Honorable Mike K. Nakagawa
United States Bankruptcy Judge

Entered on Docket
December 08, 2022

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEVADA

* * * * *

In re: MICHAEL D. FROELICH, Debtor.	Case No. 21-12864-mkn Chapter 7
EMPLOYERS MUTUAL CASUALTY COMPANY, Plaintiff, vs. MICHAEL D. FROELICH, Debtor, Defendant.	Adv. Proc. No. 21-01138-mkn Date: August 11, 2022 Time: 1:30 p.m.

ORDER ON EMPLOYERS MUTUAL CASUALTY COMPANY'S MOTION FOR SUMMARY JUDGMENT[1]

On August 11, 2022, the court heard the Employers Mutual Casualty Company's Motion for Summary Judgment. The appearances of counsel were noted on the record. After arguments were presented, the matter was taken under submission.

[1] In this Order, all references to "ECF No." are to the number assigned to the documents filed in the above-captioned bankruptcy case as they appear on the docket maintained by the clerk of court. All references of "AECF No." are to the documents filed in the above-captioned adversary proceeding. All references to "Section" or "§§ 101-1532" are to the provisions of the Bankruptcy Code. All references to "FRE" are to the Federal Rules of Evidence. All references to "Bankruptcy Rule" shall be to the Federal Rules of Bankruptcy Procedure. All references to "Civil Rule" shall be to the Federal Rules of Civil Procedure. All references to "NRS" are to the Nevada Revised Statutes.

BACKGROUND[2]

On June 3, 2021, a voluntary "skeleton" Chapter 7 petition was filed by Michael D. Froelich ("Debtor"). (ECF No. 1). A Notice of Chapter 7 Bankruptcy Case was filed scheduling a meeting of creditors ("341 Meeting") for July 12, 2021, setting a deadline of August 12, 2021, for creditors to file proofs of claim, and also set a deadline of September 10, 2021, for interested parties to object to the Debtor's Chapter 7 discharge or to object to the discharge of a particular debt. The case was assigned for administration to Chapter 7 panel trustee Brian D. Shapiro ("Trustee").

On June 30, 2021, schedules of assets and liabilities ("Schedules") and a statement of financial affairs ("SOFA") were filed on behalf of the Debtor. (ECF No. 12).

On July 13, 2021, the 341 Meeting was concluded. (ECF No. 15).

On September 9, 2021, Employers Mutual Casualty Company ("EMCC" or "Plaintiff") commenced the above-captioned adversary proceeding ("Adversary Proceeding") by filing a complaint ("Complaint") against the Debtor. (AECF No. 1). Plaintiff seeks a determination that an alleged debt owed by Debtor is nondischargeable pursuant to Section 523(a)(4).

On September 13, 2021, a stipulated order was entered granting the Trustee an extension to November 5, 2021, to object to Debtor's discharge. (ECF No. 41).

On September 14, 2021, a copy of the Complaint and summons was served on the Debtor. (AECF No. 7).

On October 1, 2021, Debtor in pro se filed his answer to the Complaint. (AECF No. 8).

On October 12, 2021, Debtor filed amended Schedules as well as an amended SOFA. (ECF No. 55.)

[2] Pursuant to FRE 201(b), the court takes judicial notice of all materials appearing on the docket in the above-captioned adversary proceeding and the above-captioned Bankruptcy Case See U.S. v. Wilson, 631 F.2d 118, 119 (9th Cir. 1980); see also Bank of Am., N.A. v. CD-04, Inc. (In re Owner Mgmt. Serv., LLC Trustee Corps.), 530 B.R. 711, 717 (Bankr. C.D. Cal. 2015) ("The Court may consider the records in this case, the underlying bankruptcy case and public records.").

On October 28, 2021, Plaintiff filed a Discovery Plan. (AECF No. 9).[3]

On February 7, 2022, Plaintiff filed a motion to extend discovery deadlines (First Request) by 45 days. (AECF No. 11).

On March 18, 2022, an order was entered granting Plaintiff an extension of the discovery deadlines. (AECF No. 20). The new discovery cutoff deadline was approved for May 18, 2022, amongst other deadlines.

On May 24, 2022, Debtor filed an opposition to Plaintiff's Complaint.[4] (AECF No. 22).

On June 14, 2022, Plaintiff filed the instant motion for summary judgment ("MSJ") to which is attached copies of thirty documents marked as exhibits. (AECF No. 24).

