UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF MICHIGAN
GRAND RAPIDS DIVISION

IN RE:	Case No. 07-02212-jtg
	Chapter 7
RYAN GOODACRE,	
	One Division Avenue North
Debtor.	Grand Rapids, MI 49503
	November 8, 2017
RYAN LANCASTER, formerly known as RYAN GOODACRE,	Case No. 16-80315-jtg
	Adversary Proceeding
Plaintiff,	
vs.	
EDUCATIONAL FINANCIAL SERVICES, a division of WELLS FARGO BANK, N.A.,	
Defendant.	

TRANSCRIPT OF TELEPHONIC BENCH OPINION
BEFORE THE HONORABLE JOHN T. GREGG
UNITED STATES BANKRUPTCY JUDGE

APPEARANCES:

For the Plaintiff:	Smith Law Group By: Austin C. Smith Three Mitchell Place Suite 5P New York, NY 10017 (917) 992-2121
For Educational Financial Services, a division of Wells Fargo Bank, N.A.:	Miller Canfield Paddock & Stone, PLC By: Ronald A. Spinner 150 West Jefferson Suite 2500 Detroit, MI 48226 (313) 496-7829

Appearances continued:

For Educational Financial Services, a division of Wells Fargo Bank, N.A.:	Miller Canfield Paddock & Stone, PLC By: Emily C. Palacios 101 North Main Street Seventh Floor Ann Arbor, MI 48104 (734) 668-7784
Also Present:	Crystal Lee Ryan Lancaster
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Proceedings recorded by electronic sound recording; transcript produced by transcription service.

(Time Not Noted)

THE COURT: Good morning. This is a telephonic bench opinion in the case of Lancaster versus Educational Financial Services, adversary proceeding number 16-80315.

A transcript will be available upon request to the Clerk's Office.

Could I have the appearances, please?

MR. SPINNER: Yes, Your Honor. Ron Spinner from Miller Canfield, for Educational Financial Services, a division of Wells Fargo Bank.

MS. PALACIOS: Yes, Your Honor. Emily Palacios, also appearing on behalf of Educational Financial Services, a division of Wells Fargo Bank, N.A.

Also, Your Honor, so you may be aware, we have a representative of Wells Fargo Bank on the line this morning, as well. It's Crystal Lee.

THE COURT: Okay, thank you.

MR. SMITH: Your Honor, Austin Smith for the Plaintiff-Debtor, Ryan Lancaster, formerly known as Ryan Goodacre.

MR. LANCASTER: And Ryan Lancaster. I'm here.

THE COURT: Okay, thank you. Before the Court is a motion to dismiss the second amended complaint.

In the motion, the Defendant, Educational Financial Services, a division of Wells Fargo Bank, National

Association, first contends that the complaint must be dismissed under Federal Rule of Civil Procedure 12(b)(1), because this Court lacks subject matter jurisdiction.

Second, even if the Court had subject matter jurisdiction, the Defendant argues that the Plaintiff, Ryan Lancaster, has failed to state a claim upon which relief can be granted under Federal Rule of Civil Procedure 12(b)(6).

The facts presented in the second amended complaint are fairly straightforward.

The Plaintiff borrowed $10,500.00 from the Federal government on May 17, 2004, to assist him with his education at an on-line university.

Later that year, the Plaintiff borrowed $15,000.00 from Wells Fargo in the form of two private non-certified, non-qualified, credit-based, direct-to-consumer loans.

The second amended complaint further states that the loans from Wells Fargo had nothing to do with his education at the on-line university, or anywhere else, for that matter.

In March of 2007, the Plaintiff filed a Petition for relief under Chapter 7 of the Bankruptcy Code in this Court.

On Schedule F, the Plaintiff identified the Defendant as having a general unsecured claim in the amount of $9,892.00.

Schedule F further described the debt he owed to the Defendant as a student loan, and "indicated that he was indebted to Wells Fargo for educational loans."

The Defendant's claim was never liquidated or otherwise adjudicated in the Plaintiff's bankruptcy, which was a no-asset case.

Likewise, neither the Plaintiff nor the Defendant commenced an adversary proceeding seeking a determination as to the dischargeability of the debt under Section 523(a)(8) during the pendency of the Plaintiff's bankruptcy case, or at any other time, for that matter, until the commencement of this adversary proceeding.

