

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

In re:

Floyd and Linda Ruggles, BKY No. 93-33827

Debtor.

ORDER

This matter came before the Court on December 4, 1997 for Evidentiary Hearing based on the Debtors' objection to the Order Directing Debtor to Surrender Property dated August 5, 1997. Appearances are as noted on the record. This ORDER is entered pursuant to the Federal and Local Rules of Bankruptcy Procedure.

I.
FACTS

On August 5, 1993, Floyd and Linda Ruggles filed for bankruptcy under 11 U.S.C. Chapter 7. Michael Iannacone was appointed trustee. The Debtors filed Schedule B, the schedule of all personal property, as required. The Debtors did not amend Schedule B during the pendency of their bankruptcy. On August 23, 1994, the Trustee filed a Notice of Sale, Abandonment, Lease or Settlement abandoning certain items listed in Debtors' Schedule B, including a legal malpractice action. The Court entered an order dated October 28, 1994 approving the abandonment. The case was closed on August 19, 1996.

On April 22, 1997, the Trustee file an Application to Reopen Case, which was approved by the Court on April 25, 1997. The basis asserted for reopening the case was the Debtors' failure to schedule a legal malpractice claim against Bruce Kennedy which resulted in a \$20,000 settlement. The Trustee asserted the settlement proceeds were property of the Debtors' bankruptcy estate. No dispute exists that the claim against Kennedy arose pre-petition.

Based on the Trustee's application, on August 5, 1997, the Court entered an Order Directing Debtors to Surrender Property. The Order required the Debtors to surrender the following property: "\$20,000 representing amount recovered in a lawsuit against Bruce Kennedy". Due to clerical error, the Order was not served until October 30, 1997. The Debtors filed their objection to the turnover on November 10, 1997, and seek vacation of the order.

II.

DISCUSSION

The issue presented is whether the Trustee abandoned the legal malpractice claim against Bruce Kennedy. The Debtor takes the following alternative positions: that the claim was abandoned by the Trustee's Notice of Sale, Abandonment, Lease or Settlement dated August 23, 1994; that the claim was abandoned by the Trustee through closure of the case; that equitable estoppel applies to prevent the Trustee from asserting an interest in the claim; and, collateral estoppel prevents the Trustee from asserting any rights in the claim.

The Trustee asserts that the legal malpractice action against Kennedy was never disclosed in Schedule B nor did he have any knowledge of the claim; therefore, the asset was not abandoned and is property of the bankruptcy estate pursuant to 11 U.S.C. Section 554(d).(1F)

A trustee may abandon property of the estate in accordance with 11 U.S.C. Section 554(a) which provides:

After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate.

The general rule is that once property of the estate has been abandoned by the trustee, it is no longer property of the estate and beyond the control of the trustee. In re Sutton, 10 B.R. 737, 739 (Bankr.E.D. Virg. 1981); In re Byrson, 53 B.R. 3, 4 (Bankr.M.D. Tenn. 1985). This rule applies regardless of whether it is later discovered that the property abandoned has greater value than believed at the time of the abandonment. In re Sutton, 10 B.R. at 740. There are two exceptions to this general rule. The first is when property has actually been concealed from the trustee by the Debtor. Id.; In re Byrson, 53 B.R. at 5. The second is when the property was unscheduled by the debtor, preventing the trustee from having knowledge of its existence.(2F) In re Sutton, 10 B.R. at 740; In re Byrson, 53 B.R. at 4. The Trustee has not alleged that the claim was actually concealed by the Debtors, so the issue is whether the property was scheduled by the Debtors and abandoned by the Trustee.

A. ABANDONMENT

1. Abandonment Through Notice

The Debtors assert the Trustee's Notice of Sale, Abandonment, Lease or Settlement dated August 23, 1994 included an abandonment of the Kennedy malpractice claim. The Notice provided:

On 20 days after mailing, or as soon thereafter as the transaction may be

completed, the undersigned trustee of the estate of the debtors named above will abandon property as follows:

5. The items listed under item 20, Debtors' Schedule B described as "unliquidated claims for back rent, damage to property, note receivable and tort damages to property totalling (sic) \$890,832.35. \$415,000 are represented by four claims alleging negligence, wrongful taking, legal malpractice for insurance agent negligence and the debtors have been unsuccessful in obtaining counsel to pursue any of these claims. . .

