

NOT FOR COMMERCIAL PUBLICATION

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

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U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
CLEVELAND

In re:)	Case No. 01-22258
)	
FRANK X. GRESLEY and)	Chapter 13
LETHA A. GRESLEY,)	
)	Judge Pat E. Morgenstern-Clarren
Debtors.)	
)	<u>MEMORANDUM OF OPINION</u>
)	(NOT FOR COMMERCIAL PUBLICATION)

Letha Gresley was treated at Four Points Neck and Back Clinic, Inc. (Four Points) for injuries suffered in a car accident. She did not pay for the services rendered, but instead entered into an assignment agreement with Four Points. A few months later, she and her husband Frank filed this Chapter 13 case. After the debtors reached a tentative settlement of the personal injury claim, they moved for authority to settle the claim and distribute the proceeds in a fashion that would not pay any funds to Four Points. Four Points objected on the ground that a portion of the settlement proceeds (\$4,060.00) belongs to Four Points under the assignment. (Docket 17, 19).

The parties agreed to allow the settlement to be approved and some of the proceeds distributed. The disputed funds are being held in escrow pending resolution of the objection. The parties submitted the issue for decision on stipulated facts and briefs. (Docket 21, 22, 23, 24). For the reasons stated below, Four Points's objection to the motion is sustained.

JURISDICTION

Jurisdiction exists under 28 U.S.C. § 1334 and General Order No. 84 entered by the United States District Court for the Northern District of Ohio. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A) and (O).

FACTS

The debtors and Four Points stipulated that:

1. On or about February 22, 2001, Letha A. Gresley . . . sustained injuries in an automobile accident.
2. After the automobile accident, [Letha Gresley] sought treatment from Four Points Neck and Back Clinic, Inc., an Ohio professional corporation engaged in the practice of chiropractic medicine . . . Such treatment commenced in or about March 2001, and was completed in or about August 2001. Four Points invoiced Debtor \$4,060.00 for treatment, of which \$310.00 is the subject of dispute between the parties and is being separately negotiated.
3. In consideration for the agreement of Four Points to not require payment for treatment when rendered, [Letha Gresley], on March 23, 2001, executed the agreement captioned "Assignment" attached hereto as Exhibit A. [Letha Gresley] has not paid Four Points for invoiced services.
4. In 2001, as expressly permitted under Paragraph 1 of the Assignment, which states

I now assign, without any right to later revoke, a part of any proceeds from my claim equal to the fees incurred by me to [Four Points] for all treatment and other services rendered by [Four Points]. I am not assigning any legal cause of action in My Claim above, but only prospective proceeds. I also assign to [Four Points] my right to enforce the obligation of any insurance company to pay settlement proceeds for any settlement agreement made by or for me in exchange for my signing such insurance company's release of claim. Prior to settlement or other disposition of My Claim, I understand and permit [Four Points] to pursue payment from any other source but me personally, including medical payments coverage in an automobile liability policy. (first emphasis in original; second emphasis added)[,]

an employee of Four Points billed the Debtors['] auto insurer for "med-pay" for services rendered. The insurer sent a check for \$914.00 to Four Points (the "Geico Payment").

5. Debtors notified Geico that they disagreed with the Geico Payment being made to Four Points. Geico then notified Four Points that Geico had issued a stop payment order on the check Geico sent to Four Points. Geico then issued a new check for \$914.00 to Debtors.
 6. Four Points was listed as an unsecured creditor in Debtors' Chapter 13 proceeding.
 7. Four Points did not object to the Debtors' Chapter 13 plan.
 8. Four Points did not file a proof of claim in the Debtors' Chapter 13 plan.
- (Docket 23).

THE ISSUE

Is Four Points entitled to be paid from the settlement proceeds?

THE POSITIONS OF THE PARTIES

Four Points asserts that it is entitled to be paid from the settlement proceeds based on Letha Gresley's assignment of a portion of the settlement proceeds to it. The debtors argue that Four Points is not entitled to be paid because the assignment: (1) is not valid under Ohio law; (2) is invalid under bankruptcy law; and (3) if valid, was waived.

The validity of the assignment is key because Four Points did not file a claim in the debtors' bankruptcy case. As a result, if Four Points is merely an unsecured creditor it will not be paid under the plan.

DISCUSSION

Although the parties have not analyzed the matter in this fashion, the critical question is whether the disputed funds are property of the bankruptcy estate (in which case Four Points is not entitled to the money) or whether the funds instead became the property of Four Points at the time of the assignment (in which case Four Points is entitled to the money).

Property of a bankruptcy estate includes “all legal or equitable interests of the debtor in property as of the commencement of the case.” 11 U.S.C. § 541(a)(1). A debtor’s unliquidated prepetition personal injury claim is property of the bankruptcy estate. *See Cottrell v. Schilling (In re Cottrell)*, 876 F.2d 540, 542 (6th Cir. 1989). When the proceeds of such a claim are received postpetition by a Chapter 13 debtor, the proceeds are also property of the estate. *See for example In re Graham*, 258 B.R. 286, 288 (Bankr. M.D. Fla. 2001). The question here is whether Letha Gresley’s prepetition agreement with Four Points changes this result.

