

DISCHARGEABLE OR NOT DISCHARGEABLE: DOES AN INTENTIONAL BREACH OF CONTRACT FALL WITHIN *WILLFUL AND MALICIOUS* UNDER SECTION 523(A)(6) OF THE BANKRUPTCY CODE?

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I. INTRODUCTION

Even though a decade has passed since the Supreme Court decided the case of *Kawaauhau v. Geiger*,¹ confusion still exists between the various federal jurisdictions as to the meaning of *willful and malicious* under § 523(a)(6) of the Bankruptcy Code when addressing contractual breach.² The Supreme Court was successful in defining *willful and malicious* in matters involving tortious conduct; however, the decision did not abate the conflict among the various jurisdictions in matters involving contract. The Supreme Court's opinion left too much room for interpretation on one particular issue: Can the injuries resulting from a breach of contract without a separate tortious act be considered *willful and malicious*?

Historically, courts have interpreted the *willful and malicious injury* of § 523(a)(6) as those damages caused solely as the result of a debtor's intentionally tortious behavior. However, since the *Geiger* case, this interpretation has been expanded by some courts to include "willful and malicious injury" caused by a breach of contract even in the absence of an accompanying tort. For example, in 2003, the Fifth Circuit Court of Appeals held that damages resulting from a breach of a contract can be considered *willful and malicious* if the breaching debtor intended to injure the non-breaching party.³ In that case, the Fifth Circuit did not require the presence of separate tortious conduct to prevent discharge under § 523(a)(6).

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¹ *Kawaauhau v. Geiger*, 523 U.S. 57 (1998).

² 11 U.S.C. § 523(a)(6) (2006); see 11 U.S.C. § 101(15) (2006) (An entity is "a person, estate, trust, governmental unit, and the United States trustee.").

³ *In re Williams*, 337 F.3d 504, 510 (5th Cir. 2003).

In sharp contrast, the Ninth Circuit and other lower federal courts continue to hold that a breach of contract must be accompanied by the commission of a legally recognized tort in order to meet the standard of *willful and malicious* under § 523(a)(6).⁴ This paper explores the language and context of § 523(a)(6) as it is being applied in Bankruptcy contract cases. This paper also analyzes the federal circuit split and contrasting interpretations of the Code Section and the legal concerns about adapting such a broader interpretation of § 523(a)(6).

II. HISTORY OF THE *WILLFUL AND MALICIOUS* INJURY EXCEPTION TO DISCHARGE

Considerable changes in the U.S. bankruptcy law(s) have taken place since the original enactment of the goals and philosophies of the bankruptcy process. The first federal bankruptcy law was enacted in 1800 and was considered a creditor's remedy. Under the Bankruptcy Act of 1800, only merchants were eligible debtors and only involuntary bankruptcy was permitted.⁵ Additionally, a discharge could only be obtained with the approval of the bankruptcy commissioners and two-thirds in number and value of the creditors holding debts of "at least fifty dollars."⁶ There were provisions for exceptions to discharge, but only on three basic grounds: 1) the debtor failing to disclose a fictitious claim, 2) a one-time gambling loss of fifty dollars or a loss of three hundred dollars in the twelve months preceding bankruptcy, or 3) debts owed to the federal government or any of the states.⁷

The Bankruptcy Code was amended in 1841 and the changes brought new protection and rights to debtors by allowing them to file voluntary bankruptcy petitions.⁸ Under the Bankruptcy Act of 1841, as long as the debtor complied with the process and provisions of the Act and obtained the consent of a majority of his creditors, he would receive a discharge. The statute only excepted from discharge debts arising from "defalcation as a public official" and fiduciary obligations. The courts also retained the previously recognized exception for debts due to the federal government or any of the states.⁹

⁴ *In re Jercich*, 238 F.3d 1202 (9th Cir. 2001); *In re Best*, No. 03-5098; 2004 U.S. App. LEXIS 13773 (6th Cir. 2004).

⁵ *See* Bankruptcy Act of 1800, § 1.

⁶ *Id.* at § 36.

⁷ *See id.* at § 37.

⁸ *See* Bankruptcy Act of 1841, § 9.

⁹ *Id.* at § 1; *see generally* Michael D. DeFrank, *An Ineffective Escape Hatch: The Textualism Mistake in Geiger*, 16 BANKR. DEV. J. 467 (2000) (Discussion of the history of the bankruptcy discharge in Section II).

When Congress again reformed the Bankruptcy Code in 1898, it recognized that the discharge of indebtedness not only freed the individual debtor, but ultimately benefitted all of society. Commentator Michael DeFrank wrote of the “social utility” theory of discharge:

The social utility justification for discharge posits that discharging obligations of individuals hopelessly in debt benefits society as a whole. Discharge frees the debtor from past debts and encourages her to resume a productive role in society.¹⁰

For the first time, the goals of the Bankruptcy Act included macro social utility and individual rehabilitation of the debtor. Under the Act of 1898, discharge became a reward for the “honest but unfortunate debtor.”¹¹ The reward of discharge did come with certain restrictions. Specifically, the Act created exceptions from discharge for debts resulting from morally and ethically unacceptable behavior, as discharging such debts was not seen as likely to restore the debtor to social utility.¹² These nondischargeable debts included those incurred as a result of a “willful and malicious injury.”¹³

The passage of the Bankruptcy Code in 1978 was the culmination of the bankruptcy reform effort of the 1970s. At that time, the Commission on the Bankruptcy Laws of the United States reviewed various proposals, but ultimately kept the “willful and malicious injury” exception intact. The notes from the Commission indicate that the *willful and malicious* exception was not substantially changed from prior law. Additionally, none of the draft statutes made or suggested a change in the *willful and malicious* exception, suggesting that Congress intended no substantive changes in this area.¹⁴

A brief review of the evolution of bankruptcy law over nearly 100 years illustrates the relative stability of this policy: Section 17(a)(2) of the Act of 1898 provided that “(a) discharge in bankruptcy shall release a bankrupt from all of his provable debts, except such as ... (2) are judgments in actions for frauds, or obtaining property by false pretenses or false representations, or for willful and malicious injuries to the person or property of another.”¹⁵ In

¹⁰ DeFrank, *supra* note 9, at 469.

¹¹ *See id.*

¹² *See* Bankruptcy Act of 1898, § 17(a) (“A discharge in bankruptcy shall release the bankrupt from all of his provable debts, except such as . . . (2) are judgments in actions for frauds, or obtaining property by false pretenses or false representations, or for willful and malicious injuries to the person or property of another, . . . or (4) were created by his fraud, embezzlement, misappropriation, or defalcation while acting as an officer, or in any fiduciary capacity.”).

¹³ *Id.* at § 17(a)(2).

¹⁴ DeFrank, *supra* note 9, at 478-79.

¹⁵ Pub. L. No. 171, 55th Cong., § 17(a)(2) (July 1, 1898).

1970, the “willful and malicious injury” provision was shifted to § 17(a)(8), which excepted from discharge “liabilities for willful and malicious injuries to the person or property of another other than conversion.”¹⁶ Non-dischargeability of liability for conversion was retained and remains in today’s bankruptcy code.¹⁷

III. THE U.S. SUPREME COURT INTERPRETS THE “WILLFUL AND MALICIOUS INJURY” LANGUAGE OF SECTION 523(A)(6) IN *KAWAAUHAU V. GEIGER*

Prior to the Supreme Court’s *Geiger* decision in 1998, two approaches to interpreting § 523(a)(6) developed in the lower courts: the *special malice* test and the *implied malice* test. The *special malice* test required an actual, subjective intent of the debtor to injure the creditor. Similar to the *specific intent* in criminal law, special malice requires the actor to not only intend to commit the act leading to injury, but to intend the consequences of that act—the injury itself.¹⁸ The *implied malice* test was described in *Tinker v. Colwell* as: “a deliberate or intentional act in which the debtor knows his act would harm the creditor’s interest and proceeds in the fact of the knowledge.”¹⁹ The *Tinker* Court held that this knowledge may be inferred by the debtor’s conduct.²⁰

In 1998, in order to attempt to resolve the split among courts as to the interpretation of *willful and malicious* under § 523(a)(6) of the Code, the U.S. Supreme Court granted certiorari in *Kawaauhau v. Geiger*.²¹ The facts of *Geiger* are relatively simple. Plaintiff Kawaauhau sought medical attention from defendant Dr. Geiger for a foot injury. Dr. Geiger diagnosed Mrs. Kawaauhau and admitted her to the hospital to reduce the risk of infection. Dr. Geiger prescribed oral penicillin, even though he knew that the most effective treatment was intravenous penicillin.²² Dr. Geiger testified that he knew that the proper standard of care under the circumstances was intravenous administration of penicillin, but that he prescribed the medication orally in response to Mrs. Kawaauhau’s desire to keep the cost of

¹⁶ Pub. L. No. 91-467, § 6, 84 Stat. 991 (1970).

