The court incorporates by reference in this paragraph and adopts as the findings and orders of this court the document set forth below. This document has been entered electronically in the record of the United States Bankruptcy Court for the Northern District of Ohio.

Dated: May 8 2014

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
WESTERN DIVISION

In Re:	)	Case No. 11-35901
	)	
Steven Paul Klausing and	)	Chapter 7
Janet Rose Klausing	)	
	)	Adv. Pro. No. 12-3034
	)	
Debtors.	)	Judge John P. Gustafson
	)	
Douglas Daley, special administrator for and on	)	
behalf of the Estate of Paula Minzing,	)	
	)	
Plaintiff,	)	
	)	
v.	)	
	)	
Janet Rose Klausing,	)	
	)	
Defendant.	)	

MEMORANDUM OF DECISION AND ORDER REGARDING DEFENDANT JANET KLAUSING'S MOTION FOR SUMMARY JUDGMENT

This Adversary Proceeding is before the court on Debtor-Defendant's Motion for Summary Judgment [Doc. #51]. Plaintiff has filed a Memorandum in Opposition to the Debtor-Defendant's Motion for Summary Judgment. [Doc. #57]. The Chapter 7 Trustee did not file a response to the Motion for

Summary Judgment, which addresses solely the dischargeability of debt issue under §523(a)(4).

The Complaint to Determine Dischargeability of Debt Pursuant to Bankruptcy 11 U.S.C. §523(a)(4) and for Determination Pursuant to 11 U.S.C. §541 of Property [Doc. #1] (hereinafter "Complaint") was filed on February 21, 2012 by Douglas Daley, Special Administrator for and on behalf of the Estate of Paula Minzing. An Answer was filed[1] by Defendant-Debtor Janet Rose Klausing (hereinafter "Janet Klausing") [Doc. #6]. An Answer was also filed by the Chapter 7 Trustee, Bruce C. French. [Doc. #7].

Many of the basic facts are not in dispute.

Janet Klausing filed for relief under Chapter 7 of the Bankruptcy Code on October 31, 2011. Complaint, ¶1; Answer of Janet Klausing ¶1.

The parties agree that the Chapter 7 Trustee is duly appointed, that jurisdiction and venue are proper and that this is a core proceeding under 28 U.S.C. §157(a).[2] Complaint, ¶¶2-4; Answer of Janet Klausing ¶1 (admitting paragraphs 1 - 9).

In Probate Court case No. 20071198, the Van Wert County Probate Judge appointed Janet Klausing as the executor of the Estate of Paula Minzing who died on September 11, 2007. Complaint, ¶5; Answer of Janet Klausing ¶1. The Plaintiff, Douglas A. Daley, is an attorney appointed as Special Administrator of the Estate of Paul Minzing, by appointment and order of the Van Wert Probate Court as a result of exceptions to the final account filed by executor Janet Klausing for the Estate of Paula Minzing. Complaint, ¶6; Answer of Janet Klausing ¶1.

On or about November 17, 2010, the Probate Court issued a Judgment that Janet Klausing pay the Estate of Paula Minzing the amount of Forty Thousand Nine Hundred Twenty-six Dollars and Ten Cents

[1]/ The document was docketed by counsel as a "Response", but captioned as an "Answer". As it is properly construed as an Answer to the Complaint, this Opinion will term it an Answer.

[2]/ Bankruptcy courts have jurisdiction to enter final judgments, both as to dischargeability and the amount of the debt. *See, In re Hart*, __ Fed. Appx. __, 2014 WL 1663029, 2014 U.S. App. LEXIS 7972 (6th Cir. April 28, 2014).

12-03034-jpg Doc 60 FILED 05/08/14 ENTERED 05/08/14 13:02:25 Page 2 of 12

($40,926.10) [hereinafter “the Judgment”]. Complaint, ¶6; Answer of Janet Klausing ¶1.

The parties agree that Janet Klausing paid the sum of Three Hundred Twenty-five Dollars ($325.00) towards the Judgment prior to the filing of the Chapter 7 Petition, “leaving a balance due the estate of $40,601.10". Complaint, ¶7; Answer of Janet Klausing ¶1.

Prior to the filing of the Chapter 7 Petition, Janet Klausing initiated suit in the Court of Common Pleas, Allen County, Ohio, Case No. CV2011-0418, against James D. Pohlman, a duly licensed attorney in the State of Ohio. The Defendant-Debtor Janet Klausing had engaged attorney Pohlman to advise and assist her in fulfilling her duties as Executor of the Estate of Paula Minzing (hereinafter “the Litigation Claim”). Complaint ¶8; Answer of Janet Klausing ¶1.

