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OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	)	BAP No. CC-10-1307-PaDKi
JAMES CASTRO and JESSICA CASTRO,	)	Bk. No. LA 08-16504 SB
Debtors.	)	Adv. No. LA 08-01660 SB
BRIAN DONLINGER; WEST COAST BUDDY, LLC; MILO, LLC,	)	
Appellants,	)	**M E M O R A N D U M**[1]
v.	)	
JAMES A. CASTRO,	)	
Appellee.	)	

Argued and submitted on March 16, 2011
at Pasadena, California

Filed - April 4, 2011

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

Hon. Samuel L. Bufford, Bankruptcy Judge, Presiding.

Appearances: David N. Tarlow appeared for Appellants.
Raymond H. Aver appeared for Appellee.

Before: PAPPAS, DUNN and KIRSCHER, Bankruptcy Judges.

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[1] 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.

This is an appeal from the bankruptcy court's order granting summary judgment in favor of chapter 7[2] debtor James A. Castro ("Castro"), dismissing the § 523(a) exception to discharge claims asserted by creditors Brian Donlinger ("Donlinger"), West Coast Buddy, LLC ("WCB"), and Milo, LLC ("Milo") (collectively, "Appellants"). We VACATE and REMAND the dismissal under § 523(a)(2)(A), and AFFIRM the dismissal under § 523(a)(4).

FACTS

Sunset Beach

Castro was an investment banker. In June 2004, he learned that a local business, Dublin's Irish Whiskey Pub ("Dublins"), intended to sell its lease rights to a commercial property on West Sunset Boulevard, West Hollywood, California. As he later recounted in his declaration, Castro was "very optimistic and excited about the possibility of opening a new venture, consisting of a restaurant and a bar, there." Because Castro had no experience in operating such a business, he invited Steve Marlton ("Marlton"), an experienced restauranteur, to join him in making a proposal to acquire the lease. Castro was the managing member of Gardner Restaurants, LLC; Marlton was president of California Restaurant Authority, Inc. Together, they formed Sunset Restaurants Limited Partnership ("SRLP"), in which their two entities were the general partners. SRLP acquired the lease rights to the commercial property on July 1, 2004.

[2] Unless otherwise indicated, all chapter, section and rule references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037. The Federal Rules of Civil Procedure are referred to as "Civil Rules."

Capital was needed to develop the property into an operating business. To assist them in attracting investors to their project, Castro and Marlton created a document called a Confidential Investment Summary (the "PPM"), which outlined the business plans and objectives of SRLP and contained information on the proposed business venture. For example, in describing what it termed "The Concept," the PPM states "Sunset Beach Restaurant and Ultra Lounge [will be] set in a casual beach inspired setting, in the same vein as the world renowned Nikki Beach [a well-known, successful restaurant and bar in Florida], that promotes mingling among its guests. . . . The bar area, located away from the main dining room, will create a focal point for guest interaction." Describing the venture's business strategy, the PPM noted in particular that, "[t]he sophisticated, full-service bar will offer a broad selection of domestic and imported bottled and draft beers, premium wines, and speciality drinks, along with top shelf liquor. . . . The Venue anticipates to be open seven days a week generally from 11:00 a.m. to 2:00 a.m. to serve its guests lunch, happy hour, dinner and late supper."

Castro and Donlinger agree that they met at a birthday party in September 2004, and that, for the first time, they discussed Donlinger's possible investment in SRLP.

On November 16, 2004, SRLP filed an application with local authorities for a Minor Conditional Use Permit ("MCUP"). Among the statements submitted to the Planning Commission of the City of West Hollywood, and contrary to the statements in the PPM, the MCUP indicated that "Sunset Beach intends to be open for Lunch during week days from 11:30 a.m. to 2:30 p.m. and for Dinner from

5:30 p.m. to 12:30 a.m. Sunday through Thursday and until 1:30 a.m. on Fridays and Saturdays." In addition, this application made no request for authority to operate a "full-service bar" at Sunset Beach to service customers independent of food services. Moreover, the proposed floor plans for the project accompanying the application show space allotted for an "espresso bar" on the first floor of the business premises, and for a "sushi bar" on the second floor.

In mid-December 2004, Castro and Donlinger met again at the El Guapo Restaurant to talk more about Sunset Beach. At that meeting Castro gave Donlinger a copy of the PPM, a form Subscription Agreement to the partnership, and an Equity Bonus Plan. The parties significantly diverge, however, in their characterization and recollection of the oral discussions at that meeting.

