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REPORT

Plaintiff's Bankruptcy and Judicial Estoppel of Employment Litigation

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Potential employment claims, if not properly disclosed in bankruptcy, can have dramatic effects on employment litigation. Even if the debtor has not filed an administrative charge or lawsuit at the time of the bankruptcy filing, that potential claim is an asset of the bankruptcy estate that, as such, must be administered by the real party in interest, the bankruptcy trustee.

Accordingly, the debtor must accurately assess and disclose the value of the claim in asset schedules, which are signed under penalty of perjury. Failure to do so may preclude recovery of damages in employment litigation. This article will address judicial estoppel in such cases and focus on problems the authors perceive in a single state, California.

Recent Decisions.

A number of recent federal decisions have recognized that judicial estoppel bars a plaintiff from proceeding with employment claims that the plaintiff failed to disclose in a bankruptcy filing.

In *Burnes v. Pemco Aeroplex Inc.*, [1] the U.S. Court of Appeals for the Eleventh Circuit held that the plaintiff was judicially estopped from pursuing monetary damages against his former employer, where the plaintiff had failed to disclose the discrimination claim in Chapter 7 bankruptcy schedules.[2] In that case, the plaintiff/debtor converted his Chapter 13 bankruptcy, which involves a repayment plan, to a Chapter 7, which calls for a discharge of debt, without amending his schedules to add the employment claim. The trustee made a ''no asset'' finding, resulting in the discharge of liabilities to creditors.

Before converting to Chapter 7, however, the plaintiff/debtor filed a charge of discrimination against the employer and joined other plaintiffs suing the employer for monetary and injunctive relief. The district court granted summary judgment for the employer because the plaintiff's failure to list the claim in his bankruptcy schedules was the basis for judicial estoppel.

Upholding summary judgment, the federal appeals court held that the failure to disclose the claim to the bankruptcy court judicially estopped the plaintiff from pursuing those claims in a civil lawsuit. It also upheld the district court's ruling that plaintiff should not be allowed to reopen the bankruptcy case to amend his filings.[3]

Burnes is not an aberration. Later decisions by the same federal appeals court have expanded its holding.[4]

[1] 291 F.3d 1282, 88 FEP Cases 1281 (11th Cir. 2002) (18 EDR 634, 5/29/02).

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[2] Although the *Burnes* court did not apply judicial estoppel to plaintiff's unreported claim for injunctive relief, the court of appeals indicated that the doctrine may apply under different facts. *Id.* at 1289 n.3 (''In reaching this conclusion, we express no opinion about other cases of undisclosed claims for nonmonetary relief to which judicial estoppel may or may not apply.'').

[3] *Id.* at 1288.

[4] *De Leon v. Comcar Indus. Inc.*, 321 F.3d 1289, 1291, 91 FEP Cases 105 (11th Cir. 2003) (applying *Burnes* in Chapter 13 context; ''We also conclude that any distinction between the types of bankruptcies available is not sufficient enough to affect the applicability of judicial estoppel because the need for complete and honest disclosure exists in all types of bankruptcies''); *Barger v. City of Cartersville*, 348 F.3d 1289, 92 FEP

A number of courts in other jurisdictions also have applied judicial estoppel to bar undisclosed employment claims.[5].

In a similar vein, a 2002 decision of the U.S. Court of Appeals for the Ninth Circuit Bankruptcy Appellate Panel recognized that nondisclosure of employment claims in a bankruptcy proceeding can bar a plaintiff from prosecuting those claims in civil court. Without reaching the issue of judicial estoppel, the appellate panel in *Lopez v. Specialty Restaurants Corp.*[6] held that the bankruptcy court erred in refusing to reopen a Chapter 7 bankruptcy where the plaintiff/debtor failed to disclose her sexual harassment claim against her former employer in her Chapter 7 schedules.

Federal Judicial Estoppel.

