NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re:	BAP No. WW-10-1314-JuMkH BAP No. WW-10-1315-JuMkH*
MARK NICHOLAS DAQUILA and LATIA BETH DAQUILA,	Bk. No. 09-15514 Bk. No. 09-13710
Debtors.	Adv. No. 09-01397 Adv. No. 09-01305
In re:	
ANTHONY RICHARD BRISTOL and KRISTEN SUZANNE BRISTOL,	
Debtors.	
CARL HAGLUND,	
Appellant,	
v.	M E M O R A N D U M**
MARK NICHOLAS DAQUILA; ANTHONY RICHARD BRISTOL,	
Appellees.	

Argued and Submitted on January 21, 2011
at Seattle, Washington

Filed - February 28, 2011

Appeal from the United States Bankruptcy Court
for the Western District of Washington

Honorable Samuel J. Steiner, Bankruptcy Judge, Presiding

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* The Panel denied the parties' request for consolidation of the appeals, but authorized them to file a single brief for both appeals.

** 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.

Appearances: John Flowers, Esq. argued for Appellant Carl Haglund
Martin E. Snodgrass, Esq., Snodgrass & Warren, Inc. PS argued for Appellees Mark L. Daquila and Anthony R. Bristol

Before: JURY, MARKELL, and HOLLOWELL, Bankruptcy Judges.

Appellant Carl Haglund ("Haglund") filed an identical complaint against chapter 7 debtors, Mark N. Daquila and Anthony R. Bristol (collectively, "Debtors"), alleging that debt arising from Haglund's business investment was nondischargeable under § 523(a)(2)(A).[1] After a trial, the bankruptcy court entered judgment for Debtors, concluding that the debt, if there was one, was dischargeable. Haglund timely appealed.

We AFFIRM.

I. FACTS

Haglund's fraud claims against Debtors arose out of a speculative investment that went bad. Haglund purchased the assets of an insolvent company named Optidisc Solutions, Inc. ("Optidisc") in December 2004, and invested funds in the company. The company failed in December 2006, and Haglund essentially lost his entire investment.

More than three years later, Bristol and Daquila filed their chapter 7 petitions on April 17 and June 5, 2009, respectively. Haglund filed identical complaints against

[1] 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.

Debtors, alleging that the funds he invested in Optidisc were nondischargeable based on Debtors' fraud. His theories of fraud evolved over time, but eventually were based on fraudulent concealment and affirmative misrepresentations.

In February 2010, the bankruptcy court held a three-day trial and took the matter under advisement. On March 11, 2010, the bankruptcy court orally made findings of fact and conclusions of law, ruling that the debt, if there was one, was dischargeable. On August 10, 2010, a single judgment was entered in favor of Debtors.

On appeal, Haglund assigns multiple errors to the bankruptcy court's factual findings. Before reaching the merits, we briefly summarize the pertinent facts and testimony believed necessary to an understanding of our rulings on this appeal.

Haglund learned about Optidisc through Patrick Mazzuca ("Mazzuca") who was Debtors' partner in 3 Dagos, LLC ("3 Dagos"), a limited liability company formed for the purpose of providing investment opportunities for its members. 3 Dagos was interested in acquiring the assets of Optidisc because it was in the CD/DVD duplication business, the same business as Marcan, a company which 3 Dagos had purchased in August 2004.

Optidisc was going out of business and 3 Dagos did not have the money to purchase its assets. Mazzuca approached Haglund, who was a seasoned real estate professional and turnaround expert with distressed properties, about the investment in

November 2004.[2] Haglund testified that Mazzuca called him with an investment opportunity in a failing company. Mazzuca stated that Optidisc had two plants, one in Kent, Washington and another in Salt Lake City, Utah. Mazzuca further stated that Optidisc failed because it built a new plant in Salt Lake City.

