

SEP 04 2009

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U.S. BKCY. APP. PANEL  
OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	)	BAP No.	NC-08-1302-JuMkD
	)		
STEVEN THOMPSON;	)		
ASTER KIFLE-THOMPSON,	)	Bk. No.	07-50303
	)		
Debtors.	)	Adv. No.	07-05070
	)		
-----	)		
STEVEN THOMPSON;	)		
ASTER KIFLE-THOMPSON,	)		
	)		
Appellants,	)		
	)		
v.	)	<b>M E M O R A N D U M</b> <sup>1</sup>	
	)		
MONTEREY MUSHROOMS, INC.,	)		
	)		
Appellee.	)		
-----	)		

Argued and Submitted on July 30, 2009  
at San Francisco, California

Filed - September 4, 2009

Appeal from the United States Bankruptcy Court  
for the Northern District of California at San Jose

Hon. Roger L. Efremsky, Bankruptcy Judge, Presiding

<sup>1</sup> This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have (see Fed. R. App. P. 32.1), it has no precedential value. See 9th Cir. BAP Rule 8013-1.

1 Before: JURY, MARKELL, and DUNN, Bankruptcy Judges.

2 Pro se<sup>2</sup> appellant-debtors Steven Thompson and Aster Kifle-  
3 Thompson (collectively "Debtors") appeal the bankruptcy court's  
4 judgment in favor of appellee, Monterey Mushrooms, Inc.  
5 ("Monterey") in a nondischargeability proceeding.

6  
7 The bankruptcy court applied the doctrine of issue  
8 preclusion, finding that Monterey's state court judgment for  
9 insurance fraud conclusively established the elements for fraud  
10 and willful/malicious conduct under § 523(a)(2)(A) and (a)(6)<sup>3</sup>  
11 and, therefore, Debtors were precluded from relitigating those  
12 elements in the bankruptcy court. Accordingly, the court held  
13 that Monterey's \$1,709,155 debt was nondischargeable.  
14

15 For the reasons set forth below, we AFFIRM.

16 **I. FACTS**

17 Monterey was a grower, distributor, and wholesaler of  
18 mushrooms, and was self-insured for its workers' compensation  
19 insurance obligations. Debtors were licensed chiropractors  
20 whose medical corporations provided treatment to Monterey  
21 employees for job-related injuries.  
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23  
24 <sup>2</sup> We construe liberally the pleadings of pro se appellants.  
25 Kashani v. Fulton (In re Kashani), 190 B.R. 875, 883 (9th Cir.  
BAP 1995).

26 <sup>3</sup> Unless otherwise indicated, all chapter, section and rule  
27 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and  
to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037.



1 Thompson; his wife, Aster Kifle-Thompson; Charles Salzberg,  
2 M.D.; Joseph Greenspan, M.D.; and Julius Mueller, M.D. – had  
3 participated in a scheme in which they submitted false claims  
4 for workers' compensation payments to Monterey. According to  
5 the complaint, Thompson had organized two corporations,  
6 Peninsula Medical Group, P.C. ("PMG"), and Integrated Family  
7 Medical Group, P.C. ("IFMG"), using Salzberg and Greenspan,  
8 respectively, as medical directors.  
9

10 The court held a bench trial on liability between  
11 September 11 and 24, 2002. The court granted nonsuit in favor  
12 of Mueller, and both Greenspan and Salzberg settled with  
13 Monterey. The court found Debtors and their wholly-owned  
14 corporate defendants liable for having "set up sham  
15 corporations, with medical doctors as ostensible owners, that  
16 presented to the public as full-service medical clinics."  
17

18 The court concluded that the medical doctors were  
19 essentially a series of absentee figureheads who gave no  
20 consideration for their ownership interests and, for the most  
21 part, had no meaningful role in the direction of patient care or  
22 general clinic operation. According to the court, Debtors'  
23 purpose for forming the corporations was to acquire patients and  
24 refer them for chiropractic treatment and to present fraudulent  
25 claims for services to third-party payors. The result was that  
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1 patients were "inevitably being directed to chiropractic  
2 'treatment,' where they were grossly over[-]treated."

