

No. 11-1518

In The
Supreme Court of the United States

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RANDY CURTIS BULLOCK,

Petitioner,

v.

BANKCHAMPAIGN, N.A.,

Respondent.

—◆—
**On Petition For Writ Of Certiorari
To The United States Court Of Appeals
For The Eleventh Circuit**

—◆—
BRIEF IN OPPOSITION

—◆—
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QUESTION PRESENTED

Whether 11 U.S.C. § 523(a)(4) bars a debtor in bankruptcy from discharging a debt incurred by the debtor while acting as a trustee of an express trust where the debt was incurred by the trustee borrowing from the trust in contravention to the express terms of the trust instrument.

CORPORATE DISCLOSURE STATEMENT

Respondent BankChampaign, N.A., is a wholly owned subsidiary of Market Place Bancshares. Market Place Bancshares is a privately held entity.

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STATEMENT OF THE CASE

Respondent contends that where a trustee of an express trust breaches his or her duty of loyalty by violating the express limitations on his or her authority to borrow money from the trust, the trustee's debt arising from such defalcation is excepted from his or her bankruptcy discharge by reason of 11 U.S.C. § 523(a)(4). Under each of the standards for defalcation while acting as a fiduciary articulated by the Circuit Courts under that statute, the debtor-trustee's debt, which arose in this case from his violation of an express limitation on borrowing set forth in the trust instrument, is nondischargeable.

If certiorari were to be granted, Respondent urges that such a strict liability standard would require an affirmance without the need for the Court to pass on the divergent approaches of the Circuit Courts in cases not involving express limitations on a trustee's authority to borrow from the trust. It is further urged by Respondent that a strict liability standard would preclude a reversal. Consequently, if the Court recognizes that a strict liability must be imposed on a trustee who violates an express limitation on his or her authority to borrow from a trust, the present case does not call for a resolution of the divergent tests applied to other types of defalcation by a trustee. Respondent thus urges the Court to deny certiorari as this case does not squarely pose the issue for which Petitioner seeks certiorari.



REASONS FOR DENYING THE PETITION

A. The Court Should Deny The Petition For A Writ Of Certiorari Because The Facts Of This Case, Involving A Trustee's Violation Of An Express Limitation Of The Trust Instrument, Do Not Call For The Court To Address The Divergent Views On The Meaning Of "Defalcation" By A Fiduciary; Under Each Of Those Views, A Trustee Would Have A Strict Liability.

Respondent urges the Court to recognize that under any view of what constitutes a defalcation by a fiduciary, no trustee of an express trust may take action in disregard of express limitations on the authority of the trustee by the terms of the trust instrument and then, when held liable for damages caused by such disregard of a trust instrument's express limitations of authority to discharge such liability in bankruptcy. In that light, the Petition should be denied because if certiorari were granted, this appeal would be decided on the merits for Respondent under each of the standards applied by the various Circuit Courts. Under any standard, without regard to a trustee's good intention, state of mind or honesty of purpose, a trustee cannot discharge through a bankruptcy filing a debt arising from the disregard of a limitation on authority expressly imposed by the trust instrument. Indeed, even under the "extreme reckless" standard advocated by the Petitioner, the Petitioner's debt to Respondent is not dischargeable.

Petitioner relies heavily on *Rutanen ex rel. Quevillon v. Baylis (In re Baylis)*, 313 F.3d 9 (1st Cir. 2002), where the First Circuit articulated an extreme reckless standard for nondischargeability pursuant to section 523(a)(4). However, Petitioner missed the crucial distinction in *Baylis* between a strict test for non-dischargeability for debts incurred by a trustee by reason of self-dealing, and debts resulting from other types of conduct that are governed by less stringent standards. *Baylis* made clear that there is a defalcation within the meaning of section 523(a)(4) if a trustee breaches his or her duty of loyalty. Where, as here, a trustee engages in self-dealing and borrows money from the trust in violation of the trust instrument, the trustee is held “to a very strict standard,” and cannot discharge the resulting debt. As stated in *Baylis*:

In evaluating whether there is a defalcation of a fiduciary duty, there must be reference to the duty involved. Of the various duties, the duty of loyalty is “[t]he most fundamental duty owed . . . the duty of a trustee to administer the trust solely in the interest of the beneficiaries.” 2A A. Scott, *The Law of Trusts* § 170 (W.F. Fratcher ed., 4th ed. 2001).

Baylis, 313 F.3d at 20. As further stated in *Baylis*:

Defalcation may be presumed from breach of the duty of loyalty, the duty not to act in the fiduciary’s own interest when that interest

comes or may come into conflict with the beneficiaries' interest.

A trustee occupies a position in which the courts have fixed a very high and very strict standard for his conduct whenever his personal interest comes or may come into conflict with his duty to the beneficiaries.

