

1 NOT FOR PUBLICATION

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3
4 UNITED STATES BANKRUPTCY COURT
5 EASTERN DISTRICT OF CALIFORNIA
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7
8 In re

Case No. 12-10802-A-7

9 Terence Edward Moore,

10
11 Debtor.
12 _____/

13 Timothy E. Moore, individually
14 and as trustee of the Edward C. Moore
15 and Marie Moore Family Trust dated
November 12, 1992,

Adv. No. 12-01135-A

16 Plaintiff,

17 vs.

18 Terence Edward Moore,

19 Defendant.
20 _____/

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23 MEMORANDUM DECISION
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This is a dispute between brothers over distributions from their father's trust. Acting as trustee, Terence E. Moore distributed a firearm collection to himself but failed to collect an equalizing payment, as required by the terms of the trust, and appropriated trust stock for his own purposes. Successor trustee Timothy E. Moore proceeds under 11 U.S.C. § 523(a)(4) to recover the value of the assets taken plus prejudgment interest and have that debt be excepted from discharge.

FACTS

Timothy E. Moore ("Timothy"), Terence E. Moore ("Terence"), and Deborah Moore Houston ("Deborah") are the adult children of Edward C. Moore ("Edward"). Plaintiff Timothy is the successor, and current, trustee of his father's inter vivos trust; defendant Terence is the former trustee. The brothers are estranged. All three children are the beneficiaries of "The Edward C. Moore and Marie Moore Family Trust." Marie Moore ("Marie") was Edward's spouse and the siblings' stepmother. This dispute arose from Terence's actions as trustee.

In 1991, Edward and Marie established an inter vivos trust known as "The Edward C. Moore and Marie Moore Family Trust." The original declaration of trust named trustees in the following order of succession: (1) Edward and/or Marie; (2) the survivor of Edward and Marie; and (3) co-trustees comprised of one of Edward's children and one of Marie's children. The initial tertiary trustees were Terence and Jonna M. Key, Marie's daughter; the successor trustees were Timothy and Vern E. Elston, Marie's son.

As relevant here, the trust had a two-pronged distribution scheme. At Edward's death, all of Edward's firearms were to go to Terence, who was to make a one-third equalizing payment to Timothy and

Deborah each:

At the time of Edward C. Moore's death, his gun collection is to be distributed to his son, Terrence E. Moore.¹ Upon distribution of the gun collection, Terrence E. Moore shall pay to both Deborah R. Moore and Timothy E. Moore a cash settlement equal to one-third (1/3) fair market value of the gun collection.

After both settlors passed, the residue of the trust was to be divided evenly between Edward and Marie's combined six children:

The Trustee shall apply and distribute equally the net income and principal of each of the shares of the resulting Trust Estate . . . set aside for the benefit of the Settlor's named beneficiaries as follows: 1) Terrence E. Moore, settlor Edward C. Moore's son[;] 2) Deborah R. Moore, settlor Edward C. Moore's daughter[;] 3) Timothy E. Moore, settlor Edward C. Moore's son[;] 4) Jonna M. Key, settlor Marie Moore's daughter[;] 5) Richard A. Elston, settlor Marie Moore's son[; and] 6) Vern E. Elston, settlor Marie Moore's son[.]

The trust also included an in terrorem clause, which, if triggered, forfeited a contesting beneficiary's interest and terminated the contesting beneficiary's status as trustee:

[I]f any beneficiary hereunder asserts any claim (except a legally enforceable debt), statutory election, or other right or interest against or in Settlor's estate, Settlor's Will, or any properties of this trust, other than pursuant to the express terms hereof or of said Will, or directly or indirectly contests, disputes, or calls into question, before any court, the validity of this instrument or of said Will or the validity of any provisions of this instrument or of said Will, then, a) Such beneficiary shall thereby absolutely forfeit any and all beneficial interests of whatsoever kind and nature which such beneficiary might otherwise have under this instrument and the interests of the other beneficiaries hereunder shall thereupon be appropriately and proportionately increased and/or advanced, . . . and c) Such claiming, electing, or contesting beneficiary, if then acting as a Trustee hereunder, shall automatically cease to be a Trustee and shall thereafter be ineligible either to select, remove, or

¹ In the pleadings and other documents filed in this bankruptcy, the name "Terence" has been used. However, in the trust, the name "Terrence" was used.