The Defendant-Debtor Janet Klausing listed the Litigation Claim as an asset in the Chapter 7 Schedules without a determination as to the value or interest of the Bankruptcy Estate. Complaint ¶9; Answer of Janet Klausing ¶1.

The Complaint alleges that “the Judgment is a debt owing by the Defendant, [Janet] Klausing that was incurred by defalcation while acting in her fiduciary capacity as executor of the estate of Paula Minzing.” Complaint ¶11. In addition, the Complaint alleges that “the Judgment is a debt arising under 11 U.S.C. §523(a)(4) as a debt for defalcation while acting in a fiduciary capacity and the Plaintiff is entitled to an order excepting the Debt from discharge pursuant to 11 U.S.C. §523(a)(4).” Complaint ¶12.

In her Answer, Janet Klausing admits “that the debt was incurred while acting in a fiduciary capacity” but denies that the debt “constitutes defalcation while acting in a fiduciary capacity pursuant to 11 USC §523(a)(4)”. Answer of Janet Klausing ¶3.

Thus, the issue in dispute on summary judgment is whether the undisputed facts in this case demonstrate that the Plaintiff-Estate cannot satisfy the legal definition of “defalcation” by a fiduciary under 11 U.S.C. §523(a)(4).

At the time the Complaint was filed on February 21, 2012, the meaning of the term "defalcation" was not settled law on a national basis. In the Sixth Circuit, an "objective recklessness" had been the standard under the precedents of *Carlisle Cashway, Inc. v. Johnson (In re Johnson)*, 691 F.2d 249, 255-256 (6th Cir. 1982) and *In re Patel*, 565 F.3d 963 (6th Cir. 2009). However, on May 13, 2013, the United States Supreme Court issued its decision in *Bullock v. BankChampaign, N.A.*, ___ U.S. ___, 133 S.Ct. 1754, 185 L.Ed.2d 922 (2013), addressing the appropriate legal standard for determining what is a "defalcation" for purposes of Section 523(a)(4).

The *Bullock* decision rejected the Sixth Circuit's "objectively reckless" standard. Instead, the Supreme Court interpreted "defalcation" as requiring a culpable state of mind:

> [W]here the conduct at issue does not involve bad faith, moral turpitude, or other immoral conduct, the term requires an intentional wrong. We include as intentional not only conduct that the fiduciary knows is improper but also reckless conduct of the kind that the criminal law often treats as the equivalent. Thus, we include reckless conduct of the kind set forth in the Model Penal Code. 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.... That risk "must be of such a nature and degree that, considering the nature and purpose of the actor's conduct and the circumstances known to him, its disregard involves a gross deviation from the standard of conduct that a law-abiding person would observe in the actor's situation."

Under the *Bullock* standard, not all breaches of fiduciary duty rise to the level of a "defalcation" under §523(a)(4). *See, In re Pearl*, 502 B.R. 429, 442 (Bankr. E.D. Pa. 2013). Accordingly, although there is a valid state court judgment finding a breach of fiduciary duty by Janet Klausing as executor for the Estate of Paula Minzing, more is required to hold some or all of the Judgment nondischargeable in bankruptcy.

The district court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. §1334(b) as a civil proceeding arising under a case under Title 11. This proceeding has been referred to this court by the district court under its general order of reference. 28 U.S.C. §157(a); General Order 2012-7 of the

12-03034-jpg Doc 60 FILED 05/08/14 ENTERED 05/08/14 13:02:25 Page 4 of 12

United States District Court for the Northern District of Ohio. Proceedings to determine the dischargeability of debts are core proceedings that the court may hear and decide. 28 U.S.C. §157(b)(1) and (b)(2)(F) and (H). For the reasons that follow, Defendant-Debtor's Motion for Summary Judgment will be denied.

Under Rule 56 of the Federal Rules of Civil Procedure, made applicable to this proceeding by Federal Rule of Bankruptcy Procedure 7056, summary judgment is proper only where there is no genuine dispute as to any material fact and the moving party is entitled to judgment as a matter of law. Fed.R.Civ.P. 56(c). In reviewing a motion for summary judgment, however, all reasonable inferences "must be viewed in the light most favorable to the party opposing the motion." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587–88, 106 S.Ct. 1348, 1356, 89 L.Ed.2d 538 (1986). The party moving for summary judgment always bears the initial responsibility of informing the court of the basis for its motion, "and identifying those portions of 'the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits if any' which it believes demonstrate the absence of a genuine issue of material fact." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 106 S.Ct. 2548, 2553, 91 L.Ed.2d 265 (1986). Where the moving party has met its

initial burden, the adverse party "may not rest upon the mere allegations or denials of his pleading but ... must set forth specific facts showing that there is a genuine issue for trial." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S.Ct. 2505, 2510, 91 L.Ed.2d 202 (1986). A genuine issue for trial exists if the evidence is such that a reasonable factfinder could find in favor of the nonmoving party. *Id*.

