AMERICAN BANKRUPTCY INSTITUTE

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# Prosecuting and Defending § 523 Adversary Proceedings


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CONCURRENT SESSION

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**Post-Petition/Pre-Litigation Tactics**

From the creditor perspective:

- Review the Debtor's Schedules and SOFA.
    - How is your client's claim being treated? Is the Debtor disputing either the amount of the debt or treatment of the claim?
    - What other information can you glean from Schedules and SOFA?
        - Maybe there are other similarly situated creditors that you can coordinate with/gather intelligence from. You may learn of other litigation/deposition testimony of Debtor that benefits you.
    - Understand the basics:
        - What is the collectability of Debtor and the prospect for payment on your client's claim? Does the Debtor have the ability to obtain funds to resolve your client's claim?
        - Does Debtor have multiple creditors or are you the only real creditor in the bankruptcy case?
- Know your theory of the case/cause of action.
    - What facts support your § 523 claim? Maybe there are multiple § 523 causes of actions that fit your facts.
    - What documentary evidence do you have that supports your cause of action?
    - What facts/documents are missing?
- If some of your facts need further development, consider appearing at the § 341 hearing or taking a Rule 2004 examination of the Debtor (or a non-debtor, if necessary).

- Debtor is under oath at the § 341 hearing and your client's claim is fair game for questioning.

- Rule 2004 examination requires motion/stipulation of Debtor, but allows you more time and greater latitude to examine the Debtor. You can also require document production by Debtor.

    - Is there an underlying tension in Debtor's counsel representing Debtor at the § 341 hearing but not in a Rule 2004 examination or any adversary proceeding? How prepared is the Debtor to answer questions at the § 341 hearing?

- Be aware of the pending proceeding rule - Rule 2004 examination may be limited or not permitted once adversary proceeding has been filed. *In re Enron Corp.*, 281 B.R. 836, 840 (Bankr. S.D.N.Y. 2002) ("Courts have imposed limits on the use of Rule 2004 examinations where the purpose of the examination is to abuse or harass, or under the well recognized rule that once an adversary proceeding or contested matter is commenced, discovery should be pursued under the Federal Rules of Civil Procedure and not by Rule 2004.") (internal citations omitted).

- Does it make sense to seek an extension of the § 523 deadline to negotiate or gather more facts?

    - If you don't have all of the facts, seek an extension from Debtor's counsel. There are situations where you decide against filing a § 523 once you have all the facts.

    - Be aware of the timing requirement in Rule 4004(b) - if you are filing a motion to extend the deadline, the motion must be filed before the time to object has expired.

From the debtor perspective:

- Put some thought into how you schedule the creditor's claim.

    - Is it contingent, unliquidated, or disputed?

- Is the claim subject to offset?
- Does Debtor have counter-claims against the creditor that need to be disclosed?

- Make sure that your client is prepared for questioning at the § 341 hearing.
  - This is where creditors' attorneys hope that the Debtor will make a mistake.
  - Object to questions on behalf of your client if necessary.
  - Seek to curtail the § 341 examination and offer to discuss a Rule 2004 examination if the questioning becomes too invasive.

- If you are representing the Debtor at the Rule 2004 examination, make sure that they are prepared.
  - You should approach the examination no differently than a deposition in a litigation case. Prepare your client, object to questions, and attempt to rehabilitate your client if necessary after examination by the creditor's attorney.

- Does it make sense to agree to § 523 extension?
  - Maybe. It is generally always preferable to work with opposing counsel to see if a § 523 can be entirely avoided. However, it also depends on your client and your specific facts.

**Push The Nuclear Button? Should You Include A § 727 Count?**

From the creditor perspective:

- Is there a good-faith basis to assert a § 727 cause of action?
  - Sometimes a § 727 might be easier than a § 523. Example - § 727(a)(4), debtor knowingly, fraudulently, and in connection with the case made a false oath. If Debtor lied at the § 341 hearing or Rule 2004 examination, a § 727 might be easier for you to prove than a § 523 action.