1 become a Trustee hereunder.

2 Under the trust, amendments and revocation were authorized during
3 the joint lives of Edward and Marie but not after either of them died.

4 Marie died in 1996, and, notwithstanding the provision precluding
5 amendment after her death, in 1997, Edward executed an amendment to
6 the trust. The amendment purported to make two changes. First,
7 Marie's children were removed as co-trustees, and Terence was named as
8 the sole successor trustee upon Edward's death, with Timothy and
9 Deborah serving as successor trustees if Terence was unwilling or
10 unable to serve as trustee. Second, it altered the distribution
11 scheme. Like the original trust instrument, the amended trust
12 distributed Edward's firearms to Terence with a one-third equalizing
13 payment to Timothy and Deborah:

14 The Trustee shall apply and distribute the net income and
15 principal of each of the shares of the resulting Trust
16 Estate set aside for the benefit of the Trustor's named
17 beneficiaries as follows: The Trustee shall distribute
18 Trustor Edward C. Moore's gun collection to Terrence E.
Moore, Trustor Edward C. Moore's son. Terrence E. Moore
shall repay one third of the fair market value of the gun
collection to Deborah R. Moore and one third of the fair
market value of the gun collection to Timothy E. Moore.

19 But the amendment removed Marie's children from the residuary clause
20 and distributed the corpus of the trust to Terence, Timothy, and
21 Deborah:

22 The Trustee shall distribute the Rest and Residue of the
23 Trust Estate, consisting of the separate property of Edward
24 C. Moore including, but not limited to the family residence
located at 482 E. Cleveland Avenue, Porterville, CA, APN
#253-121-35 and all of Trustor Edward C. Moore's investments
25 to the following named beneficiaries: Terrence E. Moore,
Trustor Edward C. Moore's son[;] Timothy E. Moore, Trustor
26 Edward C. Moore's son[; and] Deborah R. Moore, Trustor
Edward C. Moore's son.

27 It is Trustor Edward C. Moore['s] specific intent that his
28 step-children, namely: Jonna M. Key, Richard A. Elston and

1 Vern E. Elston receive nothing at all from the Trust Estate,
2 since the Trust Estate is all of the separate property of
Edward C. Moore.

3 Edward died in 2006. At his death, his assets included a bank
4 account, a residence, 49 firearms, and 400 shares of Sturm Ruger
5 stock. Immediately upon his father's death, Terence assumed the
6 position of trustee.

7 Within days of his father's death, Terence distributed the
8 firearm collection to himself. He never made an equalizing payment to
9 the trust or to Deborah or Timothy directly.

10 In August 2009, Terence moved the 400 shares of Sturm Ruger stock
11 to his personal brokerage account, sold those shares netting
12 \$4,815.31, and deposited those funds into his personal account.

13 Between 2006 and 2011, on at least eight occasions, Timothy
14 inquired of Terence as to the status of the trust. Terence angrily
15 rebuffed his brother's informal requests for information. He did not
16 prepare accountings in the years 2006 through 2010.

17 In 2011, Timothy commenced proceedings in the Fresno County
18 Superior Court to remove Terence as trustee. Under pressure from his
19 brother, Terence did file an accounting for the trust covering the
20 period from September 16, 2006, through October 31, 2011. It failed
21 to mention either the Sturm Ruger stock or the proceeds. The
22 accounting did show cash distributions to Deborah and Timothy of
23 \$150,000 each and to Terence of \$183,157.75. Notwithstanding the
24 accounting, the Fresno County Superior Court removed Terence as
25 trustee and replaced him with Timothy.

