U.S. BANKRUPTCY COURT
District of South Carolina

Case Number: **19-05887-hb**
Adversary Proceeding Number: **20-80018-hb**

ORDER

The relief set forth on the following pages, for a total of 8 pages including this page, is hereby ORDERED.

FILED BY THE COURT
05/13/2020

Entered: 05/13/2020

Chief US Bankruptcy Judge
District of South Carolina

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH CAROLINA

In re, Joey Ray Preston, Debtor(s).	C/A No. 19-05887-HB Adv. Pro. No. 20-80018-HB Chapter 7
Anderson County, Plaintiff(s), v. Joey Ray Preston, Defendant(s).	**ORDER DENYING MOTION TO DISMISS**

THIS MATTER is before the Court on the Motion to Dismiss filed by Defendant Joey Ray Preston[1] pursuant to Fed. R. Civ. P. 12(b)(6).[2] Anderson County's Complaint seeks a determination that its debt is excepted from the discharge under 11 U.S.C. § 523(a)(2)(A), (4), and (6).[3] The Motion asserts the action must fail as a matter of law because the claims are barred by decisions in prior litigation.

SUMMARY OF THE RECORD

This summary is gleaned from the Court's review of the Complaint, which attached a copy of an amended complaint filed by Anderson County against Preston in a state court action that pre-dated the bankruptcy filing, and the Motion to Dismiss, which attached copies of the state court docket and appellate court decisions rendered in that matter.

[1] ECF No. 4.
[2] Made applicable to this adversary proceeding pursuant to Fed. R. Bankr. P. 7012.
[3] ECF No. 7.

This case involves litigation between Anderson County and Preston, its former County Administrator, to recover funds paid to Preston pursuant to a severance agreement worth approximately $1,100,000.00. Anderson County asserts Preston devised a scheme to obtain this severance agreement by alleging false claims against the County to prompt the severance agreement in exchange for settling those claims and by providing improper financial benefits to certain county council members in exchange for their approval of the agreement.

After the severance agreement was approved by the outgoing county council, the new council initiated an action in the Court of Common Pleas for Anderson County seeking to invalidate and rescind the severance agreement. The litigation progressed through the South Carolina appellate courts. While the Court of Appeals affirmed the trial court's findings that Preston owed no fiduciary duty to inform the council of improper votes and his conduct did not constitute fraud, constructive fraud, or negligent misrepresentation, its decision was vacated by the South Carolina Supreme Court. The Supreme Court ultimately found the county council lacked a quorum to approve the severance agreement and, therefore, it was null and void. Without a valid severance agreement, Preston realized a benefit that would be inequitable for him to retain and the County was entitled to recover the amount paid to Preston under the severance agreement. The Supreme Court remanded the case to the trial court to determine the amount Anderson County was entitled to recover from Preston in the form of a civil judgment.

Prior to entry of a judgment, Preston filed a voluntary petition for Chapter 7 relief on November 6, 2019, and Anderson County responded with this adversary proceeding.

APPLICABLE LAW

Sections 523(a)(2)(A), (4), and (6) provide that a discharge under § 727 does not discharge an individual debtor from any debt:

> (2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—
>
> (A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;
>
> . . . .
>
> (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny;
>
> . . . .
>
> (6) for willful and malicious injury by the debtor to another entity or to the property of another entity[.]

11 U.S.C. § 523(a).

The Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1334(b) and 28 U.S.C. § 157. This matter is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I).

A motion filed under Rule 12(b)(6) challenges the legal sufficiency of the complaint and provides that a party may move to dismiss for failure to state a claim upon which relief can be granted. The legal sufficiency of the complaint is measured by whether it meets the standards for a pleading set forth in Rules 8 and 12(b)(6). *Francis v. Giacomelli*, 588 F.3d 186, 192 (4th Cir. 2009). Rule 8 requires the complaint contain "a short and plain statement of the claim showing that the pleader is entitled to relief." Fed. R. Civ. P. 8(a)(2). In order to survive a motion to dismiss, "a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678, 129 S. Ct. 1937, 173 L. Ed. 2d 868 (2009) (quoting in *Bell Atl. Corp. v. Twombly*, 550 U.S. 554, 570, 127 S. Ct. 1955, 167 L.Ed.2d 929 (2007)). A complaint meets the plausibility standard when it "articulate[s] facts, when accepted as true, that 'show' that the plaintiff has

