U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE:	§	**Case No. 03-34846-HDH-7**
	§	
PAUL ALFRED ESQUIVEL and	§	
MAGDELINE ESQUIVEL	§	
	§	
Debtors	§	

MARIA COREAS	§	
	§	
Plaintiff	§	
	§	**Adversary No. 03-3569**
v.	§	
	§	
PAUL A. ESQUIVEL, d/b/a LAW	§	
OFFICES OF PAUL A. ESQUIVEL	§	

Defendant

MEMORANDUM OPINION

I. Facts

This Court heard arguments on June 14, 2004 to determine whether Maria Coreas' claim of $1,300 was nondischargeable under § 523(a)(4) of the Bankruptcy Code.

At the trial on the adversary proceeding, the Plaintiff testified that she was a native of El Salvador and she hired the Law Offices of Paul Esquivel in June 2001 to obtain U.S. citizenship for herself and her son. She paid $1,300 for this service. Plaintiff also testified that she terminated the representation after two years had passed with no resolution in her case, and she signed an agreement to that effect.

In her amended pleading, Plaintiff stated that she filed suit against Paul Esquivel in September of 2002 for malpractice, breach of contract and fraud. The state court ordered the parties to mediation. The mediation was scheduled for July 11, 2003. At that time, Plaintiff was informed that the Debtors had filed for bankruptcy relief. The Debtors admitted in their answer that the Law Offices of Paul Esquivel had filed for Chapter 11 while Mr. and Ms. Esquivel filed for Chapter 7 relief under the Bankruptcy Code.

Plaintiff originally argued that her claim cannot be discharged under § § 523(a)(3), (4), or (6) of the Bankruptcy Code. However, this Court granted summary judgment as to § 523(a)(3) and (6), in an order entered on April 22, 2004. This Court found that the cause of action alleged under § 523(a)(4) survived the motion for summary judgment.

II. Applicable Law and Burden of Proof

Section 523 of the Bankruptcy Code provides that a debtor may not discharge certain types of debts. Under § 523(a)(4), a debt "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny" may not be discharged in bankruptcy. 11 U.S.C. § 523 (West 2003). The exceptions provided by § 523 are strictly construed towards dischargeability because the purpose of bankruptcy is to allow the debtor to have a 'fresh start.' *Texas Lottery Comm'n v. Tran (In re Tran)*, 151 F.3d 339, 342 (5th Cir. 1998).

The Fifth Circuit court stated in *Tran*, "Congress designed the discharge exception to reach 'debts incurred through abuses of fiduciary positions through active misconduct whereby a debtor has deprived others of their property by criminal acts; both classes of conduct involve debts arising from the debtor's acquisitions or use of property

that is not the debtor's.'" *Id.* at 342 (citing *Boyle v. Abilene Lumber, Inc. (In re Boyle)*, 819 F.2d 583 (5th Cir. 1987).

Moreover, the creditor who files the complaint has the burden of proof at trial to demonstrate by a preponderance of the evidence that the debt should not be discharged. *Grogan v. Garner*, 489 U.S. 279 (1991); *Hayden v. Hayden (In re Hayden)*, 248 B.R. 519 (Bankr. N.D. Tex. 2000).

To have a debt discharged under § 523(a)(4), the Plaintiff must show: "1) the existence of a fiduciary relationship between the debtor and the objecting party, and 2) a defalcation committed by the debtor in the course of that fiduciary relationship." *In re Young*, 91 F.3d 1367, 1371-72 (10th Cir. 1996).

III. Analysis

A. Fiduciary Capacity under § 523(a)(4)

The Plaintiff contends that the fiduciary relationship is created by the attorney-client relationship. The Plaintiff argues that the Debtors acted in a fiduciary capacity by placing her $1,300 in their client bank account and the Debtors committed a defalcation by using that money for their own purposes after their representation was terminated.

This Court finds this argument unpersuasive. Although the cases are split as to whether the attorney-client relationship alone creates the requisite 'fiduciary capacity,' the "majority of courts that have considered the issue have applied the above principles to require more than an attorney-client relationship alone to establish a fiduciary relationship for purposes of § 523(a)(4). . . . Courts have generally required a trust relationship to exist between an attorney-debtor and a client-creditor to find a fiduciary

relationship for purposes of dischargeability. [citations omitted]." *Young*, 91 F.3d at 1372.