There is no uniform standard for applying judicial estoppel under federal law.[7] Federal courts generally agree, however, that certain factors should guide the analysis: (1) whether the party took ''clearly inconsistent'' positions, (2) whether the party was successful in having the first tribunal adopt the position in the prior proceeding, and (3) whether the party would obtain an unfair advantage if not estopped.

Failure to disclose a prepetition claim can establish a ''clearly inconsistent'' position.[8] While the bankruptcy court can ''adopt'' or ''accept'' the nondisclosure of claims by discharging debt,[9] this is not the only way to satisfy this factor. The bankruptcy court can also ''accept'' an undisclosed claim by approving the reorganization plan or by other affirmative use of judicial authority.[10]

The last factor focuses on the intent of the party and assesses whether the party has shown bad faith or has intentionally played ''fast and loose'' with the courts by taking contradictory positions. Whether a party's failure to disclose potential claims to a bankruptcy court will bar a later civil action rests primarily on the manner in which the particular jurisdiction construes the intent requirement.

Intent to Obtain Unfair Advantage. Federal courts recognize that judicial estoppel should not apply when the failure to reveal the claim was a result of inadvertence or mistake. These courts disagree, however, as to what constitutes ''inadvertence'' and as to what showing of bad faith — if any — is required. Some circuits are reluctant to impose the doctrine and will not do so unless the party to be estopped affirmatively acted in bad faith by engaging in ''knowing misrepresentation to or even fraud on the court.''[11]

Other federal circuits utilize a strict approach that will infer bad faith absent some showing of inadvertence or mistake by the nondisclosing debtor.[12] In these jurisdictions, great weight is placed on the statutory duty to disclose fully all assets; nondisclosure is considered ''inadvertent'' only if the party lacked knowledge of the claims *or* had no motive for their concealment.[13] Ignorance of the statutory duty to disclose all claims will not prevent imposition of judicial estoppel under this approach.[14]

Judicial Estoppel Under California Law.

Federal and state courts differ significantly in applying judicial estoppel. California courts apply judicial estoppel when (1) a party has taken two positions in judicial or quasi-judicial administrative proceedings, (2) the first tribunal adopted the first position or accepted it as true, (3) the two positions are ''totally inconsistent,'' and (4) the first position was not taken as a result of ''ignorance, fraud, or mistake.''[15]

While a party's failure to disclose potential claims in bankruptcy will typically satisfy the first three ele-

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Cases 1377 (11th Cir. 2003) (21 EDR 579, 11/12/03) (applying judicial estoppel even though plaintiff reopened her bankruptcy, disclosed the claim, and received an order from the bankruptcy court stating that the plaintiff ''did not conceal the [discrimination] claim or attempt to obtain a financial advantage for herself'').

[5] *Kamont v. West*, 258 F. Supp. 2d 495 (S.D. Miss. 2003) *aff'd* by *Kamont v. West*, 2003 U.S. App. LEXIS 22440 unpublished opinion (5th Cir. 10/31/03) (judicial estoppel barred employment lawsuit where plaintiff failed to list the claims in her Chapter 7 schedules); *Casey v. Peco Foods Inc.*, 297 B.R. 73 (S.D. Miss. 2003) (judicial estoppel barred undisclosed pregnancy discrimination claim; summary judgment for employer); *Nix v. Home Depot USA Inc.*, 2003 U.S. Dist. LEXIS 19178, 14 AD Cases 1806 (N.D. Ga. 10/16/03) (21 EDR 548, 11/5/03) (plaintiff judicially estopped from pursuing disability claim for monetary damages because he failed to disclose a pending charge against his employer in bankruptcy proceeding); *Compton v. DePuy Orthopaedics Inc.*, 2002 U.S. Dist. LEXIS 9578, 88 FEP Cases 1698 (D. Mass. 2002) (applying judicial estoppel where plaintiff failed to disclose pending sex harassment lawsuit to bankruptcy court — summary judgment for employer); *Lowry v. KTI*, 795 A.2d 80 (Me. 2002) (plaintiff's failure to inform the bankruptcy court of potential claims against his former employer barred suit against that same employer for defamation and other contract-based claims)

[6] 283 B.R. 22 (BAP 9th Cir. 2002).

