The relief described hereinbelow is SO ORDERED.

SIGNED this 17th day of September, 2014.

Robert D. Berger
United States Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS

In re:

JERRY HARRISON FEAGAN and
CYNTHIA A. FEAGAN,
Debtors.

Case No. 12-21994

ORDER OVERRULING IN PART DEBTOR'S OBJECTION TO MOTION TO SELL

On July 16, 2013, the Trustee filed a Motion for Approval of Sale of real estate.[1] In the Motion, the Trustee proposed to pay $220,000 of the sale proceeds to Kaw Valley Bank to obtain a release of a mortgage. Debtors assert that KVB is only entitled to $146,263.84 because the future advances clause in the mortgage is unenforceable or, alternatively, because KVB is bound by its statements in the Motion for Relief from Automatic Stay wherein KVB asserted a total secured claim of only $146,263.84. The Trustee contests the Debtors' standing to challenge the

[1] Doc. 72.

security agreement. The Court holds that the Debtors have standing to challenge the agreement, but more evidence is needed to determine whether the future advances clause in the mortgage is enforceable. The Court also finds that statements made by KVB in the Motion for Relief from Automatic Stay do not bar KVB from claiming the full amount of security they may be entitled to under the contract.

Jurisdiction

The Court has jurisdiction over this contested matter pursuant to 28 U.S.C. § 1334(b). Reference to the Court of this proceeding is appropriate under 28 U.S.C. § 157(a) and Standing Order No. 13-1 of the United States District Court for the District of Kansas. This case is a core proceeding under 28 U.S.C. §§ 157(b)(2)(K), (N), and (O). The parties have stipulated to the jurisdiction of this Court.

Background

Debtors filed for Chapter 7 bankruptcy relief on July 23, 2012. Among their assets the Debtors listed a 50 percent interest in 138.7 acres of farmland in Cherokee County, Kansas ("Property").[2] Debtors listed the value of the Property as unknown. The Property is encumbered by a mortgage with Kaw Valley Bank ("KVB") with a maximum principal amount of $180,000 ("Mortgage").[3] The exact amount of debt secured by the Mortgage is disputed. Both Debtors and Minnie Feagan[4] signed the Mortgage. On September 28, 2012, KVB filed its Motion for

[2] Doc. 1 at 19.

[3] Doc. 34, Ex. 4.

[4] Minnie Feagan is Debtor Jerry Feagan's mother and owner of the other 50 percent interest. Doc. 72.

Relief from Stay.[5] In the Motion for Relief from Stay, KVB asserts that the Debtors held no equity in the Property.[6] In Claim #15-1, KVB asserts a secured claim of $266,000 with the value of the collateral unknown. No evidence of the Property's value was provided. The Trustee's Motion for Approval of Sale was granted on September 12, 2013, and the Property sold for $246,900.00, with $220,000 to be paid to KVB conditioned upon a further determination by this Court.

The issue arises in part from the statements made by KVB in the Motion for Relief from Automatic Stay. In this motion, KVB listed the total secured debt as $146,263.84. Specifically, KVB stated that the Debtors borrowed $33,073.76, as evidenced by a promissory note dated March 14, 2012 ("Note 1"), and $100,000, as evidenced by a promissory note dated January 5, 2012 ("Note 2"). KVB asserts that the Mortgage secures not only Notes 1 and 2, but also that the future advances clause in the Mortgage includes all other loans made by KVB to Debtors after March 14, 2008. These other loans include a promissory note for $86,000 signed on May 10, 2010 ("Note 3"); a promissory note for $200,000 signed on June 9, 2011 ("Note 4"); a promissory note for $400,000 signed on October 15, 2011 ("Note 5"); and a promissory note for $74,897.89 signed on February 4, 2012 ("Note 6"). Each of these promissory notes referenced specific collateral, but only Notes 1 and 2 referenced the Mortgage. Note 3 listed a Deed of Trust in property located in Missouri as the collateral, and Notes 4, 5, and 6 each listed various personal and business property of the Debtors. According to the Trustee, KVB asserts that by

[5] Doc. 34.

[6] Doc. 34 at 6 ¶ 32.

virtue of a future advances clause in the Mortgage, the other Notes are secured under the Mortgage and the total lien on the property is therefore $232,113.40. This amount includes the $180,000 maximum principal balance, $45,113.40 in accrued interest, and attorney's fees of $7,000.[7] Prior to filing the Motion for Approval of Sale, the Trustee and KVB agreed that KVB would receive $220,000 of the proceeds in full satisfaction of the Mortgage. The Debtors objected to this settlement agreement ("Agreement") because they assert that KVB is only entitled to the $146,900 under the terms of the Mortgage and the statements made in the Motion for Relief from Automatic Stay. If the Mortgage only secures Notes 1 and 2, then KVB is entitled to $146,900 of the proceeds as secured, but if some or all of the other promissory notes are secured by the Mortgage, then KVB's lien may be $232,113.40.

