NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	BAP No. CC-04-1052-McBMa
JOHN W. ERNST,	Bk No. SV 99-20380-KL
Debtor.	Adv. No. SV 00-01260-KL
HOVANESIAN & HOVANESIAN, A PROFESSIONAL CORPORATION,	
Appellant,	
v.	**M E M O R A N D U M**[1]
JOHN W. ERNST,	
Appellee.	

Argued and Submitted on September 28, 2005
at Pasadena, California

Filed – November 21, 2005

Appeal from the United States Bankruptcy Court
for the Central District of California

Honorable Kathleen Thompson, Bankruptcy Judge, Presiding

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Before: McMANUS,[2] BRANDT, and MARLAR, Bankruptcy Judges.

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[1]This disposition is not appropriate for publication and may not be cited except when relevant under the doctrines of law of the case, res judicata, or collateral estoppel. See 9th Cir. BAP Rule 8013-1.

[2]Hon. Michael S. McManus, Chief Bankruptcy Judge for the Eastern District of California, sitting by designation.

This is an appeal from a final order granting the appellee's renewed motion for judgment on the pleadings and dismissing the appellant's complaint objecting to the appellee's discharge pursuant to 11 U.S.C. § 727. The bankruptcy court did not commit clear error when it found that an underlying state court action had been dismissed with prejudice, nor did the bankruptcy court err when it concluded that such dismissal deprived the appellant of standing to object to the appellee's chapter 7 discharge. We therefore AFFIRM the order granting the renewed motion for judgment on the pleadings.

FACTS

Before the appellee John W. Ernst filed his bankruptcy petition, the appellant Hovanesian & Hovanesian, a professional corporation, commenced a state court action against the appellee and other defendants, including the appellee's brother, Mark Ernst, and their business, Chatsworth Insurance Services ("CIS"). The action sought recovery for implied indemnity, negligence, and negligent misrepresentation in connection with the placing of the appellant's malpractice insurance policy with a company that later became insolvent.

When the appellee filed a chapter 13 petition, on September 2, 1999, the state court action was automatically stayed as to the appellee. On January 18, 2000, the appellee's case was converted to one under chapter 7.

Despite the fact that the appellee failed to list the appellant as a creditor and did not disclose the pending lawsuit in the statement of financial affairs, the appellant managed to

commence a timely adversary proceeding objecting to the appellee's discharge pursuant to 11 U.S.C. § 727(a)(2)(A), (a)(4)(A), and (a)(4)(D). The discharge complaint alleged, amongst other things, that the appellee knowingly failed to disclose in his schedules his 50% interest in his business, CIS, and cash on hand or on deposit.

The appellee denied these allegations and pointed out that in his initial schedules he listed his CIS shares with a value of $50,000. Also, the appellee later amended his schedules to change the value of his CIS interest to "none," to add the appellant as a creditor, and to list Mark Ernst as a co-debtor of the appellant.

With the appellee protected by the automatic stay, the state court action proceeded against his co-defendants, Mark Ernst and CIS. After the state court action went to arbitration, in a letter dated January 26, 2002, the arbitrator Judge Title granted the appellant's request to dismiss Mark Ernst and CIS from the action.[3]

The state court thereafter issued an Order to Show Cause ("the OSC") for "failure to submit and file a default judgment." At an April 29, 2002 hearing on the OSC, the state court dismissed the appellee. The dismissal minute order simply indicates that the appellee "is dismissed." The reasons given

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[3]Judge Title's fax transmission to counsel indicates: "Mr. Hovanesian further states in his letter that we 'should' dismiss this arbitration as to Mark Ernst and Chatsworth Ins. Services, Inc. . . . it is my order that this matter is dismissed with prejudice as to those defendants, leaving only John Ernst as a defendant, against who the action has been stayed because of his bankruptcy proceedings."

for the dismissal are not explained in the order and no transcript of the hearing has been included in the record for this appeal.

The dismissal of the state court action prompted the appellee to file a motion for judgment on the pleadings in the section 727 action. The basis for the motion was that the dismissal of the state court action precluded the appellant from arguing that it held a claim against the appellee's bankruptcy estate. Without a claim, it had no standing to seek denial of the appellee's chapter 7 discharge.

