Causes of Action Owned by a Debtor

Garik Osipyants, Moderator
Thav Gross PC; Bingham Farms

A. Todd Almassian
Keller & Almassian, PLC; Grand Rapids

Krispen S. Carroll
Chapter 13 Trustee's Office; Detroit

Hon. Thomas J. Tucker
U.S. Bankruptcy Court (E.D. Mich.); Detroit

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WHEN IS PROPERTY OF THE ESTATE

DISTINCTION BETWEEN CAUSES OF ACTION THAT ARISE PRE-PETITION, POST-PETITION, POST-CONFIRMATION, AND POST-DISCHARGE.

KELLER & ALMASSIAN, PLC
A. TODD ALMASSIAN AND NICHOLAS S. LAUE

"When" is a cause of action property of the estate? The answer can be extremely complex. This is especially true when the debtor has a cause of action that may not have matured pre-petition. In answering this question, bankruptcy practitioners are required to determine when the cause of action matured. Thereafter, the bankruptcy practitioner must distinguish between pre-petition, post-petition, post-confirmation, and post-discharge causes of actions. Depending upon where the cause of action falls in relation to the bankruptcy filing, the debtor may or may not be entitled to keep all of the proceeds generated from the cause of action.

Determining the time at which a cause of action becomes bankruptcy property can be complicated. The question is not "what is property of the estate" but is rather "when is property of the estate." This determination requires fact intensive analysis. Whatever opinion the Debtor or counsel may have – full and complete disclosure is required and full disclosure is the best means by which to preserve a cause of action for the debtor and the estate. Failure to do so can result in the Debtor being estopped from pursuing a cause of action and potentially lead to a malpractice action against debtor's counsel.

I. Pre-petition Property

Depending on the relief pursued – (1) liquidation under chapter 7, or (2) reorganization under chapter 13 – there is a sliding spectrum between causes of action that are "property of the estate" and claims that are not property of the estate.

A. 11 U.S.C. 541

In its simplest form, a bankruptcy estate is formed upon the filing of a bankruptcy petition. According to the Bankruptcy Code, the estate consists of: "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). Sometimes this is a challenge for clients to understand. The bankruptcy estate includes all causes of action that exist and have matured as of the date of the petition. State substantive law determines the "nature and extent" of causes of action, see *Tyler v. DH Capital Mgmt., Inc.*, 736 F.3d 455, 461 (6th Cir. 2013), but federal bankruptcy law dictates when that property interest becomes property of the estate for purposes of § 541, see *In re Terwilliger's Catering Plus, Inc.*, 911 F.2d 1168, 1172 (6th Cir. 1990)." *In re Underhill*, 579 F. App'x 480, 482 (6th Cir., 2014).

B. "Sufficiently rooted in the pre-bankruptcy past…"

In determining whether a cause of action is pre-petition belonging to the estate, or post-petition belonging to the debtor, the Sixth Circuit applies the approach described in *Segal v. Rochelle*, 382 U.S. 375, 380, 86 S. Ct. 511, 15 L. Ed. 2d 428 (1966). See *In re Underhill*, 579 F. App'x 480, 482 (6th Cir., 2014). (applying *Segal*). Under *Segal*, pre-petition assets are those that are "sufficiently rooted in the pre-bankruptcy past." *Tyler v DH Capital Mgmt.*, 736 F.3d 455, 461 (6th Cir., 2013) "Pre-petition conduct or facts alone will not 'root' a claim in the past; there must be a pre-petition violation." *Id.* at 462. That

is, a cause of action qualifies as bankruptcy estate property only if the claimant suffered a pre-petition injury.

C. When did the violation occur?

In dissecting whether there is a pre-petition or post-petition cause of action, the case of *Underhill* is instructive. *In re Underhill*, 579 F. App'x at 482. In *Underhill* the debtors filed for bankruptcy on January 6, 2010. On the date of filing, the debtors had a 100% interest in Golf Chic Boutique ("Golf Chic"). Three months after the debtors received their discharge, Golf Chic sued a competitor, Ladies Pro Shop. According to Golf Chic, Ladies Pro Shop continually contacted one of Golf Chic's major suppliers complaining about Golf Chic's prices. Ladies Pro Shop's communications predated the petition date. However, after the debtors' discharge, the supplier cut ties to Golf Chic due to Ladies Pro Shop's complaints. Ultimately, Golf Chic settled with Ladies Pro Shop for $80,000.

The issue in the case focused on whether Golf Chic's claim against Ladies Pro Shop was part of the bankruptcy estate. The Sixth Circuit determined that the Golf Chic claim was not part of the estate because a violation, namely the supplier cutting ties, did not occur until post-petition. In reaching this result, the Sixth Circuit examined the elements of a tortious interference claim and determined that the claim was not mature until the supplier cut ties, which occurred long after the petition date.

The *Underhill* decision is helpful for practitioners when determining whether a "violation" has matured pre-petition or at some other time. This

requires debtor's counsel to examine the applicable state cause of action and its elements. The *Underhill* decision also assists practitioners in determining where the line for pre-petition and post-petition property may fall in a given bankruptcy case. It is also worth noting that the line between pre-petition and post-petition property does not depend upon the filing of a formal complaint, but rather, when a complaint could be filed.

D. How should the test be applied?

How this test should be applied to causes of action is the subject of disagreement. Certain courts have applied the test expansively, including contingent and unripe claims as property of the estate. For instance, in *Mueller vs. Hall (In re Parker)*, 2007 Bankr. LEXIS 1523, the court held that the legal malpractice claim of the debtors became part of the estate at the time of negligence, not when damages were incurred. The court went on to hold that the question was not whether the malpractice case accrued based on the moment the last element of the cause of action accrued, prior to the debtor filing bankruptcy, but whether the malpractice claim is sufficiently rooted in the debtors pre-bankruptcy past to constitute property of the estate. Courts have consistently held that § 541(a) is not restricted by state law concepts such as when a cause of action ripens or a statute of limitation begins to run, and "property of the estate" may include claims that are inchoate on the petition date. When I think about this concept, I think about the Chapter 7 Trustee's question, "Do you hold any lottery tickets?" Certainly, the debtor cannot make a claim to the lottery winnings before the numbers are called, but the ticket, in

and of itself, is in fact "property of the estate" and that expansive definition serves the bankruptcy code and serves your client when considering analysis of disclosure on bankruptcy schedules with respect to a pre petition cause of action.

E. Timing.

In *Johnson, Blakely, Pope, Bokor, Ruppel & Burns, P.A. v. Alvarez (In re Alvarez)* 224 F.3d 1273, 1276 (11th Cir. 2000), debtor filed a complaint against his former attorney alleging legal malpractice. The crux of the debtor's malpractice claim was his allegation that his lawyer negligently disregarded his instructions to file a Chapter 11 on his behalf, and instead filed a Chapter 7. Debtor's complaint alleged that as a result of his negligent actions the debtor sustained damages, including but not limited to, loss of control and ownership of several assets, including ownership interests in stocks, loss of opportunity, loss of assets, and other damages recoverable at law.

