UNITED STATES BANKRUPTCY COURT
DISTRICT OF IDAHO

In Re: **Peter M. Estay,** **Debtor.**	**Bankruptcy Case No. 10-42115-JDP**
David A. Johnson, Larry Tweedie, Christina Tweedie, Greg Shenton, and Lisa Shenton **Plaintiffs,** **vs.** **Peter M. Estay,** **Defendant.**	**Adv. Proceeding Nos. 11-08025-JDP**
In Re: **Scott J. Estay,** **Debtor.**	**Bankruptcy Case No. 10-42116-JDP**

David A. Johnson, Larry Tweedie, Christina Tweedie, Greg Shenton, and Lisa Shenton **Plaintiffs,** **vs.** **Scott J. Estay,** **Defendant.**	**Adv. Proceeding Nos. 11-08026-JDP**

MEMORANDUM OF DECISION

Appearances:

Aaron J. Tolson, Ammon, Idaho and David A. Johnson, Wright, Wright & Johnson, PLLC, Idaho Falls, Idaho, Attorneys for Plaintiffs David A. Johnson, Larry Tweedie, Christina Tweedie, Greg Shenton, and Lisa Shenton

Peter M. Estay, Defendant, *pro se*

Scott J. Estay, Defendant, *pro se*

Introduction

Plaintiffs David A. Johnson, Greg Shenton, Lisa Shenton, Larry Tweedie, and Christina Tweedie commenced adversary proceedings,

arising from the same facts and transactions, against chapter 7[1] debtors Peter Michael Estay ("Peter Michael") (Adv. No. 11-08025-JDP) and Scott J. Estay ("Scott") (Adv. No. 11-08026-JDP).[2] Plaintiffs seek a declaration from the Court that the amount owed to them under a state court judgment by Peter Michael and Scott is excepted from discharge under § 523(a)(2)(A) and (a)(4). Without objection from the parties, the Court consolidated these adversary proceedings for trial and other proceedings. *See* Adv. No. 11-08025, Dkt. No. 44; Adv. No. 11-08026, Dkt. No. 46.[3]

The trial took place on March 27, 2014. At the conclusion of the presentation of the evidence and testimony, the parties asked for time to submit written closing arguments, and they did so. Dkt. Nos. 61, 62 and 63. At the conclusion of the post-trial briefing, the Court took the issues

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[1] Unless otherwise indicated, all chapter and section references are to the Bankruptcy Code, 11 U.S.C. §§ 101 – 1532, and all Rule references are to the Federal Rules of Bankruptcy Procedure, Rules 1001 – 9037.

[2] The references to Defendants by their first names are for clarity; no disrespect is intended.

[3] Since the pleadings in these two actions are, for the most part, identical, for convenience, the Court will cite only to the docket in Adv. No. 11-08025.

under advisement.[4] This Memorandum constitutes the Court's findings of fact and conclusions of law. Rule 7052.

Facts

Peter Michael and Scott are brothers who have been involved in various projects to develop and sell real property in eastern Idaho for many years. Peter J. Estay, their father, introduced them to this business, and has involved them in several business entities to implement these enterprises.

Plaintiffs Larry and Christina Tweedie invested in, and Mr. Tweedie was a principal in, some of these business entities. As relevant to this dispute, Mr. Tweedie and Scott were managing members of Rock Creek Development, LLC ("RCD"), an entity formed in 2003 to develop real

[4] The Court acknowledges the considerable passage of time between the trial and entry of this Memorandum. The reason for that delay, in large part, resulted when the Court was advised by Plaintiffs' counsel that a tentative resolution had been reached between the parties. However, as it turned out, no settlement documents were ever filed. Plaintiffs' counsel recently confirmed that no compromise was ever reached.

property in Teton County, Idaho they called Aspen Pointe. The Tweedies invested over $100,000 in RCD. Mr. Tweedie's sister, Plaintiff Lisa Shenton, and her husband, Plaintiff Greg Shenton, also invested $48,000 in RCD.

