UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF COLORADO

In re:	)	
	)	
DWIGHT SAMUEL MULBERRY and JONI MICHELLE MULBERRY,	)	Case No. 23-10804-JGR
	)	
	)	Chapter 7
Debtors.	)	
	)	
	)	
MARK PETERSON and BRENDA PETERSON,	)	Adv. Proceeding No. 23-01089-JGR
	)	
Plaintiffs,	)	
	)	
v.	)	
	)	
DWIGHT SAMUEL MULBERRY and JONI MICHELLE MULBERRY,	)	
	)	
Defendants.	)	

MOTION TO DISMISS CORRECTED COMPLAINT

Dwight Samuel Mulberry and Joni Michelle Mulberry (the "Mulberrys"), through undersigned counsel appearing through the Faculty of Federal Advocates, file this Motion to Dismiss and state as follows:

INTRODUCTION

According to the complaint, the Mulberrys were the owners of Craftsman Homes & Interiors LLC ("Craftsman"). Plaintiffs Mark and Brenda Peterson (the "Petersons") entered into a preconstruction agreement (the "Agreement") with Craftsman.[1] Under the Agreement, the Petersons paid $25,000 to Craftsman to prepare plans for the construction of a custom home. The Peterson allege that Craftsman failed to complete the required plans. The Petersons

[1] The Petersons allege in the complaint that the Agreement is attached, but nothing was attached to the complaint at Docket No. 1.

do not allege Craftsman did zero work or left any subcontractors or material suppliers who may have a lien unpaid. The Petersons then use unsupported legal conclusions to attempt to turn an alleged breach of contract into fraud, theft, and an intentional injury.

As demonstrated below, the Petersons fail to allege facts (as opposed to legal conclusions) to support each element of their claims. As a result, even taking the factual allegations in the complaint as true (as opposed to the unsupported legal conclusions), the Petersons would not be entitled to judgment based on the allegations in the complaint and the claims in the complaint must be dismissed under Fed. R. Civ. P. 12(b)(6).

I. MOTION TO DISMISS STANDARD

The purpose of a motion to dismiss is to "assess whether the plaintiff's complaint alone is legally sufficient to state a claim for which relief may be granted." *Sutton v. Utah State Sch. for the Deaf & Blind,* 173 F.3d 1226, 1236 (10th Cir.1999) (citation omitted). To survive a motion to dismiss under Fed. R. Civ. P. 12(b)(6), a plaintiff "must allege enough facts to state a claim to relief that is plausible on its face." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 570 (2007). A plaintiff must provide "more than labels and conclusions, [or] a formulaic recitation of the elements of a cause of action," *Id*. at 555. While the court accepts the factual allegations in the complaint as true, the court is "not bound to accept as true a legal conclusion couched as a factual allegation." *Iqbal*, 556 U.S. at 678. A plausible claim must, therefore, "sufficiently allege[] facts supporting all the elements necessary to establish an entitlement to relief under the legal theory proposed." *Lane v. Simon,* 495 F.3d 1182, 1186 (10th Cir. 2007) (internal quotation omitted).

If the "well-pleaded facts do not permit the court to infer more than the mere possibility of misconduct," a claim must be dismissed. *Ashcroft v. Iqbal,* 556 U.S. 662, 679 (2009). Plausibility refers to the "scope of the allegations in a complaint— *i.e.,* if they are so general that they

encompass a wide swath of conduct, much of it innocent, then the plaintiffs have not nudged their claims across the line from conceivable to plausible." *Robbins v. Oklahoma,* 519 F.3d 1242, 1247–48. (10th Cir. 2008) (internal quotations omitted). The "allegations must be enough that, if assumed to be true, the plaintiff plausibly (not just speculatively) has a claim for relief." *Id.*