The Movant has attached certain documents to Defendant's Motion for Summary Judgment with Memorandum in Support. Those documents are: 1) the November 17, 2010 Judgment Entry of the Court of Common Pleas of Van Wert County Probate Division, entered by the Honorable Rex T. Fortney; 2) the Amended Complaint with Jury Demand Endorsed Hereon in Janet Klausing v. James D. Pohlman, Esq., Case No. 2011 CV 2011 0418, filed in the Common Pleas Court of Allen County, Ohio appearing to bear

12-03034-jpg Doc 60 FILED 05/08/14 ENTERED 05/08/14 13:02:25 Page 5 of 12

a file stamp of October 26, 2011; 3) the Answer of Defendant James D. Pohlman, Esquire to the Plaintiff's Amended Complaint that states it was served on October 31, 2011. None of these court documents were certified copies. *See*, Federal Rule of Evidence 902(4).

Also attached to the Motion for Summary Judgment was a copy of the Affidavit of James D. Pohlman that was apparently prepared for the litigation in Allen County Common Pleas Case No. CV 2011 0418. Paragraph 12 of the Affidavit of James D. Pohlman references Exhibits A and B, which are not attached.

Filed separately on the docket were Exhibit E, the Deposition of James D. Pohlman [Doc. #52] and Exhibit F, the Deposition of Janet Klausing[3] [Doc. #53].

An Affidavit of Anthony J. Sarno was filed on behalf of the Estate of Paul Minzing. [Doc. #56.]

The Memorandum in Opposition to Defendant's Motion for Summary Judgment discusses the two depositions filed with the Motion for Summary Judgment, stating in pertinent part: "If there is any procedural impediment to such testimony being offered into evidence as support for the motion (both depositions were taken in state court proceedings and originals, even if they may be properly considered by the court, have not been filed in this action) movant has apparently waived any objection to the use of such deposition testimony. Likewise, plaintiff waives any objection to the use of such testimony." [Doc. #57, page 6, footnote 2]. *See also*, Fed.R.Civ.P. 56(c), Fed.R.Bankr.P. 7056.

The Defendant's Motion for Summary Judgment first asserts that "Defendant's actions as Executrix of the Estate of Paula Minzing and the debt arising from the exception to account were not defalcation under 11 USC 523(a)(4)." The second argument is based upon the decision of the Probate Court somehow collaterally estopping the bankruptcy court from finding a "defalcation" by the Defendant-Debtor.

---

[3]/ The front page of the Deposition of Janet Klausing states it was taken on "the 24th day of March, 2002" - which appears to be typographical error. The correct date appears to be March 24, 2010, based on the Certificate of Deposition and the time line of events in this case.

The first argument on behalf of the Defendant emphasizes the higher standard of intent required under *Bullock*: "[C]onduct that the fiduciary knows is improper but also reckless conduct of the kind that the criminal law often treats as the equivalent." *Bullock v. BankChampaign, N.A.*, 133 S.Ct. 1754, 1759 (2013). The Defendant points to evidence that she was not an attorney, did not have actual knowledge of the standard applied by the Probate Court, and relied on the advice of counsel. Defendant's Motion for Summary Judgment, at pages 6-8 [Doc. #51].

Here, the facts must be viewed in the light most favorable to the non-moving party, the Plaintiff, Douglas Daley, Special Administrator for and on behalf of the Estate of Paula Minzing (hereinafter "the Estate").

The Plaintiff-Estate cites to sections of documents in the record that, if construed in the light most favorably to the Plaintiff, would permit the entry of judgment in its favor. *See*, Memorandum in Opposition to Defendant's Motion for Summary Judgment, at pages 7-10 [Doc. #57].

The Plaintiff points to the Defendant's receipt of $130,000 from the Estate of Paula Minzing, the billing of the Minzing Estate for an extraordinary number of hours of work that resulted in little or no benefit to the estate, and statements by the Defendant-Debtor that she did not consider whether her work was reasonable in cost compared to other options. Further, the Defendant did not seek Probate Court approval to hire herself, or her husband, and paid herself and her husband for cleaning and office work out of Estate funds on a weekly or biweekly basis prior to the filing of the Final Account. The hours that Defendant was compensated for were not well documented. While Defendant was not an attorney, she worked as an assistant for an attorney (Paula Minzing) who had been involved in hundreds of estates over the 17 years she had worked for the deceased. Moreover, there is evidence that the Defendant often had conversations with attorney Pohlman's secretary, rather than attorney Pohlman, and that they deferred to Defendant's view on some issues because of her experience. *See generally, In re Fitzgerald*, 2014 WL

1117090 at *16 - *17, 2014 Bankr. LEXIS 1087 at *17 - *18 (Bankr. N.D. Ohio March 20, 2014)(discussing the fiduciary's experience as a factor in nondischargeability proceedings after *Bullock*).

