. Hanson, 852 P.2d at 297. Probable cause is present if the "facts [are] sufficient to lead a man of prudence and caution to believe the offense had been committed." Hayes v. Sears, Roebuck & Co., 209 P.2d 468, 476 (Wash. 1949).

Debtors argue that the complaint was wrongfully initiated against Arlene McClain because 1) BECU failed to provide any facts which indicated that there was probable cause to accuse her

of check kiting; 2) BECU accused her of check kiting for purposes other than to secure an adjudication of the asserted debt; 3) the state court action was terminated in her favor; and 4) her actions did not meet the legal definition of check kiting.

As with the defamation claim, BECU has presented evidence sufficient to establish that Debtors will not be able to prove essential elements of their malicious prosecution claim at the time of trial. As previously indicated, one of the key elements of malicious prosecution is lack of probable cause to assert a particular claim.

Through declarations of BECU employees, Debtors' testimony, and bank documents, BECU has shown that it had probable cause to file the complaint against Debtors.[8] Between October 26 and 28, 2003, McClain obtained three checks made out to Arlene McClain in the amounts of $30,000 each. In a period of two days, he successfully deposited all three into his wife's personal account at BECU and then transferred $81,000 of the $90,000 deposited into the Debtors' joint account. From these funds, he was able to obtain a $24,500 cashier's check, which he later deposited into an account at a different bank, and attempted to obtain another cashier's check for $39,000 and withdraw $6,000, but was prevented from doing so when BECU learned that there were insufficient funds in each of the check writers' accounts to cover the deposited checks. Based on these facts, BECU filed its complaint against Debtors alleging that their indebtedness should not be discharged pursuant to § 523(a)(2)(A) because their

[8] A detailed account of Debtors' banking transactions can be found in footnote 3, <u>supra</u> p. 2-3.

actions represented check kiting - a fraud upon BECU.

Debtors take issue with the characterization of McClain's banking transactions as "check kiting." In this regard, they rely on the Sixth Circuit's definition of check kiting.[9] We are, however, controlled by the decisions of the Ninth Circuit and not the Sixth Circuit. See Coyne v. Westinghouse Credit Corp. (In re Global Illumination Co.), 149 B.R. 614, 617 (Bankr. C.D. Cal. 1993)("a decision of a circuit court of appeal is binding on all lower courts in the circuit"). Accordingly, we must look to the Ninth Circuit's definition to determine whether BECU had probable cause to accuse Debtors of checking kiting, and therefore, fraud for § 523(a)(2)(A) purposes.

The Ninth Circuit broadly defines checking kiting as "the practice of playing one checking account against another" in order to "create[] the appearance of funds present and immediately available for withdrawal in an account, when none in fact are there." United States v. Turner, 312 F.3d 1137, 1139 n.1 (9th Cir. 2002). Unlike the Sixth Circuit, the Ninth Circuit does not require that the funds be deposited into an account at a different bank. Applying the Ninth Circuit's definition,

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[9] The Sixth Circuit defines check kiting as

> Check kiting consists of drawing checks on an account in one bank and depositing them in an account in a second bank when neither account has sufficient funds to cover the amounts drawn. Just before the checks are returned for payments to the first bank, the kiter covers them by depositing checks drawn on the account in the second bank. Due to the delay created by the collection of funds by one bank from the other, known as the "float time," an artificial balance is created.

United States v. Stone, 954 F.2d 1187, 1188 n.1 (6th Cir. 1992).

McClain's actions clearly provide sufficient probable cause for BECU to allege that he was involved in a check kiting scheme. McClain deposited three checks each in the amount of $30,000. At the time of their deposit, none of the accounts from which the checks had been written had sufficient funds. Nevertheless, McClain immediately transferred a significant amount of the deposited funds into another account, from which he then withdrew a large sum. By depositing the checks into Arlene McClain's personal account and then immediately telephonically transferring the "funds" into the Debtors' joint account, McClain was able to convert nonexistent funds into actual funds by taking advantage of the float time. Clearly, this constitutes check kiting under the Ninth Circuit standard and thus probable cause to assert the same in the complaint.

Although Arlene McClain was not actually involved with the transfers and withdrawals, there was probable cause for BECU to name her in the adversary proceeding based upon the fact that 1) all three checks were made payable to her, endorsed with her name, and deposited into her account, 2) her name and bank account were used to create artificially high balances in the couple's joint account, which inferred that she was involved in the fraud, and 3) she potentially benefitted from the receipt of the funds. These facts would be sufficient to lead BECU to reasonably believe that Arlene McClain played some active role in the kiting transactions.

BECU's evidence is sufficient to establish that it had probable cause to initiate the complaint against Debtors. Because proof of probable cause is an absolute defense to any

malicious prosecution claim, BECU has demonstrated that Debtors have failed to establish a key element of their claim. Accordingly, we find that the bankruptcy court correctly granted summary judgment dismissal of the malicious prosecution claim.

VI. CONCLUSION

For the foregoing reasons, we AFFIRM the order entered by the bankruptcy court dismissing all counterclaims raised by Debtors.