In the Intermediate Court of Appeals of West Virginia

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No. 23-ICA-22

KAPITUS SERVICING, INC. *formerly known as Colonial Funding Network, Inc.***,** *as authorized servicing agent for First US Funding***,**

Plaintiff* / *Petitioner,

v.

TUCKER COUNTY CIRCUIT COURT
BUSINESS DIVISION
CIVIL ACTION NO. 22-C-4
PRESIDING: JUDGE LORENSEN

TIMBERLINE FOUR SEASONS UTILITIES INC. *and* **CANAAN VALLEY PUBLIC SERVICE DISTRICT,** *individually, and in its capacity as Receiver of Timberline Four Seasons Utilities Inc.***,**

Defendants* / *Respondents.

PETITIONER'S REPLY BRIEF

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Cases

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I. INTRODUCTION

In its initial appeal brief, Petitioner, Kapitus Servicing, Inc. ("Kapitus"), explained how, in reliance on (*inter alia*) various capacity, authority, and solvency representations made by Respondent Timberline Four Seasons Utilities Inc. ("Timberline Utilities"), Kapitus advanced to Timberline Utilities certain money pursuant to the parties' exchange of promises ("Agreement"). This included Timberline Utilities' promise to pledge certain of its future income to secure repayment. Timberline Utilities defaulted, however, and then filed bankruptcy in the United States Bankruptcy Court for the Northern District of West Virginia ("Bankruptcy Court").

Kapitus filed proofs of claim in Timberline Utilities' bankruptcy (collectively the "Proof of Claim"). Timberline Utilities objected to Kapitus' Proof of Claim, arguing, *inter alia*. that the Agreement was unenforceable. The Bankruptcy Court, however, *rejected* Timberline Utilities' argument, made factual findings favorable to Kapitus, and entered orders holding that Kapitus's Proof of Claim was enforceable ("the Bankruptcy Court Orders"). Of particular relevance, the Bankruptcy Court specifically rejected Respondents' argument that the Agreement was unenforceable. The Bankruptcy Court's Orders became final.

At Respondents' urging, the West Virginia Public Service Commission ("PSC") undertook to "investigate" the very same question that the Bankruptcy Court had already ruled on—*i.e.*, the enforceability of the parties' Agreement. The PSC thereafter purported to "rule" in Respondents' favor—squarely contradicting what the Bankruptcy Court had already decided.

Kapitus sued to perfect its Proof of Claim, but the Circuit Court, in part, granted Respondents' motion to dismiss, applying the PSC's Order instead of the Bankruptcy Court's earlier Order. Kapitus appealed. In its opening brief, Kapitus demonstrated, *inter alia*, that:

- The Bankruptcy Court decided the sole relevant underlying substantive issue (*i.e.*, whether the parties' agreement was enforceable under West Virginia law).

- As for the issue on appeal (*i.e.*, the effect of the Bankruptcy Court's Orders), West Virginia's law of *res judicata* required the Circuit Court to apply the Bankruptcy Court's Orders and not dismiss Kapitus's claims against Respondents (and would eventually have required judgment on those claims in Kapitus's favor).[1]

- Thus, the PSC's *subsequent* effort to redecide the very same issue with the very same facts was a legal nullity, entitled to no weight.

Although Respondents have denominated their brief as a "response" to Kapitus's appeal, one searches Respondents' brief in vain for much of an argument disputing what Kapitus has demonstrated.[2] Instead, they go off on several irrelevant tangents. They defend the Circuit Court's enforcement of the PSC's Order even though it was not within the four corners of Kapitus's Complaint.[3] They argue that the Bankruptcy Court wrongly decided the *underlying* issue about the enforceability of the parties' Agreement.[4]

Primarily, though, Respondents argue that Kapitus received notice of, and an opportunity to be heard in, the afterthought PSC proceeding to relitigate the very same issue in the very same dispute involving the very same facts that had already been decided by the Bankruptcy Court—multiple times, in fact, given Respondents' repeated motions for reconsideration and collateral attacks.[5] By not doing so, Respondents say, Kapitus somehow "waived" its "right" to enforce the Bankruptcy Court's Orders.[6] Respondents' arguments have neither merit nor relevance.