A. The Validity of the Assignment

The debtors argue that the agreement was not an assignment, but was instead only a contract to assign the proceeds in the future. Under their theory, Four Points does not have a property interest in the proceeds. State law controls this determination of property rights unless there is a countervailing federal interest. *See Kitchen v. Boyd (In re Newpower)*, 233 F.3d 922, 928 (6th Cir. 2000); *In re Richardson*, 216 B.R. 206, 215 (Bankr. S.D. Ohio 1997) (“Unless some paramount federal law controls the validity of [an] assignment, the validity of the assignment is determined by the law of the state in which the transfer takes place.”).

B. Ohio Law

The parties agree that Ohio provides the relevant state law for these purposes. Under Ohio law:

An assignment is a transfer to another of all or part of one's property in exchange for valuable consideration . . . No particular words are required to create an assignment. Rather, "[a]ny word or transaction which shows an intention on the one side to assign and on the other side to receive, if there is valuable consideration, will operate [to create an assignment]."

Hsu v. Parker, 688 N.E.2d 1099, 1101, 116 Ohio App.3d 629, 632 (Ct. App. 1996) (quoting *Grogan Chrysler-Plymouth, Inc. v. Gottfried*, 392 N.E.2d 1283, 1286, 59 Ohio App.2d 91, 96 (Ct. App.1978)) (citations omitted). In this case, the agreement unequivocally states that Letha Gresley intended to—and did—assign a part of the proceeds of her personal injury claim to Four Points in exchange for the medical services performed. The debtors' argument to the contrary flies in the face of the simple, direct language of the agreement.

Undeterred, the debtors next argue that a partial assignment of this type did not give Four Points a present property interest in the personal injury claim proceeds under Ohio law. In support, they rely on *Christmas's Adm's v. Griswold*, 8 Ohio St. 558 (Ohio 1858). The *Griswold* decision does not, however, address the effect of an assignment. Instead, it distinguishes (1) a covenant to apply a particular fund to pay a debt, from (2) an assignment, and holds that such a covenant does not operate as an assignment. That is not the situation in this case. Ohio law provides that a partial assignment conveys a property right in the assigned property at the time the assignment is made. See *Pittsburg, Cincinnati, Chicago & St. Louis Railway Co. v. Volkert*,

50 N.E. 924, 58 Ohio St. 362 (Ohio 1898) (Syllabus ¶ 2) (“Such assignment will convey to the assignee a property right in the judgment.”); *Hsu v. Parker*, 688 N.E.2d at 1102 (“Based on our ruling that a valid assignment had occurred, the client was not entitled to receive the full amount of the settlement.”). *See also In re Petry*, 66 B.R. 61 (Bankr. N.D. Ohio 1986) (discussing Ohio law on this issue). Consequently, Four Points acquired a property interest in the personal injury claim proceeds at the time Letha Gresley entered into the assignment. *Id.*

Four Points’s interest in the proceeds may be enforced: (1) in a suit at law with the consent of the debtor on the assigned debt; or (2) in equity as an equitable assignment. *See Volkert*, 50 N.E. at Syllabus ¶ 2. Ohio law also provides that a constructive trust will be imposed to protect an assignee to the extent it is necessary to prevent unjust enrichment:

If . . . the assignor does collect the claim, he is trustee of the proceeds for the assignee, because of a constructive trust which then arose to prevent unjust enrichment rather than because of any trust relationship created by the assignment itself.

6 Ohio Jur.3d , Assignments § 41 (1978). Under state law, therefore, a constructive trust exists to insure that Four Points is paid from the settlement proceeds and to prevent unjust enrichment.

C. The Bankruptcy Code

The debtors argue alternatively that if the assignment is valid under Ohio law, the equitable property interest which Four Points acquired cannot be recognized in bankruptcy. This argument, which is based on *XL/Datacomp, Inc. v. Wilson (In re Omegas Group, Inc.)*, 16 F.3d 1443 (6th Cir. 1994), is not persuasive.

Under Bankruptcy Code § 541(d), a debtor's estate does not include an equitable interest in property which is not the debtor's.¹ This provision would appear to exclude Four Points's interest in the settlement proceeds from the bankruptcy estate. The debtors contend, however, that the *Omegas Group* decision requires a different result. In *Omegas Group*, the Sixth Circuit stated that "a creditor's claim of entitlement to a constructive trust is not an 'equitable interest' in the debtor's estate existing prepetition, excluded from the estate under § 541(d)." *Id.* at 1451. The decision has been cited for the proposition that "a bankruptcy court cannot impose a constructive trust upon the debtor's assets unless a state court has determined . . . that one exists prior to the filing of the bankruptcy case." *In re Richardson*, 216 B.R. 206, 218 (Bankr. S.D. Ohio 1997). At first look, these decisions support the debtors' contention that this Court may not impose a constructive trust on the settlement proceeds to benefit Four Points.