Donlinger alleges that Castro made numerous oral representations to him at the El Guapo meeting that the "Sunset Beach Restaurant and Ultra Lounge" would be a "restaurant, full service bar and nightclub." In particular, he alleges in the Second Amended Complaint that:

> Castro told Donlinger [] that he and his partner planned to open an ultra lounge at the property called Sunset Beach, which would be a restaurant, full service bar and nightclub, which would promote an interactive experience among the customers. Castro stated that the model for Sunset Beach was a nightclub in Miami, Florida called Nikki Beach, which was an "ultra lounge" which contained a restaurant and nightclub. Castro explained that Sunset Beach would have multiple dining areas and a full service bar for alcohol service and consumption. He said the bar would be the focal point of guest interaction. He also told Donlinger that Sunset would have a disk jockey booth and a dance floor, so that its patrons could dance until 2:00 a.m. each night. Castro also told Donlinger that he was so confident in the

> success of Sunset that he had invested $150,000.00 of his own money in the company.

Donlinger's declaration submitted in opposition to Castro's summary judgment motion restates these allegations:

> Castro explained to me [at the El Guapo meeting that] SRLP proposed to open a restaurant and bar at the property, which would be an "ultra lounge." He explained to me that it was to be a hip venue on the Sunset Strip which would have two full-service bars, meal service, music, a disc jockey, happy hours, dancing, promotions and special events, among other things. He also told me that Sunset Beach would be operating under the exact same guidelines as Dublin's had operated previously. . . . Castro further explained to me that Sunset Beach would be open until 2:00 a.m. each night, and that it was intended to compete with other such venues on the Sunset Strip as Saddle Ranch Chop House and Miyagi's. . . . The real attraction of these venues is the bar/nightlife scene. They both have large bars which are their main attractions, and are frequently doing business at their bars until 2:00 a.m.

Except for the alleged representation that he had invested his own money, in his declaration in support of summary judgment, Castro does not deny that he made any of these statements to Donlinger at the El Guapo. As Castro summarizes what was said, "I explained [to Donlinger] our concept of what Sunset Beach would be, and how we expected to fund construction without any debt financing (such as a construction loan from a bank)."

Castro makes no comment in his declaration regarding Donlinger's allegation that, by describing the proposed business as "an ultra lounge," he thereby implied it would include a full-service bar that would serve alcohol to customers who were not also dining at the restaurant. He was later asked in his deposition to explain his concept of an ultra lounge:

> Question: Back in 2004 and 2005, did you have an understanding of what an ultra lounge was?

> Castro: Yes.
>
> . . . .
>
> Question: Back in 2004 and 2005, your understanding of [ultra lounge], did it include a place where someone could go and get a drink without having to order food?
>
> Castro: Yes.
>
> Question: Did it include a place where someone could go and actually walk up to a bar, sit at the bar, and have a drink there, without having to worry about being put at a restaurant table to eat?
>
> Castro: Yes.

Castro Dep. 33:13-15, 34:3-11 (December 2, 2009).

Between December 2004 and May 2005, Castro and Donlinger had several more meetings, telephone conversations and email exchanges regarding Donlinger's possible investment in SRLP. Donlinger alleges that in those communications Castro repeated his statements that Sunset Beach would stay open until 2:00 a.m. every day of the week, with music and dancing.

In one email communication on February 25, 2005, Donlinger requested that Castro send him the floor plans for the restaurant so that he could show them to other potential investors. In response, Castro sent the floor plans, which showed an espresso bar on the first floor and a sushi bar on the second. At that time, Castro also wrote, "Keep in mind, terms such as espresso bars and sushi bars are simply ways to get around the permitting process. They will simply be alcohol bars."

On March 25, 2005, in a telephone conversation, Castro informed Donlinger that he was about to "close the fund to new investors." Donlinger told Castro that he planned on becoming an investor. Castro then joined Marlton in the call, who

congratulated Donlinger on his involvement in "the next hottest club in L.A."

On April 21, 2005, Castro attended a hearing before the City of West Hollywood Planning Commission where SRLP was granted its MCUP. However, the MCUP contained several important conditions, including:

- Condition 10.12. Hours of operation: Lunch (weekdays only) 11:30 a.m. to 2:30 p.m. Dinner Sunday-Thursday 5:30 p.m. to 12:30 a.m., with alcohol consumption and service ending at 11:30 p.m. Dinner Friday and Saturday 5:30 p.m. to 1:30 a.m., with alcohol consumption and service ending at 12:30 a.m.