Typically, a cause of action for legal malpractice has three elements:

1. The attorney's employment;
2. The attorney's neglect of a reasonable duty;
3. The attorney's negligence was the proximate cause of loss to the client.

The third element of a legal malpractice claim, that the attorney's negligence was the proximate cause of loss to the client, is also referred to as the concept of redressable harm. A cause of action accrues when the last element constituting the cause of action occurs.

The court concluded that, looking to state law, this interest in property, which arose simultaneously with the filing of the debtor's bankruptcy petition, was an interest of debtor and property "as of" the commencement of the case, and thus, property of the estate.

Debtor attempted to argue that the third element of his malpractice cause of action, that of redressable harm, did not occur until after the filing of his bankruptcy petition. The court disagreed.

At the moment the debtor's bankruptcy petition was filed, his chapter 7 bankruptcy estate was created, his interest in property vested in the estate, and all of the legal ramifications creating an estate came into existence. The transfer of debtor's interest in property to a chapter 7 bankruptcy estate, rather than a chapter 11 bankruptcy estate as the debtor intended, is sufficient injury the court held to indicate the debtor had a cognasizable interest in his legal malpractice claim at the precise moment his chapter 7 petition was filed. The court specifically found that the debtor's loss of ownership and control of his assets upon the bankruptcy filing constitutes a significant and tangible change which obviously caused harm to him.

F. More about timing.

In *Witko v. Menotte (In re Witko)* 374 F.3d 1040 (11th Cir. 2004), the debtor filed a petition for bankruptcy in 1999, after a divorce proceeding was filed. In 2000, in a separate proceeding regarding the marital dissolution, the state court trial judge denied his request for alimony. Thereafter, the debtor sued his divorce counsel for malpractice. The Trustee of the debtor's

bankruptcy case intervened seeking a determination that the malpractice claim was estate property. The bankruptcy court held that the cause of action was property of the estate because the better rule is that where pre-petition acts form part of a chain of events that lead to a post-petition redressable harm, the cause of action is sufficiently rooted in the debtor's pre-petition past.

The case was appealed and the higher court, applying state law, concluded that the legal malpractice cause of action did not exist until the alimony action concluded with an adverse outcome that was proximately caused by his attorney's negligence.

The court held that until the underlying action is concluded with an outcome adverse to the client a malpractice claim is hypothetical, and damages are speculative. The court went on to suggest that a negligence malpractice cause of action accrues when the client incurs damages at the conclusion of the related or underlying judicial proceedings.

Therefore, the debtor did not suffer a harm in the alleged legal malpractice prior to or contemporaneous with his filing of a bankruptcy petition. The judicial proceedings underlying his malpractice claim did not conclude until months later. The debtor's malpractice cause of action was unknown. No one could not anticipate that the debtor would lose his alimony claim due to the attorney's malpractice. The debtor's legal malpractice cause of action did not exist at the time when he filed his bankruptcy, and the lower court was reversed.

II. The Chapter 13 - An Expansive Definition

Under chapter 13, the concept of "property of the estate" is broadened and is not so rigidly defined as pre-petition and post-petition property. "Property of the estate" is "broadened to include not only the property brought into the estate via § 541, but also all legal or equitable interests of the debtor in property, including earnings from services performed by the debtor, that the debtor acquires after the commencement of the case but before the case is closed, dismissed or converted to a case under chapter 7, 11 or 12, whichever occurs first. 11 U.S.C. § 1306(a)(1) and (a)(2)." Feature, Property of the Estate--To Be or Not to Be? That Is the Question the Trustee Asks of Thee: Part I, 21-10 ABIJ 28, 28. In other words, property of the estate may include causes of action that arise post-confirmation.

Courts have reasoned that Section 1306's extension of a Chapter 13 bankruptcy's estate is a "rational response to the relevant situation." *Carroll v. Logan*, 735 F.3d 147, 151 (4th Cir., 2013). Chapter 13 proceedings provide debtors with significant benefits: For example, debtors may retain encumbered assets and have their defaults cured, while secured creditors have long-term payment plans imposed upon them and unsecured creditors may receive payment on only a fraction of their claims. See 11 U.S.C. §§ 1322, 1325. In exchange for those benefits, a Chapter 13 debtor makes a multi-year commitment to repay obligations under a court-confirmed plan. The repayment plan remains subject to modification for reasons including a debtor's decreased ability to pay according to plan, as well as the debtor's increased ability to pay. See 11 U.S.C. § 1329.

Take the case of in *In re Granville*, ___BR___; 2014 Bankr. LEXIS 1373, at *1 (Bankr ED Ky, Apr. 4, 2014), as an example. In *Granville*, the debtor totaled her car

post-confirmation. The debtor was not at fault in the accident. The insurance company for the driver who was at fault settled the claim with the debtor. The debtor moved the bankruptcy court to keep the proceeds from the settlement and purchase another vehicle. The secured creditor on the totaled vehicle objected and requested that it receive the insurance proceeds because it had a secured lien on the totaled vehicle.

The *Granville* Court determined that the settlement proceeds were property of the estate. In reaching this conclusion, the bankruptcy court stated, "The [at-fault driver] has. . . committed a tort against the Debtor and the Debtor is entitled to compensation. . . the tort only became property of the estate under 11 U.S.C. § 1306 when the right to payment arose." *Id.* At *3. After determining that the settlement proceeds were property of the estate, the bankruptcy court permitted the debtor to purchase a new vehicle and grant the secured creditor a first priority lien on the new vehicle. The secured creditor was adequately protected under the circumstances.

Granville emphasizes the expansive scope of Section 1306. Unlike a case under chapter 7, a cause of action that matures post-petition and post-confirmation was determined to be property of the estate. This is an important distinction because debtors sometimes acquire a cause of action post-confirmation. Debtor's counsel needs to be familiar with the Bankruptcy Code and the treatment of proceeds generated from successful litigation of the cause of action.

A different conclusion was reached in the case of *In re Van Stelle* 354 B.R. 157 (Bankr. W.D. MI, 2006). The debtors' confirmed plan provided for payment of a creditor's claim which was secured by the vehicle, and the debtors proposed to

purchase a new vehicle with the insurance proceeds and grant the creditor a lien in the new vehicle as substitute collateral. The debtors contended that 11 U.S.C. § 363 allowed the debtors to use estate property to the same extent as the trustee, and thus the debtors could compel the creditor to accept the substitute collateral. The bankruptcy court held, however, that the insurance proceeds were not property of the debtors' estate and therefore § 363 did not authorize the debtors' use of the proceeds without the creditor's consent. The debtors' plan expressly and properly provided that all property of the estate vested in the debtors upon confirmation of their plan, and such vesting constituted an absolute conveyance of the estate's property back to the debtors. However, disposable income is also an issue to consider as a mechanism to require the debtor to apply proceeds to the Plan.

