

**UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF MISSISSIPPI**

IN RE:

**ALPHANETTE B. MARTIN,
DEBTOR.**

**CHAPTER 7
CASE NO. 05-07076-NPO**

**MISSISSIPPI CONFERENCE OF THE
UNITED METHODIST CHURCH, A NON-
PROFIT ORGANIZATION**

PLAINTIFF

VS.

ADV. PROC. NO. 06-00032-NPO

ALPHANETTE B. MARTIN

DEFENDANT

**MEMORANDUM OPINION
GRANTING COMPLAINT TO DETERMINE
DISCHARGEABILITY OF DEBT PURSUANT TO 11 U.S.C. §523(a)(4)**

On December 15, 2006, there came on for trial (the “Trial”) the Complaint to Determine Dischargeability of Debt Pursuant to 11 U.S.C. §523(a)(4)(Adv. Dk. No. 1)(the “Complaint”) filed by the Mississippi Conference of the United Methodist Church, a Non-Profit Organization (the “Conference”) and the Answer to Complaint to Determine Dischargeability of Debt Pursuant to 11 U.S.C. §523(a)(4)(Adv. Dk. No. 4) filed by Alphanette B. Martin (the “Debtor”) in the above-styled adversary proceeding. Jim F. Spencer and Megan B. Conner represented the Conference, and Bryant D. Guy represented the Debtor. The Court, having considered the pleadings, and the testimony, exhibits, and arguments of counsel presented at Trial, finds that the Complaint is well taken and the relief requested should be granted. Specifically, the Court finds as follows:¹

¹ The following constitutes the findings of fact and conclusions of law of the Court pursuant to Federal Rule of Bankruptcy Procedure 7052.

Jurisdiction

This Court has jurisdiction over the parties to and the subject matter of the proceeding. This matter is a core proceeding as defined in 28 U.S.C. §157(b)(2)(I). Notice of the Complaint was proper under the circumstances.

Facts

The Debtor is an ordained United Methodist minister and member of the Conference. Prior to the events in question, she was appointed by the Conference to serve as the Executive Director of the Wesley Foundation at Alcorn State University (“ASU”).

In 2001, the Conference designated \$200,000, together with accrued interest thereon, to be used by the Wesley Foundation at ASU for building a new facility (the “Facility”). The Wesley Foundation, with approval from the Conference, entered into a contract with MacArthur McGriggs (“McGriggs”) to build the Facility. The McGriggs contract (the “McGriggs Contract”) was for \$180,000.

Before the McGriggs Contract was signed, the Conference already had transferred approximately \$29,000 to the Wesley Foundation at ASU purportedly to pay for site preparation and other expenses not covered by the McGriggs Contract. The balance in the account designated for the Facility was \$194,000.

The original agreement with McGriggs required that the Conference pay McGriggs after the Conference approved the construction draw requests. The Debtor complained to Bishop Kenneth Carder that the Conference was exercising too much control over the ASU project and convinced the Bishop to have the Conference transfer the \$194,000 to the River Hills Checking Account for the Wesley Foundation (the “Account”). The evidence demonstrated that the Debtor's salary also was deposited directly to this Account. The Debtor had check writing authority for this Account, and two-party signatures were not required.

On or about July 25, 2002, the Conference received notice of a lawsuit filed by McGriggs for payment of the remaining balance on his contract and damages, totaling \$75,000. As a result of the lawsuit, the Conference launched its investigation.

Reverend Bill Barksdale was employed by the Conference as the Director of Youth and Youth Adult Minister. In this capacity, he served as the Conference's representative to the local campus ministries including the Wesley Foundation at ASU. Bishop Clay Lee was serving as interim Bishop for the Conference. Both Reverend Barksdale and Bishop Lee were responsible for overseeing the investigation by the Conference of this matter.

Reverend Barksdale determined that the Account had a balance of approximately \$45.00, and the Wesley Foundation at ASU had no money to pay McGriggs. The Conference settled the \$75,000 lawsuit for \$46,000 and paid the settlement with Conference funds. *See* Exhibit P-1.

The Conference commenced its administrative process to address the issue with the Debtor. The Debtor selected Reverend Paul Luckett, a fellow minister, to serve as her advocate. A number of meetings occurred with members of the Conference and the Debtor. The Conference retained Brent Saunders, a CPA, to investigate the activity in the Account.