On July 1, 2022, Debtor filed his opposition ("MSJ Opposition") to the MSJ. (AECF No. 27).

On July 19, 2022, EMCC filed its reply in support of its MSJ ("Reply"). (AECF No. 28).

SUMMARY JUDGMENT STANDARDS

A motion for summary judgment is governed by Civil Rule 56 which is applicable in this Adversary Proceeding under Bankruptcy Rule 7056. See Silva v. Smith's Pac. Shrimp, Inc. (In re Silva), 190 B.R. 889, 891 (B.A.P. 9th Cir. 1995). Summary judgment may be granted only if "the movant shows that there is no genuine dispute as to any material fact and that the movant is entitled to judgment as a matter of law." FED. R. CIV. P. 56(a). For summary judgment purposes

[3] On November 4, 2021, a separate adversary proceeding was commenced against the Debtor by the Trustee, denominated Adversary Proceeding No. 21-01216-mkn ("Discharge Adversary"). The Trustee seeks to deny the Debtor a Chapter 7 discharge entirely, based on Sections 727(a)(3), 727(a)(4)(A), and 727(a)(4)(D). If the Trustee prevails in the Discharge Adversary, none of the Debtor's pre-petition debts, including the claim alleged by the Plaintiff in the instant adversary proceeding, will be discharged. Because a successful objection under Section 727(a) bars a discharge of all prepetition debts, the determination of dischargeability of any specific prepetition debt under Section 523(a) is unnecessary. Thus, creditors ordinarily await the outcome of any discharge objection before expending the time and legal expenses of pursuing a dischargeability determination.

[4] On the same date, Debtor filed an opposition to a summary judgment motion filed by the Trustee in the Discharge Adversary. It appears that the Debtor simply took the opportunity to file a similar document in the instant adversary proceeding even though he had already filed an answer to the Complaint.

"[m]aterial facts are those that may affect the outcome of the case." Farmer v. Las Vegas Metro. Police Dep't, 423 F.Supp.3d 1008, 1013 (D. Nev. 2019), citing Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1985). Findings of fact may not be entered because summary judgment may only be granted where there are no disputed issues of fact. See Animal Legal Def. Fund v. U.S. Food & Drug Admin., 836 F.3d 987, 989-90 (9th Cir. 2016).

A genuine issue of material fact exists when "the evidence is such that a reasonable jury could return a verdict for the nonmoving party." Id. The moving party's evidence is judged by the same standard of proof applicable at trial. See Celotex Corp. v. Catrett, 477 U.S. 316, 323 (1986); see also Southern Calif. Gas Co. v. City of Santa Ana, 336 F.3d 885, 888 (9th Cir. 2003). The burden of proof is on the party seeking the summary judgment, but the inferences are viewed in favor of the opposing party. See Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451, 456 (1992); see also Miller v. Glenn Miller Prods., Inc., 454 F.3d 975, 987 (9th Cir. 2006). Determinations of intent or credibility generally are ill-suited for disposition by summary judgment. See Fogel Legware, etc. v. Wills (In re Wills), 243 B.R. 58, 65 (B.A.P. 9th Cir. 1999). Likewise, establishing that an opposing party had a particular state of mind, such as actual knowledge or understanding of certain facts or consequences, is difficult on summary judgment. See generally 10B Wright, Miller & Kane, FEDERAL PRACTICE AND PROCEDURE: CIVIL, §2730 (4th ed. 2022). Once the moving party demonstrates the absence of disputed material facts, the responding party must provide admissible evidence raising a genuine dispute. The responding party cannot rely solely on conclusory allegations unsupported by factual data. See Farmer v. Las Vegas Metro. Police Dep't, 423 F.Supp.3d at 1014 ("the nonmoving party cannot avoid summary judgment by relying solely on conclusory allegations that are unsupported by factual data [. . . .] Instead, the opposition must go beyond the assertions and allegations of the pleadings and set forth specific facts by producing competent evidence that shows a genuine issue for trial.") (external citations omitted).