¹⁷ The provisions of § 17(a)(2) and § 17(a)(8) were recombined in § 523 (a)(6) of the Code. 124 Cong.Rec. H 11,096 (Sept. 28, 1978); S 17,413 (Oct. 6, 1978).

¹⁸ See *Grand Piano & Furniture Co. v. Hodges*, 4 B.R. 513 (Bankr. W.D. Va. 1980); See also *Coffing v. Burdick*, 65 B.R. 105 (Bankr. N.D. Ind. 1986)(adopting a variation of the special malice test including a “totality of the circumstances”).

¹⁹ *Tinker v. Colwell*, 193 U.S. 473 (1904).

²⁰ See *id.*

²¹ *Kawaauhau v. Geiger*, 523 U.S. 57 (1998).

²² *Id.* at 59.

treatment to a minimum.²³ Dr. Geiger then went out of town, leaving Mrs. Kawauhau in the care of two other doctors. The two doctors immediately switched Mrs. Kawauhau to intravenous penicillin and decided that she should be transferred to an infectious disease specialist. When Dr. Geiger returned, he canceled the transfer and discontinued all antibiotics believing that the infection had subsided. Mrs. Kawauhau's condition subsequently deteriorated, and she was forced to have her leg amputated below the knee.²⁴

Based on Dr. Geiger's admission that he knew the proper standard of care and intentionally departed from it, the Kawauhau won a medical malpractice judgment against him in federal district court, which was affirmed by the Ninth Circuit Court of Appeals.²⁵ Shortly thereafter, Dr. Geiger, who carried no malpractice insurance, relocated to Missouri and filed for bankruptcy protection under Chapter 7.²⁶ The Kawauhau alleged that Dr. Geiger was not able to discharge the malpractice debt because the judgment gave rise to a debt for *willful and malicious* injury.²⁷ The bankruptcy court agreed that the debt was nondischargeable, holding that Dr. Geiger's treatment was so far below the standard level of care that it could be categorized as *willful and malicious* conduct.²⁸

The district court affirmed the decision, but the Eighth Circuit Court of Appeals reversed. The Eighth Circuit held that the proper standard to determine the *willfulness* of Dr. Geiger's conduct was whether he intended to cause the consequences of his actions, or at least believed that the substandard care would result in the consequence of amputation of Mrs. Kawauhau's leg.²⁹ The Court held that for the debt to be dischargeable, the victim must prove an actual intent to injure. The Court further explained that in order for the debtor's action to be found *willful and malicious*, the debtor either desired to cause the consequences of his act or subjectively believed that injury was a substantial certainty.

Justice Ginsberg, writing on behalf of a unanimous Supreme Court, addressed the issue of whether § 523(a)(6) covers "acts, done intentionally, that cause injury or only acts done with the actual intent to cause injury."³⁰ The Court concluded that the word *willful* in the statute modifies the word *injury*, indicating that nondischargeability requires a deliberate or intentional injury, not merely a deliberate or intentional act that leads to injury. Justice Ginsburg reasoned that if Congress had intended § 523(a)(6) to include debts

²³ *Id.*

²⁴ *Id.*

²⁵ *In re Geiger*, 172 B.R. 916, 919 (Bankr. E.D. Mo. 1994).

²⁶ *Geiger*, 523 U.S. at 59-60.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *In re Geiger*, 113 F.3d 848, 852-853 (8th Cir. Mo. 1997).

³⁰ *Geiger*, 523 U.S. at 61.

arising from unintentionally inflicted injuries, it would have used the phrase “willful acts that cause injury” or the additional words *reckless* or *negligent* to modify *injury* in § 523(a)(6).³¹

The court analogized that the requirement of the actor to subjectively intend the consequences of his act to the Restatement (Second) of Torts’ definition of an intentional tort. Justice Ginsburg noted that the phrase *willful and malicious*, as used historically, “triggers in the lawyer’s mind the category ‘intentional torts,’ as distinguished from negligent or reckless torts.”³² The Court noted that the definition of *intentional tort* in the Restatement required that the actor intend the consequences of her act, rather than merely intending the act itself.³³

In *Geiger*, the Court followed a broad interpretation of the discharge exception, encompassing a “wide range of situations in which an act is intentional, but injury is unintended, i.e., neither desired nor in fact anticipated by the debtor.”³⁴ Writing for the majority, Justice Ginsburg provided various illustrations, which included the following:

The Kawaauhwas’ more encompassing interpretation could place within the expected category a wide range of situations in which an act is intentional, but injury unintended... Every traffic accident stemming from an initial intentional act – for example, intentionally rotating the wheel of an automobile to make a left-hand turn without first checking oncoming traffic – could fit the exception. *A ‘knowing breach of contract’ could also qualify...* A construction so broad would be incompatible with the ‘well-known’ guide that exceptions to discharge ‘should be confined to those plainly expressed’.³⁵

Clearly, the Court felt obligations arising from knowing, but non-malicious, breaches of contract should be dischargeable in bankruptcy. This interpretation harkened back to the “social utility” rationale embodied in the Bankruptcy Act of 1898, which excluded from discharge only those debts arising from socially or ethically unacceptable practices.³⁶ The Court also held that to accept a broad interpretation that § 523(a)(6) excepted debts from discharge even in the absence of proof to injury would possibly render meaningless other sections of the Code. Examples cited by the Court

³¹ *Id.*

³² *Id.* at 62.

³³ *Id.*

³⁴ *Id.*

³⁵ *Id.* (emphasis added).

³⁶ See Bankruptcy Act of 1898, § 17(a).

included § 523(a)(9) (excepting damages caused by drunk driving) and § 523(a)(12) (the exception to maintain capital at federal depository institutions).³⁷ In all, the Court chose to interpret the phrase *willful and malicious* narrowly, adopting a specific intent standard. Since then, however, various lower courts have tested broader interpretations that would prohibit discharge of contractual debts less intentionally incurred.

IV. CIRCUITS APPLYING SECTION 523(A)(6) TO DEBTS ARISING FROM DAMAGES CAUSED BY BREACH OF CONTRACT

A. Fifth Circuit – *In Re Williams*

After the Supreme Court issued its opinion on the *willful and malicious* standard in *Geiger*, many considered the controversy surrounding the application of the language of § 523(a)(6) to be settled. However, this proved to be somewhat overconfident when the Fifth Circuit Court of Appeals issued its 2003 decision in *In re Williams*.³⁸ The *Williams* decision did not address the meaning of the terms *willful* and *malicious*, but rather the application of § 523(a)(6) to debts incurred as a result of a breach of contract. This approach was contrary to the historical application of the exception only being applied to tortious behavior.³⁹ The Fifth Circuit in *Williams* broke from previous interpretations to explicitly find that damages caused by a willful and malicious injury as the result of a breach of contract, with no accompanying tort, could also be excepted from discharge under § 523(a)(6).⁴⁰

The debtor in *Williams* was an independent electrical contractor who hired non-union electricians.⁴¹ The local electrician's union targeted Williams by sending union electricians to apply for work with Williams without telling him of their status.⁴² After Williams unknowingly hired some of the union applicants, they began demanding wage and benefit increases,

³⁷ *Geiger*, 523 U.S. at 62.

³⁸ *In re Williams*, 337 F.3d at 504.

