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A LOOK AT HOW THE DOCTRINE OF JUDICIAL ESTOPPEL HAS EVOLVED INTO AN EFFECTIVE COUNTER-ATTACK FOR SERVICERS

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While default rates across the country have significantly decreased, there remains a deluge of litigation brought against servicers. Contested foreclosures initiated by borrowers are often colorful, and take on a variety of forms depending on the jurisdiction. Borrowers' efforts to stop foreclosure or delay proceedings indefinitely may include filing a counter-claim in a judicial proceeding or filing separate action alleging wrongful foreclosure and requesting injunctive relief. These claims often follow trends specific to the jurisdiction, and include alleged statutory violations, standing or document issues, or some other type of servicer misconduct or omission.

Many of these lawsuits lack merit, and are brought primarily to delay proceedings. In many of these cases, the borrowers are significantly in default on their loan, and there may even be an element of bad faith, particularly in cases where the relief requested is not commensurate with the actual violation. For example, a defect in the origination documents should not excuse a failure to make mortgage payments. However, many judges are reluctant to dispose of borrowers' claims, frivolous or not, too quickly. The end result is increased costs to servicers and delayed foreclosures.

While the mortgage industry has been forced to ride the wave of anti-creditor sentiment, many pragmatic judges have caught on quickly to situations where borrowers have tried to take advantage of technical irregularities notwithstanding admissions that they borrowed money. The doctrine of Judicial Estoppel is becoming a growing area of protection for servicers with many courts adopting a hard line approach in any case where it appears a party is playing 'fast and loose with the courts.' This article will briefly explore the evolution of Judicial Estoppel, look at some favorable case law applying the doc-

trine, and offer some practical ways for servicers to utilize this defense effectively.

WHAT IS JUDICIAL ESTOPPEL?

Simply, Judicial Estoppel is a judge made rule designed to protect the integrity of the judicial system by prohibiting parties from taking inconsistent posi-tions in court. The court in *New Hampshire v. Maine*, U.S. 742 749 (2001), set the standard by reinforcing that a party that assumes a certain position in a pri-or legal proceeding may not take a contrary position simply because his interests have changed. The court looked at three general factors:

1. A party's later position must be clearly inconsistent with its earlier position.
2. Courts will inquire about 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 the second court was misled.
3. Does the party seeking to assert an inconsistent position derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped? Id.

In practical terms, Judicial Estoppel is often a valuable defense for servicers in cases where a borrower contests foreclosure after filing bankruptcy. Bankruptcy schedules must be acknowledged under oath, and Borrowers typically give sworn testimony at the designated 341 meeting set by the bankruptcy Trustee. Failure by a Borrower to disclose any claims of wrongful foreclosure while the bankruptcy is pending often provides a defense for a servicer if such claims existed while the bankruptcy was pending, and are brought up at a later date.

RECENT DECISIONS APPLYING JUDICIAL ESTOPPEL

One common denominator for judges applying Judi-cial Estoppel is a common sense approach taken in these cases aimed at fairness. In *Knigge v. Sun Trust Mortgage, Inc.* (In re Knigge), 479 B.R. 500 (8th Cir. 2012), the 8th Circuit upheld the court's ruling grant-ing summary judgment to Sun Trust Mortgage, and rejected borrowers' claims that the lender lacked standing to bring the lawsuit. The court was deeply troubled by "gotcha" litigation--where borrowers play along with a lender in the early part of a bankruptcy when it suits their purpose, but then try to invalidate a lender's security interest when it becomes prob-lematic or burdensome. In this case, borrowers had previously acknowledged the validity of the lender's secured claim when they entered into two separate consent orders, agreeing in both cases to cure arrear-age owed to the lender. These prior actions estopped borrowers from bringing later claims to invalidate Sun Trust's lien. As the court aptly stated, Judicial Estoppel is designed to prevent a party from playing 'fast and loose with the courts.'

The 10th circuit took a similar stance by ruling in favor of a lender sued for violations of the Fair Debt Collection Practices Act. In B*arker v. Asset Accep-tance, LLC*, 874 F. Supp.2d 1062 (D. Kan. 2012), the court granted lender's motion for summary judg-ment relying on Judicial Estoppel in its determina-tion. The factor that weighed most heavily on the court was borrower's failure to disclose the lawsuit in his bankruptcy schedule, or otherwise indicate the lawsuit existed until after the Motion for Sum-mary Judgment was filed. The court rejected borrower's attempts to reopen the bankruptcy to dis-close the claim after the Motion for Summary Judg-ment was filed.

