United States Bankruptcy Court
Northern District of Illinois
Eastern Division

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Bankruptcy Caption: In re Vence L. Jackson and Lue E. Jackson

Bankruptcy No. 98 B 15483

Adversary Caption: N/A

Adversary No. N/A

Date of Issuance: September 9, 1999

Judge: John H. Squires

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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

IN RE:	)	
VENCE L. JACKSON and	)	Chapter 13
LUE E. JACKSON,	)	Bankruptcy No. 98 B 15483
	)	Judge John H. Squires
Debtors.	)	

MEMORANDUM OPINION

______This matter comes before the Court pursuant to a Memorandum Opinion and Order from the United States District Court for the Northern District of Illinois (Honorable Suzanne B. Conlon) dated August 20, 1999, which remanded this matter for written findings on the Court's Order dated March 24, 1999. The March 24, 1999 Order granted in part and denied in part the amended motion of Sears, Roebuck & Co. ("Sears") for relief from the automatic stay. The March 24, 1999 Order denied Sears' request to file a counterclaim in a civil lawsuit pending in the District Court brought against it by Lue E. Jackson ("the Debtor") and to recover the unpaid claim owed it by the Debtor, but allowed Sears to file any affirmative defenses in that lawsuit. The following findings of fact and conclusions of law are made pursuant to the District Court's remand Order.

I. JURISDICTION AND PROCEDURE

The Court has jurisdiction to entertain this matter pursuant to 28 U.S.C. § 1334 and Internal Operating Procedure 15(a), formerly known as General Rule 2.33(A), of the United States District Court for the Northern District of Illinois. This matter is a core proceeding

under 28 U.S.C. § 157(b)(2)(G).

II. FACTS AND BACKGROUND

On May 18, 1998, the Debtor and her spouse filed a voluntary Chapter 13 petition accompanied by a Plan, Schedules of assets (totaling $116,775.00) and liabilities (totaling $126,525.00) and a Statement of Financial Affairs. Sears was listed on the Schedule F as the holder of an unsecured non-priority claim regarding a credit card debt in the sum of $1,100.00. The Plan proposed to pay the Chapter 13 Standing Trustee the sum of $650.00 per month for sixty months. From this amount all allowed priority claims would be paid in full; secured creditors would be paid 100% or the value of their security; and unsecured non-priority claims would receive 70% of their allowed claims pro rata. Tardily filed claims would receive nothing under the Plan.

On June 19, 1998, the Debtors filed amended Schedules B and C, which listed and claimed exempt under 735 ILCS 5/12-1001(b), a "potential claim against Abacus Financial Management Services and possible related persons under the Fair Debt Collection Practices Act and possibly state laws for engaging in deceptive debt collection practices. The maximum relief to which the debtor is entitled is $1,000 per case. . . . The value of the claim is speculative at present as defendant is expected to contest it." Abacus is a debt collector retained by Sears. The amended Schedules did not name Sears as a defendant.

On June 26, 1998, the Chapter 13 Standing Trustee served notice of: (1) the meeting of creditors under 11 U.S.C. § 341; (2) the confirmation hearing scheduled for August 5, 1998; (3) the deadline for filing claims pursuant to Federal Rule of Bankruptcy Procedure 3002; and (4) a plan summary. Sears was duly served at its address of record. The Chapter

13 Standing Trustee also served an amended notice of the claims bar date to all parties in interest, including Sears, advising that all general unsecured claims were to be filed by September 30, 1998.

The Court confirmed the Plan on the recommendation of the Chapter 13 Standing Trustee in the absence of any objections from any party in interest. It is undisputed that Sears received the above notices, but opted not to file any proof of claim prior to the expiration of the claims bar date. The Debtor waited until after the bar date before suing Sears, asserting for the first time a Fair Debt Collection Practices Act ("FDCPA") claim against Sears, which was not previously disclosed in any papers filed with this Court.