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1 In the alternative, as explained in Kapitus's opening brief, the Circuit Court should have applied West Virginia law on issue preclusion, with the same outcome.

2 One also scours Respondents' briefs for citations to the parties' Joint Appendix. Instead, Respondents apparently expect the Court and Kapitus to simply take Respondents' word for the *great many* uncited factual assertions (and legal positions) in Respondents' brief.

3 (*See* Resps.' Resp. § V.A.)

4 (*See* Resps.' Resp. § V.B.)

5 (*See* Resps.' Resp. at 18 ("The issue, the validity of the contract, and whether the contract should have been approved, were the same [in both the Bankruptcy Court and PSC proceedings] and involved the same object.").)

6 (*See* Resps.' Resp. §§ V.C & V.D.)

II. ARGUMENT

A. Whether it was procedurally proper for the Circuit Court to rely on the PSC's Order in dismissing Kapitus's claims notwithstanding that it was not attached to Kapitus's Complaint is entirely irrelevant.

Respondents spend a page and a half arguing that it was procedurally proper for the Circuit Court to rely on the PSC's Order in dismissing Kapitus's claims notwithstanding that the Order was not attached to Kapitus's Complaint.[7] This entire argument (which Kapitus never raised) is pointless: As Kapitus demonstrated in its brief, what the PSC ordered is factually and legally irrelevant to this appeal, because West Virginia law on *res judicata* did not permit the Circuit Court to go down that road *at all*.

In fact, like many of Respondents' arguments (*see infra*), this point cuts directly against Respondents' position: It was the *Bankruptcy Court's Orders*—prominently raised in Kapitus's pleadings—that showed that Kapitus's claim against Respondents had already been decided *by the Bankruptcy Court*—prior to both the Circuit Court case and the PSC Order.

Under West Virginia law, *res judicata* applies when three conditions are met:

> First, there must have been a final adjudication on the merits in the prior action by a court having jurisdiction of the proceedings. Second, the two actions must involve either the same parties or persons in privity with those same parties. Third, the cause of action identified for resolution in the subsequent proceeding either must be identical to the cause of action determined in the prior action or must be such that it could have been resolved, had it been presented, in the prior action.

Syl. pt. 4, *Blake v. Charleston Area Med. Ctr., Inc.*, 201 W. Va. 469, 498 S.E.2d 41 (1997).

As Kapitus demonstrated in its opening brief, all three elements were met in this case. Respondents do not even try to argue otherwise.

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[7] (*See* Resps.' Resp. § V.A.)

B. Whether the PSC Order correctly decided the enforceability of the parties' Agreement is also entirely irrelevant.

Throughout their brief, Respondents repeatedly outright argue, or at least imply, that the Bankruptcy Court got it wrong and should have ruled in Respondents' favor.

As Kapitus pointed out in its brief, however, Timberline Utilities could have appealed the Bankruptcy Court's Orders before they became final, or even sought a certified question.[8] In their response, Respondents also point out that they might have raised *Burford* abstention before the Bankruptcy Court. But Timberline Utilities did not do so and instead allowed the Bankruptcy Court's Orders to become final.

All of the arguments that Respondents make now with respect to their opinion of the Bankruptcy Court's Orders matter not, because (for the same reason as set out in the previous section) West Virginia law on *res judicata* simply forbade the Circuit Court from going down that road and effectively vacating the Bankruptcy Court's Order.

Avoiding the very duplication of effort that Respondents argue should have happened here, and obviating the very same contradictory judgments that Respondents caused to happen here are *the entire point* of *res judicata*.

C. Whether Kapitus would have been bound by the PSC's Order *but for the Bankruptcy Court's Orders* is entirely irrelevant.