II. ELEMENTS OF THE PETERSONS' CLAIMS

The Petersons assert claims under 11 U.S.C. §§ 523(a)(2)(A), 523(a)(2)(B), 523(a)(4), and 523(a)(6). It is a "well-known guide that exceptions to discharge should be confined to those plainly expressed." *Kawaauhau v. Geiger*, 523 U.S. 57, 62 (1998). Further, to promote the policy of providing debtors with a fresh start, "exceptions to discharge are to be narrowly construed, and . . . doubt is to be resolved in the debtor's favor." *Glencove Holdings, LLC v. Bloom (In re Bloom)*, No. 22-1005, 2022 U.S. App. LEXIS 19089, at *13 (10th Cir. July 12, 2022). The statutory language and elements of each of the Petersons' claims are identified and addressed in turn below.

A. NON-DISCHARGEABILITY UNDER 523(A)(4)

Pursuant to 11 U.S.C. § 523(a)(4), a debtor may not discharge a debt "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." It is not clear from complaint whether the Petersons intend to assert (1) fraud or defalcation while acting in a fiduciary capacity, (2) embezzlement, or (3) larceny under § 523(a)(4). As demonstrated below, the Petersons fail to allege factual material to support each element of a claim under any of them.

i. FRAUD OR DEFALCATION OF A FIDUCIARY

A claim for defalcation while acting in a fiduciary capacity requires: (1) a fiduciary relationship, and (2) a defalcation. *Fowler Bros. v. Young (In re Young)*, 91 F.3d 1367, 1371 (10th Cir. 1996). Whether a fiduciary relationship exists for purpose of § 523(a)(4) is determined under federal law. *Fowler Bros. v. Young (In re Young)*, 91 F.3d 1367, 1371 (10th Cir. 1996). Under

federal law, "an express or technical trust must be present for a fiduciary relationship to exist under § 523(a)(4)." *Id.* For the purpose of this motion, the Mulberrys acknowledge that courts have held the Colorado mechanic's lien trust fund statute, Colo. Rev. Stat. § 38-11-127 (the "Trust Fund Statute"), creates a technical trust that can create a fiduciary duty. *See, e.g., Pino v. Jensen (In re Jensen)*, Nos. 16-21724, 17-01078, 2019 Bankr. LEXIS 1774, at *20 (B.A.P. 10th Cir. June 7, 2019). However, the complaint does not contain any factual allegations to support the defalcation or fraud requirement.

Defalcation requires "an intentional wrong" that the "fiduciary knows is improper" or "reckless conduct of the kind that the criminal law often treats as the equivalent. Where actual knowledge of wrongdoing is lacking, we consider conduct as equivalent if the fiduciary consciously disregards (or is willfully blind to) a substantial and unjustifiable risk." *Bullock v. BankChampaign, N.A.*, 569 U.S. 267, 273-74 (2013); *see also In re Karch*, 501 B.R. 403, 407 (Bankr. D. Colo. 2013). A risk is substantial and unjustifiable if it is of "such a nature and degree that, considering the nature and purpose of the actor's conduct and the circumstances known to him, its disregard involves *a gross deviation* from the standard of conduct that a law-abiding person would observe in the actor's situation." *Id.* In short, "defalcation by a fiduciary requires a culpable state of mind involving knowledge of, or gross recklessness in respect to, the improper nature of the fiduciary behavior." *Dampier v. Credit Invs., Inc. (In re Dampier)*, Nos. CO-15-006, 14-24526, 2015 Bankr. LEXIS 3800, at *18-19 (B.A.P. 10th Cir. Nov. 5, 2015).