3 Bills were generated for these patient visits, and in some  
4 cases more than one claim was made for a single session. The  
5 court concluded that these facts demonstrated a "sophisticated,  
6 formalized and well-concealed strategy" that enabled Debtors to  
7 "maximize the number of patients and the amount [that] could be  
8 billed for visits, without due regard for patient care and  
9 needs."  
10

11 Meanwhile, Debtors maintained control of PMG and IFMG  
12 through their management corporation, Nevada Practice Management  
13 Systems, Inc., in order to "siphon off the profits" earned by  
14 PMG and IFMG.  
15

16 The court held a trial on the remedies portion of the  
17 litigation on November 6, 2002. On December 3, 2002, the court  
18 ruled that Debtors and their corporate entities were jointly and  
19 severally liable for civil penalties in the amount of  
20 \$479,115.29. The court also granted Monterey's request for  
21 injunctive relief and subsequently awarded Monterey attorneys  
22 fees in the amount of \$1,230,040.  
23

24 At Debtors' request, the trial court issued its Statement  
25 of Decision on March 18, 2003.  
26  
27

1 Debtors appealed to the California Court of Appeal, Sixth  
2 District, which affirmed the trial court's judgment. Monterey  
3 Mushrooms, Inc., 136 Cal. App. 4th 24 (Cal. Ct. App. 2006).  
4 Further review was denied by the California and United States  
5 Supreme Courts, and the judgment is final. No portion of the  
6 judgment has been paid.  
7

8 **B. The Bankruptcy Court Proceeding**

9 Debtors filed their chapter 7 petition on February 5, 2007.

10 On March 4, 2007 Monterey filed an adversary complaint to  
11 determine whether the debt arising from the state court judgment  
12 was nondischargeable under § 523(a)(2)(A), (a)(4), and (a)(6).  
13 On July 14, 2008 Monterey filed a Motion For Summary Judgment,  
14 asking the bankruptcy court to determine its state court  
15 judgment was nondischargeable under the doctrine of issue  
16 preclusion.<sup>7</sup>  
17

18 On November 6, 2008 the bankruptcy court ruled orally that  
19 the requirements for application of issue preclusion were met,  
20 precluding Debtors from relitigating the issue of fraud under  
21 § 523(a)(2)(A). The court stated:  
22

23 First, Debtors knowingly made false representation by  
24 submission of fraudulent Articles of Incorporation and

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25 <sup>7</sup> Monterey's brief uses the old style term "collateral  
26 estoppel" as the basis for its summary judgment argument. We use  
27 the more modern term "issue preclusion", as did the bankruptcy  
28 court.

1 fictitious business name permit applications. Second,  
2 Debtors held themselves out as medical clinics through  
3 invoices, liens and related documents; i.e., made  
4 false representations. Third, Debtors engaged in  
5 fraudulent billing practices.

6 The court also concluded that

7 Debtors acted with the intent to defraud by presenting  
8 and pursuing fraudulent claims for payment within the  
9 meaning of Penal Code Section 550. Furthermore,  
10 Debtors' invoices were calculated to deceive.

11 Finally, the court determined that Monterey was the target of  
12 fraudulent billing practices and suffered damage as a result.

13 In addition, the court concluded that the doctrine of issue  
14 preclusion applied to Monterey's claim for relief under  
15 § 523(a)(6). The court ruled that "the State Court found  
16 Debtors necessarily intentionally caused injury without just  
17 cause because the State Court found Debtors had committed fraud.  
18 This is sufficient for Section 523(a)(6)."

19 Finally, the court decided that the elements under  
20 § 523(a)(4) had not been met.

21 The court granted Monterey's Motion for Summary Judgment  
22 under § 523(a)(2)(A) and (a)(6) and denied the motion under  
23 § 523(a)(4) by order entered on December 16, 2008. The judgment  
24 in favor of Monterey was entered on January 23, 2009.

25 Debtors timely appealed the bankruptcy court's judgment.  
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**II. JURISDICTION**

The bankruptcy court had jurisdiction over this proceeding under 28 U.S.C. §§ 1334 and 157(b)(2)(I). We have jurisdiction under 28 U.S.C. § 158.

**III. ISSUES**

A. Whether the bankruptcy court erred in holding that the state court judgment for insurance fraud was a nondischargeable debt under § 523(a)(2)(A).

B. Whether the bankruptcy court erred in holding that the state court judgment for insurance fraud was a nondischargeable debt under § 523(a)(6).