When Haglund became interested, the parties orally agreed to a 50/50 ownership in Optidisc, with Debtors and Mazzuca contributing their knowledge of the CD/DVD industry and business expertise for their share and Haglund contributing the capital necessary to purchase the assets and continue operations for his share. The agreement did not cover any further details and was never reduced to writing. Debtors characterized it as a "handshake deal" in their brief. Haglund further testified that "there was no going over roles."[3]

The record shows that the group had to act quickly and make a decision about purchasing the assets because Optidisc's secured lender, BFI Business Financial ("BFI"), was in possession or control of Optidisc's equipment and receivables and was in the process of shutting down the company's operations. Therefore, Haglund and Mazzuca went to visit Optidisc's plant in Kent, Washington and met with management and other key employees. Haglund testified that the management or

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[2] Haglund testified that he had structured a lot of workouts in the real estate business and, as a result, was familiar with how the banks worked when they took back assets.

[3] Later Haglund testified that the role delegated to Bristol was to look over the books, including the accounts receivable, and that Daquila was supposed to go over the financial projections.

employees of Optidisc communicated the “same scenario” that Mazzuca had communicated to him; i.e., that “Kent was a great plant” and that the company had lost their working capital by purchasing another plant in Salt Lake City. Haglund also testified that Optidisc’s management provided him with the historical financial data for the company prior to his purchase. Finally, Haglund testified that he looked at the financial records before he made his investment.

On November 19, 2004, Haglund prepared a letter of intent to purchase the assets and receivables of Optidisc. On November 24, 2004, Haglund formed a new limited liability company, Optical Disc Technology, LLC, (“ODT”) with himself as the only member. He also applied for an Employer Identification Number for ODT on the same day.

In the same time frame, Haglund requested his real estate attorney to form a new LLC, with Haglund owning 50% and 3 Dagos the other 50%. The new LLC would purchase the assets and receivables of Optidisc. Haglund later wrote another note to his attorney on the same day stating that he wanted an additional clause in the LLC agreement that would allow for the three members of 3 Dagos to each have an equal vote in matters regarding the new company. That agreement was later prepared, along with a buy/sell agreement governing the disposition of the members’ ownership rights. It is undisputed that none of the agreements were ever signed.

On December 1, 2004, Haglund purchased the assets of Optidisc through a liquidation sale conducted by BFI. As a separate transaction, Haglund purchased the account receivables,

the major advantage being that BFI would lend up to 80% of the value of the receivables.

In mid-December, Haglund changed the name of ODT to Arrow Disc, LLC ("Arrow Disc").

After the purchase, Haglund and Mazzuca prepared an "Executive Summary" for Arrow Disc. The undated document states that Haglund was 100% owner of Arrow Disc but within 60 days he would sell a portion of the company to three other partners. The summary went on to provide a "general strategy" for controlling costs and increasing immediate profitability. The purpose of the summary was to persuade a company that had repossessed one of Optidisc's machines to bring it back to the Kent plant and make it possible for Arrow Disc to repurchase it.

Haglund also worked on shutting down the plant in Salt Lake City and making Arrow Disc operational. Mazzuca worked part time at the Kent plant for a salary. By January 2005, the purchase of the receivables turned out to be a bad deal, as over a half-million was written off as bad debt.

In mid-January 2005, approximately forty-five days after the purchase, Haglund entered into a forty-one month lease with Ranch Associates who owned both the land and building used by Optidisc in Kent, Washington. Haglund signed a personal guaranty on the lease, as did Debtors and Mazzuca, even though no formal agreement regarding their ownership interests was in place.

By mid-February 2005, there still was no definite agreement between the parties. Haglund called a meeting to finalize the partnership and discuss future plans given that the company had

taken huge write offs on the receivables. It was during that meeting that Haglund proposed that Marcan combine with Arrow Disc and that he would own 84% and Debtors and Mazzuca would hold 16%. Debtors and Mazzuca communicated to Haglund that they did not wish to negotiate any further about their ownership interests and left the meeting.