The issues before the Court arise from an agreement entered into by Mr. Tweedie on the one side, and Peter Michael, Scott, and Peter J. Estay on the other, related to RCD. In particular, when the parties' business relationship became strained, in order to resolve the conflicts, they entered into a written agreement dated November 21, 2004 (the "Agreement"). *See* Exh. 102; Exh. 200. Mr. Tweedie testified that the Estays prepared the Agreement, and that its purpose was to finalize the operations of RCD, to define the parties' responsibilities for the company's various debts, and to account for its receivables. The focus of this action is paragraph 8 of the Agreement, which provides:

> 8. Estays agree to further guarantee obligations of [RCD] by giving Greg [and] Lisa Shanton [sic] security in Block I Lot 6 and [Larry] Tweedie in Block I Lot 10 of the Sagewood Subdivision in Driggs, Idaho subject to:

1) Partial release provision in place with lenders.

2) A sixty-day buy-back provision that would facilitate a potential cash sale.

a) BLK I Lot 6 Sagewood @ $52,000
b) BLK I Lot 10 Sagewood @ 62,000

3) That in the event the buy[-]back provision is not exercised, the new owners agree to build a plan selection from the pre-approved list submitted in "Exhibit B".

4) That they agree to obey all the ordinances and directions of City, County and CC&R filings set forth within the Sagewood Final Plat.

In the event that such plat is not yet recorded or approved sufficient to enable the actual conveyance by deed as anticipated herein, the deed and/or assignment to accomplish the foregoing shall be given and recorded upon completion of the master plan and creation of the legal parcel for the house lots.

Exh. 102 at 2.

Mr. Tweedie testified at trial that his understanding of this provision was that the Estays would transfer the lots identified therein in a subdivision that was being developed by the Estays to him and the

Shentons.

In contrast, when called by Plaintiffs as witnesses to testify regarding the meaning of, and the facts surrounding, the Agreement, both Peter Michael and Scott refused to answer the questions of Plaintiffs' counsel. Instead, in response to each question as it pertained to their activities and intent with respect to the Agreement, or as to their other real estate ventures, they indicated that their answers may incriminate them, and thus, they declined to respond citing their Fifth Amendment privilege.

Peter Michael's and Scott's assertion of the privilege came as no surprise to the Court. Prior to trial, in their bankruptcy cases, an attorney representing both Peter Michael and Scott had filed an affidavit stating that he was representing them in connection with in "an investigation by the United States Department of Treasury,"and that he had advised them "that they may need to assert their [F]ifth [A]mendment privilege" when asked questions in their cases due to this pending investigation. *See* Dkt.

No. 47. However, in an affidavit submitted in a state court lawsuit, discussed below, Scott stated, "[a]s expressed in Paragraph 8 of the Agreement it was contemplated that my brother, Peter [Michael][,] my father, Peter J. Estay[,] and I would guaranty [sic] that the obligations of RCD would be paid and that we would provide security for such [a] guaranty in the lots mentioned. It was never contemplated that such lots [(i.e. lots 6 and 10)] would be merely transferred to [] Plaintiffs." Exh. 152 at ¶ 10. Scott then went on to state in the affidavit that after the Agreement was signed, the Tweedies and Shentons sold the remaining lots in Aspen Pointe for more than enough to pay all of the debts of RCD, including those owed to the Tweedies and Shentons. *Id.* at ¶ 12. Therefore, Scott stated, there was no need to transfer lots discussed in the Agreement to Plaintiffs. *Id.* at ¶ 13.

It is undisputed that the lots, as described in paragraph 8 of the Agreement, were never transferred to the Tweedies or Shentons. Thereafter, the Tweedies and Shentons engaged an attorney, Plaintiff

David A. Johnson, to represent them. Mr. Johnson prepared a "revised agreement" and sent it to Peter J. Estay along with an explanatory letter, on February 4, 2005. Exh. 149. The revised agreement was necessary, Mr. Johnson testified, because he found the original Agreement was "unclear" as to the transfer of the lots. According to Johnson, the revised agreement, as it related to paragraph 8 of the Agreement, provided that the Estays would "convey to Tweedie, free and clear of any encumbrance, by Warranty Deed, Block I, Lot 10 of the Sagewood Subdivision . . .", and that the Estays would "convey to Greg and Lisa Shenton, free and clear of any encumbrance, by Warranty Deed, Block I, Lot 6 of the Sagewood Subdivision." *Id.* at 3. The revised agreement was never executed by the Estays.

