

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE: *
*
EDWIN D. BAILEY and *
JAMIE S. BAILEY, * CASE NUMBER 05-41609
*
Debtors. *
*

*
MERCHANTS EXPRESS MONEY ORDER *
COMPANY, *
* ADVERSARY NUMBER 05-4077
*
Plaintiff, *
*
vs. *
*
EDWIN D. BAILEY and *
JAMIE S. BAILEY, * HONORABLE KAY WOODS
*
Defendants. *
*

M E M O R A N D U M O P I N I O N

This cause is before the Court on a Motion for Judgment on the Pleadings (the "Motion") filed by Plaintiff Merchants Express Money Order Company ("Plaintiff"). After an extension of time to file a response and a denial of a second extension, Edwin Bailey and Jamie Bailey ("Debtors") filed a Motion to File a Response Instanter ("Debtors' Response"), which this Court granted. Because this is a motion on the pleadings, this Court disregarded all "matters outside the pleadings" when reviewing the Motion. See FED. R. CIV. P. 12(c).

This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to

28 U.S.C. § 157(b)(2)(I). The following constitutes the Court's findings of fact and conclusions of law pursuant to FED. R. BANKR. P. 7052.

As set forth below, this Court grants the Motion, in part.

STANDARD OF REVIEW

Judgment on the pleadings is governed by FED. R. CIV. P. 12(c) which is made applicable to this proceeding pursuant to FED. R. BANKR. P. 7012. Rule 7012 provides, in pertinent part:

After the pleadings are closed but within such a time as not to delay the trial, any party may move for judgment on the pleadings.

Judgment on the pleadings is proper when no material issue of fact exists and the party is entitled to judgment as a matter of law. *Paskvan v. Cleveland Civil Service Commission*, 946 F.2d 1233, 1235 (6th Cir. 1991). In determining if a material issue of fact exists, the Court must construe the complaint in the light most favorable to the non-moving party, *Estill County Board of Education v. Zurich Insurance Co.*, 84 Fed. Appx. 516 (6th Cir. 2003), and take all well-pleaded material of the non-moving party as true. *United States v. Moriarty*, 8 F.3d 329, 332 (6th Cir. 1993) (quoting *Southern Ohio Bank v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 479 F.2d 478, 480 (6th Cir. 1973)). However, the Court is not required to accept "sweeping unwarranted averments of fact," *Official Committee of Unsecured Creditors v. Austin Financial Services, Inc. (In re KDI Holdings, Inc.)*, 277 B.R. 493, 502 (Bankr. S.D. N.Y. 1999) (quoting *Haynesworth v. Miller*, 820 F.2d 1245, 1254 (D.C. Cir. 1987)), or "conclusions of law or unwarranted deduction." *In re KDI Holdings*

Inc., 277 B.R. at 502 (quoting *First Nationwide Bank v. Gelt Funding Corp.*, 27 F.3d 763, 771 (2d Cir. 1994)). Judgment on the pleadings may only be granted if the moving party is clearly entitled to judgment. *Southern Bank of Ohio*, 479 F.2d at 480.

FACTS

On March 28, 2005, Debtors filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code. Subsequently, on April 7, 2005, Plaintiff initiated an adversary proceeding against Debtors by filing a complaint (the "Complaint").¹ On August 4, 2005, after numerous extensions, Debtors filed an answer (the "Answer"). The following facts were articulated in the Complaint and admitted in the Answer.