DISCUSSION[5]

[5] In the Discharge Adversary, the Trustee's motion for summary judgment on all claims under Sections 727(a)(3), 727(a)(4)(A) and 727(a)(4)(D) was denied by an order ("Discharge Adversary Order") entered on October 24, 2022. In that proceeding, the Trustee's evidence in

The Bankruptcy Code is designed to give the honest but unfortunate debtor a fresh start in bankruptcy; thus, exceptions to discharge should be construed strictly against the creditor and liberally in favor of the debtor. See Landsdowne v. Cox (In re Cox), 41 F.3d 1294, 1297 (9th Cir.1994). "[E]xceptions to discharge 'should be confined to those plainly expressed.'" Kawaauhau v. Geiger, 523 U.S. 57 (1998), quoting Gleason v. Thaw, 236 U.S. 558 (1915). A preponderance of the evidence standard applies to proceedings to determine dischargeability of debt under Section 523. See Grogan v. Garner, 498 U.S. 279, 286 (1991).

Having considered the MSJ, the materials submitted, and the written and oral arguments presented, the court concludes there are genuine disputes of material fact, and Plaintiff is not entitled to summary judgment.

I. The Debtor's Prior Litigation and Bankruptcies.

Debtor was the owner and president of a company called Construction Services Unlimited ("CSU") in Nevada. See MSJ at 4:4-5. CSU bid upon and entered into a public works contract with the Clark County Water Reclamation District ("CCWRD") for the construction of a security center ("Project"). Id. at 4:5-7. As a condition of entering into the contract, CSU was required to post a performance bond and a payment bond with CCWRD. Id. at 4:7-9. The performance bond guarantees the completion of the Project while the payment bond guarantees payment to CSU's subcontractors and suppliers on the Project. Id. at 4:9-10.

To satisfy the bonding requirements, Debtor requested the Plaintiff to issue a performance bond ("Performance Bond") and a payment bond ("Payment Bond"). Thereafter, Plaintiff issued a Performance Bond in the amount of $539,750.00 with CSU as principal and CCWRD as obligee for the Project. See MSJ at 4:11-14. The Performance Bond assured CCWRD that Plaintiff would complete the Project should CSU default. Id. at 4:14-15. Plaintiff also issued a Payment Bond in the amount of $539,750.00 with CSU as principal and the CCWRD as obligee for the Project. Id. at 4:15-17. The Payment Bond assured CCWRD that Plaintiff would pay qualifying suppliers and subcontractors of CSU should CSU fail to do so. Id.

---

support of summary judgment included transcripts of the Debtor's sworn testimony at a deposition and at the 341 Meeting, as well as the Debtor's belated response to a request for admissions.

at 4:17-18. In consideration for Plaintiff's issuance of these bonds, Debtor and CSU, among others, executed a "General Agreement of Indemnity" ("GAI"). Under the GAI, Debtor is required to hold harmless and indemnify Plaintiff for any loss arising from the issuance of the Performance Bond and the Payment Bond. Id. at 4:19-22. Eventually, a number of events occurred regarding the Project, resulting in a federal lawsuit between the Plaintiff and the Debtor.

On August 19, 2015, Plaintiff commenced a civil action against Debtor, and several others who are not parties to this Adversary Proceeding, in the United States District Court for the District of Nevada ("USDC"). Subject matter jurisdiction was based on diversity of citizenship under 28 U.S.C. §1334. That action, denominated Case No. 2:15-cv-01592-JCM-GWF ("USDC Case"), sought to recover Plaintiff's losses resulting from its issuance of the Performance and Payment Bonds. See MSJ at ¶ 32. On December 11, 2015, Plaintiff requested entry of default in the USDC Case when Debtor failed to answer the civil complaint ("USDC Complaint"). Id. at ¶ 37. On December 14, 2015, default was entered in the USDC Case against all of the named defendants. Id. at ¶ 38.

On December 30, 2016, Debtor filed a Chapter 13 proceeding, denominated Case No. 16-16917-MKN, at which time the USDC Case was still pending ("First Bankruptcy"). See MSJ at ¶ 39. On June 7, 2018, a default judgment in the amount of $566,425.98 was entered against the named defendants other than the Debtor, including CSU, Global Development Group, LLC, and Barbara Froelich. Id. at ¶ 41.