³⁹ *See infra* Section IV. A simple breach of contract does not cause an injury that may be excepted from discharge, however an intentional breach of contract accompanied by willful and malicious tortious conduct may be excepted. *See In re Riso*, 978 F.2d 1151 (9th Cir. 1992); *Matter of Haynes*, 19 B.R. 849 (Bankr. E.D. Mich. 1982); *In re Colclazier*, 134 B.R. 39 (Bankr. W.D. Okla. 1991) (holding that exception to discharge will be granted under Code 523(a)(6) only upon finding of an independent, willful tort); *In re Hallahan*, 78 B.R. 547 (Bankr. C.D. Ill. 1987), *aff'd*, 936 F.2d 1496 (7th Cir. 1991).

⁴⁰ *See In re Williams*, 337 F.3d at 511-13.

⁴¹ *Id.* at 506.

⁴² The *Williams* Court cited Williams' brief in defining the Union practice of "salting," which he described as occurring when Union workers conceal their Union membership when applying for non-union jobs, then demanding union-level wages and benefits. *Id.*

and ultimately went on strike when Williams refused. Williams eventually agreed to enter into a collective bargaining agreement (CBA) with the International Brotherhood of Electrical Workers Local 520 for one project.⁴³ The CBA required Williams to use the Union hall as the “sole and exclusive source of referral of applicants for employment.”⁴⁴ Upon having alleged problems with the Union employees, however, Williams terminated some of them and hired some non-union electricians to complete a project.⁴⁵ The Union filed a successful complaint for violations of the CBA, and Williams entered an Agreed Final Judgment and Decree, which was approved and entered by the U.S. District Court for the Western District of Texas.⁴⁶ The Decree required Williams to use only Union electricians on all of his commercial projects and to allow an audit of Williams’s records to determine past compliance with the CBA.⁴⁷

When Williams violated the Decree by hiring non-union electricians for a subsequent commercial project, the District Court found he had willfully and purposely violated the Decree and held him in contempt.⁴⁸ After a court-ordered audit revealed Williams had breached the terms of the original CBA, the court ordered him to pay \$155,855.39 in restitution.⁴⁹ The Court further awarded the Union \$106,911.43 in damages (plus attorney fees) in the contempt action.⁵⁰

A few weeks after the District Court’s judgment, Williams and his wife filed for bankruptcy protection. When the Williams received an Order of Discharge under Chapter 7, the Union filed a complaint seeking to except its judgments under § 523(a)(6).⁵¹ The U.S. Bankruptcy Court for the Western District of Texas found that both of Williams’s debts to the Union – the \$155,855.39 judgment for his breach of the CBA and the \$106,911.43 judgment for violation of the Agreed Judgment and Decree – were excepted from discharge because they represented *willful and malicious* injuries to the Union.⁵² Williams appealed the District Court’s decision to the Fifth Circuit Court of Appeals, arguing that the U.S. Supreme Court had interpreted §

⁴⁴ *Id.* at 507.

⁴⁵ Williams claimed to have at least one of the union employees was found asleep at the jobsite, and on one occasion, Union electricians left the construction site and spent the afternoon at a topless bar. *Id.*

⁴⁶ *In re Williams*, 337 F.3d at 507.

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *Id.* at 508.

⁵² *Id.*

523(a)(6) as requiring tortious conduct to except debts from discharge in *Geiger*.⁵³

The Fifth Circuit began its analysis in *Williams* by noting that *Geiger* had defined *willful and malicious* injuries as “acts done with the actual intent to cause injury, but exclude[ing] intentional acts that cause injury.”⁵⁴ The *Williams* Court also pointed out that *Geiger* had in fact included knowing breaches of contract among the examples of intentional acts causing unintended injuries.⁵⁵ By using the example of “a knowing breach of contract,” the *Williams* Court recognized that the *Geiger* opinion did not reject the proposition that a debt arising from an intentional breach of contract constitutes *willful and malicious* injury under § 523(a)(6).⁵⁶ However, the *Williams* Court did not read *Geiger* as foreclosing the possibility that one may intentionally, and with motive to cause harm, breach a contract, and thus create a *willful and malicious* injury.⁵⁷

The *Williams* Court cited two previous Fifth Circuit decisions, *Texas v. Walker*⁵⁸ and *In re Miller*,⁵⁹ for the proposition that a breach of contract alone may result in an intentional or substantially certain injury, thus satisfying the *willful and malicious* standard. Ironically, neither the *Walker* nor *Miller* decisions actually excluded a debt from discharge under § 523(a)(6). They simply indicated in dicta that it was possible to create a *willful and malicious* injury solely as a result of the breach of contract.⁶⁰

The underlying facts of *Walker* and *Miller* help shed some light on the Fifth Circuit Court’s analysis in *Williams*. In *Walker*, the debtor signed an employment agreement with his employer, the University of Texas, which included a provision requiring him to turn over to the University certain professional fees he might receive.⁶¹ During his employment, Dr. Walker received considerable fees covered by the employment contract, but failed to remit them to the University.⁶² Dr. Walker filed for bankruptcy protection and the University claimed the failure of Walker to remit the fees constituted a breach of his employment agreement and a *willful and malicious* injury, which should be excluded from discharge. The Court found that although Walker’s keeping the fees was intentional, he lacked sufficient understanding of the employment agreement to willfully and maliciously cause the

⁵³ *Id.*

⁵⁴ *In re Williams*, 337 F.3d at 509 (quoting *Geiger*, 118 S.Ct. at 977).

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ *Texas v. Walker*, 142 F.3d 813 (5th Cir. 1998).

⁵⁹ *In re Miller*, 156 F.3d 598 (5th Cir. 1998).

⁶⁰ *Walker*, 124 F.3d at 823; *In re Miller*, 156 F.3d at 606.

⁶¹ *Walker*, 124 F.3d at 813.

⁶² *Id.* at 815.

University harm and thus allowed the discharge.⁶³ The *Walker* Court noted, however,

[I]f a factfinder were to decide that [the debtor] knew of his obligations under the... contract... then [a factfinder] might also find that [the debtor] knowingly retained his professional fees in violation of the [contract], an act which he knew would necessarily cause the University's injury. This, in turn, could result in a finding of 'willful and malicious' injury.⁶⁴

Thus, as the Fifth Circuit later noted in *Williams*, a bare breach of contract may create a *willful and malicious* injury if committed with the requisite specific intent.⁶⁵

The *Williams* Court cited *Miller* for the idea that the knowledge and intent of the debtor is more important than the type of conduct in establishing a *willful and malicious* injury. In *Miller*, the court did not decide the § 523(a)(6) issue but instead remanded the case for a determination of the defendant's intent or objective certainty to cause injury, holding that his actions could have been *willful and malicious* under § 523(a)(6) if they were "at least substantially certain to result in injury."⁶⁶

The *Williams* Court interpreted *Miller's* decision to remand the case as suggesting that the determination of the debtor's mental state in causing an injury was the penultimate decision regarding dischargeability under § 523(a)(6).⁶⁷ Thus, *Williams* held that regardless of where the debtor's behavior fell into accepted legal categories, discharge under § 523(a)(6) depended on the "knowledge and intent of the debtor at the time of the breach, *rather than whether conduct is classified as a tort or falls within another statutory exception.*"⁶⁸ Thus, in the Fifth Circuit, a breach of contract alone may constitute a *willful and malicious* injury given the appropriate proof of intent.

There is one anomalous, unreported Fifth Circuit case, *In re Deasy*, on this issue in which the court held that an intentional breach of contract without a separate intent to injure did not qualify as *willful* under § 523(a)(6).⁶⁹ The Court reviewed a creditor's claim that the debtor had caused him a *willful and malicious* injury by failing to pay his realtor's commission

⁶³ *Id.* at 824.

⁶⁴ *Id.*

⁶⁵ *Id.* at 510.

⁶⁶ *In re Miller*, 156 F.3d at 606.

⁶⁷ *In re Williams*, 124 F.3d at 510.

⁶⁸ *Id.* (emphasis added).

