No. 21-1154

In the
Supreme Court of the United States

SPEECH & LANGUAGE CENTER, LLC AND
CHRYSSOULA MARINOS-ARSENIS,
Petitioners,
v.

HORIZON BLUE CROSS BLUE SHIELD OF NEW JERSEY,
Respondent.

**On Petition for Writ of Certiorari to the
to the Supreme Court of New Jersey**

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether the state courts erred in declining to issue an advisory ruling on what effect, if any, a federal bankruptcy judge in a hypothetical non-dischargeability proceeding might give to terms in a written settlement agreement which cited 11 U.S.C. § 523(a)(2) to reflect the parties' intent that the settlement debt be non-dischargeable based upon the Respondent's underlying fraud claims against the debtor.

RULE 29.6 DISCLOSURE

There is no parent or publicly held company owning 10% or more of Respondent Horizon Blue Cross Blue Shield of New Jersey's stock.

STATEMENT OF RELATED PROCEEDINGS

The following pending proceedings are related to this case: (1) Respondent's application to the Superior Court of New Jersey, Law Division to determine the amount of a judgment, including attorneys' fees and interest, relating to Petitioners' default in making payment under the parties' settlement agreement (Docket No. SOM-L-281-15); (2) Petitioners' applications to the Superior Court of New Jersey, Appellate Division, for leave to file an interlocutory appeal from the trial court's January 27, 2022 order and for a stay pending appeal (Docket No. A-355-21); (3) Petitioners' application to the Superior Court of New Jersey, Law Division, to dismiss the trial court's January 27, 2022 order because the trial court lacked jurisdiction to determine any settlement disputes after August 30, 2019 (Docket No. SOM-L-281-15).

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STATEMENT OF THE CASE

In 2014, Respondent Horizon Blue Cross and Blue Shield of New Jersey filed a Complaint against Petitioners alleging statutory fraud, pursuant to the New Jersey Insurance Fraud Prevention Act, N.J.S.A. § 17:33A-1 to -34, as well as common law counts of fraud, negligent misrepresentation, breach of contract, and unjust enrichment. The Complaint alleged that Petitioners engaged in a scheme to submit false and fraudulent insurance claims that resulted in millions of dollars in damages, subject to trebling.

After years of litigating the matter, the parties entered into settlement discussions and agreed to material settlement terms memorialized in writing (the "Term Sheet"), which were confirmed by Petitioners under oath and on the record before the trial judge in the Superior Court of New Jersey, Somerset County Law Division. The same proceeding "obligated [Petitioners'] execution of a written agreement that included the provisions in the term sheet, including the bankruptcy provision." (Pet. App. 8). In the event of default on the monthly payments owed, Petitioners specifically agreed that Respondent would be entitled to confess judgment for the full unpaid amount immediately due and owing, supported by stipulated language in the agreement, including Petitioners' agreement to execute documents in support of the judgment and their agreement not to contest Respondent's allegations. (Pet. App. 18). Relatedly, Petitioners agreed to language stating, "Ms. Arsenis agrees and intends that the judgment debt will be a non-dischargeable debt, pursuant to 11 U.S.C.

§ 523(a)(2) *in the event of a bankruptcy, or in any similar proceeding*." (Pet. App. 18) (emphasis added).[1] The Term Sheet provided that Respondent could pursue its reasonable fees upon Petitioners' default and would be permitted to use confidential information as necessary to "prosecute a non-dischargeability complaint in bankruptcy court relating to the [Petitioners'] settlement debt pursuant to 11 U.S.C. § 523(a)(2)." (Pet. App. 19).

Despite their agreement to do so promptly, Petitioners refused to execute written documents in accordance with the Term Sheet. Petitioners argued that provisions which were verbatim to the Term Sheet deviated from the agreement reached on the record. (Pet. App. 7-8). Petitioners did not support their claim with a factual certification. (Pet. App. 8-9).

