

NOT FOR PUBLICATION

JUN 10 2013

SUSAN M SPRAY, CLERK
U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT

In re:) BAP No. EC-12-1163-MkDJu
)
 JOHN ERNEST BORSOS and) Bk. No. 10-53374
 CLARE HART BORSOS,)
)
 Debtors.) Adv. No. 11-02183
)
)
 JOHN ERNEST BORSOS,)
)
 Appellant,)
)
 v.) **MEMORANDUM***
)
 UNITED HEALTHCARE WORKERS-WEST,)
)
 Appellee.)
)

Argued and Submitted on March 22, 2013
at Sacramento, California

Filed - June 10, 2013

Appeal from the United States Bankruptcy Court
for the Eastern District of California

Honorable Christopher M. Klein, Chief Bankruptcy Judge, Presiding

Appearances: Daniel M. Siegel of Siegel & Yee argued for
appellant John E. Borsos; Jeffrey B. Demain of
Altshuler Berzon LLP argued for appellee United
Healthcare Workers-West.

Before: MARKELL, DUNN and JURY, Bankruptcy Judges.

*This disposition is not appropriate for publication.
Although it may be cited for whatever persuasive value it may
have (see Fed. R. App. P. 32.1), it has no precedential value.
See 9th Cir. BAP Rule 8013-1.

1 **INTRODUCTION**

2 Before his removal from office on January 27, 2009, John
3 Borsos ("Borsos") was an elected officer and employee of United
4 Healthcare Workers West ("UHW"). A jury verdict rendered in
5 federal district court found Borsos and others liable for
6 diverting UHW resources for non-UHW purposes, and on April 12,
7 2010, the district court entered judgment against Borsos in the
8 amount of \$66,600. Later that same year, in December 2010,
9 Borsos filed a chapter 7¹ bankruptcy case. UHW then filed a
10 nondischargeability complaint against Borsos under § 523(a)(4).
11 Based primarily on the district court jury's findings, the
12 bankruptcy court held after trial that the district court
13 judgment debt arose from a fiduciary defalcation excepted from
14 discharge under § 523(a)(4). Borsos appealed.

15 During the pendency of this appeal, the United States
16 Supreme Court ("Supreme Court") decided Bullock v. BankChampaign,
17 N.A., 133 S.Ct. 1754 (2013). In Bullock, the Supreme Court
18 interpreted § 523(a)(4) defalcation as requiring a specific
19 subjective state of mind. Bullock's scienter requirement
20 effectively abrogated Ninth Circuit law, which formerly did not
21 require any particular state of mind to except a debt from
22 discharge based on a § 523(a)(4) fiduciary defalcation.

23 Following now-abrogated Ninth Circuit law, the bankruptcy
24 court did not make any findings regarding Borsos' state of mind.

26 ¹Unless specified otherwise, all chapter and section
27 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532.
28 All "Civil Rule" references are to the Federal Rules of Civil
Procedure.

1 Consequently, we must VACATE AND REMAND so the bankruptcy court
2 can make further findings.

3 **FACTS²**

4 This appeal is one skirmish in a larger battle between the
5 Service Employees International Union ("SEIU") and the former
6 management of UHW. SEIU is a large international labor union,
7 and UHW has been a local SEIU affiliate since the 1930's.³

8 Over the last several years, SEIU and former UHW management
9 ("Former UHW Management") have increasingly disagreed on various
10 policy and organizational matters. These disagreements
11 ultimately came to a head in January 2009, when Former UHW
12 Management refused to cooperate with the SEIU-ordered transfer of
13 65,000 UHW members to a different local SEIU affiliate.⁴

14 That refusal to cooperate was the impetus for SEIU's
15 appointment of a trusteeship on January 27, 2009, to take over
16 the management of all of UHW's affairs. The transition of
17 control to the trusteeship did not occur in a peaceful or orderly
18 manner. As Former UHW Management left their offices upon being
19

20 ²There is little dispute over the basic facts relevant to
21 this appeal. As the bankruptcy court indicated, the real dispute
22 is over what those facts demonstrate in terms of the
dischargeability of UHW's judgment against Borsos.

23 ³Some of the facts set forth herein are drawn from Serv.
24 Employees Int'l Union v. Nat. Union of Healthcare Workers,
25 598 F.3d 1061 (9th Cir. 2010) ("SEIU v. NUHW"). Others are drawn
from the District Court's preliminary injunction order, which was
the order on appeal in SEIU v. NUHW.

