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Bankruptcy and Gambling
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I. Dischargeability of Gambling Debt

A. Objections related to the discharge of gambling debt are ordinarily brought under two sections of the Bankruptcy Code.

1. A successful objection under 11 USC §523 results in a specific debt being determined non-dischargeable.

2. A successful objection under 11 USC §727 results in an order denying the debtor's discharge.

B. Objections to the discharge may be brought by a creditor, the trustee, or the United States Trustee.

C. The moving party has the burden of establishing non-dischargeability by a preponderance of the evidence. See Grogan v. Garner, for actions brought under §523. 498 U.S. 279, 287 (1991). The moving party has the burden of establishing the grounds for denial of discharge by a preponderance of the evidence. See In Re Scott, for actions brought under §727. 172 F.3d 959, 966 (7th Cir. 1999).

II. Determination of Non-Dischargeability under 11 U.S.C. §523(a)(2)

11 U.S.C. §523(a) provides, in part, that an individual debtor is not entitled to a discharge 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;

(B) use of a statement in writing-
(i) that is materially false;
(ii) respecting the debtor's or an insider's financial condition;
(iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and
(iv) that the debtor caused to be made or published with intent to deceive

Courts have applied various theories when dealing with the representation issue, or lack of face-to-face contact, in credit card transactions:

1. **Implied Representation:** The use of a credit card is an implied representation that the debtor has both the intent and the ability to pay. See In Re Clagg, 150 B.R. 697 (Bankr. C.D. Ill. 1993).

2. **Assumption of Risk:** Until the point of revoking the debtor's right to use the card, the credit card issuer is presumed to have voluntarily assumed the risk of nonpayment. See First National Bank of Mobile v. Roddenberry, 701 F.2d 927 (11th Cir. 1983).

3. **Totality of the Circumstances or Objective Approach:** The court is to apply a number of factors to determine if the debt should be dischargeable. See In Re Dougherty, 84 B.R. 653 (9th Cir. BAP 1988).

   * The length of time between the charges made and the filing of bankruptcy;
   * Whether or not an attorney was consulted concerning the filing of bankruptcy before the charges were made;
   * The number of charges made;
   * The amount of the charges;
   * The financial condition of the debtor at the time the charges were made;
   * Whether the charges were above the credit limit of the account;
   * Whether the debtor made multiple charges on the same day;
   * Whether or not the debtor was employed;
   * The debtor's prospects for employment;
   * The financial sophistication of the debtor;
   * Whether there was a sudden change in the debtor's buying habits;
   * Whether the purchases were made for luxuries or necessities.

4. **Common Law or Subjective Approach:** Considers the debtor's subjective intent at the time of the transaction using the debtor's

testimony and relevant circumstances. In Re Briese, 196 B.R. 440 (Bankr.W.D.Wis.1996).

**In Re Briese, 199 B.R. 440 (Bankr. W.D.Wis.1996).** Chevy Chase Bank brought an adversary proceeding to have its debt determined non-dischargeable under §11 U.S.C. 523(a)(2)(a) alleging that Mrs. Briese obtained credit through fraudulent intent. Chevy Chase Bank sent the debtors a pre-approved credit card solicitation with a credit limit of $10,000. Chevy Chase Bank acknowledged that after a credit check, it recognized that the Briese's unsecured debts exceeded ⅔ of their annual income, that they carried large balances, and that they made timely payments. Mrs. Briese obtained cash advances on her credit cards and spent them at the casino. Only after winning two jackpots totalling approximately $33,000, did Mrs. Briese calculate her debts and realize the magnitude of her credit card debt. She used some of the jackpot winnings to pay taxes, unsecured debt, and to make a few home improvements. She then took the remaining $15,000 to the casino in an unsuccessful attempt to pay off her remaining credit card debt. Mrs. Briese was current on her minimum monthly credit card payments, as of the date of the filing of her bankruptcy.

After considering other theories, Judge Utschig ultimately chose the **common law or subjective approach**, looking to Supreme Court's decision in Field v. Mans, 516 U.S. 59 (1995).

The standard for fraud in an action under 523 (a)(2)(A) is **actual fraud** under the common law the creditor must prove:

1. the debtor made false representations to the creditor;
2. the debtor knew the representation was false (or recklessly disregarded its truth);
3. the debtor intended to deceive the creditor;
4. the creditor relied on the representation; and
5. the creditor suffered a loss as a result.