More recently, the 11th Circuit Court of Appeals ruled in *Failla v. CitiBank, N.A.*, 838 F.3d 1170 (11th Cir. 2016), that borrowers who file a statement of intention to surrender property in bankruptcy are estopped from later contesting a foreclosure action. The Failla court went even further by holding that bankruptcy courts have broad power and authority to sanction viola-tions for misconduct and dishonesty. A bankruptcy court can order borrowers who surrender property to drop their opposition to foreclosure in state court. If the facts are egregious enough, the bankruptcy court can sanction borrowers who lie about their intent to surrender the property.

Similarly, another Florida court denounced borrow-ers' assertion of affirmative defenses and prosecution of a foreclosure counterclaim as inconsistent with the Chapter 13 Plan providing "surrender" of the property, and a violation of the Confirmation Order. See *In re Lapeyre*, 544 B.R. 719 (D. Florida 2016). The Lapeyre court reaffirmed that bankruptcy courts may lack jurisdiction to tell state courts what to do, but a court can exercise its jurisdiction by telling parties what they can and cannot do in a non-bankruptcy forum. Simply stated, these courts did not permit borrowers to take inconsistent positions to the detriment of the lender.

The 9th Circuit appears to take a more narrow approach in applying the doctrine. Specifically, In A*h Quin v County of Kauai Dept. of Transportation*, 733 F.3d 267 (9th Cir. 2013), the court held that if a debtor seeks to reopen the bankruptcy proceeding, the court must examine the subjective intent at the time debtor completed the bankruptcy schedules to determine whether Judicial Estoppel applies. Failure to disclose a lawsuit in a bankruptcy schedule due to "mistake" or "inadvertence" might be excusable in the 9th circuit if the borrower can show that the omission was an accident or inadvertent.

PRACTICAL SUGGESTIONS FOR SERVICERS

Litigation often involves trying to gain an upper hand over your opponent, but Judicial Estoppel reminds us that borrowers cannot have their cake and eat it too. Courts are generally wary to reward inconsistency and have little tolerance for parties changing positions to gain an unfair advantage. Here are a few suggestions for servicers in a position to utilize Judicial Estoppel as a defense.

First, remember that a prior bankruptcy may preclude borrowers from bringing claims contesting the foreclosure at a later date. Under 11 U.S.C § 521(1) of the Bankruptcy Code, a debtor is required to file a "schedule of assets and liabilities…..and a statement of the debtor's financial affairs." In simple terms, this means that borrowers filing bankruptcy have a duty to file under oath a complete an accurate schedule of assets with the court. Failure to do so could have significant consequences including denial of discharge under 11 U.S.C. 727 or loss of any interest in the concealed asset.

Therefore, servicer's counsel should take great care in reviewing prior bankruptcy proceedings in situations where borrowers have brought subsequent litigation contesting the foreclosure. Lenders have a strong argument that any claims of wrongful foreclosure that exist at the time of the bankruptcy must be disclosed by borrowers on their bankruptcy schedules. Failure to disclose these claims could invoke the doctrine of Judicial Estoppel and prohibit borrowers from filing a lawsuit at a later date.

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Servicers should also be mindful of the importance of the debtor examination required under 11 U.S. Code §341. The purpose of the creditor meeting is to allow the trustee to verify the accuracy of the bankruptcy petition and schedules. From an evidentiary standpoint, valuable information may be gleaned from borrowers' testimony at the creditors meeting. The trustee may ask questions about the loan and security instrument, and confirm whether the loan is delinquent.

Borrowers' failure to disclose concerns or claims concerning the mortgage at the creditors meeting such as perfection issues or the servicer's standing to file a lawsuit may judicially estop borrowers from raising these issues at a later date. Moreover, depending on the jurisdiction, transcripts are often easily obtainable for years after a bankruptcy filing. Reviewing prior pleadings, consent orders, and transcripts may estop borrowers from bringing later claims contesting foreclosures and are effective methods that aid in resolution of contested matters more quickly.