- Does a § 727 cause of action generate any tactical advantage?
    - It might if the Debtor has a lot of debts. On the other hand, if your client is the only real creditor in the bankruptcy case, § 727 versus § 523 likely makes no difference.
- Negative aspects of § 727?
    - Riding the coattails concern - other creditors benefit from your prosecution of a § 727. If all creditors are able to pursue Debtor for their debts, it reduces potential recovery to your client.
    - But, is this a legitimate concern? How many creditors pursue a non-dischargeable debt if they were not actively involved in the bankruptcy case?
- Be aware of § 727 resolution issues. For example, Eastern District of Michigan has Local Rule 7041-1:

> **Rule 7041-1 Dismissal of a Complaint Objecting to the Discharge of the Debtor**
>
> When the parties to an action under § 727 propose to dismiss the action, they must file a joint statement of the consideration received or to be received by the plaintiff. The plaintiff must then serve the joint statement on all creditors and the trustee, with a notice stating that the deadline to file objections is 14 days after service, and file a certificate of service. If no timely objection is filed, the plaintiff must promptly file a certificate of no response and submit the agreed proposed dismissal order. If a timely response is filed, the court will set the matter for hearing. An original signature from a pro se party is not necessary to authorize the filing of a joint statement under this rule; a fax, email or written signature or consent is sufficient.

From the Debtor perspective:

- Order copies of all of your client's prior depositions, including § 341 and Rule 2004 transcripts. You need to accurately understand what your client testified to. Do not rely on your memory or the Debtor's memory.
- You need to understand the collectability of your client and prospect for future earnings. You also need to discuss if your client has ability to

obtain money from third-parties. This will help you understand whether there is a path towards resolution or a viable "poverty" defense.

- Does the § 727 make a substantial difference in the Debtor's view? Depends on whether there are multiple creditors. If it makes a substantial difference, try to resolve with the objecting creditor.

**Mediation Strategies**

- The Eastern District of Michigan has a wonderful mediation panel - Use It.
    - Every mediator on list is capable of handling your matter.
    - It is important to understand what kind of "personality" you need in a mediator.
- Timing - There are two basic approaches. Mediate right away or mediate after some/all discovery has been completed. Discuss this during your Rule 26(f) Conference with opposing counsel. Consider setting a mediation completion date that is incorporated into the Rule 26(f) Report.
    - Considerations in mediation timing:
        - Is factual development necessary?
        - Are the parties in different settlement ballparks?
        - Is motion practice necessary to eliminate some or all of your opponent's claims before you mediate?
- Resistance to mediation - Generally speaking, don't resist efforts to mediate, but:
    - Do you have enough facts to proceed with mediation?
    - If vindication is what your client wants, mediation might be a waste of time.
    - Maybe the personalities of the lawyers/clients requiring softening (motion practice) before going to mediation.

- Approach to mediation:
    - Presumably, you mutually agreed on a mediator with the other side. Trust the mediator and let the mediator handle the mediation as they see fit. However, be realistic - if the two sides can't be in the same room together, tell the mediator ahead of time.
    - What is the Debtor's collectability, prospect for future earnings, and access to monies from others? Sometimes, you don't know the answers to these questions until you get into a mediation.
        - Discuss all of these concepts with your client ahead of time. This sets expectations for mediation.
    - What are potential ways to resolve the dispute? In a §§ 523 or 727, there are generally three ways: money, non-dischargeable judgment in agreed upon amount, or a combination of the first two items.
        - Remember - be creative! This is what sets us bankruptcy lawyers apart from other lawyers. We solve difficult problems with creative solutions.
- You reach a resolution at mediation. Now what? Put your resolution in writing and have it signed by all of the parties. Even if the writing is a term sheet that is subject to a definitive settlement agreement, get it signed by the parties. Rely on the mediator if there is a subsequent breakdown in documenting the settlement.

# Timeline of a Bankruptcy Trial and the Court Rules and Tools for Litigation

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## Introduction

Having an organized and strategic approach to litigation is invaluable to an attorney's success in litigating a bankruptcy adversary proceeding. Even though ultimate success may be "winning" at the end of a trial, in bankruptcy cases, the financial resources to litigate a case are likely limited on either or both sides of the adversary proceeding and winning may have many different definitions. For example, there may be no solid defense of a debtor in a nondischargability action. Winning in those circumstances may mean narrowing issues, reducing liabilities and exposure and ultimately resolving a nondischargability claim on terms the defendant can live by and satisfy. Short of going to trial, litigation and the procedural steps involved can provide meaningful strategic opportunities to reach a final resolution of disputes or opportunities to organize and refine the defense or prosecution before the trial date arrives. Using each stage of the adversary proceeding as strategic step in advocating for a client's interests will make the litigation manageable and an organized trial presentation achievable.