- Condition 10.14. Sale, service and consumption of alcohol only permitted when accompanied by meal service, or to patrons waiting for a table for meal service.

- Condition 10.15. Patrons not permitted to be served alcohol at the espresso bar unless they are seated at the bar for meal service.

- Condition 10.23. No happy hour or alcohol related promotions permitted.

- Condition 11.12. Restaurant may not limit the entry of minors into the establishment.

On May 17, 2005, apparently unaware of the conditions in the MCUP, Donlinger signed a Subscription Agreement and invested $150,000 of his own funds in SRLP in exchange for three limited partnership units. Among the provisions in the Subscription Agreement relevant to the current appeal are the following:

- That a copy of the PPM was provided to Subscriber (i.e., Donlinger); and that Subscriber represented that he had "received, read and is familiar with the" PPM.

- That Subscriber represented that he is a sophisticated investor, knowledgeable and experienced in financial and business matters and is capable of evaluating the merits and risks of an investment. That Subscriber is aware of the highly speculative nature of any investment in the partnership.

- That the imposition of non-standard restrictions on the liquor license could materially adversely affect the proposed business of the partnership. However, the Subscription Agreement also provides that there are numerous licenses and permits, including the liquor license and "no assurances can be made that they will be obtained and, if so, that there will not be any additional conditions imposed on the Partnership that are not currently anticipated."

Of paramount concern in this appeal is what the bankruptcy court and parties refer to as a "disclaimer clause" in the Subscription Agreement. There are actually two "disclaimer" or waiver clauses.[3] The first appears at ¶ 5(x), and provides that: "Subscriber has not received any representations or warranties from the General Partners, the Partnership or any of their employees or agents, other than those expressly set forth in this Agreement and the Investment Summary." Then, at ¶ 7(iv), the Subscription Agreement provides: "Entire Agreement. This Agreement contains the entire agreement of the parties with respect to the subject matter of this Agreement, and the parties shall not rely upon any representations, covenants or other agreements that are not set forth in this Agreement."

As early as the El Guapo meeting in December 2004 where he offered Donlinger the Equity Bonus Plan, Castro had encouraged Donlinger to recruit additional investors in SRLP. Donlinger did just that. From December 2004 through July 2005, Donlinger passed information he had received from Castro to his former boss, Joel Leonard, to solicit Leonard's company, WCB, to invest in SRLP. The declarations of both Donlinger and Leonard submitted in opposition to Castro's summary judgment motion state that

[3] The parties and the court used the terms disclaimer and waiver interchangeably.

Donlinger specifically passed on Castro's representations that Sunset Beach would have two full service bars, meal service, music, disc jockeys, dancing, promotions and special events.

Castro acknowledged during his deposition that he was aware and expected that Donlinger would convey the information Castro gave him to Leonard. And although Castro had only one brief telephone conversation with Leonard, he did provide copies of the PPM and Subscription Agreement to Leonard. As Leonard would later summarize, from the PPM and oral representations conveyed to him by Donlinger, he was led to believe that his company, WCB, would be "buying into a bar and nightclub in the nightlife hospitality industry, and not merely a restaurant." Leonard caused WCB to invest $150,000 in SRLP on August 2, 2005; Leonard signed the Subscription Agreement.

In late Summer 2005, construction commenced on Sunset Beach. At the same time, Marlton left his management duties at Sunset Beach to work on a movie project in Southeast Asia. In December 2005, Castro hired Barnaby Holm to replace Marlton.

By April 2006, Castro contacted Donlinger, telling him that construction costs had exceeded expectations and offered Donlinger the opportunity to invest an additional $200,000 in the partnership in return for 24.49% of cash distributions received by Gardner [general partner of SRLP controlled by Castro] from Sunset Beach. A Consulting Agreement indicates that Donlinger, through his controlled limited liability company, Milo, invested $200,000 in SRLP on April 19, 2006. Donlinger would later testify in his declaration opposing summary judgment that he invested the additional $200,000 on behalf of Milo based on the oral

representations of Castro and the statements in the PPM.