**IV. STANDARDS OF REVIEW**

Since this case arises on summary judgment, the standard of review is de novo. Marshack v. Orange Comm'l Credit (In re Nat'l Lumber & Supply, Inc.), 184 B.R. 74, 77 (9th Cir. BAP 1995).

"[S]ummary judgment is proper 'if the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.'" Celotex Corp. v. Catrett, 477 U.S. 317, 322 (1986). In making this determination, conflicts are resolved by viewing all facts and

1 reasonable inferences in the light most favorable to the  
2 non-moving party. United States v. Diebold, Inc., 369 U.S. 654,  
3 655 (1962).

4 On appeal we may affirm the bankruptcy court on any ground  
5 supported by the record, even if it differs from the bankruptcy  
6 court's stated rationale. Pollard v. White, 119 F.3d 1430, 1433  
7 (9th Cir. 1997).  
8

#### 9 V. DISCUSSION

10 The doctrine of issue preclusion applies to bankruptcy  
11 dischargeability proceedings. Grogan v. Garner, 498 U.S. 279,  
12 284 (1991). Monterey had the burden of proving that the  
13 elements for issue preclusion were met. See Kelly v. Okoye  
14 (In re Kelly), 182 B.R. 255, 258 (9th Cir. BAP 1995), aff'd,  
15 100 F.3d 110 (9th Cir. 1996). To sustain this burden, Monterey  
16 must have introduced "a record sufficient to reveal the  
17 controlling facts and pinpoint the exact issues litigated in the  
18 prior action." Kelly, 182 B.R. at 258. "Any reasonable doubt as  
19 to what was decided by a prior judgment should be resolved  
20 against allowing the [issue preclusion] effect." Id.  
21  
22

23 Whether the state court judgment has a preclusive effect is  
24 determined under California law. See Gayden v. Nourbakhsh  
25 (In re Nourbakhsh), 67 F.3d 798, 800 (9th Cir. 1995).  
26  
27  
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1 In California, issue preclusion may be applied when (1) the  
2 issue decided in the prior suit is identical to the issue  
3 presented in the second action; (2) the issue was actually  
4 litigated in the prior suit; (3) the issue was necessarily  
5 decided in the prior suit; (4) there was a final judgment on the  
6 merits in the prior suit; and (5) the party against whom  
7 preclusion is sought was a party, or in privity with a party, to  
8 the prior suit. Lucido v. Superior Court, 51 Cal. 3d 335, 337  
9 (1990). And, even if all these requirements are met, issue  
10 preclusion should only be applied when the public policies  
11 underlying the doctrine would be furthered. Id. at 354.  
12

13  
14 There is no dispute that Debtors were parties in the  
15 underlying state court action or that the disposition is final  
16 since Debtors have exhausted all direct attacks on the judgment.  
17 Therefore, the remaining questions before us are whether the  
18 issues litigated in the state court are identical to those in a  
19 nondischargeability proceeding under § 523(a)(2)(A) and (a)(6)  
20 and whether those issues were actually litigated and necessarily  
21 decided in the state court.<sup>8</sup>  
22

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25 <sup>8</sup> To determine whether there is an identity of issues, we  
26 compare the elements under § 523(a)(2)(A) and (a)(6) with the  
27 elements under the California Penal Code sections encompassed by  
28 Cal. Ins. Code § 1871.7 and examine the state court's findings of  
fact and legal rulings.

1 The burden of proof in the state court action was the same  
2 as that for nondischargeability – preponderance of the evidence.  
3 Monterey Mushrooms, Inc., 136 Cal. App. at 37-38; Grogan, 498  
4 U.S. at 291.

