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The U.S. Supreme Court handed down its first bankruptcy decision of 2013 on May 13. In a unanimous ruling, the court held in *Bullock v. BankChampaign N.A.*, 2013 BL 125909 (U.S. May 13, 2013), that the term "defalcation" for purposes of denying discharge of a debt under section 523(a)(4) of the Bankruptcy Code includes a "culpable state of mind" requirement involving knowledge of, or gross recklessness with respect to, the improper nature of a fiduciary's behavior.

Section 523(a)(4) bars from discharge any debt of an individual debtor "for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." In *Bullock*, the bankruptcy court held that a debtor who had acted as trustee for his father's insurance trust was guilty of defalcation for making loans to himself during the time he controlled the trust. That ruling was upheld on appeal by a district court and the Eleventh Circuit Court of Appeals, which reasoned that "defalcation requires a known breach of fiduciary duty, such that the conduct can be characterized as objectively reckless." The Eleventh Circuit thereby aligned itself with the Fifth, Sixth, and Seventh Circuits. The Supreme Court agreed to review the case on October 29, 2012.

In its unanimous ruling, the Supreme Court vacated the decision and remanded the matter below for additional deliberations. Writing for the court, Justice Stephen Breyer stated that "where the conduct at issue does not involve bad faith, moral turpitude, or other immoral conduct, the term requires an intentional wrong." Justice Breyer explained as follows:

> We include as intentional not only conduct that the fiduciary knows is improper but also reckless conduct of the kind that the criminal law often treats as the equivalent. Thus, we include reckless conduct of the kind set forth in the Model Penal Code. 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" that his conduct will turn out to violate a fiduciary duty. That risk "must be 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." (citations omitted).

Because the Eleventh Circuit applied a standard of "objective recklessness," the Supreme Court instructed it to determine on remand "whether further proceedings are needed and, if so, to apply the heightened standard that we have set forth."