Arrow Disc continued operating with heavy losses. The company eventually defaulted on payments to BFI to which it owed over $2.3 million. BFI held a private sale in December 2006, of all equipment, inventory and general intangibles of Arrow Disc. After Arrow Disc's operations ceased, Haglund continued with payments to the landlord who had sued him for rent due in November 2008, in the Superior Court of Washington for King County.

In early 2009, Marcan's business failed. A few months later, Debtors filed their chapter 7 petitions which included debts associated with Marcan.

A. Haglund's Fraudulent Concealment Claim

In support of his fraudulent concealment claim, Haglund devoted a significant portion of the trial to exploring Marcan's business and its eventual downfall. Haglund's theory was that Debtors knew the CD/DVD industry was "imploding" because shortly after they purchased Marcan, it lost one of its largest customers, Boeing, which decided to purchase its own CD/DVD duplication machine. As a result of the lost revenue which Haglund maintains was significant, Marcan started selling and servicing the duplication machines and also expanded their business to include digital printing. In other words, Marcan

knew the landscape for CD/DVD duplication services was changing and, therefore, Debtors and Mazzuca took steps to move away from that business — the very business Optidisc was in.

The bankruptcy judge questioned the witnesses from time to time to bring out the facts of the case. The bankruptcy judge asked Daquila why Marcan went out of business in 2009. Daquila testified that it was because of the economy and the market. Daquila also testified that Marcan's downfall did not have anything to do with their largest customer, Boeing, producing its own CDs because Marcan pursued a different business model by selling duplication machines and servicing them. Finally, Daquila testified that the CD/DVD duplication business was always profitable when 3 Dagos owned Marcan.

Bristol's testimony was in accord. He too blamed the economy and tightening of credit for Marcan's downfall.

B. Haglund's Affirmative Misrepresentation Claims

The record shows that Haglund's alleged misrepresentation claims were also difficult to pin down. When questioned by the bankruptcy judge, Haglund articulated two misrepresentations: Debtors' promise to contribute their "sweat equity" in exchange for 50% equity ownership in Optidisc and Debtors' promise or obligation to perform the necessary due diligence of the Optidisc assets, customer base, receivables, and equipment. According to Haglund, Debtors contributed nothing and failed to perform the necessary due diligence.

Besides Haglund, Debtors testified about the roles of the parties before and after the acquisition. Daquila testified that he had no "formal agreement or arrangement" with Haglund.

He further testified that Haglund "never asked me to do any due diligence through email or phone or any other face to face. I was never asked to do any kind of due diligence." Bristol testified that he was not assigned particular tasks with the acquisition of Optidisc. Bristol further testified that he reviewed the financials and learned what they all knew; i.e., that Optidisc had a failing business and was not profitable.

C. The Bankruptcy Court's Ruling

Based on the documentary evidence and testimony, the bankruptcy court found that Haglund failed to prove fraud by way of affirmative misrepresentation or by omission. The court concluded there was no evidence that showed either debtor had any intention of deceiving Haglund nor did they receive anything directly or indirectly from Haglund as a result of what happened. Finally, the bankruptcy court rejected outright the notion that Debtors had talked Haglund into the investment at a time when they knew the industry was failing. "It would seem obvious that . . . had they had such knowledge, they never would have guaranteed the lease on the Kent plant."

With this background, we discuss Haglund's fraud claims and factual assignments of error below.

II. JURISDICTION

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

III. ISSUE

Whether the bankruptcy court erred in finding that the debt, if there was one, was dischargeable because Haglund failed

to prove the elements for fraud by a preponderance of the evidence under § 523(a)(2)(A).