26 In 2012, Terence filed a Chapter 7 bankruptcy. Timothy,

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1 individually and as trustee of the trust,² filed an adversary
2 proceeding under 11 U.S.C. § 523(a)(4), proceeding under a defalcation
3 theory, to recover the value of the equalizing payment for the firearm
4 collection and of the 400 shares of Sturm Ruger stock as
5 nondischargeable debts. The matter was tried in December 2013. In
6 early February 2014, each side filed closing briefs, which raised new
7 issues. Timothy sought to amend his pleadings to conform to proof to
8 additionally recover Terence's disproportionate distributions to
9 himself of \$33,157.75 under the residuary clause and to include
10 prejudgment interest on the damages for Terence's breaches of
11 fiduciary duty. Terence raised the statute of limitations; Timothy's
12 standing, contending that he had triggered the in terrorem clause
13 resulting in his "automatic" removal as trustee; and exemptions. The
14 court invited reply briefs, which were submitted by each side. Final
15 arguments were made in April 2014.

16 JURISDICTION

17 This court has jurisdiction. See 28 U.S.C. §§ 1334, 157(a); 11
18 U.S.C. § 523; General Order No. 182 of the U.S. District Court for the
19 Eastern District of California. This is a core proceeding in which
20 this court may enter final judgment. See 28 U.S.C. § 157(b)(2)(I);
21 *Deitz v. Ford (In re Deitz)*, 469 B.R. 11, 17-24 (B.A.P. 9th Cir. 2012)
22 (holding that dischargeability actions are constitutionally core
23 matters, notwithstanding *Stern v. Marshall*, 131 S. Ct. 2594 (2011)).

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27 ² Both a trustee and a beneficiary may assert a claim for damages
28 on behalf of the trust against a former trustee for breaching the
trust. See Cal. Prob. Code § 16420(a)(3).

1 DISCUSSION

2 I. Procedural Matters

3 A. Amendments to Conform to Proof

4 In certain instances, a party may amend the pleadings to conform
5 to proof. See Fed. R. Civ. P. 15(b), *incorporated by* Fed. R. Bankr.
6 P. 7015.

7 When an issue not raised by the pleadings is tried by the
8 parties' express or implied consent, it must be treated in
9 all respects as if raised in the pleadings. A party may
10 move--at any time, even after judgment--to amend the
11 pleadings to conform them to the evidence and to raise an
12 unpleaded issue.

13 Fed. R. Civ. P. 15(b)(2). Amendment is proper if the nonmoving party
14 consented to trial of the issue and is not be prejudiced by the
15 amendment. *Prieto v. Paul Revere Life Ins. Co.*, 354 F.3d 1005, 1012
16 (9th Cir. 2004); *Gilbane Bldg. Co. v. Fed. Reserve Bank of Richmond*,
17 80 F.3d 895, 901 (4th Cir. 1996). Consent may be express or implied.
18 *Freeman v. Chi. Park Dist.*, 189 F.3d 613, 618 (7th Cir. 1999). "To
19 establish implied consent, the [moving party] must demonstrate that
20 [the nonmoving party] understood evidence had been introduced to prove
21 [the new issue], and that [the new issue] had been directly addressed,
22 not merely inferentially raised by incidental evidence." *LaLonde v.*
23 *Davis*, 879 F.2d 665, 667 (9th Cir. 1989) (citations omitted); see also
24 *Acequia, Inc. v. Clinton (In re Acequia, Inc.)*, 34 F.3d 800, 814 (9th
25 Cir. 1994).

26 In the post-trial briefs and closing arguments, each side raised
27 claims or affirmative defenses not reflected in the pleadings.³
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26 ³ Neither party has moved to amend the pleadings, but a formal
27 motion is not required. *Torry v. Northrop Grumman Corp.*, 399 F.3d
28 876, 879 (7th Cir. 2005). Here, the court treats each side's
arguments on the issue as a motion to amend the pleadings to conform
to proof. See Fed. R. Civ. P. 15(b)(2).