The following outline sets out a basic adversary proceeding timeline and the steps involved in the lawsuit from filing the complaint all the way to trial. Rules and case law are cited throughout as helpful reference points for building either a strong prosecution or defense. Even the rules that seem most obvious are included as helpful reminders to eliminate minor but common errors that can create unnecessary speedbumps in developing a case. More complex

and significant rules are citied along with useful case law (thanks to Judge Thomas J. Tucker for a list of relevant citations to his opinions) to help frame important pleadings and motions that may be useful in practical application.

## I. Complaint Filed.

### A. Causes of action requiring the filing of an adversary proceeding.

Fed. R. Bankr. P. 7001 outlines the specific actions that must be initiated by the filing of an adversary proceeding. The following actions are the most likely lawsuits that a party in interest may file in a bankruptcy proceeding require more than a motion:

- ✓ 7001(2) a proceeding to determine the validity, priority, or extent of a lien or other interest in property, but not a proceeding under Rule 3012 or Rule 4003(d)
- ✓ 7001(4) a proceeding to object to or revoke a discharge, other than an objection to discharge under §§727(a)(8), (a)(9), or 1328(f) [11 USCS § 727(a)(8), (a)(9), or 1328(f)];
- ✓ 7001(5) a proceeding to revoke an order of confirmation of a chapter 11, chapter 12, or chapter 13 plan;
- ✓ 7001 (6) a proceeding to determine the dischargeability of a debt;
- ✓ Creditors may be in the position of defending actions under 7001(2) and 7001(1) – recovery of money or property from a third party such as a preference action pursuant to 11 U.S.C. §547;

### B. Pleadings to accompany a party's initial filings.

Additional requirements that parties to an adversary proceeding include the filing of a statement of corporate ownership Fed. R. Bankr. P. 7007.1 where the filing party is not a person. This is a requirement whether initiating the adversary proceeding with the filing of a complaint or filing the very first responsive pleading as defense counsel. A form is available on the court's website to complete this statement.

### C. Jurisdictional averments required in a bankruptcy adversary proceeding.

In addition to the jurisdictional pleading required under Fed. R. Civ. P. 8, in an adversary proceeding Fed. R. Bankr. P. 7008 provides that the jurisdictional statements "shall also contain a reference to the name, number, and chapter of the case under the Code to which the adversary proceeding relates and to the district and division where the case under the Code is pending. In an adversary proceeding before a bankruptcy court, the complaint, counterclaim, cross-claim, or third-party complaint shall contain a statement that the pleader does or does not consent to entry of final orders or judgment by the bankruptcy court."

### D. Summons Issued (Instantly issued by clerk on ECF)

### E. Summons Service Executed

#### 1. Summons and complaint must be served directly to defendant.

An Adversary Proceeding is a new proceeding even though it stems from a bankruptcy filing. The complaint therefore must be mailed/served directly on the defendant even if defendant is represented by bankruptcy counsel in the main bankruptcy proceeding. See *Tex-Link Communs., Inc. v. Lopez* (*In re Lopez*), 2008 Bankr. LEXIS 3146, 61 Collier Bankr. Cas. 2d (MB) 205. "Plaintiff relied on Debtor's Attorney's ECF agreement, service upon Debtor's Attorney through ECF is effective only to the extent of his written consent. There is nothing in the record to indicate that Debtor's Attorney consented in writing to service of the Complaint by electronic means."

2. Service of a summons and complaint in a bankruptcy adversary proceeding is permissible by First Class Mail

Fed. R. Bankr. P. 7004(b) permits service of the summons and complaint within the United States by first class mail rather than by personal service. Service on a human being is required even if named defendant is a corporation or business entity. If the lawsuit is served on a corporation, partnership or other business entity, Fed. R. Bankr. P. 7004(b)(3) requires service on an "officer, a managing or general agent, or to any other agent authorized by appointment or by law to receive service of process." This means it is imperative to specify in the proof of service and the complaint the name of a corporate officer or resident agent of a business entity named as a defendant in the lawsuit. Service on a business entity without a named officer or agent will be defective and rejected by the court. If the debtor is a plaintiff and suing for discharge of federal student loans or for any other reason the named defendant is the United States or an agency of the United States, Fed. R. Bankr. P. 7004(b)(5) provides proper instructions for service on the United States agency named in the lawsuit.