The Sixth Circuit, however, later examined and explained the *Omegas Group* decision in *Poss v. Morris (In re Morris)*, 260 F.3d 654 (6th Cir. 2001), a case not cited by either party. The *Morris* decision makes it clear that while a mere claim of entitlement to the equitable remedy of a constructive trust does not place property outside the bankruptcy estate, a right to property based on a constructive trust that arises by operation of law before the bankruptcy filing is so excluded:

¹ Section 541(d) provides that:

Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest . . . becomes property of the estate under subsection (a)(1) . . . of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

11 U.S.C. § 541(d).

Essentially, Ohio courts will use the remedy of constructive trust "where there is some ground . . . upon which equity will grant relief." In these situations, Ohio law creates an equitable duty to convey property. Accordingly, every wrongful acquisition or holding of property will not give rise to a constructive trust. For example, breach of contract or failure to pay a debt without more cannot give rise to a constructive trust. Yet, a wrongful acquisition of or retention of property cognizable in equity will. Where an equitable duty to convey property exists, it is not necessary for a court to impress a constructive trust by decree. Rather, in Ohio it attaches by operation of law.

Morris, 260 F.3d at 668 (internal citations omitted). While the *Morris* decision dealt with the equitable duty to convey real property under Ohio law, the same logic applies to impose a similar duty with respect to the disputed settlement proceeds in this case.

In sum, Four Points obtained a property interest in the settlement proceeds under Ohio law before the debtors filed their bankruptcy case. Additionally, as a result of the assignment,

a trust [was] created in favor of [Four Points] on the fund, and [it] constitute[s] an equitable lien upon it. By other of the authorities such transfer is said to create an interest in the fund in the nature of an equitable property. By others it is denominated an equitable assignment. But whatever term is applied to it by way of description, the result reached is to give to [Four Points] a property right in the thing assigned, – a right which is cognizable and enforceable in a court of equity.

Volkert, 50 N.E. at 926 (citations omitted). Letha Gresley's personal injury claim proceeds were subject to a constructive trust for the benefit of Four Points before the debtors filed this Chapter 13 case. Consequently, the assigned settlement proceeds did not become property of the bankruptcy estate. See 11 U.S.C. § 541(d).

D. Waiver

The debtors' final alternative argument is that Four Points waived its rights under the assignment when it delivered the Geico Payment to Letha Gresley. Four Points, on the other hand, argues that it did not waive its rights but simply accommodated Letha Gresley. "Waiver as applied to contracts is a voluntary relinquishment of a known right." *White Co. v. Canton Transp. Co.*, 2 N.E.2d 501, 131 Ohio St. 190 (Ohio 1936) (Syllabus ¶ 1). The party asserting a waiver must prove it. *Id.* (Syllabus ¶ 4).

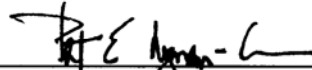
The parties' stipulations simply state that Four Points received a check for \$914.00 from Geico and that Geico stopped payment on the check when the debtors complained. (Stipulation ¶¶ 4 and 5). This stipulation is insufficient to prove that Four Points knowingly relinquished its assignment rights. Certainly it does not support the debtors' argument that "[after] Four Points was notified by [debtors'] counsel that [it] had no right to proceed against any funds without the consent of counsel, Creditor returned those funds to the Debtors." (Debtors' memorandum in opposition at page 6). The debtors failed to establish that Four Points waived its assignment rights.

CONCLUSION

For the reasons stated, the objection of Four Points Neck and Back Clinic, Inc. to the debtors' motion for authority to settle personal injury claim is sustained. Four Points is entitled

to be paid from the settlement proceeds.² A separate Order will be entered in accordance with this Memorandum of Opinion.

Date: 9 June 2003



Pat E. Morgenstern-Clarren
United States Bankruptcy Judge

Served by mail on: Burl Robinette, Esq.
Peter Igel, Esq.
John Lowry, Esq.
Craig Shopneck, Trustee

By: Joyce L. Gordon, Secretary

Date: 6/9/03

² The amount will be at least \$3,750.00. See Stipulation ¶2 concerning a dispute over the remaining \$310.00.

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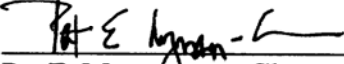
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In re:) Case No. 01-22258
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FRANK X. GRESLEY and) Chapter 13
LETHA A. GRESLEY,)
Debtors.) Judge Pat E. Morgenstern-Clarren
) **ORDER**
) (NOT FOR COMMERCIAL PUBLICATION)

For the reasons stated in the Memorandum of Opinion filed this same date,

IT IS, THEREFORE, ORDERED that the objection of Four Points Neck and Back Clinic, Inc. to the debtors' motion for authority to settle personal injury claim is sustained and Four Points is entitled to be paid from the settlement proceeds. (Docket 17, 19).

Date: 9 June 2003


Pat E. Morgenstern-Clarren
United States Bankruptcy Judge

Served by mail on: Burl Robinette, Esq.
Peter Igel, Esq.
John Lowry, Esq.
Craig Shopneck, Trustee

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