III. What about Post-Discharge?

Whether a cause of action is "property of the estate" post-discharge turns on whether the debtor filed for a Chapter 7 or Chapter 13 bankruptcy.

If the debtor filed for a Chapter 7, the determination turns on when the violation occurred and matured. For example, the bankruptcy court in *Sikirica v. Harber (In re Harber)*, 553 B.R. 522 (Bankr. W.D. Pa. 2016) determined that a medical malpractice claim for debtor's hip replacement was not property of the estate, despite the hip surgery occurring pre-petition. The bankruptcy court rested its determination on Pennsylvania law, which stated, a cause of action "accrues" when the plaintiff could institute the lawsuit. Damages which are "physically objective and ascertainable" are an essential element of a personal injury tort action. Because damages were not ascertainable, the bankruptcy court determined that the medical malpractice associated with the hip replacement was a post-petition cause of action

belonging to the debtor. However, if the malpractice occurred pre-petition despite the lack of knowledge does that claim "arise" pre-petition?

Under Chapter 13, the analysis is the same with the exception that the concept of the bankruptcy estate is broadened. In other words, if a cause of action matures pre-petition or post-confirmation, but before the debtor receives his or her discharge, the cause of action is considered to be property of the estate. However, there is a question whether a cause of action maturing post-discharge is property of the estate subject to the trustee's administration.

As discussed *supra*, Section 1306 encompasses "all legal or equitable interests of the debtor in property, including earnings from services performed by the debtor, that the debtor acquires after the commencement of the case but before the case is closed, dismissed or converted to a case under chapter 7, 11 or 12, whichever occurs first." The language in 1306 does not extend to a discharge, but instead extends until the "case is closed." While this issue has not been litigated, there could be circumstances where the debtor completes the applicable commitment period and receives a discharge, but a cause of action matures before the case is closed. A trustee could argue the cause of action is part of the bankruptcy estate because of the plain language of Section 1306. This is likely a rare circumstance. Nevertheless, practitioners should be aware of such a result as their debtors complete their Chapter 13 plan.

IV. Conclusion

The distinction between pre-petition, post-petition, post confirmation, and post discharge as it relates to causes of action is an important one. The distinction is especially important when a debtor's cause of action has the ability to pay all of the

debtor's creditors. Bankruptcy practitioners should be mindful of these distinctions and advise their debtors accordingly. And as always, disclose, disclose, disclose.

VALUATION AND TREATMENT OF CAUSES OF ACTIONS IN CHAPTER 13 CASES

Krispen S. Carroll

Chapter 13 Trustee – Detroit

Many potential Chapter 13 debtors have pending lawsuits and/or potential causes of action when they seek out legal advice from their attorney regarding a bankruptcy filing. What is the debtor required to disclose in the Chapter 13 filing and what is the impact of that disclosure on confirmation? The answer to that question starts with a review of §541 defining property of the estate in all chapters and then §1306 defining what is additional property of the estate in a Chapter 13.

Under §541 a pending lawsuit and/or cause of action is clearly a legal interest of the debtor considered property of the estate and subject to disclosure on both Schedule B and on the Statement of Financial Affairs under question #9. Determination of how to disclose, value and exempt the debtor's interest in a cause of action is explored below:

Pending Complaints vs. Unfiled Causes of Action. Whether a lawsuit has been formally filed by the debtor, does not affect the debtor's duty of disclosure. If the event giving rise to the cause of action occurred prior to the filing of the case, the interest of the debtor should be disclosed on Schedule B and exempted on Schedule C to the extent allowable.

Available exemptions of pre-petition causes of action.

a. Exemptions of proceeds from pre-petition causes of action are generally available under §522(d)(11)(A), (B), (D), or (E) and also under §522(d)(5) – the wildcard.
b. §522(d)(11)(D) and §522(d)(5) are restricted to monetary limits.

c. §522(d)(11)(B) and (E) do not have monetary limits but are restricted to amounts "reasonably necessary for the support of the debtor and any dependent of the debtor". (§522(d)(11)(A) has no restrictions but is limited to awards under a crime victim's reparation law).

Valuing a cause of action – what factors do you look at?

a. If a lawsuit has been filed, what does the complaint request?
b. Has the lawsuit been mediated? Are there any settlement offers?
c. What are the estimated amounts of your client's damages?
d. What is the likelihood of recovery? What are the estimated contingency fees and costs?

SPECIAL CONSIDERATIONS IN A CHAPTER 13 PROCEEDING

Property of the estate in Chapter 13 Proceedings:

11 USC §1306

(a) Property of the estate includes, in addition to the property specified in section 541 of this title –

(1) all property of the kind specified in such section that the debtor acquires after the commencement of the case before the case is closed, dismissed, or converted to a case under chapter 7, 11, or 12 of this title, whichever occurs first.

Proceeds stemming from a cause of action received by a debtor anytime during the pendency of a Chapter 13 plan are property of the estate under §1306 and may be required to be paid into to a Chapter 13 Trustee for distribution to creditors. This is true not only for causes of action pending at the time of filing, but also causes of action that arise post-filing.

Determining any potential liquidation issues related to causes of action: In Chapter 13 a debtor is required to provide payment to creditors that meets or exceeds the hypothetical distribution in a Chapter 7 proceedings, which is commonly refer to as the liquidation analysis. If there are identifiable non-exempt proceeds stemming from a debtor's cause of action, those proceeds would need to be included in the liquidation analysis. However, most often the amount of distribution the debtor can expect is difficult to know or accurately value. Causes of action are frequently listed on Schedule B as "unknown" where the debtor's recovery is not guaranteed and the actual amounts a debtor is able to obtain through settlement, mediation, or verdict is difficult to estimate. Likewise, many attorneys will attempt to exempt proceeds under unrestricted monetary limits as "100%".

Exempt proceeds are still considered to be disposable income in a Chapter 13. Despite exemptions of lawsuit proceeds taken by the debtors on Schedule C, the proceeds are still considered as disposable income in a Chapter 13 under controlling Sixth Circuit case law. In re Freeman, 86 F.3d 478 (6th Cir. 1996). In Freeman, the court found that the plain language of §1325(b)(1)(B) makes no express or implied reference to the exempt status of income and concluded that disposable income includes income that is exempt and would not be available in a Chapter 7 liquidation.

Typical Chapter 13 Trustee objections to confirmation concerning lawsuit proceeds. Where courts have ruled inconsistently on whether or not a Chapter 13 Trustee must assert an

interest in potential lawsuit proceeds prior to confirmation, it has become common practice for the Chapter 13 trustees to file objections related to pending and potential causes of action. Post-BAPCA cases such as In re Connor, 463 B.R. 14 (E.D. Mich 2012) following the Supreme Court's ruling in Hamilton v Lanning, 130 S.Ct. 2464 (2010), further add support to the need to finalize the determination of how the receipt of proceeds will be addressed at the time of confirmation. Aside from objections relating to the exemption itself, the Chapter 13 Trustee may object to confirmation and request a determination that any proceeds received by the debtor during the life of the plan are committed as additional funding for the benefit of creditors.