The Fifth Circuit stated in *Tran*, "Under § 523(a)(4), 'fiduciary' is limited to instances involving express or technical trusts. The purported trustee's duties must, therefore, arise independent of any contractual obligation." 151 F.3d at 342. Therefore, constructive trusts or trusts *ex malificio* do not meet the § 523(a)(4) requirements. *Id.* However, the court found that statutory trusts could satisfy the requirements of § 523(a)(4), the "statutory trust must (1) include a definable res and (2) impose 'trust-like' duties. *Id.* at 343.

In this case, the Plaintiff argued that a statutory trust is created by the Texas Disciplinary Rules that oblige a lawyer to keep client funds in a separate 'trust or escrow account.' *See* Tex. Disciplinary Rules Art. 10 § 9, Rule 1.14 and Art. 11, § 5. The Fifth Circuit stated in *Tran*, "we have not expressly identified the particular 'trust- like' duty—or combination of duties—that a state statute must impose to create the specie of fiduciary that meets muster under § 523(a)(4). Nonetheless, once such duty has loomed large—the duty that a trustee refrain from spending trust funds for non-trust purposes." 151 F.3d at 343-44.

The Disciplinary Rules maintain that a separate account be kept for client funds, it is understood, though not stated, the lawyer may not spend funds in the client account for his own purposes. *See* Tex. Disciplinary Rules Art. 10 § 9, Rule 1.14 and Art. 11, § 5. The Plaintiff argued that the Debtors held her funds in trust until they 'earned it' and had no right to keep her $1,300 once she terminated their representation because no results had been obtained in her case.

But "if the gist of a client's complaint is that the attorney did not exercise that degree of care, skill, or diligence as attorneys of ordinary skill and knowledge commonly possess, then that complaint should be pursued as a negligence claim, rather than some other claim." *Deutch v. Hoover, Bax & Slovacek, L.L.P.*, 97 S.W.3d 179, 189 (Tex. App.—Houston [14th Dist.] 2002).

Additionally, "under Texas law, a breach of fiduciary duty claim does not arise from a failure to properly represent the client, and a client may not re-cast an ordinary malpractice claim as one for breach of fiduciary duty – that is an impermissible fracturing of claims under Texas law." *Armstrong v. Jenkins*, case no. 02-38913-BJH-7 (N.D. Tex. 2003) (citing *Aiken v. Hancock*, 115 S.W.3d 26 (Tex. App. —San Antonio 2003)). The Plaintiff has attempted to 're-cast' her malpractice claim as a breach of fiduciary duty claim.

B. Defalcation under §523(a)(4)

Even if this Court determined that the Debtors had acted in a fiduciary capacity with regard to the Plaintiff's funds, the debt would still be discharged because no evidence presented to show fraud or defalcation as required by § 523(a)(4).

Defalcation generally requires: 1) a fiduciary relationship; 2) breach of that fiduciary relationship; and 3) a resulting loss. *Garver v. Garver (In re Garver)*, 116 F.3d 176, 178 (6th Cir. 1997). As stated previously, the attorney-client relationship, without an express or technical trust, is not enough to establish the requisite fiduciary relationship for defalcation under § 523(a)(4). *Id.* at 179. "Defalcation then occurs through the misappropriation or failure to properly account for those trust funds." *Id.* at 180.

Even assuming that the Plaintiff established that a trust existed as to her funds, there was no evidence shown that the Debtors either misappropriated or failed to account for those funds. In *Hayes v. Hayes (In re Hayes)*, 183 F.3d 162 (2nd Cir. 1999), the court stated:

> The term defalcation may well not fit comfortably when used in the context of a dispute over the value of legal services, at least where no bad faith or other breach of fiduciary duty is shown. A lawyer or other fiduciary is allowed to act in his or her self-interest in charging for services in good faith. It is therefore arguable that, where the need for particular services or the size of a fee is a close one and bad faith is not shown, a dispute that is resolved against the fiduciary provider of services does not give rise to a debt nondischargeable under § 523(a)(4). *Id.* at 172.

The Plaintiff has failed to show by a preponderance of the evidence that her debt is nondischargeable under § 523(a)(4) because there was no proof that the Debtors acted in bad faith or with fraudulent intent as to the funds.

IV. Conclusion

The claim of Ms. Coreas is dischargeable because the Debtors were not acting in a fiduciary capacity as defined by § 523(a)(4). In addition, there was no evidence shown to prove defalcation or fraud under §523(a)(4). For these reasons, judgment will be entered in favor of the Defendant.

Signed this 30th day of June, 2004

HONORABLE HARLIN D. HALE
UNITED STATES BANKRUPTCY JUDGE