The Mulberrys acknowledge that the complaint contains sufficient allegations for a Trust Fund Statute claim, for which no intent is required. *See* Colo. Rev. Stat. § 38-22-127. But the complaint contains no factual allegations to support the intent element of defalcation required under *Bullock*—not even a recitation of the required intent element as a legal conclusion. The

Petersons do not allege any factual material to suggest that the Mulberrys were aware of the Trust Fund Statute. While the Petersons' allegations would have been sufficient for a § 523(a)(4) defalcation claim before *Bullock*, the Petersons do not state a claim in light of *Bullock*'s intent/scienter requirement. Because the complaint fails to contain factual allegations to support an essential element of a defalcation claim, it fails to state a claim. *Lane v. Simon,* 495 F.3d 1182, 1186 (10th Cir. 2007) (a plausible claim must "sufficiently allege[] facts *supporting all the elements* necessary to establish an entitlement to relief under the legal theory proposed.").

The Petersons do not allege any factual material to support fraud. As demonstrated more fully in the section under § 523(a)(2)(A), the Petersons' allegation that the Mulberrys lacked the intent to cause Craftsman to perform under the Agreement is an unsupported legal conclusion. There are no factual allegations in the complaint that the Mulberrys misrepresented anything, no factual allegations to support a conclusion that the Mulberrys had any intent to deceive, and no factual allegations to support fraud. Because the complaint fails to contain factual allegations to support an essential element of a fraud claim, it fails to state a claim. *Lane v. Simon,* 495 F.3d 1182, 1186 (10th Cir. 2007) (a plausible claim must "sufficiently allege[] facts *supporting all the elements* necessary to establish an entitlement to relief under the legal theory proposed.").

ii. EMBEZZLEMENT OR LARCENY

For the purpose of determining dischargeability under § 523(a)(4), embezzlement and larceny are determined under federal law, but the bankruptcy code provides no definitions of larceny or embezzlement. Most courts have concluded that larceny and embezzlement claims are similar—the primary difference is that with embezzlement, "the debtor initially acquires the property lawfully, whereas larceny requires that the funds originally come into the debtor's hands unlawfully." *Alternity Capital Offering 2, LLC v. Ghaemi (In re Ghaemi)*, 492 B.R. 321, 325

(Bankr. D. Colo. 2013) quoting *Bombardier Capital, Inc. v. Tinkler (In re Tinkler)*, 311 B.R. 869, 876 (Bankr. D. Colo. 2004). An embezzlement claim under § 523(a)(4) has five elements: "1. Entrustment (property lawfully obtained originally); 2. Of property; 3. Of another; 4. That is misappropriated (used or consumed for a purpose other than that for which it was entrusted); 5. With fraudulent intent." *Ghaemi*, 492 B.R. at 325 quoting *Bryant v. Tilley (In re Tilley)*, 286 B.R. 782, 789 (Bankr. D. Colo. 2002).

Most courts have concluded that, with respect to the intent requirement, both larceny and embezzlement require "fraud in fact, involving moral turpitude or intentional wrong, rather than implied or constructive fraud." *Ghaemi*, 492 B.R. at 325 quoting *Driggs v. Black (In re Black)*, 787 F.2d 503, 507 (10th Cir. 1986); *see also Bullock v. BankChampaign, N.A.*, 569 U.S. 267, 273 (2013). Federal common law also describes the intent requirement as "*animus furandi* or intention to steal." *Bryant v. Lynch (In re Lynch)*, 315 B.R. 173, 181 (Bankr. D. Colo. 2004) (internal citations omitted). However the intent/scienter requirement for larceny and embezzlement is measured, it is clear from the Supreme Court's reasoning in *Bullock* that defalcation requires a "culpable state of mind requirement akin to that which accompanies application of the other terms in the same statutory phrase," (*Bullock*, 569 U.S. at 269), that larceny and embezzlement require no lower an intent standard than defalcation.