II. Responsive pleading due (30 Days after Summons Date) Fed. R. Bankr. P. 7012

Defendants may choose to simply answer the complaint and file affirmative defenses. Affirmative defenses ought to be filed with the answer to avoid risk of losing those defenses. Debtors' attorneys have an imperative professional duty to communicate with debtor clients about the deadline for filing an affirmative response and the repercussions for failing to timely respond. Irrespective of the professional duties, debtors' attorneys are not obliged to act as

defense counsel for debtor clients.[1] Debtors' attorneys can enter new retainer agreements to handle the adversary proceeding or may refer debtors to other counsel to handle litigation.

**Motions to dismiss pursuant to Fed. R. 12(b)(6) for failure to state a claim upon which relief may be granted.** Outright dismissal under Fed. R. Bankr. P. 7012/Fed. R. Civ. P. 12(b)(6) is rare. Courts are within their discretion to grant plaintiffs an opportunity to file an amended complaint pursuant to Fed. R. Bankr. P. 7015/Fed. R. Civ. 15(a) if the complaint fails to meet the standards of specificity set forth by Fed. R. Bankr. P. 7009/Fed. R. Civ. P. 9.

**A. Dismissal of time-barred lawsuits.**

Dismissal motions will consistently succeed where there is a statutory time-bar to the adversary proceeding filed. For instance, the court will dismiss an untimely filed non-dischargability action where the creditor had proper notice of the bankruptcy case. Debtors' counsel should consider though of Fed. R. Bankr. P. 1009-1 regarding amendments to add creditors – the deadline for nondischargability actions is extended for creditors who are added to receive notice when added within 14 days prior to or anytime after the meeting of creditors. LR (ED Mich) 1009-1(d).

In *Wahrman v. Bajas* (*In re Bajas*), 443 B.R. 768, 773 (ED Mich), the dismissal pursuant to Fed. R. Civ. P. 12(b)(6) was granted primarily because of the creditors untimely filed nondischargeability complaint. The plaintiff made no argument for equitable tolling of the complaint deadline nor had the court found there was any basis to rule in plaintiff's favor on equitable tolling. This example of where there was an untimely filing of a nondischargeability

[1] Attorneys should take caution to write their retainer agreements and complete Form 2016(b) in a manner that sets this out clearly for clients and communicate this to clients particularly where there is a known risk that a nondischargability action may arise.

complaint is a concrete example of where there is no opportunity for a creditor to amend a defective complaint.

A debtor's attorney defending a complaint to object to discharge or for nondischargability should take caution in freely consenting to amendments to the complaint to add new counts. There is case law to support the denial of leave to amend a pleading if a new set of facts is alleged for a new reason to deny discharge or dischargability once the discharge deadline has passed. The distinction may be narrow but worth considering before allowing a plaintiff to add more to the complaint.

### B. Failure to state a claim with particularity.

Plaintiffs who seek relief in counts related to bankruptcy specific remedies will typically overcome 12(b)(6) motions. The standard for 12(b)(6) is "failure to state a claim upon which relief can be granted." It is important to carefully distinguish grounds for dismissal for failure to state a claim and a grounds for a motion for summary judgment where based on undisputed facts, movant is entitled to a judgment or ruling in their favor based on law.

Fed. R. Bankr. P. 7009/Fed. R. Civ. P. 9(b) sets out the particularity requirements in the context of fraud allegations and provides:

> In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.

*Gold v. Winget* (*In re NM Holdings Co., LLC*), 407 B.R. 232, 257 (ED Mich, 2009) offers a thorough analysis of the requirements of particularity of fraud allegations. It provides an additional level of analysis for pleading requirements as it relates to

bankruptcy trustees who have only third-party knowledge of the transactions that must be alleged in the complaint. The ruling additionally adopts the finding that the particularity requirement does not apply to constructive fraud allegations. *Id.* at 259. Rather, Rule 9 applies to allegations of actual or intentional fraud. *Id.* In alleging "a debtor's actual intent 'to defraud,' Rule 9(b) does apply, and the plaintiff must plead the 'circumstances constituting fraud' with particularity." The court instructs that the particularity can be met but setting forth in the complaint:

- ✓ the date of the transfer;
- ✓ the amount of the transfer (or if the transfer was of property other than money, the property that was transferred and its value);
- ✓ the name of the transferor;
- ✓ the name of the initial transferee; and
- ✓ the consideration paid, if any, for the transfer.