On November 21, 2007, represented by Mr. Johnson, the Tweedies and Shentons filed a lawsuit against the Estays in the Idaho state district court asserting that the Estays had breached the Agreement and converted the Sagewood lots. They sought money damages for breach of contract

and conversion, an accounting, and foreclosure of a lien. *See* Exhs. 107 and 108. Around the same time that the state court complaint was filed, Mr. Johnson prepared and recorded a "claim of lien" on behalf of the Tweedies and Shentons in the Teton County Recorder's Office, purportedly based upon the Agreement, wherein they claimed a lien in lots 6 and 10 of the Sagewood Subdivision. Exhs. 103 and 104.

The Estays, representing themselves, contested these state court claims. At a trial on March 26, 2010, the Tweedies and Shentons withdrew their claims for an accounting and for conversion. Exh. 108 at 2. After the trial, in a May 14, 2010 written decision, the state court quoted paragraph 8 of the Agreement, and concluded "as a matter of law . . . the Agreement was unambiguous and accurately reflects the intentions of the parties . . . the Court concludes that [the] Estays' signatures are valid and effective in conveying their own and Sagewood's interest [in lots 6 and 10]." *Id.* at 3, ¶ 8. The court found that after the Agreement was executed, "[l]ots 6 and 10 were later sold by [the] Estays to third parties . . . [and] [n]either

Tweedie nor Shenton were ever paid for the lots as provided in Paragraph 8(2) of the Agreement." *Id.* at 4, ¶ 9. Based upon this finding, the state court concluded that Peter Michael and Scott had breached the Agreement, and it granted the Tweedies and Shentons a money judgment against them for breach damages in the amount of $114,000, and decreed that they were "entitled to collect upon their liens from any interest [the Estays] may have in Block 1, Lots 6 and 10, of the Sagewood Subdivision in Driggs, Teton County, Idaho, pursuant to [Idaho Code] § 45-804[.]" *Id.* at 11. After entry of this judgment, on September 17, 2010, the state court amended the money judgment to $214,423.80 (to include attorney's fees, interest, and costs); granted the Tweedies and Shentons a lien against lots 6 and 10; and authorized them to foreclose the liens via a sheriff's sale. Exh. 110. Plaintiffs did not foreclose on either lot.

On July 7, 2005, Sagewood, LLC had apparently transferred lot 6 to an unrelated party. *See* Affidavit of Scott, Exh. 152 at ¶ 9 ("After the Sagewood Subdivision was properly platted, Sagewood Subdivision sold

Block I, Lot 6 to Steve Meyers on July 7, 2005 . . . .").[5] Lot 10, on the other hand, had been transferred by Sagewood, LLC to Peter Michael on February 28, 2007 (Exh. 103), who then granted a deed of trust on the lot to MMF, LLC on August 6, 2007 (Exh. 106) to secure repayment of a loan. On July 23, 2010, Peter Michael transferred the lot to Essco Investments via a "Warranty Deed in Lieu of Foreclosure" (Exh. 112), after the state district court entered its judgment against the Estays, but before entry of the amended judgment.

On November 29, 2010, Peter Michael and Scott each filed for relief under chapter 13. *See* Bankr. No. 10-42115, Dkt. No. 1 and Bankr. No. 10-42116, Dkt. No. 1, respectively. The bankruptcy cases were eventually converted to chapter 7 on March 10, 2011. Dkt. No. 66 and Dkt. No. 52. These adversary proceedings were commenced on March 7, 2011, wherein Mr. Johnson, the Tweedies, and the Shentons seek an exception to discharge in both cases for amounts owed to them on the state court

[5] Exhibit 120, identified by Plaintiffs as "Sagewood Ownership Listing," shows that Mr. Meyers received lot 6 on August 3, 2005, however.

judgment pursuant to § 523(a)(2)(A) and (a)(4) based upon the Agreement. Peter Michael and Scott each filed answers to the complaints generally denying that Plaintiffs were entitled to any relief under those Code provisions.