Respondents argue at length that Kapitus received notice of and had an opportunity to be heard at the PSC hearing. Thus, argue Respondents, Kapitus's failure to do so "waived" any power of the Bankruptcy Court's Orders. Their argument is a little hard to understand. They

[8] Respondents characterize the Circuit Court's dismissal of Kapitus's claim as having "conducted a review [of the PSC's Order] as the Supreme Court might have if there had been a direct appeal from the PSC by Kapitus." (Resps.' Resp. at 16.) Respondents also could have said that the Circuit Court's dismissal "conducted a review as the district court might have if there had been a direct appeal from the Bankruptcy Court by Respondents."

begin by saying that "the PSC generally operates in rem."[9] They then argue that "[i]n rem proceedings are distinct from in personam proceedings in some ways."[10] One of these ways, they say, is the nature of the service required (and, thus, personal jurisdiction under the Due Process Clause) in the two different kinds of cases.[11] Discussing *Mullane v. Cent. Hanover Bank & Tr. Co.*, 339 U.S. 306 (1950), and just when the reader believes Respondents are going to argue that constructive notice to Kapitus was adequate, Respondents say that "the PSC ordered the [PSC] Secretary to give notice to Kapitus" and "that such notice was actually given."[12] Having knocked down that strawman, Respondents next assert that because "Kapitus [h]ad [n]otice and an [o]pportunity to [b]e [h]eard [b]efore the PSC," "[b]inding Kapitus to an outcome where Kapitus enjoyed the benefits of due process is not unfair."[13]

Kapitus never argued that enforcing the PSC Order violated Due Process—*i.e.*, whether Kapitus would have been bound by the PSC's Order ***but for the Bankruptcy Court's Orders***—so Kapitus has no idea why Respondents went down this path. Instead, Kapitus demonstrated that not enforcing the Bankruptcy Court's Orders—that is, that instead enforcing the PSC's contrary Order—violated West Virginia's law of *res judicata*.

In fact, Respondents never do actually *argue* their "waiver" theory; they just assert it, *ipse dixit*, without justifying it or citing any law as the theory's source. Kapitus can only imagine that Respondents mean to apply their own version of *res judicata* but enforcing the PSC's Order instead of the Bankruptcy Court's. They have offered no valid reason to do so.

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9 (Resps.' Resp. at 8.)

10 (Resps.' Resp. at 9.)

11 (Resps.' Resp. at 9.)

12 (Resps.' Resp. at 10.)

13 (Resps.' Resp. at 10.)

Respondents assert, without citation, that "[e]ven had Kapitus appeared [before the PSC], and asserted that something that occurred in Bankruptcy Court was res judicata [*sic*], the statutory authority vested the right to make the first decision in the PSC."[14] Respondents did not identify this supposed "statutory authority." The only conceivable candidate would be W. VA. CODE § 24-2-12. But as the Bankruptcy Court already held, Respondents' assertion is false: that section provides only that an agreement not passed on by the PSC "shall be void ***to the extent that the interests of the public in this state are adversely affected*** …." W. VA. CODE § 24-2-12 (emphasis added). It is not an absolute proscription against such agreements, and it certainly does not mean that a *court* cannot apply the statute. The Bankruptcy Court held that the parties' Agreement was not void under this provision. Even if West Virginia law permitted second-guessing that decision (it does not), Respondents have identified no reason to do so.

Simply put, Respondents offer no explanation for their "waiver" argument, and the Court should reject it as contrary to West Virginia law.

D. Respondents' "detour" from their main detour is entirely irrelevant.

In the middle of their detour from the sole relevant issue on appeal—*i.e.*, whether West Virginia law on *res judicata* allowed the Circuit Court to ignore the Bankruptcy Court's order and enforce the contradictory PSC's Order—Respondents take yet another detour.[15] There, they spend two and a half pages discussing how they moved the Bankruptcy Court to reconsider its order but, as they are finally forced to admit, ultimately ***denied*** their motion and decided the underlying issue (*i.e.*, enforceability of the parties' Agreement) in Kapitus's favor. It is difficult to imagine what difference the rest of § V.E of their argument makes.[16] If Respondents intended

[14] (Resps.' Resp. at 4.)