⁶⁹ *Cotton v. Deasy (In re Deasy)*, 2002 U.S. Dist. LEXIS 17851, 2002 WL 31114061 *6 (N.D. Tex. 2002), *aff'd*, *In re Deasy*, 66 Fed.Appx. 526, 2003 WL 21018189 (5th Cir. 2003).

as agreed.⁷⁰ Debtor Deasy had contracted with real estate broker Neal Cotten to pay him five percent of the sale price of his property if it sold before the end of April 1986.⁷¹ Deasy subsequently found a buyer on his own and signed a real estate contract on February 3rd with the closing set for May 1, 1986, one day after Cotten's listing ended.⁷² Cotten filed suit in state court and obtained a judgment for his unpaid commission of \$146,336.34.⁷³ When Deasy filed for bankruptcy protection, Cotten contested the dischargeability of the debt, claiming Deasy had caused a *willful and malicious injury*.⁷⁴

In a short opinion, issued shortly before the *Williams* decision was published, the Fifth Circuit construed *Geiger* as “explicitly reject[ing] a construction of ‘willful’ under which a breach of contract could qualify [under § 523(a)(6)].”⁷⁵ The Court also cited a post-*Geiger*, Ninth Circuit case as authority for the proposition that an intentional breach of contract can be excepted from discharge *only* when accompanied by willful, tortious conduct.⁷⁶ Since Deasy did not commit any tort along with the breach of contract, the Court held his debt could not be excepted from discharge as a matter of law.⁷⁷ Ironically, the *Deasy* Court also cited *Miller* (the same case cited a few months later in *Williams*) as support for its interpretation of *Geiger*.⁷⁸ The Fifth Circuit's apparent reversal of stance in the short time between the two opinions may explain why the *Deasy* opinion is not reported.

B. Tenth Circuit – *Sanders v. Vaughn*

The Tenth Circuit Court of Appeals has addressed this issue once in an unpublished opinion *Sanders v. Vaughn (In re Sanders)*.⁷⁹ In that case, Plaintiff Sanders hired attorney Vaughn on a contingent fee basis to assist him in an attempt to recover tax refunds from previous years from the Internal Revenue Service (IRS).⁸⁰ Vaughn secured a power of attorney from Sanders and negotiated a refund of approximately \$30,000.⁸¹ Before the IRS mailed the refund check, however, Sanders sent them a letter indicating that

⁷⁰ *In Re Deasy*, 2002 WL 31114061, at *2-4.

⁷¹ *Id.*

⁷² *Id.*

⁷³ *Id.*

⁷⁴ *Id.*

⁷⁵ *In Re Deasy*, 2002 WL 31114061, at *6.

⁷⁶ *See infra* Section IV.

⁷⁷ *In re Deasy*, 2002 WL 31114061 at *7-8.

⁷⁸ *Id.* at *6.

⁷⁹ *In re Sanders*, 210 F.3d 390 (Table): 2000 U.S. App. LEXIS 5763(10th Cir. 2000)(full text).

⁸⁰ *Id.* at *2.

⁸¹ *Id.*

he was revoking Vaughn's power of attorney and that the check should be sent directly to him (Sanders).⁸² In March of 1995, the IRS mailed the refund check to Sanders, care of Vaughn.⁸³ Sanders then filed a Taxpayer Statement Regarding Refund form, informing the IRS that he did not receive the check.⁸⁴ The IRS stopped payment on the first check mailed to Vaughn and issued a replacement check to Sanders, who cashed it and informed Vaughn that he did not owe Vaughn anything since he had terminated their agreement.⁸⁵ Vaughn filed suit against Sanders in Oklahoma state court and obtained a judgment based on Sanders' failure to pay the contingency fee. Shortly thereafter, Sanders filed for bankruptcy protection, and Vaughn instituted an adversarial action under § 523(a)(6) seeking to have the debt declared non-dischargeable. The trial court held that "because this was an act deliberately intended to harm Vaughn by avoiding his contractual right to the contingent fee it was willful and malicious under 11 U.S.C. § 523(a)(6), thereby exempting Sanders' debt to Vaughn from discharge."⁸⁶

Sanders appealed, arguing (1) the trial court committed an error of fact in finding he possessed the requisite intent to harm Vaughn, and (2) the U.S. Supreme Court expressly excluded breaches of contract from § 523(a)(6) in *Geiger*.⁸⁷ The Tenth Circuit Court of Appeals declined to overturn the trial court's finding of fact regarding Sanders' intent, finding it was not clearly erroneous.⁸⁸ The Court then turned to Sanders' interpretation of *Geiger*, calling it a "misreading" of the opinion.⁸⁹ According to the *Sanders* court, nothing in *Geiger* suggests the Supreme Court intended "to immunize debtors under § 523(a)(6) for willful and malicious breaches of contract."⁹⁰ Instead, it said *Geiger* simply stands for the proposition that a debtor must intend to cause an injury, not just commit an intentional act that causes an injury. Finding *Geiger* was silent on the application of § 523(a)(6) to contract breaches, the *Sanders* Court looked to the Fifth Circuit's *Walker* opinion for guidance.⁹¹ The *Walker* decision (at least in dicta) allowed for the possibility that breaches of contract could constitute *willful and malicious* injuries given the requisite proof of intent. Applying this reasoning to the

⁸² *Id.*

⁸³ *Id.* at *3.

⁸⁴ *In re Sanders*, 2000 U.S. App. LEXIS 5763 at *3.

⁸⁵ *Id.*

⁸⁶ *Id.* at *4.

⁸⁷ *Id.*

⁸⁸ The Court commented on the trial court's finding, "the bankruptcy court determined that Sanders's proffered explanations for his actions were not credible. The trial court stated, 'Frankly, it looked like Sanders figured out he was going to get these refunds, about \$30,000, (and thought) well, before I get them, I'm going to beat the lawyer out of his fees.'" *Id.* at *6.

⁸⁹ *In re Sanders*, 2000 U.S. App. LEXIS 5763 at *8.

⁹⁰ *Id.*

⁹¹ *Id.*

facts in *Sanders*, the Tenth Circuit affirmed the district court's ruling that Sanders's deliberate breach constituted a *willful and malicious* injury under § 523(a)(6).⁹² Had the *Sanders* decision been published, it would represent a direct precedent in the Tenth Circuit for allowing an intentional breach of contract, without accompanying tortious behavior, to satisfy the *willful and malicious*.

V. CIRCUITS REFUSING TO APPLY SECTION 523(A)(6) TO DEBTS ARISING FROM DAMAGES CAUSED SOLELY BY A BREACH OF CONTRACT

In contrast to the Fifth and Tenth Circuits decisions discussed above, other courts have adopted the traditional view of § 523(a)(6) as applying only to tortious behavior.

A. Ninth Circuit – *In Re Jercich*

The Ninth Circuit Court of Appeals has been the most consistent in its approach to the application of § 523(a)(6) to injuries caused by a breach of contract. Prior to *Geiger*, the Ninth Circuit held in *In re Riso*, holding, “[i]t is well settled that a simple breach of contract is not the type of injury addressed by § 523(a)(6).”⁹³ Since *Geiger*, the Court has remained consistent in this position, most recently addressing the issue in the 2001 *In re Jercich*.⁹⁴

In *Jercich*, the employee Petralia sued realtor Jercich in California state court for unpaid wages, statutory penalties relating to the non-payment of wages and punitive damages. Petralia was granted a judgment, with the trial court finding that Jercich had the means to pay Petralia, but instead used the funds personally.⁹⁵ The trial court found Jercich's refusal to be willful and “oppressive” under California statutory law, subjecting Jercich to additional penalties, including punitive damages.⁹⁶ After the judgment was entered, Jercich filed a bankruptcy petition and Petralia filed an adversarial proceeding seeking to have the judgment excepted from discharge under § 523(a)(6). The trial court found in favor of Jercich, holding that since the

⁹² *Id.*

⁹³ *In re Riso*, 978 F.2d 1151 (9th Cir. 1992), *See also* *Barbachano v. Allen*, 192 F.2d 836 (9th Cir. 1951); *In re Akridge*, 71 B.R. 151 (Bankr. S.D. Cal. 1987).

⁹⁴ *In re Jercich*, 238 F.3d 1202 (9th Cir. 2001).

⁹⁵ *Id.* at 1203-04.