The Petersons have failed to allege factual material to support the intent requirement of embezzlement or larceny. This is not a Fed. R. Civ. P. 9(b) issue, which permits the Petersons to allege intent generally. This is a *Twombly, Iqbal*, and *Lane v. Simon,* 495 F.3d 1182, 1186 (10th Cir. 2007) issue. Each of those cases requires factual allegations to support legal conclusions: "a court is "not bound to accept as true a legal conclusion couched as a factual allegation." *Iqbal*, 556 U.S. at 678. In fact, the issue for which the Supreme Court was testing the factual allegations in

the complaint in *Iqbal* was discriminatory intent. The Court in *Iqbal* stated "Rule 9 merely excuses a party from pleading discriminatory intent under an elevated pleading standard. It does not give him license to evade the less rigid--though still operative--strictures of Rule 8." *Ashcroft v. Iqbal*, 556 U.S. 662, 686-87 (2009). "And Rule 8 does not empower respondent to plead the bare elements of his cause of action, affix the label "general allegation," and expect his complaint to survive a motion to dismiss. *Id.*

An allegation that the Mulberrys did something "with the intent to deprive Plaintiffs permanently of the use of their money" appears to be an attempt to address a portion of the intent requirement under Colorado's theft statute, Colo. Rev. Stat. § 18-4-401.[2] However, it is a legal conclusion: "intent, moreover, cannot be alleged as a legal conclusion; a complaint must plead facts sufficient to give rise to a plausible inference of intent. *Clarke v. Swanson*, Nos. 13 B 14970, 13 A 1340, 2014 Bankr. LEXIS 4565, at *13 (Bankr. N.D. Ill. July 7, 2014) (internal quotations omitted). "The requirement to plead facts rather than legal conclusions applies to allegations of a defendant's intent as well as allegations about a defendant's conduct." *Kaplan v. Al Jazeera*, 2011 U.S. Dist. LEXIS 61373, at *11-12 (S.D.N.Y. June 7, 2011). "Respondent finally maintains that the Federal Rules expressly allow him to allege petitioners' discriminatory intent 'generally,' which he equates with a conclusory allegation. . . . But the Federal Rules do not require courts to credit a complaint's conclusory statements without reference to its factual context." *Iqbal*, 129 S. Ct. at 1954. That legal conclusion cannot satisfy the requirement to plead factual material to support the intent element of the Petersons' claims.

[2] Whether or not the Colorado theft constitutes embezzlement or larceny requirement under § 523(a)(4), the Petersons failed to allege any factual material or even the legal conclusions necessary for a claim under Colorado's theft statute, including that "a person commits theft when he or she *knowingly* obtains, retains, or exercises control over anything of value of another *without authorization* or *by threat or deception*…." Colo. Rev. Stat. § 18-4-401(1).

As demonstrated above, the Petersons' complaint fails to allege factual material to support each element of their claim under § 523(a)(4) (the intent requirement), and as a result, the Petersons fail to state a claim. *Lane v. Simon,* 495 F.3d 1182, 1186 (10th Cir. 2007) (a plausible claim must "sufficiently allege[] facts *supporting all the elements* necessary to establish an entitlement to relief under the legal theory proposed.").

NON-DISCHARGEABILITY UNDER 523(A)(6)

Pursuant to 11 U.S.C. § 523(a)(6), a debtor may not discharge a debt "for willful and malicious injury by the debtor to another entity or to the property of another entity." 11 U.S.C. § 523(a)(6). The willful prong requires "a deliberate or intentional *injury*, not merely a deliberate or intentional *act* that leads to injury." *Kawaauhau v. Geiger*, 523 U.S. 57, 61 (1998). Willful and malicious injury means "intentional torts, as distinguished from negligent or reckless torts. Intentional torts generally require that the actor intend "the *consequences* of an act," not simply the act itself." *Id.* at 61-62. The willful prong requires that the act is done "in conscious disregard of one's duties and without just cause or excuse… or wrongful and without just cause or excuse." *First Am. Title Ins. Co. v. Smith (In re Smith)*, 618 B.R. 901, 919 (B.A.P. 10th Cir. 2020) (internal quotations omitted).