On February 1, 1999, Sears filed its original motion for relief from the automatic stay "to file a compulsory counterclaim against the Debtor regarding all matters arising from or relating to the unpaid and overdue debt owed by the Debtor to Sears in relation to a Sears charge card." The motion alleged that she had filed a lawsuit against Sears and others alleging violations of the FDCPA. The motion requested relief from the automatic stay to "repossess, foreclose upon and otherwise exercise its contractual and statutory rights with respect to all claims arising from the unpaid and overdue debt owed by the Debtor to Sears, and . . . granting such other and further relief as the Court deems just and proper." With the consent of counsel and consistent with 11 U.S.C. § 362(e), the Court set the matter for preliminary hearing on March 24, 1999. Sears filed an amended motion on February12, 1999, in which it cited no additional supporting authority or other grounds for relief.

Sears argues that the Debtor's claimed cause of action against it was not specifically listed among her scheduled assets and that she waited until after the claims bar date had run

before filing the District Court action, which is based on alleged pre-petition wrongful conduct by Sears. Thus, Sears seeks to assert counterclaims sounding in recoupment and set off. Sears contends that no harm will result to the estate or the Debtor because the Debtor has conceded that her FDCPA claim against Sears is limited to statutory damages of $1,000.00, which, if recovered, was not income included or anticipated anywhere in her Plan or Schedules. The prejudice to Sears is that it would be precluded from fully defending itself without being able to assert all available defenses. Sears points out that it would be willing to limit its recovery on its counterclaim to the amount recovered individually by the Debtor in order to allay the concerns that the confirmed Plan could be threatened by Sears' defense and counterclaims. Sears further asserts that it is likely to prevail on the merits of its counterclaim and that the District Court would likely accept ancillary jurisdiction over that issue.

At the hearing, neither party sought to file any additional papers or introduce any evidence. Rather, both parties stood on their respective pleadings and made supplemental oral arguments. The parties' points and arguments were weighed and considered by the Court. In making its abbreviated oral findings and conclusions, the Court did not articulate the full extent and rationale upon which it made its ruling. Thus, the oral ruling is hereby supplemented as directed by the remand Order.

III. APPLICABLE STANDARDS

Section 362(d) of the Bankruptcy Code provides two grounds under which relief from the automatic stay can be granted. In re 8th Street Village Ltd. Partnership, 88 B.R. 853, 855

(Bankr. N.D. Ill.), aff'd, 94 B.R. 993 (N.D. Ill. 1988). The first ground is cause, including lack of adequate protection. 11 U.S.C. § 362(d)(1). The authoritative treatises collect a legion of cases in which cause has been found to modify the automatic stay to allow litigation to be completed on its merits in other forums, including federal district court proceedings. See generally, 1 D. Epstein, S. Nickles and J. White, Bankruptcy § 3-30 at 309 n.4 (1992); 1 R. Ginsberg and R. Martin, Ginsberg & Martin on Bankruptcy § 3.05F at 3-66 n.342 (4th ed. 1999); 2 W. Norton, Jr., Norton Bankruptcy Law and Practice 2d § 36:34 at 36-77 (1997). The second ground is that the debtor does not have any equity in the property and the property is not necessary to an effective reorganization. 11 U.S.C. § 362(d)(2). Sears requested relief under the first ground.

"Cause" as utilized in § 362(d) "'has no clear definition and is determined on a case-by-case basis.'" In re Fernstrom Storage and Van Co., 938 F.2d 731, 735 (7th Cir. 1991) (quoting In re Tucson Estates, 912 F.2d 1162, 1166 (9th Cir. 1990)) (citations omitted). The Seventh Circuit adopted a three part test for determining whether "cause" exists to lift the automatic stay so that a creditor can maintain an action against the debtor: (1) any great prejudice to either the bankrupt estate or the debtor will result from continuation of the civil suit, (2) the hardship to the creditor by maintenance of the stay considerably outweighs the hardship of the debtor, and (3) the creditor has a probability of prevailing on the merits. Id.