In ruling on Respondent's motion to enforce litigant's rights, the Superior Court entered an Order on November 15, 2019, finding that the parties had reached a voluntary agreement approved by the Court on August 30, 2019, and that Petitioners were bound to sign documents containing references to fraud consistent with the Term Sheet. (Pet. App. 45-47). The court declined to rule on the agreement's effect on the dischargeability or non-dischargeability of the debt as "[t]hat determination is within the providence of the Bankruptcy Court." (Pet. App. 40).

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[1] The parties' Term Sheet initially had express references to the term "fraud", which Petitioners' counsel asked to have removed and proposed instead the bare citation to 11 U.S.C. § 523(a)(2) as having the same meaning. (Pet. App. 30, 32).

Petitioners appealed to the Superior Court of New Jersey, Appellate Division, which upheld the trial court's decision that Petitioners knowingly and voluntarily agreed to the references to fraud. (Pet. App. 8). The Appellate Division declined to decide the question of nondischargeability. (Pet. App. 10).

Petitioners sought review to the Supreme Court of New Jersey, which only granted review on the request to strike the bankruptcy citation in one section of the unsigned settlement agreement. After supplemental briefing and oral argument, the court vacated certification as "improvidently granted" and dismissed the appeal because "[t]he enforceability of section 3.8 of the settlement agreement – which states that 'the judgment debt will be a non-dischargeable debt, pursuant to 11 U.S.C. § 523(a)(2) in the event of a bankruptcy' – is for the Bankruptcy Court to resolve if a bankruptcy petition is filed." (Pet. App. 4).

REASONS FOR DENYING THE WRIT

The state courts correctly recognized the exclusivity of the future bankruptcy court to determine whether the settlement debt at issue will ultimately be found non-dischargeable pursuant to 11 U.S.C. § 523(a). Accordingly, the state courts declined to issue an advisory ruling that, should Petitioners ever file a bankruptcy petition in the future, a bankruptcy court would give no effect to settlement terms citing 11 U.S.C. § 523(a)(2) as an expression of the parties' intent that the settlement debt is non-dischargeable because it is traceable to the factual allegations underlying Respondent's fraud claims. The Petition at page 3, therefore, misleadingly asserts that "the New

Jersey courts enforced the provisions." There was, in fact, no determination below that the parties' agreement would be given issue preclusive effect in a future bankruptcy proceeding.

Bankruptcy is intended to provide "honest but unfortunate" debtors with a fresh start. *Cohen v. de la Cruz*, 523 U.S. 213, 217 (1998); *Grogan v. Garner*, 498 U.S. 279, 286-87 (1991) (citations and internal quotation omitted). The "fresh start", however, is unavailable to debts that arise on account of fraud. This Court has repeatedly stressed the breadth of the fraud exception under 11 U.S.C. § 523(a)(2), explaining that it encompasses debts "resulting from" or "traceable to" fraud. *Cohen*, 523 U.S. at 218 (quoting *Field v. Mans*, 516 U.S. 59, 61, 64 (1995)). The same principle applies with equal force to debts reduced to settlements. The agreed-to language can be referenced in a future bankruptcy proceeding to provide clarity on the issue of traceability of the settlement debt to Petitioners' fraudulent conduct, and Petitioners have not established otherwise. This is particularly important here, where the underlying state court complaint contained both fraud and non-fraud counts.

Petitioners further fail to establish how they are prejudiced by the state courts' decisions below to refrain from issuing an advisory ruling on arguments that may potentially be raised in a hypothetical, future bankruptcy proceeding. Although claiming that the provisions are "void" because they effectuate a waiver of rights, Petitioners fail to cite any decision of the courts which effectively impedes exercise of their rights under the Bankruptcy Code. Indeed, after initially

granting partial certification improvidently, the New Jersey Supreme Court dismissed the appeal because the dispute over references to Section 523(a)(2)'s discharge exemption for fraudulent debts "is for the Bankruptcy Court to resolve if a bankruptcy petition is filed." (Pet. App. 4). A bankruptcy court, therefore, retains discretion to reject consideration of the disputed language, whether it is stricken or not.