5 **A. Section 523(a)(2)(A)**

6 Under § 523(a)(2)(A), a debt for services obtained by  
7 “false pretenses, a false representation, or actual fraud” is  
8 nondischargeable.  
9

10 To establish a debt as nondischargeable on any of these  
11 grounds, a creditor must show: (1) a misrepresentation,  
12 fraudulent omission, or deceptive conduct by the debtor;  
13 (2) knowledge of the falsity or deceptiveness of his statement  
14 or conduct; (3) an intent to deceive; (4) justifiable reliance  
15 by the creditor on the debtor’s statement or conduct; and  
16 (5) damage to the creditor proximately caused by his reliance on  
17 the debtor’s statement or conduct. Turtle Rock Meadows Home  
18 Owners Ass’n v. Slyman (In re Slyman), 234 F.3d 1081, 1085  
19 (9th Cir. 2000).  
20

21 Cal. Penal Code § 550 makes it illegal to knowingly  
22 prepare, present and pursue false or fraudulent insurance  
23 claims, or to make oral or written statements to support them or  
24 to conceal information which affects entitlement to the  
25 insurance benefit claimed, with intent to defraud. Cal. Penal  
26  
27

1 Code § 550(a)(1), (5), (6), (7), (b)(1)-(3).<sup>9</sup> Cal. Penal Code

2  
3 <sup>9</sup> Cal. Penal Code § 550 states in relevant part:

4 (a) It is unlawful to do any of the following, or to aid, abet,  
5 solicit, or conspire with any person to do any of the following:

6 (1) Knowingly present or cause to be presented any  
7 false or fraudulent claim for the payment of a loss or  
8 injury, including payment of a loss or injury under a  
9 contract of insurance.

10 . . . .

11 (5) Knowingly prepare, make, or subscribe any writing,  
12 with the intent to present or use it, or to allow it to  
13 be presented, in support of any false or fraudulent  
14 claim.

15 (6) Knowingly make or cause to be made any false or  
16 fraudulent claim for payment of a health care benefit.

17 (7) Knowingly submit a claim for a health care benefit  
18 that was not used by, or on behalf of, the claimant.

19 . . . .

20 (b) It is unlawful to do, or to knowingly assist or conspire with  
21 any person to do, any of the following:

22 (1) Present or cause to be presented any written or  
23 oral statement as part of, or in support of or  
24 opposition to, a claim for payment or other benefit  
25 pursuant to an insurance policy, knowing that the  
26 statement contains any false or misleading information  
27 concerning any material fact.

28 (2) Prepare or make any written or oral statement that  
is intended to be presented to any insurer or any  
insurance claimant in connection with, or in support of  
or opposition to, any claim or payment or other benefit  
pursuant to an insurance policy, knowing that the  
statement contains any false or misleading information  
concerning any material fact.

(continued...)

1 § 549 makes it a crime to refer or accept business knowing or  
2 with reckless disregard for whether the person the business is  
3 referred to or accepted from intends to violate Cal. Penal Code  
4 § 550.<sup>10</sup>

5 The state court found that Debtors defrauded Monterey with  
6 a scheme broader than any single misrepresentation. The court  
7 concluded that Debtors submitted 703 separate claims under the  
8 auspices of PMG in violation of Cal. Penal Code § 550. The  
9 court itemized the multiple violations of Cal. Penal Code § 550  
10 which occurred with the submission of each false claim:  
11

12 presentation of a claim as PMG (violates § 550(a)(1) and (6),  
13 (b)(1)); preparation of a temporary disability authorization as  
14

15 \_\_\_\_\_  
16 <sup>9</sup>(...continued)

17 (3) Conceal, or knowingly fail to disclose the  
18 occurrence of, an event that affects any person's  
19 initial or continued right or entitlement to any  
20 insurance benefit or payment, or the amount of any  
21 benefit or payment to which the person is entitled.

22 <sup>10</sup> Cal. Penal Code § 549 states in relevant part:

23 Any firm, corporation, partnership, or association, or  
24 any person acting in his or her individual capacity, or  
25 in his or her capacity as a public or private employee,  
26 who solicits, accepts, or refers any business to or  
27 from any individual or entity with the knowledge that,  
28 or with reckless disregard for whether, the individual  
or entity for or from whom the solicitation or referral  
is made, or the individual or entity who is solicited  
or referred, intends to violate Section 550 of this  
code or Section 1871.4 of the Insurance Code is guilty  
of a crime . . . .

1 PMB or IFMG (violates § 550(a)(6), (b)(1), (2)); upcoding the  
2 treating physician visit to a consulting physician visit which  
3 was not provided to the patient (violates § 550 (a)(7), (b)(1));  
4 and submission of a lien for the charges on the claim by PMG  
5 (violates § 550(b)(1)-(3)). The court also decided that the  
6 referral of business was sufficient to violate Penal Code § 549.  
7

8 We conclude that the state court's itemized violations of  
9 Cal. Penal Code §§ 549 and 550 cumulatively demonstrate the  
10 basic elements of wrongdoing inherent in fraud under  
11 § 523(a)(2)(A).

