

# Trustee Not Permitted to Pursue Pre-Petition “Asset”

By **Craig D. Robins**

Here’s an unusual situation. Ten years after a routine Chapter 7 case was closed, the trustee sought to re-open it to pursue an undisclosed “asset” worth over a hundred thousand dollars.

The undisclosed asset, however, was rather atypical as it consisted of a products liability claim the debtor did not even know existed when she filed her case.

Central Islip Bankruptcy Judge Robert E. Grossman just issued a decision preventing the trustee from re-opening the case to pursue this asset. *In re: Ross* (E.D.N.Y. Case No. 04-87445-reg, April 14, 2016).

The debtor in that case, in 1998 and 1999, underwent several surgical procedures in which a medical device was implanted and removed. A number of years later in 2004 the debtor filed for Chapter 7 relief and received a discharge shortly thereafter. Presumably, her medical situation was unrelated to her need to file bankruptcy. Also, she did not schedule any claims regarding the medical procedure as assets.

In 2012 while watching TV, the debtor saw one of those attorney solicitation commercials we often see, from a mass tort law firm looking to sign up injured consumers to a class action suit. This commercial just happened to refer to the medical device that had been implanted.

Upon learning that the device might be “defective,” even though it had been removed in 1999, she retained the law firm to seek recovery. Although it turned out that the debtor was not eligible to join the class action suit she was nevertheless offered a settlement of \$105,000

in exchange for her release of all present or future claims in connection with the device.

The panel trustee, Alan Mendelsohn, upon learning of the settlement offer, filed a motion in October 2015 seeking to reopen the case to administer the settlement proceeds for the benefit of those creditors the debtor had scheduled 10 years earlier. The debtor, who was represented by Melville attorney, Michael G. McAuliffe, opposed this relief.

Thus, the issue before the court was whether the settlement proceeds were pre-petition assets that the trustee was entitled to administer, or whether they belonged to the debtor.

What really made this case unusual is that the parties agreed that neither the debtor nor the medical community had knowledge that the device could cause the debtor harm as of the date the petition was filed, and in fact, the debtor had not suffered any physical harm from the device.

However, the trustee argued that because the device was implanted pre-petition, any cause of action that may ultimately accrue based upon possible harm from the device, including the settlement proceeds, constituted property of the estate.

Under Bankruptcy Code § 541(a)(1), property of the estate includes “all legal or equitable interests of the debtor” that exist “as of the commencement of the case.” As the judge put it, “the question is generally temporal: when did the debtor acquire a legal interest in the settlement proceeds?”

In this case, the only events that took place pre-petition were the implant and



Craig Robins

removal of the device. Did implanting the device, standing alone, vest rights in the debtor to receive the settlement proceeds as of the date she filed her bankruptcy?

Thus, resolving this issue required Judge Grossman to analyze whether the settlement was property of the estate. He stated, “What standard should

the court adopt in determining whether a cause of action, based upon an unrecognized injury to a debtor, is property of the bankruptcy estate?”

The judge observed that if the trustee’s position were taken to its logical conclusion, the court would be adopting a standard that would permit a trustee to capture any proceeds recovered by a debtor in his or her lifetime, so long as the right to recover the proceeds can be traced to a pre-petition event.

He also noted that determining whether this debtor’s settlement proceeds are property of the estate is complicated by the fact that the debtor suffered no injury pre-petition or post-petition. The settlement payment was being made in exchange for the debtor’s agreement not to bring a suit in the future.

Judge Grossman determined that in cases such as this, which involve potential tort claims, the proper focus is on whether there was a viable cause of action the debtor could bring under applicable law on the date the petition was filed.

If an action existed, regardless of what the debtor knew, then that cause of action and all its proceeds would constitute property of the estate. If, however, as is true in this case, no cause of action had matured, it is irrelevant whether the

debtor ultimately develops an injury; the cause of action resulting from that injury would not be property of the estate under Bankruptcy Code § 541.

Here, as of the date she filed the petition, the debtor had no expectation that a device implanted in her and removed pre-petition, for which no warning had ever been issued, would create a right to receive the settlement proceeds several years later.

Judge Grossman commented that had the medical community been aware of any danger inherent in using the device pre-petition, and had the debtor suffered an injury, the answer would be different.

Thus, because the elements necessary to commence an action under state law were not present as of the date the debtor filed her petition, the right to receive the settlement proceeds were not sufficiently rooted in the debtor’s pre-petition past to warrant inclusion of the settlement proceeds in the debtor’s bankruptcy estate.

Judge Grossman expressed serious concern as to what could happen if he had adopted the trustee’s position. “Opportunistic trustees would be scrambling to latch onto every possible claim that may someday arise, however attenuated,” he stated.

*Note: Craig D. Robins, a regular columnist, is a Long Island bankruptcy lawyer who has represented thousands of consumer and business clients during the past twenty-nine years. He has offices in Melville, Coram, and Valley Stream. 516-496-0800. He can be reached at [CraigR@CraigRobinsLaw.com](mailto:CraigR@CraigRobinsLaw.com). Please visit his bankruptcy website: [www.BankruptcyCanHelp.com](http://www.BankruptcyCanHelp.com) and his bankruptcy blog: [www.LongIslandBankruptcyBlog.com](http://www.LongIslandBankruptcyBlog.com).*