The decision to lift the automatic stay pursuant to § 362(d) is committed to the discretion of the bankruptcy court and the decision may be overturned only upon a showing of abuse of discretion. In re Boomgarden, 780 F.2d 657, 660 (7th Cir. 1985); In re Holtkamp, 669 F.2d 505, 507 (7th Cir. 1982) (citation omitted). "Hearings to determine whether the stay

should be lifted are meant to be summary in character." In re Vitreous Steel Prods. Co., 911 F.2d 1223, 1232 (7th Cir. 1990).

IV. DISCUSSION

On March 24, 1999, the Court denied the motion to modify the automatic stay to allow Sears to file a counterclaim against the Debtor in the District Court action. The Court, however, did modify the automatic stay to allow Sears to plead by way of an affirmative defense the unpaid balance of its claim against the Debtor. The Court considered and briefly discussed the three Fernstrom factors. First, the Court noted that there would be no prejudice to the bankruptcy estate or the Debtor to allow modification of the automatic stay for the purpose of allowing Sears to assert by way of affirmative defense the unpaid claim Sears has against the Debtor. The Court further noted that the hardship to Sears was not great if the stay was only modified to allow it to assert the unpaid credit card bill as an affirmative defense. The Court also held that it had no way of predicting the outcome of the District Court litigation so that the final factor regarding the creditor's probability of prevailing on the merits of that litigation was even.

The District Court remanded this matter to this Court for written findings and an amplified rationale for its ruling. Accordingly, the Court will further articulate its reasons and rationale behind the March 24, 1999 Order. In retrospect, the Court could have done this at the outset with the attendant delay, but this motion was one of over 140 matters on the Court's calendar that morning and the parties sought no further hearing. Rather, they rested on their papers and oral arguments. Moreover, pursuant to Vitreous Steel, the hearing on

motions for relief from the stay are summary in nature. 911 F.2d at 1232.

A. Prejudice to the Debtor or the Estate

The Court found that to allow Sears to assert its claim for the unpaid balance owed it from the Debtor by way of an affirmative defense in the District Court litigation would not unfairly prejudice the Debtor. That is because under Federal Rule of Bankruptcy Procedure 7008(c) and Federal Rule of Civil Procedure 8(c), an affirmative defense does not seek any affirmative relief. It is purely a pleading defensively asserted wherein the party asserting it seeks no additional relief against the plaintiff other than to defeat the plaintiff's claim. If an affirmative defense is not pleaded, it is waived to the extent that the party who should have pleaded it may not introduce evidence in support thereof. See Brunswick Leasing Corp. v. Wisconsin Cent., Ltd., 136 F.3d 521, 530 (7th Cir. 1998) (citation omitted); Bank Leumi Le-Israel, B.M. v. Lee, 928 F.2d 232, 235 (7th Cir. 1991).

The Court found, however, that to allow Sears to assert a counterclaim in the District Court litigation might prejudice the Debtor or adversely impact her performance under the Plan. The Court notes that it was not provided with a copy of the proposed counterclaim Sears was seeking to file. Thus, it was difficult for the Court to more precisely evaluate the prejudice to the Debtor.

It is one thing to allow Sears to assert an affirmative defense, but another to allow it to assert a counterclaim, potentially amendable to seek other relief against the Debtor. A counterclaim includes both set off and recoupment, but is broader in that it includes other claims and may be used as the basis for affirmative relief. See 3 J. Moore, Moore's Federal Practice § 13.90[1] at 13-78 (3d ed. 1999). To allow Sears to file a counterclaim would

allow it to later seek an amount or relief exceeding the recovery sought by the Debtor. Thus, there would be resulting prejudice to the Debtor and/or her other creditors because that could adversely affect Plan consummation and payments to the other creditors, not merely diminish or defeat the Debtor's claim. The prejudice to the Debtor is that if Sears' counterclaim is sustained on the merits, the Debtor loses her $1,000.00 FDCPA statutory recovery. If the Court allows Sears to proceed on its counterclaim against the Debtor, which could include unknown affirmative relief against her, it could disrupt the Plan payments to the detriment of the Debtor and the estate's creditors who timely filed allowed claims and are receiving Plan payments. If Sears were allowed to successfully assert any counterclaim and recover affirmative relief against the Debtor, it would effectively end run around the bar date of Bankruptcy Rule 3002 and possibly undermine the finality of the confirmation order via 11 U.S.C. § 1327.