26 ⁴The stated purpose of the transfer was to consolidate all
27 California long-term healthcare workers who were members of
28 various local SEIU affiliates into a single local affiliate
dedicated exclusively to long-term healthcare workers.

1 relieved of their duties, UHW stewards and rank-and-file UHW
2 members barricaded themselves in the union offices to protest and
3 resist the trusteeship. As a net result of this transition, key
4 union records and other union assets were misplaced, removed
5 and/or destroyed.

6 The day after the appointment of the trusteeship, Former UHW
7 Management took the next step in their campaign to resist SEIU's
8 initiatives, and SEIU took the next step in its campaign to quell
9 that resistance. Former UHW Management formally resigned their
10 membership in UHW and announced the formation of a rival union
11 known as the National Union of Healthcare Workers ("NUHW").
12 Meanwhile, SEIU filed a complaint ("District Court Complaint")
13 against Former UHW Management and NUHW in the United States
14 District Court for the Northern District of California (Case
15 No. C-09-00404). That complaint stated claims for the following
16 relief: (1) injunctive relief, (2) breach of fiduciary duty under
17 the Employee Retirement Income Security Act ("ERISA"), (3) breach
18 of fiduciary duty under the Labor-Management Reporting and
19 Disclosure Act of 1959 ("LMRDA"), (4) breach of contract,
20 (5) breach of fiduciary duty under California law, (6) specific
21 recovery of certain materials (including records, data, notes,
22 blueprints, etc.) allegedly wrongfully taken from UHW, and
23 (7) misappropriation of trade secrets under California law.

24 While the District Court Complaint covered much ground, by
25 the time the trial was completed and the matter submitted to the
26 jury for decision, the focus of the litigation had been
27 significantly refined. In relevant part, the final charge to the
28 jury ("Jury Instructions") instructed the jury to determine the

1 liability of the individual defendants, all Former UHW
2 Management, for "diversion of resources" and "salary and
3 benefits" during January 2009, up until the time they were
4 removed from or resigned their positions as UHW officials.

5 The Jury Instructions directed the jury to impose
6 diversion of resources liability to the extent each defendant
7 used UHW-resources for non-UHW purposes, measured by the value of
8 the resources diverted. See Jury Instructions (April 6, 2010) at
9 10:2-7.

10 In addition, the Jury Instructions directed the jury to
11 impose salary and benefits liability to the extent each defendant
12 was in breach of his or her fiduciary duties during January 2009.
13 In imposing salary and benefits liability, the Jury Instructions
14 in essence called upon the jury to ascertain what proportion of
15 each defendant's January 2009 work time was diverted to non-UHW
16 purposes and to assess damages equal to the value of the diverted
17 work time, using each defendant's January 2009 salary and
18 benefits as a measure. See Jury Instructions (April 6, 2010) at
19 9:18-27; see also id. at 6:18-7:27 (identifying the fiduciary
20 duties the defendants owed to UHW).

21 Based on the Jury Instructions, the jury rendered a verdict
22 finding many of the individual defendants, including Borsos,
23 liable for diversion of resources and for salary and benefits.
24 However, the jury's verdict and the Jury Instructions indicate
25 that the jury was not required to consider, and did not consider,
26 the mental state of any of the defendants in diverting UHW
27 resources and work time to non-UHW purposes.

28 The jury found Borsos individually liable in the amount of

1 \$60,000 for diversion of resources liability and in the amount of
2 \$6,600 for salary and benefits liability, for a total liability
3 in the amount of \$66,600. On April 12, 2010, the district court
4 entered judgment against Borsos in that amount based on the
5 jury's verdict.⁵

6 Borsos thereafter filed his chapter 7 bankruptcy on
7 December 22, 2010. In his Schedule D of secured creditors,
8 Borsos listed SEIU and UHW jointly as creditors holding a secured
9 claim against his residence based on an abstract of judgment they
10 recorded in October 2010.

11 On March 15, 2011, UHW filed a nondischargeability complaint
12 against Borsos, alleging that the district court judgment against
13 Borsos constituted "'a debt . . . for . . . defalcation while
14 acting in a fiduciary capacity' within the meaning of 11 U.S.C.
15 § 523(a)(4). . . ." Complaint (Mar. 15, 2011) at ¶ 14.

16 Both sides filed cross-motions for summary judgment, which
17 the bankruptcy court denied. Instead, the bankruptcy court held
18 a one-day trial on February 13, 2012. By stipulation of the
19 parties, trial was limited to the presentation of materials from
20 the record in the district court litigation. On March 15, 2012,
21 the bankruptcy court orally recited its findings of fact and
22 conclusions of law into the record.