Resolving the issue of whether all post-petition proceeds should be committed as disposable income. §1325(b)(2) defines the term "disposable income" as current monthly income received by the debtor less amounts reasonably necessary to be expended for the maintenance and support of the debtor and the debtor's dependents. Asking the Court for a determination that the potential lawsuit proceeds are disposable income is a ruling that can be made at the time of confirmation. A ruling determining whether the retention of any portion of those proceeds is reasonably necessary for the debtor, is much more difficult. A typical resolution of this issue is to preserve the debtor's right to request retention of the proceeds upon the filing of a motion to approve any settlement or distribution.

Approval of employment for a non-bankruptcy attorney pursuing the cause of action. The attorney representing the debtor in a pre-petition cause of action should apply for approval of that employment and any previously executed contingency fee agreement with the Bankruptcy Court. The Chapter 13 Trustee or bankruptcy attorney may reach out to non-bankruptcy counsel to get this process started. Both the Trustee and the Bankruptcy Attorney may seek periodic updates concerning the progress of the litigation.

Bankruptcy Court approval should be sought prior to debtor's entry into settlements. Either the bankruptcy attorney or the non-bankruptcy attorney can seek the approval of a proposed settlement on the debtor's behalf. Notice of the proposed disposition of the case and the debtor's intention with regard to the proceeds should be provided to all parties listed on the matrix. A Trustee seeking the turnover of proceeds may request a determination from the court as to whether it is reasonably necessary for the debtor to retain any portion of the exempt proceeds.

DISCLOSE OR NOT TO DISCLOSE? CHAPTER 13 DEBTORS' OBLIGATION TO AMEND SCHEDULES TO DEAL WITH POST-PETITION EVENTS THAT CREATE CAUSES OF ACTION

By: Garik Osipyants,

Thav Gross P.C.

I. Relevant Code Sections

a. 11 USC § 521 - When filing a bankruptcy case, debtors must file schedules and statements disclosing all of their assets and liabilities. This duty to disclose is intended to serve as a tool to establish the bankruptcy estate.

b. 11 USC § 541(a) - Bankruptcy estate includes "all legal or equitable interests of the debtor in property as of the commencement of the case."

c. 11 USC § 1306(a) – This section expands the definition of what is property of the estate in a Chapter 13 context. The section puts after-acquired property into the Chapter 13 estate until the estate is "closed, dismissed, or converted . . . ."

d. 11 USC §1327(b) -reduces the scope of what constitutes property of the estate and provides that "[e]xcept as otherwise provided in the plan or order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor."

II. Discussion

It goes without saying that when a debtor seeks bankruptcy protection, he must disclose a great deal of information to the court, bankruptcy trustee and creditors. One of many vital pieces of information is the full disclosure of debtor's assets, which includes causes of action held by the debtor at the time the bankruptcy case is commenced.

This disclosure is critical in determining whether a Chapter 13 plan will comply with the bankruptcy code and whether it can ultimately be confirmed. At the same time, the question is frequently raised as to whether debtor's obligation to disclose information continues after the

petition is filed and after the bankruptcy plan is ultimately confirmed. It is notable that there is no specific code section, or a bankruptcy rule requiring a debtor to file amendments to the initial disclosure of assets.

Be that as it may, the bankruptcy code appears to create an unresolved question created by friction between section 11 USC §1306(a) and 11 USC § 1327(b) that generates uncertainty as to whether a debtor must disclose causes of action post-confirmation. § 1306(a), indicates that the new post-confirmation cause of action is property of the estate until the case is closed, converted or dismissed. § 1327(b) suggests that all assets, including the cause of action is "vested" in the debtor at the time of confirmation and hence not part of the bankruptcy estate and, as a result, not necessary to be disclosed.

Logically, there has been a split between courts on the question of whether a debtor has a duty to disclose post-confirmation causes of action. The United States Court of Appeals for the Sixth Circuit has yet to reconcile the friction between 11 USC §1306(a) and 11 USC § 1327(b). There are two principal positions. One, there is a duty to disclose. Two, there is not.

a. Duty to Disclose

In an unpublished opinion, the Sixth Circuit Court of Appeals opted to not address directly the statutory requirement of debtor's duties to disclose post-petition causes of action. Nevertheless, the court in *Kimberlin v. Dollar Gen. Corp.*, 520 Fed. Appx. 312 (6th Cir. 2013) did promote a theory of why disclosure is required. The case involved a bankruptcy court barring the debtor from pursuing a cause of action due to debtor's failure to disclose the potential claim in her bankruptcy case.

In *Kimberlin,* the court was troubled by the debtor's inaction of not disclosing the lawsuit to the bankruptcy court and her creditors. The court addressed the fact that the debtor's lack of disclosure precluded the trustee and the creditors from attempting to modify the plan and to give creditors the opportunity to share some of the potential future recovery. "Because the debtor never amended her schedules, she deprived the court, trustee and creditors of possible options." Presumably, one of the options was to file a plan modification and to include some of the recovery from the lawsuit in the plan. At the end of the day, the court concluded that debtors have an "affirmative and ongoing duty to disclose assets, including unliquidated litigation interests." *Id* at 314. Regrettably, the court chose to skip over the "vesting" issue presented by 11 USC § 1327(b).

Whether an exact bankruptcy rule, or code section exists to place the duty on the debtor to disclose post-confirmation assets, including causes of action, appears to be irrelevant to the majority of the courts that have tackled this issue. *In Flugence v. Axis Surplus Ins. Co.*, 738 F.3d 126 (5th Cir. 2013) the Fifth Circuit Court of Appeals concluded that a debtor who was injured in a car accident after confirmation and failed to disclose the personal injury lawsuit had a duty to inform the court of the potential cause of action. The court indicated that understanding, or knowing of the duty to disclose the cause of action was irrelevant. Again, the court chose not to connect the post-confirmation duty to disclose to a specific rule or section of the bankruptcy code, but rather solidified an unwritten rule that the bankruptcy court ought to resolve whether an asset should be available for the creditors, not the debtor. The *Frugence* court, decided that there is in fact a continuing duty to disclose in a Chapter 13 proceeding. "Whether a particular asset should be available to satisfy creditors is often a contested issue, and the debtor's duty to disclose

assets—even where he has a colorable theory for why those assets should be shielded from creditors—allows that issue to be decided as part of the orderly bankruptcy process." *Id.* at 130.

These line of cases embrace the position that post-confirmation causes of action are brought into the bankruptcy estate by 11 USC § 1306(b). At the same time, not much emphasis is placed on 11 USC §1327(b). Accordingly, the majority seem to suggest that "[b]ecause a debtor has a duty to account for all 'property of the estate' under 11 USC § 521, it follows that there be a presumed duty to disclose" post-confirmation property as well. *In re Poesnecker*, 2014 Bankr. LEXIS 4562, 3-4 (Bankr. M.D. Pa. 2014). In another case, the district court in *Autos, Inc. v. Gowin*, 330 B.R. 788 (D. Kan. 2005), explained that for a Chapter 13 bankruptcy case to work, again primarily relying on § 1306(b), the Chapter 13 debtor has a continuing duty to disclose property and earnings acquired after the commencement of the case.