At a hearing on October 17, 2002, the bankruptcy court allowed the appellee additional time to present further evidence in support of the motion. When he presented nothing, the court denied the motion on January 8, 2003, on the basis that there was no evidence that the state court action had been adjudicated on the merits. After the denial of this motion, the appellee returned to state court and obtained an order clarifying the original minute order dismissing him from the state court action. The second state court order, dated April 30, 2003, provided that "the Defendant JOHN ERNST is dismissed with prejudice from this case." The court also interlineated the words "effective 4-29-02" indicating that such dismissal was effective from the date of the original minute order. With this new evidence, the appellee renewed his motion for judgment on the pleadings in the section 727 action. The bankruptcy court granted his motion on January 13, 2004 and the instant appeal ensued.

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JURISDICTION

The bankruptcy court had jurisdiction over the adversary proceeding pursuant to 28 U.S.C. §§ 1334 and 157(b)(1). The panel has jurisdiction over the appeal under 28 U.S.C. § 158(a)(1).

ISSUES

1. Whether the bankruptcy court committed clear error when it found that the state court action had been dismissed with prejudice.

2. Whether the bankruptcy court erred in concluding that the dismissal of the state court action precluded the appellant from asserting its claim against the appellee's bankruptcy estate and thereby depriving it of standing to object to the appellee's discharge pursuant to section 727.

STANDARD OF REVIEW

The bankruptcy court's findings of fact are reviewed for clear error and its conclusions of law are reviewed de novo. Higgins v. Vortex Fishing Sys., Inc., 379 F.3d 701, 705 (9th Cir. 2004), *quoting* Galam v. Carmel (In re Larry's Apt., LLC), 249 F.3d 832, 836 (9th Cir. 2001). We review de novo the preclusive effect of a judgment, which presents a mixed question of law and fact in which legal issues predominate. The Alary Corp. v. Sims (In re Associated Vintage Group, Inc.), 283 B.R. 549, 554 (9th Cir. BAP 2002).

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DISCUSSION

In the adversary proceeding, the appellee sought and obtained a judgment on the pleadings on the grounds that the dismissal of the appellee from the state court action was a retraxit, which operated as an adjudication on the merits of the appellant's claims, thereby depriving the appellant of its standing as a creditor to object to the appellee's discharge. The appellant contends that the state court dismissal was an involuntary dismissal for failure to prosecute, and therefore not a retraxit or an adjudication on the merits. Thus, it maintains that it is still a creditor with standing to object to the appellee's discharge in bankruptcy.

I

In its decision granting the appellee's motion for judgment on the pleadings, the bankruptcy court found that the state court dismissal was a retraxit, a common law term describing "an open and voluntary renunciation of the suit in open court." Rice v. Crow, 81 Cal. App. 4th 725, 733 (2002), *citing* Ghiringhelli v. Riboni, 95 Cal. App. 2d 503, 506 (1950). A voluntary dismissal with prejudice is the modern-day equivalent of the common law doctrine of retraxit. According to Black's Law Dictionary, a retraxit is the following:

> A plaintiff's voluntary withdrawal of the lawsuit in court so that the plaintiff forfeits the right of action. In modern practice, retraxit is called *voluntary dismissal with prejudice*.

Black's Law Dictionary, 1342 (8th ed. 2004) [emphasis in original].

Ascertaining whether the dismissal of the state court action was a retraxit or an involuntary dismissal is not a simple task. The minute order dismissing the action states only that the appellee "is dismissed."[4] There is no mention of whether the dismissal was voluntary or involuntary, or with or without prejudice.

The appellant asserts that the dismissal of the appellee from the state court action was based on his failure to submit a default judgment. It argues that it opposed the dismissal at the hearing. Hence, the dismissal was involuntary and therefore without prejudice and not a disposition on the merits.

Pursuant to Cal. Civ. Proc. Code § 581(g) and (h), a court may dismiss a complaint for any inexcusable delay in prosecuting the complaint. Cal. Civ. Proc. Code § 581(g) & (h); see B.E. Witkin, California Procedure, Proceedings Without Trial §§ 341 & 458 (4th ed. 1997).[5] Such dismissals are without prejudice to a further action by the plaintiff. Id. Thus, if the dismissal was

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[4]The entirety of the text of the minute order is as follows:

> Nature of Proceedings:
> OSC Re: Failure to Submit and File a Default Judgment
> Matter is called for hearing.
> Counsel argue.
> Defendant John Ernst is dismissed from this case.
> Matter is continued to 5-3-02 at 8:30 a.m. in this department.