[15] (*See* Resps.' Resp. § V.E.)

[16] Respondents briefly mention the 11 U.S.C. § 349 issue before saying that they do not want to argue it. Kapitus accordingly relies on its discussion of that issue in its brief.

this section to introduce their primary argument—*i.e.*, that Kapitus "waived" *res judicata*—Kapitus demonstrates the invalidity of Respondents' argument herein.

E. "Hypothetical [a]rguments that Kapitus [c]ould [h]ave [m]ade [b]efore the PSC" are, obviously, entirely irrelevant.

Respondents devote § V.F of their brief to "speculat[ing] what would have occurred if Kapitus had appeared before the PSC" and discussing "[h]ypothetical [a]rguments that Kapitus [c]ould [h]ave [m]ade [b]efore the PSC."[17]

First, this argument lacks a shred of merit. Respondents propose that some law—they never say which—required Kapitus to show up before the PSC, to argue that it was up to the ***PSC*** to have enforced the ***Bankruptcy Court's Orders***, and, if the PSC refused to do so, to have accepted that the PSC had somehow thereby neutered the Bankruptcy Court's Orders.

Accepting Respondents' argument would entirely gut *res judicata*. *Res judicata* requires that once the first court lawfully and finally decides a claim, it is decided forever. There is absolutely nothing that a party to that first-reached decision needs to do to continuously "re-defend" or "preserve" his victory. The dispute is over. If Respondents' argument had any merit, a party wanting a do-over could just re-start the judicial wheels turning on a claim, wait for the prior victor to no-show, and then claim "waiver" in a subsequent enforcement action. There is a reason why Respondents cite no law to support this argument: there isn't any.

Second, Kapitus thinks Respondents doth protest too much. They argue that *Burford* abstention somehow counsels in favor of rejecting the Bankruptcy Court's Orders in favor of the later-decided PSC's Order.[18] Section V.F of Respondents' brief should be titled, "Hypothetical Arguments that *Respondents* Could Have Made Before the *Bankruptcy Court*." *Burford*

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17 (Resps.' Resp. at 13–16.)

18 *Cf. Burford v. Sun Oil Co.*, 319 U.S. 315, 319 (1943).

abstention is exactly that: an *abstention* argument that can be made *to a federal court* to (perhaps temporarily) not exercise jurisdiction over an issue that a state regulatory agency has made (or will make during a stay of the federal proceedings). It is not an exception to *res judicata* to be invoked by a party who decided not to argue it earlier and thereby invalidate an *already final* decision by a federal court in "deference" to a *later* decision by a state regulatory body. Like a certified question or an appeal, a stay pursuant to *Burford* is exactly the kind of "hypothetical argument" that *Respondents* could have made in the earlier *Bankruptcy Court* proceeding. Understandably, Respondents want this Court to pretend like they did. But they have given the Court no reason to rewrite history, much less ignore well-settled West Virginia law.[19]

It is absolutely critical to recall at all times that the *Bankruptcy Court Orders came first, before the PSC Order*. Respondents had their chance to raise all of this before the Bankruptcy Court. They are asking for the very worst kind of hindsight-driven do-over.

