

**AUG 16 2005**

**HAROLD S. MARENUS, CLERK  
U.S. BKCY. APP. PANEL  
OF THE NINTH CIRCUIT**

**NOT FOR PUBLICATION**

**UNITED STATES BANKRUPTCY APPELLATE PANEL  
OF THE NINTH CIRCUIT**

6	In re:	)	BAP No.	CC-04-1584-KMoB
		)		
7	ISIDORE KAWA,	)	Bk. No.	LA 01-44191-AA
		)		
8	Debtor.	)	Adv. No.	LA 02-01303-AA
		)		
9	_____	)		
		)		
10	NATIONAL UNION FIRE INSURANCE	)		
	COMPANY OF PITTSBURGH, as	)		
11	assignee of FIRST	)		
	PROFESSIONAL BANK, N.A.,	)		
12		)		
	Appellant,	)		
13		)		
	v.	)	<b>MEMORANDUM*</b>	
14		)		
	ISIDORE KAWA,	)		
15		)		
	Appellee.	)		
16	_____	)		

Submitted without Oral Argument on July 29, 2005  
at Pasadena, California

Filed - August 16, 2005

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

Honorable Alan M. Ahart, Bankruptcy Judge, Presiding

Before: KLEIN, MONTALI, and BRANDT, Bankruptcy Judges.

\_\_\_\_\_  
\*This disposition is not appropriate for publication and may not be cited except when pertinent under the doctrine of law of the case or the rules of res judicata, including issue and claim preclusion. See 9th Cir. BAP Rule 8013-1.

1 A creditor appeals from a judgment in favor of the debtor  
2 after a trial on a complaint to except debt from discharge under  
3 11 U.S.C. §§ 523(a)(2)(A) and (a)(2)(B). We AFFIRM.

4  
5 FACTS

6 The debtor, Isidore Kwaw, M.D., filed a chapter 7 bankruptcy  
7 case on November 15, 2001.

8 First Professional Bank, N.A. ("Bank") commenced an  
9 adversary proceeding seeking nondischargeability of a debt  
10 pursuant to 11 U.S.C. §§ 523(a)(2)(A), 523(a)(2)(B), and  
11 523(a)(6).

12 Appellant, National Union Fire Insurance Company of  
13 Pittsburgh, is the assignee of the Bank.<sup>1</sup>

14 The complaint arose from a series of bank loans and  
15 overdrafts in the total amount of approximately \$2.4 million on  
16 which the debtor was liable.

17 The complaint alleged that the debtor, a medical doctor,  
18 supplied the Bank's former president with prescription pain  
19 killers (to support her habit) in return for bank loans for which  
20 he was not creditworthy.<sup>2</sup> The Bank specifically alleged that the  
21 financial statements the debtor provided to the Bank were largely  
22 false and fraudulent in that he overstated his financial  
23 condition by understating his debts and tax obligations.

24  
25 \_\_\_\_\_  
26 <sup>1</sup>For convenience, we refer to the "Bank" as plaintiff, even  
27 though the record suggests that the assignment to National Union  
28 Fire Insurance Company of Pittsburgh occurred before the trial.

<sup>2</sup>The Bank sued its former president in state court for  
breach of fiduciary duty.

1           During discovery, the Bank attempted to depose the debtor.  
2 The debtor's counsel asserted the debtor's Fifth Amendment  
3 privilege against self-incrimination and instructed the debtor  
4 not to answer most of the substantive questions regarding his  
5 loans, his financial statements, his employment, and his  
6 relationship with the Bank and the Bank's former president.

7           The Bank later filed a Motion in Limine seeking to exclude  
8 all testimonial and documentary evidence of the debtor at trial  
9 because of the debtor's repeated invocation of the Fifth  
10 Amendment privilege during discovery.

11           Trial was held on November 4, 2004. At the time of trial,  
12 the court granted the Bank's Motion in Limine and excluded all  
13 testimony and declarations of the debtor.