Contrary to the Debtor's argument, the doctrine of res judicata is inapplicable, as Sears correctly argues, because there was no prior litigation between the parties and the merits of the Debtor's unscheduled claim against Sears was not before the Court at the time of confirmation of the Plan. See Strong v. United States (In re Strong), 203 B.R. 105, 114 (Bankr. N.D. Ill. 1996).

B. Prejudice to Sears

In a footnote in its reply to the motion to lift the stay, Sears agreed to limit its relief under the counterclaim to the extent of any recovery made by the Debtor against Sears. Based on this statement, the prejudice to Sears then is nil if it is allowed to assert any and all affirmative defenses to the Debtor's claim. A counterclaim, which Sears could easily seek

to amend in the District Court litigation, might seek additional affirmative relief that could upset the Plan payments and give Sears unfair advantage over the other creditors. An affirmative defense, on the other hand, will only allow Sears to set off or recoup its $1,100.00 undisputed claim against the Debtor's statutory claim of $1,000.00 against it. If not allowed to assert its defense of set off or recoupment, the prejudice to Sears would be the maximum statutory recovery of $1,000.00 if the Debtor prevails, plus taxable costs and any allowed attorney's fees in unknown amounts under FDCPA.

C. <u>Sears' Probability of Prevailing on the Merits</u>

With respect to modifying the automatic stay to allow Sears to file its affirmative defense, the Court notes that the Debtor scheduled Sears' claim as undisputed and for a liquidated sum. Hence, the Debtor admitted that she owed the debt to Sears. There was no indication anywhere that she disputed the claim. The Court notes that 11 U.S.C. § 553 generally preserves pre-petition set off rights of creditors regarding mutual debts with debtors. Accordingly, Sears' probability of prevailing on the merits of an affirmative defense such as set off or recoupment is likely, if these are viable defenses for purposes of FDCPA.

Unfortunately, however, the Court was unable to adequately evaluate the likelihood of Sears' success on the merits of its counterclaim because Sears never provided the Court a copy of the proposed counterclaim and the parties did not adequately address whether set off or recoupment are or are not valid defenses under FDCPA. Thus, the Court had a limited record before it and could not adequately make that determination.

Moreover, the Court holds the view that the bankruptcy court lacks subject matter jurisdiction via 28 U.S.C. § 1334 over the putative class claims of the non-debtor class

members against Sears. Thus, the Court would not be the appropriate forum to adjudicate the merits of the other class members' claims against Sears, even though it potentially could adjudicate the Debtor's individual claim against Sears for the alleged violation of FDCPA. See, e.g., Fisher v. Federal Nat'l Mortgage Ass'n (In re Fisher), 151 B.R. 895 (Bankr. N.D. Ill. 1993). The bankruptcy court, unlike the district court, does not have ancillary or supplemental jurisdiction under 28 U.S.C. § 1367. Id. at 899. Thus, it would be singularly inappropriate for this Court to guesstimate the probability of Sears prevailing on its potential counterclaim, which this Court concluded after balancing the equities, could be fairly asserted as an affirmative defense.

The parties argue over whether or not the District Court should exercise its supplementary or ancillary jurisdiction under 28 U.S.C. § 1367 over Sears' counterclaim. This is because each counterclaim must meet jurisdictional requirements as noted by Federal Rule of Civil Procedure 8(a)(1), whether or not it is compulsory under Federal Rule of Civil Procedure 13(a) or permissive under Rule 13(b). Because the District Court already has jurisdiction over the Debtor's FDCPA claim, it clearly has jurisdiction to consider any and all of Sears' affirmative defenses thereto, and will not need to enter the fray over that issue if Sears can only assert its affirmative defenses.

V. CONCLUSION

The foregoing constitutes the Court's written findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052 and pursuant to the remand Order of the District Court.

ENTERED:

DATE: ____

John H. Squires
United States Bankruptcy Judge

cc: See attached Service List