



**IT IS ORDERED as set forth below:**

**Date: January 09, 2009**

**Paul W. Bonapfel  
U.S. Bankruptcy Court Judge**

**UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF GEORGIA  
ATLANTA DIVISION**

IN THE MATTER OF:	:	CASE NUMBER: A07-67780-PWB
	:	
JEREMY MICHAEL BLACK	:	
and WENDY DAWN BLACK,	:	
	:	IN PROCEEDINGS UNDER
	:	CHAPTER 7 OF THE
Debtors.	:	BANKRUPTCY CODE
	:	
_____	:	
KENDALL ELECTRIC, INC.,	:	
	:	
Plaintiff	:	
	:	
v.	:	ADVERSARY PROCEEDING
	:	NO. 07-6409
JEREMY MICHAEL BLACK	:	
and WENDY DAWN BLACK,	:	
	:	
Defendants.	:	

**ORDER DENYING MOTION FOR SUMMARY JUDGMENT**

The Plaintiff seeks a determination that a default judgment it obtained against the

Debtors and Black Electric, Inc., is excepted from discharge pursuant to 11 U.S.C. § 523(a)(4). For reasons stated herein, the Plaintiff's motion for summary judgment is denied.

On or about December 6, 2006, the Plaintiff commenced an action against the Debtors and Black Electric, Inc., a Michigan corporation of which the Debtors were officers, in the 37<sup>th</sup> Judicial Circuit Court for Calhoun County, Michigan (the "Michigan Action"). The Plaintiff sued Black Electric for the amount due on an open account and the Debtors on their guaranty of Black Electric's debt. In addition, the Plaintiff alleged that Black Electric and the Debtors were liable to the Plaintiff under the Michigan Building Contract Fund Act, M.C.L. § 570.151, *et seq* (the "MBCFA"), under the theory that Black Electric, as trustee of funds to be used for a building project, owed the Plaintiff a fiduciary duty to pay the trust funds to the Plaintiff for the materials supplied by the Plaintiff to the building project. Further, the Plaintiff alleged in the Michigan Action that the Debtors, as officers and directors of Black Electric with dominion and control over Black Electric's payments, were personally liable under the MBCFA.

On March 9, 2007, the Michigan court entered a default judgment in favor of the Plaintiff against the Debtors and Black Electric in the amount of \$20,580.90. The judgment provides the following "other conditions" to the judgment:

Judgment is granted against the Defendants, BLACK ELECTRIC, INC. & WENDY D. BLACK & JEREMY BLACK, Individually, for the full amount outlined above. Also, Judgment is entered on Count II of the Plaintiff's Complaint & the Builder's Trust Fund Act has been pled as violated & is determined to have been violated. The relief of this Judgment is not different in kind nor does it [sic] exceed the amount of relief demanded in the Complaint.

The Plaintiff contends that the March 9, 2007 judgment should be given collateral estoppel effect in this dischargeability proceeding. The Plaintiff contends that the application of collateral estoppel, or issue preclusion, with respect to the judgment on the MBCFA count renders its debt excepted from discharge pursuant to 11 U.S.C. §523(a)(4) as a matter of law. The Debtors have filed no response to the Plaintiff's motion for summary judgment.

Section 523(a)(4) excepts from discharge any debt "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny ." 11 U.S.C. § 523(a)(4). In order for a debt to be nondischargeable based upon defalcation while acting in a fiduciary capacity, the debtor must have stood in a fiduciary relationship with the creditor alleging nondischargeability of the debt; the fiduciary relationship must have existed prior to the creation of the debt; and the debt must have resulted from some act of fraud or defalcation by the debtor. *Quaif v. Johnson*, 4 F.3d 950, 953-955 (11th Cir. 1993). Thus, the Court must determine whether the issues determined by the default judgment, satisfy the requirements of a § 523(a)(4) defalcation claim.

