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Using Non-Dischargeability As A Remedy Against Financial Abusers Of The Elderly

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Bankruptcy Judge Donald Steckroth, recently handed down an unpublished decision that declared nondischargeable a debt for money taken by a caregiver-daughter from her elderly mother. *Buttimore as Executor for the Estate of Helen C. Buttimore, Plaintiff v. Carole Wolke.* Defendant Adversary Case Number 07-01756(DHS). (Bankr. D.N.J. Feb. 13, 2008). The decision interpreted Bankruptcy Code §523(a)(4), which renders nondischargeable a debt owed for the return of funds taken from an elderly parent's assets without consent. The decision is noteworthy because there was not previous state court ruling finding the daughter's actions wrongful.

Carole Wolke (debtor) was a registered nurse for 25 years. Her Mother, an elderly widow, moved in with her in 1997. Mom's health declined and Wolke became her caretaker. Until August of 2005, the debtor was a joint holder of two of her mother's bank accounts, which were used to pay her Mother's expenses. Between February 2003 and July 2005, however, the debtor appropriated more than $400,000 of her Mother's money for her personal use, including transferring some to one of her friends for "investment" purposes. The debtor admitted the withdrawals were without her mother's consent.

In August 2005, when confronted about the use of her Mother's money, the debtor wrote a letter to her brother, who eventually became the estate's executor, in which she admitted taking the money. In the letter, the debtor equated her actions to receiving her share of Mom's estate "up front." Shortly afterwards, Mom passed away. Acknowledging her actions, the debtor signed an affidavit and disclaimer, waiving any right to distribution from Mom's estate. In July 2006, the debtor's brother, as executor Mom's estate sued the debtor in state court alleging fraud, breach of fiduciary duty and conversion.

Before the action in state court was heard, the debtor filed a chapter 13 bankruptcy case, which was later converted to chapter 7. On June 7, 2007, the executor/brother filed an adversary proceeding against the debtor, alleging that the $400,000 debt owed to the estate was nondischargeable under 11 U.S.C. 523(a)(4), which renders nondischargeable debts "for fraud or defalcation while acting in a fiduciary capacity, embezzlement or larceny." The estate moved for

summary judgment, asserting that there was no material issue of fact as to the §523(a)(4) requirement of defalcation while in a fiduciary capacity because of the debtor's prior admissions of wrongdoing.

In response, the debtor claimed that she had executed the affidavit and disclaimer under duress. She averred that her use of $400,000 of her mother's money was justified because, she alone, cared for her mother for eight years without help from her siblings. She also alleged that she invested her mother's money with the intention of receiving a favorable return.

The court, interpreting the "defalcation while acting in a fiduciary capacity" prong, of Code §523(a)(4), noted that the plaintiff must prove that:

(1) there was a pre-existing fiduciary relationship between the debtor and the creditor;
(2) debtor acted in violation of that relationship and
(3) the creditor suffered economic loss as a consequence.

See Pa. Lawyers Fund for Client Security v. Baillie (In re Baillie), 368 B.R. 458, 469(Bankr. W.D. Pa 2007) (citing *Commonwealth Land Title Co. v. Blaszak (In re Blaszak),* 397 F. 3d 386, 390 (6th Cir. 2005)).

The court found the third element clear: the estate suffered a loss of $400,000 due to the defendant's actions. As to the first two elements, the court noted that the "crux of this adversary proceeding is whether a fiduciary relationship existed between the debtor and her mother and whether the debtor's conduct constituted a defalcation."

Fiduciary Duty

Traditionally, a fiduciary is someone who is in a relationship of confidence, trust and good faith with some one else. Bankruptcy courts find this definition to be too broad for the purposes of the bankruptcy laws. See *Mercedes-Benz Credit Corp. v. Carretta (In re Carretta),* 219 B.R. 66, 69 (Bankr. D.N.J. 1998). Bankruptcy courts limit the definition of a fiduciary for §523(a) (4) purposes to situations where the fiduciary debtor holds an express or technical trust on behalf of

beneficiary/creditor. See *Int'l Fidelity Ins. Co. v. Marques (In re Marques)*, 358 B.R. 188, 194 (Bankr. E.D. Pa. 2006) (citing *Harris v. Dawley (In re Dawley)*, 312 B.R. 765, 777 (Bankr. E.D. Pa. 2004)). Further, the fiduciary relationship, "[M]ust have existed prior to or independent of the particular transaction from which the debt arose. The debt must be due to the fiduciary acting in that capacity." (citing *Pa. Manufacturers' Assoc. In. Co. v. Desiderio (In re Desiderio)*, 213 B.R. 99, 102-03 (Bankr. E.D. Pa. 1997)); *see also In re Carretta*, 219 B.R. at 69) ("The Trustee's duties must be independent of any contractual obligation between the parties and must be imposed prior to, rather than by virtue of, any claim of misappropriation"). Judge Steckroth noted that "implied or constructive trusts and trusts ex maleficio do not impose fiduciary relationships within the context of §523(a)(4)."