Analysis and Disposition

Plaintiffs argue that the debts owed to them by Peter Michael and Scott, evidenced by the state court money judgment, should be excepted from discharge in each bankruptcy case because, in entering into the Agreement, Peter Michael and Scott perpetrated a fraud against them. In particular, Tweedies and Shentons allege that Peter Michael had "no intent to comply" with their contractual obligations under the Agreement when they prepared and signed that document. Dkt. No. 61 at 2. Further, Plaintiffs argue that the transfers of lot 10 from Sagewood, LLC to Peter Michael, and then to Essco Investments, constituted fraud or defalcation while both Peter Michael and Scott were acting fiduciaries under the Agreement. *Id.* at 5. Finally, Plaintiffs argue Peter Michael's transfer of lot

10 after the entry of the state court judgment in May 2010, was a fraudulent conveyance[6] and that (somehow) this transfer also supports a finding that the debts at issue are excepted from discharge.

I. Standing to Assert an Exception to Discharge Claim

Before discussing whether Tweedies and Shentons are entitled to an exception to discharge in Peter Michael's and Scott's bankruptcy case, the Court will first review Mr. Johnson's claim for that relief. The Court concludes Mr. Johnson lacks legal standing to assert a claim for an exception to discharge because he is not a "creditor" in the bankruptcy cases.[7]

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[6] Plaintiffs acknowledge that an action to avoid and recover a debtor's prebankruptcy fraudulent conveyance is properly prosecuted by the chapter 7 trustee in the bankruptcy case. Nevertheless, Plaintiffs state, "[t]he Trustee has not pursued this fraudulent conveyance, but Tweedies are pursuing the same." Dkt. No. 61 at 7. Plaintiffs do not explain how this allegation of a fraudulent transfer by Peter Michael and Scott can serve as a basis for excepting the judgment debt from discharge.

[7] Peter Michael and Scott have not challenged Mr. Johnson's standing in these actions. However, standing to prosecute an action is a jurisdictional prerequisite, and the Court is therefore obliged to independently examine Mr. Johnson's status. *General Elec. Capital Auto Lease, Inc. v. Broach (In re Lucas Dallas, Inc.)*, 185 B.R. 801, 804 (9th Cir. BAP 1995).

"Only 'the creditor to whom such a debt is owed' may request a determination by the bankruptcy court concerning whether a debt . . . should be excepted from discharge under either § 523(a)(2)(A) or (a)(4)." *State of Idaho v. McClung (In re McClung)*, 304 B.R. 419, 421 (Bankr. D. Idaho 2004) (quoting § 523(c)(1) and citing *Fezler v. Davis (In re Davis)*, 194 F.3d 570, 574 (5th Cir. 1999)). A "creditor" is an "entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor." § 101(10)(A). A "claim" is a "right to payment . . . or . . . [a] right to an equitable remedy for breach of performance if such breach gives rise to a right to payment . . . ." § 101(5)(A) and (B). A "'[r]ight to payment" means 'nothing more nor less than an enforceable obligation.'" *Securities Exchange Comm'n v. Cross (In re Cross)*, 218 B.R. 76, 78 (9th Cir. BAP 1998) (quoting *Johnson v. Home State Bank*, 501 U.S. 78, 83 (1991)). "[W]hen the Bankruptcy Code uses the word 'claim'—which the Code itself defines as a 'right to payment' . . . it is usually referring to a right to payment recognized under state law." *Travelers Cas. and Sur. Co. of America*

v. Pacific Gas and Elec. Co., 549 U.S. 443, 450 (2007).

In this case, Mr. Johnson asserts that he is proper party-plaintiff in the adversary proceedings, and is entitled to an exception to discharge, because the state court judgment awarded the Tweedies and Shentons attorneys fees and costs they incurred for his services. In Idaho, while a "prevailing party" may be entitled to an award of attorney's fees incurred in prosecuting an action, there is nothing in the statutes or in the relevant case law that vests that right in the "prevailing party's" attorney. *See, e.g.*, Idaho Code § 12-121 (stating "the judge may award reasonable attorney's fees to the prevailing party or parties"); Idaho Code § 12-120(3) (stating "the prevailing party shall be allowed a reasonable attorney's fee . . . ."); *Kinghorn v. Clay*, 283 P.3d 779, 784 (Idaho 2012) (concluding that an attorney who was not a party to an action, but who claimed an attorney's lien, lacked standing to appeal a judgment because he was not a party to the case, and holding "an attorney who seeks to participate in an appeal in order to advance his or her personal interest with regard to a claimed

charging lien . . . must become a party in order to have standing."); *see also Smith v. South Side Loan Co.*, 567 F.2d 306, 307 (5th Cir. 1978) ("[A]n award [of attorney's fees] is the right of the party suing not the attorney representing him.").