Mr. Saunders created a check register and sorted it by activity. He then created a list of “questionable expenditures.” Meetings were held with the Debtor in which she attempted to explain and document the expenditures as legitimate expenses of the Wesley Foundation. Mr. Saunders and a private investigator retained by the Conference attempted to verify the explanations and to obtain additional documentation. Ultimately, Mr. Saunders provided the Conference the following summary of his reconciliation of the Account:²

² *See* Exhibit P-2.

Total of Questionable Expenditures	149,464.66
Less Salary Paid to Martin Per Payroll Records	(63,240.46)
Less Cash Paid and Personal Note Signed by Martin to MS Business Furnishings	(17,546.45)
Less Cash Receipts Found	<u>(4,800.75)</u>
Net Questionable Expenses to be Accounted For	63,877.00
Plus Check Cashed by Martin (2-23-01) Payable to Wesley Foundation	<u>2,500.00</u>
Grand Total	<u>66,377.00</u>

Reverend Barksdale met with the Debtor further and the questionable expenditure amount of \$66,377.00 was reduced to \$59,849.26 as set forth in Exhibit P-3. Ultimately, the Debtor acknowledged an amount owing of \$59,000 in her handwritten statement. *See* Exhibit P-4. As a result she signed a promissory note (the “Note”) in the amount of \$39,000 and paid the Conference \$20,000 from her pension funds. *See* Exhibits P-5 and P-6, respectively. In the event she paid the required monthly payments under the Note, no interest would accrue.³

The Debtor testified at the Trial that she never had any intentions of paying the amount due under the Note and believed that the Note would be reduced or eliminated and funds returned to her which she had paid, if she was able to provide appropriate receipts to the Conference. However, the Debtor failed to present any credible evidence to substantiate her belief, and the Conference denied that such an understanding existed. Moreover, over four (4) years after the Note was signed and ten (10) months after the Complaint was filed by the Conference and discovery was completed, no additional receipts were offered as evidence by the Debtor at Trial in an attempt to reduce the amount owed under the Note.

The Debtor's testimony at Trial was revealing. When asked specific questions about the

³ The Debtor made one monthly payment on the Note in the amount of \$150.

“questionable expenditures” listed as Exhibit P-2, the Debtor's responses were either evasive or non-responsive.⁴ Significantly, prior to the filing of the Complaint by the Conference, the Debtor listed the Conference as the holder of an unsecured debt “claim/suit”, in the amount of \$38,000 (presumably the Note) and did not schedule it as contingent, unliquidated, or disputed.

Conclusions of Law

11 U.S.C. §523(a)(4)⁵ excepts from discharge any debt “for fraud or defalcation while acting in a fiduciary capacity, embezzlement or larceny.” The Fifth Circuit Court of Appeals has stated that:

[T]his discharge exception was intended to reach those debts incurred through abuses of fiduciary positions and 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 acquisition or use of property that is not the debtor's.

Miller v. J.D. Abrams Inc. (Matter of Miller), 156 F.3d 598, 602 (5th Cir. 1998) (quoting In re Boyle, 819 F.2d 583, 588 (5th Cir. 1987)).

The Fifth Circuit has further opined that “[t]he scope of the concept of fiduciary under 11 U.S.C. § 523(a)(4) is a question of federal law; however, state law is important in determining whether or not a trust obligation exists.” Schwager v. Fallas (In re Schwager), 121 F.3d 177, 186 (5th Cir. 1997). Moreover, “under § 523(a)(4), ‘fiduciary’ is limited to instances involving express or technical trusts.” In re Miller, 156 F.3d at 602; *see also* Sellers v. Parks (In re Parks), 352 B.R. 66, 68 (Bankr. W.D. La. 2006).

Under Mississippi law, “[w]hether a fiduciary relationship exists depends upon factual circumstances.” Mabus v. St. James Episcopal Church, 884 So.2d 747, 757 (Miss. 2004). “While

⁴ As examples, the Debtor refused to explain the checks to BMW Financial, described other expenditures as “business” expenses, and stated that she had not heard of Direct Financial.