12 The first element under § 523(a)(2)(A) requires a  
13 misrepresentation, fraudulent omission, or deceptive conduct by  
14 the debtor. Debtors argue that they did not make false  
15 representations to Monterey. They contend that the same claims  
16 at issue in the state court lawsuit were brought in front of the  
17 Workers' Compensation Appeals Board ("WCAB"). Debtors point out  
18 that the administrative law judges examined every issue and  
19 confirmed that the bills and treatments Debtors rendered were  
20 reasonable and necessary. Debtors argued in their opening brief  
21 filed in this appeal and at oral argument that the WCAB found no  
22 fraud and ordered Monterey to pay the bills.  
23  
24

25 However, our review of the record shows the state court  
26 ruled that the issues raised before the WCAB were not the same  
27

1 as those raised in the state court lawsuit for insurance fraud.<sup>11</sup>  
2 Monterey Mushrooms, Inc. v. Thompson, 136 Cal. App. 4th at 31-  
3 32. To the extent Debtors seek to have us exercise appellate  
4 review over the state court's ruling in this regard, we are  
5 unable to do so. Our review is limited to whether the  
6 bankruptcy court properly held the debt nondischargeable.  
7 Hendrichs v. Valley View Dev., 474 F.3d 609, 613 (9th Cir.  
8 2007).

10 The state court's factual findings support the conclusion  
11 that Debtors engaged in conduct that included multiple  
12 misrepresentations and repeated deceptive conduct. The state  
13 court found that Debtors were co-conspirators with each other  
14 and the corporations they created. The state court observed  
15 that the fraudulent activity involved not just workers'  
16 compensation claims of questionable validity, but also the  
17 creation of "multifarious corporations . . . to accomplish the  
18 deception." Finally, the state court rejected Debtors' "claim  
19 of innocent intent and belief in compliance with the law"  
20 regarding their formation of their corporations, finding they  
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25 <sup>11</sup> It is without question that California courts may apply  
26 principles of claim and issue preclusion to WCAB proceedings to  
27 foreclose relitigation of the same causes of action or the same  
28 issues between the same parties. Azadiqian v. Workers' Comp.  
Appeals Bd., 7 Cal. App. 4th 372, 376-77 (Cal. Ct. App. 1992).

1 were not credible. Thus, the first requirement under  
2 § 523(a)(2)(A) is met.

3 The second element under § 523(a)(2)(A) requires that the  
4 debtor have knowledge of the falsity or deceptiveness of his  
5 statement or conduct, and the third element requires that the  
6 debtor intend to deceive. Cal. Penal Code § 550 defines the  
7 fraudulent offenses in the statute by requiring that they must  
8 be accompanied by a "knowing" state of mind. However,  
9 California courts have held that an essential element of the  
10 statutory offenses described in Cal. Penal Code § 550 is an  
11 intent to defraud. See People v. Blick, 153 Cal. App. 4th 759,  
12 772-73 (Cal. Ct. App. 2007) (noting that an essential element of  
13 the fraud offenses described in Penal Code § 550(b)(3) is an  
14 intention to defraud and that fraud is integral to the offense);  
15 People v. Scofield, 17 Cal. App. 3d 1018, 1025-26 (Cal. Ct. App.  
16 1971). In other words, one can be convicted or held liable for  
17 damages in a civil suit under Cal. Penal Code §550 only when the  
18 person intended to commit a fraud. People v. Blick, 153 Cal.  
19 App. 4th at 773-74 (noting that specific intent to defraud is  
20 imputed "where the statute . . . omits any other element of  
21 intent.").

22 The state court's findings demonstrate that Debtors had the  
23 requisite knowledge of their deceptive conduct and intent to  
24

1 deceive. The court concluded that "[e]ach invoice falsely and  
2 fraudulently represented that it was submitted on behalf of a  
3 medical corporation . . . [and was] prepared in a way that was  
4 calculated to deceive the recipient, by concealing and hindering  
5 detection of false and misleading information stated in the  
6 bills, in order to increase the payments obtained in the  
7 workers' compensation system."