Under the subjective approach adopted by Judge Utschig, the creditor failed to prove that the Mrs. Briese intended to deceive the creditor. "In this case, Mrs. Briese had an honest, if questionable and undoubtedly foolish, belief that she could win enough to pay her debts." Briese, 191 B.R. at 453.

Pursuant to Field v. Mans, the creditor must also prove **justifiable reliance** on a debtor's fraudulent representation. Judge Utschig found it doubtful that the creditor relied on the debtor's representation, noting the credit check that the creditor made prior to issuing the card:

> It is clear that the plaintiff made an examination of the debtors' finances which indicated a high debt load and an inability to make more than minimum payments. This indicates that the plaintiff knew it was unlikely the debtors could ever pay a large account balance in full. The plaintiff chose to blindly ignore

> those warning signs and proceeded to extend credit to the debtors ….
> Briese, 191 B.R. at 454.

**Citibank (S. Dakota), NA v. Michel, 220 B.R. 603 (N.D. Ill., 1998).** Citibank brought an adversary proceeding under 11 U.S.C. §523(a)(2)(A) alleging that the debtor had borrowed money by fraudulent means, where the debtor had traveled to Las Vegas and gambled at the blackjack tables. The District Court affirmed the bankruptcy court judge's determination that under the subjective standard that the debtor did not commit fraud.

Citing the bankruptcy court's decision at page 605:

> [Michel] had deluded himself into believing that there was a realistic possibility that he would win. Given his credit, employment and family history, all of which were good, there is no reason to believe that he did not intend to use his winnings to pay his debts. Indeed, I believe the reason he changed his pattern of behavior by gambling more than he ever had was that he was trying to pay the large debts he had.

**In re Murphy, 190 B.R. 327 (Bankr. N.D. Ill. 1995).** Chase Manhattan Bank and American Express Travel Related Services Co., Inc. brought adversary proceedings under 11 U.S.C. § 523(a)(2)(A) alleging fraudulent intent. The debtor used his credit cards to finance his gambling on riverboat casinos, his golf game and his investments in stock options and common stocks. The bankruptcy judge applied the subjective intent test and found that the debtor did not commit fraud.

> [T]he Court finds that at the time the Debtor incurred the debts at issue he intended to repay them and believed (however unreasonably) that he would have the means to do so from his gambling and investments. The Debtor had for years successfully relied on such "income" to pay off his credit card debt. As late as May, 1994, the Debtor was able to pay his credit card debts in full after making a profit in the stock market. The Debtor did not significantly alter his spending habits in the months preceding the filing of the bankruptcy petition; rather his betting did not come through for him as it had in the past.
> Murphy, 190 B.R. at 334.

**In Re Peterson, 444 B.R. 573 (Bankr. W.D. Wis., 2011).** Desert Palace Inc. dba Caesers Palace brought an adversary proceeding under 11 U.S.C. §523(a)(2)(A)&(B). Debtor was a frequent gambler with Caesers organizing trips for him and extending him credit in the form of markers. On the first night of a trip in 2008, the debtor won $1.5 million, but lost $3.5 million on the second night. Peterson's losses exceeded the previous credit he was extended through markers. Per the debtor, on the return trip to Wisconsin, the pilot turned the plane around and the debtor was greeted in the hangar by a Caesers employee who presented a $3.5 million marker and told him that he could not leave until he signed it. After an initial refusal to sign,

debtor signed under duress on advice of local counsel. The marker was presented to debtor's bank and returned as no account was found.
Peterson subsequently filed a lawsuit in Nevada District Court related to the hangar incident and after Peterson's attorney withdrew, Caesers filed an amended counterclaim alleging fraud related to the casino debt. A default judgment was entered against Peterson for $2.6 million.

In 2010, Peterson filed a Chapter 7. Caesers filed for summary judgment in the adversary proceeding arguing that the bankruptcy court was precluded from re-litigating the facts supporting the findings of fraud in the Nevada District Court under the doctrine of issue preclusion. Judge Martin applied the Nevada issue preclusion law and denied the motion for summary judgment finding that Nevada law requires that the the issue be actually and necessarily litigated. Judge Martin determined that the issue was not litigated as Peterson's counsel had withdrawn and Peterson was not aware of the amended counterclaim that asserted the claim of fraud.