In the complaint, the Petersons fail to include any factual material to support a conclusion that the Mulberry's committed an intentional tort and deliberately caused an injury. The Petersons simply parrot the language of § 523(a)(6), which is insufficient to state a claim. The second claim for relief under § 523(a)(6) must be dismissed for failing to state a claim.

B. NON-DISCHARGEABILITY UNDER 523(A)(2)(A)

Pursuant to 11 U.S.C. § 523:

> A discharge under section 727, 1141, 1192, 1228(a), 1228(b), or 1328(b) of this title [11 USCS § 727, 1141, 1192, 1228(a), 1228(b), or 1328(b)] does not discharge an individual debtor from any debt—

> (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—
>
> > (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

11 U.S.C. § 523(a)(2).

The Petersons' claim is premised on the conclusion that the Mulberrys lacked the intent to cause Craftsman to perform the Agreement when the Agreement was made. In essence, that the Mulberrys fraudulently induced the Petersons to enter into the Agreement. The elements for a claim of fraudulent inducement are: "(1) the defendant's misrepresentation of a material fact; (2) the plaintiff's justifiable reliance on that misrepresentation; and (3) such reliance resulting in damage to the plaintiff. *Kirzhner v. Silverstein*, 09-cv-02858-CMA-BNB, 2011 U.S. Dist. LEXIS 106139, at *28 (D. Colo. Sep. 20, 2011) citing *J.A. Walker Co., Inc. v. Cambria Corp*., 159 P.3d 126, 132 (Colo. 2007). The intention to not perform an agreement can form the basis of a fraudulent inducement claim only if "coupled with a present intention not to fulfill that promise." *Kirzhner*, at *28 quoting *H & H Distribs., Inc. v. BBC Int'l, Inc.*, 812 P.2d 659, 662 (Colo. App. 1990). The Petersons fail to allege any factual material to support a conclusion that the Mulberrys lacked the intent to perform at the time the agreements were made.

For a fraud claim, the Petersons are required to allege the circumstances constituting fraud with specificity as required by Fed. R. Civ. P. 9(b). The Petersons have failed to give the who, what, where, and when of how the breach of contract is somehow fraud. *See, e.g., Farlow v. Peat, Marwick, Mitchell & Co.*, 956 F.2d 982, 986 (10th Cir. 1992) (identifying the basic requirements of Rule 9(b); *Lawrence Nat'l Bank v. Edmonds (In re Edmonds*), 924 F.2d 176, 180 (10th Cir. 1991) (stating that Rule 9(b) requires a fraud claimant to "set forth the time, place and contents of

the false representation, the identity of the party making the false statement and the consequences thereof."). In fact, the Petersons fail to identify any of the circumstances constituting the alleged fraud other than the unsupported conclusion that the Mulberrys allegedly lacked the intent to perform when he entered into the agreement. Moreover, as shown below, the statement in Rule 9 that intent may be pleaded generally does not save the Petersons because their claim under § 523(a)(2)(A) still fails the *Twombly* standard.

In general, "courts are justifiably loathe to allow tort claims and damages in actions that are fundamentally about enforcing legitimate business expectations rather than vindicating social policy." *Kirzhner*, at *31-32 (internal quotation omitted). An allegation that a party lacked the intent to perform is a legal conclusion not entitled to a presumption of truth. *See, e.g, Kirzhner*, at *28; *Areias v. Applied Underwriters, Inc.*, No. 21-cv-00023-JST, 2021 U.S. Dist. LEXIS 262098, at *25-26 (N.D. Cal. Oct. 19, 2021). Further, for a claim based on an alleged lack of intent to perform an agreement, "plaintiff must provide some factual basis for conclusory allegations of intent. Proof of fraudulent intent must be based on more than mere showing of later nonperformance of the alleged promise." *Kirzhner*, at *30-31. "The fact that someone ultimately breaches a contract does not provide any factual support for an allegation that the person intended to breach the contract at the time of contract formation." *Id.* "An intention not to perform under an agreement cannot be "established solely by proof of . . . nonperformance [], nor does the promisor's failure to perform the agreement throw upon him the burden of showing that his nonperformance was due to reasons which operated after the agreement was entered into." *Chevy Chase Bank FSB v. Kukuk (In re Kukuk)*, 225 B.R. 778, 786 (B.A.P. 10th Cir. 1998) (quotations omitted). But that is exactly what the Petersons' complaint attempts.