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2 **1. Timothy: Excess Distributions under the Residuary**
3 **Clause⁴**

4 Timothy seeks to include Terence's excess distributions of
5 \$33,157.75 to himself under the residuary clause as an additional
6 defalcation. Because he has not shown that Terence expressly or
7 impliedly consented to trial of this new issue, Timothy's motion to
8 amend the pleadings to conform to proof will be denied. The key is
9 implied consent, which turns on whether Terence understood at the time
10 of trial that a new, previously unpleaded issue was being introduced.
11 At the outset of the trial and in response to inquiries made by the
12 court, the parties narrowly and specifically defined the issues:

13 THE COURT: Do I understand correctly that the portion of the
14 trust that is in play, that has brought us here today, is
15 allegedly 49 guns and 200 shares of Sturm, Ruger and Company
16 stock?

17 MR. KRBECHER [counsel for Timothy]: It's actually 400
18 shares, sir, but it is 49 guns.

19 THE COURT: It is 400 shares?

20 MR. KRBECHER: Yes, sir. That's reflected in the pretrial
21 submissions that we had made.

22 THE COURT: Okay. That's fine. Let me get to Mr. Reich on
23 this in just a second. That's in essence the guts of the
24 problem.

25 . . .

26 THE COURT: Mr. Reich?

27 ⁴ Having pleaded a § 523(a)(4) claim that includes a request for
28 damages, it was unnecessary for Timothy to separately plead a claim
for prejudgment interest. See Fed. R. Civ. P. 54(c) ("Every other
final judgment [besides a default judgment] should grant the relief to
which each party is entitled, even if the party has not demanded that
relief in its pleadings."), incorporated by Fed. R. Bankr. P. 7054(a);
Fed. Sav. & Loan Ins. Corp. v. Tex. Real Estate Counselors, Inc., 955
F.2d 261, 269-70 (5th Cir. 1992) (providing that catch-all prayer for
"any other relief" to which the plaintiff is entitled supports award
of prejudgment interest).

1 MR. REICH [counsel for Terence]: Those are the two issues in
2 front of the Court, the one regarding the guns and the other
regarding the stock.

3 Trial Tr. 11:11-12:4, Dec. 13, 2013, ECF No. 52; see also Trial Tr.
4 55:21-56:5.

5 The linchpin of Timothy's case on the question of
6 disproportionate distributions under the residuary clause is the trust
7 accounting. But when that document was offered, Timothy indicated
8 that it was offered for impeachment purposes. Trial Tr. 123:15-
9 124:26, 125:24-130:26. During trial, the stated purpose for the
10 introduction of the accounting never changed, and the disproportionate
11 distribution was first raised as an additional claim for relief in
12 Timothy's post-trial brief. See Pl.'s Closing Br. 8:1-11:20,
13 Feb. 7, 2014, ECF No. 59. The court finds that since Terence did not
14 understand that the accounting and his testimony adduced thereunder
15 were being offered to also establish an additional instance of
16 defalcation until nearly two months after the evidence closed, Terence
17 did not impliedly consent to trial of the issue.

18 **2. Terence: Statute of Limitations**

19 Similarly, Terence's motion to amend his answer to include the
20 statute-of-limitations defenses described in California Probate Code
21 §§ 16061.8 and 16460(a)(2) is denied. No express consent existed.
22 Moreover, the record lacks support for implied consent. No evidence
23 was offered on the applicability of the statute of limitations, and
24 from that, it follows that Timothy did not understand that Terence was
25 raising an as-of-yet unpleaded issue.

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1 **B. Statute of Limitations**

2 [T]here are two distinct issues to consider in the
3 dischargeability analysis: first, the establishment of the
4 debt itself, which is subject to the applicable state
5 statute of limitations; and, second, a determination as to
6 the nature of that debt, an issue within the exclusive
7 jurisdiction of the bankruptcy court and thus governed by
8 Bankruptcy Rule 4007.