8  
9 Moreover, the court found Debtors jointly and severally  
10 liable with their corporations for referral of business under  
11 Cal. Penal Code § 549 because the purpose of Debtors'  
12 corporations was to allow them to accomplish the deception;  
13 i.e. to acquire patients and refer them for chiropractic  
14 treatment and to present fraudulent claims for services to  
15 third-party payors.  
16

17 In short, the statutes upon which the judgment was based,  
18 coupled with the state court's findings of fact, demonstrate  
19 that the scienter element in the state court action is identical  
20 to the second and third requirements for nondischargeability  
21 under § 523(a)(2)(A).  
22

23 Under the fourth requirement of § 523(a)(2)(A), the  
24 creditor must have justifiably relied on the debtor's statement  
25 or conduct, and under the fifth requirement the damage to the  
26 creditor must have been proximately caused by the creditor's  
27

1 reliance on the debtor's statement or conduct. We consider the  
2 fourth and fifth requirements together in this context.

3 In their opposition to the Motion for Summary Judgment,  
4 Debtors contended that Monterey did not justifiably rely on  
5 anything because it did not pay the workers' compensation claims  
6 until ordered to do so by the administrative law judges.  
7 Debtors' contention is nothing more than a continuation of their  
8 theory that the WCAB's decision addressed all the issues  
9 considered in the state court lawsuit and therefore the WCAB's  
10 decisions should be given full faith and credit in their  
11 bankruptcy. As previously mentioned, the state court ruled that  
12 the issues in the civil lawsuit were not the same as those in  
13 the WCAB actions. Accordingly, the WCAB's decisions would not  
14 have precluded the state court from considering Debtors' alleged  
15 violations under the Insurance Frauds Prevention Act. We may  
16 not review the state court's decision, but only the decision of  
17 the bankruptcy court.  
18  
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21 We observe that there is no express statutory requirement  
22 for proof of reliance under Cal. Penal Code §§ 549 or 550. We  
23 conclude, however, that the necessary finding of reliance is  
24 implicit in the state court's award of damages for violation of  
25 the criminal statutes. Molina v. Seror (In re Molina), 228 B.R.  
26 248, 252 (9th Cir. BAP 1998) (Notwithstanding the absence of a  
27

1 specific finding of fraud in an arbitration award, the state  
2 court judgment which confirmed the arbitration award and awarded  
3 punitive damages for fraud was entitled to issue preclusion  
4 effect in dischargeability proceeding because necessary fraud  
5 findings were implicit in the state court's award of punitive  
6 damages for fraud).

7  
8 The state court found that Monterey was the target of  
9 fraudulent billing practices and awarded damages to Monterey as  
10 a result. The state court's damage award was based on proof  
11 that Monterey was damaged in the amount it paid on the inflated  
12 invoices Debtors' submitted, the amounts it incurred in legal  
13 and related expenses due to Debtors' fraudulent claims, and  
14 those amounts incurred in disability expenses attributable to  
15 those claims.<sup>12</sup>

16  
17 Implicit in the court's ruling on damages is a  
18 determination on the issue of causation; i.e., that Debtors'  
19 fraudulent acts proximately caused the damages. There is  
20 generally no causation without reliance. See Hall v. Time Inc.,  
21 158 Cal. App. 4th 847, 855 n.2 (Cal. Ct. App. 2008) (In a fraud  
22 case, justifiable reliance is the same as causation).

23  
24  
25 \_\_\_\_\_  
26 <sup>12</sup> Monterey's workers' compensation oversight manager  
27 testified at the remedies phase of the trial as to the total  
28 billing and costs Monterey incurred as a result of the fraudulent  
claims.

1 Accordingly, we conclude the state court's award of damages  
2 demonstrates Monterey's justifiable reliance.<sup>13</sup>

3 The fact the state court trebled the amount billed as  
4 authorized by Cal. Ins. Code § 1871.7(b) and awarded a remedial  
5 assessment under subsection (c) does not change the character of  
6 the full \$1,709,155 figure as damages. For purposes of  
7 dischargeability, where the liability which is nondischargeable  
8 is subject to trebling or other increase under non-bankruptcy  
9 law for punitive or deterrence purposes, the entire amount of  
10 the judgment as trebled or otherwise increased is  
11 nondischargeable. Cohen v. de la Cruz, 523 U.S. 213, 223  
12 (1998); see also Suarez v. Barrett (In re Suarez), 400 B.R. 732,  
13 740 (9th Cir. BAP 2009) (legal costs are nondischargeable when  
14 they stem from the same underlying conduct which makes the  
15 remedial damages nondischargeable).