Debtors claim to have standing to challenge the Trustee's administration of the case and the estate assets based on the existence of certain non-dischargeable priority tax debt which may receive a greater distribution from the proceeds of the sale if KVB's secured claim is reduced, thereby lowering Debtors' post-discharge liability. The Trustee challenges this position because the Debtors will not receive any proceeds from the sale of the Property, regardless of the outcome of this dispute.

Discussion

There are two separate issues before the Court: First, whether the Debtors have standing to challenge the extent of KVB's secured claim when the Debtors' only pecuniary interest arises from a potential reduction in their post-discharge liability. Second, what rights does KVB

[7] Doc. 72 at 2 ¶ 9.

maintain under the Mortgage in light of the claims made in the Motion for Relief from Stay? There is a split of authority on the first issue,[8] and this Court was not able to find controlling Tenth Circuit precedent. Determining KVB's rights under the Mortgage involves two issues. First, whether the future advances clause is enforceable, and second, whether the doctrines of judicial admissions or judicial estoppel limit KVB to the statements of value and security stated in the Motion for Relief from Automatic Stay.

A. Debtors have standing to challenge the settlement agreement.

The Trustee contests the Debtors' standing to challenge his administration of the estate because the Debtors cannot receive any funds from the sale of the Property, regardless of the outcome of this issue. The Trustee bases his position on the general rule that chapter 7 debtors lack standing to challenge the administration of their case unless the debtor would receive a distribution under 11 U.S.C. § 726(a)(6).[9] The Trustee asserts that unless the distribution of the assets of the estate would produce a surplus to the Debtors, the Debtors are not parties-in-interest and therefore lack standing.

This Court has previously held that a chapter 7 debtor has standing to challenge a proposed settlement agreement if the debtor will be adversely affected by that agreement.[10]

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[8] *Compare In re Adams*, 424 B.R. 434, 436-37 (N.D. Ill. 2010) (holding that chapter 7 debtor lacked standing because the effect on the non-dischargeable debt liability was indirect and that granting debtor standing in these cases would "interfere with the administration of chapter 7 cases") *with McGuirl v. White*, 86 F.3d 1232, 1235 (D.C. Cir. 1996) (holding that the possible reduction of post-discharge liability is direct benefit to the debtor, sufficient to confer standing).

[9] 4 COLLIER ON BANKRUPTCY ¶ 502.02[2][c], at 502-13 (Alan N. Resnick & Henry J. Sommer, eds., 16th ed. 2014). All future statutory references are to title 11 of the United States Code, unless otherwise specified.

[10] *In re Middendorf*, 381 B.R. 774, 776 (Bankr. D. Kan. 2008).

Other courts have approached the issue by looking to see whether the debtor has any pecuniary interest in the outcome of the dispute.[11] In *McGuirl v. White*, the Court of Appeals for the D.C. Circuit held that a debtor had standing to challenge the Trustee's administration of the estate because the impact on the debtor's non-dischargeable debt affected the debtor's pecuniary interest in the outcome of the bankruptcy. The court held that a reduction in the debtor's post-discharge liability was sufficient for the debtor to have standing to challenge the trustee's application for administrative expenses. In *In re Adams*, the Bankruptcy Court for the Northern District of Illinois disagreed and held that a chapter 7 debtor in a non-surplus case lacked standing to challenge the trustee despite the existence of non-dischargeable debt. The courts reached opposite conclusions because they disagreed on whether the reduction in post-discharge liability directly affected the debtor's pecuniary interests. This Court concludes that a reduction in a debtor's post-discharge priority tax liability benefits the debtor nearly as directly as an increase in a surplus distribution. Because a possible outcome in favor of the Debtors here will mean that they owe less debt after their discharge, the Court will not prevent the Debtors from challenging the Agreement. Further, this conclusion supports the manifest preference under the Code to favor the payment of tax liabilities. *See, e.g.*, § 523(a)(1) and 507(a)(8).

This outcome fairly reconciles the interest of the Trustee in administering the estate and the Debtors' pecuniary interest. Allowing standing in this case also follows the reasoning in *In re Middendorf* because the Debtors may be adversely affected by the Agreement.

B. Whether the future advances clause in the Mortgage is enforceable up to the

[11] *See In re Cult Awareness Network*, Inc., 151 F.3d 605, 607 (7th Cir. 1998); *In re Kieffer-Mickes, Inc.*, 226 B.R. 204, 208-09 (B.A.P. 8th Cir. 1998); *In re Adams*, 424 B.R. 434 (N.D. Ill. 2010).

stated maximum obligation of $180,000, plus interest and fees, is a factual question.