14           At the conclusion of trial, the court rejected the Bank's  
15 complaint on the merits. It ruled that there was insufficient  
16 evidence of fraud, collusion, or conspiracy to support a claim  
17 under § 523(a)(2)(A).

18           With respect to the count under § 523(a)(2)(B), the court  
19 found that a written financial statement provided by the debtor  
20 was materially false, but found that the Bank did not  
21 "reasonably" rely on that financial statement in making the loans  
22 to the debtor. The court further declined to find that the  
23 debtor presented the particular financial statement with an  
24 intent to deceive.

25           Based on its findings, the court ruled in favor of the  
26 debtor on all counts.<sup>3</sup>

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27  
28           <sup>3</sup>Although the court's ruling did not mention the Bank's  
§ 523(a)(6) claim, the Bank does not argue that theory on appeal.  
(continued...)

1 This timely appeal ensued.

2  
3 JURISDICTION

4 The bankruptcy court had jurisdiction via 28 U.S.C. §§ 1334  
5 and 157(b)(1). We have jurisdiction under 28 U.S.C. § 158(a)(1).  
6

7 ISSUE

8 Whether the court erred when it ruled in favor of the debtor  
9 on the Bank's complaint to except debt from discharge under  
10 §§ 523(a)(2)(A) and (a)(2)(B).  
11

12 STANDARD OF REVIEW

13 The bankruptcy court's factual findings are reviewed for  
14 clear error. Banks v. Gill Distrib. Ctrs., Inc. (In re Banks),  
15 263 F.3d 862, 867 (9th Cir. 2001). We review evidentiary rulings  
16 for an abuse of discretion. Rudy-Glanzer v. Glanzer, 232 F.3d  
17 1258, 1263 (9th Cir. 2000).  
18

19 DISCUSSION

20 The Bank sets forth three arguments for why the bankruptcy  
21 court erred. First, the Bank contends that the court erred in  
22 finding, under § 523(a)(2)(B), that it did not "reasonably" rely  
23 on the debtor's written financial statements. Second, because  
24 the debtor invoked his Fifth Amendment rights, the Bank contends  
25 that the burden of proof should have shifted to the debtor to  
26 "justify his acts in submitting false financial documents."  
27

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28 <sup>3</sup>(...continued)

Any issue in that respect is deemed waived. Turner v. Marshack  
(In re Turner), 186 B.R. 108, 117 (9th Cir. BAP 1995).

1 Because the court did not shift the burden of proof, but rather  
2 placed the entire burden of proof on the Bank, it is contended  
3 that the court erred. Finally, it is also contended that the  
4 debtor's assertion of his Fifth Amendment rights should have  
5 caused the bankruptcy court to draw negative inferences as to all  
6 of the questions the debtor refused to answer. If the court had  
7 properly drawn negative inferences, then the Bank argues that it  
8 would have prevailed on every element of its § 523(a)(2)(B)  
9 claim.

10 On appeal, the Bank continues to argue that the money the  
11 debtor owes to it should be excepted from discharge under either  
12 §§ 523(a)(2)(A) or (a)(2)(B).<sup>4</sup>

13 Section 523(a)(2) provides, in pertinent part:

14 (a) A discharge under section 727, 1141, 1228(a),  
15 1228(b), or 1328(b) of this title does not discharge an  
individual debtor from any debt - . . .

16 (2) for money, property, services, or an  
17 extension, renewal, or refinancing of credit, to  
the extent obtained by -

18 (A) false pretenses, a false  
19 representation, or actual fraud, other  
20 than a statement respecting the debtor's  
or an insider's financial condition;  
[or]

21 (B) use of a statement in writing -

22 (i) that is materially false;

23 (ii) respecting the debtor's or an  
24 insiders financial condition;

25 (iii) on which the creditor to whom  
26 the debtor is liable for such  
money, property, services, or  
credit reasonably relied; and

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27  
28 <sup>4</sup>As noted, the Bank makes no argument with respect to  
§ 523(a)(6).