On April 3, 2019, this court entered an order denying confirmation of the Debtor's proposed Chapter 13 plan in the First Bankruptcy, and also dismissed the case "pursuant to 11 U.S.C. §1307(c)(1), unreasonable delay that is prejudicial to creditors caused by Debtor's failure to confirm a Plan and resolve the issues[.]" See MSJ at ¶ 42, citing Exhibit 14 (internal quotations omitted). The First Bankruptcy was subsequently closed without a Chapter 13 discharge. Id. at ¶ 42, citing Exhibit 15. Upon this change in circumstances, Plaintiff sought to amend the judgment in the USDC Case to include the Debtor. Id. at ¶ 43. On August 6, 2019, default judgment was entered in the USDC Case against Debtor and in favor of Plaintiff in the

amount of $566,425.98. That default judgment was recorded with the Clark County Recorder on August 23, 2019. Id. at ¶ 44, citing Exhibit 17.

On January 23, 2020, Debtor again filed for bankruptcy relief under Chapter 13 and the proceeding was assigned case number: 20-10343-MKN ("Second Bankruptcy"). See MSJ at ¶ 45, citing Exhibit 18. Eventually, the Second Bankruptcy was closed and dismissed without entry of a discharge. Id. at ¶ 47, citing Exhibit 21.

On June 3, 2021, Debtor commenced a bankruptcy proceeding under Chapter 7 ("Third Bankruptcy"), denominated Case No. 21-12864-MKN, which is currently pending before this court. See MSJ at ¶ 48. Plaintiff has filed a proof of claim in the pending Chapter 7 case and also commenced the instant Adversary Proceeding based on the debt established by the default judgment entered in the USDC Case ("USDC Judgment"). Id. at ¶¶ 49-50.

In this Adversary Proceeding, Plaintiff alleges the debt encompassed by the USDC Judgment is nondischargeable under Section 523(a)(4). See generally MSJ. Plaintiff maintains that the GAI contains an express trust provision. It argues that the Debtor failed as a trustee and fiduciary to fulfill his duties to hold money obtained from CCWRD on the Project in trust for the payment of subcontractors and suppliers on the Project. Plaintiff also contends that Debtor breached his fiduciary duties by failing to use or account for all Project funds for the payment of subcontractors and suppliers, including the termination from the Project. Plaintiff maintains that the Debtor failed to fulfill his promises under the GAI in reckless or conscious disregard of his duties as a fiduciary and trustee. See MSJ at ¶ 50.

II. Exceptions to Discharge- 11 U.S.C. § 523(a)(4).

A. The Applicable Legal Standard.

Under Section 523(a)(4), a Chapter 7 discharge does not include a debt "for fraud or defalcation while acting in a fiduciary capacity, larceny, or embezzlement." 11 U.S.C. § 523(a)(4).[6] Under this provision, whether the debt was incurred through fraud or defalcation, the

[6] Section 523(a)(4) also excepts debt incurred through larceny or embezzlement. Neither of those theories require the debtor to be acting in a fiduciary capacity.

debtor must have been acting in a fiduciary capacity. See Peltier v. Van Loo Fiduciary Services, LLC (In re Peltier), 2022 WL 3371637, at *5 (B.A.P. 9th Cir. Aug. 16, 2022).

"Federal bankruptcy law determines whether a fiduciary relationship exists within the meaning of § 523(a)(4)." See In re Park, 2021 WL 6138231, at *6 (Bankr. C.D. Cal. Dec. 29, 2021). In federal court, "fiduciary" is narrowly defined. See In re Lookofsky, 2022 WL 527738, at *4 (Bankr. C.D. Cal. Feb. 22, 2022) (external citation omitted). The broad definition of a fiduciary as a relationship involving confidence, trust, and good faith, is inapplicable under Section 523(a)(4). Id. "Instead, bankruptcy law must clearly and expressly impose trust-like obligations on the party." Id., citing Double Bogey, L.P. v. Enea (In re Appian Construction, Inc.), 794 F.3d 1047, 1050 (9th Cir. 2015). For the purposes of Section 523(a)(4), a fiduciary relationship must be one which arises "from an express or technical trust that was imposed before and without reference to the wrongdoing that caused the debt." In re Park, 2021 WL 6138231, at *6 (internal quotations omitted) (external citation omitted). That trust relationship can be created by statute or an express agreement between the parties. See ATR-Kim Eng Fin. Corp. v. Bonilla (In re Bonilla), 2008 WL 4414153, at *5 (N.D. Cal. Sept. 25, 2008) (internal quotations omitted) (external citation omitted). State law is consulted when determining whether a trust exists in the strict sense. See In re Schultz, 46 B.R. 880, 884 (Bankr. D. Nev. 1985) (external citation omitted). The Ninth Circuit makes it clear that state law is to be consulted to ascertain whether the requisite express or technical trust relationship exists. See In re Tolman, 491 B.R. 138, 150 (Bankr. D. Idaho 2013) (external citations omitted).