9 *Banks v. Gill Distributions Ctrs., Inc.*, 263 F.3d 862, 868 (9th Cir.
10 2001). A debt barred by the applicable state statute of limitations
11 will not support a dischargeability action. *Id.*

12 Here, Terence contends that Timothy's state law claims that form
13 the basis of the adversary proceeding were time-barred by California
14 Probate Code §§ 16061.8 and 16460(a)(2). The problem is the
15 affirmative defense of the statute of limitations must be pleaded in
16 the answer. Fed. R. Civ. P. 8(c), *incorporated by* Fed. R. Bankr. P.
17 7008. In most instances, an affirmative defense is waived if not
18 pleaded in the answer. *Moore, Owen, Thomas & Co. v. Coffey*, 992 F.2d
19 1439, 1445 (6th Cir. 1993); *Harris v. Sec'y, U.S. Dep't of Veterans*
20 *Affairs*, 126 F.3d 339, 343 (D.C. Cir. 1997). Since Terence did not
21 plead the affirmative defense of statute of limitations, he waived it.

22 **C. Standing and Real Party in Interest**

23 Terence argues that Timothy lacks standing to pursue an action
24 under § 523(a)(4) and, by extension, is not the real party in interest
25 in this action. *See Veal v. Am. Home Mortg. Servicing, Inc. (In re*
26 *Veal)*, 450 B.R. 897, 907 (B.A.P. 9th Cir. 2011); Fed. R. Civ. P.
27 17(a), *incorporated by* Fed. R. Bankr. P. 7017. Terence's argument
28 progresses in three steps. First, Timothy triggered the in terrorem
29 clause by seeking Terence's removal as trustee and by pursuing the
30 § 523(a)(4) adversary proceeding. Second, having triggered the in
31 terrorem clause, Timothy forfeited his status as a beneficiary and his

1 right to serve as trustee. Third, as a result, Timothy is not a
2 "creditor to whom such debt is owed" within the meaning of § 523(c),
3 the provision which describes standing to pursue a § 523(a)(4) action.

4 Terence's argument fails because Timothy has not triggered the in
5 terrorem clause. Except as otherwise provided by law, in terrorem, or
6 no-contest, clauses are enforceable against a beneficiary "who brings
7 a contest within the terms of the no contest clause." Cal. Prob. Code
8 § 21303.⁵ Such clauses are strictly construed. Cal. Prob. Code
9 § 21304. In this case, the in terrorem clause is only activated by
10 the assertion of a claim (1) against the estate, will, or properties
11 of the trust, "other than pursuant to the express terms [of the trust
12 or will];" or (2) disputing the validity of the trust or will. Here,
13 Timothy's actions in seeking Terence's removal and pursuing this
14 adversary proceeding are not against the trust, will, or trust
15 properties, nor do they seek to invalidate the trust or will. Rather,
16 these are acts against Terence, occasioned by his failure to follow
17 the express terms of the trust. Moreover, the no-contest clause
18 specifically excepts from its reach claims asserted pursuant to its
19 express terms. In this case, Timothy's adversary proceeding seeks to
20 enforce the beneficiaries' interests as defined by the trust's express
21 terms. As a result, Timothy has not triggered the no-contest clause,
22 and Terence's argument fails.

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25 ⁵ A no-contest clause is governed by Part 3 of Division 11 of the
26 California Probate Code. Because the trust at issue became
27 irrevocable before January 1, 2001, the current version of Part 3,
28 containing California Probate Code §§ 21310-21315, does not apply.
See Cal. Prob. Code § 21315(b). Instead, the trust is governed by the
former, now-repealed version of Part 3, which was previously
enumerated at California Probate Code §§ 21300-21308, 21320-21322.
See *Fazzi v. Klein*, 190 Cal. App. 4th 1280, 1283 n.2 (2010).