1 (iv) that the debtor caused to be  
2 made or published with intent to  
deceive[.]

3 11 U.S.C. § 523(a)(2)(A)-(B) (emphasis supplied).

4 Subsections (A) and (B) are mutually exclusive. See Field  
5 v. Mans, 516 U.S. 59, 66 (1995). Subsection (A) “applies  
6 expressly when the debt follows a transfer of value or extension  
7 of credit induced by falsity or fraud (not going to financial  
8 condition[.])” Id. Subsection (B) applies “when the debt follows  
9 a transfer or extension induced by a materially false and  
10 intentionally deceptive written statement of financial condition  
11 upon which the creditor reasonably relied.” Id.

12 The type of fraud contemplated by § 523(a)(2)(A) is actual  
13 fraud. Citibank (South Dakota), N.A. v. Eashai (In re Eashai),  
14 87 F.3d 1082, 1086-87 (9th Cir. 1996). Actual fraud under  
15 § 523(a)(2)(A) is established by proving that:

- 16 (1) the debtor made the representations;
- 17 (2) that at the time he knew they were false;
- 18 (3) that he made them with the intention and purpose of  
19 deceiving the creditor;
- 20 (4) that the creditor relied on such representation; and
- 21 (5) that the creditor sustained the alleged loss and damage  
22 as the proximate result of the representations having been made.  
23 Id. at 1086.

24 The reliance element is one of justifiable reliance. Field,  
25 516 U.S. at 77; Eashai, 87 F.3d at 1090.

26 The Bank’s Fifth Amendment argument affects our analysis  
27 under both subsections.

1           The Fifth Amendment to the United States Constitution  
2 provides that “[n]o person . . . shall be compelled in any  
3 criminal case to be a witness against himself. . . .” U.S. CONST.  
4 amend V. The privilege applies to civil proceedings. See  
5 Lefkowitz v. Turley, 414 U.S. 70, 77 (1973).

6           In civil proceedings, the trier of fact is entitled, but not  
7 required, to draw negative inferences from a party’s invocation  
8 of his or her Fifth Amendment right. Baxter v. Palmigiano, 425  
9 U.S. 308, 317-18 (1976); Rudy-Glanzer, 232 F.3d at 1264.

10 Moreover, negative inferences are usually only drawn “when  
11 independent evidence exists of the fact to which the party  
12 refuses to answer.” Rudy-Glanzer, 232 F.3d at 1264. “[W]hen  
13 there is no corroborating evidence to support the fact under  
14 inquiry, the proponent of the fact must come forward with  
15 evidence to support the allegation, otherwise no negative  
16 inference will be permitted.” Id.

17           A negative inference may be drawn when there is a  
18 “substantial need for the information and there is not another  
19 less burdensome way of obtaining that information.” Id. at 1265.

20           In this instance, the court declined to draw the negative  
21 inferences urged by the Bank.

22           The Bank argues that because the debtor refused to answer  
23 all questions regarding his submission of false/fraudulent  
24 financial statements to the Bank, the Bank was entitled to the  
25 benefit of negative inferences to be drawn on every question the  
26 debtor refused to answer. Had the court done so, the inferences  
27 would have established that the debtor intentionally and  
28 materially misrepresented facts to the Bank to obtain the loans

1 and that the Bank relied on those false statements. As noted,  
2 however, this is not an accurate statement of law.

3 For a negative inference to be drawn, the Bank was required  
4 to come forward with evidence of the debtor's intent to deceive.  
5 Rudy-Glanzer, 232 F.3d at 1264. Even then, the negative  
6 inference regarding the content of testimony is optional with the  
7 court in the sense that a trier of fact may disbelieve the  
8 testimony.