A query is presented, how do these courts address section 11 USC § 1327(b) when deciding that a debtor has a duty to disclose the cause of action? The section undoubtedly indicates that, unless stated otherwise, all assets of the estate vest back to the debtor at confirmation. In response, some courts attempt to reconcile this dichotomy between § 1306(a) and § 1327(b) by suggesting that "property of a Chapter 13 estate that is in existence and disclosed as of the date of confirmation vests in the Debtor pursuant to § 1327(b). Any property acquired post-confirmation, however, is property of the estate pursuant to § 1306(a)." *In re Nott*, 269 B.R. 250, 257 (Bankr. M.D. Fla. 2000) Observably, this type of approach would have been better if Congress had specifically indicated that § 1306(a) is operative in spite of § 1327(b).

b. No Duty to Disclose

A counter position to the question of whether the debtor has a duty to amend schedules, post-confirmation, to disclose a potential cause of action involves a stricter interpretation of 11 USC §1327(b). Stated differently, when the plan is confirmed the bankruptcy estate has been established and, unless stated otherwise in the plan, all assets of the estate revert back to the debtor. This position presents an argument that at the time of confirmation the "bargain" between the debtor and the creditors is solidified as it relates to the assets of the bankruptcy estate. Debtor agrees to pay all of his disposable income to his creditors in order to keep his nonexempt assets. (See David Gray Carlson, *The Chapter 13 Estate and Its Discontents*, 17 Am. Bankr. Inst. L. Rev. 233, 253 (2009).)

This line of reasoning is strengthened by pointing out that the confirmation period is the only time when the liquidation analysis is made to determine the amount that unsecured creditors would receive if the debtor's estate was liquidated under Chapter 7 as of the date of confirmation. An argument can be raised that the valuation of post-confirmation assets is irrelevant as the bankruptcy estate is vested in the debtor at confirmation. Some argue that the only benefit the creditors are entitled to after confirmation is debtor's disposable income. To underline this position, some courts utilize other sections of the code, specifically the section that deals with conversion of a case from a Chapter 13 to another chapter. For example, 11 USC §348(f)(1) provides that:

> … when a case under chapter 13 of this title is converted to a case under another chapter under this title--
> (A) property of the estate in the converted case shall consist of property of the estate, as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion;

The bankruptcy code states that, when conversion is involved, from a Chapter 13 to another chapter, the bankruptcy estate consists of property as of the date of the petition and will only include post-petition assets into the estate if the conversion was determined to be in bad faith. See *In Re Brown*, 375 B.R. 362 (Bankr. W.D. Mich. 2007) For that reason, one can argue, how can one penalize a debtor who completed his Chapter 13 case in good faith by making him include into the bankruptcy estate causes of action that would not have been included if he would have converted to another chapter in good faith? (See David Gray Carlson, *The Chapter 13 Estate and Its Discontents*, 17 Am. Bankr. Inst. L. Rev. 233 (2009))

To illustrate this point further, a District Court for the Southern District of Alabama concluded that a personal injury defendant cannot argue that the Chapter 13 debtor's failure to disclose the post-confirmation cause of action in his bankruptcy barred the debtor from pursuing the cause of action. The court relied on 11 USC §348(f)(1) on its decision and ruled that since there was no evidence of bad faith, the conversion was appropriate and ruled that a debtor "had no affirmative duty to disclose any property acquired after confirmation of their Chapter 13 plan." See *Smith v. Scales Express*, Inc., 2006 U.S. Dist. LEXIS 53638, 7-8 (S.D. Ala. 2006)

Other courts, although deciding that the causes of action were property of the bankruptcy estate, still didn't go as far as creating a duty to disclose. In *Waldron v. Brown*, 536 F.3d 1239 (11th Cir. 2008) the Eleventh Circuit Court of Appeals ruled that a post confirmation cause of action was included in the bankruptcy estate. At the same time the court stated that the bankruptcy code nor the bankruptcy rules instill a duty on the debtor to disclose post confirmation assets. *Id.* at 1246.

III. Practice pointer

As it currently stands, the Sixth Circuit appears to lean towards an assumed duty to disclose post-petition causes of action. Although there is no clear resolution as to which part of the bankruptcy code creates a duty to disclose post-confirmation causes of action, the moral of this material is that failure to disclose may have negative results on the debtor. The debtor may be denied further relief in the bankruptcy case, he may be denied exemptions, and he may be barred by judicial estoppel to move forward with his cause of action.

For this reason, a solid approach for a bankruptcy practitioner is when in doubt, disclose, disclose, disclose. This will place the burden on the creditors, or the trustee to take some action in order to obtain potential proceeds from the cause of action. Even if there is a great argument of why the asset should not be part of the bankruptcy estate, disclose the asset and allow the bankruptcy court to make the decision. In conclusion, always err on the side of disclosing.

Debtor's Causes of Action — Potential Judicial Estoppel Issues

Judge Thomas J. Tucker,
United Bankruptcy Court for the Eastern District of Michigan
Detroit, Michigan

with substantial assistance from Alesia Dobbins, Law Clerk

A. Judicial estoppel in general, and in the bankruptcy context

Judicial estoppel is an equitable doctrine which "generally prevents a party from prevailing in one phase of a case on an argument and then relying on a contradictory argument to prevail in another phase." *Pegram v. Herdrich*, 530 U.S. 211, 227, n. 8 (2000). It is "meant to preserve the integrity of the courts by preventing a party from abusing the judicial process through cynical gamesmanship, achieving success on one position, then arguing the opposite to suit an exigency of the moment." *Eubanks v. CBSK Financial Group, Inc.*, 385 F.3d 894, 897 (6th Cir. 2004) (quoting *Teledyne Indus., Inc. v. NLRB*, 911 F.2d 1214, 1218 (6th Cir. 1990)).

The Supreme Court has stated that

> several factors typically inform the decision whether to apply the doctrine in a particular case: **First, a party's later position must be clearly inconsistent with its earlier position. Second, courts regularly inquire whether the party has succeeded in persuading a court to accept that party's earlier position,** so that judicial acceptance of an inconsistent position in a later proceeding would create the perception that either the first or second court was misled. Absent success in a prior proceeding, a party's later inconsistent position introduces no risk of inconsistent court determinations, and thus poses little threat to judicial integrity. **A third consideration is whether the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped.**

New Hampshire v. Maine, 532 U.S. 742, 750-51 (2001) (internal quotations and citations omitted) (emphasis added). The Sixth Circuit has "placed particular emphasis on the second factor, stating that judicial estoppel governs a dispute only if the first court adopted the position urged by the party, either as a preliminary matter or as part of a final disposition." *Pennycuff v. Fentress Cty. Bd. of Edu.*, 404 F.3d 447, 453 (6th Cir. 2005) (internal quotations omitted); *see also Gold v. Winget* (*In re NM Holdings Co., LLC*), 407 B.R. 232, 283-84 (Bankr. E.D. Mich. 2009) (rejecting judicial estoppel argument because the first court had not adopted the party's prior position). However,

"[t]he 'prior success' requirement does not mean that the party against whom the judicial estoppel doctrine is to be invoked must have prevailed on the merits. Rather judicial acceptance means only that the first court has adopted the position urged by the party, either as a preliminary matter or as part of a final disposition." *Reynolds v. C.I.R.*, 861 F.2d 469, 473 (6th Cir. 1988) (internal quotations omitted).