II. Nondischargeability

A. Legal Standards

Bankruptcy Code § 523(a)(4) excepts from discharge debts for "defalcation while acting in a fiduciary capacity." To except such a debt from discharge, a creditor must prove by a preponderance of the evidence, see *Lovell v. Stanifer (In re Stanifer)*, 236 B.R. 709, 713 (B.A.P. 9th Cir. 1999), that "1) an express trust existed, 2) the debt was caused by . . . defalcation, and 3) the debtor acted as a fiduciary to the creditor at the time the debt was created," *Otto v. Niles (In re Niles)*, 106 F.3d 1456, 1459 (9th Cir. 1997) (quoting *Klingman v. Levinson*, 831 F.2d 1292, 1295 (7th Cir. 1987) (citing cases)), *abrogated on other grounds, Bullock v. BankChampaign, N.A.*, 133 S. Ct. 1754 (2013). Once the creditor has done so, the burden shifts to the debtor to render an accounting. *Id.* at 1462; see also *Pemstein v. Pemstein (In re Pemstein)*, 492 B.R. 274, 280 (B.A.P. 9th Cir. 2013). Terence conceding the first and third elements of *Klingman*, the only issue is defalcation.

Defalcation itself has two elements: The act of defalcation and the wrongful intent. The act of defalcation includes misappropriating trust assets or by failing to account for such assets. *Blyler v. Hemmeter (In re Hemmeter)*, 242 F.3d 1186, 1190 (9th Cir. 2001) (citing *Lewis v. Scott (In re Lewis)*, 97 F.3d 1182, 1186 (9th Cir. 1996)). A fiduciary also commits defalcation by using trust property in a manner inconsistent with the duties and obligations imposed by the trust. See *Lovell*, 236 B.R. at 719 (holding that a debtor's violation of the legal duties and obligations under a trust created under both statute and case law constituted a defalcation under § 523(a)(4)).

Wrongful intent requires a culpable state of mind "involving

1 knowledge of, or gross recklessness in respect to, the improper nature
2 of the relevant fiduciary behavior." *Bullock*, 133 S. Ct. at 1757.
3 Reckless conduct qualifies as the equivalent of "actual knowledge of
4 wrongdoing." *Id.* at 1759. A fiduciary's conduct is reckless "if the
5 fiduciary 'consciously disregards' (or is willfully blind to) 'a
6 substantial and unjustifiable risk' that his conduct will turn out to
7 violate a fiduciary duty." *Id.* (quoting Model Penal Code § 2.02(2)(c)
8 (1985)). "That risk 'must be of such a nature and degree that,
9 considering the nature and purpose of the actor's conduct and the
10 circumstances known to him, its disregard involves a *gross deviation*
11 from the standard of conduct that a law-abiding person would observe
12 in the actor's situation.'" *Id.* at 1760 (quoting Model Penal Code
13 § 2.02(2)(c)).

14 **B. Firearm Collection Equalizing Payment**

15 Timothy has sustained his burden of proof on the issue of
16 defalcation with respect to the equalizing payment for the firearm
17 collection. "If a trust has two or more beneficiaries, the trustee
18 has a duty to deal impartially with them and shall act impartially in
19 investing and managing the trust property, taking into account any
20 differing interests of the beneficiaries." Cal. Prob. Code § 16003.
21 To the same effect, "[t]he trustee shall administer the trust with
22 reasonable care, skill, and caution under the circumstances then
23 prevailing that a prudent person acting in a like capacity would use
24 in the conduct of an enterprise of like character and with like aims
25 to accomplish the purposes of the trust as determined from the trust
26 instrument." Cal. Prob. Code § 16040.

27 Here, the trust required Terence, as the beneficiary, to make an
28 equalizing payment of two-thirds of the value of the firearms in

1 exchange for their receipt and also required Terence, as the trustee,
2 to collect that payment on behalf of the other beneficiaries:

3 The Trustee shall distribute Trustor Edward C. Moore's gun
4 collection to Terrence E. Moore, Trustor Edward C. Moore's
5 son. Terrence E. Moore shall repay one third of the fair
6 market value of the gun collection to Deborah R. Moore and
one third of the fair market value of the gun collection to
Timothy E. Moore.

7 As trustee, Terence distributed the gun collection to himself, the
8 beneficiary, without collecting the equalizing payment, which violated
9 his duties of impartiality and prudence.