⁹⁶ California's Civil Code allows for punitive damages where it is proven by clear and convincing evidence that the defendant has committed fraud, oppression or malice. California Civil Code § 3294.

state court did not find specifically that Jercich had the intent to cause Petralia harm, the specific-intent-like injury requirement of *Geiger* was not satisfied. The case was appealed to the Bankruptcy Appellate Panel (BAP), which affirmed the decision for Jercich, but for a different reason. The BAP held that where the debtor commits both a breach of contract and a tort, the resulting injury is not covered by § 523(a)(6) unless the tort is independent of the breach of contract. The BAP defined “independent” as conduct that would be tortious even in the absence of an agreement between the parties.⁹⁷

The Ninth Circuit overturned both prior decisions, holding that no tort independent of a contract need exist to be subject to § 523(a)(6).⁹⁸ The *Jercich* court noted that tortious conduct related to the breach of the contract (such as interference with contractual relations, fraud, etc.) may constitute a willful and malicious injury. The court reasoned that requiring a tort separate from the existence of a contract would unduly limit one of the fundamental principles of bankruptcy—allowing the “honest but unfortunate debtor” a “fresh start.”⁹⁹

While finding that a separate tort distinct from the breach of contract did not need to exist, the Ninth Circuit was not willing to go as far as the Fifth Circuit’s holding that a bare breach of contract may create a *willful and malicious injury* if committed with the requisite specific intent.¹⁰⁰ The *Jercich* court made it clear that tortious behavior must also be present. In its analysis, the court stated, “we therefore hold that to be excepted from discharge under § 523(a)(6), a breach of contract must be accompanied by some form of tortious conduct that gives rise to a ‘willful and malicious injury.’”¹⁰¹ Subsequent courts have seized on the highlighted portion above to use *Jercich* as authority for the position that some tortious conduct is necessary and that a bare breach of contract cannot create a willful and malicious injury under § 523(a)(6).¹⁰²

B. Sixth Circuit – *In Re Best*

The Sixth Circuit (although an unpublished opinion) has also held a breach of contract cannot render a debt nondischargeable under § 523(a)(6). In *In re Best* debtor, Michael Best, was an orthopedic surgeon whose

⁹⁷ *In re Jercich*, 238 F.3d at 1204 (citing *In Re Jercich*, 234 B.R. 747 (9th Cir. BAP 2000)).

⁹⁸ *Id.* at 1205.

⁹⁹ *Id.* at 1206.

¹⁰⁰ *In re Williams*, 124 F.3d at 510.

¹⁰¹ *In re Jercich*, 238 F.3d at 1206.

¹⁰² *In re Picard*, 339 B.R. 542, 555 (Bankr. D. Conn. 2006) (“However, a breach of contract unaccompanied by tortious conduct (e.g., conversion of collateral) does not give rise to a Section 523(a)(6) nondischargeability claim.”); *In re Jacobs*, 381 B.R. 128, 133 (Bankr. E.D. Pa. 2008).

corporation conducted disability exams for worker's compensation claimants.¹⁰³ Plaintiff Anthony Steier invested \$300,000 in the corporation but later sued, claiming Best had failed to honor a contract condition entitling him to the refund of his stock purchase price.¹⁰⁴ Steier obtained a judgment against Best for breach of contract, and Best filed a bankruptcy petition. Steier filed an adversarial action under § 523(a)(6), claiming Best had maliciously concealed his assets to prevent Steier from collecting on the judgment. The Bankruptcy Court granted summary judgment for Best and Steier appealed.¹⁰⁵

The Sixth Circuit Court of Appeals affirmed the lower court's decision, holding Best's debt to be dischargeable.¹⁰⁶ The main issue resolved by the Court was whether the post-judgment activity of the debtor could qualify under the *willful and malicious injury* exception. The Sixth Circuit held that, under § 523(a)(6), the creditor has the burden of proving that it sustained an injury as a result of a willful and malicious act on the part of the debtor.¹⁰⁷ Since Best's actions (hiding assets to avoid execution of the judgment) occurred *after* the debt had been incurred, the concealment could not have caused or given rise to the judgment debt.

Creditor Steier also claimed Best's original failure to repay his investment constituted willful and malicious behavior in its own right.¹⁰⁸ The court ruled that Best's failure to pay Steier amounted to a breach of contract, but that "consistent with *Geiger*, we have held that *a breach of contract cannot* constitute the willful and malicious injury required to trigger Section 523(a)(6)."¹⁰⁹ Thus, the Sixth Circuit made clear that it interprets *Geiger* as rejecting a bare breach of contract as a willful and malicious injury. This decision seems to align the Sixth Circuit with the Ninth, in requiring that some sort of tortious conduct must accompany the breach of contract for it to fall under the exception of § 523(a)(6).

VI. LOWER COURT DECISIONS FROM CIRCUITS WITH NO CLEAR RULE REGARDING BREACH OF CONTRACT AND SECTION 523(A)(6)

Although no other federal Circuit Courts of Appeals have addressed this issue directly since *Geiger*, several district courts have. The lower court decisions in circuits not mentioned above generally follow the Ninth and

¹⁰³ *In re Best*, No. 03-5098; 2004 U.S. App. LEXIS 13773 (6th Cir. 2004).

¹⁰⁴ *Id.*

¹⁰⁵ *Id.* at *2-4.

¹⁰⁶ *Id.*

¹⁰⁷ *Id.* at *4.

¹⁰⁸ *In re Best*, 2004 U.S. App. LEXIS 13773 at *8.

¹⁰⁹ *Id.* (emphasis added).

Sixth Circuits in requiring tortious behavior for a breach of contract to fall under the willful and malicious injury exception of § 523(a)(6). While bankruptcy and district court decisions have limited precedential value, it is significant that none seem to have taken the position of the Fifth and Tenth Circuits that a bare breach of contract can justify a discharge exception. The lower court decisions also demonstrate the need clarification when addressing *willful and malicious* contractual claims under § 523(a)(6).

A. Lower Courts In The Second Circuit – Breach of Contract Alone insufficient

The lower court opinions in the Second Circuit since *Geiger* have generally required a finding of independent tortious activity before excepting contractual damages from discharge.¹¹⁰ The most recent decision on the issue, *In re Picard*, came from the U.S. Bankruptcy Court in the Central District of Connecticut in 2006.¹¹¹ In *Picard*, the debtor personally guaranteed repayment of credit extended to his company.¹¹² Piccard subsequently filed for bankruptcy under Chapter 7, seeking to discharge his personal obligation under the guarantee. The creditor alleged that prior to filing the bankruptcy petition, Piccard fraudulently transferred assets out of his bankruptcy estate making them unavailable to satisfy his debt.¹¹³ The Court found the debtor had not committed any fraudulent transfers, and that his inability to perform on the guarantee was simply a breach of contract.¹¹⁴ Citing several Ninth Circuit cases, including *Jercich*, the Court held, “a breach of contract unaccompanied by tortious conduct (e.g., conversion of collateral) does not give rise to a Section 523(a)(6) nondischargeability claim.”¹¹⁵

B. Lower Courts In The Third And Fourth Circuits – No Clear Rule

The Third and Fourth Circuits each have lower court decisions regarding nondischargeability of debts arising from contract breaches. The

¹¹⁰ *In re Mitchell*, 227 B.R. 45 (Bankr. S.D.N.Y. 1998)(holding since the debtor failed to prove independent tortious activity, the breach of contract claim was outside the exception of Section 523(a)(6)); *In re Radcliffe*, 317 B.R. 581 (Bankr. D. Conn. 2004)(debt for breach of promise to repay loan discharged absent proof of tortious conduct was not willful and malicious conduct); *In re Picard*, 339 B.R. 542 (Bankr. D. Conn. 2006).

¹¹¹ *See In re Picard*, 339 B.R. at 542.

¹¹² *See id.*

¹¹³ *See id.*

¹¹⁴ *Id.* at 554.

¹¹⁵ *Id.* at 555 (citing *In re Saylor*, 108 F.3d 219 (9th Cir. 1997); *In re Riso*, 978 F.2d 1151 (9th Cir. 1992); 238 F.3d 1202 (9th Cir. 2001)).