23 Among its key findings, the bankruptcy court stated the
24 district court jury had found that Borsos had used UHW resources

25
26 ⁵The district court's judgment was entered pursuant to Civil
27 Rule 54(b). The ERISA claim for relief was not tried at the same
28 time as all of the other claims for relief, and the district
court stated in its Civil Rule 54(b) judgment that the ERISA
claim would be resolved sometime later.

1 and funds "in ways that were not appropriate" in the process of
2 resisting SEIU's appointment of a trusteeship over UHW's affairs.
3 The bankruptcy court also stated the district court jury found
4 Borsos liable in the amount of \$60,000 for diversion of resources
5 and \$6,600 for salary and benefits.

6 The bankruptcy court held that a trust existed for purposes
7 of § 523(a)(4) and that Borsos was fiduciary of that trust. The
8 court ruled: (1) that under LMRDA, codified at 29 U.S.C. § 501,
9 UHW's "money and property" were property of a technical trust
10 created by statute without reference to and before the occurrence
11 of any particular wrongdoing; (2) that Borsos and the other
12 individual defendants in the district court action were trustees
13 of that trust; and (3) that 29 U.S.C. § 501(a)⁶ imposed on Borsos

14
15 ⁶The full text of 29 U.S.C. § 501(a) provides:

16 (a) Duties of officers; exculpatory provisions and
17 resolutions void

18 The officers, agents, shop stewards, and other
19 representatives of a labor organization occupy
20 positions of trust in relation to such organization and
21 its members as a group. It is, therefore, the duty of
22 each such person, taking into account the special
23 problems and functions of a labor organization, to hold
24 its money and property solely for the benefit of the
25 organization and its members and to manage, invest, and
26 expend the same in accordance with its constitution and
27 bylaws and any resolutions of the governing bodies
28 adopted thereunder, to refrain from dealing with such
organization as an adverse party or in behalf of an
adverse party in any matter connected with his duties
and from holding or acquiring any pecuniary or personal
interest which conflicts with the interests of such
organization, and to account to the organization for
any profit received by him in whatever capacity in
connection with transactions conducted by him or under

(continued...)

1 and the other individual defendants certain fiduciary duties with
2 respect to that trust, including in relevant part the following
3 duties:

4 [T]o hold its money and property solely for the benefit
5 of the organization and its members; and to manage,
6 invest and expend the same in accordance with its
constitution and bylaws . . . and any resolution of the
governing bodies adopted [thereunder]

7 Trial Tr. (Mar. 15, 2012) at 9:19-23.

8 The bankruptcy court also determined that, under the
9 doctrine of issue preclusion, it would not revisit the district
10 court jury's findings. The court indicated that it was relying
11 upon the jury verdict and Jury Instructions in concluding that
12 the district court judgment should be excepted from discharge
13 under § 523(a)(4).

14 Finally, the bankruptcy court ruled that the conduct for
15 which the jury found Borsos liable constituted defalcation for
16 purposes of the nondischargeability statute. However, in making
17 its defalcation ruling, the court did not make any findings as to
18 Borsos' state of mind when he diverted his work time and other
19 UHW resources to non-UHW purposes.

20 On March 16, 2012, the bankruptcy court entered its
21 nondischargeability judgment, and Borsos filed his notice of
22 appeal from that judgment on March 21, 2012.

23
24 _____
25 ⁶(...continued)
26 his direction on behalf of the organization. A general
27 exculpatory provision in the constitution and bylaws of
28 such a labor organization or a general exculpatory
resolution of a governing body purporting to relieve
any such person of liability for breach of the duties
declared by this section shall be void as against
public policy.

1 **JURISDICTION**

2 The bankruptcy court had jurisdiction pursuant to 28 U.S.C.
3 §§ 1334 and 157(b)(2)(I). We have jurisdiction under 28 U.S.C.
4 § 158.

5 **ISSUE**

6 Did the bankruptcy court err in ruling that the district
7 court jury’s liability findings established a debt based on
8 defalcation for purposes of § 523(a)(4)?

9 **STANDARDS OF REVIEW**

10 On appeal from a nondischargeability judgment, we review the
11 bankruptcy court's findings of fact under the clearly erroneous
12 standard and its conclusions of law de novo. See Honkanen v.
13 Hopper (In re Honkanen), 446 B.R. 373, 382 (9th Cir. BAP 2011).
14 However, the ultimate question of whether a particular debt is
15 dischargeable is a mixed question of fact and law that we review
16 de novo. Id.; see also Searles v. Riley (In re Searles),
17 317 B.R. 368, 373 (9th Cir. BAP 2004) (stating that mixed
18 questions are reviewed de novo when they require the court “to
19 consider legal concepts and exercise judgment about values
20 animating legal principles.”).

