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NOT FOR PUBLICATION

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

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re: ) BAP No. CC-12-1344-TaPaKi  
 )  
 6 DAVID BRUCE KLUGE, ) Bk. No. 10-29300-BB  
 )  
 7 Debtor. ) Adv. No. 10-03019-BB  
 )  
 8 \_\_\_\_\_ )  
 )  
 9 DAVID BRUCE KLUGE, )  
 )  
 10 Appellant, )  
 )  
 11 v. ) **MEMORANDUM\***  
 )  
 12 RHI/10223 SEPULVEDA, LLC; )  
 13 ROSENDO GONZALEZ, Chapter 7 )  
 14 Trustee; UNITED STATES )  
 TRUSTEE, )  
 Appellees. )

Argued and Submitted on March 22, 2013  
at Pasadena, California

Filed - April 10, 2013

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

Honorable Sheri Bluebond, Bankruptcy Judge, Presiding

Appearances: Benjamin M. Hill of METAL Law Group, LLP on behalf  
 of Appellant David Bruce Kluge and Alan F. Broidy  
 of Law Office of Alan F. Broidy, APC on behalf of  
 Appellee RHI/10223 Sepulveda, LLC.

Before: TAYLOR, PAPPAS, and KIRSCHER, Bankruptcy Judges.

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



1 against Kluge seeking to bar his discharge under § 727(a)(4).<sup>3</sup>  
2 In its complaint, RHI alleged that Kluge's petition and schedules  
3 contained a number of inaccuracies and omissions, including an  
4 intentional failure to list creditors and assets. In particular,  
5 RHI alleged that Kluge failed to account for income received from  
6 Affirm Direct or to properly account for the nature and value of  
7 his shares in the corporation. It also alleged that Kluge caused  
8 Affirm Direct to transfer money into his wife's personal bank  
9 account and that Kluge and his wife utilized these distributions  
10 for personal and household expenses.

11 The bankruptcy court scheduled a trial for May 23, 2012.  
12 Prior to trial, it entered a stipulated Joint Pre-Trial Order  
13 ("PTO"). The PTO established certain admitted facts, including  
14 that Kluge listed his monthly income as \$0 on his Schedule I and  
15 that he listed his earnings as \$0.01 for the years 2008, 2009,  
16 and 2010 on his SOFA. The PTO also established that Kluge and  
17 his wife owned Affirm Direct and that each held a 50% ownership  
18 interest in the corporation; that at his Rule 2004 Examination,  
19 Kluge testified that the transfers to his wife were income; that  
20 the transfers were for household expenses; and that the amount  
21 transferred each month to his wife was approximately \$2,000. In  
22 addition, the PTO identified the remaining facts and legal  
23 issues<sup>4</sup> to be litigated at trial.

24 The bankruptcy court held a one-day trial on May 23, 2012.

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25  
26 <sup>3</sup> RHI also objected to Kluge's discharge under §§ 727(a)(2),  
727(a)(3), and 727(a)(5).

27 <sup>4</sup> The PTO identified §§ 727(a)(4) and (a)(5) as the sole  
28 issues of law that remained to be litigated.

1 It began the proceeding by narrowing the disputed factual and  
2 legal issues to be tried.<sup>5</sup> The bankruptcy court then heard  
3 testimony, primarily from Kluge, but also from Kluge's wife.

4 As to his scheduled valuation of Affirm Direct, Kluge  
5 testified that he discussed the value of Affirm Direct with his  
6 bankruptcy counsel<sup>6</sup> prior to filing bankruptcy and that, based on  
7 those discussions, he was under the impression that because the  
8 corporation was unprofitable, he was not required to assign it  
9 any value on the schedules. As to money received from Affirm  
10 Direct, he gave facially inconsistent testimony. First, he  
11 denied any receipt of pre-petition salary from Affirm Direct.  
12 But, he acknowledged that the corporation transferred funds to  
13 his wife's account upon his request. Kluge during his testimony  
14 discussed these payments as a return on investment. He explained  
15 that he invested working capital into Affirm Direct when he  
16 started the corporation and continued to do so over the years.  
17 He testified that, according to his bookkeeper, between 2003 and  
18 2009, he intermittently invested approximately \$280,000 into  
19 Affirm Direct. Kluge stated that his bookkeeper advised him

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21 <sup>5</sup> The bankruptcy court determined that most of the disputed  
22 factual issues identified by Kluge were irrelevant to the legal  
23 issues before it. It then narrowed the legal issues as arising  
24 only under § 727(a)(4)(A). In doing so, the bankruptcy court  
25 concluded that it would not consider the § 727(a)(5) claim,  
26 because it did not apply under the circumstances. Ultimately,  
27 the bankruptcy court entered judgment in favor of RHI on the  
28 § 727(a)(4)(A) claim, and judgment in favor of Kluge on all other  
claims.