To prove fraud under Section 523(a)(4), a plaintiff must show fraud in fact, involving moral turpitude or intentional wrong, rather than implied or constructive fraud. See In re Zimmerman, 2011 WL 1753779, at *4 (Bankr. D. Ariz. May 6, 2011). Circumstantial evidence may be used to determine fraudulent intent. Id.

Because Section 523(a)(4) also includes the words "fraud," "larceny," and "embezzlement," the Supreme Court in Bullock v. BankChampaign, 569 U.S. 267 (2013) addressed only the particular state of mind encompassed by the term "defalcation." Id. at 273. To prove defalcation, a plaintiff must demonstrate that the debtor acted with knowledge of the

improper nature of the conduct of a fiduciary, **or**, acted with gross recklessness in respect to the improper nature of the conduct. Id. at 269. The Court held that proof of either is sufficient to establish the culpable state of mind required to find defalcation under Section 523(a)(4). Id.[7] After discussing the meaning of the separate term "fraud" under bankruptcy law, the Court explained in Bullock:

> We believe that the statutory term 'defalcation' should be treated similarly. Thus, where 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…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."

569 U.S. at 273-74 (emphasis added). Thus, proof that a debtor has knowledge that his or her conduct is improper is sufficient to establish defalcation. In the alternative, proof of a debtor's gross recklessness is established when a fiduciary consciously disregards, or is willfully blind to, a substantial and unjustifiable risk that his or her conduct will turn out to violate a fiduciary duty. See In re Maxwell, 509 B.R. 286, 289 (Bankr. E.D. Cal. 2014). The risk must be such that considering the nature and purpose of the debtor's conduct and the known circumstances, the conduct involves a gross deviation from the standard of conduct that a law-abiding person would observe in the debtor's situation. Id., citing ALI, Model Penal Code § 2.02(2)(c), at 226 (1985).

B. Application of the Legal Standard in this Adversary Proceeding.

Plaintiff alleges the default judgment entered in the USDC Case is nondischargeable pursuant to Section 523(a)(4). See generally MSJ. To support this claim, Plaintiff argues an express trust exists via the GAI, where trust language is found in Section 10. See MSJ at 21:17, 22:9-10; see also MSJ at Exhibit 1, Exhibit 1C. Section 10 of the GAI reads as follows:

---

[7] Interpreting the word defalcation in the context of the entire language in Section 523(a)(4), the Court expressly stated: "We hold that it includes a culpable state of mind requirement akin to that which accompanies application of the other terms in the same statutory phrase. We describe that state of mind as one involving knowledge of, or gross recklessness in respect to, the improper nature of the relevant fiduciary behavior." 569 U.S. at 269. (Emphasis added.)

> The Undersigned [the Indemnitors] covenant and agree that all payments received for or on account of contract(s) which are bonded by the Surety [EMCC] shall be held as trust funds in which the Surety has an interest. To secure said interest, it is agreed that all monies paid to the Principal [CSU] and/or Undersigned covered by the Bond(s) are trust funds for the benefit of and the payment for direct labor, materials and services furnished in the prosecution of the work specified in the contract(s) for which the Surety may be or become liable under any of said Bond(s). The trust funds are specifically reserved as set forth above, and any breach of said duty shall be deemed a breach of the duties or obligations of the Undersigned under this Agreement of Indemnity.

See MSJ at Exhibit 1, Exhibit 1C.

NRS 163.003 states that an express trust requires: "[t]he settlor properly manifests an intention to create a trust; and [] [t]here is trust property [. . .]." See NEV.REV.STAT. § 163.003; see also Plyam v. Precision Development, LLC (In re Plyam), 530 B.R. 456, 472 (B.A.P. 9th Cir. 2015). "There are various methods to create a trust, including a declaration by the owner of property that he or she holds the property as trustee or a transfer of property by the owner during his or her lifetime to another person as trustee." Id. at 472, citing NEV.REV.STAT. § 163.002. Here, the GAI contains an express trust provision in Section 10 and defines what trust property exists under the trust. See MSJ at Exhibit1, Exhibit 1C. Plaintiff and Debtor both executed the GAI, which shows an intention to create the trust. Id. Neither Plaintiff nor Debtor deny that the language in the GAI created a trust, with Debtor acting in a fiduciary capacity for the trust. See MSJ Opposition at ¶¶ 60(e)-60(f); see generally MSJ. Plaintiff and Debtor executed the GAI, and thus created the trust in 2013. See MSJ at Exhibit 1, Exhibit 1C. Thus, Debtor began his fiduciary relationship with Plaintiff in 2013. Id.