The Affidavit of Anthony J. Sarno avers that offers were made to the Defendant to assist, without charge, in preparing items of personal property for auction, and those offers were refused. Affidavit of Anthony J. Sarno, ¶8 [Doc. #56]. The Probate Court Judgment held that an an Estate asset (a conference table) worth $125 had been kept by the Defendant-Debtor without any payment to the Estate.

In short, there are genuine issues of material fact in this case as to whether the Defendant's actions as a fiduciary for the Estate of Paula Minzing were a "defalcation". Viewing the facts most favorably to the non-moving party, a reasonable fact finder could find in favor of the Plaintiff-Estate.

The second argument of the Defendant is that under the doctrines of res judicata and collateral estoppel, the Judgment of the Probate Court acts to prevent a finding of nondischargeability, either because the Probate Court did not find the required state of mind for a "defalcation" under *Bullock*, or because the findings of fact in the Probate Court decision preclude a finding of a "defalcation".

The Supreme Court has addressed these issues in previous cases:

> At the outset, we distinguish between the standard of proof that a creditor must satisfy in order to establish a valid claim against a bankrupt estate and the standard that a creditor who has established a valid claim must still satisfy in order to avoid dischargeability. The validity of a creditor's claim is determined by rules of state law. *See Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 161, 67 S.Ct. 237, 239, 91 L.Ed. 162 1946). Since 1970, however, the issue of nondischargeability has been a matter of federal law governed by the terms of the Bankruptcy Code. *See Brown v. Felsen*, 442 U.S. 127, 129-130, 136, 99 S.Ct. 2205, 2208-2209, 2211, 60 L.Ed.2d 767 (1979).

Grogan v. Garner, 498 U.S. 279, 283-4, 111 S.Ct. 654, 657-8, (1991)(footnotes omitted).

The Probate Court's Judgment, which was entered after a contested hearing, has determined the amount of the claim against the Defendant-Debtor for breach of her fiduciary duty as executor of the Estate of Paula Minzing. *See, In re Springhart*, 450 B.R. 725 (Bankr. S.D. Ohio 2011); *In re Phillips*, 434 B.R.

475, 485 (6th Cir. BAP 2010)(state court judgment preclusive on issues of damages and liability); *In re Langeslag*, 366 B.R. 51, 56–57 (Bankr.D.Minn.2007). However, res judicata is generally not applicable to claims and defenses that concern the dischargeability of a claim previously reduced to judgment in a state court action. *See*, *In re Kunkle*, 462 B.R. 914, 922 (Bankr. N.D. Ga. 2011); *In re Tague*, 137 B.R. 495, 503 (Bankr. D. Colo. 1991).

Facing a similar issue in a pre-*Bullock* defalcation case, Judge Speer stated:

> Concerning a prior claim, the Supreme Court has held that res judicata does not apply to bankruptcy courts in their determinations of nondischargeability. *Brown v. Felsen*, 442 U.S. 127, 138–39, 99 S.Ct. 2205, 60 L.Ed.2d 767 (1979). The Court in *Brown* reasoned that the petition for bankruptcy is essentially the offering of a "new defense" to the judgment entered against the debtor and "the mere fact that a conscientious creditor has previously reduced his claim to judgment should not bar further inquiry into the true nature of the debt." *Id*. at 133, 138, 99 S.Ct. 2205. The Court then went on to further explain that res judicata does not apply to claims of dischargeability because bankruptcy courts have "exclusive jurisdiction" over claims of dischargeability. *Id*. at 136, 99 S.Ct. 2205, *citing* S.Rep. No. 91–1173, p. 2 (1970).

In re Kelley, 360 B.R. 753, 757 (Bankr. N.D. Ohio 2006).

The *Kelley* opinion continued: "Defendant argues that because the claims were not litigated in the state court, this Court is barred from deciding the matter, an argument completely contrary to the doctrine's fundamental tenet: that the issue to be precluded have been previously litigated. Accordingly, the Defendant's arguments regarding both the preclusionary doctrines of res judicata and collateral estoppel have no merit." *Id*., at 758.