[7] *New Hampshire v. Maine*, 532 U.S. 742, 750-51, 121 S. Ct. 1808 (2001) (declining to ''establish inflexible prerequisites or an exhaustive formula on the applicability of judicial estoppel'' because it is ''probably not reducible to any general formulation of principle'').

[8] *Hamilton v. State Farm Fire & Cas. Co.*, 270 F.3d 778, 784 (9th Cir. 2001) (filing suit against defendant for claims that were undisclosed in bankruptcy schedules constitutes assertion of inconsistent positions); *In re Coastal Plains Inc.*, 179 F.3d 197, 210 (5th Cir. 1999) (same).

[9] *Hamilton*, 270 F.3d at 784 (holding that discharge of debt constitutes judicial acceptance even if it is later vacated)

[10] *Donaldson v. Bernstein*, 104 F.3d 547, 555-56 (3rd Cir. 1997) (approval of debtor's reorganization plan satisfied judicial acceptance prong); *Coastal Plains*, 179 F.3d. at 210 (lifting a stay based on debtor's nondisclosure in schedules and in stipulation constituted judicial acceptance).

[11] *Total Petroleum Inc. v. Davis*, 822 F.2d 734, 737 n.6 (8th Cir. 1987) (because the purpose of judicial estoppel is to protect the integrity of the judicial process, it does not apply unless there was a ''knowing misrepresentation to'' or ''fraud on the court'').

[12] *Hamilton*, 270 F.3d at 784 (''Judicial estoppel will be imposed when the debtor has knowledge of enough facts to know that a potential cause of action exists during the pendency of the bankruptcy but fails to amend his schedules or disclosure statements to identify the cause of action as a contingent asset''); *Coastal Plains*, 179 F.3d at 210 (failure to disclose claim is only inadvertent if the debtor lacks knowledge or has no motive for concealment); *Burnes*, 291 F.3d. at 1287-88 (same).

[13] *Id.*

[14] *Coastal Plains*, 179 F.3d at 212 (debtor's lack of awareness of statutory duty to disclose claims not relevant to consideration of whether to impose judicial estoppel).

[15] *Kelsey v. Waste Management*, 76 Cal. App. 4th 590, 598 (1999).

  EDR ISSN 1072-1967

ments,[16] California courts have shown a reluctance to apply judicial estoppel in this context by broadly construing the intent element (*i.e.*, that the first position was not taken due to ''ignorance, fraud, or mistake''). Unlike the Ninth Circuit, which readily infers intent to circumvent the affirmative disclosure requirements of bankruptcy law, California courts have permitted nondisclosing debtors to avoid estoppel of their civil claims by asserting that they received mistaken legal advice regarding the worthlessness of claims[17] and by claiming ignorance of the bankruptcy disclosure requirements.[18]

While not completely foreclosing the application of judicial estoppel,[19] these California appellate courts reason, in *dicta*, that judicial estoppel would ''rarely [be] appropriate in a Chapter 7 context'' because the nondisclosing party could reopen the bankruptcy, reveal the undisclosed claims, and have them discharged or prosecuted by the trustee.[20] For these reasons, these California courts presume that ''[t]here is no possibility of unfair advantage,'' making judicial estoppel unnecessary.[21]

The seeming reluctance of California appellate courts to apply judicial estoppel in cases involving nondisclosing debtors ignores the purpose of the doctrine of judicial estoppel and erodes the integrity of the bankruptcy court.

Judicial estoppel protects the integrity of the judicial process by preserving the sanctity of litigants' oaths and preventing parties from changing positions based on the exigencies of the moment.[22] The doctrine, applied strictly, will deter the abuse of judicial resources for personal gain.