U.S. Bankruptcy Court for the Eastern District of Pennsylvania, in the Third Circuit, seemingly adopted the position of the Ninth and other Circuits requiring tortious activity to accompany a breach of contract in *In re Jacobs*.¹¹⁶ Without specifically adopting the rule in *Jercich* (requiring an accompanying tort in order to qualify under § 523(a)(6)), the *Jacob* court opined that some limiting principle was necessary to keep § 523(a)(6) from being overbroad.¹¹⁷ It was unsuccessfully argued in *Jacob* that a debt arising from a deliberate decision to breach a contract almost always falls within the *willful and malicious* category, since the breaching party in most cases is substantially certain the breach will cause an injury to the non-breaching party.¹¹⁸ In dismissing this argument, the *Jacob* Court held that such a broad interpretation of § 523(a)(6) was not what Congress intended. Citing *Riso* and *Jercich*, the Court stated, “the most obvious limiting principle would be the requirement that the creditor’s injury be caused by ‘tortious’ conduct, not by breach of contract.”¹¹⁹ They concluded that such a limitation would be consistent with the U.S. Supreme Court’s decision in *Geiger*.¹²⁰

In the Fourth Circuit, one of lower court cases clearly followed the Ninth Circuit in requiring an intentional tort, but another issued an ambiguous decision that could be interpreted as allowing a breach of contract alone to constitute willful and malicious conduct. In *In re Heilman*, the U.S. Bankruptcy Court for the District of Maryland held that breaches of contract do not constitute a willful and malicious injury unless the conduct is also an intentional tort, such as conversion.¹²¹ The court stated, “A mere technical conversion does not fall within the scope of Section 523(a)(6) either. A wrongful and intentional deprivation of another’s property is required. Furthermore, Section 523(a)(6) requires that the nondischargeable debt arise out of a tort as opposed to a breach of contract.”¹²²

The U.S. Bankruptcy Court for the Eastern District of Pennsylvania employed similar reasoning but was less clear in its holding in *In re Harland*.¹²³ In that case, the Plaintiff argued that its claims were nondischargeable under § 523(a)(6) because the debtor was found to have deliberately and willfully breached his employment contract and covenant

¹¹⁶ *In re Jacobs*, 381 B.R. 128 (Bankr. E.D. Penn. 2008).

¹¹⁷ *See id.*

¹¹⁸ *See id.* at 138.

¹¹⁹ *Id.*

¹²⁰ *Id.*

¹²¹ *In re Heilman*, 241 B.R. 137 (Bankr. D. Md. 1999) (citing *In re Riso* 978 F.2d 1151 (9th Cir. 1992)).

¹²² *Id.* at 172. The Court also cited older, pre-*Geiger* cases, such as: *In re Haynes*, 19 B.R. 849 (Bankr. E.D. Mich.1982); *Barbachano v. Allen*, 192 F.2d 836 (9th Cir.1951); *but see Rivera v. Moore-McCormack Lines, Inc.*, 238 F.Supp. 233 (S.D.N.Y.1965).

¹²³ *In re Harland*, 235 B.R. 769 (Bankr. E.D. Pa. 1999).

not to compete by misappropriating confidential business information. The court cited for the proposition that nondischargeability takes a deliberate or intentional injury, not merely a deliberate or intentional act that leads to injury.¹²⁴ Applying the *Geiger* holding to the facts of *Harland*, the Court concluded:

[T]he Debtor clearly acted intentionally, and his actions clearly resulted in injury to the Plaintiff. However, by the very terms of State Court's findings, the Debtor's intent was focused entirely on maximizing his personal financial interests, not intentionally harming the Plaintiff. The injury which resulted flowed from the Debtor's breaches of his contract, but there is no finding that it actually was a goal of the scheme he pursued, as opposed to the goal of benefitting himself. We must therefore hold that the instant record is insufficient to support the Plaintiff's claims under § 523(a)(6).¹²⁵

While the court found insufficient evidence of specific intent to harm in that case, it did not foreclose the possibility that a breach of contract could result in a nondischargeable debt. The court rested its decision on the lack of evidence of intent, rather than the type of injury present, implying that had the debtor possessed the requisite intent when he breached the contract, the injury could be considered willful and malicious.¹²⁶

C. Lower Courts In The Seventh Circuit – Tort Required To Be Willful and Malicious

In *In re Salvino*, the U.S. District for the Northern District of Illinois (in the Seventh Circuit) has directly addressed the question of whether a “bare” breach of contract, without any accompanying tortious behavior, could constitute a willful and malicious injury under § 523(a)(6).¹²⁷ The *Salvino* case arose from the sale of a company, WISH Holding, LLC (hereafter “Old Wish”), which operated numerous bariatric surgery centers around the country.¹²⁸ The business was created in 1992 and financed with accounts receivables, real estate and a personal guarantee from Doctors Salvino, one of the principle physicians at the surgery centers.¹²⁹ In 2005, Old Wish

¹²⁴ *Id.* at 779.

¹²⁵ *Id.*

¹²⁶ *Id.*

¹²⁷ *See In re Salvino*, 2008 WL 182241 (N.D. Ill. 2008).

¹²⁸ *See id.*

¹²⁹ *See id.*

defaulted on its loans, and in an effort to repay the bank, raised money from new investors who formed an entity called WISH Acquisition LLC. During negotiations between Old Wish and WISH Acquisition, Dr. Salvino signed an employment agreement that included a five year commitment to stay with the company. Old Wish filed a Chapter 11 Bankruptcy case to facilitate WISH Acquisition's purchase of assets, but before the filing, Dr. Salvino sought alternative employment in violation of his agreement. On July 14, 2005, the Bankruptcy Court approved the sale of Old Wish's assets and WISH Acquisition agreed to amend Salvino's employment agreement. The amended agreement required Salvino to commit to WISH Acquisition for five years, and in exchange released him from his remaining \$1.5 million guarantee. The employment agreement also included a liquidated damages provision requiring Salvino to pay damages of \$1.5 million if he terminated the contract during the first year, with declining damages for a breach each year thereafter. Within seven days of the closing on the final sale, Dr. Salvino sought employment at John C. Lincoln Hospital, where he ultimately accepted a full time position. Shortly thereafter, Dr. Salvino and his wife filed for Chapter 7 bankruptcy, seeking a discharge of his personal debts, including the liquidated damages from his agreement with WISH Acquisition. WISH Acquisition filed a complaint with the Bankruptcy Court seeking to declare Salvino's debt nondischargeable under § 523(a)(6).¹³⁰

The U.S. Bankruptcy Judge issued a memorandum decision in which he found Salvino's debt dischargeable since the injury was created solely by a breach of contract with no accompanying tort. WISH Acquisition appealed the decision to the U.S. District Court for the Northern District of Illinois, without contesting the fact that its injury was the result of a breach of contract alone. In its opinion, the Court first noted that the Seventh Circuit had not addressed the issue directly since *Geiger*. The *Salvino* court then recognized the Circuit split between the Fifth Circuit (*In re Williams*) and the Ninth Circuit (*In re Jercich*) on the issue of whether tortious conduct is a requirement for § 523(a)(6). The district court concurred with the reasoning of the Bankruptcy Judge, holding that the better rule is the one requiring tortious conduct as an essential element of a *willful and malicious* injury. In so finding, the court adopted four basic reasons stated by the Bankruptcy Judge in his memorandum:

- (1) [T]he common application of "willful and malicious" strongly suggests its limitation to torts, making nondischargeable only debts arising from the same sort of conduct that the common law discourages by punitive damages;
- (2) the reenactment of the "willful and malicious injury" standard for nondischargeability

¹³⁰ See *id.*

from the Bankruptcy Act of 1898 indicates Congress' presumptive intent to continue the established practice of limiting its application to tortious conduct; (3) the common law definition of "willful and malicious" applied by the Fifth Circuit, which encompasses not only actual intent to harm but also intentional acts that the debtor believes are substantially certain to cause harm, was not developed in connection with breach of contract, and when applied in the context of Section 523(a)(6) dramatically expands the number of nondischargeable debts and diminishes the scope of bankruptcy discharge; and (4) making intentional breaches of contract nondischargeable under § 523(a)(6) would create substantial tension with § 365(a) of the Bankruptcy Code, which authorizes a debtor to intentionally breach a contract if doing so will maximize the value of the debtor's property.¹³¹

For these reasons and to preserve the integrity of the bankruptcy discharge, the court held unequivocally that tortious conduct is an essential element of a willful and malicious injury under § 523(a)(6). It remains to be seen whether the Seventh Circuit, and others, follow *Salvino* in an effort to unify this rule.