*Id.* at 261.

Ultimately, the plaintiff in *Winget* was provided the opportunity to amend the complaint to allege intentional fraud with more particularity.

Even if the court is likely to provide a Plaintiff a second chance to meet the particularity requirements of Rule 9(b). There remain important legal and strategic reasons that could support filing a Rule 12(b)(6) motion under allegations of intentional fraud. The motion provides an opportunity to present a recitation of the facts more favorably to the defendant, especially where fraud is alleged, it is helpful to reframe the positive facts. Additionally, if the complaint is objectively vague, it will be important to pin down exactly what the plaintiff must prove. So while the plaintiff might still inevitably have to re-draft the complaint, it will help narrow the issues.

Plaintiffs also should consider the importance of the complaint as the first line of advocacy for the client. Alleging vague instances or actions of fraud erode the credibility of the complainant. Every debtor filing bankruptcy is avoiding paying creditors. That's the point! Sometimes debtors even execute settlement agreements only to file a petition the very next day. We all have that right (with of course the exception of serial filers)! What are the exact instances or actions of the debtor that constitute intentional fraud? Do they really exist? If they do, identify them. Who, what, when, where and how.

## III. Fed. R. Bankr. P. 7026(f) Status Conference

Counsel for plaintiff and defendant confer by phone, email or in person to draft 26(f) Report setting deadlines for discovery and proposed date for trial. The meeting is initiated by Plaintiff's attorney and report is prepared and filed by Plaintiff. Although deadlines set out in the 26(f) Report can be extended, counsel should consider how much time will be necessary to complete discovery and set out a calendar based on what can be realistically accomplished in the time agreed upon.

NOTE: <u>The timeline after the status conference.</u> The following timeline is not necessarily in the order an adversary proceeding must follow. Discovery, mediation and summary judgment may all have particular deadlines for completion, however, one does not necessarily follow the other. It is important for counsel to be aware of the facts and issues in the case and the resources to determine what comes next. Mediation may come immediately after the status conference or it may be better placed mid or post-discovery or immediately prior to trial or at some other place. Discovery is ongoing from the end of the parties' discovery conference until its deadline. A summary judgment motion may be better placed after an initial discovery response is filed or after discovery is concluded.

## IV. Discovery commences upon conclusion of 26(f) conference between attorneys. DO NOT DELAY!

Plaintiff and defense counsel should each consider serving written discovery: requests for admissions, interrogatories and production of documents. Defense counsel should not look at discovery as only the plaintiff's job to do. Discovery can be an invaluable tool to defense litigation. The goal is not to prove or disprove the case. The goal is to narrow the facts and issues. The goal is to clarify what the plaintiff is really after or what evidence the plaintiff may use at trial.

### A. Depositions.

Counsel should also identify what depositions need to be conducted, who are the witnesses? Which witnesses' testimony will be useful to have before trial? What testimony will be useful in seeking summary judgment relief? Is there testimony that may be helpful for potential witness impeachment at trial? Deposition notices should be deployed in a strategic and effective way. For instance, depositions of organizations such as the State of Michigan, corporations or non-human entities should be done pursuant to Fed. R. Civ. P. 30(b)(6). Setting up an adversary proceeding calendar and proactive planning as plaintiff's counsel and likewise for defense attorneys will save time and client resources. As defense counsel, a discovery plan should identify the elements of each count that opposing counsel must prove in much the same way that plaintiff's counsel must dissect the elements of each count that plaintiff must prove. What witnesses, documents and other information will give credit to or discredit these counts?

Working backward from the trial date and the discovery cut-off deadlines, who needs to testify before trial? What documents should the opposing party have that help or hurt your client?

