UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

In re

FRANCIS E. DICHTEL, **Case No. 96-21371-K**

Debtor. **Chapter 7**

EDWARD L. MONTEDONICO, Chapter 7 Trustee of the Estate of SHEILA TAYLOR,

Plaintiff, **Adv. Proc. No. 97-0129**

vs.

FRANCIS E. DICHTEL, the above-named Chapter 7 Debtor,

Defendant.

MEMORANDUM AND ORDER RE COMPLAINT UNDER 11 U.S.C. § 523(a)(4) COMBINED WITH NOTICE OF THE ENTRY THEREOF

Plaintiff, Edward L. Montedonico, Chapter 7 Trustee for the estate of Sheila Taylor, case no. 92-33297 (Bankr. W.D. Tenn.), seeks a nondischargeability judgment under 11 U.S.C. § 523(a)(4) against the defendant, Francis E. Dichtel ("Mr. Dichtel"), the above-named debtor.

By virtue of 28 U.S.C. § 157 (b)(2)(I) this is a core proceeding. The court has jurisdiction of this action under 28 U.S.C. §§ 1334(a)-(b) and 157(a) and Miscellaneous District Court Order No. 84-30 entered on July 11, 1984. Based on sworn testimony of plaintiff, statements of counsel, and the case record as a whole, the following shall constitute the court's findings of fact and conclusions of law in accordance with Fed. R. Bankr. P. 7052.

The relevant background facts may be briefly summarized as follows. On December 4,

1992, Sheila Taylor ("Ms. Taylor") filed a chapter 11 case. She employed Mr. Dichtel as her chapter 11 attorney and paid him a retainer fee of $2,000. After Ms. Taylor's chapter 11 case was converted to a case under chapter 7, Mr. Dichtel filed an application for additional compensation for services rendered. Written objections were filed thereto by the United States Trustee and the Bank of Bartlett. On February 23, 1995, an order denying the application was entered prohibiting Mr. Dichtel from distributing the $2,000 retainer fee until authorized by the bankruptcy court. On October 25, 1995, an order was entered directing Mr. Dichtel to turn over the $2,000 retainer fee and also an unrelated $500 that Mr. Dichtel had received from Ronald H. Droust, Esquire, a closing attorney, as partial proceeds from the sale of a parcel of Ms. Taylor's real estate. Despite a subsequent order for turnover entered on April 12, 1996, Mr. Dichtel failed to turn over the $2,500.

On January 30, 1996, Mr. Dichtel filed his own chapter 7 case. Plaintiff, Edward L. Montedonico in his capacity as Chapter 7 Trustee of the estate of Sheila Taylor, a creditor of Mr. Dichtel, filed the above-referenced adversary proceeding under 11 U.S.C. § 523(a)(4) seeking an exception to Mr. Dichtel's general discharge - that is, the plaintiff seeks a nondischargeable judgment for the $2,500 debt owed to the estate of Sheila Taylor by Mr. Dichtel.

Section 523(a)(4) of the Bankruptcy Code provides that:

> (a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt —
>
> * * *
>
> (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.

Since there is no indication of fraud, embezzlement, or larceny, the plaintiff must show by a

preponderance of the evidence that the debt was incurred through defalcation while acting in a fiduciary capacity. *Grogan v. Garner*, 498 U.S. 279, 291 (1991).

The term "fiduciary duty" has been construed differently among the federal courts. For example, some federal courts construe the term broadly, holding that the attorney-client relationship by itself satisfies the necessary fiduciary relationship for purposes of section 523(a)(4). See*,* for example, *Tudor Oaks Ltd. Partnership v. Cochrane (In re Cochrane)*, 179 B.R. 628 (Bankr. D. Minn. 1995); *Tai v. Charfoos (In re Charfoos)*, 183 B.R. 131 (Bankr. E.D. Mich. 1994).

The Sixth Circuit Court of Appeals in *Garver v. Garver*, 116 F.3d 176, 179 (6th Cir. 1997), adopted a narrower interpretation of the term "fiduciary duty" and held that "[t]he attorney-client relationship, without more, is insufficient to establish the necessary fiduciary relationship for defalcation under section 523(a)(4)." Furthermore, The *Garver* court defined defalcation as the "misappropriation of trust funds held in any fiduciary capacity and the failure to properly account for such funds." The court stated that the defalcation provision in section 524(a)(4) is limited only to situations involving an express or technical trust arising from placement of money or property in the hands of the debtor. *Id.* at 180. See also *Capitol Indem. Corp. v. Interstate Agency, Inc. (In re Interstate Agency)*, 760 F.2d 121 (6th Cir. 1985)*; Fowler Bros. V. Young (In re Young)*, 91 F.3d 1367 (10th Cir. 1996); *Evans v. Pollard (In re Evans)*, 161 B.R. 474 (9th Cir. BAP 1993); *Kayes v. Klippel (In re Klippel)*, 183 B.R. 252 (Bankr. D. Kan. 1995); *Kartchner v. Kudla (In re Kudla)*, 105 B.R. 985 (Bankr. D. Colo. 1989).