On or about May 21, 1998, Debtors entered into a Personal Money Trust Agreement (the "Agreement") with Plaintiff on behalf of Convenient Food Mart, which was also signed in their individual capacities.² (Complaint at ¶ 4; Answer at ¶ 1; Agreement at p. 3.) Pursuant to the Agreement, Debtors agreed to: (i) act as an agent for Plaintiff for the sale of Plaintiff's money orders (*Id.*); (ii) act as trustees to "receive and hold in trust for [Plaintiff] all blank money orders delivered to [Debtors] by [Plaintiff] and all

¹The Complaint references several exhibits, including the Note, as Exhibit 3. The Complaint was filed without any exhibits attached, but on April 8, 2005, Plaintiff filed the Exhibits, which were docketed as "Exhibit/Witness List." The Exhibits were filed of record the day after the Complaint was filed. The filed exhibits matched the referenced exhibits in the Complaint. Debtors have not raised any issue concerning whether the exhibits were incorporated into and made a part of the Complaint. As a consequence, this Court finds that the exhibits docketed at Docket No. 5 are part of the Complaint.

²Debtor Edwin Bailey signed the Agreement as President of Convenient Foodmart; however, both Debtors signed the note individually guaranteeing the Agreement. (Agreement at p. 3.)

money received by [Debtors] from the sale of money orders, including without limitation the money order fees established by [Plaintiff] from time to time ("trust funds")" (Complaint at ¶ 5; Answer at ¶ 1; Agreement at ¶ 2); (iii) "hold the trust funds separate and apart from the other funds of [Debtors]" (*Id.*); (iv) make full payment to Plaintiff for Plaintiff's money orders sold by Debtors (Complaint at ¶ 7; Answer at ¶ 1; Agreement at ¶ 9A.); and (v) reimburse Plaintiff for all costs of collection, including interest, fees and attorney fees in enforcing the Agreement (Complaint at ¶ 8; Answer at ¶ 1).

From May 1998 through January 2002, Debtors co-mingled Plaintiff's funds held in an express trust with their own funds held in a National City Bank account. (Answer at ¶ 7.) Plaintiff monitored the aforementioned National City Bank account and electronically withdrew money owed to it based on the Agreement. (Answer at ¶ 7.)

Plaintiff is a creditor of Debtors due to Debtors' failure and refusal to pay Plaintiff Seventeen Thousand Six Hundred Sixty-Three and 22/100 Dollars (\$17,663.22) plus costs of collection, attorney's fees and interest due at the rate of 18% from January 27, 2002, per the judgment in Trumbull County Common Pleas Court Case No. 2002 CV 780 obtained against Debtors due to Debtors' breach of the Agreement (the "Judgment"). (Complaint at ¶ 2; Answer at ¶ 1.) Debtors contend that they have "made one or more payment on said Judgment . . . in an amount not less than \$200.00." (Answer at ¶ 6.) Debtors have not made any other payments on the Judgment. (Complaint

at ¶¶ 2, 10, 16; Answer at ¶ 1.) Accordingly, there is no genuine issue that Plaintiff is a creditor of Debtors for at least Seventeen Thousand Four Hundred Sixty-Three and 22/100 Dollars (\$17,463.22) (*i.e.*, the Judgment amount less \$200.00).

DISCUSSION

Section 541 of the Bankruptcy Code defines property of the estate. 11 U.S.C. § 541. Property of the estate includes "all legal and equitable interests of the debtor in property at the commencement of the case." 11 U.S.C. § 541(a)(1). Thus, the Bankruptcy Code embraces the distinction between legal and equitable interests in property. In that regard, Section 541 of the Bankruptcy Code provides:

Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest . . . becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that debtor does not hold.

11 U.S.C. § 541(d). Accordingly, the Bankruptcy Code specifies that a debtor's bankruptcy estate does not include property held in trust for another. *Ohio Farmers Insurance Co. v. Hughes-Bechtol, Inc.*, 249 B.R. 735, 740 (S.D. Ohio 1998); See *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 205 n.10 (1983) (Providing in dicta, "We note only that Congress plainly excluded [from debtor's estate] property of others held by the debtor in trust at the time of the filing of the petition").

Furthermore, the nature and extent of a debtor's property interest is determined by state law in that Congress decided to leave "the determination of property rights in the assets of a bankrupt's estate to state law." *Butner v. United States*, 440 U.S. 49, 54 (1979). Therefore, the Court must look to state law to determine whether a trust was created.