Rule 30(b)(6) is an important time-saver, it requires the entity to produce the witness with actual knowledge of the facts and circumstances for which testimony will be produced. That rule provides that the notice "must describe with reasonable particularity the matters for examination. The named organization must then designate one or more officers, directors, or managing agents, or designate other persons who consent to testify on its behalf; and it may set out the matters on which each person designated will testify. . . ." "Essentially, '[i]n a Rule 30(b)(6) deposition, there is no distinction between the corporate representative and the corporation.'" *Rosenruist-Gestao E Servicos LDA v. Virgin Enters.*, 511 F.3d 437, 445 (4th Cir. 2007) (Quoting *Sprint Commc'ns. Co. v. Theglobe.com, Inc.*, 236 F.R.D. 524, 527 (D. Kan. 2006)). Where

B. Initial disclosures.

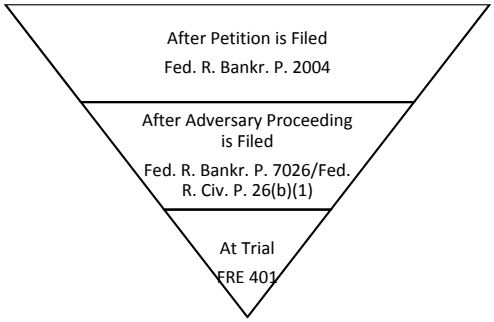
Counsel will also need to file initial disclosures by the parties' agreed deadline to identify known witnesses and exhibits unless the parties agree to waive this requirement in 26(f) report.

C. Written discovery requests.

Requests to admit ("RTAs") pursuant to Fed. R. Bankr. P. 7036/Fed. R. Civ. P. 36 are a great tool to narrow issues, or to force confirmation of the allegations. Failure to timely respond to RTAs without a proper extension will mean the facts are admitted pursuant to R. 36(a)(3). Lack of a timely response to RTAs will be useful evidence to seek a motion for summary judgment.

### D. Scope of discovery in an adversary proceeding versus a bankruptcy proceeding.

When determining how to develop or respond to discovery requests, counsel should heed the distinctions of Fed. R. Bankr. P. 2004 and its broad scope of discovery of debtors and parties in interest and the narrower scope of discovery upon the commencement of an adversary proceeding. Counsel for parties considering filing an adversary proceeding should use the pre-litigation period to as an opportunity to discover records and information that may help develop or expand the claims and supporting facts. Defense counsel should carefully consider what is requested in written discovery to ensure that the scope of discovery is related to the claims filed to safeguard clients from the "fishing expedition" that is permissible in pre-litigation bankruptcy discovery.




### E. Discovery of electronically stored information.

Procedures for electronic discovery – LR (ED Mich) 7026-4 directs parties to implement the Model Order Relating to The Discovery Of Electronically Stored Information ("ESI") which is available on the District Court Website for Easter District of Michigan. If there is any likelihood that prosecution or defense of the adversary proceeding will involve e-mails, electronic

calendars, internal corporate messaging systems, text messages, these items are ESI and should not be overlooked or underestimated in their value to the case.

## V. Mediation

Plaintiff and Defendant may seek mediation, or the court may order mediation to occur. The court has a list of court-approved mediators that parties may choose from, mediators on the list are all experienced bankruptcy counselors who have obtained mediation training. In most circumstances the parties will be given the discretion to jointly select a mediator. Each mediator may have minor differences in their approach to the mediation.

Mediation is another good strategy point. For the plaintiff it can stem legal costs heaped on the economic loss already incurred. It provides both plaintiff and defendant to articulate their claims and defenses in a simple way. It allows the parties themselves to hear the strengths and weaknesses of their claims or defenses from someone other than their own legal counsel. It is an opportunity to narrow the issues.

## VI. Settlement

Settlement of adversary proceedings will come in a myriad of ways. It may or may not require the use of a mediation or settlement conference. However, plaintiffs invoking a count under 11 U.S.C. §727 will be required to give notice and an opportunity for other parties to object to the dismissal of a §727 lawsuit. See LR (ED Mich) 7041-1 regarding dismissal of a complaint objecting to discharge of the debtor.