Despite numerous problems, Sunset Beach opened in September 2006. However, the financial problems continued to escalate. Between September and November 2006, Sunset Beach was cited for five violations of the MCUP. Castro was dissatisfied with the management performance of Holm and discharged him in November 2006. Marlon returned shortly thereafter, but his participation was insufficient to cure the problems. Castro and Marlton attempted a relaunch of the restaurant, renaming Sunset Beach as The Beach on Sunset. Nothing succeeded, and in February 2008, the restaurant was forced to close.

The Litigation

On May 5, 2008, Castro and his wife, Jessica, filed a joint petition for relief under chapter 7. On August 11, 2008, Appellants filed a complaint against Castro asking the bankruptcy court to declare that their claims against Castro were excepted from discharge under §§ 523 (a)(2)(A), (a)(4), (a)(6) and (a)(19)(A)(1). Appellants dropped several claims in their Second Amended Complaint filed on February 25, 2009, this time alleging nondischargeability solely under §§ 523(a)(2)(A) and (a)(4). Regarding the (a)(2)(A) claim, the Second Amended Complaint alleged that, from December 2004 through December 2005, Castro orally, and through the PPM, made misrepresentations to Donlinger, and through Donlinger, to Leonard/WCB and Milo, that (1) Sunset Beach was going to be a full service bar and "ultra lounge"; (2) Sunset Beach would remain open until 2:00 a.m. seven days a week; (3) Sunset Beach was taking over the permits of Dublins to operate a full service bar; (4) there would be promotions, dancing, and

Happy Hours at the restaurant; (5) Sunset Beach's limited partners would be paid on a "first money out to limited partners" basis; (6) Castro invested his own moneys in Sunset Beach; (7) Castro misstated Holm's qualifications to be manager of a restaurant; and (8) Castro withheld information on the serious financial difficulties of the restaurant which resulted in its borrowing approximately $1 million from another party, Jerry Nelson. The Second Amended Complaint alleged that Castro knew these representations were false when he made them and, specifically, that Castro made the representations when he had already caused SRLP to apply for an MCUP that was materially inconsistent with the representations.

As to the (a)(4) claim, Appellants alleged that Castro had breached his fiduciary duty to his partners by embezzling funds of the partnership, and that they were damaged by Castro's acts of defalcation resulting in their loss of their investments of $500,000.

For the two claims, Appellants sought compensatory and punitive damages, and a judgment declaring the damage awards excepted from discharge under §§ 523(a)(2)(A) and (a)(4).

Castro filed a motion for summary judgment on February 15, 2010, arguing that there were no genuine issues of material fact regarding any of the claims in the Second Amended Complaint. Castro argued that the record showed that he either never made the misrepresentations as alleged in the complaint, or that the representations were in fact true. As to embezzlement or defalcation, Castro asserted that the specific acts cited by Appellants did not constitute embezzlement or defalcation, or that

Castro was not in financial control of SRLP and did not participate in any of the challenged transactions. The motion was supported by declarations from Castro and Marlton, and excerpts from the depositions of Castro and his attorney.

Appellants filed a brief in opposition to the motion on March 19, 2010. Appellants supported their position with declarations from Donlinger and Appellants' attorney, and with excerpts from Donlinger's deposition. In the brief, Appellants argued that Castro knew that Sunset Beach was to be a restaurant, not a full service bar and nightclub, even before he solicited Donlinger's investment. In particular, Appellants noted that the MCUP application Castro filed with the City of West Hollywood was inconsistent with critical elements in the PPM. Moreover, Appellants argued, at the El Guapo meeting, Castro knowingly made written and oral misrepresentations regarding Sunset Beach, and that Castro continued to make material misrepresentations throughout the period when Appellants were considering making their investments, and never informed Appellants that the approved MCUP was inconsistent with those representations. In Appellants' view, genuine issues of fact remained for trial regarding the § 523(a)(2)(A) claim. As to the (a)(4) claim, Appellants repeated their assertions from the Second Amended Complaint.

Castro responded to Appellants' brief on April 6, 2010. He argued that Appellants could not prove that he had made any misrepresentations prior to their investment. As to the embezzlement claims, Castro argued that he had no control over the finances of SRLP at the times alleged and therefore Appellants could not prove embezzlement. Regarding defalcation, Castro

argued that Appellants could not prove that Castro failed to account for any of Sunset Beach's money.

