

FILED & ENTERED

MAR 10 2011

CLERK U.S. BANKRUPTCY COURT  
Central District of California  
BY craig DEPUTY CLERK

1  
2  
3  
4  
5  
6  
7  
8 **UNITED STATES BANKRUPTCY COURT**  
9 **CENTRAL DISTRICT OF CALIFORNIA**  
10 **RIVERSIDE DIVISION**

11 In re:

12 Robert Leroy Munson and Kimberly Marie  
13 Munson,

14 Debtor(s),

15 SureTec Insurance Company, a Texas  
16 corporation,

17 Plaintiff(s),

18 Vs.

19 Robert Leroy Munson, an individual and  
20 Debtor, and Kimberly Marie Munson, an  
21 individual and Debtor

22 Defendant(s).

Case No.: 6:10-bk-38482-SC

Adversary No.: 6:11-ap-01060-SC

Chapter: 7

**MEMORANDUM OPINION**

**Hearing Date:**

**Date: March 9, 2011**

**Time: 2:00 p.m.**

**Location: Video Hearing Room 126,  
3240 Twelfth Street, Riverside, CA 92501**

**and**

**Ronald Reagan Federal Building & Court  
House, Courtroom 5C  
411 West Fourth Street  
Santa Ana, CA 92701**

23  
24  
25 **I.**

26 **Summary**

27 This is a motion to dismiss the above-captioned adversary proceeding (the "Motion")  
28 filed by Debtors and Defendants Robert Leroy Munson and Kimberly Marie Munson ("Debtors")

1 or “Defendants”). The adversary proceeding for nondischargeability of debt pursuant to 11  
2 U.S.C. §§523(a)(2) and (a)(4) (the “Complaint”) filed by Plaintiff SureTec Insurance Company,  
3 a Texas corporation (“Plaintiff” or “SureTec”) alleges that the Debtors are the *alter egos* of their  
4 now defunct corporation which operated a commercial plumbing business which participated in  
5 certain public works projects for which Plaintiff issued bonds. After the commercial plumbing  
6 business defaulted on its obligations related to the bonded projects, Plaintiff was required to  
7 pay on claims submitted by third parties pursuant to the bonds. Plaintiff alleges that the  
8 agreement signed by the commercial plumbing business and Defendants created an express  
9 trust with respect to the funds received by the commercial plumbing business relative to the  
10 public works projects, and that, as a result, Defendants had a fiduciary relationship with  
11 Plaintiff, which was breached by the use of the bonded project funds for overhead expenses,  
12 personal payments and the failure to pay suppliers, subcontractors, and laborers.

13 Plaintiff also alleges that Defendants made misrepresentations in connection with the  
14 issuance of the bonds.

## 15 II.

### 16 Factual Background

17 Specifically, the Complaint alleges the following facts:

18 Robert Munson is the president and sole shareholder of a plumbing company, Munson  
19 Plumbing, Inc. (“MPI”) [Complaint, ¶7]. Kimberly Munson was the office manager of MPI  
20 [Complaint, ¶8]. Plaintiff is an issuer of surety bonds.

21 Defendants approached Plaintiff for the issuance of four surety bonds, as follows:

- 22
- 23 a. Subcontract Performance Bond No.4372568 and Subcontract Labor and Material  
24 Payment Bond No. 4372568 (“Arcadia Science Building Bonds”) on behalf of MPI  
25 for its performance of its subcontract with PW Construction, Inc. to provide  
26 plumbing labor and materials for the Arcadia High School New Science Building  
27 project.
  - 28 b. Subcontract Performance Bond No. 4372568 and Subcontract Labor and  
Material Payment Bond No. 4372569 (“Arcadia Student Building Bonds”) on  
behalf of MPI for its performance of its subcontract with PW Construction, Inc. to  
provide plumbing labor and materials for the Arcadia High School Student  
Services Building project.