**First National Bank of Omaha v. Sysouvanh, 11-cv-675-wmc (W.D. Wis. 2013).** FNBO filed an adversary proceeding under 11 U.S.C.§523(a)(2)(A) & (B) alleging fraud and a false written financial statement. Applying the clearly erroneous standard, the district court affirmed Judge Martin's finding that Mrs. Sysouvanh had intended to pay her credit card debt, while noting that she "veered dangerously close to fraud territory." The district court also affirmed Judge Martin's finding that the credit application in which Mrs. Sysouvanh, a full-time homemaker, indicated she was self-employed and listed her husband's salary under income was not a false written statement.

Most notably, the district court also affirmed the bankruptcy court's award of attorneys' fees and costs to the debtor under 11 U.S.C. §523(d) which states:

> If a creditor requests a determination of dischargeability of a consumer debt under subsection(a)(2) of this section, and such debt is discharged, the court shall grant judgment in favor of the debtor for the costs of, and a reasonable attorney's fee for, the proceeding if the court finds that the position of the creditor was not substantially justified, except that the court shall not award such costs and fees if special circumstances would make the award unjust.

The court found that there was no direct or circumstantial evidence of fraudulent intent offered under §523(a)(2)(B). With regard to §523(a)(2)(A), the circumstantial evidence was found to be more substantial, but not enough to justify an adversary proceeding on its own. It was noted that the creditor did not attend the §341 meeting of creditors or request a 2004(b) examination in an effort to investigate its claim.

III. Denial of Discharge under 11 U.S.C. §727

11 U.S.C. §727 provides, in part, that the court shall grant a discharge to an individual debtor unless:

(2) the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be transferred, removed, destroyed, mutilated, or concealed-

(A) property of the debtor, within one year before the date of the filing of the petition; or

(B) property of the estate, after the date of the filing of the petition;

(3) the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or preserve any recorded information, including books, documents, records, and papers, from which the debtor's financial condition or business transactions might be ascertained, unless such act or failure to act was justified under all of the circumstances of the case;

(4) the debtor knowingly and fraudulently, in or in connection with the case-

(A) made a false oath or account;

(B) presented or used a false claim;

(C) gave, offered, received, or attempted to obtain money, property, or advantage, or a promise of money, property, or advantage, for acting or forbearing to act; or

(D) withheld from an officer of the estate entitled to possession under this title, any recorded information, including books, documents, records, and papers, relating to the debtor's property or financial affairs;

(5) the debtor has failed to explain satisfactorily, before determination of denial of discharge under this paragraph, any loss of assets or deficiency of assets to meet the debtor's liabilities;

**Matter of Ramos, 8 B.R. 490, 7 B.C.D.458 (Bank.W.D.Wis. 1981).** Suppliers of the debtor's sole proprietorship fencing business brought an adversary proceeding under 11 U.S.C. §727(a)(2), (3), (4)(A), and (5). Distressed about his business, Ramos drank five nights a week and gambled regularly on cards and football games. Admittedly aware of his insolvency, he closed the business accounts and transferred the funds to his personal accounts. He applied the accounts receivable of the business to personal expenses, rather than business debts. In the last month that the business operated, $5,800 was taken in cash and checks made payable to his wife. Ramos agreed that his budgeted expenses were $1,100 monthly and that he had recreation expenses of $720 per month. No explanation was offered for funds withdrawn from

the business other than that they were used for “personal expenses”. Furthermore, Ramos did not disclose any gambling losses or the $1,000 he received for a 25% ownership interest in another business in his Statement of Financial Affairs. At trial, Ramos admitted to gambling losses in excess of $1,000 and “hopefully” less that $5,000 in the year prior to filing bankruptcy.

Judge Martin first addressed the allegation that the debtor made false oaths. Under §727(a)(4)(A), the oath must have been knowingly and fraudulently made and must have related to a material fact. Judge Martin focused on the non-disclosures on the Statement of Financial Affairs of both the gambling losses and the transfer of the business interest. Finding those omissions sufficient to deny discharge, Judge Martin went on to discuss the remaining allegations of transfers of monies Ramos made to his wife as evidence of his intent to hinder, delay or defraud his creditors.