IV. STANDARDS OF REVIEW

Whether a claim is dischargeable presents mixed issues of law and fact, which we review de novo. Peklar v. Ikerd (In re Peklar), 260 F.3d 1035, 1037 (9th Cir. 2001). The bankruptcy court's findings made in the context of the dischargeability analysis, including the court's finding with respect to intent to defraud, are factual findings reviewed under the clearly erroneous standard. Candland v. Ins. Co. of N. Am. (In re Candland), 90 F.3d 1466, 1469 (9th Cir. 1996); Advanta Nat'l Bank v. Kong (In re Kong), 239 B.R. 815 (9th Cir. BAP 1999).

"A court's factual determination is clearly erroneous if it is illogical, implausible, or without support in the record." Retz v. Samson (In re Retz), 606 F.3d 1189, 1196 (9th Cir. 2010) (citing United States v. Hinkson, 585 F.3d 1247, 1261-62 & n.21 (9th Cir. 2009) (en banc).

The clearly erroneous standard does not "entitle a reviewing court to reverse the finding of the trier of fact simply because it is convinced that it would have decided the case differently." Anderson v. City of Bessemer City, N.C., 470 U.S. 564, 573 (1985). Moreover, when factual findings are based on determinations regarding the credibility of witnesses, we give great deference to the bankruptcy court's findings, because the bankruptcy court, as the trier of fact, had the opportunity to note "variations in demeanor and tone of voice that bear so heavily on the listener's understanding of and belief in what is said." Id. at 575.

V. DISCUSSION

Section 523(a)(2)(A) excepts from discharge debts incurred through "false pretenses, a false representation, or actual fraud." To establish that a debt is nondischargeable under § 523(a)(2)(A), a creditor must establish by the preponderance of the evidence the following: (1) a misrepresentation, fraudulent omission or deceptive conduct by the debtor; (2) knowledge of the falsity or deceptiveness of his statement or conduct; (3) an intent to deceive; (4) justifiable reliance by the creditor on the debtor's statement or conduct; and (5) damage to the creditor proximately cased by its reliance on the debtor's statement or conduct. Turtle Rock Meadows Homeowners Ass'n v. Slyman (In re Slyman), 234 F.3d 1081, 1085 (9th Cir. 2000).

We construe the Code's limited exceptions to the general policy of discharge narrowly. Snoke v. Riso (In re Riso), 978 F.2d 1151, 1154 (9th Cir. 1992). On the other hand, the very purposes of § 523(a)(2)(A) "'are to prevent a debtor from retaining the benefits of property obtained by fraudulent means and to ensure that the relief intended for honest debtors does not go to dishonest debtors.'" Slyman, 234 F.3d at 1085.

A. The Bankruptcy Court Did Not Err In Concluding That Haglund Failed To Prove His Fraudulent Concealment Claim

A debtor's failure to disclose material facts constitutes a fraudulent omission under § 523(a)(2)(A) if the debtor was under a duty to disclose and possessed an intent to deceive. Apte v. Japra (In re Apte), 96 F.3d 1319, 1322 (9th Cir. 1996). To determine whether there was a duty to disclose, we look to the

traditional common law rule stated in the Restatement (Second) of Torts § 551 (1976) which provides in relevant part:

> (1) One who fails to disclose to another a fact that he knows may justifiably induce the other to act or refrain from acting in a business transaction is subject to the same liability to the other as though he had represented the nonexistence of the matter that he has failed to disclose, if, but only if, he is under a duty to the other to exercise reasonable care to disclose the matter in question.
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> (2) One party to a business transaction is under a duty to exercise reasonable care to disclose to the other before the transaction is consummated,
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> . . . .
>
> (e) facts basic to the transaction, if he knows that the other is about to enter into it under a mistake as to them, and that the other, because of the relationship between them, the customs of the trade or other objective circumstances, would reasonably expect a disclosure of those facts.

Apte, 96 F.3d at 1324.