- 1 c. Subcontract Performance Bond No. 4375085 and Subcontract Labor and  
2 Material Payment Bond No. 4375085 (“Bauchet Storage Bonds”) on behalf of  
3 MPI for its performance of its subcontract with S. J. Amoroso to provide plumbing  
4 labor and materials for the Bauchet Street Storage and Facilities Maintenance  
5 Structure project; and  
6  
7 d. Performance Bond No. 4369970 and Payment Bond No. 4369970 (“Middle  
8 School Bonds”) on behalf of MPI for its performance of its subcontract with the  
9 Cucamonga School District of San Bernardino, CA to provide labor and materials  
10 for the Rancho Cucamonga Middle School Modernization project.

11 [Complaint, ¶14. Copies of the Bonds are attached to the Complaint as Ex. A].

12 As part of the consideration for the issuance of the above referenced bonds (the  
13 “Bonds”), the Defendants and MPI signed a General Agreement of Indemnity (“GAI”)  
14 [Complaint, ¶15, See, Ex. B. to Complaint]. Pursuant to the GAI, Defendants agreed to jointly  
15 and severally indemnify Plaintiff and to deposit collateral with Plaintiff upon demand by  
16 Plaintiff. [Complaint ¶¶16-17]. The GAI contained language that all project funds received by  
17 MPI would be held in trust for the benefit of Plaintiff [Complaint, ¶19]:

18 All monies due and to become due under any contract or contracts covered by bonds  
19 issued by [SureTec] are trust funds, whether in the possession of [Defendants], or  
20 otherwise, for the benefit of and for payment of all obligations for which the Company  
21 would be liable under any of said bonds, which said trust also insures to the benefit of  
22 [SureTec] for any liability or loss it may have or sustain under any of said bonds, and  
23 this Agreement shall constitute notice of said trust.

24 See, also, Ex. A to Complaint, ¶24.

25 Plaintiff has alleged that the Defendants were the *alter egos* of MPI [Complaint, ¶¶11-  
26 13]. MPI failed to complete the four projects, failed to pay several subcontractors, and Plaintiff  
27 began receiving claims on the Bonds. [Complaint, ¶21]. Plaintiff believes that Defendants  
28 received payment funds of at least \$95,053 from S.J. Amoroso on the Bauchet Street Project  
which was not used for related payment obligations and asserts this is just one specific  
example of what appears to be the improper use of funds from the Projects by Defendants.  
[Complaint, ¶23]. Plaintiff believes that Defendants directed the funds from the Projects to be

1 utilized for the payment of non-bonded obligations, including payments to themselves.

2 [Complaint, ¶24].

3 SureTec has paid at least \$436,125.85 covering losses under the Bonds. [Complaint,  
4 ¶25].

5  
6 **III.**

7 **Standards for a Motion to Dismiss**

8 Federal Rule of Civil Procedure Rule 12(b)(6) is made applicable to these proceedings  
9 pursuant to Federal Rule of Bankruptcy Procedure Rule 7012.

10 “A Rule 12(b)(6) motion to dismiss tests the legal sufficiency of a claim.” *Navarro v.*  
11 *Block*, 250 F.3d 729, 732 (9<sup>th</sup> Cir. 2001). “To survive a motion to dismiss, a complaint must  
12 contain sufficient factual matter, accepted as true, to ‘state a claim to relief that is plausible on  
13 its face.’” *Ascroft v. Iqbal*, 129 S.Ct. 1937, 1949 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550  
14 U.S. 544, 570 (2007)). A claim has facial plausibility when the plaintiff pleads factual content  
15 that allows the court to draw the reasonable inference that the defendant is liable for the  
16 misconduct alleged. “The plausibility standard is not akin to a ‘probability requirement,’ but it  
17 asks for more than a sheer possibility that a defendant has acted unlawfully.” *Iqbal*, 129 S.Ct.  
18 at 1949. “Where a complaint pleads facts that are ‘merely consistent with’ a defendant’s  
19 liability, it ‘stops short of the line between possibility and plausibility of entitlement to relief’” *Id.*  
20 (quoting *Twombly*, 550 U.S. at 557).

21 For the purposes of a motion to dismiss, the Court must treat all factual allegations in  
22 the complaint as true, although the Court is “not bound to accept as true a legal conclusion  
23 couched as a factual allegation.” *Iqbal*, 129 S.Ct. at 1950.