Under Ohio law, an express trust requires (i) a manifestation of intent, either written or oral, to create a trust, (ii) a trust corpus and (iii) a fiduciary relationship between the trustee and a beneficiary. *Indiana Lumbermens Mutual Insurance Co., Inc. v. Construction Alternatives, Inc. (In re Construction Alternatives Inc.)*, 2 F.3d. 670, 677 (6th Cir. 1993); *Ohio Farmers Insurance Co.*, 249 B.R. at 741.

It is a well-settled principal of law in this and other jurisdictions that if one person pays money to another it depends upon the manifested intention of the parties whether a trust or a debt is created. If the intention is that the money shall be kept or used as a separate fund for the benefit of the payor, or a third person, a trust is created. If the intention is that the person receiving the money shall have the unrestricted use thereof, being liable to pay a similar amount whether with or without the interest to the payor or to a third person, a debt is created. The intention of the parties will be ascertained by a consideration of their words and conduct in light of the surrounding circumstances.

Federal Insurance Co. v. Fifth Third Bank, 867 F.2d 330, 333 (6th Cir. 1989) (quoting *The Guardian Trust Co. v. Kirby*, 50 Ohio App. 539, 543 (1935)).

Once a trust relationship is established, the beneficiary must identify the trust fund and the property of the estate, and if such fund or property has been co-mingled with the debtor's property, the beneficiary must trace the trust property. *Amedisys, Inc. v. JP Morgan Chase Manhattan Bank (In re National Century Financial Enterprises, Inc.)*, 310 B.R. 580, 599 (S.D. Ohio 2004).

The situation frequently occurs where the trust funds have been traced into a general bank account of the debtor. The following general principals have been applied. The bankruptcy court will follow the trust fund and decree restitution where the amount of the deposit has at all times since the intermingling of funds equaled or exceeded the amount of the trust fund. But where, after the appropriation and mingling, all of the moneys are withdrawn, the equity of the cestui is lost, although moneys from other sources are subsequently deposited in the same account. In the intermediate case where the account is reduced by a smaller sum than the trust fund, the latter must be regarded as dissipated, except as to the balance, and funds subsequently added from other sources cannot be subject to the equitable claim of the cestui que trust. If new money is deposited before the balance is reduced, the reduction should be considered to be from the new money and not from the monies held in trust. This analysis may be referred to as the lowest intermediate balance test.

In re National Century Financial Enterprises, Inc., 310 B.R. at 600)
(citations omitted).

Therefore, property held in trust is not property of the estate because the debtor does not have an equitable interest in such property. The Court must follow the lowest intermediate balance test to determine what constitutes trust property (and, thus, is not property of the estate). Accordingly, property of the estate does

not include (i) moneys held in trust if the amount of deposit at all times exceeded the amount of the trust and (ii) the balance of the moneys held in the account if the amount of deposit falls below the amount of the trust. In other words, any amount that is dissipated is no longer held in trust and any claim for such dissipated amount becomes a general unsecured claim against the bankruptcy estate.

Debtors admit they held funds for Plaintiff in an express trust. (Answer at ¶ 5.) Even if, *arguendo*, Debtors did not admit to holding the proceeds of the money orders in trust, the Agreement created an express trust under Ohio law. First, the parties manifested the intent to create an express trust in the Agreement. The Agreement states, "[Debtors] shall receive and hold in trust . . . all money received by [Debtors] from the sale of money orders, including without limitation the money order fees established by [Plaintiff] from time to time ('trust funds')." (Complaint at ¶ 4; Answer at ¶ 1; Agreement at ¶ 2.) The trust corpus, involved in this dispute, consists of the funds Plaintiff earned from Debtors' sale of the money orders in the amount of Seventeen Thousand Six Hundred Sixty-Three and 22/100 Dollars (\$17,663.22) which was deposited in Debtors' National City Bank account. (Complaint at ¶¶ 2, 10; Answer at ¶ 1.) Finally, a fiduciary relationship existed between the Plaintiff and the Debtors pursuant to the Agreement, which delegated a fiduciary duty to Debtors for the benefit of the Plaintiff. (Agreement at ¶¶ 1, 2, 6(D).) As a result of the

aforementioned, the Agreement satisfies the requirements of an express trust.