Less than a year after filing his bankruptcy Petition, the Plaintiff received a discharge of his debts.

The order granting the Plaintiff a discharge states that the Plaintiff is granted a discharge under Section 727 of the Bankruptcy Code. The discharge order includes a rider entitled "explanation of bankruptcy discharge in a Chapter 7 case."

Under a sub-heading entitled "debts that are not discharged," the rider generally explains that "some of the common types of debts which are not discharged" are "debts for most student loans."

The discharge order makes no mention of the specific debt owed to the Defendant, however.

In 2007, and after the entry of the discharge order, the Defendant commenced a civil action against the Plaintiff in Michigan State Court to collect the debt related to the two loans.

According to the second amended complaint, the State Court complaint made no mention of the Plaintiff's previous bankruptcy or resulting discharge.

Neither the State Court complaint, nor any other pre-judgment pleadings, are attached to the second amended complaint in this adversary proceeding.

The second amended complaint states that "Wells Fargo forced the Plaintiff into a consent judgment on October 23, 2008."

Moreover, the second amended complaint states that "after inducing the Plaintiff into the consent judgment, Wells Fargo then proceeded to collect on this discharged debt in monthly installments of $150.00 for the next seven years."

In 2015, the Plaintiff "was forced to borrow $8,000.00 to repay the consent judgment in full."

The Plaintiff alleges that because he is still repaying this new debt today, he is "continuing to suffer injury-in-fact resulting from Wells Fargo's actions."

The Plaintiff further alleges that he has suffered harm from the illegal collection efforts of the Defendant.

On November 16, 2016, and after the Court re-

opened the underlying bankruptcy case, the Plaintiff commenced this adversary proceeding against the Defendant and Thomas Alward, the latter of whom has been voluntarily dismissed.

The Court subsequently granted the Defendant's motion to dismiss the first amended complaint on April 18, 2017, because the Plaintiff had failed to state a claim upon which relief could be granted.

However, the Court granted the Plaintiff leave to file an amended complaint.

In his second amended complaint, the Plaintiff asserts two claims for declaratory judgment under one count.

First, at paragraph 64, the Plaintiff requests a "declaratory judgment that the loans from Wells Fargo were discharged by operation of law on November 29, 2007, because the loans were not a student debt protected by any sub-section of Section 523(a)(8)."

Alternatively, the Plaintiff requests "a declaratory judgment that the loans are dischargeable because they are not protected by any sub-section of Section 523(a)(8)."

In lieu of an answer to the second amended complaint, the Defendant filed its motion to dismiss, and brief in support thereof.

The Defendant advances five arguments in its

motion:

First, the *Rooker-Feldman* doctrine deprives this Court of jurisdiction.

Second, the adversary proceeding is moot because there is no debt.

Third, the doctrine of *res judicata,* or claim preclusion, bars any litigation as to the dischargeability of the debt under Section 523(a)(8).

Fourth, the doctrine of laches bars further pursuit of the claims.

Fifth, the second amended complaint fails to plead a claim for which relief can be granted with respect to one of the two loans from Wells Fargo.

In his response, the Plaintiff, of course, disagrees with the Defendant's position on all issues, other than perhaps the failure to state a claim regarding the first loan. The Plaintiff's response is silent in this regard.

The Defendant filed a reply brief, and thereafter the Court held a hearing on the motion.

After carefully considering the parties' arguments, the Court shall deny the motion to dismiss.

The Court shall first address the jurisdictional issues.

Article III of the Constitution limits Federal Court jurisdiction to actual cases and controversies. *See*

Chafin v. Chafin, 133 S. Ct. 1017, at page 1023.

To invoke the jurisdiction of a Federal Court, a litigant must have suffered or been threatened with an actual injury traceable to the defendant, and likely to be redressed by a favorable judicial decision. *See Lewis v. Continental Bank Corporation,* 494 U.S. Rptr. 472, at page 477, a decision from the United States Supreme Court in 1990.

The case for controversy must exist through all stages of the case, from the filing of the complaint in the first instance, through final adjudication, and ultimately through any review by an appellate tribunal.