Here, Mr. Johnson is not a "creditor to whom such debt is owed" for purposes of the bankruptcy cases of Peter Michael or Scott because he does not hold an enforceable, direct right to payment from either of the debtors. *See Blixseth v. Blixseth (In re Blixseth)*, 459 B.R. 444, 456 (Bankr. D. Mont. 2011) (stating "'creditor to whom such debt is owed' means literally that the creditor is owed money by the debtor, and that the creditor holds a claim in its own behalf or in its own right."). Indeed, Mr. Johnson has not explained to the Court, in his briefs, or during an exchange with the Court while testifying, how he is a "creditor" in the bankruptcy cases clothed with standing to assert a claim for relief under § 523(a). The Court presumes Mr. Johnson would argue, as the attorney in the state court action, that the amended judgment entered by the state court, which

awarded attorney's fees to his clients, gives him standing in these cases. But he is incorrect, and the Court concludes that Mr. Johnson lacks standing to assert a claim in these actions because he is not a "creditor" in the bankruptcy cases of either Peter Michael or Scott.

II. Fifth Amendment Privilege in Exception to Discharge Cases

Peter Michael and Scott declined to answer otherwise appropriate questions at trial because they claimed doing so might tend to incriminate them in connection with, what they describe as a pending IRS investigation of their affairs. The Court therefore begins by exploring the implications of their invocation of the protections of the Fifth Amendment.

The Fifth Amendment to the United States Constitution provides, in relevant part, "[n]o person . . . shall be compelled in any criminal case to be a witness against himself . . . ." U.S. CONST. amend V. This privilege applies in bankruptcy proceedings. *In re Ross*, 156 B.R. 272, 274 (Bankr. D. Idaho 1993) (citing *McCarthy v. Arndstein*, 266 U.S. 34, 41 (1924)). "A debtor may assert the privilege if presented with a real hazard of

incrimination, and the privilege protects information that might provide a lead or clue to evidence that has the tendency to incriminate, in addition to information that would support a criminal conviction." *In re Galan*, 455 B.R. 214, 225 (Bankr. D. Idaho 2011) (citing *In re Ross*, 156 B.R. at 274).

However, a witness's decision to invoke the Fifth Amendment may have consequences. For example, in a civil case, the trier of fact may draw an adverse inference from a party's invocation of his Fifth Amendment rights. *Baxter v. Palmigiano*, 425 U.S. 308, 317-18 (1976); *Doe ex rel. Rudy-Glanzer v. Glanzer*, 232 F.3d 1258, 1264 (9th Cir. 2000). Adverse inferences may be drawn only "when silence is countered by *independent evidence* of the fact being questioned, but cannot be drawn when, for example, silence is the answer to an allegation contained in the complaint." *Glanzer*, 232 F.3d at 1264 (citing *Nat'l Acceptance Co. v. Bathalter*, 705 F.2d 924, 930 (7th Cir. 1983)) (emphasis in original); *see also Nationwide Life Ins. Co. v. Richards*, 541 F.3d 903, 912 (9th Cir. 2008) (stating "the inference may be drawn only when there is independent evidence of the fact about which the party

refuses to testify.") (citing *Glanzer*, 232 F.3d at 1264). In other words, if there "is no corroborating evidence to support the fact under inquiry, the proponent of the fact must come forward with evidence to support the allegation, otherwise no negative inference will be permitted." *Glanzer*, 232 F.3d at 1264 (citing *LaSalle Bank Lake View v. Seguban*, 54 F.3d 387, 391 (7th Cir. 1995)). Further, the adverse inference "may not be drawn 'unless there is a substantial need for the information and there is not another less burdensome way of obtaining the information.'" *Nationwide Life Ins. Co.* 541 F.3d at 912 (quoting *Glanzer*, 232 F.3d at 1266).