The doctrine of issue preclusion prevents the relitigation of any issue that was necessarily adjudicated in rendering the prior judgment. The Supreme Court has recognized that issue preclusion applies in dischargeability litigation. *Grogan v. Garner*, 498 U.S. 279 (1991). When determining the preclusive effect of a state court judgment in dischargeability litigation, it is unsettled whether a bankruptcy court must apply state or federal issue preclusion law. *See Colorado West Trans. Co., Inc. v. McMahon (In re McMahon)*, 356 B.R. 286 (Bankr. N.D. Ga. 2006), *rev'd and remanded*, 380 B.R. 911 (N.D. Ga. 2007). In this case, the threshold issue is whether Michigan law or federal law would give issue preclusive effect to a default judgment entered in the prior proceeding. Whether a default judgment is "actually litigated" is a

determinative factor.

In *Vogel v. Kalita (In re Kalita)*, 202 B.R. 889, 913 (Bankr. W.D. Mich. 1996), the bankruptcy court engaged in a thorough review of the decisions of Michigan courts and federal courts applying Michigan law on collateral estoppel. The *Kalita* court concluded that a default judgment has preclusive effect if there was sufficient participation by the parties. For example, where the parties have engaged in discovery or where the debtor has filed an answer and later abandoned the case, the resulting default judgment is entitled to preclusive effect. However, the *Kalita* court confirmed, in the event of a “true default,” where no answer has been filed by a defendant, Michigan courts do not give preclusive effect to a default judgment in a later proceeding. *Kalita*, 202 B.R. at 913-915. *Kalita*’s analysis has been cited with approval by other Michigan bankruptcy courts. See *Building Communications, Inc. v. Rahaim (In re Rahaim)*, 324 B.R. 29 (Bankr. E.D. Mich. 2005); *Universal Underwriters Group v. Allen (In re Allen)*, 243 B.R. 683 (Bankr. E.D. Mich. 1999); *contra, Micco Construction Co. v. Brunett (In re Brunett)*, 394 B.R. 425 (Bankr. E.D. Mich. 2008).

Application of the federal law of issue preclusion to a true default judgment leads to the same result. See *Colorado West Trans. Co., Inc. v. McMahon (In re McMahon)*, 356 B.R. 286, 301 (Bankr. N.D. Ga. 2006), *rev’d and remanded*, 380 B.R. 911 (N.D. Ga. 2007) (discussing “countervailing statutory policy” of § 523(c) which would except default judgments in dischargeability litigation from the operation of 28 U.S.C. § 1738).

In the instant case, there is no evidence as to the basis for entry of default judgment in the Michigan case. The fact that only three months elapsed between the filing of the complaint and the entry of default suggests that this is a “true default” situation. Because the Court cannot

conclude that it is anything but a true default, and because neither Michigan law nor federal law would give preclusive effect to a default judgment based on a true default, the Plaintiff's default judgement is not entitled to preclusive effect in this dischargeability proceeding.

Because the Court concludes that the default judgment is not entitled to preclusive effect, the Court must determine whether the Plaintiff has nevertheless established sufficient facts to support a finding that its debt is excepted from discharge under § 523(a)(4).

The Plaintiff contends that the Debtors' violation of the MBCFA constitutes an act of defalcation by the Debtors in their fiduciary capacity as trustees of the building trust fund and their failure to pay the debt of the Plaintiff, a materialman and beneficiary of the trust.

The MBCFA, M.C.L. § 570.151, provides:

In the building construction industry, the building contract fund paid by any person to a contractor, or by such person or contractor to a subcontractor, shall be considered by this act to be a trust fund, for the benefit of the person making the payment, contractors, laborers, subcontractors or materialmen, and the contractor or subcontractor shall be considered the trustee of all funds so paid to him for building construction purposes.

The MBCFA imposes a duty upon the contractor receiving the payments to act as trustee "to use the money in the building contract fund to first pay laborers, subcontractors and materialmen on the particular project for which the funds were deposited before he uses the fund for any other purpose." *In re Johnson*, 691 F.2d 249, 252 (6<sup>th</sup> Cir. 1982). The trust *res* is the funds paid by a person to the contractor into the building contract fund. *Id.* Bankruptcy courts have concluded that when a debtor violates the MBCFA in his capacity as a contractor and fiduciary of the building contract fund, the resulting debt may be nondischargeable pursuant to 11 U.S.C.