Upon review of the allegations in the second amended complaint, the Court concludes that this adversary proceeding is not moot. Although the debt has been satisfied, the Plaintiff seeks a declaration that the Defendant's actions were taken in violation of the discharge injunction pursuant to Section 524(a), and that Section 523(a)(8) affords no relief to the Defendant.

The State Court determined that the Plaintiff is liable to the Defendant for the repayment of the loans. In the second amended complaint, the Plaintiff argued that it suffered an actual injury because the Defendant violated the discharge, the scope of which has yet to be determined by this Court or the State Court.

Simply put, if this Court finds that the discharge

has been violated because the loans were not student loans under Section 523(a)(8), the Defendant will have been injured by being forced to satisfy the State Court judgment notwithstanding the discharged nature of the debt.

The Court, therefore, concludes that the adversary proceeding is not moot at this time.

The Defendant also argues that the *Rooker-Feldman* doctrine precludes this Court from exercising subject matter jurisdiction.

As the Sixth Circuit Bankruptcy Appellate Panel recently observed, the *Rooker-Feldman* doctrine frequently raises thorny issues, particularly where the discharge injunction is invoked. *See, In Re Isaacs,* 569 B.R. 135, at page 142, a decision from the Bankruptcy Appellate Panel for the Sixth Circuit in 2017.

The *Rooker-Feldman* doctrine is derived from two decisions from the United States Supreme Court: *Rooker v. Fidelity Trust Company,* 263 U.S. Rptr. 413, a decision in 1923; and *District of Columbia Court of Appeals v. Feldman,* 460 U.S. 462, a decision from the Supreme Court in 1983.

The doctrine involves a situation where the losing party in State Court files a suit in Federal Court, after the State Court proceedings have ended, complaining of an injury caused by the State Court judgment, and seeking review in rejection of that judgment. *See, ExxonMobil Corporation v.*

Saudi Basic Industries Corporation, 544 U.S. 280, at page 291, a decision from the United States Supreme Court in 2005.

In other words, it prohibits cases brought by State Court losers complaining of injuries caused by State Court judgments. *See, In Re Hamilton,* 540 F. 3d 367, at page 372, a decision from the Sixth Circuit Court of Appeals in 2008.

In a case favorably cited by *Isaccs,* the Seventh Circuit Court of Appeals explained that: "The *Rooker-Feldman* doctrine asks: Is the federal plaintiff seeking to set aside a state court judgment, or does he present some independent claim, albeit one that denies a legal conclusion that a state court has reached in a case to which he was a party? If the former, then the district court lacks jurisdiction; if the latter, then there is jurisdiction and state law determines whether the defendant prevails under principles of preclusion." That's a cite to *Gash Associates v. The Village of Rosemont, Illinois,* 995 F. 2d 726, at page 728, a decision from the Seventh Circuit Court of Appeals in 1993.

The parties in this adversary proceeding devote significant portions of their briefs to the *Rooker-Feldman* doctrine, focusing, in large part, on the Sixth Circuit's decision in *Hamilton.*

In *Hamilton,* after the debtor filed for bankruptcy, the Bankruptcy Court held that the debtor's debt

to his ex-wife was dischargeable, and thus subject to the discharge order.

Later, the ex-wife filed a third party complaint against the debtor for indemnification relating to a debt upon which they had been jointly liable.

For whatever reason, the debtor did not raise his discharge in bankruptcy as an affirmative defense.

After the State Court entered a judgment against the debtor, the debtor commenced an adversary proceeding in the Bankruptcy Court to enjoin any collection attempts by his ex-wife.

The Sixth Circuit held that although state courts have jurisdiction to construe or interpret a discharge order, they do not have jurisdiction to modify a discharge order by construing it incorrectly.

According to the Sixth Circuit, the State Court judgment improperly modified the discharge order, because it awarded money damages on a pre-petition debt, even though the discharge order had clearly extinguished the debtor's personal liability for such debt.

In the instant matter, the Plaintiff argues that the State Court impermissibly modified the discharge injunction entered by this Court, because the loans from the Defendant were not student loans.

As such, the Plaintiff asserts the debts of the

Plaintiff to the Defendant were discharged.