Promissory notes and mortgages are contracts between the parties, and therefore subject to the same rules of construction as other contracts. The "primary rule in interpreting promissory notes and mortgages is to determine the intention of the parties."[12] Courts determine the intent of the parties by examining the mortgage and note together, not each one individually.[13] Future advances clauses in real estate mortgages are enforceable in Kansas, provided that the subsequent promissory note either specifically refers to the prior mortgage, or if the subsequent debt is "of the same kind or character as, or part of the same transaction or series of transactions with, that originally secured by the mortgage."[14] Whether the subsequent debt is of the same kind or character, or part of the same transaction or series of transactions, is a factual question. A lien on future advances cannot exceed the maximum obligation stated in the mortgage.[15] Pursuant to § 363(p)(2), "the entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest."

Two of the promissory notes signed by the Debtors specifically state that the notes are secured by the Mortgage. There is no question that the Mortgage secures these notes and the parties do not contest the issue. The other four notes list other security, however, and therefore the Court must determine whether the parties intended for the Mortgage to secure Notes 3-6.

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[12] *Mark Twain Kansas City Bank v. Cates*, 248 Kan. 700, 709 (Kan. 1991) (citing *Carpenter v. Riley*, 234 Kan. 758, 763 (Kan. 1984)).

[13] *See Mark Twain Kansas City Bank v. Cates*, 248 Kan. at 710.

[14] *Id.* at 700 (1991).

[15] K.S.A. 9-1101; K.S.A. 58-2336.

Absent a specific reference to the Mortgage in the promissory note, Notes 3-6 will only be secured if they were "of the same kind or character as, or part of the same transaction or series of transactions with, that originally secured by the mortgage."[16] Since there has been no evidence submitted on the record to indicate to the Court that Notes 3-6 were executed in the same transaction or a series of the same transactions as Notes 1 and 2, this Court cannot presently rule on the issue.

C. The doctrines of judicial estoppel and judicial admissions do not limit KVB's security to the amount stated in the Motion for Relief from Automatic Stay.

Debtors argue that the representations KVB made in its Motion for Relief from Automatic Stay regarding the secured portion of the claim should be binding on KVB throughout this bankruptcy case. In the Motion for Relief from Automatic Stay, KVB stated that the Property served as collateral for Notes 1 and 2 totaling $146,900. The Motion for relief from stay stated only that Notes 1 and 2 were secured by the Property, that the Property was completely encumbered, and therefore that relief from the stay was appropriate. The motion was unopposed and it was granted. The issue now is whether the statements made by KVB in the Motion for Relief from Automatic Stay bind KVB on the extent of its lien.

1. The statements made in the Motion for Relief from Automatic Stay do not constitute judicial admissions.

Debtors assert that KVB is bound by its statements in the Motion for Relief from Automatic Stay because KVB "admitted that the value of its claim against the [Property] is limited to the two Notes." Debtors' position is that because KVB claimed that only the two

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[16] *Mark Twain Kansas City Bank v. Cates*, 248 Kan. at 709.

Notes referenced in the Motion for Relief from Automatic Stay were secured, KVB is prohibited from asserting the validity of the future advances clause with regards to Notes 3-6.

"'Judicial admissions are formal admissions . . . which have the effect of withdrawing a fact from issue and dispensing wholly with the need for proof of the fact.'"[17] Judicial admissions in pleadings are formal concessions or stipulations that are binding on the party making them.[18] A statement will not be held as a judicial admission if the circumstances do not justify such a finding.[19] Whether a statement made in a pleading is binding on the party is up to the court's discretion.[20]

The representations made by KVB in the Motion for Relief from Automatic Stay must be understood in context. Under the Code, a party-in-interest may obtain relief from the automatic stay upon a showing that the debtor does not have an equity in the property and the property is not necessary to an effective reorganization.[21] In other words, "[a] creditor can meet its burden of proof that a debtor has no equity by showing that the liens exceed the value stated. When the motion is uncontested . . . [t]he court need not determine the exact value."[22] The Motion for Relief from Automatic Stay filed by KVB met these requirements, and since it was unopposed,

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[17] *Koch v. Koch Indus., Inc.*, 996 F. Supp. 1273, 1277 (D. Kan. 1998) (quoting *Guidry v. Sheet Metal Workers Intern. Ass'n, Local 9*, 10 F.3d 700, 716 (10th Cir. 1993)).

[18] *See Koch*, 996 F. Supp. at 1277 (quoting Michael H. Graham, *Federal Practice and Procedure: Evidence § 6726*).

[19] *See Koch*, 996 F. Supp. at 1277 (quoting *Schott Motorcycle Supply v. American Honda Motor Co.*, 976 F.2d 58, 61 (1st Cir. 1992)).