21 **DISCUSSION**

22 Borsos assigns error to two distinct aspects of the
23 bankruptcy court’s nondischargeability determination. Most
24 relevant for our purposes, Borsos contends on appeal that the
25 conduct for which the jury found him liable did not qualify as
26 defalcation under § 523(a)(4), so the bankruptcy court should not
27 have found § 523(a)(4)’s defalcation requirement satisfied.
28 Borsos also contends on appeal that 29 U.S.C. § 501 did not

1 impose upon him the type of fiduciary capacity covered by
2 § 523(a)(4).⁷

3 In Borsos' view, the district court jury's liability
4 findings simply don't add up to defalcation under § 523(a)(4).
5 In order to address Borsos' defalcation argument, we must
6 consider what constitutes defalcation under § 523(a)(4). In
7 terms of conduct, defalcation can occur for purposes of
8 § 523(a)(4) if the fiduciary either misappropriated trust assets
9 or failed to account for them. See Blyler v. Hemmeter
10 (In re Hemmeter), 242 F.3d 1186, 1190 (9th Cir. 2001) (citing
11 Lewis v. Scott (In re Lewis), 97 F.3d 1182, 1186 (9th Cir.
12 1996)). In turn, a fiduciary misappropriates trust assets if he
13 uses them for an improper purpose in light of the trust's terms.
14 See Lovell v. Stanifer (In re Stanifer), 236 B.R. 709, 719 (9th
15 Cir. BAP 1999); see also OXFORD ENGLISH DICTIONARY (defining a
16 misappropriation in relevant part as an "[a]ppropriation of
17 (something) for a wrong use").

18 As set forth in the facts section, supra, all of the
19 district court jury's liability findings against Borsos were
20 based on Borsos' diversion of his work time and other UHW
21 resources for non-UHW purposes. This conduct squarely falls
22 within the definition of misappropriation, which in turn
23 satisfies the conduct component of § 523(a)(4)'s defalcation
24 requirement.

25 But our examination of Borsos' defalcation argument does not
26

27 ⁷In light of our holding on the defalcation issue, we need
28 not and will not address the fiduciary capacity issue.

1 end there because the Supreme Court recently held that
2 § 523(a)(4)'s defalcation requirement consists not only of a
3 conduct component but also of a scienter component. See Bullock,
4 133 S.Ct. at 1759-60. As the Court stated its holding:

5 [W]here the conduct at issue does not involve bad
6 faith, moral turpitude, or other immoral conduct, the
7 term requires an intentional wrong. We include as
8 intentional not only conduct that the fiduciary knows
9 is improper but also reckless conduct of the kind that
10 the criminal law often treats as the equivalent. Thus,
11 we include reckless conduct of the kind set forth in
12 the Model Penal Code. Where actual knowledge of
13 wrongdoing is lacking, we consider conduct as
14 equivalent if the fiduciary "consciously disregards"
15 (or is willfully blind to) "a substantial and
16 unjustifiable risk" that his conduct will turn out to
17 violate a fiduciary duty.

18 Id. at 1759 (quoting American Law Institute, Model Penal Code
19 § 2.02(2)(c), p. 226 (1985)).

20 As a result, in order to qualify as a § 523(a)(4)
21 defalcation, debtors must have acted either with knowledge that
22 their conduct would constitute a breach of their fiduciary duty,
23 or with conscious disregard or willful blindness to "a
24 substantial and unjustifiable risk" that their conduct would
25 constitute a breach of their fiduciary duty. Id. at 1759.

26 Prior to Bullock, the rule in the Ninth Circuit was that no
27 particular state of mind was required to satisfy § 523(a)(4)'s
28 defalcation requirement. See Sherman v. Sec. and Exch. Comm'n
(In re Sherman), 658 F.3d 1009, 1017-18 (9th Cir. 2011). Indeed,
even an innocent failure to account for trust property could
constitute a defalcation. See id. (citing In re Hemmeter,
242 F.3d at 1190-91). Bullock, however, has overruled
In re Sherman and In re Hemmeter to the extent those two
decisions did not recognize that § 523(a)(4)'s defalcation

1 requirement included a scienter component. As such, we are not
2 required to follow them. See Deitz v. Ford (In re Deitz),
3 469 B.R. 11, 23 (9th Cir. BAP 2012) (Ninth Circuit case not
4 binding precedent when it has been effectively superseded by an
5 intervening Supreme Court decision containing reasoning "clearly
6 irreconcilable" with prior Ninth Circuit decision).