California courts that allow litigants to reopen bankruptcy cases to cure nondisclosure reason that strict application of judicial estoppel can ''frustrate the primary objectives of bankruptcy law'' because it unfairly penalizes the creditors by preventing the equitable distribution of assets.[23]

These courts believe that if the case is reopened, the bankruptcy court can ''take appropriate action to promote bankruptcy goals and protect the bankruptcy court's process.'' This belief, however, is misplaced.

First, judicial estoppel is intended as a tool for the *second* tribunal to ''protect *itself* against manipulation.''[24] By focusing narrowly on the function of the *bankruptcy* process, California courts have diminished the more important consideration that the litigant has been dishonest with the *civil* court.

Second, while courts have excused their refusal to apply judicial estoppel as promoting the objectives of bankruptcy, the truth is that this judicial refusal only erodes the process.

Practical Considerations in California. Because federal courts in California are more apt to bar undisclosed civil claims, the importance of forum is crucial. This is especially true because the Ninth Circuit holds that federal law concerning judicial estoppel governs its application to state law claims litigated in federal court.[25]

Because application of the doctrine requires the consideration of factual issues, a motion for summary judgment, not a demurrer, is the appropriate vehicle to address an opposing party's failure to disclose claims in bankruptcy. Issues of judicial estoppel also can be raised in motions in limine to exclude evidence or limit damages.

To determine if judicial estoppel is appropriate, the bankruptcy files of the plaintiff should be examined carefully. This examination would include both the disclosure statements and the transcript of the bankruptcy's 341-A hearing. Because some courts require a showing of bad faith beyond the mere failure to disclose potential assets, discovery should be conducted to establish evidence of intent. This would include conducting discovery to determine if the plaintiff failed to disclose, or discounted, other assets during the bankruptcy.

Conclusion. California courts should do more to hold plaintiffs accountable when their bankruptcy filings fail to disclose, or undervalue, their employment claims. Employers should examine the plaintiff's bankruptcy records in all employment discrimination cases. When fraud is discovered, the employer should move to dismiss the claim on the basis that plaintiff is judicially estopped from pursuing the claim or from seeking more than the value of the claim listed in the asset schedules.

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[16] *Id.* at 598-99 (evidence that plaintiff/debtor had bankruptcy plan confirmed without disclosing potential discrimination claim established all elements of affirmative defense except for the intent element — i.e., whether first position was taken due to ignorance, fraud, or mistake.)

[17] *Haley v. Dow Lewis Motors Inc.*, 72 Cal. App. 4th 497, 502 (1999) (refusing to apply judicial estoppel based on debtors/plaintiffs' assertion that they did not disclose claims because of legal advice that the claims were worthless).

[18] *Kelsey*, 76 Cal. App. 4th at 516 (represented party not judicially estopped despite failing to disclose claim because he was unaware of any obligation to do so); *see also Cloud v. Northrup Gruman Corp.*, 67 Cal. App. 4th 995, 1020-2 (1998) (nondisclosing debtor/plaintiff did not have standing to prosecute employment claim but should be allowed leave to amend to add the bankruptcy trustee as the real party-in-interest).

[19] *Cloud*, 67 Cal. App. 4th at 1010-11 (recognizing, under the holding of *Coates v. K-Mart Corp.*, 215 Cal. App. 3d 961 (1989), that a plaintiff who lacked standing and made ''knowing misrepresentations to the defendant and the court'' may be barred from amending her complaint to add the real party-in-interest).

[20] *Haley*, 72 Cal. App. 4th at 511(1999) (''we share the view of *Cloud* that judicial estoppel is rarely appropriate in a Chapter 7 context in a case in which the debtor has failed to schedule a claim.'')

[21] *Id.*

[22] *New Hampshire*, 532 U.S. at 749-50.

[23] *Cloud*, 67 Cal. App. 4th at 1020.

[24] *Rissetto v. Plumbers & Steamfitters Local 343*, 94 F.3d 597, 603-04 (9th Cir. 1996)

[25] *Id.*, 94 F.3d at 603 (applied federal law on judicial estoppel in FEHA case—''federal law governs the application of judicial estoppel in federal court'').