UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In Re **JOHN PETERSEN, f/d/b/a** **PETERSEN CONSTRUCTION,** **Debtor.**	:	**Case No. 99-1765-WH** **Chapter 7**
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ERMAN MULLINS, **Plaintiff,** **vs.** **JOHN PETERSEN f/d/b/a** **PETERSEN CONSTRUCTION,** **Defendant.**	:	**Adv. No. 99-99138**

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<u>ORDER— MOTION FOR ADJUDICATION OF LAW POINTS</u>

On January 21, 2000, telephonic hearing was held on Creditor/Plaintiff's Motion for Summary Judgment and Motion for Adjudication of Law Points. Plaintiff appeared by his attorney of record, John W. Kocourek, and Debtor/Defendant appeared by his attorney of record, C. R. Hannan. At the conclusion of the hearing and by written order the court overruled and denied the motion for summary judgment finding issues of material fact concerning the nature of the contract between the parties, performance under the contract, and how Defendant was to handle the payments. The court took the Motion for Adjudication of Law Points under advisement. The issue considered by the court is whether the placement of the names of the creditor, the creditor's mortgagee bank, and the debtor on insurance proceed checks, along with acts by the parties, created a trust and imposed a fiduciary obligation on the part of the debtor. The court considers the matter fully submitted.

The court has jurisdiction of these matters pursuant to 28 U.S.C. §157(b)(1) and §1334 and order of The United States District Court for the Southern District of Iowa pursuant to 28 U.S.C §157(a). This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(I). The court upon review of the pleadings, affidavits, briefs, and arguments of counsel, now enters its findings and conclusions pursuant to Fed. R. Bankr. P. 7052.

DISCUSSION

Plaintiff filed this adversary to determine the dischargeability of a debt. In this motion, he asks the court to determine as a matter of law, that Defendant held insurance proceeds in trust for the benefit of Plaintiff and his mortgagee bank. Plaintiff argues that an express trust is evidenced by the insurance policy, the mortgage agreement, the construction contract, and the insurance proceeds check that was made out to Plaintiff, Plaintiff's bank, and Defendant. Plaintiff argues that Defendant converted the insurance proceeds because he did not pay for materials charged a local lumberyard and thereby breached his fiduciary duties. Consequently, Plaintiff's claim should be excepted from discharge pursuant to § 523(a)(4).

Defendant argues that the matter is nothing more than a breached contract. No trust was intended nor did one arise as a matter of law, and he had no fiduciary duties to Plaintiff or the mortgagee bank. Therefore, the debt is not excepted from discharge. For the following reasons, the court agrees with Defendant.

The Bankruptcy Code provides that a discharge under § 727 does not discharge a debt for "for fraud or defalcation while acting in a fiduciary capacity." 11 U.S.C. § 523(a)(4). The term "fiduciary" is determined by federal law. Evans v. Pollard (In re Evans), 161 B.R. 474, 478 (B.A.P. 9th Cir. 1993); Bybee v. Geer (In re Greer), 137 B.R.

37, 40 (Bank. W.D. Mo. 1991). Federal law limits fiduciary relationships to express trusts or technical trusts that are imposed by statute and not trusts implied from contract. Id.; Werner v. Hofmann (In re Hofmann), 144 B.R. 459, 462 (Bank. D.N.D. 1992); see also Devaney v. Dloogoff (In re Dloogoff), 600 F.2d 166, 168 (8th Cir. 1979) (interpreting the similar language of § 17(a)(4) of the Bankruptcy Act). The fiduciary relationship must have existed before and apart from the incident that created the debt. In re Dloogoff, 600 F.2d at 168; Naham v. Jacks (In re Jacks), 243 B.R. 385, 393 (Bankr. C.D. Cal. 1999). Courts may look to state law to determine whether an express or technical trust exists. In re Evans, 161 B.R. at 478.

A trust is a "'fiduciary relationship with respect to property, subjecting the person by whom the title to property is held to equitable duties to deal with the property for the benefit of another person....'" In re Evans, 161 B.R. at 478 quoting Restatement (Second) of Trusts § 2 (1959). It is "created by an agreement between two parties to impose a trust relationship." In re Hofmann, 144 B.R. at 462. A typical express trust includes a declaration of a trust, a trust res, and intention to create a trust relationship. Id.; see also State v. Caslavka, 531 N.W.2d 102, 105 (Iowa 1995)(the court "cannot ignore the requirement that there be some objective manifestation of an intention to create the relationship").

Ordinary commercial transactions do not create trust relationships. In re Geer, 137 B.R. at 40; Onbank & Trust Co. v. Siddell (In re Siddell), 191 B.R. 544, 551 (Bank. N.D.N.Y. 1996). In Iowa, in the context of a construction contract, cash advanced as a down payment is not a transfer in a trust, but rather is an outright transfer of title and

possession of the funds. State v. Galbreath, 525 N.W.2d 424, 426-27 (Iowa 1994); Caslavka, 531 N.W.2d at 104.

In this case, Plaintiff has not demonstrated an objective manifestation of an intention to create an express trust on the part of the insurance company. Plaintiff's argument that by including all the parties' names on the proceeds checks the insurance company demonstrated the requisite intent, is in error. The only intent of the insurance company, that the court discerns, is an intent to fulfill its contractual obligation to pay a claim.

Plaintiff's mortgage agreement required him to carry insurance on the property. This policy was required to contain a standard mortgage clause. (Exh. E. Para. 10b). In the event of damage to the house, the agreement required that "all sums paid under any insurance policy required by this Mortgage shall be paid to Mortgagee...." (Exh. E, Para. 10f). The policy acquired by Plaintiff contained the necessary mortgage clause which stated any payment for loss will be paid to the mortgagee and the insured. (Exh. F). Therefore, when the insurance company issued the check, it was fulfilling its contractual obligation.

The fact that Defendant is named a payee of the check is of no import to the court's analysis. Plaintiff has not offered any evidence of authorization that would permit the insurance company to fulfill its contractual obligation by means of a payment to a trust. Nor has Plaintiff offered any evidence that the court could construe as a declaration of a trust, on the part of the insurance company or Plaintiff. There is no evidence that the funds paid to Defendant were to be segregated or in an escrow account. See Belfry v. Cardozo (In re Cardozo), 862 F.2d 661, 663 (8th Cir. 1988)(a fiduciary relationship

might possibly be found if the agreement required that expenses be paid with the actual dollars that were received by the debtor).

While the parties dispute the terms, they agree that there was a contract for repair of Plaintiff's home. They also agree that the checks were signed over to Defendant as payment pursuant to the contract. "It is not uncommon for a contractor who has entered into a construction contract to default in the performance of that contract. In such a situation, it is not uncommon for the contractor to have left unpaid those who have furnished labor and materials for the project which was the subject matter of the contract." Randall v. Colby190, F.Supp. 319, 327 (N.D. Iowa 1961). Such a situation gives rise to a breach of contract, and the court will not infer a fiduciary relationship. See In re Greer, 137 B.R. at 40 (mere existence of a contract does not imply a fiduciary relationship).

ORDER

IT IS THEREFORE ORDERED as follows: it is the law of this case that the debtor, John Petersen, f/d/b/a Petersen Construction, did not become a trustee of the insurance proceeds for the use and benefit of the creditor(s) and was not a fiduciary under 11 U.S.C. § 523(a)(4).

Dated this __________ day of August, 2000.

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RUSSELL J. HILL, CHIEF JUDGE
U.S. BANKRUPTCY COURT