An express trust that was imposed before and without reference to the wrongdoing that caused the debt establishes a fiduciary relationship within the context of federal bankruptcy law. See In re Tolman, 491 B.R. at 149. Debtor does not deny that he is a fiduciary under the trust created by the GAI, but argues that he did not breach his duties.[8] See MSJ Opposition at ¶¶

[8] Debtor does deny being "[. . .] a trustee or part thereof to an express trust account [. . .]." See MSJ Opposition at ¶ 69. Debtor executed the express trust in the GAI; therefore, he was a part of the express trust, and furthermore, one cannot state they were a fiduciary to an express trust but not a part of an express trust. See MSJ at Exhibit 1, Exhibit 1C. The analysis under Section 523(a)(4) involves whether Debtor was acting in a fiduciary capacity as

60(e)-60(g), 69. Furthermore, the debt owed to Plaintiff was created while Debtor was acting as a fiduciary. The MSJ details a series of events occurring in 2015, such as the alleged failure of CSU to submit certified payroll reports regarding a supplier and/or subcontractor on the Project. See MSJ at ¶ 14. Eventually, lawsuits were filed. See generally MSJ. Between 2015-2017, losses were incurred, and subcontractors and suppliers were allegedly unpaid by CSU. Id. at ¶ 30. Debtor was acting as a fiduciary during the time these debts were created under the GAI. See generally MSJ; see also MSJ Opposition at ¶ 69. Under these circumstances, the court concludes that as a matter of law, Debtor was acting in a fiduciary capacity under Section 523(a)(4) at the time of any allegation defalcation.

Debtor argues, however, that he never breached his fiduciary duties. See MSJ Opposition at ¶ 60(g). Debtor further maintains that Plaintiff failed to cooperate with CCWRD and CSU on all grounds, and Plaintiff's claims are caused by its own lack of judgment towards the Project's completion, evidenced by Plaintiff's own breach of the Performance Bond. Id. at ¶ 64. Debtor argues that budget and scheduling issues were created by Plaintiff's own approach to the Project, but despite these issues, Debtor did not breach any fiduciary duties or misappropriate any funds. Id. at ¶¶ 60(k), 67. In short, Debtor maintains that even if he was acting in a fiduciary capacity within the meaning of Section 523(a)(4), there was no fraud and there was no defalcation.

To establish fraud under Section 523(a)(4), Plaintiff must demonstrate fraud in fact, involving moral turpitude or intentional wrong, rather than implied or constructive fraud. See In re Zimmerman, 2011 WL 1753779, at *4. While fraudulent intent may be established by circumstantial evidence, a determination of intent typically involves an assessment of the credibility of the alleged wrongdoer. To establish defalcation under Section 523(a)(4), both the demonstration of the alleged wrongdoer's knowledge of impropriety, or the wrongdoer's conscious disregard or willful ignorance of risk, involves an assessment of the credibility of the alleged wrongdoer. As previously explained, determinations of knowledge or intent is generally inappropriate through summary judgment. See, e.g., In re Kinikini, 2019 WL 4580364, at *2

---

determined by federal law, which for the reasons supra, Debtor is considered a fiduciary for the purposes of Section 523(a)(4).

(Bankr. D. Idaho Sep. 20, 2019) ("Additionally, [c]redibility determinations, the weighing of the evidence, and the drawing of legitimate inferences from the facts' are inappropriate at the summary judgment stage.") (internal quotations omitted) (external citation omitted).