In this case, the Court determined early on in the bankruptcy cases that because Peter Michael and Scott were (and may still be) under active investigation by the IRS, and because their testimony about their financial dealings could well provide information which might tend to incriminate them in connection with that investigation, Peter Michael and Scott could validly assert the privilege provided by the Fifth Amendment. When they did so again at the trial of these adversary proceedings, Plaintiffs did not

contest their right to assert the privilege.

Considering all of the evidence and testimony proffered, the Court declines to draw any adverse inferences from Peter Michael's or Scott's invocation of the privilege in these actions. This is because, as is explained below, Plaintiffs failed to produce independent evidence to support a finding, as alleged, that Peter Michael or Scott perpetrated a fraud in their dealings with Plaintiffs, by way of actual fraud, or through fraud or defalcation as fiduciaries, with respect to the Agreement. In addition, Plaintiffs have also not shown that the information they solicited during the trial examination of Peter Michael an Scott was not otherwise available to them. Under these circumstances, the Court declines to infer that Peter Michael's and Scott's refusal to answer trial questions supports Plaintiffs' claim of fraud.

III. Exceptions to Discharge

Chapter 7 debtors are provided a "fresh start" in bankruptcy, in part, when they receive a discharge of their prebankruptcy debts. *See*

§ 727(a). Congress has determined, however, that certain kinds of debts, catalogued in § 523(a), should be excepted from discharge. § 727(b). Here, Plaintiffs assert that their claims against Peter Michael and Scott should be excepted from discharge pursuant to § 523(a)(2)(A) and (a)(4) because they engaged in fraud. Under § 523(c), debts arising from fraud, or fraud or defalcation by a fiduciary, are discharged unless, on request by a creditor, the bankruptcy court determines that such debts should be excepted from discharge. As Plaintiffs have done here, such a request is made through a timely adversary proceeding. *See* Rules 7001(6) and 4007(a).

In a § 523(a) action, the creditor bears the burden of proving that a debt should be excepted from discharge by a preponderance of the evidence. *Grogan v. Garner*, 498 U.S. 279, 288 (1991). In deciding such cases, the bankruptcy courts must limit exceptions to discharge to those plainly expressed in § 523(a). *Bullock v. BankChampaign, N.A.*, 133 S. Ct. 1754, 1760 (2013); *Sachan v. Huh (In re Huh)*, 506 B.R. 257, 267 (9th Cir. BAP 2014) (en banc).

A. Section 523(a)(2)(A)

Section 523(a)(2)(A) provides "[a] discharge under section 727 . . . of this title does not discharge an individual debtor from any debt— . . . (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by— (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition[.]" As can be seen, to obtain an exception to discharge, this provision requires a creditor to prove each of five elements: "(1) misrepresentation, fraudulent omission or deceptive conduct by the debtor; (2) knowledge of the falsity or deceptiveness of his statement or conduct; (3) an intent to deceive; (4) justifiable reliance by the creditor on the debtor's statement or conduct; and (5) damage to the creditor proximately caused by its reliance on the debtor's statement or conduct." *Turtle Rock Meadows Homeowners Ass'n v. Slyman (In re Slyman)*, 234 F.3d 1081, 1085 (9th Cir. 2000) (citing *American Express Travel Related Servs. Co. v. Hashemi (In re Hashemi)*, 104 F.3d 1122, 1125 (9th Cir. 1996);

Citibank (South Dakota), N.A. v. Eashai (In re Eashai), 87 F.3d 1082, 1086 (9th Cir. 1996)).

All things considered, the Court concludes that Plaintiffs have not proven that the debts based upon the state court judgment against Peter Michael and Scott should be excepted from discharge under § 523(a)(2)(A). In particular, Plaintiffs' proof failed as to the first three elements identified above.