VII. ANALYSIS – WHY THE CIRCUITS SHOULD REQUIRE TORTIOUS BEHAVIOR IN ADDITION TO A BREACH OF CONTRACT UNDER SECTION 523(A)(6)

Section 523(a)(6) and *Geiger* should be interpreted to require tortious behavior in addition to a breach of contract to be considered a *willful and malicious* injury. This reasoning (1) is more consistent with statutory construction, (2) promotes uniformity and efficiency, and (3) prevents an unwise merger between what constitutes a tort versus a breach of contract.

A. Statutory Construction

The most persuasive reason for adopting the tort requirement for § 523(a)(6) is that it is more consistent with traditional statutory interpretation methods. As the Supreme Court in *Geiger* pointed out, the phrase "willful and malicious injury...triggers in the lawyer's mind the category of intentional torts."¹³² The use of the terms *willful* and *malicious* in the law generally connotes a level of reprehensibility of conduct that points to, at a

¹³¹ *Id.* at 10-11.

¹³² *Kawaauhau v. Geiger*, 523 U.S. 57, 61 (1998).

minimum, tortious behavior. In fact, the term malicious is often associated in the civil law with a high degree of reprehensibility and is used often in conjunction with the assessment of punitive damages. The Bankruptcy Judge in *Salvino* cited the venerable treatise Prosser on Torts to describe this recognized meaning:

Something more than mere commission of a tort is always required for punitive damages. There must be circumstances of aggravation or outrage, such as spite or ‘malice’, or a fraudulent or evil motive on the part of the defendant, or such a conscious and deliberate disregard of the interest of others that his conduct may be called willful or wanton.¹³³

Further, placing this in a historical context, the phrase *willful and malicious* indicates a desire to include not only intentional tortious conduct, but that which is so wrongful, it must be deterred.¹³⁴ The same motive is not applicable in the contract arena however. Generally, the motive behind a breach of contract is irrelevant, given that punitive damages are not generally

¹³³ *In re Salvino*, 2007 WL 2028577 (Bankr. N.D. Ill. 2007) citing William Prosser, *The Law of Torts* Section 2 at 9-10 (4th ed. 1971).

¹³⁴ See *Brandon v. Anesthesia & Pain Mgmt. Assocs., Ltd.*, 277 F.3d 936 (7th Cir. 2002) (Punitive damages...may be awarded where torts are committed with fraud, actual malice, deliberate violence or oppression, or when the defendant acts willfully, or with such gross negligence as to indicate a wanton disregard of the rights of others); *Nakajima v. General Motors Corp.*, 857 F.Supp. 100 (D.D.C. 1994) (Punitive damages are not favored under District of Columbia law; they may be awarded only if plaintiffs prove, by at least preponderance of evidence, that defendant’s conduct is willful and outrageous, exhibits recklessness and willful disregard of the rights of others, or is aggravated by evil motive, actual malice, or deliberate violence or oppression); *T & S Serv. Assocs., Inc. v. Crenson*, 505 F.Supp. 938 (D.R.I., 1981) (A plaintiff seeking punitive damages under law of Rhode Island must demonstrate that defendant has acted with malice, wantonness or willfulness of such an extreme nature as to amount to criminality which, for good of society and warning to individual, ought to be punished); *Northern v. McGraw-Edison Co.*, 542 F.2d 1336 (8th Cir. 1976) (In Missouri, punitive damages are awarded for the purpose of punishing the wrongdoer and to serve as an example and deterrent to others engaging in similar conduct in the future; punitive damages are allowed only when there is a finding of legal malice); *Wegner v. Rodeo Cowboys Ass’n.*, 290 F.Supp. 369 (D.Colo., 1968) (Exemplary damages are awarded for purpose of punishing persons who have inflicted injuries with malice); *Williams v. Jader Fuel Co., Inc.*, 944 F.2d 1388 (7th Cir. 1991) (Illinois courts take dim view of punitive damages, and insist that plaintiff seeking them demonstrate extraordinary or exceptional circumstances clearly showing malice or willfulness); *Oros v. Hull & Assocs., Inc.*, 302 F.Supp.2d 839 (N.D. Ohio. 2004) (Party seeking punitive damages must establish that the offending party acted with actual malice); *West Des Moines State Bank v. Hawkeye Bancorporation*, 722 F.2d 411 (8th Cir. 1983) (Under Iowa law, award of punitive damages is designed to deter and punish, and should be made only upon finding of either actual or legal malice); *Morse v. Duncan*, 14 F. 396 (C.C.S.D.Miss., 1882) (In the absence of gross negligence, recklessness, willfulness, malice, insult, or inhumanity, actual damages can only be allowed).

available.¹³⁵ Thus, to interpret the *willful and malicious* language of § 523(a)(6) as including a breach of contract, even when committed to cause a specific injury to the non-breaching party, without an accompanying tort, would be inconsistent with its historical meaning.

Another reason mentioned in *Salvino* for adopting the tort requirement under Bankruptcy Code § 523(a)(6) is that the legislative history supports such an interpretation.¹³⁶ As discussed in Section II above, the sections of the Code relating to exceptions to discharge have been amended repeatedly since their inclusion in the Bankruptcy Act of 1898. Prior to the *Geiger* case, and prior to the latest amendment to § 523(a)(6) of the Code, the *willful and malicious* exception has always been synonymous with tortious conduct.¹³⁷ Moreover, the legislative history of the 1978 amendment of the Bankruptcy Code suggests Congress intended to overrule an interpretation that a debt could be non-dischargeable even if the debtor did not specifically intend the injury.¹³⁸ Nothing in the legislative history, however, indicated a Congressional intent to change the application of the *willful and malicious* standard to suddenly include conduct that does not involve the commission of a tort. Neither the Fifth nor the Tenth Circuit indicated in their decisions, *Williams* and *Sanders* respectively any reason to alter the historical interpretation that a breach of contract must be accompanied by tortious behavior or intentional infliction of harm to be non-dischargeable.

B. Uniformity And Efficiency

Allowing a bare breach of contract to be included in the willful and malicious injury language of § 523(a)(6) could cause the bankruptcy courts to be flooded with claims and litigation. The term *willful and malicious* has been defined by the Supreme Court in *Geiger*, and restated in subsequent decisions. *Geiger* establishes that § 523(a)(6) applies to acts committed with the actual intent to cause injury, but excludes intentional acts that cause injury.¹³⁹ Broken down further, the term *willful* modifies the word *injury*,

¹³⁵ In general, motive is irrelevant to a breach of contract claim. See *Globe Ref. Co. v. Landa Cotton Oil Co.*, 190 U.S. 540 (1903) (The motive for the breach commonly is immaterial in an action on the contract.); *Koufakis v. Carvel*, 425 F.2d 892, 906 (2d Cir.1970) (A breach is a breach; it is of marginal relevance what motivations led to it.); *Weiskopf v. Am. Kennel Club, Inc.*, NO. 00-CV-471, 2002 WL 1303022, at *6 n. 1 (E.D. N.Y. 2002) (motive irrelevant to claim of breach of contract).

¹³⁶ See *In re Salvino*, 2007 WL 2028577 at *8.

¹³⁷ See *In re Haynes*, 19 B.R. 849 (Bankr. E.D. Mich. 1982) (“Moreover, any realistic reading of the discharge and dischargeability provisions of the Code clearly establishes that the Section 523(a)(6) exception, like section 17(a)(8) from which it is derived, was not intended to make non-dischargeable debts arising from mere breach of contract.”).

¹³⁸ See *In re Salvino*, 2007 WL 2028577 at *8.