Based on the above quoted language, the claim against Kennedy must have been scheduled in Schedule B in order to have been abandoned through the Notice.

11 U.S.C. Section 521(1) requires the Debtor to file a schedule of assets and liabilities. The Debtors filed Schedule B, including an attachment expanding on item 20 of Schedule B.(3F) The attachment lists:

2. David Lawson, Attorney- legal malpractice
[amount claimed owed to debtors] in excess of 50,000

The Debtors assert that the above disclosure put the Trustee on notice of the legal malpractice claim against Kennedy. It is their position that the above description is sufficient to include the universe of legal malpractice claims against any attorney.

Merely listing the name of a specific attorney and a claim for "legal malpractice" is not sufficient to include the universe of legal malpractice claims against all possible attorneys, especially attorneys of another firm. The disclosure in no way reveals anything more than a single legal malpractice claim against Lawson, and failed to put the Trustee on notice of the legal malpractice claim against Kennedy.

Additionally, the Debtors argue that the state court case against Kennedy and Lawson was a single joint cause of action against both attorneys and therefore, was properly disclosed on the schedules. The Trustee asserts that the state case involved two separate claims which could have been filed as two separate cases, making disclosure insufficient. Examination of the Hennepin County State Court Complaint does not support the Debtors' position. Kennedy and Lawson were not members of the same firm. The Complaint pleads a legal malpractice claim against two attorneys individually. Nothing in the complaint

appears to require the parties be joined pursuant to Minn.R.Civ.P 19.01.(4F) It appears that the parties were permissively joined under Minn.R.Civ. P. 20.01.(5F) Therefore, the argument that involved was a single "action" fails.

2. Abandonment Through Closure

The Debtors argue that the Trustee abandoned the claim against Kennedy through closing the case pursuant to 11 U.S.C. Section 554(c). 11 U.S.C. Section 554(c) provides:

Unless the court orders otherwise, any property scheduled under section 521(1) of this title not otherwise administered at the time of the closing of a case is abandoned to the debtor and administered for purposes of section 350 of this title. (emphasis added)

The quoted language makes it clear that the property needs to be scheduled in order to be abandoned by the trustee through the closing of the case. As it has already been determined that the claim was not scheduled, the claim could not have been abandoned through closure.

B. ESTOPPEL

1. Equitable Estoppel

The Debtors argue that equitable estoppel prevents the Trustee from asserting a claim over the settlement proceeds, arguing that the Trustee had knowledge, outside the schedules, of the legal malpractice claim against Kennedy. In support of their position, the Debtors assert that a February 26, 1996 letter from David Lawson to the Trustee put the Trustee on notice of the claim against Kennedy. However, the letter never mentions Kennedy, nor does it give any indication that the Debtors had a claim against any attorney besides Lawson. The letter alone could not have put the Trustee on notice of the claim against Kennedy.

The Debtors further assert that the Trustee's responsive letter dated March 8, 1996, shows the Trustee had knowledge of the claim against Kennedy. The following reference is made to Kennedy in the caption of the letter:

Re: Ruggles v. Kennedy & Lawson
Bankruptcy 93-33827
Your File: 6038

The Trustee explained that he took the name "Kennedy" from the state court complaint he received as an attachment to the February 26, 1996 letter from Lawson. In the Trustee's responsive letter he states that he has:

review[ed] all the documentation in the file and find that the tort claim which

is the subject matter of the litigation referenced above [Ruggles v. Kennedy & Lawson] was abandoned by me on August 22, 1994. . . Accordingly, the estate has no interest in this litigation. Debtors' Exhibit F.

Debtors believe that this letter proves both that: the Trustee had knowledge of the claim against Kennedy; and, the Trustee knowingly abandoned it. The letter standing alone does not support either conclusion. As any knowledge the Trustee may have possessed about the Kennedy claim came from the complaint, an examination of the complaint is necessary.

The state court complaint, the Debtors also argue, provided the Trustee with knowledge of the claim against Kennedy. The Trustee testified that he read the complaint. However, he believed Kennedy and Lawson were from the same firm, and asserts there was nothing in the complaint to call his attention to the fact they were not part of the same firm at the time of the events giving rise to the cause of action. The complaint did not state that Kennedy and Lawson were employed at separate firms at the time of the occurrences giving rise to the complaint. Therefore, the complaint was not sufficient notice to the Trustee of the separate claim against Kennedy.