24 “While a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need  
25 detailed factual allegations, a plaintiff’s obligation to provide the grounds of entitlement to relief  
26 requires more than labels and conclusions, and a formulaic recitation of the elements of the  
27 cause of action will not do.” *Twombly*, 550 U.S. at 545 (internal quotations omitted).

28 “Determining whether a complaint states a plausible claim for relief... [is] a context-specific  
task that requires the reviewing court to draw on its judicial experiences and common sense.  
But where the well-pleaded facts do not permit the court to infer more than the mere possibility

1 of misconduct, the complaint has alleged -- but it has not “shown” -- that the pleader is entitled  
2 to relief.” *Iqbal*, 129 S.Ct. at 1950.

3 **IV.**

4 **First Cause of Action – 11 U.S.C. § 523(a)(4).**

5 Plaintiff has asserted a claim for nondischargeability of debt pursuant to 11 U.S.C.  
6 §523(a)(4) [Defalcation While Acting in a Fiduciary Capacity With Respect to Project Trust  
7 Funds].

8 Plaintiff alleges that (1) an express trust was created by GAI ¶24, which placed  
9 applicable fiduciary duties upon the Defendants and (2) applicable fiduciary duties upon the  
10 Defendants arose by California statutes (including Business & Professions Code §7108 and  
11 Penal Code §§ 484b, 484c and 506.)

12 Under California law, an express trust is created by acts or words of the trustor which  
13 indicate (1) an intention to create a trust and (2) the subject, purpose, and beneficiary of the  
14 trust. *Abrams v. Crocker-Citizens Nat'l Bank*, 41 Cal.App. 3d 55, 59, 114 Cal. Rptr. 913, 915  
15 (1974). The parties' intent must be ascertained from their words and conduct in light of the  
16 circumstances surrounding the transaction. *Petherbridge v. Prudential Savings & Loan Ass'n*,  
17 79 Cal.App. 3d 509, 516, 145 Cal.Rptr. 87, 93 (1978) (citing *Abrams*, 41 Cal.App. 3d at 59,  
18 114 Cal.Rptr. at 915).

19 The Court has reviewed the allegations with respect to the GAI's ¶24, and the language  
20 of the GAI in its entirety, and finds that as a matter of law, the language contained in the GAI  
21 does not impose fiduciary duties upon the individual Defendants, even though they executed  
22 the GAI. The Complaint “bootstraps” those duties, if any, upon the individual Defendants by  
23 way of the alleged bad acts of the Defendants, the doctrine of *alter ego* or California statutes,  
24 all which arise *ex maleficio*. Indeed, this Court does not need to determine whether a “trust”  
25 was created in the GAI. If a trust was created, it imposed the fiduciary duty obligations on the  
26 corporation, the receiver and disburser of the project funds. The individuals signing the GAI  
27 were creating only a creditor-debtor relationship (and a contingent one at that) between the  
28 Plaintiff and the individuals. They were “indemnifying” the Plaintiff, as the Plaintiff accurately  
indicates in its Complaint.

1 With respect to the allegations contained in the Complaint's ¶¶ 34 to 38, inclusive, that  
2 California law imposes upon the Defendants "an obligation to be fiduciary and hold all funds  
3 from the Projects for the sole purpose of using and applying same to the Projects' obligations"  
4 (Complaint ¶ 34), during oral argument the Plaintiff has acknowledged that *if* any trusts or  
5 fiduciary responsibilities are created because of them, they arise *ex maleficio*, and are  
6 excluded from the application of §523(a)(4). The case law is certain on this result.