[5]While failure to file a default judgment previously constituted an independent ground for dismissal under former Cal. Civ. Proc. Code § 581a(c), that statute was repealed in 1984. Cal. Civ. Proc. Code § 467. A dismissal for delay in entering a default judgment is now incorporated into the general provisions regulating dismissal for failure to prosecute. Id. (citation omitted).

involuntary, as the appellant argues, then the dismissal was without prejudice.

The appellee counters that the OSC for failure to prosecute was not issued with reference to the appellee. Rather, the OSC was issued due to the appellant's failure to file proof that process had been served and/or to request default judgments against the other defendants in the action.[6]

Indeed, the issuance of the OSC did not likely involve the appellee. He was protected by the automatic stay, a fact that had previously been noted by the state court in connection with the mandated arbitration. Consequently, because the automatic stay enjoined prosecution of the case against the appellee, it is difficult to believe that the state court would threaten to dismiss the appellant's case against the appellee because of a failure to prosecute it.

The appellee further asserts that at the hearing on the OSC, the state court judge noted that the appellant had voluntarily dismissed Mark Ernst and CIS from the action and inquired whether the appellant wished to dismiss the claims against the appellee as well. According to the appellee, the appellant agreed to voluntarily dismiss him from the state court action and, as a result, the dismissal was with prejudice.

Neither the appellant's nor the appellee's version of what transpired at the OSC hearing can be verified because neither

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[6]According to the appellee, the OSC was issued because the appellant had failed to "tidy up either the services of process or the defaults on the other 25 named defendants." Appellee's Brief at 9, n. 2.

party provided a transcript of that hearing to the bankruptcy court.

As noted above, the language of the state court minute order dismissing the appellee is likewise of no assistance in determining the basis for the dismissal. As it turns out, that minute order was also ineffective. Cal. Civ. Proc. Code § 581d provides that a dismissal ordered by the court "shall be in the form of a written order signed by the court and filed in the action." Id. Here, the minute order was not signed by the judge, and therefore was not effective. Cal. Civ. Proc. Code § 581d; see B.E. Witkin, California Procedure, Judgment § 49 (4th ed. 1997).

However, the minute order's ambiguity and the lack of signature were rectified when the state court filed another order on April 30, 2003. That order was signed and provided that the action against the appellee had been dismissed with prejudice, effective April 29, 2002.

The fact that the April 30, 2003 order specifies that the dismissal was with prejudice suggests that the appellee must have requested the dismissal. After all, and as noted by the appellant, an involuntary dismissal is generally without prejudice under California procedure. And, the nature of the dismissal was something the state court obviously deliberated upon. Not only did it enter a second order clarifying that the dismissal was with prejudice, the state court added text to the second order indicating that such dismissal was effective April 29, 2002.

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Other facts support the conclusion that the dismissal was voluntary. First, the appellant did not appeal or otherwise attack the April 30, 2003 state court order even though it unambiguously provides that the dismissal was with prejudice. Second, the voluntary dismissal of the appellee's brother and CIS supports the inference that the dismissal of the appellee was also voluntary.[7]

Finally, other than the language of the OSC, the appellant failed to present any evidence to the bankruptcy court demonstrating that the appellee's dismissal was involuntary. If the appellant had not requested the dismissal at the state court OSC hearing, the transcript of that hearing would have shown this to be the case. Yet, the appellant did not produce that transcript.

The appellant further argues that "no hearing was noticed or held in connection with this second order of dismissal." However, the appellant does not dispute that the April 30, 2003 order was entered by the state court. If a hearing was necessary before entry of the order, the appellant should have appealed or otherwise challenged the April 30, 2003 order in state court. It did not. And, given that California law prohibits unsigned minute orders dismissing actions, the April 30, 2003 order was the first and only effective order issued by the state court. No

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[7]In his fax transmission, Judge Title states as to Mark Ernst and CIS that: "While ambiguous, it appears reasonable to assume that [plaintiff] is now dismissing as to those defendants with prejudice as per the previous dismissal form which he sent me. Any such dismissal must under the circumstances be considered to be with prejudice in view of the impending trial date."

authority has been cited by the appellant to support its contention that the state court was required to hold a hearing to decide the form of its order.