Haglund argues in conclusory fashion that Debtors had a duty to disclose, presumably because the parties were involved in a "business transaction." Haglund contends that the bankruptcy court erred by not discussing this issue in its oral ruling – an error subject to our de novo review. We need not address this issue, however, because the record shows that even if there was a duty, Haglund failed to carry his burden with respect to other essential elements of his fraudulent concealment claim. Namely, that Debtors had knowledge of the omitted fact he complains of (the "imploding" of the CD/DVD industry)[4] and that they had the required intent to deceive.

[4] Haglund often refers to the "fact" that the industry was "imploding." This concept is hardly a fact. It is an opinion, conclusion, or speculation, none of which are a "fact" to be concealed or misrepresented.

Both elements involve factual determinations subject to the clearly erroneous standard of review.

Our review of the entire record convinces us that the bankruptcy court's account of the evidence was plausible and supported by inferences that may be drawn from the facts in the record. For example, Debtors' personal guaranty of a forty-one month lease signed in mid-January 2005 after Haglund's asset purchase was objective evidence from which the bankruptcy court could reasonably infer that Debtors had no knowledge that the CD/DVD duplication industry was "imploding." Moreover, the bankruptcy court heard exhaustive testimony regarding Marcan's business. Debtors testified that the CD/DVD duplication business was profitable for Marcan, they explained their decision to pursue a different business model, and further testified as to their belief that Marcan failed due to the economy. From this testimony, the bankruptcy court could also reasonably infer that Debtors had no knowledge that the CD/DVD industry was "imploding."

Haglund, who has the burden of proof, does not point to any inconsistencies or contradictions in Debtors' testimony that would support his concealment claim. Instead, Haglund points to the Executive Summary as persuasive evidence that Debtors portrayed Optidisc as a "very positive investment opportunity indeed." However, the record shows that Mazzuca and Haglund — not Debtors — prepared the summary and that its purpose was to convince a secured lender to return a repossessed machine to the company. Thus, this evidence does not support the inference that Haglund suggests.

Further, Haglund's recitation of the evidence as it relates to Marcan and Marcan's alleged troubles is nothing more than an invitation for us to reweigh the evidence — something we do not do on appeal. Anderson, 470 U.S. at 573-74 ("If the [trial] court's account of the evidence is plausible in light of the record viewed in its entirety, [we] may not reverse it even though convinced that had [we] been sitting as the trier of fact, we would have weighed the evidence differently.").

In sum, the inference that Debtors had no knowledge that the CD/DVD industry was imploding is supported by facts in the record. It follows that if Debtors had no knowledge of the "fact" Haglund complains of, they could not have possessed the required intent to deceive him. Accordingly, we conclude the bankruptcy court's legal conclusion that Haglund failed to prove his fraudulent concealment claim is manifestly correct.

B. The Bankruptcy Court Did Not Err In Concluding That Haglund Failed To Prove His Affirmative Misrepresentation Claims

Haglund relies solely on the initial oral agreement between the parties for his affirmative misrepresentation claims. He argues that, prior to his purchase, Debtors promised to contribute their "sweat equity" in exchange for 50% equity ownership in what later became Arrow Disc and to perform the necessary due diligence of the Optidisc assets, customer base, receivables, and equipment prior to the purchase.

A promise of future performance or intention is generally not actionable as fraud at common law unless at the time the promise was made debtor had no intention of carrying through. Restatement (Second) of Torts § 530 (1976) ("A representation of

the maker's own intention to do or not to do a particular thing is fraudulent if he does not have that intention."); see also Stiley v. Block, 925 P.2d 194, 204 (Wash. 1996) (same).

On appeal, Haglund "disagrees" with the bankruptcy court's factual finding that neither debtor made misrepresentations with an intent to deceive Haglund. Haglund rehashes many of his arguments with conclusory statements, such as that Debtors never intended to make the efforts necessary to cause Arrow Disc to reverse its adverse, and serious problems and that they intentionally covered up the difficulties they had with their own company, Marcan. Haglund relies on his own testimony to refute the bankruptcy court's findings of fact regarding Debtors' alleged intent to deceive. However, while Haglund's testimony may have been consistent with his theories behind Debtors alleged fraud, it was not necessarily probative, and certainly not dispositive, on the issue of Debtors' alleged intent.