The hearing on Castro's motion for summary judgment took place on May 11, 2010. From the beginning of the hearing, the bankruptcy judge made it clear that, in assessing the (a)(2)(A) claims, he would not consider any alleged misrepresentations by Castro that were not in the PPM or Subscription Agreement:

> THE COURT: Let me make sure I understand what representations are properly before the Court. This was a case where there was an offering circular and subscription agreement?
>
> TARLOW (Appellants' attorney): Yes, your Honor.
>
> THE COURT: And those documents said that they embody the entire agreement between the parties and there are no representations or warranties given apart from that?
>
> TARLOW: That's what the papers said, but there were other representations made.
>
> THE COURT: And they were disclaimed in the agreement, were they not?
>
> TARLOW: There was a disclaimer in the agreement, yes.
>
> THE COURT: So under California law, they disappear.

Hr'g Tr. 1:20-2:9 (May 11, 2010).

In its ruling at the end of the hearing, the bankruptcy court repeated its decision to effectively decline to consider any oral representations: "With respect to the fraud claims, apart from the two documents, the subscription agreement and the [PPM], [Appellants] have disclaimed any other representations and warranties. So I can't give weight to any others." Hr'g Tr. 31:21-25.

The bankruptcy court next examined the PPM, and noted that the evidence before the court showed that the PPM was a "concept"

document. The court then explained that, in its view, Castro's written statements about his business concepts and strategies could not support a fraud claim:

> The evidence before the Court is that there was a concept document, set forth a concept. Concepts are never realized exactly the way they're originally put forth, at least not in this kind of context. That there should be a variation is not surprising. It's expected and does not give rise to a claim for fraud.
>
> There is also business strategy. Business strategy is different from specific representations also. Business strategy is not always realized. That does not — and if the business strategy is not realized . . . that alone is not a basis for a claim of fraud.
>
> In this adversary proceeding, the claims of fraud are based on particular details, not on the overall business strategy or the overall concept. And so on these grounds, then I find there's no triable issue of fact, and summary judgment has to be granted to the Defendant.

Hr'g Tr. 32:5-23 (May 11, 2010).

As to the § 523(a)(4) claim, the bankruptcy court determined that Appellants had not presented adequate evidence to support the claims of embezzlement or defalcation. The court noted that a defalcation requires the existence of a trust relationship between the parties, which Appellants had not shown. Instead, the court observed that Appellants had raised conclusory arguments about Castro's alleged failure to explain various financial transactions, and the court was satisfied with Castro's explanations. The court concluded that Appellants had not shown a material question of fact remained regarding the defalcation or embezzlement claims to justify nondischargeability under § 523(a)(4).

The bankruptcy court entered its order granting summary judgment to Castro on July 28, 2010. Appellants filed a timely appeal on August 11, 2010.

JURISDICTION

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

ISSUE

Whether the bankruptcy court erred in granting summary judgment to Castro dismissing Appellants' complaint for exceptions to discharge under §§ 523(a)(2)(A) and (a)(4).

STANDARD OF REVIEW

We review de novo a bankruptcy court's decision to grant summary judgment. Wood v. Stratos Prod. Dev. (In re Ahaza Sys., Inc.), 482 F.3d 1118, 1123 (9th Cir. 2007) (stating that both the Court of Appeals and the BAP apply de novo review to a bankruptcy court's decision to grant summary judgment).

DISCUSSION

Summary judgment may be granted "if the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law." Civil Rule 56(c)(2), incorporated by Rule 7056. Barboza v. New Form, Inc. (In re Barboza), 545 F.3d 702, 707 (9th Cir. 2008). The court does not weigh evidence in resolving a motion for summary judgment, but rather determines only whether any material factual dispute remains for trial. Covey v. Hollydale Mobilehome Estates, 116 F.3d 830, 834 (9th Cir. 1997).

The party seeking summary judgment bears the initial burden

of establishing the absence of a genuine issue of material fact. Margolis v. Ryan, 140 F.3d 850, 852 (9th Cir. 1998). A dispute is genuine if there is sufficient evidence for a reasonable fact finder to hold in favor of the non-moving party, and a fact is "material" if it might affect the outcome of the case. Far Out Prods., Inc. v. Oskar, 247 F.3d 986, 992 (9th Cir. 2001) (citing Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248-49 (1986)). When the movant has carried its burden under Civil Rule 56(c), the non-moving party must come forward with "specific facts showing that there is a genuine issue for trial." Id. at 1035 (quoting Civil Rule 56(e)); Hayes v. Palm Seedlings Partners (In re Agric. Research), 916 F.2d 528, 533 (9th Cir. 1990).