§ 523(a)(4). See *In re Kriegish*, 275 B.R. 838 (E.D. Mich. 2002); *In re Little*, 163 B.R. 497 (Bankr. E.D. Mich. 1994).

Thus, in order for this transaction to fall within the coverage of the MBCFA, the following elements must be present: (1) funds must have been paid by persons to the Debtors; (2) for building construction purposes; and (3) a debt was owed by the Debtors to the Plaintiff.

The fiduciary relationship recognized by the MBCFA is not inherent in building construction transactions. Instead, it arises only “at the time any monies are paid to the contractor or subcontractor whether or not there are any beneficiaries of the trust at that time and continues until all of the trust beneficiaries have been paid.” *Johnson*, 691 F.2d at 253. However, the *Johnson* court also emphasizes, “Until some person makes a payment into the building contract fund, the contractor or subcontractor is liable to suppliers and laborers solely based on contract.” *Id.*

The Plaintiff alleges in its Statement of Material Facts [Doc. 8] that “Black Electric, Inc. has used the product supplied by Plaintiff in a building construction project” (¶ 4) and that “Black Electric, Inc., has received funds from the owner or contractor for the project for the material costs associated with the project.” (¶ 5). However, the Plaintiff has pointed to no evidence in the record to establish that funds were paid by an owner to the Debtors that would constitute a building construction fund for purposes of the MBCFA. See *Hairston v. Gainesville Sun Pub. Co.*, 9 F.3d 913, 918 (11<sup>th</sup> Cir. 1993) (“The party seeking summary judgment bears the initial burden to demonstrate to the [trial] court the basis for its motion for summary judgment and identify those portions of the pleadings, depositions, answers to interrogatories, and admissions which it believes

show an absence of any genuine issue of material fact.”).<sup>1</sup>

The Debtors denied these allegations in the complaint. (Answer, ¶ 11). The Debtors have not contested the allegations in response to the motion for summary judgment by disputing the Plaintiff’s statement of material facts, but the Court cannot enter summary judgment merely because the motion was unopposed; rather, the Court must consider whether there is an evidentiary basis for the motion. *United States v. One Piece of Real Property Located at 5800 SW 74<sup>th</sup> Ave., Miami, Florida*, 363 F.3d 1099, 1101-1102 (11<sup>th</sup> Cir. 2004). Because the critical element that funds were paid by an owner to the Debtors that would constitute a building construction fund for purposes of the MBCFA has not been shown, the Court cannot conclude at this time that this is a trust fund debt, as opposed to a debt owed by the Debtors to the Plaintiff based solely on contract. See *Johnson*, 691 F.2d at 253. Accordingly, summary judgment is inappropriate.

Because the Michigan default judgment is not entitled to preclusive effect and because the Plaintiff has not otherwise demonstrated that its debt is one which is encompassed by the Michigan Building Contract Fund Act, the Court concludes that the Plaintiff is not entitled to summary judgment. The Court shall schedule this matter for a status conference as set forth herein. It is

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<sup>1</sup>The affidavit of Judith Gates [Doc. 12], an employee and agent of the Plaintiff, states that the Plaintiff supplied electrical products and supplies to Black Electric on a credit line open account. She further states that Black Electric would designate the name and/or address of the party for whom Black Electric was performing its services. Attached to the affidavit is a statement of the unpaid orders on the account which lists the invoice date, invoice number, the customer identification or address (presumably identified by Black Electric), and the rolling balance owed to the Plaintiff. This information, however, does not establish the creation of building contract funds for any of the parties identified by Black Electric.

ORDERED that the Plaintiff's motion for summary judgment is denied. It is

FURTHER ORDERED that the Court shall hold a status conference on February 3, 2009, at 11:00 a.m., in Courtroom 1401, U.S. Courthouse, 75 Spring Street, S.W., Atlanta, Georgia.

End of Order

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