Baylis, 313 F.3d at 20-21 (internal citation omitted). The court there concluded that the debtor's use of trust money for personal attorney fees and to settle a lawsuit brought against him personally was "in violation of his duty of loyalty," and thus, that the debtor-trustee's "actions as to this component of the debt do constitute defalcation." 313 F.3d at 22. In sum, it is clear that where, as here, a trustee borrows money from the trust for personal use in violation of the trust instrument, the trustee's breach of the duty of loyalty constitutes a defalcation which is non-dischargeable as a matter of law under § 523(a)(4).

The Petitioner in the present case unquestionably breached his duty of loyalty by self-dealing. Pet. App. at 57a ("It is undisputed that Defendant lent money to entities in which he had a financial interest or to relatives. Clearly this placed him in a position where he would be tempted to act in his interest, possibly against the interests of the beneficiaries."). As this court has stated with regard to the duty of loyalty and self-dealing,

[a]mong the most fundamental fiduciary obligations of a trustee is "to administer the

trust solely in the interest of the beneficiaries.” 2A A. Scott & W. Fratcher, *Law of Trusts* § 170, p. 311 (4th ed. 1987); see *Meinhard v. Salmon*, 249 N. Y. 458, 464, 164 N. E. 545, 546 (1928) (Cardozo, C. J.) (“Not honesty alone, but the punctilio of an honor the most sensitive,” is “the standard of behavior” for trustees “bound by fiduciary ties”).

United States v. Jicarilla Apache Nation, 131 S. Ct. 2313, 2336 (2011). It is this conduct of self-dealing that is characterized as “objectively reckless” by the Eleventh Circuit (see Pet. App. at 11a) and characterized as “extremely reckless” by the Second Circuit. *Baylis*, 313 F.3d at 22. In essence, these courts essentially imposed a strict rule governing non-dischargeability, ruling that self-dealing constitutes a defalcation under section 523(a)(4). Thus, under either standard, the Petitioner’s conduct is not dischargeable pursuant to 11 U.S.C. § 523(a)(4).

This case thus does not present an appropriate opportunity to address the various approaches to the meaning of defalcation taken by the various Circuit Courts because Respondent should prevail under any of the various approaches. A grant of certiorari will not serve to underscore the lesson of this case. A trustee should not be able to discharge a debt that arises from action that exceeds the express limitations on his or her authority by the trust instrument.

B. The Court Should Deny The Petition For A Writ Of Certiorari Because Respondent Does Not Have To Show A Loss In Order For Its Claim To Be Nondischargeable Pursuant To 11 U.S.C. § 523(a)(4).

The Petitioner further argues that the Court should grant the Petition because “the Eleventh Circuit here did not require that respondent prove a loss of principal . . . ” Pet. at 10. Petitioner’s contention, however, ignores that Petitioner incurred a debt to Respondent for his own financial benefit that he enjoyed as a result of his defalcation. The Bankruptcy Code does not discharge a “loss,” but rather discharges debts. See 11 U.S.C. § 524(a)(1) (voiding judgments “with respect to any [discharged] *debt*”) (emphasis added); 524(a)(2) (enjoining actions for any “*debt* as a personal liability of the debtor”) (emphasis added). See also 11 U.S.C. § 523(a) (stating that a discharge “does not discharge an individual debtor from any *debt* . . . ”) (emphasis added). The Bankruptcy Code defines a debt as a “liability on a claim.” 11 U.S.C. § 101(12). A “claim” is defined as a “right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured or unsecured.” 11 U.S.C. § 101(5)(A). This Court has stated that “‘claim’ has ‘the broadest available definition’” (*FCC v. NextWave Pers. Communs. Inc.*, 537 U.S. 293, 302 (2003) (citing *Johnson v. Home State Bank*, 501 U.S. 78, 83 (1991))) and that the “plain meaning of a ‘right to payment’ is

nothing more nor less than an enforceable obligation.” *FCC v. NextWave*, 537 U.S. at 302 (citing *Pennsylvania Dep’t of Pub. Welfare v. Davenport*, 495 U.S. 552, 559 (1990)).

Thus, the debt that the Petitioner seeks to discharge is not limited to a loss of the trust’s principal by reason of Petitioner’s defalcation, but also all debts that arise from all of Respondent’s enforceable claims against the Petitioner, including the disgorgement of the Petitioner’s benefit as ordered by the Illinois state court. *See* Pet. App. at 47a. Because Petitioner committed a defalcation while acting as a fiduciary, the Petitioner cannot discharge any liability on Respondent’s claim, including the liability for the financial benefit he received as a result of his defalcation.

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CONCLUSION

For the foregoing reasons, the Court should deny Petitioner’s petition for a writ of certiorari.

Respectfully submitted,

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