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[19] Without conceding that there is a shred of relevance to *Burford* given Respondents' decision to raise it here and now, of all places, Kapitus notes that *Burford* abstention also would not have required the Bankruptcy Court to proceed any differently than it did:

> The Supreme Court has repeatedly instructed that "federal courts have a strict duty to exercise the jurisdiction that is conferred upon them by Congress." *Quackenbush v. Allstate Ins. Co.,* 517 U.S. 706, 716 (1996); *see, e.g., Deakins v. Monaghan,* 484 U.S. 193, 203 (1988) ("[T]he federal courts have a virtually unflagging obligation to exercise their jurisdiction . . . ."
>
> Abstention doctrines constitute "extraordinary and narrow exception[s]" to a federal court's duty to exercise the jurisdiction conferred on it. . . .
>
> . . . . *Burford* permits abstention when federal adjudication would "unduly intrude" upon "complex state administrative processes" because either: (1) "there are difficult questions of state law . . . whose importance transcends the result in the case then at bar"; or (2) federal review would disrupt "state efforts to establish a coherent policy with respect to a matter of substantial public concern." Moreover, the Supreme Court has directed that "*Burford* allows a federal court to dismiss a case only" when presented with these "extraordinary circumstances." … "This balance only rarely favors abstention."

Martin v. Stewart, 499 F.3d 360, 363–64 (4th Cir. 2007) (citations, internal citations, and parallel citations omitted). The instant dispute would not require the Bankruptcy Court to abstain from deciding whether the parties' Agreement was adverse to the interests of West Virginia's public.

F. Respondents' admission that the Circuit Court did not apply *res judicata* does not help them like they appear to think it does.

Respondents point out in detail that the Circuit Court did not really even purport to analyze Kapitus's invocation of the fact that *res judicata* required enforcing the Bankruptcy Court's Orders and ignoring the PSC's Order.[20] Respondents use this admission to introduce another argument that the Bankruptcy Court got it wrong. But Kapitus has already demonstrated that West Virginia law required the Circuit Court to apply *res judicata* and simply apply the Bankruptcy Court's Orders. Respondents' reliance on the Circuit Court's failure to even inquire into the applicability of *res judicata* entirely undercuts, not supports, their position.

G. Respondents' only argument against application of *res judicata* to the Bankruptcy Court's Orders lacks merit.

In what might be called Respondents' only argument that the Circuit Court did not err by refusing to give the Bankruptcy Court's Orders *res judicata* effect, they appear to argue that following *res judicata* here "would plainly defeat the ends of justice."[21] Specifically, they argue that it would defeat the ends of justice to apply the Bankruptcy Court's Orders because the Bankruptcy Court misapplied W. VA. CODE § 24-2-12, so the Circuit Court should have deferred to the PSC. Respondents are wrong.

As demonstrated in Kapitus's opening brief and discussed again herein, the Bankruptcy Court correctly held that § 24-2-12 does ***not*** void every agreement not passed on by the PSC. Instead, § 24-2-12 only voids such an agreement *to the extent that the interests of the public in West Virginia are adversely affected by the agreement*. Because the Bankruptcy Court

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[20] (*See* Resps.' Resp. at 16 ("At the end of the day, in examining the Order of the PSC and the Order of the Bankruptcy Court, Judge Lorensen seems not to have explicitly ruled on res judicata. Instead, he determined that he should look more to the merits of the underlying orders each party advocated should be followed. The Judge conducted a review as the Supreme Court might have if there had been a direct appeal from the PSC by Kapitus. He did not leap into the principle of res judicata . . . .").)

[21] *Gentry v. Farruggia*, 132 W. Va. 809, 811, 53 S.E.2d 741, 742 (1949).

concluded the parties' Agreement here did *not* adversely affect the interests of the public in West Virginia, it was not void and, thus, enforceable.

There is nothing remotely novel about that holding, which derives directly from the statute's clear and unambiguous language. The PSC decided the case differently from the Bankruptcy Court and, arguably, from how the Circuit Court might have. But none of those results means that the Bankruptcy Court's holding that the parties' Agreement was enforceable "defeats the ends of justice." In fact, it is difficult to perceive how allowing Respondents to take Kapitus's money and then claim, "We don't have to pay you back because you shouldn't have believed us when we promised that had the authority to borrow this money from you" does not obviously itself defeat the ends of justice.