In the bankruptcy context, the issue of judicial estoppel comes up frequently — one commentator has suggested several times each week around the nation[1] — when a bankruptcy debtor has a claim or potential claim against another entity and either fails to disclose it entirely or discloses it in a manner that could be deemed inconsistent with the debtor's position when the debtor later attempts to take action on the claim. But the Sixth Circuit's emphasis on the second factor of the judicial estoppel inquiry, regarding judicial acceptance, raises some interesting questions in the bankruptcy context.

At least in the context of chapter 7, one could argue that the bankruptcy court's merely granting a discharge is not an "acceptance" or "adoption" of a debtor's position regarding the accuracy of the debtor's schedules of assets. Most of the Sixth Circuit cases do not address judicial estoppel in the context of chapter 7. In *Reynolds*, for example, a chapter 11 debtor and the IRS had entered into a consent agreement regarding the debtor's tax liability, which was specifically approved by the bankruptcy court in the chapter 11 case. When the IRS later tried to hold the debtor's ex-spouse liable for the same taxes, taking a position inconsistent with its position taken in the bankruptcy case, the ex-spouse argued the IRS was judicially estopped from asserting the claim against him. The Sixth Circuit agreed, stating that "when a bankruptcy court — which must protect

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[1] William H. Burgess, *Dismissing Bankruptcy-Debtor Plaintiffs' Cases on Judicial Estoppel Grounds*, 62-MAY Fed. Law 54, 55 (2015).

the interests of all creditors — approves a payment from a bankruptcy estate on the basis of a party's assertion of a given position that, in our view, is sufficient 'judicial acceptance' to estop the party from later advancing an inconsistent position." *Id.* at 473.

Later Sixth Circuit opinions relied on this language to invoke judicial estoppel in the chapter 13 context. In *Lewis v. Weyerhaeuser Co.*, 141 Fed.Appx. 420, 425 (6th Cir. 2005) (unpublished), the court cited the above quote from *Reynolds* and stated "it is also clear that in confirming Lewis's Chapter 13 plan, the bankruptcy court adopted Lewis's statement that she had no potential cause of action." Likewise, in *White v. Wyndham Vacation Ownership, Inc.*, 617 F.3d 472, 479 (6th Cir. 2010), also a chapter 13 case, the court reasoned that "the bankruptcy court entered an order requiring White to make payments to the trustee and directing her to attend a meeting of the creditors. At this point, the bankruptcy court adopted her position." The Court then went on to quote the language from *Reynolds* above. The Court did not explain how directing the debtor to attend a 341 meeting equated to adoption of her statements regarding her assets. However, one can understand how judicial estoppel might apply in the chapter 13 context, in which plan payments are determined, in part, after consideration of the value of the debtor's assets, so that the court can be said to implicitly adopt the debtor's position regarding those assets when it confirms a plan. *See, e.g.*, 11 U.S.C. § 1325(a)(4) (liquidation test).

Chapter 7 is different, but other cases have applied judicial estoppel in the chapter 7 context with very little analysis of whether the application is truly appropriate. For example, in *Stephenson v. Malloy*, 700 F.3d 265, 274 (6th Cir. 2012), the Sixth Circuit, relying on *White*, summarily stated that "when the bankruptcy court granted [debtor's chapter 7] discharge . . ., it acted in reliance on the representations he had made concerning his assets – including the representation that this lawsuit did not exist." Likewise, in a recent D.C. Circuit Court case, the court stated that "the bankruptcy

court's decision to initially discharge [the debtor] from Chapter 7, and the District Court's decision to allow this case to continue even during the pendency of [the debtor's] bankruptcy proceedings, leave little doubt that [the debtor] succeeded in hiding the inconsistency from the courts and 'creating the perception that either the first or the second court was misled.'" *Marshall v. Honeywell Tech. Sys. Inc.*, --- F.3d ---, 2016 WL 3726039, *5 (D.C. Cir. July 12, 2016) (quoting *Moses v. Howard Univ. Hosp.,* 606 F.3d 789, 799 (D.C. Cir. 2010) and *New Hampshire*, 532 U.S. at 750). *See also Tennyson v. Challenge Realty*, 313 B.R. 402 (Bankr. W.D. Ky. 2004) (applying judicial estoppel because debtor's failure to disclose asset in prior chapter 7 was not inadvertent, without discussing whether that bankruptcy court had adopted the debtor's position); *Rizka v. State Farm Fire and Cas. Co.*, No. 13-cv-14870, 2015 WL 9314248, *5 (E.D. Mich. Dec. 23, 2015) ("based in part on [debtor's] repeated sworn statements . . . the bankruptcy court discharged over $45,000 in debt [debtor] had incurred. . . . The bankruptcy court thereby adopted [debtor's] position that she owned no real property."); *but see Pavelka v. Allstate Prop. and Cas. Ins. Co.*, 91 F.Supp.3d 931, 938 (E.D. Mich. 2015) ("The Court also notes, as relevant to this [judicial acceptance] inquiry, that bankruptcy courts serve a special purpose. They operate under a distinct set of statutes and customs. As a result, what occurs in bankruptcy proceedings will often have little to no relevance to separate, non-bankruptcy proceedings.").

B. The Sixth Circuit standard, and a tougher approach taken by some other circuits

The Sixth Circuit has held that,

> to support a finding of judicial estoppel, we must find that: (1) [the debtor] assumed a position that was contrary to the one that she asserted under oath in the bankruptcy proceeding; (2) the bankruptcy court adopted the contrary position either as a preliminary matter or as part of a final disposition; and (3) [the debtor's] omission did not result from mistake or inadvertence. In determining whether [the debtor's] conduct resulted from mistake or inadvertence, this court considers whether: (1) she lacked knowledge of the factual basis of

> the undisclosed claims; (2) she had a motive for concealment; and (3) the evidence indicates an absence of bad faith. In determining whether there was an absence of bad faith, we will look, in particular, at [the debtor's] "attempts" to advise the bankruptcy court of her omitted claim.