The appellant also contends that "[a]dding the words 'with prejudice' after one year to the earlier Order of dismissal entered April 29, 2002, adds nothing." The appellant cites Goddard v. Security Title Ins. & Guarantee Co., 14 Cal. 2d 47 (1939), for the proposition that a mere statement in a dismissal order that it is with prejudice is not conclusive. In Goddard, the court held that a judgment based on the sustaining of a special demurrer for defects in form is not an adjudication on the merits for res judicata purposes, even when the dismissal order recites that it is with prejudice. Id. at 52 (citations omitted).

Here, unlike in Goddard, the appellant failed to present any evidence beyond the language of the OSC that the dismissal was not on the merits. The appellant's dismissive attitude toward the April 30, 2003 order has continued in its appeal and is reflected in its argument that the appellee "did not present any new or further evidence to support the same contentions that were proffered in his first motion which was denied by the [bankruptcy] court . . . ." Appellant's Opening Brief at 6. This is factually incorrect. The appellee submitted the April 30, 2003 order with his renewed motion for judgment on the pleadings.

Therefore, the bankruptcy court's finding that the underlying state court action had been dismissed voluntarily and with prejudice is supported by the record of the state court

action, at least to the extent that record was made available to the bankruptcy court. That is, based on the wording of the April 30, 2003 order, the appellant's failure to appeal such order, the voluntary dismissal of the appellee's brother and CIS, the bankruptcy court did not commit clear error in finding that the state court dismissal was voluntary and with prejudice.

II

The bankruptcy court was required to give full faith and credit to the state court order dismissing the action. See 28 U.S.C. § 1738. This means that whatever preclusive effect the order would have in a subsequent state court action also had to be accorded in any proceeding filed in the bankruptcy court. See Smyth v. City of Oakland (In re Brooks-Hamilton), 329 B.R. 270, 279 (9th Cir. BAP 2005), *citing* In re Nourbakhsh, 67 F.3d 798, 800 (9th Cir. 1995).

Under California law, the doctrine of claim preclusion applies when the following requirements are met:

> 1) a claim or issue raised in the present action is identical to a claim or issue litigated in a prior proceeding;
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> 2) the prior proceeding resulted in a final judgment on the merits; and
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> 3) the party against whom the doctrine is being asserted was a party or in privity with a party to the prior proceeding.

In re Brooks-Hamilton, 329 B.R. at 279, *citing* Brinton v. Bankers Pension Serv., Inc., 76 Cal. App. 4th 550, 556 (1999).

Here, the appellant disputes the second factor, arguing that the dismissal was without prejudice and therefore it continued to

hold a claim against the appellee and had standing to seek the denial of the appellee's chapter 7 discharge. However, the premise of this argument is false. The state court ordered the dismissal of the state court action with prejudice. It therefore was an adjudication on the merits of the appellant's claim against the appellee. See Johnson v. County of Fresno, 111 Cal. App. 4th 1087, 1095 (2003).

The claim the appellant was attempting to preserve in the appellee's bankruptcy case was the same claim that was dismissed with prejudice by the state court. The state court action involved the same parties. Consequently, all three elements of claim preclusion are present. The appellant had no claim against the appellee when the adversary proceeding was dismissed by the bankruptcy court.[8]

III

As noted by the bankruptcy court in its ruling, in order for a case to be adjudicated in federal court, "an actual controversy

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[8]At the hearing on the renewed motion for judgment on the pleadings, the appellant acknowledged that he has no further remedy in state court:

THE COURT: You and I know that you can't go back and resurrect this case in state court, or at least that's my belief; that the way you get past this result is that you demonstrate that in state court you still got a cause of action, because you don't, under California law. And you don't have an independent cause of action under bankruptcy law.