Accordingly, Debtors admit that they held money in an express trust for the benefit of the Plaintiff. Even if Debtors did not admit to the express trust, the Agreement satisfied the elements of an express trust.

The amount in question (Seventeen Thousand Six Hundred Sixty-Three and 22/100 Dollars (\$17,663.22)) was held in trust for Plaintiff's benefit in an account at National City Bank. (Complaint at ¶¶ 2, 10; Answer at ¶ 1.) Plaintiff seeks to have its debt declared non-dischargeable; however, since the moneys that are the subject of Plaintiff's Complaint were held in trust by Debtors, those moneys are not property of Debtors' estate. As a consequence, the relief Plaintiff seeks, *i.e.*, an order of non-dischargability pursuant to Sections 11 U.S.C. §§ 523(a)(2)(A), 523(a)(4), and 523(a)(6) of the Bankruptcy Code, is not appropriate under these facts.³

The moneys in question was allegedly co-mingled with Debtors' own funds. As a consequence, to the extent, if any, that the trust amount was dissipated, any claim for such dissipated portion of the trust became a general unsecured debt. A determination of whether there was any dissipation would require the Court to apply the lowest intermediate balance test. That issue cannot be addressed by the Court at this time because there are no facts or

³Debtors deny that there was any fraud or conversion of the trust. (Answer at ¶ 8.)

allegations concerning the amount of the funds that Debtors held in trust.

CONCLUSION

In viewing the pleadings in the light most favorable to Debtors, the Court has concluded the following:

Debtors held moneys in trust for the benefit of Plaintiff in Debtors' National City Bank account. Money held in trust by Debtors for the benefit of Plaintiff is not property of Debtors' estate. Consequently, the Complaint is dismissed to the extent it seeks to determine the non-dischargeability of debts relating to the aforesaid moneys held in trust.

To the extent Plaintiff holds or may hold a general unsecured claim against the Debtors' bankruptcy estate, based upon dissipation of trust moneys, that issue has not been properly pled before this Court. As a consequence, this Court cannot make a determination whether the trust funds were dissipated and, if so, to what extent.

Based upon the pleadings, this Court finds that Plaintiff is entitled to judgment that Debtors held moneys in trust for Plaintiff's benefit, pursuant to the Agreement. The relief requested by Plaintiff - *i.e.*, an order that the debt is not dischargeable - is not appropriate because funds held in trust are not property of the estate. Accordingly, this Court grants the motion in part. The Motion is denied to the extent it seeks an order of non-dischargeability, but granted to the extent that the pleadings establish that Debtors held moneys in trust for the benefit of

Plaintiff. This Court orders the parties to appear on February 21, 2006, at 9:45 a.m., the date previously docketed as the final pre-trial conference, for a status conference.

An appropriate order will follow.

HONORABLE KAY WOODS
UNITED STATES BANKRUPTCY JUDGE

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O R D E R

For the reasons set forth in this Court's Memorandum Opinion entered this date, the Court finds that Plaintiff is entitled to judgment that Debtors held moneys in trust for Plaintiff's benefit, pursuant to the Agreement. The relief requested by Plaintiff - i.e., an order that the debt is not dischargeable - is not appropriate because funds held in trust are not property of the estate. Accordingly, this Court grants the motion in part. The Motion is denied to the extent it seeks an order of non-dischargeability, but granted to the extent that the pleadings establish that Debtors held moneys in trust for the benefit of

Plaintiff. This Court orders the parties to appear on February 21, 2006, at 9:45 a.m., the date previously docketed as the final pre-trial conference, for a status conference.

IT IS SO ORDERED.

**HONORABLE KAY WOODS
UNITED STATES BANKRUPTCY JUDGE**