In any event, like Respondents' "waiver" argument, allowing *res judicata* to be ignored whenever a later court disagrees with an earlier one would completely eliminate the rule: All a loser would have to do to defeat *res judicata* would be to refile his claim in other fora until he got a result that he liked, then argue that the prior, now contrary case "defeats the ends of justice." *Res judicata* is not so easily cast aside, lest it be swallowed by this "exception": "An erroneous ruling of the court will not prevent the matter from being *res judicata*."[22]

Respondents could have made all the arguments that they make here to the Bankruptcy Court. They did not. It does not defeat the ends of justice to refuse to give them yet another bite at the litigation strategy apple.

H. Respondents' "alternative basis" for affirmation lacks merit.

Kapitus is uncertain what, exactly, Respondents intend to argue in § V.H of the response brief. In good faith, Kapitus believes Respondents to be arguing that this Court might "review the propriety of the PSC decision" and itself find the PSC Order better reasoned than the

[22] *Blake*, 201 W. Va. at 477, 498 S.E.2d at 49 (indentation, quotations, and citations omitted).

Bankruptcy Court's Orders. As explained in great detail herein, West Virginia law does not allow this, either. Respondents are simply encouraging this Court to do what the Circuit Court did: *i.e.*, to disregard *res judicata* and—for at least the third time—re-decide the issue of enforceability of the parties' Agreement. Not even this Court has the authority to ignore West Virginia's *res judicata* law; as noted *supra*, even "[a]n erroneous ruling of the court will not prevent the matter from being *res judicata*."[23] *See also Bison Ints., LLC v. Antero Res. Corp.*, 244 W. Va. 391, 401, 854 S.E.2d 211, 221 (2020) ("Moreover, the fact that the McCarthy order may have erroneously refused to determine the issue provides no excuse for Antero's failure to obtain a determination in the 2015 litigation. . . . *[S]ee Federated Dep't Stores, Inc. v. Moitie*, 452 U.S. 394, 398 (1981) ('Nor are the res judicata consequences of a final, unappealed judgment . . . altered by the fact that the judgment may have been wrong[.]'); *see also* [*Angel v. Bullington*, 330 U.S. 183, 187 (1947)] ('That the adjudication of federal questions by the North Carolina Supreme Court may have been erroneous is immaterial for purposes of res judicata. A higher court was available for an authoritative adjudication of the federal questions involved.'") (parallel citations and quotations omitted) (scattered alterations in original).

III. CONCLUSION

Contrary to what Respondents say, the Circuit Court case was in no "odd procedural context"[24]—either because of the PSC's effort to interfere with an already-decided question, or Respondents' effort to have the Circuit Court go down a road that West Virginia law outright prohibited it from going down. In other words, dismissal of the bankruptcy case in no way meant that "all roads seemed to lead to the PSC."[25] After the Bankruptcy Court decided this

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[23] *Blake*, 201 W. Va. at 477, 498 S.E.2d at 49 (indentation, quotations, and citations omitted).

[24] (Resps.' Resp. at 3.)

[25] (Resps.' Resp. at 13.)

dispute on the merits, all roads led back there, to the Bankruptcy Court's Orders. No legal road led to the PSC. The PSC's proceedings were, as a matter of West Virginia's well-settled law of *res judicata*, a non-event with regard to the Bankruptcy Court's Orders and, thus, the Circuit Court case. The Circuit Court was wrong to ignore that law and the Bankruptcy Court's Orders.

Accordingly, this Court should reverse the Circuit Court's dismissal, hold that the Bankruptcy Court's Orders are entitled to *res judicata*, and remand this case to the Circuit Court for further proceedings in conformity with such holdings.

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CERTIFICATE OF SERVICE

I hereby certify that on the 26th day of June 2023, I served the foregoing **"*Petitioner's Reply Brief*"** upon all counsel of record by electronically filing the same through the West Virginia E-Filing System which will send notice and a copy to counsel of record:

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