There is no factual basis in the complaint to support a conclusion that the Mulberrys lacked the intent to have Craftsman perform the Agreement at the time it was made. The allegation that Craftsman breached does not support the intent requirement. The allegation that the Mulberrys lacked the intent to cause Craftsman to perform is a legal conclusion not entitled to any presumption of truth. As a result, the Petersons have failed to "allege facts supporting all the elements necessary to establish an entitlement to relief under the legal theory proposed" (*Lane v. Simon*, 495 F.3d 1182, 1186 (10th Cir. 2007)) for their claim under 11 U.S.C. § 523(a)(2). The Petersons' third claim for relief under 11 U.S.C. § 523(a)(2)(A) must be dismissed pursuant to Fed. R. Civ. P. 12(b)(6) for failing to state a claim.

C. NON-DISCHARGEABILITY UNDER 523(A)(2)(B)

In their complaint, the Petersons' state their fourth claim for relief is for false pretenses under § 523(a)(2)(A). However, the allegations for the claim are that either the Mulberrys or Craftsman (from the complaint it's not clear who), was insolvent. It appears that the Petersons assert the financial condition of either the Mulberrys or Craftsman was misrepresented somehow (they do not allege how). A statement about the debtor's or an insider's finances is actionable only under § 523(a)(2)(B), which requires such statement to be made in writing. The Petersons did not assert a claim under § 523(a)(2)(B), nor could they without a writing, which they have not alleged. *Lamar, Archer & Cofrin, LLP v. Appling*, 138 S. Ct. 1752, 1761 (2018) ("a statement is 'respecting' a debtor's financial condition if it has a direct relation to or impact on the debtor's overall financial status. A single asset has a direct relation to and impact on aggregate financial condition, so a statement about a single asset bears on a debtor's overall financial condition and can help indicate whether a debtor is solvent or insolvent, able to repay a given debt or not. Naturally, then, a statement about a single asset can be a 'statement respecting the debtor's financial condition.'").

The claim also fails the particularity requirement of Rule 9(b), which requires, among other things, that the Petersons "set forth the time, place and contents of the false representation, the identity of the party making the false statements." *Koch v. Koch Indus.*, 203 F.3d 1202, 1236 (10th Cir. 2000). The complaint identifies none of those.

The Petersons' fourth claim for relief must be dismissed because a claim respecting the financial condition of a debtor or an insider is actionable only under § 523(a)(2)(B). The Petersons have not alleged a writing as required under § 523(a)(2)(B) and they also fail to identify with particularity the alleged circumstances of the fraud—the who, what, where, and when. As a result, the Petersons' fourth claim for relief must be dismissed pursuant to Fed. R. Civ. P. 12(b)(6).

CONCLUSION

The Petersons fail to allege sufficient factual material to support each element of their claim. The under § 523(a)(2) for the alleged fraudulent inducement is based only on unsupported legal conclusion. The Petersons also fail to allege any factual material to support the intent element of a claim under § 523(a)(4). The Petersons also fail to allege any factual material in the complaint to support the willful element of a claim under § 523(a)(6). As a result, the Petersons' complaint must be dismissed pursuant to Fed. R. Civ. P. 12(b)(6).

Dated: June 8, 2023.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that on June 8, 2023, a copy of the foregoing was served on Plaintiff's counsel and anyone requesting electronic notice through CM/ECF pursuant to the Federal Rules of Bankruptcy Procedure and the Court's Local Rules.

s/ Barbara A. Moss