16 We conclude from the nature of the claims asserted and a  
17 close reading of the statutes upon which the judgment was based  
18 that the identical issue requirement for application of issue  
19 preclusion under California law has been met. The  
20 previously-decided facts in the state court lawsuit are the same  
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23

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24  
25 <sup>13</sup> Justifiable reliance is not a difficult standard for a  
26 creditor to meet – a creditor only fails to meet the standard if  
27 his reliance was manifestly unreasonable. Medley v. Ellis (In re  
28 Medley), 214 B.R. 607, 614 (9th Cir. BAP 1997).

1 facts that Monterey would otherwise need to establish in the  
2 bankruptcy court to prove a discharge exception under  
3 § 523(a)(2)(A). The issues were actually litigated and  
4 necessarily decided because they were essential to the final  
5 judgment. Therefore, we hold that the bankruptcy court  
6 correctly applied the doctrine of issue preclusion and found  
7 Monterey's state court judgment nondischargeable under  
8 § 523(a)(2)(A).  
9

10 **B. Section 523(a)(6)**

11 In order to establish that a debt is nondischargeable under  
12 § 523(a)(6), a creditor must establish that the debt stems from  
13 the debtor's willful and malicious infliction of injury. Fraud  
14 is an intentional tort, and § 523(a)(6) makes many intentional  
15 torts nondischargeable. Petralia v. Jercich (In re Jercich),  
16 238 F.3d 1202, 1204-06 (9th Cir. 2001); Diamond v. Kolcum  
17 (In re Diamond), 285 F.3d 822, 828 (9th Cir. 2002). But not all  
18 intentional torts are willful and malicious as a matter of law.  
19 Kawaauhau v. Geiger (In re Geiger), 523 U.S. 57, 64 (1998) ("not  
20 every tort judgment for conversion is exempt from discharge").  
21  
22

23 Willful and malicious are separate requirements that are  
24 analyzed independently. Suarez, 400 B.R. at 736. A finding of  
25 willfulness requires proof that the debtor deliberately injured  
26 the creditor and that in doing so, the debtor intended the  
27

1 consequences of his act, not just the act itself. Id. at 737.  
2 The debtor must act with a subjective motive to inflict injury  
3 or with a belief that injury is substantially certain to result  
4 from the conduct. Id.; see also Diamond, 285 F.3d at 828 (the  
5 willful requirement of § 523(a)(6) is fulfilled if the debtor  
6 intentionally injures the creditor).  
7

8 The criminal statutes that were involved in the state court  
9 lawsuit do not use the word willful and the state court did not  
10 explicitly make a finding that Debtors' acts were willful.  
11 However, the state court found that Debtors' corporations were  
12 formed for the purpose of allowing Debtors to acquire patients  
13 and refer them for chiropractic treatment and to present  
14 fraudulent claims for services to third-party payors.<sup>14</sup>  
15 Moreover, the criminal offenses outlined in Cal. Penal Code  
16 § 550 require a specific intent to defraud.<sup>15</sup>  
17

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18  
19 <sup>14</sup> Under Cal. Penal Code § 549, either reckless disregard or  
20 knowledge of intent of another to commit insurance fraud is an  
21 element of the offense. Here, the record is unambiguous with  
22 respect to Debtors' liability under Cal. Penal Code § 549 because  
23 the court found that the formation of Debtors' corporations was  
24 part and parcel of their fraudulent scheme to acquire patients  
and refer them. Thus, their liability under Cal. Penal Code  
§ 549 was based on intentional rather than merely reckless  
behavior.

25 <sup>15</sup> The criminal offense described in Cal. Penal Code  
26 § 550(b)(3) requires a specific intent to defraud. People v.  
27 Blick, 153 Cal. App. 4th at 762. Although the California Court  
of Appeal did not address the other subsections of Cal. Penal

(continued...)