The standard of proof for discharge exceptions is a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279 (1991); Melton v. Moore, 964 F.2d 880 (9th Cir. 1992).

In this appeal, we conclude that the bankruptcy court erred when it determined that, because of the disclaimer clause in the Subscription Agreement, it should not consider any other alleged representations made by Castro to Appellants. In doing so, the bankruptcy court effectively refused to consider what we deem were "specific facts showing that there is a genuine issue for trial." When those facts are considered, it is clear that genuine issues of material fact remained for trial. The bankruptcy court also erred when it concluded that the statements in the PPM were “concept” or “business strategy” only and, as a result, could not constitute the basis for a fraud claim. Consequently, we will vacate the bankruptcy court’s grant of summary judgment to Castro on Appellants’ claims under § 523(a)(2)(A).

However, we conclude that Castro established the absence of a genuine issue of material fact regarding the claims under § 523(a)(4), and that Appellants failed to come forward with evidence to establish that a genuine issue of material fact remained for trial. Thus, we will affirm the bankruptcy court's grant of summary judgment to Castro on nondischargeability under § 523(a)(4).

I.
The bankruptcy court erred in granting summary judgment to Castro on the § 523(a)(2)(A) claim.

Section 523(a)(2)(A) provides that, "A discharge under section 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[.]" This provision mirrors the concept of common law fraud, and requires a showing of: 1) misrepresentation of a material fact; 2) knowledge of the falsity of the representation; 3) intent to induce reliance; 4) justifiable reliance; and 5) damages. Apte v. Japra (In re Apte), 96 F.3d 1319, 1322 (9th Cir. 1996); Tsurukawa v. Nikon Precision, Inc. (In re Tsurukawa), 287 B.R. 515, 520 (9th Cir. BAP 2002); see Turtle Rock Meadows Homeowners Ass'n v. Slyman (In re Slyman), 234 F.3d 1081, 1086 (9th Cir. 2000) (holding that in two party transactions strict evidentiary proof of misrepresentation and reliance is required); see also Field v. Mans, 516 U.S. 59, 61 (1995) (holding that § 523(a)(2)(A) elements mirror common law fraud).

Appellants argued that disputed issues of material fact existed concerning whether Castro had committed fraud in inducing Appellants to invest in Sunset Beach. In particular, Appellants attempted to show the bankruptcy court that Castro made misrepresentations of material facts via both the written documents given to them, and through his oral statements. Among the false statements allegedly made were that Sunset Beach was going to be a full service bar and "ultra lounge" that would serve alcohol without requiring patrons to eat meals there; that Sunset Beach would remain open until 2:00 a.m. seven days a week as a nightlife center competing with neighboring facilities, by using disc jockeys, promotions, dancing, and “Happy Hours”; that Sunset Beach's limited partners would be paid on a "first money out to limited partners" basis; that Castro had invested his own moneys in Sunset Beach; that Castro misstated Holm's qualifications to be manager of a restaurant; and that Castro withheld information on the serious financial difficulties of the restaurant which resulted in its borrowing approximately $1 million from another party, Jerry Nelson. Although Appellants argued that their position was supported in many respects by the contents of the PPM, each of the claims rested, at least in part, on the oral representations made by Castro at the El Guapo meeting with Donlinger, and in his continuing communications with Donlinger that he knew would be passed on to Leonard during the period before Appellants made their investments in Sunset Beach.

The bankruptcy court ruled that, under California law, because of the disclaimer provision in the contract documents the court was prevented from considering external, or parol evidence

of other representations allegedly made by Castro. This legal conclusion was incorrect.

A claim for nondischargeability of a debt under 523(a)(2)(A), alleging fraudulent concealment, fraud and misrepresentation to obtain funds may be analyzed as a claim for fraud in the inducement under California law. Franklin v. Commonwealth Fin. Corp. (In re Franklin), 922 F.2d 536, 539 (9th Cir. 1991); In re Nga Tuy Pham, 2009 WL 3367046 (Bankr. N.D. Cal. 2009) ("A debt is excepted from discharge if it results from fraud in the inducement. 11 U.S.C. § 523(a)(2)[A]."); see also O'Neil v. Goode (In re Goode), 2011 Bankr. LEXIS 607, at *12 (Bankr. E.D. Tenn 2011) (applying Tennessee law); Gonzalez v. Cantu (In re Cantu), 2009 Bankr. LEXIS 4447, at *12 (Bankr. S.D. Tex. 2009) (applying Texas law); Gamble v. Overton (In re Overton), 2009 Bankr. LEXIS 478, at *17 (Bankr. D. Idaho 2009) (applying Wyoming law). Where a creditor is induced to enter into an agreement by fraudulent misrepresentations, not only does California's law of fraud in the inducement apply, but any disclaimer in the agreement cannot be used to prevent the court from considering oral representations. As a leading treatise on California law opines, a party that is charged with fraudulently inducing another party to enter an agreement