White, 617 F.3d at 478; *see also Kimberlin v. Dollar General Corp.*, 520 Fed. Appx. 312, 314-15 (6th Cir. 2013) (applying *White* standards to judicially estop former Chapter 13 debtor's wrongful termination action against her former employer). The Sixth Circuit standard leaves the debtor with considerable room to argue mistake, inadvertence, and good faith, in order to avoid judicial estoppel. Similar standards are also followed by the Seventh and Ninth Circuits.

The Fifth, Tenth and Eleventh Circuits take a tougher view — they "take a dim view of inadvertence arguments." Burgess, *supra*, at 56. Under the case law from these circuits, if a debtor fails to disclose a claim in a bankruptcy case, there is a presumption that the omission was intentional:

> In [the Fifth, Tenth, and Eleventh circuits], a debtor's failure to disclose a lawsuit to the bankruptcy court is presumed to be deliberate and is *only* regarded as inadvertent or mistaken "when the debtor either lacks knowledge of the undisclosed claims or has no motive for their concealment."

Id. (italics in original, footnote omitted); *see also Browning Manufacturing v. Mims (In re Coastal Plains, Inc.)*, 179 F.3d 197 (5th Cir. 1999); *Eastman v. Union Pac. R.R. Co.*, 493 F.3d 1151 (10th Cir. 2007).

C. Can a debtor amend the Schedules to "fix" a judicial estoppel problem?

The question arises whether a debtor who fails to disclose a claim, either intentionally or inadvertently, can later avoid a judicial estoppel defense by simply amending the bankruptcy schedules. In *Eubanks*, the Sixth Circuit held that judicial estoppel was not appropriate, finding it significant that the debtor-plaintiffs had "actually made numerous attempts through their counsel to

advise the court and the Trustee of their claim." 385 F.3d at 898. Those attempts included orally informing the trustee of their claim at their meeting of creditors, contacting the trustee multiple times during the bankruptcy to determine whether he would pursue the claim on behalf of the estate, asking the bankruptcy court for a status conference regarding abandonment of the claim and, finally, amending their Schedule B to disclose the claim. As a result, the Court held that the debtors' omission of their claim in their bankruptcy was due to inadvertence or mistake.

However, many courts have held that when a debtor attempts to amend the bankruptcy schedules only after a defendant has filed a motion to dismiss or for summary judgment, it is "too little, too late." In *White*, the evidence that the debtor attempted to correct her omission in bankruptcy court included (1) an affidavit from her attorney that he discussed the lawsuit with the trustee; (2) an application to employ counsel for the claim; and (3) an amendment to the debtor's statement of financial affairs which was filed after the defendants in the lawsuit filed a motion to dismiss the case. The Court stated that it "will not consider favorably the fact that [debtor] updated her initial filing after the motion to dismiss was filed. To do so would encourage gamesmanship . . . ." 617 F.3d at 481.

Likewise, in *Johnson v. Lewis Cass Intermediate Sch. Dist.*, 345 B.R. 816 (Bankr. W.D. Mich. 2006), the debtor failed to disclose a pending wrongful termination action in her initial paperwork. Only after the defendant learned of the bankruptcy and filed a motion to dismiss or for summary judgment did the debtor contact her trustee and tell him about the claim. The court held that judicial estoppel barred the claim, holding that

> There exists no evidence from which this court may infer a good faith mistake or inadvertence. Indeed, "[a]llowing [a debtor] to back-up, re-open the bankruptcy case, and amend his bankruptcy filings, only after his omission has been challenged by an adversary, suggests that a debtor should consider disclosing potential assets only if he is caught concealing them. This so-called remedy would only diminish

> the necessary incentive to provide the bankruptcy court with a truthful disclosure of the debtors' assets."

Id. at 824 (quoting *Tyler v. Fed. Express Corp.*, 420 F.Supp.2d 849, 859 (W.D. Tenn. 2005) (other quotations omitted)). Significantly, in *Johnson* the court acknowledged the potential prejudice to the debtor's estate by applying judicial estoppel to bar the debtor's claim. However, the court stated "[w]hen [the interests of the relatively few number of creditors are] weighed against the Debtor's dishonest conduct in failing to disclose the wrongful discharge action to this court and the Trustee, the balance of the equities favors application of judicial estoppel." *Id.* at 825 n. 7. *See also Maxwell v. MGM Grand Detroit, LLC*, No. 03-73134, 2007 WL 2050795 (E.D. Mich. July 16, 2007) (judicial estoppel applied despite debtor-plaintiffs' attempts to reopen their bankruptcy cases to add discrimination lawsuit); *Hawkins v. Michigan Dep't of Corr.*, No. 15-cv-10172, 2016 WL 3230663 (E.D. Mich. June 13, 2016) (judicial estoppel applied to undisclosed claim because, *inter alia*, debtor-plaintiff only voluntarily dismissed her chapter 13 case after the defendant filed its motion for summary judgment).

D. Does judicial estoppel apply to the trustee?

The court's observations in *Johnson* illustrate another issue that comes up when courts are faced with a judicial estoppel defense: given that an undisclosed claim remains part of a bankruptcy estate which can be administered for the benefit of a debtor's creditors, should judicial estoppel apply to the trustee when the debtor fails to disclose a claim?

In *Stephenson v. Malloy*, 700 F.3d 265 (6th Cir. 2012), the Sixth Circuit answered this question in the negative. In that case, the debtor filed bankruptcy two months after initiating a lawsuit against the driver of the other car involved in a car accident. The debtor did not list the lawsuit against the driver in his bankruptcy paperwork but he did list a separate action against an insurance company related to the same accident. After learning of the bankruptcy, the individual

defendant filed a motion for summary judgment, which the district court granted despite the fact that there was evidence that the trustee had known about the undisclosed lawsuit since early in the bankruptcy case, and that the trustee by that point had substituted in as the real party in interest. The Sixth Circuit reversed, citing cases from the Fifth, Tenth and Eleventh Circuits for the "proposition that a debtor's errors or omissions should not be attributed to the trustee for purposes of judicial estoppel." *Id.* at 272. The rationale is that the "[d]efendants allege no wrongdoing by the trustee; it was [the debtor] who omitted the lawsuit from the bankruptcy filings. The trustee's pursuit of this action is therefore not contrary to a position he previously asserted under oath." *Id.*

Later Sixth Circuit cases have followed *Malloy*. *Stevenson v. Haddad*, 529 Fed.Appx. 522, 523 (6th Cir. 2013)(unpublished) ("The court's categorical estoppel-of-all-claims-by-all-parties cannot stand in light of our recent decision in *Stephenson v. Malloy* . . . ."); *Williams v. Saxon Mortg. Serv., Inc.*, No. 13-10817, 2014 WL 765055, *9 (E.D. Mich. Feb. 26, 2014) (citing *Malloy:* "The undersigned first notes that Saxon's estoppel arguments do not apply to the bankruptcy Trustee, who may bring the instant claim for the benefit of plaintiffs' bankruptcy estate.").