10 Terence had actual knowledge that his conduct with respect to the
11 firearm collection was improper. *Bullock*, 133 S. Ct. at 1757 (stating
12 that culpable state of mind includes "knowledge of . . . the improper
13 nature of the relevant fiduciary behavior"). Most importantly,
14 Terence knew that the terms of the trust obligated him to collect a
15 payment of two-thirds the value of the firearms collection in exchange
16 for the firearms collection. And Terence, as the trustee, knew that
17 he, as the beneficiary with the payment obligation, had the ability to
18 make this payment. He received the guns within a few days of Edward's
19 death on September 16, 2006. By his own estimate, the high iteration
20 of the fair market value of the collection was \$17,186, making the
21 equalizing payment \$11,457.33. His accounting shows that on September
22 20, 2006, he received \$75,000 from his father's estate. In the five
23 years following his father's death, Terence received a total of
24 \$183,157.75 in cash from his father's estate. Despite knowing that he
25 had the means to make the equalizing payment, Terence, as the trustee,
26 never attempted to collect the equalizing payment on behalf of the
27 other beneficiaries. Knowledge of the obligation, the passage of
28 time, and knowledge of his ability to perform give rise to the

1 inference that Terence made a conscious decision to violate his
2 fiduciary duties.

3 Further facts showing actual knowledge that his actions were
4 improper include Terence's delayed administration of the trust for
5 more than five years coupled with refusal to provide information to
6 Timothy when asked. During that time, his brother Timothy made
7 informal requests for information eight times. In response, he was
8 told "[i]t was none of [his] ***** [expletive deleted] business" and
9 "It's none of your business. I'm handling it. There's nothing you
10 need to know. I'm the trustee. I'll get around to it. I haven't
11 done that yet." Trial Tr. 142:5-13. Until forced to do so by his
12 brother, Terence failed to file an accounting for the estate, from
13 which third parties could have detected the failure to collect the
14 equalizing payment. The refusal to provide information suggests that
15 Terence was attempting hide his refusal to perform.

16 The court finds that Terence knew of his obligations under the
17 trust and knew that his failure to collect the equalizing payment from
18 himself was improper but made a conscious decision not to do so. As a
19 result, Terence committed a defalcation with respect to the equalizing
20 payment for the firearm collection.

21 **C. 400 Shares of Sturm Ruger Stock**

22 Timothy has sustained his burden of proof on the issue of
23 defalcation with respect to the 400 shares of Sturm Ruger stock.
24 Terence breached his fiduciary duty by moving the Sturm Ruger stock
25 from his father's account to his own, selling it, and retaining the
26 proceeds. See Cal. Prob. Code § 16003 (duty of impartiality).
27 Unlike the firearm collection, the stock was governed by the residuary
28 clause. The conversion of trust assets, which should have been

1 divided between all three sibling beneficiaries, to Terence's own
2 personal use is a breach of his fiduciary duties.

3 Terence's actions show that at the very least he consciously
4 disregarded a substantial and unjustifiable risk that retention of the
5 stock proceeds violated his fiduciary duty--and probably had actual
6 knowledge that retention of the proceeds was improper. This is well
7 demonstrated by these facts. At the outset, the residuary clause of
8 the trust specifically and unequivocally provides that the stock, not
9 otherwise provided for in the trust, should have passed to each of the
10 residuary beneficiaries. Terence admits reading each document dozens
11 of times, from which he is charged with knowledge of their terms.
12 Further, the appropriation of trust assets for personal use, without
13 sufficient explanation, is a gross deviation from the conduct a law-
14 abiding person would observe. That Timothy was unaware of the
15 existence of the stock suggests a greater than ordinary chance that
16 the appropriation would not be detected. As with the equalizing
17 payment for the firearm collection, Terence refused to provide
18 information for five years and when the accounting was filed it
19 omitted the Sturm Ruger stock. These facts suggest an intention to
20 hide the transaction and, from that, a knowledge of its impropriety.
21 For each of these reasons, the court finds that Terence knew of his
22 obligations under the trust and knew that his appropriation of the
23 stock was improper. As a result the burden of proof shifts to Terence
24 to render an accounting. *Otto*, 106 F.3d at 1462; *see also Pemstein*,
25 492 B.R. at 280.

