When a Prior Bankruptcy Judicially Estops a Debtor from Filing a Claim:

The Applicability of a "Clearly Inconsistent Position" under Washington Law

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Judicial estoppel is a legal principle which deprives a party from asserting a claim or position inconsistent with the party's position in a prior legal proceeding if three elements are met: (1) the party's later position is clearly inconsistent with its earlier position; (2) judicial acceptance of an inconsistent position in a later proceeding will create the perception that either the first or second court was misled; and (3) the party seeking to assert an inconsistent position would receive an unfair advantage or impose an unfair detriment on the opposing party. Most Washington cases analyzing the applicability of judicial estoppel focus on the first element, that is, whether the two positions maintained by a party are "clearly inconsistent."

In a prior bankruptcy proceeding, Washington courts have consistently held that when a debtor failed to disclose a potential claim or other asset as an asset in a bankruptcy proceeding, the debtor is judicially estopped from later asserting the claim or seeking recovery of the asset post-discharge. *See*, *McFarling v. Evaneski*, 141 Wn. App. 400 (2007); *Skinner v. Holgate*, 141 Wn. App. 840 (2007); *Cunningham v. Reliable Concrete Pumping, Inc.*, 126 Wn. App. 222 (2005). When a debtor first represents in a bankruptcy proceeding that he has no potential claim or asset against another and then later represents in a lawsuit that he does have such a claim or asset, the debtor has taken two clearly inconsistent positions. Washington courts reason that if a debtor was allowed to not disclose a potential claim or asset in bankruptcy and later seek recovery of the claim or asset, he has deprived the bankruptcy trustee and his creditors from potentially being compensated for his debts and instead is able to collect for himself.

Conversely, Washington courts have held that if a debtor does disclose the potential claim or asset in his bankruptcy petition, even if the claim or asset is significantly undervalued, the disclosure is sufficient to put the bankruptcy trustee and creditors on notice to determine whether

to attempt to collect on the potential claim or asset. If the debtor's bankruptcy is then discharged, the debtor is free to pursue collection of the claim or asset. *See*, *Baldwin v. Silver*, 147 Wn. App. 531 (2008); *Ingram v. Thompson*, 141 Wn. App. 287 (2007); *see also*, *Cusano v. Klein*, 264 F.3d 936 (9th Cir. 2001) (relied on in *Ingram*).

For example, in *Ingram v. Thompson*, the parties were involved in a car accident. Two years later, Ingram filed a Chapter 7 bankruptcy petition. He listed his claim against Thompson as a personal injury lawsuit, as "value unknown, but believed to be less than $5,000." The bankruptcy trustee did not pursue the claim and the bankruptcy court discharged Ingram's debts. Then, Ingram filed a lawsuit against Thompson and provided an itemized statement of damages totaling $150,000. Thompson filed a motion for partial summary judgment to cap Ingram's damages recoverable at $5,000 based on judicial estoppel, and the trial court granted Thompson's motion.

Thompson argued that undervaluing an asset on a bankruptcy schedule is equivalent to failing to list the asset because the debtor has represented that his assets are less than what he later claims. The appellate court disagreed with Thompson, holding that stating a lower value for an asset is not equivalent to completely failing to list an asset in a debtor's bankruptcy schedules. The Court explained, "The bankruptcy trustee had the opportunity to inquire into the [personal injury] claim to decide whether the potential benefit to the creditors was worth the cost of litigating it." The Washington Court of Appeals held that, given the uncertainty inherent in valuation of the personal injury claim, and the fact that Ingram disclosed its existence, Ingram did not take clearly inconsistent positions.

In 2014, Washington had to determine whether a debtor could be judicially estopped from recovering an asset post-discharge if the debtor disclosed the asset in the bankruptcy, but represented that the asset had no value (as opposed to merely undervaluing or not specifying the value of the asset). This issue was decided in *Harris v. Fortin*, 183 Wn. App. 522 (2014). The Washington Court of Appeals had to determine whether a debtor's disclosure of a potential asset,

with the debtor's representation that the asset had no value and would never be collected, is tantamount to failing to disclose the potential asset.

In *Harris v. Fortin*, the debtor (Harris) disclosed in his Chapter 7 bankruptcy petition that another person (Fortin) owed him $400,000 on a promissory note. However, Harris represented to the bankruptcy court the value of the asset as $0 and further represented at his debtor's hearing that the asset had no value because Harris would not be able to collect the money as Fortin was not able to repay Harris. After Harris's bankruptcy was discharged and the bankruptcy trustee stated that the bankruptcy was a no-asset bankruptcy, Harris then sued Fortin on the promissory note. Fortin claimed that judicial estoppel prohibited Harris from asserting the claim because Harris had maintained in bankruptcy that the asset had no value.

The Washington Court of Appeals agreed, holding that when a debtor represents that an asset has no value and cannot be collected and then sues to collect on that asset, the debtor has taken clearly inconsistent positions (i.e., the asset has no value and is uncollectable, and then the asset does have value and can be collected). Furthermore, the clearly inconsistent positions are unfairly advantageous to the debtor since he did not have to pay his debts in bankruptcy based on not having any assets with which to pay the debts.

Washington courts have now established three different scenarios for determining whether judicial estoppel prohibits a debtor from later seeking to collect on an asset: (1) if the debtor did not disclose the asset in bankruptcy, he is judicially estopped from later attempting to collect on the asset; (2) if the debtor did disclose the asset in bankruptcy, even if the asset was undervalued, he is <u>not</u> judicially estopped from later attempting to collect on the asset; or (3) if the debtor did disclose the asset in bankruptcy, but affirmatively represented to the bankruptcy court and the creditors that the asset had no value, then he is judicially estopped from later attempting to collect on the asset.