Defendant contends that the Plaintiff's failure to raise Section 523(a)(8) and the discharge injunction in the State Court resulted in an implicit determination by the State Court that the debt was non-dischargeable.

The Defendant, therefore, posits that the State Court did not modify the discharge order. Instead, the State Court implicitly construed the discharge order.

It is important to keep in mind what the discharge order does and does not say. It provides that certain debts could be non-dischargeable, but makes no specific declaration regarding any one debt in particular.

And because Section 523(a)(8) is self-executing, a student loan debt is non-dischargeable absent a determination.

However, the self-executing nature of Section 523(a)(8) is premised on the debt actually being one for a student loan, a determination that was not previously made by this Court or the State Court which had concurrent jurisdiction to do so.

And although the Plaintiff's Schedules seemed to indicate that the Plaintiff believed the loans were for scholastic pursuits, the Schedules are matters of fact, not law.

While the first amended complaint failed to state

a claim, the second amended complaint does not suffer from the same defects.

It is clear that the primary issue is whether the two loans are student loans for purposes of Section 523(a)(8).

In the State Court action, neither party requested that the State Court affirmatively decide whether the debt was subject to the discharge, including whether the debt was even a student loan debt excepted from discharged under Section 523(a)(8).

As a result, the State Court never considered the issue.

According to *Hamilton,* if the State Court had made such a determination, and assuming that the determination did not conflict with the discharge injunction entered by this Court in 2007, the *Rooker-Feldman* doctrine would apply to bar the Court from considering whether the debt was subject to discharge.

But that is not the case here. As previously noted, when a State Court construes a discharge, the State Court must do so correctly.

Here, the State Court did not construe the discharge correctly, nor did it construe the discharge incorrectly. Instead, it simply made no determination on the claim of non-dischargeability or the affirmative defense of

the discharge under Section 524(a).

Because the issue has yet to be decided, this Court is now tasked with determining whether the debt was subject to the discharge, or was otherwise non-dischargeable.

Hamilton and the decisions cited therein recognize as much. *Hamilton* places great emphasis on the inability of a debtor to waive the discharge.

In the event that this Court concluded that the *Rooker-Feldman* doctrine applies, such a decision would be tantamount to endorsing a waiver of the discharge. By doing so, creditors like the Defendant would be incentivized to commence suit in State Court to circumvent *Hamilton's* holding.

Hamilton relies in part on, and the Defendant cites favorably to, a decision from the Bankruptcy Appellate Panel for the Ninth Circuit. *See In Re Pavelich,* 229 B.R. 777, again a decision from the Ninth Circuit Bankruptcy Appellate Panel in 1999.

In *Pavelich,* the Court explained the concept of construing the discharge only to the extent that it is construed correctly.

As noted by the Defendant in its brief, *Pavelich* held: "*Rooker-Feldman* applies to exceptions to discharge that are determined by state courts that have concurrent jurisdiction over the specific non-dischargeability issue."

The key is that the exception to discharge must be determined, which, as previously noted, was not in this adversary proceeding.

The Defendant improperly attempts to stretch *Pavelich's* pronouncements regarding concurrent jurisdiction to situations where the State Court has not determined, but is instead silent on, whether a specific debt was discharged.

According to the Defendant, silence on the issue is tantamount to an implicit determination that the debt is non-dischargeable.

The Court disagrees.

It is clear from *Pavelich* that it is not enough for the State Court to remain silent. It must make an actual determination regarding the discharge; something lacking in the present adversary proceeding.

A review of *Singleton,* another decision relied on by *Hamilton,* yields the same conclusion. *See In Re Singleton,* 230 B.R. 533, a decision from the Bankruptcy Appellate Panel for the Sixth Circuit in 1999.

In *Singleton,* a state court decided that the automatic stay did not apply to the sale of certain real estate because it was property of a third party, not the debtor.

On appeal by the debtor, after the adversary proceeding was dismissed for failure to state a claim, the

Bankruptcy Appellate Panel for the Sixth Circuit held that the *Rooker-Feldman* doctrine barred review of the State Court's decision.

Paramount to the Panel's decision was the fact that the State Court actually considered whether the automatic stay applied to the sale, and did so correctly.

Again, the facts here are significantly different, because the State Court never made any such determination.