9 Throughout the trial, the court questioned the Bank's  
10 counsel about what evidence it had of the debtor's intent to  
11 deceive, and, if the financial statements were actually false,  
12 what evidence did the Bank have to show that it would not have  
13 loaned the money to the debtor anyway. No such evidence was  
14 presented so the court properly exercised its discretion by  
15 declining to draw a negative inference from the debtor's silence.

16 Even though the court found that one of the written  
17 financial statements was materially false, it was not persuaded  
18 that the debtor made it with an intent to deceive. We cannot say  
19 that the court was clearly wrong in this respect. Thus, the Bank  
20 did not meet its burden to demonstrate the debtor's intent to  
21 deceive to justify excepting the debt from discharge.

22 With respect to the reliance element under both  
23 §§ 523(a)(2)(A) and (a)(2)(B), the Bank contends that once the  
24 debtor invoked his Fifth Amendment rights, the court should have  
25 shifted to the defendant the burden of going forward with  
26 evidence to rebut the Bank's claim. The Bank argues that if the  
27 court had shifted the burden to the debtor, the ruling on the  
28 Bank's Motion in Limine would have prevented the debtor from



1 testifying and thus the debtor would have had no evidence to  
2 present at trial to rebut the Bank's claims and judgment would  
3 have been in its favor.

4 The Bank cites a bankruptcy court decision from another  
5 circuit, Clark & Gregory, Inc. v. Hanson (In re Hanson), 225 B.R.  
6 366, 372 (Bankr. W.D. Mich. 1998), to support this argument. In  
7 Hanson, the court purported to shift the burden to the defendant  
8 who invoked his Fifth Amendment right "concerning matters  
9 uniquely within his own knowledge." Id.

10 We are not persuaded, however, that Hanson represents the  
11 sweeping proposition for which appellant argues. Moreover, the  
12 present situation is distinguishable because the question of  
13 whether the Bank relied on the debtor's financial statements is  
14 not a matter uniquely within the debtor's knowledge. Thus, we  
15 are not persuaded that Hanson applies.

16 Additionally, one must not conflate the burden of going  
17 forward from the burden of proof. When a burden of going forward  
18 shifts to a defendant, the burden of proof does not necessarily  
19 shift, and a trier of fact may find in favor of a defendant who  
20 does nothing in response to the shifting of the burden of going  
21 forward.

22 Further, the court found that it was unreasonable for the  
23 Bank to continue to loan money to the debtor given the large  
24 amount of defaults, overdrafts, and knowledge by the Bank of the  
25 debtor's precarious financial condition. Cf.  
26 § 523(a)(2)(B)(iii).

27 The court had before it evidence provided by the Bank in the  
28 declaration of its new president that the loan to the debtor had

1 been considered a "problem loan" with the Bank and that the  
2 debtor's loans had been internally classified as "substandard"  
3 since 1996. In 1999, the Bank "wrote-off" overdrafts of the  
4 debtor in the amount of \$124,815.90. Even after writing off the  
5 overdrafts, the Bank's loan committee approved consolidation and  
6 renewal of the debtor's loans and overdrafts. The debtor's loan  
7 balances grew by \$281,000 in 1997, \$647,000 in 1998, \$1,256,686  
8 in 1999, and \$2,245,433 in 2003 (not including the \$124,915.90 in  
9 overdrafts the Bank wrote-off). The bank presented no expert  
10 evidence regarding the reasonableness of its conduct, even in the  
11 declaration of its new president. Thus, the court found that any  
12 reliance on the debtor's financial statements by the Bank was  
13 unreasonable considering the debtor's known "problem" status.

14 We cannot say that the court erred when it refused to grant  
15 the Bank relief under either §§ 523(a)(2)(A) or (a)(2)(B).

#### 17 CONCLUSION

18 The bankruptcy court did not err when it refused to except  
19 from discharge the debt owed to the Bank. AFFIRMED.