Additionally, the Debtors assert that the failure to disclose the claim against Kennedy did not harm the estate, as the Trustee would have abandoned the claim. The Trustee does not dispute that he would have abandoned the claim had it been properly scheduled. Debtor Floyd Ruggles testified that he was not aware of a claim against Kennedy when he filed his schedules, but became aware of the claim before the close of the case. The Debtors never amended the schedules to separately list the claim of Kennedy, even though they were under a duty to modify their schedules to list any property interests they failed to schedule. As the Debtors failed to comply with their duty, they are bound to the consequences of their non-disclosure, regardless of whether the Trustee would have abandoned the property.

2. Collateral Estoppel

The Debtors argue that the "same issue" was presented to the Hennepin State Court Judge, and this Court should be bound to that holding. This argument was made during the evidentiary hearing, but was not briefed and not actively pursued by the Debtors. Further, the holding of the state court which was argued to collaterally estop this Court, was never offered into evidence. Additionally, the Trustee was never a party to the state court action. The collateral estoppel argument is without merit.

III.
DISPOSITION

Based on the forgoing analysis the Court finds that the claim against Kennedy was not scheduled, and not abandoned by the trustee. Therefore, the claim is property of the bankruptcy estate pursuant to 11 U.S.C. Section 554(d).(6F)

IT IS HEREBY ORDERED THAT:

1. The Kennedy legal malpractice claim is property of the bankruptcy estate; and,
2. Debtors' Motion to Vacate the August 5, 1997 Order requiring the turnover of settlement proceeds is DENIED.

Dated: February 19, 1998

By the Court:

Dennis D. O'Brien
Chief United
States Bankruptcy
Judge

(1F). Section 554(d) provides:

Unless the court orders otherwise, property of the estate that is not abandoned under this section and that is not administered in the case remains property of the estate.

(2F). Case law has classified this as an "exception" to the rule that abandonment is irrevocable.

Actually, property not scheduled is not abandoned and remains property of the estate under 11 U.S.C. Section 554. Therefore, the issue is whether there was an abandonment, not whether a revocation of abandonment is proper.

(3F). Item 20 is where "other contingent and unliquidated claims of every nature, including tax refunds, counterclaims of the debtor, and rights to set off claims" are to be listed. Described by the Debtors in item 20 is "unliquidated claims for back rent, damage to property, notes receivable and tort damage to property" in the amount of \$890,832.35.

(4F). Rule 19.01. Persons to be Joined if Feasible

A person who is subject to service of process shall be joined as a party in the action if (a) in the person's absence complete relief cannot be accorded among those already parties, or (b) the person claims an interest relating to the subject of the action and is so situated that the disposition of the action in the person's absence may (1) as a practical matter impair or impede the person's ability to protect that interest or (2) leave any one already a party subject to a substantial risk or incurring double, multiple, or otherwise inconsistent obligations by reason of the person's claimed interest. If the person has not been so joined, the court shall order that the

person be made a party. If the person should join as a plaintiff but refuses to do so, the person may be made a defendant, or, in a proper case, an involuntary plaintiff.
(5F). Rule 20.01. Permissive Joinder

All persons may join in one action as plaintiffs if they assert any right to relief, jointly, severally, or in the alternative with respect to or arising out of the same transaction, occurrence, or series of transactions or occurrences and if any question of fact or law common to all these persons will arise in the action. All persons may be joined in one action as defendants if there is asserted against them jointly, severally, or in the alternative, any right to relief with respect to or arising out of the same transaction, occurrence, or series of transactions or occurrences and if any question of law or fact common to all defendants will arise in the action. A plaintiff or defendant need not be interested in obtaining or defending against all the relief demanded. Judgment may be given for one or more of the plaintiffs according to their respective rights to relief, and against one or more defendants according to their respective liabilities.

(6F). At the hearing, the Debtors argued that Linda Ruggles should not be a party to this action, based on a state court order. The state court order was never offered into evidence. Further, the removal of Linda Ruggles was never briefed nor mentioned before closing arguments. In view of the foregoing, Linda Ruggles is not dismissed from this proceeding.