In sum, because neither the Bankruptcy Court nor the State Court ever affirmatively determined whether the loans were subject to the discharge, the *Rooker-Feldman* doctrine does not apply.

Although the claims in this Court might effectively deny a legal conclusion of the State Court, *i.e.*, an award of damages for breach of contract, they are nonetheless independent from the State Court judgment.

This Court, therefore, has subject matter jurisdiction to consider whether the two loans were non-dischargeable under Section 523(a)(8), or subject to the discharge under Section 524(a).

Having disposed of the jurisdictional issues, the Court turns to the Plaintiff's arguments that the second amended complaint fails to state -- excuse me, the Defendant's arguments that the second amended complaint fails to state a claim upon which relief can be granted.

This Court has previously set forth the standard for a motion to dismiss in *In Re Perkins,* 533 B.R. 242, at page 252, a decision, again, from this Court in 2015, which the Court shall incorporate by reference into this Bench Opinion.

The Court turns to the Defendant's argument that *res judicata,* or claim preclusion, precludes the Plaintiff from pursuing its claims.

In *ExxonMobil,* the United States Supreme Court explained that *Rooker-Feldman* does not otherwise override or supplant preclusion doctrine or augment the circumscribed doctrines that allow Federal Courts to stay or dismiss proceedings in deference to State Court actions.

If a federal plaintiff presents some independent claim, albeit one that denies a legal conclusion that a state court has reached in a case to which he was a party, then there is jurisdiction, and state law determines whether the defendant prevails under principles of preclusion. That is, again, a quote from *In Re ExxonMobil,* which has previously been cited.

As such, even though *Rooker-Feldman* does not apply in this adversary proceeding, such a determination does not foreclose application of principles of preclusion, such as *res judicata.*

Pursuant to the United States Constitution and

Federal Statute, each state must give full faith and credit to the judicial proceedings of every other state; *citing* United States Constitution, Article IV, Section I, as well as 28 U.S.C. sec. 1738.

Thus, a Federal Court must give a State Court judgment the same preclusive effect as would be given that judgment under the law of the state in which the judgment was rendered. *See In Re Bursack,* 65 F. 3d 51, a decision from the Sixth Circuit Court of Appeals in 1995.

Under Michigan law, *res judicata* precludes multiple suits alleging the same cause of action. *See Adair v. State of Michigan,* 470 Mich. Rptr. 105, at page 121, a decision from the Michigan Supreme Court in 2004.

The doctrine bars a second subsequent action where the prior action was decided on the merits, both actions involved the same parties or their privies, and the matter in the second case was, or could have been, resolved in the first.

To be accorded the conclusive effect of *res judicata,* the judgment must ordinarily be a firm and stable one, the last word of the rendering court. *See Kosiel v. Arrow Liquors Corporation,* 446 Mich. Rptr. 374, at page 381, a decision from the Michigan Supreme Court in 1994.

Michigan Courts have applied the doctrine of *res judicata* broadly, prohibiting not only claims already

litigated, but every claim arising from the same transaction that the parties exercising reasonable diligence could have raised, but did not. *See Sewell v. Clean Cut Management, Inc.*, 463 Mich. Rptr. 569, at page 575, a decision from the Michigan Supreme Court in 2001.

It is well established in Michigan that *res judicata* applies to consent judgments. *See, e.g., Barraga Company v. State Tax Commission,* 243 Mich. Ct. App. Rptr. 452, at pages 455 through 456, a decision from the year 2000.

In this case, the State Court action was decided on the merits, and the parties were the same.

However, the Defendant argues that because the Plaintiff did not raise the discharge in State Court, he is now barred from doing so. This Court must disagree.

As the Sixth Circuit noted in *Hamilton,* Section 524(a)(2) makes it wholly unnecessary to assert the discharge injunction as an affirmative defense in a subsequent State Court action.

Here, that is precisely what the Defendant was arguing the Plaintiff was required to do.

Although *res judicata* could generally apply where a party has failed to raise an issue that could have been litigated, *Hamilton* recognizes an exception when the effect would be a waiver in contravention of Section 524(a).

The Court next considers whether the second

amended complaint fails to state a claim upon which relief can be granted for the first of the two loans.