Intent is not an essential element of defalcation under section 523(a)(4); an innocent or

simple failure to account for funds is sufficient to render the debt nondischargeable. See, for example, *In re Waters*, 20 B.R. 277, 280 (Bankr. W.D. Tex. 1982). Defalcation is evaluated by an objective standard and no element of intent or bad faith need be shown. *In re Turner*, 134 B.R. 646 (Bankr. N.D. Okla. 1994). Negligent misconduct may constitute defalcation even though the debtor derived no personal benefit. *In re Galbreath*, 112 B.R. 892 (Bankr. S.D. Ohio 1990).

The threshold issue before the court is whether the totality of the circumstances surrounding the $2,000 retainer fee and the $500 sale proceeds constitute an express or technical trust for purposes of determining whether a fiduciary duty existed as contemplated under section 523(a)(4) of the Bankruptcy Code. While federal law is determinative when considering whether the debtor is a "fiduciary" for bankruptcy dischargeability purposes, state law is relevant in determining whether such trust actually exists. See *Interstate Agency*, 760 F.2d at 124; *In re Johnson*, 691 F.2d 249 (6th Cir. 1982); In re Pedrazzini, 644 F.2d 756 (9th Cir. 1981); *In re Ducey*, 160 B.R. 465 (Bankr. D.N.H. 1993).

Under applicable Tennessee state law, the Code of Professional Responsibility provides that "[a]ll client funds paid to a lawyer or law firm, including advances for costs and expenses, shall be deposited in one or more identifiable insured depository institutions." DR 9-102(A). Therefore, all attorneys in the State of Tennessee must hold the property of clients in trust and that money should be clearly designated in a separate trust account. This rule is particularly applicable to attorneys in a bankruptcy setting since under section 329 of the Bankruptcy Code and Fed. R. Bankr. P. 2016 all payments to an attorney before the order for relief are subject to the court's review as to whether or not the retainer paid exceeded the reasonable value of

services rendered. Retainers paid to counsel are to be held in trust and the debtor's equitable interest is property of the estate. *Mapother & Mapother, P.S.C., v. Cooper (In re Downs)*, 103 F.3d 472 (6th Cir. 1996); *In re Rittenhouse*, 76 B.R. 610 (Bankr. S.D. Ohio 1987).

When Ms. Taylor delivered the $2,000 retainer to Mr. Dichtel and signed the required disclosure statement pursuant to Rule 2016(b), she entrusted him to place the money in a separate account. Clearly, an express and technical trust was created. Additionally, the $500 that was distributed to Mr. Dichtel by Ronald Droust, Esquire, as partial proceeds from the sale of real estate was to be held in escrow or a trust pending further order of the court.

This court finds under the circumstances that the attorney-client relationship between Mr. Dichtel and Ms. Taylor coupled with the entrustment of such funds in the hands of Mr. Dichtel created a fiduciary duty for purposes of section 523(a)(4). See *In re Ducey*, 160 B.R. at 471-72; *In re Kudla*, 105 B.R. at 991. Mr. Dichtel failed to properly account for the trust funds when he refused to obey three turnover orders entered by the bankruptcy court.[1] Accordingly, this court holds that Mr. Dichtel committed defalcation while acting in a fiduciary capacity and the resulting $2,500 debt is nondischargeable under section 523(a)(4) of the Bankruptcy Code.

Based on the foregoing,

IT IS ORDERED AND NOTICE IS HEREBY GIVEN that the plaintiff's complaint for an exception to Mr. Dichtel's general discharge be granted and the $2,500 debt is rendered nondischargeable under 11 U.S.C. § 523(a)(4) to bear interest pursuant to 28 U.S.C. § 1961.

---

[1] Compare *In re Calvert*, 105 F.3d (6th Cir. 1997) and the doctrine of collateral estoppel.

BY THE COURT

David S. Kennedy
Chief United States Bankruptcy Judge

Dated: August 15, 1997

cc: David A. Kirkscey, Esquire
Attorney for Plaintiff
22 N. Front, Suite 760
Memphis, TN 38103

Mr. Edward L. Montedonico
Chapter 7 Trustee for the estate of Ms. Taylor
200 Jefferson #222
Memphis, TN 38103

Mr. Francis E. Dichtel, Pro Se
7787 Wolf River Road
and 2914 S. Mendenhall
Memphis, TN 38115

Mr. Preston Wilson
Chapter 7 Trustee of the estate of Mr. Dichtel
200 Jefferson, Suite 900
Memphis, TN 38103

U.S. Trustee for Region 8
200 Jefferson, 4th floor
Memphis, TN 38103