MR. HOVANESIAN: Even without the dismissal with prejudice, we would not have a cause of action that would stand up to challenge because we'd be barred at this point by the statute of limitations.

must be extant at all stages of review, not merely at the time the complaint is filed." Arizonans for Official English v. Arizona, 520 U.S. 43, 45 (1997), *quoting* Preiser v. Newkirk, 422 U.S. 395, 401 (1975).

Pursuant to section 727(c)(1), only the trustee, a creditor, or the United States Trustee may object to the granting of a debtor's discharge. 11 U.S.C. § 727(c)(1). A creditor is defined in the Bankruptcy Code as "an entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor." 11 U.S.C. § 101(10)(A). A claim, in turn, is a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or . . . an equitable remedy for breach of performance . . . ." 11 U.S.C. § 101(5)(A).

In order to file an objection to a debtor's discharge, a creditor must have a claim that will be affected by the debtor's discharge. See Stanley v. Vahlsing (In re Vahlsing), 829 F.2d 565, 567 (5th Cir. 1987), *citing* In re Chandler, 138 F. 637 (7th Cir. 1905).

In re Vahlsing involved an appeal by a debtor of the bankruptcy court's denial of discharge at the behest of a creditor. In re Vahlsing, 829 F.2d at 567. The judgment in favor of the creditor was entered even though the bankruptcy court had previously modified the automatic stay to permit the creditor to proceed with its claim against the debtor in state court. But the state court resolved the claim in favor of the debtor. Id. at 566.

In reversing the judgment of the bankruptcy court, the Fifth Circuit concluded that once the claim of the "would-be creditor" had been dismissed by the state court, there was no possibility that the grant or denial of a discharge could affect the putative creditor's interests. Id. at 567.[9] Therefore, the creditor lacked standing to continue with its adversary proceeding to deny the debtor's discharge.

The appellant asserts that In re Vahlsing is distinguishable because in that case there was a full evidentiary hearing in state court. The appellant's argument is misplaced. Here, like in In re Vahlsing, the appellant's claim was dismissed in the state court. Whether the dismissal followed a full evidentiary hearing or not, under California law, it is dispositive of the appellant's claim against the appellee. See Torrey Pines Bank v. Superior Court, 216 Cal. App. 3d 813, 820 (1989).

The appellant also argues that he has maintained his creditor status because a claim need not be adjudicated in state court in order for it to be a valid claim in a bankruptcy case. In support of this assertion, the appellant cites First Commercial Fin. Group, Inc. v. Hermanson (In re Hermanson), 273 B.R. 538 (Bankr. N.D. Ill. 2002), for the proposition that a creditor has standing to object to a debtor's discharge even

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[9]See also Jeffrey M. Goldberg & Assocs., Ltd. v. Holstein (In re Holstein), 299 B.R. 211, 225, n.13 (Bankr. N.D. Ill. 2003) ("Some courts have denied a creditor standing when the automatic stay had been modified to permit the creditor to pursue his claim in another court, and the creditor did so and lost" (citations omitted)); see generally 6 Collier on Bankruptcy ¶ 727.14[1], p. 727-62, 63 (Alan N. Resnick & Henry J. Sommer eds., 15th ed. rev. 2005)(citations omitted).

though its claim may be disputed and not yet liquidated or fully adjudicated.

In re Hermanson is distinguishable from the present case, however, because the appellant's claim is no longer subject to any dispute. The appellant's claim does not exist. It has been dismissed with prejudice, and therefore adjudicated on the merits. The appellant no longer has a right to payment, and hence has no claim that could be affected should the appellee's discharge be denied. Without his creditor status, the appellant does not have standing to challenge the appellee's discharge under section 727.

CONCLUSION

Based on the April 30, 2003 order dismissing the underlying state court action with prejudice, the bankruptcy court did not clearly err when it found that the dismissal of the state court action was voluntary and with prejudice. Further, given that the dismissal was with prejudice, the bankruptcy court properly concluded that the doctrine of claim preclusion barred any subsequent action in state court and deprived the appellant of his status as a creditor in the bankruptcy proceeding. Accordingly, the appellant lacked standing to continue with its objection to the appellee's discharge. The panel therefore AFFIRMS the bankruptcy court's granting of the appellee's renewed motion for judgment on the pleadings and dismissal of the appellant's section 727 adversary proceeding.