As the Defendant notes in its motion, the second amended complaint states that the first of two loans from the Defendant to the Plaintiff occurred prior to the loan from the Federal government.

Taken in isolation, the second amended complaint might be viewed as not stating a claim, because the allegations are inconsistent with the documents attached to the complaint.

However, the second amended complaint also states that both loans were not for any educational purpose, and were thus not student loans that could be deemed non-dischargeable.

Taking the allegations in the complaint as true for purposes of a motion to dismiss under 12(b)(6), the second amended complaint plausibly states a claim upon which relief can be granted. *See Bell Atlantic Corporation v. Twombly,* 550 U.S. 544, at page 570, a decision from the U.S. Supreme Court in 2007; as well as *Ashcroft v. Iqbal,* 556 U.S. 662, at page 678, a decision from the Supreme Court in 2009.

Ultimately, of course, the Court may determine that the facts do not support the allegations that form the basis for the cause of action. However, on its face, the complaint properly alleges a cause of action for non-

dischargeability in violation of the discharge, regardless of whether it involves the first or the second loan.

Finally, the Defendant argues that the doctrine of laches provides an equitable defense to the Plaintiff's claims.

The Sixth Circuit has described laches as "a negligent and unintentional failure to protect one's rights." *See Elvis Presley Enterprises, Inc. v. Elvisly Yours, Inc.,* 936 F. 2d 889, at page 894, again a decision from the Sixth Circuit in 1991.

A party asserting laches must show lack of diligence by the party against whom the defense is asserted, and prejudice to the party asserting it. *See Herman Miller, Inc. v. Palazzetti Imports and Exports, Inc.,* 270 F. 3d 298, at page 320, a decision from the Sixth Circuit in 2001.

The Sixth Circuit has further explained that "laches does not result from a mere lapse of time, but from the fact that during the lapse of time changed circumstances inequitably worked to the disadvantage or prejudice of another, if the claim is now to be enforced."

"By his negligent delay, the Plaintiff may have misled the Defendant, or others, into acting on the assumption that the Plaintiff has abandoned his claim, or that he acquiesces in the situation, or changed circumstances may make it more difficult to defend against the claim." *See*

Chirco v. Crosswinds Communities, Inc., 474 F. 3d 227, at page 231, a decision from the Sixth Circuit in 2007.

The Court can consider an affirmative defense as part of a motion to dismiss, including the affirmative defense of laches. *See, e.g., Stein v. Regions Morgan Keegan Select High Income Fund*, 821 F. 3d 780, at page 786, a decision from the Sixth Circuit in 2016, where the Court noted that the basis for the defense must be shown by the facts in the complaint.

See also Lennon v. Seaman, 63 F. Supp. 2d 428, at page 439, a decision from the District Court for the Southern District of New York in 1999, where the Court required laches to be clear on the face of the complaint, and found that the plaintiff could not demonstrate any facts to counter the defense.

In the instant matter, the Defendant contends that laches should apply because the Defendant incurred legal fees and other administrative costs after entry of the State Court judgment, that record retention, witness availability issues, are a concern, as well.

As the Defendant concedes in its motion, however, none of these facts are addressed in the complaint. Therefore, insofar as the Defendant seeks dismissal due to laches, the motion is denied.

Of course, the Defendant may raise laches at

another stage of this proceeding where the facts are in issue.

For the foregoing reasons, the Court shall deny the motion to dismiss.

The Court shall enter an order consistent with its decision, providing the Defendant with 14 days to answer the second amended complaint.

I appreciate everyone dialing in this morning.

Are there any questions from the parties on a procedural nature with respect to the ruling?

MR. SPINNER: Ron Spinner here. No, Your Honor.

MR. SMITH: Austin Smith, Your Honor. No, Your Honor. Thank you.

THE COURT: Okay, very good. Thank you, gentlemen, and Ms. Palacios.

MS. PALACIOS: Thank you, Your Honor.

MR. SPINNER: Thank you, Your Honor.

(Time Not Noted)

* * * * *

CERTIFICATE

I, RANDEL RAISON, certify that the foregoing is a correct transcript from the official electronic sound recording of the proceedings in the above-entitled matter, to the best of my ability.

_____ November 10, 2017

Randel Raison