To begin, the Court concludes that insufficient evidence was offered by Plaintiffs to prove that either Peter Michael or Scott made a misrepresentation, fraudulent omission, or engaged in deceptive conduct in connection with the Agreement. Of course, "[e]ntering a contract implies a 'representation of intent to honor its terms.'" *Burks v. Bailey (In re Bailey)*, 499 B.R. 873, 888 (Bankr. D. Idaho 2013) (quoting *Sharma v. Salcido (In re Sharma)*, 2013 WL 1987351, at *10 (9th Cir. BAP May 14, 2013)). And a party's failure to take steps to adhere to a contract may be circumstantial evidence of fraudulent intent. *Cowen v. Kennedy (In re Kennedy)*, 108 F.3d

1015, 1018 (9th Cir. 1997); *Fetty v. DL Carlson Enters., Inc. (In re Carlson)*, 426 B.R. 840, 855 (Bankr. D. Idaho 2010). But a party's breach of contract alone—even a breach without excuse—is generally not sufficient to establish an exception to discharge under § 523(a)(2)(A). *Businger v. Storer (In re Storer)*, 380 B.R. 223, 235 (Bankr. D. Mont. 2007); *see also* 4 COLLIER ON BANKRUPTCY ¶ 523.08[1][d] (Alan N. Resnick & Henry J. Sommer eds., 16th ed.) ("The failure to perform a mere promise is not sufficient to make a debt nondischargeable, even if there is no excuse for the subsequent breach. A debtor's statement of future intention is not necessarily a misrepresentation if intervening events cause the debtor's future actions to deviate from previously expressed intentions. A misrepresentation . . . to perform contractual duties, however, may be a false representation . . . if the debtor had no intention of performing any of the obligations under the contract. This intent may be inferred from the fact that the debtor failed to take any steps to perform under the contract.").

Here, Plaintiffs assert that, through the Agreement, Peter Michael

and Scott promised to transfer lots 6 and 10 to the Tweedies and Shenton, that they failed to do so, and that they instead participated in the transfer of these lots to other parties. This, they argue, constitutes a breach of the Defendants' obligations under Agreement, and that this conduct was the basis for the state court's judgment against them. But even assuming that Peter Michael and Scott agreed to such a transfer in Paragraph 8 of the Agreement, and that they breached the contract by failing to do so,[8] and despite the state court's judgment, Plaintiffs have not shown that Defendants engaged in fraud. In other words, that Peter Michael and Scott failed to later transfer the lots as promised is not sufficient evidence in the Court's opinion to establish that, at the time they entered the Agreement, they had no intent to perform. Because the proof is lacking that either

[8] The party's use of the word "security" in Paragraph 8 of the Agreement, even if further provisions of the paragraph suggest that an outright transfer of the lots was intended, makes this question a closer call in the Court's mind. Notably, Mr. Johnson testified candidly that he thought this paragraph was "unclear" to effect a transfer to his clients, and therefore he attempted to revise the Agreement with more clear and concise transfer language in a revised agreement, which the Estays did not sign. *See* Exh. 149.

Peter Michael or Scott made a misrepresentation, fraudulent omission, or engaged in deceptive conduct in connection with entering into the Agreement, Plaintiffs have not shown they are entitled to a § 523(a)(2)(A) exception to discharge.

To show fraudulent intent, Plaintiffs point to the transfer of the lots to other parties. By doing this, Plaintiffs note that Peter Michael and Scott obtained the benefits of the Agreement, without shouldering its burdens. Plaintiffs argue their intent must have been to deceive. But without more proof, this is a leap of logic the Court is not inclined to take.

Notably, Plaintiffs offered in evidence Scott's affidavit filed in the state court case. Exh. No. 149. In it, Scott explained that the purpose of the Agreement was to specify how the debts of RCD would be paid, and that through subsequent sales of lots, all of RCD's debts were indeed paid, including the debts owed to Tweedies and Shentons. At least in Scott's view, because the debts were paid, the primary purpose of the Agreement was achieved. Presumably, then, there was no continuing need to transfer

the lots to Tweedies and Shentons. While Scott's interpretation of the obligation he and Peter Michael undertook through the Agreement may be flawed, it is evidence that they did not intend through their post-Agreement actions to defraud Plaintiffs.

While the proof is perhaps subject to varying interpretations, Plaintiffs have not shown by a preponderance of the evidence that Peter Michael and Scott engaged in fraud. The Court therefore declines to determine that the debt owed to Plaintiffs by Peter Michael and Scott should be excepted from discharge under § 523(a)(2)(A) in either bankruptcy case.