7 In excepting from discharge the district court judgment
8 debt, the bankruptcy court explicitly ruled that Borsos' conduct
9 constituted defalcation under § 523(a)(4). But in making that
10 ruling, the bankruptcy court did not make any findings regarding
11 Borsos' mental state.⁸ Civil Rule 52(a) applies in adversary
12 proceedings and requires bankruptcy courts to make factual
13 findings in support of their decisions. When the bankruptcy
14 court does not provide complete findings, we may vacate and
15 remand for further findings. See First Yorkshire Holdings, Inc.
16 v. Pacifica L 22, LLC. (In re First Yorkshire Holdings, Inc.),
17 470 B.R. 864, 871 (9th Cir. BAP 2012).

18 Notwithstanding the above, we are not obligated to vacate
19 and remand for further findings if the record otherwise provides
20 us with a complete understanding of the issues appealed. See id.
21 (citing Simeonoff v. Hiner, 249 F.3d 883, 891 (9th Cir. 2001)).
22 We also need not remand if we reasonably can infer from the
23 court's findings other facts that would suffice to support the
24 court's decision. See Brock v. Big Bear Market No. 3, 825 F.2d

25
26 ⁸The bankruptcy court's omission makes perfect sense. At
27 the time of its ruling, Bullock was not yet before the Supreme
28 Court, and In re Sherman and In re Hemmeter did not require the
bankruptcy court to make any findings regarding Borsos' mental
state.

1 1381, 1384 (9th Cir. 1987). Nonetheless, we must vacate and
2 remand here because we cannot ascertain with any certainty
3 Borsos' mental state either from the bankruptcy court record or
4 from the bankruptcy court's findings.

5 Put another way, when the bankruptcy court does not apply
6 the correct legal standard, remand still may be unnecessary if
7 the record is complete and the outcome of the case is beyond
8 doubt upon our application of the correct legal standard. See
9 Hopkins v. Asset Acceptance LLC (In re Salgado-Nava), 473 B.R.
10 911, 922 (9th Cir. BAP 2012) (citing Wharf v. Burlington N.R.R.
11 Co., 60 F.3d 631, 637 (9th Cir. 1995)). Here, however, the
12 outcome regarding Borsos' state of mind is not beyond doubt.
13 There are facts in the record from which the bankruptcy court
14 arguably could have inferred that Borsos diverted UHW's resources
15 without the culpable state of mind Bullock requires.

16 For instance, Borsos claimed at trial and on appeal that,
17 when Former UHW Management were still in charge of UHW, they
18 passed a resolution authorizing Borsos to take the actions that
19 the district court jury later found him liable for. Therefore,
20 Borsos reasoned, he did not commit § 523(a)(4) defalcation.
21 While we agree with the bankruptcy court's conclusion that Borsos
22 cannot use his authorization argument to collaterally attack the
23 jury's finding that Borsos diverted UHW resources, the jury made
24 no findings regarding Borsos' mental state. Thus, the bankruptcy
25 court arguably could have inferred that, to the extent Borsos
26 believed he had been duly authorized by Former UHW Management, he
27 did not divert UHW resources either knowing that he was breaching
28 his fiduciary duty or in reckless disregard of that duty. On the

1 other hand, the bankruptcy court also might have reasonably
2 inferred the opposite result from the same facts: that Borsos did
3 not really believe that he was duly authorized to use UHW
4 resources for the purposes of undermining SEIU's initiatives and
5 starting up a rival union.

6 In the final analysis, what the bankruptcy court ultimately
7 finds on remand regarding Borsos' mental state likely will hinge
8 in part on the bankruptcy court's assessment of Borsos'
9 credibility. See generally Hernandez v. New York, 500 U.S. 352,
10 364 (1991) (noting that findings regarding a person's state of
11 mind largely turn on the court's assessment of credibility);
12 Batson v. Kentucky, 476 U.S. 79, 98 & n. 21 (1986) (same).
13 Accordingly, the bankruptcy court may find it appropriate on
14 remand to reopen the record to permit the presentation of
15 additional evidence, including but not necessarily limited to the
16 presentation of testimony from Borsos.

17 **CONCLUSION**

18 For the reasons set forth above, we VACATE the bankruptcy
19 court's judgment, and we REMAND so the bankruptcy court can make
20 further findings.
21
22
23
24
25
26
27
28