7  
8 "Whether a person is a fiduciary under § 523(a)(4) is a question of federal law. *Lewis v.*  
9 *Scott (In re Lewis)*, 97 F.3d 1182, 1185 (9th Cir. 1996) (*citing Ragsdale v. Haller (In re*  
10 *Haller)*, 780 F.2d 794, 795 (9th Cir. 1986)). The origins of the fiduciary capacity  
11 discharge exception date to the Bankruptcy Act of 1841. 5 Stat 440. From 1884 to the  
12 present, courts have construed "fiduciary" in the bankruptcy discharge context as  
13 including express trusts, but excluding trusts *ex maleficio*, i.e., trusts that arose by  
14 operation of law upon a wrongful act. *Davis v. Aetna Corp.*, 293 U.S. 328, 333, 79 L. Ed.  
15 393, 55 S. Ct. 151 (1934); *Chapman v. Forsyth*, 43 U.S. 202, 2 HOW 202, 208, 11 L.  
16 Ed. 236 (1844). We have adhered to this construction in interpreting the scope of 11  
17 U.S.C. § 523(a)(4), refusing to deny discharge to those whose fiduciary duties were  
18 established by constructive, resulting and implied trusts. *Runnion v. Pedrazzini (In re*  
19 *Padrazzini)*, 644 F.2d 756, 758 (9th Cir. 1981); *Schlecht v. Thornton (In re Thornton)*,  
20 544 F.2d 1005, 1007 (9th Cir. 1976)." The core requirements are that the relationship  
21 exhibit characteristics of the traditional trust relationship, and that the fiduciary duties be  
22 created before the act of wrongdoing and not as a result of the act of wrongdoing."  
23 *Runnion*, 644 F.2d at 758.

24 *Blyler v. Hemmeter (In re Hemmeter)*, 242 F.3d 1186, 1189-1190 (9th Cir. Cal. 2001).

25 With respect to the Plaintiff's allegations of *alter ego*, even if ¶24 created fiduciary duties  
26 on the corporation, it is irrelevant. Notwithstanding allegations of *alter ego* which may create  
27 personal liability of corporate debt onto an officer of a corporation, fiduciary duties of a  
28 corporation do not flow to corporate officers simply because of imposition of liability of  
*corporate debt* based on the doctrine of *alter ego*. The general purpose of the doctrine of *alter*  
*ego* is to look through the fiction of the corporation and to hold the individuals doing business  
in the name of the corporation *liable for its debts* in those cases where it should be so held in  
order to avoid fraud or injustice. *D. N. & E. Walter & Co. v. Zuckerman*, 214 Cal. 418 (6 P.2d  
251, 79 A.L.R. 329). *Sequoia Prop. & Equip. Ltd. Pshp. v. United States*, 1998 U.S. Dist.

1 LEXIS 7877 (E.D. Cal. 1998). The doctrine of *alter ego*, at least in California, is a device  
2 imposed by courts to disregard the corporate entity and hold individuals responsible for acts  
3 knowingly and intentionally done in the name of the corporation. *Ivy v. Plyler*, 246 Cal. App. 2d  
4 678, 682 (Cal. App. 5th Dist. 1966). If a finding of *alter ego* were to be considered as imposing  
5 fiduciary duties, any such imposition would be *ex maleficio*, i.e., trusts that arose by operation  
6 of law upon a wrongful act. *Davis v. Aetna Corp.*, 293 U.S. 328, 333, 79 L. Ed. 393, 55 S. Ct.  
7 151 (1934).

8  
9 Accordingly, the Defendants' Motion to Dismiss is granted as to the First Cause of  
10 Action, without leave to amend.

11  
12 **V.**

13 **The Second Cause of Action - 11 U.S.C. §523(a)(2)(A)**

14 Plaintiff has asserted a claim for nondischargeability of debt pursuant to 11 U.S.C.  
15 §523(a)(2)(A) [Fraud].

16 With respect to this Claim, Plaintiff has alleged as follows: Defendants agreed in ¶24 of  
17 the GAI to hold and properly use the bonded project funds, to use all funds for the projects'  
18 obligations and to hold the funds in trust. [Complaint, ¶54]. SureTec issued the Bonds in  
19 reliance of these representations [Complaint, ¶55] and believes that at the time the GAI was  
20 executed, Defendants had "no intention of having payments for the projects used to obligations  
21 under the projects". [Complaint, ¶57]. Defendants "made a knowing decision to conspire and  
22 use the funds from the projects for their personal expenses and other non-project uses."  
23 [Complaint, ¶59]. The extent of the diversion was hidden. [Complaint, ¶60].

24 Based upon the amount of claims and loses experienced by SureTec, it is informed that  
25 Defendants embezzled, defalcated, misappropriated, converted or diverted a sum, subject to  
26 proof, in funds such that they were not used to pay the projects' obligations, but personal and  
27 other non-project expenses. [Complaint, ¶56].