B. Section 523(a)(4)

The Ninth Circuit Bankruptcy Appellate Panel recently summarized the requirements for an exception to discharge under § 523(a)(4):

> In pertinent part, § 523(a)(4) excepts from discharge debts incurred for "for fraud or defalcation while acting in a fiduciary capacity." § 523(a)(4). The term "fiduciary" is narrowly defined for purposes of § 523(a)(4). *Honkanen v. Hopper (In re Honkanen)*, 446

> B.R. 373, 378 (9th Cir. BAP 2011) (citing *Cal–Micro, Inc. v. Cantrell (In re Cantrell)*, 329 F.3d 1119, 1125 (9th Cir. 2003)). In order for there to be nondischargeability under § 523(a)(4), the debtor's fiduciary capacity "must be arising from an express or technical trust that was imposed before, and without reference to, the wrongdoing that caused the debt . . . ." *In re Cantrell*, 329 F.3d at 1125 (quoting *Lewis v. Scott (In re Lewis)*, 97 F.3d 1182, 1185 (9th Cir. 1996)). A trust "ex maleficio"—that is, a trust imposed by law as a remedy for malfeasance or wrongful actions—will not suffice. *In re Honkanen*, 446 B.R. at 379. Moreover, "[t]he broad, general definition of fiduciary—a relationship involving confidence, trust and good faith—is inapplicable in the dischargeability context." *In re Cantrell*, 329 F.3d at 1125 (quoting *Ragsdale v. Haller*, 780 F.2d 794, 796 (9th Cir. 1986)).

Zandt v. Mbunda (In re Mbunda), 484 B.R. 344, 356 (9th Cir. BAP 2012); *see also Med. Recovery Servs., LLC v. Ford (In re Ford)*, 12.1 IBCR 35, 36 (Bankr. D. Idaho 2012).

The Supreme Court has held that the term "defalcation" in § 524(a)(4) requires an intentional wrong committed by a fiduciary who knows the conduct is improper, or who engages in reckless conduct that violates his or her fiduciary duties. *Bullock*, 133 S. Ct. at 1759-60. "Where

actual knowledge of wrongdoing is lacking, we consider conduct as equivalent if the fiduciary 'consciously disregards' (or is willfully blind to) 'a substantial and unjustifiable risk' that his conduct will turn out to violate a fiduciary duty." *Id.* at 1759 (quoting Model Penal Code § 2.02(c), p. 226 (1985)).

The Court need not decide whether Peter Michael and Scott engaged committed a fraud or defalcation because Plaintiffs have not shown that the Agreement created a fiduciary relationship between the parties. Plaintiffs provide no support for their conclusion the Agreement created "an express or technical trust,"and the Court is unaware of any such proof in the record. *See High Valley Concrete, LLC v. Sargent*, 234 P.3d 747, 752 (Idaho 2010) (stating "a [fiduciary] relationship does not exist when parties are dealing with one another at 'arm's length:' 'Idaho law establishes that no fiduciary duty ordinarily arises between parties to an arm's length business transaction.'") (quoting *Wade Baker & Sons Farms v. Corp. of Presiding Bishop of Church of Jesus Christ of Latter-Day Saints*, 43 P.3d 715, 712

(Idaho Ct. App. 2002)). Because Plaintiffs have not shown that, through the Agreement, Peter Michael and Scott were fiduciaries as to Plaintiffs, they are not entitled to exception to discharge under § 523(a)(4).

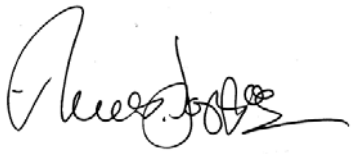
Conclusion[9]

Mr. Johnson lacks legal standing to pursue a discharge exception because he is not a creditor of either Peter Michael or Scott. The Tweedies and Shentons did not adequately prove their § 523(a)(2)(A) and (a)(4) claims. The debts represented by the state court judgment are therefore dischargeable. The Court will enter a separate judgment in favor of Defendants

[9] As noted above, Plaintiffs claim the transfer of lot 10 after entry of the state court judgment was a fraudulent conveyance by Peter Michael and Scott, and thus, Plaintiffs argue, the Court should determine the judgment debt should be excepted from discharge. Plaintiffs have not supported this argument with any authority, and the Court is aware of none. Therefore, the Court declines to further consider Plaintiffs' theory.

September 4, 2014

Dated:



Honorable Jim D. Pappas
United States Bankruptcy Judge