## VII. Summary Judgment

Plaintiff and Defendant may file motions for summary judgment. It requires an analysis of Fed. R. Bankr. P. 7056/Fed. R. Civ. P. 56. What facts are undisputed? What can be decided as a matter of law? Rule 56 "provides that a motion for summary judgment 'shall' be granted "if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." *Madden v. Morelli* (*In re Energy Conversion Devices, Inc.*), 548 B.R. 208, 215 (ED Mich, 2016) (Quoting *In Cox v. Kentucky Dep't of Transp.*, 53 F.3d 146, 149-50 (6th Cir. 1995). *Morelli* goes on to incorporate the thorough analysis of the summary judgment standards set forth in *Cox.* The court further says: "In determining whether the moving party has met its burden, a court must "'believe the evidence of the nonmovant, and draw all justifiable inferences in favor of the nonmovant.'" *Id.* (Quoting *Ingram v. City of Columbus*, 185 F.3d 579, 586 (6th Cir.1999), other citations omitted).

Summary judgment is another good strategic litigation tool. Passing up the opportunity to file a summary judgment motion should not be decided upon lightly. Summary judgment provides a three-fold opportunity (1) The defendant has an opportunity to kick out some or all of the counts to narrow the issues for trial; (2) It can provide defense and plaintiff's counsel each the necessary foundation for the joint final pretrial brief – a summary judgment brief is the first chance to organize exhibits, identify evidence that exists or is lacking and to implement a structure for presentation at trial and (3) The hearing itself and the court's ruling can provide clues for what is inadequate in your prosecution or defense – what in the court's view was lacking? What will you need to do at trial to convince the judge?

## VIII. Pre-Trial

Plaintiff and Defendant draft their joint final pretrial brief and compile exhibits. This is due to court BEFORE the joint final pre-trial conference. At the point when counsel is drafting the joint-final pretrial brief there are a couple of resources that are already developed. LR (ED Mich) 7016-1 sets out parties' responsibility to file a joint final pretrial brief and the required contents of the brief. The motion for summary judgment and related brief is a useful first draft of a joint final pretrial brief. At this point all exhibits should be organized and prepared for presentation to the court. Judges in the Eastern District of Michigan expect that documents are presented prior to trial. Attorneys should have a plan for preparing enough "trial copies" of exhibits. (1) Witness Copy (2) Plaintiff's Copy (3) Defendant's Copy and (4) Judge's Copy. Are the exhibits labeled clearly? Are they easy for witnesses to locate?

IX. Joint final pre-trial conference is held.

X. Trial

a. Admission of exhibits into the record

b. Plaintiff's Case in Chief

c. Defendant's Case in Chief

# The Necessary Elements for Collateral Estoppel in Michigan Bankruptcy Adversary Proceedings

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## *What is Collateral Estoppel?*

**Collateral Estoppel prevents a party from relitigating issues of fact or law, which were necessarily decided by a previous final judgement. See Smith v. Sushka, 417 F.3d 965,969 (6th Cir. 1997).**

**In Bankruptcy cases, collateral estoppel applies in non-dischargeablity proceedings; under the Bankruptcy Code, such as Adversary proceedings. See Grogan v. Garner, 498 U.S. 279 (1991).**

**If state courts would give "preclusive effect" (which is collateral estoppel) to the judgement, then the bankruptcy court must also give the judgement preclusive effect . The exception to this rule is if Congress has expressly or impliedly created an exception to 28 U.S.C.§1738, which should be applied to the facts before the federal court.**

**In determining the application of Collateral Estoppel in a bankruptcy proceeding, one must first consider the law of the State which the in which the judgment was rendered to determine preclusive effect. See Full Faith and Credit Statute, 28 U.S.C.§1738.**

**In order to invoke the doctrine of collateral estoppel, the party seeking estoppel must establish that:**

1. **There has been a final judgment on the merits in a prior action;**
2. **The issues are identical; and**
3. **The party to be estopped was a party or in privity with a party in the prior action.**

**With issue preclusion, it is important to note that the issue must have been "actually litigated and determined" in the prior litigation.**

**Under Michigan law, the following requirements must be met in order for collateral estoppel to apply:**

1. **There is identity of parties across the proceedings;**
2. **There was a valid, final judgment in the first proceeding;**
3. **The same issue was actually litigated and necessarily determined in the first proceeding; and**
4. **The party against whom the doctrine is asserted had a full and fair opportunity to litigate the issue in the earlier proceeding.**
   **See McCallum v. Pixley (In re Pixley), 456 B.R. 770 (Bankr. E.D. Mich. 2011).**