Petitioners' real concern is that they want the Court to relieve them of their voluntary agreement that the settlement debt be traceable to the fraudulent conduct alleged in the state court complaint. But that relief was requested and rejected under state law respecting settlement agreements, and the specific factual circumstances of the instant case. (Pet. App. 33). In rejecting that relief, the trial court, who was closely involved with the negotiations and the entry of the agreement on the record, stated:

> Based upon the Defendants' response, it can be said that there is no dispute that as part of the material terms, the Defendants agreed, by virtue of the specific language cited in the bankruptcy code § 523(a)(2), that the settlement debt was properly characterized as one that arose out of Horizon's claims based on Defendants' fraudulent conduct. Defendants' crafty wordsmithing to avoid their agreement should not prevail, as it was clear from the parties' negotiated terms, after extensive exchanges amongst counsel and the Court, that there be no confusion down the road that the settlement debt arose from Horizon's claims for

> fraud which were asserted in this state court action. What Defendants are apparently seeking now is to renege on their express and voluntary agreement [….]

(Pet. App. 33).

Moreover, no decision below actually opined on the so-called "conflict" among federal bankruptcy courts that Petitioners raise for the first time in this Court. The "conflict" raised by Petitioners is illusory at best and is contradicted by this Court's recognition that the doctrine of collateral estoppel may apply in bankruptcy cases. Without any actual conflict opinion, error in the law, or overriding need of public significance to compel the lower courts to issue an advisory ruling, the instant petition does not meet this Court's standards for the discretionary grant of certiorari.

Therefore, for all the reasons set forth herein, the petition should be denied.

ARGUMENT

A. The State Courts' Decisions Below, Which Decline To Pre-Determine Issues For A Future Bankruptcy Court, Do Not Warrant This Court's Review

The instant petition challenges the state courts' decision to "postpone" ruling on questions under the exclusive jurisdiction of the bankruptcy courts. (Pet. 11). Without a decision on the merits, Petitioners are unable to point to any ruling of law that is erroneous, contradicts the supreme federal law, or

opines on an actual conflict of law between higher courts.

The New Jersey Supreme Court issued an order determining certification was "improvidently granted" and declined to rule on a question that "is for the Bankruptcy Court to resolve if a bankruptcy petition is filed." (Pet. App. 1-2). Similar to this Court's discretionary standard for only granting certiorari in compelling cases, the New Jersey Supreme Court thoroughly reviewed the issue presented and made the rare decision to revoke certification after supplemental briefing and argument. That decision was compelled by the factual record below and the law establishing the federal bankruptcy court as the exclusive forum to determine non-dischargeability for fraud. That decision was also consistent with the Appellate Division, which found that the dispute "has no significance until [Mrs. Marinos-Arsenis] files a bankruptcy petition." (Pet. App. 9). The trial court likewise declined to address questions regarding non-dischargeability of the debt because the bankruptcy court has exclusive jurisdiction to decide such questions. (Pet. App. 40).

The state courts were correct in their understanding that the bankruptcy court has exclusive jurisdiction to make a final determination of a debt's non-dischargeability under 11 U.S.C. § 523(a)(2). This Court has held that dischargeability under § 523(a)(2) should not be determined outside the purview of the bankruptcy court, and to give finality to those rulings would undercut Congress' intention to commit such issues "to the jurisdiction of the bankruptcy court." *Brown v. Felsen*, 442 U.S. 127, 135-36 (1979). The

language at issue is incorrectly likened to cases involving self-executing prepetition waivers of the right to file for bankruptcy, to list obligations in the petition, or to exempt property from the automatic stay. But, an exemption under 11 U.S.C. 523(a)(2) is not self-executing. Because a debt arising from fraudulent conduct is not *ipso facto* non-dischargeable, Respondent would need to meet its burden of proof before the Bankruptcy Court under § 523(a)(2) after the filing of a complaint in an adversary proceeding. *See* 11 U.S.C. §523(c)(1); Fed. R. Bankr. P. 4007.