[20] *See Koch*, 996 F. Supp. at 1278 (quoting *Guidry*, 10 F.3d at 716).

[21] *See* 11 U.S.C. 362(d)(2).

[22] *Thomas v. Countrywide Home Loans, Inc. (In re Thomas)*, 344 B.R. 386, 393 (Bankr. W.D. Penn. 2006).

the Motion for Relief from Automatic Stay was granted by default. The Court dismisses the argument because KVB asserted a lien balance that was apparently sufficient to satisfy Debtors that there was no equity in the Property. The Debtors have also changed their position now that the value of the Property turns out to be higher than the Debtors might have thought. Because the issue of valuation and the extent and validity of KVB's liens were never actually litigated, the Court will not bind KVB to the statements made in the Motion for Relief from Automatic Stay. In further support of the Court's conclusion, neither the Debtors nor the Trustee objected to KVB's proof of claim in which KVB asserted a secured claim of $266,000.

The Court determines that the statements made in the Motion for Relief from Stay by KVB must be considered in the context of the specific purposes of that motion. Because KVB only needed to demonstrate that Debtors lacked equity in the Property, KVB is not barred from attempting to collecting the full value of the lien from the proceeds of the sale of the Property.

2. The doctrine of judicial estoppel does not prohibit KVB from asserting the full value of the lien on the Property.

Debtors aver that KVB is judicially estopped from asserting a greater lien on the Property than what was stated in the Motion for Relief from Stay. "Judicial estoppel is an equitable doctrine, 'which protects the integrity of the judicial process by prohibiting parties from deliberately changing positions according to the exigencies of the moment.'"[23] In the Tenth Circuit, three factors are used to determine whether the doctrine of judicial estoppel should be

[23] *Barker v. Asset Acceptance, LLC*, 874 F. Supp. 2d 1062, 1065 (D. Kan. 2012) (quoting *Eastman v. Union Pac. R.R.*, 493 F.3d 1151, 1156 (10th Cir. 2007)).

applied.[24] Judicial estoppel may be applied if: (1) the party's later position is clearly inconsistent with his earlier position; (2) the party has succeeded in persuading a court to accept the earlier position, so as to create the perception that either the first or second court was misled; and (3) whether the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if he were not estopped.[25] "Application of the doctrine of judicial estoppel as applied to estimates of value in a bankruptcy is considered with a different, more relaxed view."[26]

Here, the alleged amount of the secured claim of KVB increased from when the Motion for Relief from Automatic Stay[27] and the Motion for Approval of Sale[28] were filed. However, this position is not "clearly inconsistent" with the prior position, because the statements made in the Motion for Relief from Automatic Stay were for the limited purpose of obtaining relief from the automatic stay under § 362(d). Moreover, as noted above, KVB needed only to show that it was entitled to the limited relief from the automatic stay; the Motion for Relief from Automatic Stay was not in this case a final adjudication of KVB's rights under the Mortgage. There is no indication that the Court was misled by the statements made in the Motion for Relief from Automatic Stay. KVB demonstrated that it was entitled to relief, and because there was no opposition, the motion was granted. Finally, Debtors assert that they might have opposed the

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[24] *In re Riazuddin*, 363 B.R. 177, 185 (B.A.P. 10th Cir. 2007).

[25] *Id.*

[26] *Kasbee v. Huntington Nat'l Bank (In re Kasbee)*, 466 B.R. 719, 726 (Bankr. W.D. Penn. 2010).

[27] Doc. 34 filed on September 28, 2012.

[28] Doc. 72 filed on July 16, 2013.

Motion for Relief from Automatic Stay had KVB listed the value of the lien at the higher amount. This argument is not persuasive. The Debtors are now asking this Court to intercede and find that KVB has misled the Court because the Property was actually worth more than the Debtors thought. The Court declines this invitation and therefore determines that the doctrine of judicial estoppel is not applicable to this case.

Conclusion

Debtors have standing to challenge the Agreement because their post-discharge liability may be decreased upon a favorable finding on the issue of KVB's lien. If KVB's lien amount is reduced, then there will be more estate assets available to pay on priority unsecured tax claims. This is of sufficient benefit to Debtors to impart standing. The extent of KVB's lien cannot be ascertained at this time, as the Court lacks the necessary evidence to make a final determination as to the extent that KVB's claim is secured by the Mortgage. Further proceedings are necessary to fully resolve Debtors' Objection and an evidentiary hearing consistent with this opinion will be set forthwith. This Court rejects Debtors' arguments under the doctrines of judicial admissions or judicial estoppel.

IT IS SO ORDERED.

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ROBERT D. BERGER
U.S. BANKRUPTCY JUDGE
DISTRICT OF KANSAS