In this instance, Plaintiff has established that there is no dispute of material facts that the Debtor acted in a fiduciary capacity. Genuine issues of material fact exist, however, as to whether Debtor committed fraud or defalcation while acting in his fiduciary capacity.[9]

III. Claim Preclusion and Issue Preclusion.

Plaintiff additionally argues the doctrine of *res judicata* should apply in the instant case and enforce the USDC Case's default judgment against Debtor. See MSJ at 27:12-14. The preclusive effect of a prior adjudication is often referred to as *res judicata.* Some courts consider *res judicata* to encompass claim preclusion only while referring to issue preclusion as collateral estoppel, while other courts simply refer to both claim and issue preclusion as *res judicata*. See In re Antonie, 432 B.R. 843, 848 (Bankr. D. Idaho 2010), *aff'd*, 447 B.R. 610 (D. Idaho 2011); see also Taylor v. Sturgell, 128 S. Ct. 2161, 2171 (2008). Both claim and issue preclusion have unique requirements and effects. See Five Star Capital Corp. v. Ruby, 124 Nev. 1048, 1055, 194 P.3d 709, 713 (2008), holding modified by Weddell v. Sharp, 131 Nev. 233, 350 P.3d 80 (2015) ("[. . .] while claim preclusion can apply to all claims that were or could have been raised in the initial case, issue preclusion only applies to issues that were actually and necessarily litigated and on which there was a final decision on the merits.").

As previously mentioned, subject matter jurisdiction in the USDC Case was based on diversity of citizenship. In diversity cases, the preclusive effect given to the federal court's judgment generally is determined by the laws of the State in which the federal court presides.

---

[9] Exhibits 24 and 25 attached to the MSJ consist of copies of the same Request for Admissions dated February 4, 2022, that Plaintiff previously propounded to the pro se Debtor. Request No. 19 asked the pro se Debtor to "Admit that You breached Your fiduciary duties to EMCC identified in Section 10 of the GAI." Because the pro se Debtor did not respond to that discovery, Plaintiff requests that the subject matter be treated as "admitted" under FRCP 36(a)(3). On its face, the utility of requesting a pro se party to admit to any legal conclusion is problematic at best especially when it comes to duties imposed by law. Because a defalcation while acting in a fiduciary capacity encompassed by Section 523(a)(4) is different from a simple breach of fiduciary duty, the admission requested by the Plaintiff is relevant but not material.

See Semtek Intern. Inc. v. Lockheed Martin Corp., 531 U.S. 497, 508 (2001). Although it is not clear what preclusive effect would be given by a Nevada court to a prior federal diversity judgment, compare Dalbotten v. C.R. Bard, Inc., 2022 WL 2910125, at *2 (D. Mont. July 22, 2022) (uncertainty under Arizona law), it is clear that Nevada courts require that issues are actually litigated and necessarily decided before affording preclusive effect to federal or state judgments. See, e.g., In re Sandoval, 126 Nev. 136, 140-141 (2010) (Nevada default judgment not given issue preclusive effect in a nondischargeability claim under Section 523(a)(6) asserting willful and malicious injury").

A. Claim Preclusion

It is well established that claim preclusion does not apply in dischargeability proceedings because exceptions to discharge are determined by the bankruptcy court. See Grogan v. Garner, 498 U.S. 279, 284 (1991). See also In re Lyndon, 2018 WL 3004588, at *2 (Bankr. D. Haw. June 13, 2018); In re Szewc, 568 B.R. 348, 360 (Bankr. D. Or. 2017). As a practical matter, the prospect of a defendant's subsequent bankruptcy should not encourage plaintiffs to pursue fraud and similar claims for fear that they would be barred from pursuing them in bankruptcy. In this instance, only the judgment in the USDC Case would be subject to a res judicata analysis, but no party asserts that the judgment disposed of any claim that was not raised by either party. Thus, the claim preclusion component of res judicata is immaterial.

B. Issue Preclusion

Issue preclusion, also known as collateral estoppel, does apply in dischargeability and other bankruptcy proceedings. See Black v. Bonnie Springs Family Ltd. P'ship (In re Black), 487 B.R. 202, 211 (B.A.P. 9th Cir. 2013); see also Taylor v. Sturgell, 128 S. Ct. 2161, 2171 (2008). Issue preclusion prevents re-litigation of an issue of fact or law that was decided in a prior proceeding. See Villamar v. Hersh, 37 Fed. Appx. 919, 920 (9th Cir. 2002); see also Taylor v. Sturgell, 128 S. Ct. at 2171 ("Issue preclusion [. . .] bars successive litigation of an issue of fact or law actually litigated and resolved in a valid court determination essential to the prior judgment, even if the issue recurs in the context of different claim.") (internal quotations omitted) (external citation omitted).