State law has bearing in determining whether an express or technical trust relation exists *See State of New Jersey v. Kaczynski (In re Kaczynski)*, 188 B.R. 770, 773 (Bankr. D.N.J.1995). In *Kaczynski*, the court noted that an express trust requires, "(1) a declaration of trust; (2) a clearly defined trust res and (3) an intent to create a trust relationship." *See also Windsor v. Librandi*, 183 B.R. 379, 382 (M.D. Pa. 1995). A trust can be created in writing, orally or based on circumstantial evidence. *Mugno v. Casale*, No. 96-6228, 1997 U.S. Dist. LEXIS 3867, at *24-25 (E.D. Pa. 1997). Technical trusts are not as clearly defined. Instead, it is one that arises out of the state statute or by operation of common law. *See In re Kaczynski*, 188 B.R. at 774; *In re Librandi*, 183 B.R. at 383.

Unlike this case, in each of the cases cited above, there was already a state court judgment against the defendant when the bankruptcy was filed. The ruling in this case is noteworthy in that the court did not require the state court to render a judgment determining that the debt was a violation of trust imposed under fiduciary duty and/or there has been a finding of defalcation.

When an elderly person turns over control of money or other property to another by creating a joint bank account, an entrustment of funds exist. The requisite elements of an express (but unwritten) trust existed between the late Mrs. Buttimore and the debtor, based on the circumstances and their actions. For this

reason, by New Jersey law, Judge Steckroth found that a "fiduciary relationship exists between Helen Buttimore and the defendant."

Violation of Fiduciary Duty

The Code does not define defalcation. (*See Chao v. Rizzi*, No. 06-711, 2007 U.S. Dist. LEXIS 57773, at *7 (W.D. Pa. August 8, 2007); *Silver Car Ctr. V. Parks*, No. 05-37154, 2007 Bankr. LEXIS 2373, at *51 (Bankr. D.N.J. July 10, 2007))

Judge Steckroth noted that while affirmative misconduct was necessary, bad intent was not required to establish defalcation. Defalcation is evaluated by an objective standard and no element of intent or bad faith need be shown. *Brown v. Colangelo (In re Colangelo)*, 206 B.R. 78, 85 (Bankr. M.D. Pa. 1996). The judge in *Wolke* noted that there was a clear showing that the debtor used money belonging to her mother without her mother's knowledge or consent. The debt and resulting liability flowed from that action. Because there was no consent and because the monies were used for a purpose other than Mom's care, the court determined that affirmative misconduct existed. The court did not find fraudulent or criminal intent, but still pointed out "this court has no doubt the defendant's conduct constitutes a defalcation under §523(a)(4)." *Buttimore, supra, at* 15.

Judge Steckroth drew a distinction between pre-existing trust relationships created by an express trust or by a trust implied by law (such as the creation of a joint bank account between the trustee and beneficiary) and trusts which are imposed by courts as a result of an actual, wrongful taking. For purposes of §523(a)(4), the trust relationship must predate the wrongful conduct. Significantly, if there was a preexisting trust, the funds taken may never have become property of the debtor's estate. As a result, they are not subject to the claims of competing creditors of the same or higher priority.

<u>Undue influence:</u>

New Jersey law addressing undue influence is important in considering whether or not there has been a pre-existing relationship of confidence and trust. It is possible that an elderly person has been taken advantage of and persuaded or manipulated into signing a document creating a trust or a fiduciary relationship.

New Jersey Courts think about undue influence as a form of fraud. Undue influence has been defined as "mental, moral or physical exertion which destroyed the free agency of a testator (or settlor) by preventing the testator from following the dictates of his own mind and will and accepting those of another," *See In the Matter of Niles Trust*, 176 N.J. 282 at page 299 823 A.2d 1 (NJ 2003) and *Haynes v. First National State Bank of New Jersey*, 87 N.J. 163, 176 (1981), 432 A.2d 890 (NJ 1981). While these cases relate to will contests, they explore the concept of undue influence over an elderly person. In litigating an adversary case with facts similar to those in *Wolke*, these principles help to prove existence of a trust implied by operation of law.

Confidential relationship:

In analyzing facts to determine whether a trust has been created, it is useful to see if there is a "confidential relationship" between the elderly person and the person against whom the judicial imposition of an implied trust is sought. *Haynes, supra* addresses "when trust is reposed by reason of a testator's weakness or dependence although the parties occupied relations in which reliance is naturally inspired or actually exists." 87 N.J. at 176, 432 A.2d 890.

Suspicious circumstances:

New Jersey courts also look to what are called "suspicious circumstances" to create a presumption of undue or improper influence. The suspicious circumstance could include where the elderly person is excluded from contact from other family members or with friends. Other circumstances should also be considered. (*See In Re Blakes Will*, 21 N.J. 50,57(1955), 120 A.2d 745 (1956).

Conclusion

The elderly can be attractive targets. Persons over the age of 50 are said to control over 70 percent of the nation's wealth. See National Committee for the Prevention of Elder Abuse website at www.preventelderabuse.org/elderabuse/fin_abuse.html (an excellent website for basic guidelines on the prevalence and indicators of financial abuse of the elderly). Financial abuse of the elderly can span a broad spectrum of conduct. This includes

taking money or property without permission. Very often the perpetrators are caretakers who stand to inherit from the victim and feel justified in taking what they believe is almost or rightfully theirs. They may also feel entitled to an older person's funds if they have been the primary caretaker and resent others who may inherit from the elderly person without having participated in the caregiving. Or, they may view their actions as justifiably getting what will eventually come to them, like the debtor in Wolke. Economic abuse of the elderly is wrong. The ability to prevent the discharge of debts arising out of the financial abuse of older persons is a powerful tool for justice.