28 Plaintiff argues that it has sufficiently stated a claim under 523(a)(2) because it has  
alleged (1) misrepresentations (2) which the debtor knew at the time were false; (3) made with

1 the intent of deceiving the plaintiff; (4) which plaintiff reasonably relied upon; and (5) plaintiff  
2 sustained losses.

3 Plaintiff argues that pursuant to Rule 9(b) it has placed the debtor on notice of the  
4 precise misconduct he allegedly committed.

5 Plaintiff's allegations, however, do not meet the standards articulated in *Ascroft v. Iqbal*,  
6 129 S.Ct. 1937, 1949 (2009), above.

7 FRCP 9(b) requires fraud to be pled with sufficient particularity to meet the heightened  
8 pleading standard for a fraud claim. See FRCP (9)(b) ("in all averments of fraud . . . the  
9 circumstances constituting fraud . . . shall be stated with particularity."). Moreover, in addition  
10 to pleading requirements pertaining to the "time, place and content of the alleged  
11 misrepresentation [or concealment]," the plaintiff's complaint "must set forth what is false or  
12 misleading about a statement and . . . an explanation as to why the statement or omission  
13 complained of was false or misleading." *Yourish v. Cal. Amplifier*, 191 F.3d 983, 993 n.10 (9th  
14 Cir. 1999); *Rubke v. Capitol Bancorp, Ltd.*, 551 F.3d 1156 (9<sup>th</sup> Cir. 2009). Here, other than  
15 conclusory allegations, which the Court is not required to accept as true, Plaintiff fails to allege  
16 facts supporting a claim pursuant to 11 U.S.C. §523(a)(2)(A). Accordingly, the Defendants'  
17 Motion to Dismiss is granted, with leave to amend.

18 The Court shall enter an Order consistent with its determinations herein.

19  
20 ###

21  
22  
23  
24  
25  
26 

27  
28 DATED: March 10, 2011

United States Bankruptcy Judge



**NOTE TO USERS OF THIS FORM:**

- 1) Attach this form to the last page of a proposed Order or Judgment. Do not file as a separate document.
- 2) The title of the judgment or order and all service information must be filled in by the party lodging the order.
- 3) **Category I.** below: The United States trustee and case trustee (if any) will always be in this category.
- 4) **Category II.** below: List ONLY addresses for debtor (and attorney), movant (or attorney) and person/entity (or attorney) who filed an opposition to the requested relief. DO NOT list an address if person/entity is listed in category I.

**NOTICE OF ENTERED ORDER AND SERVICE LIST**

Notice is given by the court that a judgment or order entitled (*specify*) **MEMORANDUM OPINION** was entered on the date indicated as "Entered" on the first page of this judgment or order and will be served in the manner indicated below:

**I. SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING ("NEF")** – Pursuant to controlling General Order(s) and Local Bankruptcy Rule(s), the foregoing document was served on the following person(s) by the court via NEF and hyperlink to the judgment or order. As of March 9, 2011, the following person(s) are currently on the Electronic Mail Notice List for this bankruptcy case or adversary proceeding to receive NEF transmission at the email address(es) indicated below.

- Arturo Cisneros (TR) amctrustee@mclaw.org, acisneros@ecf.epiqsystems.com
- Helen R Frazer hfrazier@aalrr.com
- Sonia N Linnaus slinnaus@wthf.com, bnavarro@wthf.com
- United States Trustee (RS) ustpregion16.rs.ecf@usdoj.gov

Service information continued on attached page

**II. SERVED BY THE COURT VIA U.S. MAIL:** A copy of this notice and a true copy of this judgment or order was sent by U.S. Mail to the following person(s) and/or entity(ies) at the address(es) indicated below:

Service information continued on attached page

**III. TO BE SERVED BY THE LODGING PARTY:** Within 72 hours after receipt of a copy of this judgment or order which bears an "Entered" stamp, the party lodging the judgment or order will serve a complete copy bearing an "Entered" stamp by U.S. Mail, overnight mail, facsimile transmission or email and file a proof of service of the entered order on the following person(s) and/or entity(ies) at the address(es), facsimile transmission number(s) and/or email address(es) indicated below:

Service information continued on attached page