> cannot absolve himself from the effects of his fraud by any stipulation in the contract, either that no representations have been made, or that any right which might be grounded upon them is waived. Such a stipulation or waiver will be ignored, and parol evidence of misrepresentations will be admitted, for the reason that fraud renders the whole agreement voidable, including the waiver provision.

B.E. Witkin, SUMMARY OF CALIFORNIA LAW CONTRACTS § 304(1) (10th ed.

2010). California courts have consistently recognized as well-settled law that parol or extrinsic evidence is admissible to prove fraud in the inducement of a contract "even though the contract recites that all conditions and representations are embodied therein." Ron Greenspan Volkswagen, Inc. v. Ford Motor Land Dev. Corp., 32 Cal. App. 4th 985, 990 (Cal. Ct. App. 1995) (quoting Ferguson v. Koch, 268 P. 342, 347 (Cal. 1928)); Morris v. Harbor Boat Building Co., 247 P.2d 589, 596 (Cal. Ct. App. 1952) ("[I]t was never intended that the parol evidence rule should be used as a shield to prevent the proof of fraud . . . even though the contract recites that all conditions and representations are embodied therein."); Oak Industries, Inc. v. Foxboro Co., 596 F. Supp. 601, 607 (S.D. Cal. 1984) (holding that under California law, extrinsic evidence is admissible to prove fraud in the inducement notwithstanding a contract provision that no representations have been made other than those stated in the agreement); Applications Inc. v. Hewlett Packard Co., 501 F. Supp. 129, 134 (S.D.N.Y. 1980) (applying California law, holding that parol evidence is admissible to prove fraud despite contract provision waiving representations not stated in the agreement). Therefore, under the controlling law, the disclaimer clause in the Subscription Agreement did not insulate Castro from Appellants' claims that he defrauded them through oral misrepresentations, thereby inducing them to invest in Sunset Beach.

After incorrectly declining to consider the alleged oral misrepresentations made by Castro to induce Appellants to invest, the bankruptcy court next examined the effect of the representations made in the written PPM. The court ruled that

statements concerning the nature of the proposed Sunset Beach operation were "concepts" or "business strategy," or that those statements were in fact true representations. The bankruptcy court then concluded, without citing anything in the record to support its factual conclusion, that business concepts and strategies always vary from the final results. As a result, the bankruptcy court concluded that Appellants could not justifiably rely upon such statements to support a claim for fraud.

We disagree with the bankruptcy court's approach in this procedural context, and its conclusion. For example, the PPM states, "The sophisticated, full-service bar will offer a broad selection of domestic and imported bottled and draft beers, premium wines, and specialty drinks, along with top-shelf liquor." Appellants argue that this statement supports their position in that a "sophisticated, full service bar" implies a bar available for drinks without food. The bankruptcy court found that those types of liquor were, indeed, actually served at Sunset Beach, and that the PPM did not indicate that the full-service was to be a bar to accommodate late-night, non-diners. However, when viewed in the context of the numerous oral representations made by Castro that Sunset Beach would have a "full-service bar" and that the restaurant was also intended as a nightlife spot, and especially in view of the exchange of emails that the espresso and sushi bars shown on proposed floor plans were actually to be, in Castro's own words, "alcohol bars," a reasonable trier of fact could conclude that Sunset Beach was not merely to be a restaurant but also a club catering to a nightlife crowd. In the context of a summary judgment proceeding, the bankruptcy court was not empowered to

determine whether Sunset Beach was in fact intended or represented by Castro to be a nightclub, but only with whether there was a triable issue of fact in that regard. And a fair view of the evidence submitted to the bankruptcy court could lead a trier of fact to find that, when the written documents are viewed together with the oral representations, several triable issues of fact emerged. It was therefore error for the bankruptcy court to conclude, as a matter of fact, that any "concept" or "business strategy" representations were not reliable, or that the other statements in the PPM were true and exclusive to a restaurant-only interpretation.