stated a claim entitling him to relief, i.e., the 'plausibility of entitlement to relief.'" *Giacomelli*, 588 F.3d at 193 (quoting *Iqbal*, 556 U.S. at 678, 129 S. Ct. 1937). The pleader must provide more than mere "labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." *Twombly*, 550 U.S. at 555, 127 S. Ct. 1955 (citations omitted). Pursuant to Rule 12(b)(6), the Court must accept as true all factual allegations contained in the complaint and draw reasonable inferences in the nonmoving party's favor. *E.I. du Pont de Nemours and Co. v. Kolon Indus., Inc.*, 637 F.3d 435, 440 (4th Cir. 2011) (citations omitted).

Ordinarily, on a motion to dismiss, the court may not consider any documents that are outside the complaint or not expressly incorporated therein. *Braun v. Maynard*, 652 F.3d 557, 559 n.1 (4th Cir. 2011). Rule 12(d) provides if matters outside the pleadings are considered in ruling on a motion to dismiss under Rule 12(b)(6), "the motion must be treated as one for summary judgment under Rule 56." Fed. R. Civ. P. 12(d). Rule 56(a) states "[t]he court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." "[S]ummary judgment should be granted in those cases in which it is perfectly clear that no genuine issue of material fact remains unresolved and inquiry into the facts is unnecessary to clarify the application of the law." *Hyman v. Ford Motor Co.*, 142 F. Supp. 2d 735, 738 (D.S.C. 2001). On summary judgment, the court must "view the facts and the reasonable inferences drawn therefrom in the light most favorable to the nonmoving party." *United Rentals, Inc. v. Angell*, 592 F.3d 525, 530 (4th Cir. 2010).

However, "[i]n reviewing a Rule 12(b)(6) dismissal, [the court] may properly take judicial notice of matters of public record." *Philips v. Pitt Cty. Mem'l Hosp.*, 572 F.3d 176, 180 (4th Cir. 2009) (citing *Hall v. Virginia*, 385 F.3d 421, 424 (4th Cir. 2004)). Courts may

also consider documents attached to the complaint, or attached to the motion to dismiss, "so long as they are integral to the complaint and authentic." *Id.* (citing *Blankenship v. Manchin*, 471 F.3d 523, 526 n.1 (4th Cir. 2006)). When a plaintiff does not challenge the authenticity of a document attached to the defendant's motion to dismiss, the court may presume the document is authentic. *Am. Chiropractic Ass'n v. Trigon Healthcare, Inc.*, 367 F.3d 212, 234 (4th Cir. 2004). Furthermore, when considering a motion to dismiss on grounds of *res judicata*, the Court "may take judicial notice of facts from a prior judicial proceeding when the *res judicata* defense raises no disputed issue of fact." *Q Int'l Courier, Inc. v. Smoak*, 441 F.3d 214, 216 (4th Cir. 2006); *see also Clark v. Wells Fargo Fin., Inc.*, No. 1:08CV343, 2008 WL 4787444, at *3 n.4 (M.D.N.C. Oct. 30, 2008) ("Affirmative defenses such as *res judicata* and collateral estoppel may properly be raised through a motion to dismiss under Rule 12(b)(6) if the affirmative defense appears on the face of the complaint, or in documents properly attached to the complaint of which the court may take judicial notice." (citing *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 322 (2007) and *Andrews v. Daw*, 201 F.3d 521, 524 n.1 (4th Cir. 2000))).

To determine whether *res judicata* applies, "[f]ederal courts are required to refer to the preclusion law of the state in which the judgment was rendered." *In re Pujdak*, 462 B.R. 560, 567 (Bankr. D.S.C. 2011) (quoting *In re Rodgers*, Adv. Pro. No. 10-00171-8-JRL, 2010 WL 5014340, at *4 (Bankr. E.D.N.C. Dec. 3, 2010)). Under South Carolina law, "[r]es judicata requires proof of three elements: 1) a final, valid judgment was entered on the merits of the first suit; 2) the parties to both suits are the same; and 3) the subsequent action involves matters properly included in the first action." *Id.* at 568 (quoting *Judy v. Judy*, 383 S.C. 1, 8, 677 S.E.2d 213, 217 (Ct. App. 2009)).