<sup>6</sup> Kluge was represented by different counsel in the  
adversary proceeding.

1 that, after deducting the \$2,000 monthly transfers to his wife  
2 from the \$280,000, his net unrecovered investment was  
3 approximately \$53,000.

4 Kluge, however, also characterized the distributions as loan  
5 repayments. He testified that Affirm Direct booked these  
6 investments as a "loan from officer," but acknowledged that he  
7 previously (and erroneously) characterized the transactions  
8 during the bankruptcy proceedings as a "loan to officer." Kluge  
9 further testified that he did not consider these transfers to be  
10 income, because it was his own money and because the corporation  
11 booked the transfers as a loan. But Kluge subsequently testified  
12 that he omitted the loans that Affirm Direct allegedly owed him  
13 on his Schedule B, because he "didn't think about it as a loan."  
14 Trial Tr. (May 23, 2012) at 87:16.

15 At the close of argument, the bankruptcy court announced an  
16 oral ruling on the record. It discussed three potential false  
17 oaths that possibly gave rise to denial of discharge, but  
18 concluded that RHI had not met its burden on two of the three  
19 potential misstatements. The bankruptcy court then focused on  
20 the issue of the omitted monthly distributions from Affirm Direct  
21 and found that Kluge's testimony attempting to excuse his failure  
22 to disclose these payments was not credible. The bankruptcy  
23 court based this conclusion on its determination that there were  
24 numerous inconsistencies in Kluge's testimony at his Rule 2004  
25 Examination<sup>7</sup> and in his testimony at trial and on its observation

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26  
27 <sup>7</sup> At trial, the bankruptcy court read a portion of Kluge's  
28 testimony into the record that it identified as testimony from  
(continued...)

1 of Kluge's demeanor during his testimony.

2 The bankruptcy court noted that at his Rule 2004  
3 Examination, Kluge acknowledged that the omitted income was  
4 income to his wife, but not income to him. In contrast, the  
5 bankruptcy court found that Kluge's testimony at trial was vague  
6 and inconsistent. The bankruptcy court, therefore, determined  
7 that the omitted monthly transfers were income, that Kluge should  
8 have disclosed this income on his Schedule I and SOFA, and that  
9 his failure to disclose this income was not justified. The  
10 bankruptcy court, thus, concluded that Kluge knowingly and  
11 fraudulently made a false oath in his case and that this  
12 warranted denial of discharge.

13 On June 19, 2012, the bankruptcy court entered a judgment  
14 denying Kluge's discharge under § 727(a)(4)(A). Kluge timely  
15 appealed.

#### 16 JURISDICTION

17 The bankruptcy court had jurisdiction pursuant to 28 U.S.C.  
18 §§ 1334 and 157(b)(2)(J). We have jurisdiction under 28 U.S.C.  
19 § 158.

#### 20 ISSUE

21 Did the bankruptcy court err when it denied Kluge a  
22 discharge under § 727(a)(4)(A)?

#### 23 STANDARD OF REVIEW

24 In an action for denial of discharge, we review: (1) the

25 \_\_\_\_\_  
26 <sup>7</sup>(...continued)  
27 his § 341(a) meeting. It is likely, however, that the bankruptcy  
28 court meant Kluge's Rule 2004 Examination; the parties referred  
to the Rule 2004 Examination during the trial and parts of  
Kluge's Rule 2004 Examination were admitted into evidence.

1 bankruptcy court's determinations of the historical facts for  
2 clear error; (2) its selection of the applicable legal rules  
3 under § 727 de novo; and (3) its application of the facts to  
4 those rules requiring the exercise of judgments about values  
5 animating the rules de novo. Searles v. Riley (In re Searles),  
6 317 B.R. 368, 373 (9th Cir. BAP 2004) (citation omitted), aff'd,  
7 212 Fed.Appx. 589 (9th Cir. 2006).