In Taylor v. Sturgell, the Court observed that "[t]he preclusive effect of a federal-court judgment is determined by federal common law." 128 S.Ct. at 2171. Additionally, the Nevada Supreme Court observed that "[w]ith regard to federal-question cases, federal common law endeavors to develop a uniform rule of preclusion." Garcia v. Prudential Ins. Co. of Am., 129 Nev. 15, 20, 293 P.3d 869, 872 (2013). As previously mentioned, the complaint filed in the USDC Case, however, was not a federal-question case, but jurisdiction was based on diversity of citizenship between the parties. See MSJ at Exhibit 5, ¶ 6. In Semtek Int'l Inc. v. Lockheed Martin Corp. the Court described the application of preclusion principles under state law to diversity judgments. 121 S. Ct. at 1028-1029. Because Nevada law determines the issue preclusive effect of the subject judgment, Plaintiff must establish the following:

> (1) the issue decided in the prior litigation must be identical to the issue presented in the current action; (2) the initial ruling must have been on the merits and have become final; ... (3) the party against whom the judgment is asserted must have been a party or in privity with a party to the prior litigation; and (4) the issue was actually and necessarily litigated.

Five Star Capital Corp. v. Ruby, 124 Nev. 1048, 1055, 194 P.3d 709, 713 (2008), holding modified by Weddell v. Sharp, 131 Nev. 233, 350 P.3d 80 (2015) (internal quotations omitted).

Here, Plaintiff does not mention issue preclusion nor attempt to establish the elements of issue preclusion required under Nevada law. See generally MSJ. Even if Plaintiff tried to establish issue preclusion, the USDC Complaint involves contractual indemnity, equitable indemnity, declaratory relief, *quia timet*, and specific performance. See MSJ at Exhibit 5. It is unclear how these issues are identical to those required under Section 523(a)(4). More important, the judgment entered in the USDC Case was by default. See generally MSJ. As further explained by the Supreme Court of Nevada, an issue must have been actually litigated and not simply that the party had an opportunity to litigate the issue. See In re Sandoval, 126 Nev. 136, 141, 232 P.3d 422, 425 (2010). A review of the docket in the USDC Action reveals that a default judgment was entered without an answer ever being filed by the Debtor. Compare id., 126 Nev. at 141, 232 P.3d at 425 ("When a default judgment is entered where an answer has not been filed, the issue presented was not actually and necessarily litigated, and issue preclusion

does not apply in such circumstances."). Because a default judgment would not be given issue preclusive effect under Nevada law, issue preclusive effect cannot be given to the default judgment entered in the USDC Case.[10]

Based on the foregoing, the court concludes that genuine issues of material fact exist as to the Debtor's alleged fraud or defalcation in a fiduciary capacity. The default judgment entered in the USDC Case does not alter that conclusion.

IT IS THEREFORE ORDERED that the Employers Mutual Casualty Company's Motion for Summary Judgment, Adversary Docket No. 24, be, and the same hereby is, **GRANTED IN PART** and **DENIED IN PART.**

IT IS FURTHER ORDERED that as a matter of law the Defendant was acting in a fiduciary capacity for the matters alleged in this Adversary Proceeding.

IT IS FURTHER ORDERED that triable issues of fact remain as to whether the debt asserted in this Adversary Proceeding occurred as a result of fraud or defalcation while acting in a fiduciary capacity.

IT IS FURTHER ORDERED that a scheduling conference will be held in this Adversary Proceeding on **January 11, 2023 at 9:30 a.m.**

Copies sent via CM/ECF ELECTRONIC FILING
Copies sent via BNC to:
MICHAEL D. FROELICH
1369 OPAL VALLEY ST.
HENDERSON, NV 89052

# # #

[10] Plaintiff argues that a default judgment is a determination on the merits for the purposes of res judicata and supports this statement by citing to Howard v. Lewis, 905 F.2d 1318, 1323 (9th Cir. 1990). See MSJ at 27:25-28. The Howard case, however, addressed a federal habeas corpus petition that followed an unsuccessful state habeas corpus petition. The circuit panel was unwilling to extend the successive habeas petition doctrine to circumstances where prison officials impeded the petitioner's ability to respond to a motion to dismiss. In fact, the Howard court acknowledged that the merits of the claims underlying the prior habeas petition were not determined. 905 F.2d at 1322. Nothing in the case supports the conclusion that the default judgment entered in the USDC Case is entitled to issue preclusive effect under Nevada law.