**When filing your complaint, one must plead pursuant to F.R.C.P. 8(a)(2), a "short and plain" statement of the claim showing that the pleader is entitled to relief. "Detailed factual allegations "are not required. See Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2000). The Twombly case sets forth the "flexible plausibility standard" obligating a pleader to amplify a claim with factual allegations where necessary to render it plausible. See Ashcroft v. Iqbal, 490 F.3d 143 (2009). The rule set forth above does not call for sufficient factual matter, accepted as true, but only to "state a claim to relief that is plausible on its face". These cases set forth the standard for pleading the allegations necessary to set forth the plausibility of the Debtor being liable for damages in an adversary proceeding.**

**When a motion to dismiss is being considered, it should be noted that a motion to dismiss does not need detailed factual allegations, a moving party's obligation to provide "the grounds of his entitlement to relief requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do. See Wahrman v. Bajas (In re Bajas) 443 B.R. 768 (Bankr. E.D. Mich. 2011). In relying upon the legal theory of collateral estoppel, factual allegations must be enough**

**to raise a right to relief above the speculative level, on the assumption that all of the allegations in the complaint are true in fact. See also, Ashcroft v. Iqbal et al , 490 F.3d 143 (2009).**

**In Re Wahrman outlines in great detail, the standard upon which a motion to dismiss, pursuant to F.R.C.P. 12(b)(6) is overcome with the Twombly "plausibility" requirement. In the case, McCallum v. Pixley (In re Pixley) 504 B.R. 852 (Bankr. E.D. Mich. 2014), the court discusses whether or not the exact cause of action was litigated regarding a default judgment in the State court action. Substantial participation by a defendant in a state court case is not necessary in order for collateral estoppel to apply. The court determined in the above referenced cases that failure of the defendant to participate in the litigation process did not preclude collateral estoppel standing for and in the bankruptcy case.**

**Under Michigan law, a "true default" judgment meets Michigan's "actually litigated" requirement and must therefore be given preclusive effect under the doctrine of collateral estoppel. Substantial participation by a defendant in a State court case is not necessary in order for collateral estoppel to apply. The court determined that failure of the defendant to participate in the litigation process did not preclude collateral estoppel standing for the bankruptcy case.**

**The Michigan Supreme court has stated that a default judgment is just as conclusive as adjudication and as binding upon the parties of whatever is essential to support the judgement as one which has been rendered following answer and contest. See Barnes v. Jeudevine, 475 Mich. 696,718 N.W.2d 311, 315 (Mich. 2006). The Sixth Circuit's Bankruptcy Appellate Panel concurred, stating that the Barnes Court shows that "the Michigan Supreme Court does not distinguish among judgments, whether entered by default or otherwise, in applying the preclusive effect of the collateral estoppel doctrine".**

**In the case of Townsel v. Recon Mgmt. Group,LLC, 2017 W.L. 1130094 (E.D. Mich. 2017), the court sets forth in Michigan, the process**

**for determining how an issue is "actually litigated". In this case, the same elements were established by the moving party in their adversary proceeding, by incorporating by reference, the elements of embezzlement from the debtor's state court conviction. The court concluded that the definition of embezzlement was the same as set forth in the bankruptcy court, specifically, 11U.S.C. §523(a)(4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement or larceny. See further 11 U.S.C §523(a)(4) regarding embezzlement.**

**In this case, different from In McCallum v. Pixley (In re Pixley) 504 B.R.852 (E.D. Bankr. Mich. 2014), the court noted that the count of fraud was only noted in the default judgement and was not plead in the complaint.**

**By way of comparison, several cases in this district have set forth reasons why collateral estoppel will not be able to be applied in an adversary proceeding See Chamberlain v. Messer, 500 B.R. (Bankr. E.D. Mich. 2013). In this case, the issue of the application of collateral estoppel is voided, because the same elements were not plead in both cases; including both the state and the bankruptcy court adversary proceeding.**

**The Michigan Supreme Court has stated that "a default judgment is just as conclusive an adjudication and as binding upon the parties of whatever is essential to support the judgment as one which has been rendered following answer and contest". See Barnes v. Jeudevine, 475 Mich. 696, 718 N.W. 2d 311, 315 (Mich.2006).**

**In conclusion, it is very clear that in order to rely upon the doctrine of collateral estoppel in a bankruptcy proceeding, creditors must set forth the same elements in both state court actions and the judgments that follow must fall in line with the elements set forth as necessary in bankruptcy court adversary proceedings.**