8 Factual findings are clearly erroneous if illogical,  
9 implausible, or without support in the record. Retz v. Samson  
10 (In re Retz), 606 F.3d 1189, 1196 (9th Cir. 2010) (citation  
11 omitted). We give great deference to the bankruptcy court's  
12 findings when they are based on its determinations as to the  
13 credibility of witnesses. Id. (noting that as the trier of fact,  
14 the bankruptcy court has "the opportunity to note variations in  
15 demeanor and tone of voice that bear so heavily on the listener's  
16 understanding of and belief in what is said.") (citation and  
17 quotation marks omitted).

#### 18 **DISCUSSION**

19 Section 727 provides that a court must grant the debtor a  
20 discharge unless, among other things, the debtor knowingly and  
21 fraudulently makes a false oath or account in the bankruptcy case  
22 or in connection with the case. 11 U.S.C. § 727(a)(4)(A). It is  
23 well established that a fundamental purpose of § 727(a)(4)(A) is  
24 to incentivize a debtor to provide the trustee and creditors with  
25 accurate information so that they do not need to conduct costly  
26 investigations. Fogal Legware of Switz., Inc. v. Wills  
27 (In re Wills), 243 B.R. 58, 62 (9th Cir. BAP 1999) (citation  
28 omitted). A claim for denial of discharge under § 727(a)(4)(A),

1 however, is liberally construed in favor of the debtor and  
2 against the objector to discharge. Roberts v. Erhard (In re  
3 Roberts), 331 B.R. 876, 882 (9th Cir. BAP 2005) (citation  
4 omitted). The objector bears the burden to prove by a  
5 preponderance of the evidence that the debtor's discharge should  
6 be denied under § 727(a)(4)(A). Khalil v. Developers Sur. and  
7 Indem. Co. (In re Khalil), 379 B.R. 163, 172 (9th Cir. BAP 2007),  
8 aff'd, 578 F.3d 1167 (9th Cir. 2009) (citation omitted).

9 **A. The Bankruptcy Court Did Not Err When It Denied Kluge's**  
10 **Discharge Pursuant to § 727(a)(4)(A).**

11 To obtain a denial of discharge under § 727(a)(4)(A), the  
12 objector must show that: (1) the debtor made a false oath in  
13 connection with the case; (2) the oath related to a material  
14 fact; (3) the oath was made knowingly; and (4) the oath was made  
15 fraudulently. In re Retz, 606 F.3d at 1197 (citation omitted).

16 **1. False Oath**

17 A false statement or omission in the debtor's schedules or  
18 statement of financial affairs may constitute a false oath for  
19 the purposes of § 727(a)(4)(A). In re Khalil, 379 B.R. at 172;  
20 In re Wills, 243 B.R. at 62. Here, the bankruptcy court found  
21 that Kluge omitted the monthly Affirm Direct distributions to his  
22 wife from his Schedule I and SOFA. Kluge does not dispute that  
23 he omitted this information. This is sufficient to establish a  
24 false oath. See In re Searles, 317 B.R. at 377 ("A false oath is  
25 complete when made."). Thus, the bankruptcy court did not err in  
26 finding that Kluge made a false oath when he executed and filed  
27 his Schedule I and SOFA.



1                   **2.   Materiality**

2           Kluge focuses the majority of his argument on appeal on the  
3 alleged immateriality of his omission of the Affirm Direct  
4 income. He argues that the bankruptcy court erred when it  
5 determined that the income was material without first making  
6 other findings. Kluge contends that, pursuant to In re Wills,  
7 the bankruptcy court was required first to determine whether the  
8 income was property of the estate or whether his omission of the  
9 income detrimentally affected the administration of the estate.

10          At oral argument, Kluge asserted that the record was unclear  
11 on what standard the bankruptcy court applied in determining  
12 materiality. To the extent the bankruptcy court applied the  
13 materiality test set forth in In re Khalil, Kluge argued that it  
14 was erroneous to do so because In re Khalil involved assets of  
15 the estate and, thus, did not apply because the omitted income  
16 was not an asset of the estate.

17          In response, RHI argues that Kluge's failure to disclose the  
18 income affected administration of the estate, and counters that  
19 the bankruptcy court was not required to first determine whether  
20 it was property of the estate. It maintains that income is never  
21 property of the estate, and, thus, that Kluge's reliance on  
22 In re Wills, which involved assets of the estate rather than  
23 income, is misplaced.