Against this statutory backdrop, Petitioners have not cited a single case that supports their claim that the state trial court was required to strike all references to the Bankruptcy Code citation for the fraud exemption (included at Petitioners' request), nor do Petitioners cite any decision that establishes the need for an advisory ruling from the state courts. Each of Petitioners' supporting cases were issued in the context of an actual bankruptcy proceeding where the creditor sought to enforce a prepetition waiver of rights without securing a post-petition affirmation of the non-dischargeability of the debt. This case, however, is not similarly postured to those matters.

Accordingly, there was no clear error of the state courts in abstaining from deciding questions that should be left to the exclusive providence of the Bankruptcy Court and therefore the petition should be denied.

B. Petitioners Have Failed To Establish A Conflict Of Law Actually Implicated By The State Courts' Decisions Below

Petitioners ask this Court to resolve a conflict that was not actually decided by the New Jersey state courts. The mere distinction between waiver and estoppel principles applied by bankruptcy courts is not shown to be a true "conflict" that mandates this Court's review at all, let alone in the context of the instant case.

1. This Court Has Held That Collateral Estoppel Applies In Bankruptcy Cases

As Petitioners recognize, this Court has previously held that the collateral estoppel doctrine can apply in dischargeability actions under 11 U.S.C. § 523(a). *See Grogan*, 498 U.S. at 285 ("[C]ollateral estoppel principles do indeed apply in discharge exception proceedings pursuant to § 523(a)."). If a creditor has reduced a fraud claim to a valid and final judgment, a bankruptcy court can properly give collateral estoppel effect to those elements of the claim that are identical to the elements required for discharge and which were actually litigated in the prior action for fraud. *Id*. This Court has also noted that "settlements ordinarily occasion no issue preclusion . . . unless it is clear . . . that the parties intend their agreement to have such an effect." *Archer v. Warner,* 538 U.S. 314, 322 (2003) (quoting *Arizona v. California,* 530 U.S. 392, 414 (2000)). That bankruptcy courts have "exclusive jurisdiction over dischargeability issues does not alter this rule." *Rally Hill Prods., Inc. v. Bursack (In re Bursack*), 65 F.3d 51, 53 (6th Cir. 1995). *See also*

Marrese v. Am. Acad. of Orthopaedic Surgeons, 470 U.S. 373, 380 (1985) ("[A] state court judgment may in some circumstances have preclusive effect in a subsequent action within the exclusive jurisdiction of the federal courts."); *Spilman v. Harley*, 656 F.2d 224, 227 (6th Cir. 1981) ("[T]hat Congress intended the bankruptcy court to determine the final result — [of] dischargeability or not — does not require the bankruptcy court to redetermine all the underlying facts."). The party seeking to invoke issue preclusion has the burden of establishing its applicability. *Hinze v. Robinson (In re Robinson)*, 242 B.R. 380, 385 (Bankr. N.D. Ohio 1999).

While there have been varying outcomes in cases where collateral estoppel has been raised with respect to prepetition litigation, the analysis has been guided by applicable state law. *See, e.g., Wolstein v. Docteroff (In re Docteroff)*, 133 F.3d 210, 214-15 (3d Cir. 1997) (finding collateral estoppel under state law principles based on a default judgment in a fraud action entered after the debtor actively litigated the case).

Not all courts may find that references to fraud in a settlement agreement incorporated into a final judgment are sufficient to meet the standards under state law for collateral estoppel. There are, however, instances where a settlement and judgment providing for the non-dischargeability of the debt have been given collateral estoppel effect in dischargeability proceedings against the debtor after a bankruptcy is filed. In so ruling, courts have indicated that the parties' stipulations of fact satisfied the elements of non-dischargeability under §523(a), and that there was