⁵ Hereinafter, all code sections refer to the United States Bankruptcy Code located at Title 11 of the United States Code, unless otherwise noted.

Mississippi law does not require any ‘magic words,’ there must be evidence that both parties understood that a special trust and confidence was being reposed.” Id. at 758.

There is no question that the Debtor was in a fiduciary relationship with the Conference. As an ordained minister and member of the Conference, the Debtor was in a covenant relationship to the Conference and its ministers. The Book of Discipline and her ordination vows created, at the very least, a fiduciary relationship. This relationship between the Debtor and the Conference extended to her capacity as the Executive Director of the Wesley Foundation at ASU and as the person responsible for managing the funds in the account for the building project.

Defalcation refers to a failure to produce funds entrusted to a fiduciary and applies to conduct that does not necessarily reach the level of fraud, embezzlement, or misappropriation. L. King, 3 Collier on Bankruptcy ¶523.10 at 523-70 (15th ed. rev. 2006). In Central Hanover Bank & Trust Co. v. Herbst, 93 F.2d 510 (2d Cir. 1937), Judge Learned Hand discussed the meaning of defalcation, as follows:

“[D]efalcation” may demand some portion of misconduct; we will assume *arguendo* that it does. All we decide is that when a fiduciary takes money upon a conditional authority which may be revoked and knows at the time it may, he is guilty of a “defalcation” though it may not be a “fraud,” or an “embezzlement,” or perhaps not even a “misappropriation.”

Central Hanover Bank, 93 F.2d at 512.

Subsequently, in Moreno v. Ashworth (Matter of Moreno), 892 F.2d 417 (5th Cir. 1990), the Fifth Circuit, relying on both of the above-cited authorities, defined defalcation as “a willful neglect of duty, even if not accompanied by fraud or embezzlement.” In re Moreno, 892 F.2d at 421. The Fifth Circuit further held that “a ‘willful neglect’ of fiduciary duty constitutes a defalcation - essentially a recklessness standard.” In re Schwager, 121 F.3d at 185; *see also* Office of Thrift Supervision v. Felt (In re Felt), 255 F.3d 220 (5th Cir. 2001) (willfulness is measured objectively by reference to what a reasonable person in the debtor’s position knew or reasonably should have

known; the objective standard charges the debtor with knowledge of the law without regard to actual intent or motive).

Application of the above standards to the facts of this case leads the Court to the conclusion that the Debtor's conduct constitutes a defalcation while acting in a fiduciary capacity pursuant to §523(a)(4). As an initial matter, the Court did not find the Debtor's testimony to be the more credible explanation of the “questionable expenditures.” When confronted with specific expenses or unexplained cash withdrawals from the Account, the Debtor could only offer a general statement that the money went into the ASU building project, it came from her salary included in the Account, or she could not remember. The specifics of the Saunders reconciliation essentially went unanswered by the Debtor. As an ordained minister entrusted with over \$200,000 for a Wesley Foundation building project at ASU, she had a duty to account for all expenditures. Instead, after the building funds and her salary were commingled in the Account, she withdrew cash and wrote checks for personal expenses over and above her salary, and then provided inadequate documentation or unsubstantiated explanations for expenditures of large sums of money. Such conduct was reckless and a willful neglect of her duty.

Based on the preponderance of evidence, the Conference established that the Debtor's conduct constituted a defalcation while acting in a fiduciary capacity.⁶ A separate final judgment consistent with this Memorandum Opinion will be entered by the Court in accordance with Federal Rules of Bankruptcy Procedure 7054 and 9021. The amount of the judgment will be \$38,850, together with: a) attorney's fees in an amount to be determined at a future evidentiary hearing; b) prejudgment interest at the rate of 10% per annum from February 28, 2003; c) postjudgment interest

⁶ Having found that the debt is not dischargeable as a defalcation while acting in a fiduciary capacity, the Court does not reach a separate conclusion of whether an embezzlement also occurred.

calculated in accordance with 28 U.S.C. §1961 from the date of the entry of this judgment until paid;
and d) all costs of court.

DATED this the 21st day of December, 2006.

/s/ Neil P. Olack
NEIL P. OLACK
UNITED STATES BANKRUPTCY JUDGE