24          Kluge, and to some extent RHI, misinterpret the standard for  
25 materiality. Whether a fact is material is broadly defined:  
26 "[a] fact is material if it bears a relationship to the debtor's  
27 business transactions or estate, or concerns the discovery of  
28 assets, business dealings, or the existence and disposition of

1 the debtor's property." In re Khalil, 379 B.R. at 173 (citation  
2 omitted). While the standard for materiality does not expressly  
3 refer to "income," it is sufficiently broad such that it may  
4 encompass income based on the particular circumstances in a case.  
5 See id. at 177 (observing that non-disclosure of information such  
6 as creditors and debts is also important because "[i]nformation  
7 regarding business and personal dealings can lead to discovery of  
8 assets, potentially avoidable transfers, or other relevant  
9 information such as grounds to deny a debtor's discharge.").

10 Here, although the bankruptcy court did not explicitly state  
11 the standard for materiality, the record supports the bankruptcy  
12 court's determination that Kluge's omission was material. First,  
13 the record shows that the monthly transfers constituted income  
14 from Kluge's corporation and that Kluge previously acknowledged  
15 that it was income. Second, the income clearly bore a connection  
16 to Kluge's business dealings and the existence of property,  
17 including the alleged loans and investments made to Affirm  
18 Direct. Had Kluge properly disclosed the alleged loans or  
19 income, it would have allowed for a prompt investigation as to  
20 potential assets. The fact that Affirm Direct may have owed  
21 Kluge thousands of dollars or had the ability to transfer  
22 thousands of dollars is significant. And the monthly payments to  
23 his wife were significant in amount. Kluge, in fact,  
24 acknowledged at oral argument that the amount of the monthly  
25 transfers were not a de minimis amount in proportion to his  
26 wife's monthly income from her employment.

27 Moreover, the bankruptcy court's determination of  
28 materiality was linked to its conclusion that Kluge was not

1 candid about the nature of the monthly transfers. It considered  
2 the evidence presented and found that Kluge's testimony was not  
3 credible, based on his demeanor at trial and several  
4 inconsistencies in his testimony within the trial itself and at  
5 his Rule 2004 Examination. The bankruptcy court determined that  
6 Kluge knew that the transfers were income from his corporation,  
7 which he should have scheduled but instead omitted. The  
8 bankruptcy court's determinations are supported by the record,  
9 and we emphasize that we give great deference to the bankruptcy  
10 court's determination as to Kluge's credibility as a witness.  
11 See In re Retz, 606 F.3d at 1203.

12 In doing so, we reject Kluge's assertion that the bankruptcy  
13 court was required to explicitly make certain findings in its  
14 path to decision. In In re Wills, we held that a misstatement or  
15 omission as to an asset with little value or that was not  
16 property of the estate could be material if it detrimentally  
17 affected the administration of the estate. See 243 B.R. at 64.  
18 This language, however, does not create a bright line standard  
19 for determining materiality in a § 727(a)(4)(A) context. Nor is  
20 there other case law establishing that a bankruptcy court must  
21 always consider and make these particular findings in a  
22 § 727(a)(4)(A) context.

23 In re Wills also provides that: "[a] false statement or  
24 omission that has no impact on a bankruptcy case is not grounds  
25 for denial of a discharge under § 727(a)(4)(A)." 243 B.R. at 63.  
26 But, this statement stands only for the general proposition that  
27 any material misstatement or omission will necessarily impact the  
28 estate. This truism does not establish some kind of sub-element

1 that the bankruptcy court must expressly find in rendering a  
2 determination of materiality in a § 727(a)(4) context. This is  
3 particularly evident in the face of subsequent case law, which  
4 does not discuss "impact" as a standalone sub-element. See  
5 In re Retz, 606 F.3d 1189 (no express discussion as to "impact"  
6 on the estate); In re Khalil, 379 B.R. at 172 (states general  
7 proposition, but no express discussion as to "impact" on the  
8 estate.) Thus, the bankruptcy court was not required to  
9 expressly make the findings that Kluge emphatically argues should  
10 have been made.

11 On this record, and based on the broad definition of  
12 materiality, the bankruptcy court correctly concluded that  
13 Kluge's omission of the income related to a material fact.

### 14 **3. *Knowingly Made***

15 A debtor "acts knowingly if he or she acts deliberately and  
16 consciously." In re Retz, 606 F.3d at 1198 (citation and  
17 quotation marks omitted).