a clearly manifested intent that the stipulated fact be binding on the issue in future litigation. *See, e.g., Halpern v. First Georgia Bank (In re Halpern),* 810 F.2d 1061, 1062, 1064-65 (11th Cir. 1987) (finding consent judgment's stipulations of fact binding in dischargeability proceedings under §523(a)(2)); *Martin v. Hauck (In re Hauck)*, 489 B.R. 208, 214-16 (D. Colo. 2013), *aff'd*, 541 Fed. Appx. 898 (10th Cir. 2013), (finding agreement with stipulated judgment that incorporated by reference facts in the fraud complaint was sufficient for collateral estoppel under 11 U.S.C. §§523(a)(2) and (a)(4)). *See also Kohlenberg v. Baumhaft (In re Baumhaft),* 271 B.R. 517, 522-23 (Bankr. E.D. Mich. 2001) (applying collateral estoppel to conclude a debt was excepted from discharge pursuant to § 523(a)(2), with consideration of the parties' agreement providing that the debtor would not object to the dischargeability of the debt in any subsequent bankruptcy proceeding).

Petitioners have not established the existence of a conflict between waiver and estoppel principles that mandates this Court's review.

2. There Is No Confusion Created By This Court's Decision In *Brown v. Felson*

Contrary to Petitioners' claim, there is nothing about this Court's decision in *Brown* that contradicts the permissible application of collateral estoppel as recognized by this Court's decision in *Grogan*.

This Court's holdings in *Brown v. Felsen*, 442 U.S. 127 (1979), and *Archer v. Warner*, 538 U.S. 314 (2003), both establish that a debt which is otherwise

nondischargeable under 11 U.S.C. 523(a)(2) does not become dischargeable simply because the parties enter into a settlement agreement or consent judgment under which the amount of the debt is liquidated. *See Brown*, 442 U.S. at 138 ("[T]he mere fact that a conscientious creditor has previously reduced his claim to judgment should not bar further inquiry into the true nature of the debt."); *Archer*, 538 U.S. at 321 (allowing a bankruptcy court to look beyond the settlement agreement to fulfill Congress' intent "to ensure that all debts arising out of fraud are excepted from discharge, no matter what their form") (quotations omitted). *See also United States v. Spicer*, 57 F.3d 1152, 1156 (D.C. Cir. 1995) ("[A] fraudulent debtor may not escape nondischargeability, imposed as a matter of public policy by Congress…merely by altering the *form* of his debt through a settlement agreement.").

Indeed, a debtor who defrauds a creditor and then settles is no more honest than a debtor who defrauds a creditor and then loses at trial. Congress intended for "'the creditors' interest in recovering full payment of debts in [§ 523(a)'s exceptions from discharge to outweigh] the debtors' interest in a complete fresh start.'" *Cohen*, 523 U.S. at 222 (quoting *Grogan*, 498 U.S. at 287). Accordingly, a bankruptcy court may consider evidence extrinsic to the judgment and record of a prior state court suit when determining whether a debt reduced to judgment in the state court is dischargeable in bankruptcy. *See Brown*, 442 U.S. at 138-39.

3. Petitioners Ignore Acceptance Of Collateral Estoppel Principles In Their Own Supporting Cases

While there may be general language in each of Petitioners' cited cases that support the proposition that prepetition agreements which restrict a party's rights in a bankruptcy proceeding are void as a waiver of rights without a post-petition affirmation, the courts generally do not conclude their analysis there. Instead, the courts typically proceed with an analysis of collateral estoppel, and then if not satisfied, they may review additional proofs in support of the exemption.

In support of their so-called "conflict" analysis, Petitioners argue that this "Court should affirm rationale like the Ninth Circuit's in [*Bank of China v. Huang (In re Huang)*], 275 F.3d 1173 (9th Cir. 2002), which invalidated a provision very similar to those between Horizon and Ms. Arsenis." (Pet. 10). In that case, the Bankruptcy Court held that a settlement agreement's restraint on the debtor from entering bankruptcy and providing that the judgment and debt are not dischargeable was unenforceable as a waiver of rights. However, the court went on to recognize that if the debtor actually defrauded the Bank, then the debt would be non-dischargeable under 11 U.S.C. § 523(a)(2)(A)). *Id.* at 1177. The court stated that "the Bank must prove the fraud, unless the Bank succeeds by collateral estoppel." *Ibid.* Therefore, the court recognized that the prepetition agreements may still be referenced for evaluation of collateral estoppel during a nondischargeability proceeding. Ultimately, the court was critical that "[f]raud, or facts showing fraud, are

not mentioned in the Settlement Agreement or in the judgment enforcing it." *Id.* at 1178.