The "intent to deceive under § 523(a)(2)(A), can be inferred and established from the surrounding circumstances." Alexander & Alexander of Wash., Inc. v. Hultquist (In re Hultquist), 101 B.R. 180, 183 (9th Cir. BAP 1989). We do not find any evidence in the record that shows Debtors made promises to Haglund or, if there were, that those promises were made without an intention to perform. Rather, the factual circumstances revealed in the record, coupled with the testimony of the parties, at most supports an inference that if Debtors made any promises to Haglund at all, it was to do something in the future, i.e., contribute their skill and knowledge in

exchange for 50% ownership in the new company, Arrow Disc.

However, the undisputed trial testimony was that the initial "agreement" between the parties was never formalized or reduced to writing before or after the asset purchase. Moreover, the record shows that the parties' alleged "agreement" regarding ownership kept changing. Bristol testified that after the asset purchase, Haglund wanted to change the deal to a two-thirds, one-third split, with Haglund getting two-thirds because he put more capital into Optidisc than he originally planned. At another point, Bristol testified about the February 2005 meeting where Haglund proposed Debtors take less and throw Marcan into the deal. Haglund does not dispute these facts.

Moreover, the parties' testimony regarding their roles was not drastically different. Daquila testified that he had no formal agreement or arrangement with Haglund and that he was never asked to do any due diligence. Likewise, Bristol testified that he was not assigned particular tasks with the acquisition of Optidisc. Bristol further testified that he reviewed the financials and learned what they all knew: that Optidisc was a failing business and was not profitable. Haglund also testified that there was no "going over" roles, but he later assigned roles to Debtors in his testimony.

Based on the undisputed testimony that the structure of Debtors' ownership interests kept changing, the bankruptcy court could reasonably infer that Debtors did not make any promises to Haglund with an intent to deceive. Further, although the bankruptcy court did not make any credibility determinations in its findings, it is implicit that such determinations

necessarily were made given that there is rarely direct evidence of fraudulent intent. Mindful of our deferential standard of review and the knowledge that the bankruptcy court, unlike us, had the opportunity to observe the witnesses' testimony, we cannot say the bankruptcy court clearly erred in finding that Haglund failed to prove that Debtors made the alleged promises, or, if they did, that they made the promises with the intent to deceive Haglund. Haglund's failure to establish elements essential to his misrepresentation claim makes all other elements immaterial.

C. The Bankruptcy Court's Finding That Debtors Did Not Benefit From Haglund's Investment Was Harmless Error

Haglund "strongly disagrees" with the bankruptcy court's finding that "it is very important to note that neither defendant received anything directly or indirectly from Haglund as a result of what happened." However, § 523(a)(2)(A) does not require a finding of receipt of a benefit through the fraudulent conduct. Lee v. Tcast Commc'n, Inc., 335 B.R. 130, 136 (9th Cir. BAP 2005) (citing Muegler v. Bening, 413 F.3d 980, 983-84 (9th Cir. 2005)). Although the bankruptcy court's finding regarding benefit was in error, it does not warrant reversal because it was harmless. The court's finding of no benefit was unnecessary to its primary conclusion that Haglund failed to prove fraud either by way of affirmative misrepresentation or by omission. See Litton Loan Serv'g, LP v. Garvida (In re Garvida), 347 B.R. 697, 704 (9th Cir. BAP 2006); See also Rule 9005 ("Harmless Error")(incorporating into bankruptcy rules Fed. R. Civ. P. 61, which provides: "[a]t every stage of the

proceeding, the court must disregard all errors and defects that do not affect any party's substantial rights.").

VI. CONCLUSION

For the reasons stated above, we AFFIRM.