18 Here, the bankruptcy court found that Kluge knowingly  
19 omitted the income. It found that Kluge's testimony at trial was  
20 inconsistent with his testimony at the Rule 2004 Examination with  
21 respect to whether Kluge knew that the monthly transfers were  
22 income. Based on its assessment of Kluge's credibility during  
23 his testimony at trial, the bankruptcy court stated that it did  
24 not believe Kluge's protestations of innocence or mistaken  
25 belief. It determined that Kluge was aware that the transfers  
26 were income and, consequently, that he consciously omitted the  
27 income from his Schedule I and SOFA. On this record, the  
28 bankruptcy court did not err in finding that Kluge knowingly made

1 a false oath in his case.

2 **4. Fraudulent Intent**

3 A debtor acts with fraudulent intent when: (1) the debtor  
4 makes a misrepresentation; (2) that at the time he or she knew  
5 was false; and (3) with the intention and purpose of deceiving  
6 creditors. In re Retz, 606 F.3d at 1198-99 (citation omitted).  
7 Fraudulent intent is typically proven by circumstantial evidence  
8 or by inferences drawn from the debtor's conduct. Id. at 1199  
9 (citation omitted). Circumstantial evidence may include showing  
10 a reckless indifference or disregard for the truth. Id.  
11 (citation omitted); In re Wills, 243 B.R. at 64 (intent may be  
12 established by a pattern of falsity, debtor's reckless  
13 indifference, or disregard of the truth).

14 Here, the bankruptcy court found that Kluge acted with  
15 fraudulent intent when he omitted the income on his Schedule I  
16 and SOFA. Citing to In re Khalil, the bankruptcy court stated  
17 that circumstantial evidence of fraudulent intent existed. As  
18 previously discussed, it observed a number of inconsistencies in  
19 Kluge's testimony and found that his testimony at trial lacked  
20 credibility.

21 To the extent Kluge contends that he followed the advice of  
22 his bankruptcy counsel when he initially filed his schedules, he  
23 presented no credible evidence that his reliance was reasonable  
24 or that he relied in good faith. Lack of intent may be proven by  
25 a debtor's reliance on his attorney's advice. In re Retz,  
26 606 F.3d at 1199 (citation omitted). The debtor's reliance,  
27 however, must be made in good faith, and such reliance is not a  
28 defense when the error should have been obvious to the debtor.

1 Id. (citation omitted).

2 At the trial, Kluge testified that he discussed the alleged  
3 loans and money transfers with his bankruptcy counsel at the time  
4 of filing. He testified that he discussed with counsel the type  
5 of investment loans he had made to Affirm Direct and that counsel  
6 expressly acknowledged a "loan to officer" type of loan. Kluge  
7 also testified that he disclosed the income to counsel. Yet, he  
8 subsequently testified that while he explained to counsel that  
9 the money transfers were repayments on his investments, he did  
10 not use accounting loan terms or disclose that it would go to  
11 household expenses.

12 The record is devoid of any testimony from Kluge's  
13 bankruptcy counsel. Moreover, Kluge's testimony as to what he  
14 disclosed to his bankruptcy counsel is inconsistent, even within  
15 the trial itself. Kluge has not shown either that he relied on  
16 his counsel's advice when he failed to disclose the income or  
17 that his reliance on counsel's advice, if any, was reasonable or  
18 made in good faith. See In re Retz, 606 F.3d at 1199 ("[A]  
19 debtor cannot, merely by playing ostrich and burying his head  
20 deeply enough in the sand, disclaim all responsibility for  
21 statements which he has made under oath.").

22 On this record, there are sufficient patterns of falsities  
23 or reckless indifference on Kluge's part to support the  
24 bankruptcy court's determination that advice of counsel was not a  
25 defense. And, again, we give abundant deference to the  
26 bankruptcy court's findings based on its assessment of Kluge's  
27 credibility at trial. Id. at 1196. Thus, the bankruptcy court  
28 did not err in finding that Kluge fraudulently made a false oath

1 in his case.

2 In sum, the bankruptcy court did not err in finding that  
3 Kluge made a false omission on his Schedule I and SOFA, that his  
4 false omission related to material facts, and that he omitted the  
5 information knowingly and fraudulently. Therefore, the  
6 bankruptcy court did not err in denying Kluge's discharge under  
7 § 727(a)(4)(A).

8 **CONCLUSION**

9 Based on the foregoing, we AFFIRM.

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