In contrast, here, the parties specifically negotiated the terms of the settlement agreement to refer to the claims sounding in fraud as the genesis for the settlement payment. The trial court's November 15, 2019 ruling confirmed this fact and Mrs. Arsenis never submitted a certification in contest. (Pet. App. 33). *In re Huang* supports the need to include a specific reference to the fraud exemption in prepetition agreements.

Petitioners also rely on *Hayhoe v. Cole (In re Cole),* 226 B.R. 647 (B.A.P. 9th Cir. 1998), addressing only its holding with regards to waivers of bankruptcy rights. (Pet. 10). However, Petitioners ignore the Ninth Circuit's discussion of collateral estoppel, and the key distinguishing fact "that the underlying debt that was the subject of the state court litigation was a mere business debt, and thus, dischargeable in bankruptcy." *Id.* at 650, n.5. There was no support found for the creditor's § 523(a)(2) claim beyond the settlement documents because the merits of the creditor's state court lawsuit against the debtor had nothing to do with actual fraud. *Id.* at 656-57. Therefore, the bankruptcy court declined collateral estoppel application on the basis of the settlement documents. *Ibid.*

Here, unlike the complaint allegations settled in *In re Cole*, Horizon's complaint is replete with allegations of fraud and is supported by the underlying evidence in the state court litigation. Those documents can be presented in full to the future Bankruptcy Court, who is free to independently weigh their sufficiency.

Crucially, the court in *In re Cole* observed a distinction with cases involving a stipulation to facts that support a finding of nondischargeability. *Ibid.* (citing *Klingman v. Levinson*, 831 F.2d 1292, 1296 n.3 (7th Cir. 1987)). In *Klingman*, the parties specifically agreed that the debt owed would "'not be dischargeable in any bankruptcy or similar proceeding and that in any subsequent proceeding all of the allegations of the Complaint and findings of this Court may be taken as true and correct without further proof." *Klingman*, 831 F.2d at 1296. The court found it "reasonable to conclude that the parties understood the conclusive effect of their stipulation in a future bankruptcy proceeding" and "therefore applied the principle of collateral estoppel and held that the debt was not dischargeable under 11 U.S.C. § 523(a)(4)." *Ibid.*

The decisions in *In re Cole* and *In re Huang* do not establish a conflict with *Klingman* or other cases evaluating whether issue preclusion applies. Rather, the very decisions that Petitioners rely upon make clear that the two tests are entirely distinct, and that collateral estoppel principles can indeed be evaluated against the facts of each case without running afoul of supreme federal law. Like the court in *Klingman*, a bankruptcy court may find that a voluntary agreement placed on the record is evidential for collateral estoppel purposes because it specifically provided that the debtor agreed and intended that the debt owed be deemed to arise from fraud.

Viewing the language that Petitioners agreed to, after extensive negotiations and with acknowledgement under oath on the record, a future bankruptcy court

could reasonably conclude that Petitioners understood the effect of their factual stipulation. Petitioner also agreed to default provisions that permitted Respondent's allegations to be accepted as true and without dispute by Petitioners. (App. 33, 42-43). If a future bankruptcy court does not find collateral estoppel, then Respondent would be free to submit its proofs of actual fraud under an ordinary preponderance of the evidence standard. *See Grogan*, 498 U.S. at 287 (ruling that a debtor does not have "an interest in discharge sufficient to require a heightened standard of proof" for provisions designed to exempt certain claims from discharge).

That said, each of the state courts below chose not to engage in hypothetical or advisory rulings on how a future bankruptcy court may proceed. The courts below were clear in their abstention from pre-determining what preclusive effect, if any, a bankruptcy court would give to the agreement and confession of judgment language. Because the courts did not err in rejecting Petitioners' invitation to invade the providence of the bankruptcy court to make a premature or advisory ruling, there is no compelling reason to disturb those decisions.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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