In reaching its decision in *Malloy*, the Sixth Circuit relied heavily on the decision in *Parker v. Wendy's Int'l, Inc.*, 365 F.3d 1268 (11th Cir. 2004) and also cited *Reed v. City of Arlington*, 650 F.3d 571 (5th Cir. 2011), which itself relied heavily on *Parker*. However, in a later decision, the Eleventh Circuit pointed out that *Parker* is actually in direct conflict with its other decisions rejecting the debtors' arguments that they should be able to go back and amend their schedules to allow the trustees to administer the assets. *Slater v. U.S. Steel Corp.*, 820 F.3d 1193, 1208, n. 20 (11th Cir. 2016) ("We note in passing that *Parker* . . . reached the opposite conclusion. . . . In contrast, *Barger* [*v. City of Cartersville*, 348 F.3d 1289 (11th Cir. 2003)] held that the trustee was bound by the debtor's failure to disclose in her bankruptcy filings that the claims she was prosecuting were assets

of the bankruptcy estate. Under our prior-panel-precedent rule . . . we are bound to follow *Barger* and to disregard *Parker's* holding to the contrary.").

Despite the apparent uncertainty that may exist for courts in the Eleventh Circuit, *Malloy* remains binding precedent in the Sixth Circuit, where judicial estoppel against a debtor does not apply to a trustee who attempts to pursue undisclosed assets.

E. When a debtor lists a claim but indicates a value of "$0," a lesser amount, or "unknown"

Another issue can arise when a debtor includes a potential claim in the bankruptcy schedules but lists the value as "$0" or some value less than the value sought in a later action. Does judicial estoppel apply to limit the damages the debtor can seek?

Decisions addressing this question are rather mixed. For example, in *Szyszlo v. Akowitz*, 818 N.W.2d 424 (Mich. Ct. App. 2011), the debtor filed bankruptcy three months after being blinded during surgery to correct orthopedic injuries. The debtor listed the potential malpractice claim in his bankruptcy and listed the value as "unknown" at one point and as $15,000 at another. After the trustee filed a no asset report but before the bankruptcy case was closed, the debtor filed a malpractice claim against the anesthesiologist from his surgery and the defendant argued that the debtor should be judicially estopped from seeking damages in excess of $15,000. The court disagreed, reasoning that the "fair market value" of a potential claim at the time a bankruptcy is filed is different from the "amount in controversy" which is based on damages claimed. "Thus, it was entirely consistent for plaintiff to list the market value of his claim as $15,000 while claiming damages in excess of $25,000. The listed market value was not a statement of actual damages from the alleged malpractice and so could not be an 'unequivocal' statement of such damages." *Id.* at 432. *See also Crider v. Misty Acres, Inc.*, 893 So.2d 1165, 1172 (Al. Civ. App. 2004) (no judicial estoppel

where complaint sought unspecified amount of damages and there was "no evidence indicating that the [debtors] attempted to mislead the bankruptcy court").

On the other hand, in *Bone v. Taco Bell of America, LLC*, 956 F.Supp.2d 872 (W.D. Tenn. 2013), the court held that the debtor was limited to the value of the claim she listed in her previous bankruptcy. In that case, a few months prior to filing bankruptcy, the debtor slipped and fell at one of the defendant's restaurants. In her bankruptcy, she listed the claim and indicated on Schedule B that its value was zero. Two months after receiving a discharge, the debtor instituted an action against the defendant seeking damages up to the jurisdictional limit of $25,000. However, two days after the bankruptcy case was closed, she submitted a settlement demand to the defendant of $500,000. In that case, the court held that judicial estoppel did apply to limit the debtor's damages because her "position in the instant litigation is clearly inconsistent with the position that she asserted under oath in her bankruptcy proceedings." *Id.* at 881. It was also significant to the court that "the timing of events in the bankruptcy proceeding and the petitioner's choice of when to file her claim indicate[d] bad faith." *Id.* at 884. *See also*, *Caplener v. U.S. Nat. Bank of Oregon*, 857 P.2d 830 (Or. 1993) (judicial estoppel applied when debtor sought $11 million in damages from defendant after listing value of claim as $451,000 in its bankruptcy schedules and stipulating to the validity of a claim by the defendant against the debtor in its prior bankruptcy).

Another situation that arises is when a debtor submits an insurance claim which includes values for damaged personal property that are significantly higher than the values listed for that property in a prior bankruptcy. Decisions addressing this issue are also mixed. In *Pavelka v. Allstate Prop. and Cas. Ins. Co.*, 91 F.Supp.3d 931 (E.D. Mich. 2015), the debtors listed their personal property as having a value of $24,500 in their prior bankruptcy. Later, their home and personal property was destroyed by a fire. In the insurance claim, the debtor-plaintiffs claimed the value of

the destroyed personal property was between $268,809 and $317,292. Allstate argued, among other things, that the plaintiffs were judicially estopped from claiming the much higher value for their property. The court disagreed on the grounds that the methods for calculating values were different in bankruptcy than for insurance purposes. In bankruptcy, the court said, the value is traditionally placed on the "liquidation" or "garage sale" value whereas for insurance, it is the "replacement value." Since the methods are different, the positions taken by the debtor-plaintiffs were not inconsistent. *Id.* at 936-39.

On the other hand, in *Rizka v. State Farm Fire and Cas. Co.*, No. 13-cv-14870, 2015 WL 9314248 (E.D. Mich. Dec. 23, 2015), the plaintiff had previously filed bankruptcy and indicated on her schedules that she did not own a home – she said she was renting the home in which she lived from her sister – and that her personal property was worth only $1,700. After discharge, the home sustained damage in a fire and she filed a claim under a homeowners' insurance policy she had obtained on the residence pre-petition. As part of the insurance claim, she said she was the owner of the home and claimed the replacement cost of the damaged personal property was over $200,000. State Farm argued that the plaintiff was judicially estopped from claiming to own the home and additional personal property. The court agreed holding that the plaintiff's position in the insurance claim were directly contradictory to her sworn statements in her prior bankruptcy. Because she could not claim to be an owner of the home, she was barred from any recovery under the homeowners' policy.

One way to try to avoid judicial estoppel is to disclose the potential claim in the bankruptcy schedules with a listed value of "unknown." While cases involving this scenario are much less common, it appears that courts may be more hesitant to find judicial estoppel as a bar to later litigation in this situation. For example, in *Holber v. Segal*, 510 B.R. 753 (Bankr. E.D. Penn. 2014),

the debtor listed a potential claim under a consulting contract in his bankruptcy schedules with a value of "unknown." When the claim later turned out be worth upwards of $2 million, the bankruptcy court still refused to apply judicial estoppel, noting that the claim had been disclosed and several interested parties had had extensive conversations with the trustee regarding the nature and potential outcomes of litigation involving that claim. As a result, the debtor was not later estopped from pursuing his claim. The court's reliance on the additional information provided to the trustee in *Holber* suggests, though, that if a court were to find that a debtor was attempting to mislead the trustee or bankruptcy court by listing a value of "unknown," it may be more willing to find that judicial estoppel bars a debtor's later pursuit of the claim.