More specifically, the issue in this case is whether the breach of fiduciary duty by Defendant found by the Probate Court rises to the level of being a "defalcation" under the *Bullock* standard. The Defendant's stated arguments focus on issue preclusion. Because the Van Wert County Probate Court Judgment was entered by a state court, Ohio law governs the application of collateral estoppel in this dischargeability proceeding. *See*, 28 U.S.C. §1738; *Marrese v. Am. Acad. of Orthopaedic Surgeons*, 470 U.S. 373, 380, 105

S.Ct. 1327, 1332, 84 L.Ed.2d 274 (1985)("This statute directs a federal court to refer to the preclusion law of the State in which judgment was rendered."); *Corzin v. Fordu (In re Fordu)*, 201 F.3d 693, 703 (6th Cir.1999)("The full faith and credit statute, 28 U.S.C. §1738, requires a federal court to accord a state court judgment the same preclusive effect that the judgment would have in a state court.").

Under Ohio law, there are four elements to the application of issue preclusion: "(1) The party against whom estoppel is sought was a party or in privity with a party to the prior action; (2) There was a final judgment on the merits in the previous case after a full and fair opportunity to litigate the issue; (3) The issue must have been admitted or actually tried and decided and must be necessary to the final judgment; and (4) The issue must have been identical to the issue involved in the prior suit." *Cashelmara Villas Ltd. Partnership v. DiBenedetto*, 87 Ohio App.3d 809, 814 (1993); *Sill v. Sweeney (In re Sweeney)*, 276 B.R. 186, 189 (B.A.P. 6th Cir.2002).

While elements one and two are not in issue, Defendant's Motion for Summary Judgment does not support a finding that elements three or four have been demonstrated. The party asserting issue preclusion carries the burden of pleading and proving its requirements by a preponderance of the evidence. *See*, *Am. Fiber Sys., Inc. v. Levin*, 125 Ohio St.3d 374, 378 (2010)("The burden of pleading and proving the identity of the issues currently presented and the issues previously decided rests on the party asserting the estoppel."); *see also*, *In re Monas*, 309 B.R. 302, 306 (Bankr.N.D.Ohio 2004).

The issue of whether the breach of fiduciary duty by the Defendant rose to the level of a "defalcation" was never "tried and decided", and was not necessary to the Judgment issued by the Probate Court.

In the Probate Court decision, the fact that Janet Klausing failed to seek court approval prior to employing herself and her husband, was held to be sufficient to warrant denial of all compensation: "The logical conclusion from ORC §§2113.36, 2113.30 and 2109.44 is that the executor is required to obtain

court approval to "hire herself" if she is paying herself for services over and above the executor's fees allowed by Ohio law. The heirs deserve notice and the Probate Court has the duty and the obligation to oversee the requests to insure the extraordinary fee are needed as over and above normal executor's fees and to insure the amounts paid are appropriate. . . . [F]ailure of the executor to make application for approval, and then the objection of the heirs, requires the court to disallow all fees over and above the statutory executor fees except for reimbursement for items or postage bought for the estate." *Matter of the Estate of Paula Minzing*, Case No. 20071198, November 17, 2010 Judgment Entry of the Probate Court, at pages 10 - 11, attached as Exhibit A to Defendant's Motion for Summary Judgment [Doc. #51].

In contrast, the issue in this case - whether there was a "defalcation" under the *Bullock* standard - involves a different legal standard than the breach of fiduciary duty found by the Probate Court. Moreover, the *Bullock* decision, establishing a heightened scienter requirement for nondischargeability, had not been issued at the time the Probate Court Judgment was entered.

Where additional or different elements of proof are required for a finding of nondischargeability under Section 523(a), debtors have not been shielded by a prior finding of liability on a state law claim under a different standard of proof. For example, where a finding of breach of contract resulted in a judgment for the creditor, that creditor was not prohibited from seeking to except that judgment from discharge based upon a claim of defalcation by a fiduciary under §523(a)(4). *See*, *In re Kunkle*, 462 B.R. 914 (Bankr. N.D. Ga. 2011)(decided under a pre-*Bullock* defalcation standard.).

In this case, the defalcation issue was not litigated in the Probate Court, nor were there any factual findings in the state court Judgment that would either require, or preclude, a finding of nondischargeability under §523(a)(4).

THEREFORE, for the foregoing reasons, good cause appearing,

IT IS ORDERED that Defendant-Debtor's Motion for Summary Judgment [Doc. #51] be, and is

hereby, **DENIED**.

IT IS FURTHER ORDERED that this matter is set for further pre-trial on Monday, June 2, 2014 at 3:30 p.m.