Where a creditor previously liquidated its claim, claim preclusion applies in bankruptcy proceedings to conclusively establish the existence, amount, and validity of the claim. *In re Crespin*, 551 B.R. 886, 897 (Bankr. D.N.M. 2016) ("A state court judgment is entitled to claim preclusion effect to establish the existence and amount of the debt in a dischargeability proceeding.").

> However, in the bankruptcy context, there is a general rule that state court judgments do not have *res judicata* effect on nondischargeability actions under § 523. "Under *Brown v. Felsen*, 442 U.S. 127, 139 n.10, 99 S. Ct. 2205, 60 L. Ed. 2d 767 (1979) and *Pahlavi v. Ansari (In re Ansari)*, 113 F.3d 17, 23 (4th Cir. 1997), the correct preclusion principle in a § 523 case is collateral estoppel, and not res judicata, because a because a § 523 action cannot be the same cause as an underlying state-court cause of action."

Pujdak, 462 B.R. at 569 (quoting *In re Webb*, Adv. Pro. No. 08-ap-65, 2009 WL 1139548, at *3 (Bankr. N.D.W.Va. Mar. 31, 2009)).

"[T]he party asserting collateral estoppel must demonstrate that the issue in the present lawsuit was (1) actually litigated in the prior action; (2) directly determined in the prior action; and (3) necessary to support the prior judgment." *Id.* at 571 (quoting *Cross v. Deutsche Bank Trust Co. Americas*, C/A No. 3:11-1010-CMC-PJG, 2011 WL 1624958, at *4 (D.S.C. April 28, 2011)). "Under the law-of-the-case doctrine, a party is precluded from relitigating, after an appeal, matters that were either not raised on appeal, but should have been, or raised on appeal, but expressly rejected by the appellate court." *Flexon v. PHC-Jasper, Inc.*, 413 S.C. 561, 571, 776 S.E. 2d 397, 403 (Ct. App. 2015) (citations omitted). Even if an issue is actually litigated and ruled on by the trial court, the trial court's decision is stripped of any effect if it is vacated or reversed on appeal. *Builders Mut. Ins. Co. v. Bob Wire Elec., Inc.*, 424 S.C. 161, 165, 817 S.E.2d 807, 809 (Ct. App. 2018) (citing several cases). As a result, a "vacated judgment carries no preclusive effect under *res judicata* or any other doctrine known to us." *Id.* at 809-10 (citing *Shaw Components, Inc. v. Nat'l Bank of S.C.*, 304 S.C. 114, 115, 403

S.E.2d 153, 154 (Ct. App. 1991) (issue preclusion cannot be based on reversed judgment); *Erebia v. Chrysler Plastic Prod. Corp.*, 891 F.2d 1212, 1215 (6th Cir. 1989) (vacated judgment is "deprived of all conclusive effect, both as res judicata and as collateral estoppel"); *No E.-W. Highway Comm., Inc. v. Chandler*, 767 F.2d 21, 24 (1st Cir. 1985) ("A vacated judgment has no preclusive force either as a matter of collateral or direct estoppel or as a matter of the law of the case.")).

CONCLUSIONS

Preston's Motion asserts this adversary proceeding should be dismissed because Anderson County's claims under § 523(a)(2)(A), (4), and (6) are barred by prior litigation. No party has questioned the authenticity of the documents attached to the Motion to Dismiss or asserted that the Motion should be treated as one for summary judgment. Moreover, such documents are matters of public record. Therefore, the Court takes judicial notice of the orders entered by the state courts to consider this matter under the standards of Rule 12(b)(6) and concludes the Motion must be denied.[4]

After careful review, the Court finds there was no state court decision finally determining the elements of dischargeability under § 523(a)(2)(A), (4), or (6). Further, any relevant issues litigated and ruled on by the state trial court lost any preclusive effect when the Supreme Court vacated the Court of Appeals' decision that affirmed those findings. Therefore, preclusion does not apply, and Preston has failed to demonstrate that dismissal of Anderson County's Complaint pursuant to Fed. R. Civ. P. 12(b)(6) is appropriate.

IT IS, THEREFORE, ORDERED that Preston's Motion to Dismiss is denied.

[4] Regardless of applying the standards of Rule 12(b)(6) or Rule 56, the Court's decision is the same.