1 We conclude the only plausible inferences from the state  
2 court's findings of fact and ruling is that Debtors either had  
3 the subjective motive to injure Monterey or that their  
4 intentional acts were certain or substantially certain to result  
5 in injury to Monterey. Accordingly, we hold that the state  
6 court's ruling conclusively established that Debtors' acts were  
7 willful.  
8

9 A finding of maliciousness requires proof of (1) a wrongful  
10 act; (2) done intentionally; (3) which necessarily causes  
11 injury; and (4) was done without just cause or excuse. Suarez,  
12 400 B.R. at 737. Debtors' intentional wrongdoing was well  
13 documented in the state court's decision. Moreover, where a  
14 person intentionally commits the offenses outlined in the  
15 criminal statutes, the fraudulent acts themselves demonstrate a  
16 knowledge of necessary harm. Although an element of mistake or  
17 excuse would have prevented a finding of liability, the state  
18

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19  
20 <sup>15</sup>(...continued)  
21 Code § 550 that were involved in the underlying state court  
22 lawsuit here, we conclude from its reasoning that the offenses  
23 listed in Cal. Penal Code § 550 require a specific intent to  
24 defraud. The court explained that its interpretation was  
25 faithful to the statute's purpose and the "evil which it seeks to  
26 remedy – to criminalize and punish the making of false or  
27 fraudulent claims to obtain benefits." Id. at 774. A specific  
28 intent crime is defined as the intent to accomplish the precise  
criminal act that one is later charged with as opposed to a  
general intent crime, which is the intent to perform an act even  
though the actor does not desire the consequences that result.  
Black's Law Dictionary (8th ed. 2009).

1 court rejected Debtors' contention that they believed their  
2 medical corporations were legal. Finally, Debtors' wrongful  
3 acts could hardly be described as being done with "just cause".  
4 The state court found their numerous acts of fraud committed in  
5 violation of Cal. Penal Code §§ 549 and 550 were illegal. An  
6 illegal act cannot be "just".  
7

8 We conclude that the issues sought to be precluded under  
9 § 523(a)(6) were the same as those involved in the state court  
10 lawsuit. Those issues were actually litigated and necessarily  
11 decided because their determination was essential to the final  
12 judgment.  
13

14 Accordingly, the entire amount of the judgment is  
15 nondischargeable under § 523(a)(6). Cohen, 523 U.S. at 223;  
16 Suarez, 400 B.R. at 740.<sup>16</sup>

### 17 **C. Policy Considerations**

18 The bankruptcy court determined that public policy  
19 considerations underlying the doctrine of issue preclusion  
20 would be furthered by its application here. Our own assessment  
21 leads us to the same conclusion. Public policies which support  
22 application of issue preclusion are preservation of the  
23

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24  
25 <sup>16</sup> The trial court stated that § 523(a)(6)  
26 nondischargeability was established because the state court found  
27 Debtors had committed fraud. We do not adopt this approach  
because a separate analysis is necessary for each of the willful  
and malicious elements. Suarez, 400 B.R. at 736.

1 integrity of the judicial system, promotion of judicial economy  
2 and protection of litigants from repetitious and costly  
3 litigation. Lucido, 51 Cal. 3d at 343.

4 We conclude that under these circumstances application of  
5 issue preclusion preserves the integrity of the judicial system.  
6 State courts were fully capable of adjudicating the issues  
7 subsequently presented to the bankruptcy court. The public's  
8 confidence in the state judicial system would be undermined if  
9 the bankruptcy court relitigated the question of the  
10 nondischargeability of the debt under § 523(a)(2)(A) or (a)(6).  
11 Moreover, relitigation in bankruptcy court of the issues decided  
12 by the state court would conflict with the principle of  
13 federalism that underlies the Full Faith and Credit Act.  
14 See 28 U.S.C. § 1738.

17 Turning to the second policy, it is obvious that  
18 application of issue preclusion in the present context will  
19 promote judicial economy. If Debtors were not precluded from  
20 relitigating the fraud and willful/malicious elements, the  
21 bankruptcy court would have to conduct an evidentiary hearing to  
22 determine whether Debtors committed fraud and intentionally  
23 acted to injure Monterey. Relying on the state court's  
24 determination allows the bankruptcy court to conserve judicial  
25 resources.  
26