¹³⁹ *Geiger*, 523 U.S. at 59.

indicating that non-dischargeability requires a deliberate or intentional injury, not simply an intentional act that happens to cause an injury.¹⁴⁰ The term *malice* was not directly defined in *Geiger*, but subsequent courts have allowed an implied malice standard to suffice under § 523(a)(6).¹⁴¹ The Restatement (Second) of Torts defines the willful and malicious standard as, “if the actor knows that the consequences are certain, or substantially certain, to result from his act, and still goes ahead, he is treated by the law as if he had in fact desired to produce the result.”¹⁴² Similarly, the Fifth Circuit held the intent to injure under § 523(a)(6) requires only, “a showing that the debtor intentionally took action that necessarily caused, or was substantially certain to cause, the injury.”¹⁴³ This definition allows malice to be implied to circumstances where the debtor does not overtly exhibit an intent to cause injury, but that such intent may be implied from his/her actions.

If the courts allow a willful and malicious injury to be established by showing that a debtor was *substantially certain* that an injury would occur as a result of a breach of contract, the proverbial floodgates would be opened to litigation on the issue. Logically, it could be argued that nearly all breaches of contract could constitute *willful and malicious* injuries. Every breach of a contractual obligation to pay for goods or services (e.g., non-payment of rent, default on credit card debt, or mortgage debt, failure to pay medical bills), as long as non-payment is intentional, is substantially certain to cause an injury to the non-breaching party.¹⁴⁴ Almost every debt incurred is contractual (from credit cards to unsecured bank loans) and every debtor foresees that non-payment will financially harm the creditor. If this means every debt could conceivably be non-dischargeable, the exception swallows the rule. The Supreme Court recognized this hazard in *Geiger*, when it held, “A knowing breach of contract could also qualify. A construction so broad would be incompatible with the ‘well known’ guide that exceptions to discharge should be confined to those plainly expressed.”¹⁴⁵ The result of allowing an intentional breach of contract, under the implied malice standard, to constitute a willful and malicious injury would be to increase the amount of litigation, decrease the efficiency of the Bankruptcy system and significantly dilute the effect of the bankruptcy discharge.

Additionally, allowing intentional breaches of contract without any accompanying tortious activity to constitute willful and malicious injuries under § 523(a)(6) would create inconsistencies within the Bankruptcy Code.

¹⁴⁰ *See id.*

¹⁴¹ *See In re Williams*, 337 F.3d at 509; *see also, Walker*, 142 F.3d at 823.

¹⁴² RESTATEMENT (SECOND) OF TORTS, Sec. 8A, Comment b (1965).

¹⁴³ *See In re Williams*, 337 F.3d at 509.

¹⁴⁴ *See In re Salvino*, 2007 WL 2028577 at *8.

¹⁴⁵ *Geiger*, 523 U.S. at 62.

Section 365(a) of the Code allows a debtor to reject executory contracts that are not in the best interest of the bankruptcy estate.¹⁴⁶ *Salvino* recognized this inconsistency noting,

[T]he rejection of an executory contract is a breach, always intentional, that will almost certainly harm the other party (since a contract burdensome to the estate is likely beneficial to that party). Thus, if Section 523(a)(6) applied to contract, the Code would punish under that provision the very conduct it encourages under Section 365(a).¹⁴⁷

To maintain consistency, uniformity and certainty, any interpretation that puts two portions of the same law at odds should not be accepted.

C. Unwise Merger of Contract And Tort

The final reason the Fifth and Tenth Circuits' interpretation of § 523(a)(6) should be rejected is that it represents a step toward the elimination of the distinction between contracts and torts. Allowing a breach of contract to constitute a *willful and malicious* injury, a status previously reserved for torts only, represents a shift in the legal division of the two areas of law. Contract actions are created to enforce the intentions of the parties to an agreement, whereas tort law is primarily designed to enforce public policy.¹⁴⁸ When we begin to allow parties with a contract claim to access the remedies or utilize attributes exclusive to torts, then the distinctions between tort and contract become meaningless and the purposes behind the distinctions are thwarted. According to some, it is happening already, not just in the area of Bankruptcy, but in all areas of business litigation. More and more, when attorneys file a claim for a breach of contract, they will include a negligence and/or fraud claim arising out of the non-performance of the contract in order to attempt to access the additional tort remedies. Courts are faced with an intentional blurring of the two causes of action into one "contort" claim, described as the "nebulous and troublesome region where tort and contract law intersect and where finding the dividing line between the two fields is often difficult."¹⁴⁹

¹⁴⁶ 11 U.S.C. § 365(a) (1978).

¹⁴⁷ *In re Salvino*, 2007 WL 2028577 at *9.

¹⁴⁸ See *Applied Equip. Corp. v. Litton Saudi Arabia Ltd.*, 869 P.2d 454 (Cal. 1994); See also *Foley v. Interactive Data Corp.*, 47 Cal.3d 654 (1988).

¹⁴⁹ Christopher W. Arledge, *When Does a Breach of Contract Also Give Rise To a Tort Claim? A Primer for Practitioners*, 48 ORANGE COUNTY LAWYER 42 (2006).

Some courts are willing to entertain a blurring of the distinction between contract and tort in order to access tort remedies (e.g., economic and punitive damages) to attempt to vindicate a sympathetic plaintiff. This is nothing new, as courts have always been sympathetic to victims of intentional breaches of contract, especially when the facts are egregious. Perhaps it was even this phenomenon that gave rise to the law school axiom, “bad facts make bad law.”

It seems wise, however, for courts to resist the temptation to punish the breaching party in a contract dispute for his/her motives for the breach. The goal of contract remedies has always been to compensate the innocent party for the breach, rather than compel the promisor to perform.¹⁵⁰ A contract creates reciprocal, private duties for its parties. Freedom of contract allows the parties themselves to negotiate the rules and conditions that will give rise to and govern their legal obligations. The parties are able to negotiate their exposure to potential liability and take on only those risks they deem acceptable. It follows that contract actions enforce the parties’ intentions and private, bargained-for obligations, whereas tort actions are designed to compensate the victim for all his/her injuries based on enforcement of a social duty. There is typically little ability to negotiate the terms and application of a social duty prior to acting.

Basic concepts of *fairness* would dictate that contract remedies should be confined to those damages within the contemplation of the parties. The California Supreme Court explained that limited contract damages, “serves to encourage contractual relations and commercial activity by enabling parties to estimate in advance the financial risks of the enterprise.”¹⁵¹ Confusing the potential liability to contractual parties by combining tort and contract remedies works to undermine the basic and recognized common law goals of contract remedies.

The bottom line is that a breakdown in the distinction between contract and tort would serve to increase risk in contracts, creating higher transaction costs, less efficiency and could create a chilling effect on contract creation. Although allowing a breach of contract to join tortious conduct in creating a *willful and malicious* injury under Bankruptcy Code § 523(a)(6) will not, by itself, eliminate all distinctions between contracts and torts, it is a step down the slippery slope of that direction.

¹⁵⁰ See generally William S. Dodge, *The Case for Punitive Damages in Contracts*, 48 DUKE L.J. 629, 630 (1999).

¹⁵¹ *Erlich v. Menezes*, 981 P.2d 978, 982 (Cal. 1999).

VIII. CONCLUSION

While the U.S. Supreme Court's opinion in *Kawaauhau v. Geiger* may have cleared up some confusion as to the definition of the terms *willful and malicious* under Bankruptcy Code § 523(a)(6), its language may have actually created more uncertainty concerning the application of the same terms in matters of contract. As specifically noted above, two appellate courts (the Fifth and Tenth Circuits) have interpreted *Geiger* to mean that a breach of contract alone can be willful and malicious if the debtor intends to cause injury or is substantially certain that an injury will result to the nonbreaching party. Two other circuits—and nearly all other reported cases on this issue from lower courts in the remaining circuits—disagree, holding separate tortious conduct must accompany the breach to make it nondischargeable. The latter seems to be the more logical, practical, and theoretically consistent rule. Section 523(a)(6) and *Geiger* should be interpreted to require tortious behavior in addition to a breach of contract in order to be considered a *willful and malicious* injury.