Appellants' submissions to the bankruptcy court addressed each of the elements under the case law to establish an exception to discharge under § 523(a)(2)(A). Appellants submitted proof that Castro made a variety of representations to Donlinger that Sunset Beach would be an ultra lounge and full-service bar. Because such representations were seemingly inconsistent with the MCUP previously issued by the local authorities to Castro, Appellants have shown the existence of at least an issue of fact whether Castro knew these statements to Donlinger were false when he made them. The record also shows some evidence that Castro intended Appellants to rely on his representations so they would invest in the business by withholding other information from them, such as the true terms of the MCUP. While it is true that Appellants signed a Subscription Agreement containing a provision disclaiming that they relied upon other information in investing, when the record as a whole is considered, issues of fact exist as to whether they justifiably relied on Castro's representations,

and whether, without those representations, they would have invested in Sunset Beach. Finally, it is undisputed that Appellants lost their investments, and arguably suffered damages as a result of Castro's alleged fraud. Clearly, then, there are triable issues of fact on Appellants' fraud claims.

In sum, the bankruptcy court erred when it ruled that it could not consider representations made by Castro other than in the PPM because of the disclaimer provision in the Subscription Agreement. It also erred in concluding that the statements in the PPM about Sunset Beach were concepts and business strategy that could not serve as a basis for a fraud claim by Appellants. Because the record demonstrates that there were genuine issues of fact as to Appellants' fraud claims, a trial was required. We must therefore vacate the bankruptcy court's grant of summary judgment to Castro on the § 523(a)(2)(A) issues, and remand this action for trial.

II.
The bankruptcy court did not err in granting summary judgment to Castro under § 523(a)(4).

Section 523(a)(4) provides that a " discharge under section 727 . . . does not discharge an individual debtor from any debt-- . . . (4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny." In an action to except a debt from discharge under § 523(a)(4), a creditor must establish: (1) that an express trust existed between the debtor and creditor; (2) that the debt was caused by the debtor's fraud or defalcation; and (3) that the debtor was a fiduciary to the creditor at the time the debt was created. Otto v. Niles, (In re Niles), 106 F.3d

1456, 1459 (9th Cir. 1997); Nahman v. Jacks (In re Jacks), 266 B.R. 728, 735 (9th Cir. BAP 2001).

The bankruptcy court properly found that there was no express trust between Castro and Appellants. An express trust in California requires three elements: 1) sufficient words to create a trust; 2) a definite subject; and 3) a certain and ascertained object or res." Schlecht v. Thornton (In re Thornton), 544 F.2d 1005, 1007 (9th Cir. 1976); Destfino v. Bocking (In re Destfino), 2010 Dist. LEXIS 107749, at *7 (E.D. Cal. 2010). There is simply no evidence that the parties intended to create a trust.

As to Appellants' more specific arguments that Castro embezzled funds entrusted to him, Appellants failed to provide sufficient facts to support their argument. Under federal law, embezzlement in the context of § 523(a)(4) is "the fraudulent appropriation of property by a person to whom such property has been entrusted or into whose hands it has lawfully come." Transamerica Comm. Fin. Corp. v. Littleton (In re Littleton), 942 F.2d 551, 555 (9th Cir. 1991) (quoting Moore v. United States, 160 U.S. 268, 269 (1885)). The bankruptcy court found, and we agree, that Appellants submitted no evidence to support a claim of embezzlement. Instead, Appellants made numerous conclusory statements that SRLP funds had been used for improper purposes, but provided no evidence that Castro was in control of the finances of SRLP or that funds had been used for an improper purpose. On the contrary, the court found that the only evidence before the court was that Castro had properly accounted for each of the alleged misuses.

Because there was no triable issue of fact regarding whether

Castro and Appellants' relationship was a trust for purposes of § 523(a)(4) or that Appellants had submitted evidence in support of their claims of embezzlement, the bankruptcy court correctly granted summary judgment to Castro.

CONCLUSION

We VACATE the bankruptcy court's order granting summary judgment to Castro on Appellants' § 523(a)(2)(A) claim, and REMAND this matter to the bankruptcy court for further proceedings consistent with this decision. We AFFIRM the bankruptcy court's order granting summary judgment to Castro on the § 523(a)(4) claim.