26 But Terence has not sustained his burden. He suggests the stock
27 was sold to reimburse himself for expenses. Yet, the only accounting
28 he has provided is, by his own words, incomplete and inaccurate.

Moreover, the court finds this explanation not credible in light of the trust's other cash assets.

As a result, Timothy has carried his burden of proof establishing Terence's defalcation in failing to collect the equalizing payment for the firearm collection and misappropriating the 400 shares of Sturm Ruger stock.

III. Damages

A. Legal Standards

In a § 523(a)(4) action, the amount of the nondischargeable debt (i.e., the damages) is determined by state law. See *Roussos v. Michaelides (In re Roussos)*, 251 B.R. 86, 93 (B.A.P. 9th Cir. 2000), *aff'd*, 33 F. App'x 365 (9th Cir. 2002). Under California law, a trustee who commits a breach of trust is typically liable for the "loss or depreciation in value of the trust estate resulting from the breach of trust." Cal. Prob. Code § 16440(a)(1).

Prejudgment interest may also be awarded. See *Cobe v. Smith (In re Cobe)*, 229 B.R. 15, 18 (B.A.P. 9th Cir. 1998) (citing *Cohen v. de la Cruz*, 523 U.S. 213, 218-23 (1998)). "In the context of a § 523(a)(4) proceeding, it has been held [by the Ninth Circuit] that it is proper for the bankruptcy court to apply state law to calculate prejudgment interest into the amount of the nondischargeable debt." *Roussos*, 251 B.R. at 94 (emphasis added) (citing *Otto*, 106 F.3d at 1463); *accord Otto*, 106 F.3d at 1463 ("Because the debt the court found to be nondischargeable arose under state law, the award of prejudgment interest on that debt is also governed by state law." (citation omitted)). California law provides for interest at 10% per annum. See Cal. Prob. Code §§ 16440(a)(1), 16441(a)(1); Cal. Civ. Proc. Code § 685.010(a); *Uzyel v. Kadisha*, 188 Cal. App. 4th 866, 921

(2010). Interest "begins to accrue on the date of the loss or depreciation in value," *Uzyel*, 188 Cal. App. 4th at 923 n.42, and continues to accrue even after the petition is filed, see *Foster v. Bradbury (In re Foster)*, 319 F.3d 495, 497 (9th Cir. 2003) (per curiam) (nondischargeable child support debt); *Ward v. Bd. of Equalization (In re Artisan Woodworkers)*, 204 F.3d 888, 891-92 (9th Cir. 2000) (nondischargeable tax debt); *Great Lakes Higher Educ. Corp. v. Pardee (In re Pardee)*, 218 B.R. 916, 921 (B.A.P. 9th Cir. 1998) (nondischargeable student loan debt), *aff'd*, 193 F.3d 1083 (9th Cir. 1999). Thus, prejudgment interest in a nondischargeability proceeding is calculated through the date of judgment. See *DeVries v. Clark (In re Clark)*, Bankr. No. 12-00649-TLM, Adv. No. 13-06034-TLM, 2014 WL 174935, at *5 (Bankr. D. Idaho Jan. 10, 2014).

B. Firearm Collection Equalizing Payment

As to the equalizing payment for the firearm collection, the trust provides for two-thirds of the fair market value of the collection. The court believes that term is defined by the fair market retail value, after discounting the firearms for condition but without costs of sale, and determines that amount to be \$17,186. As a result, the two-thirds payment due to Timothy, as trustee, is \$11,457.33. Interest on this amount is \$8,989.82.⁶ As a result, the aggregate due for the defalcation with respect to the firearm collection equalizing payment is \$20,447.15.

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⁶ On the debt owed with respect to the equalizing payment, interest accrues at a rate of \$3.14 a day (\$11,457.33 principal x 10% annual interest rate ÷ 365 days). Interest accrues from September 16, 2006, through July 18, 2014, or 2,863 days. As of July 18, 2014, the total amount of prejudgment interest is \$8,989.82 (\$3.14 daily interest x 2,863 days).

