

**UNITED STATES BANKRUPTCY COURT  
For the Southern District of Iowa**

<b>In Re</b>	:	<b>Case No. 98-00587-CH</b>
	:	
<b>ROY CLINTON FAUST JR., and</b>	:	<b>Chapter 7</b>
<b>THERESA BELLE FAUST,</b>	:	
	:	
<b>Debtors.</b>	:	
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<b>UNIVERSAL BANK, N.A.,</b>	:	<b>Adv. No. 98-98099</b>
	:	
	:	
<b>Plaintiff,</b>	:	
	:	
<b>v.</b>	:	
	:	
<b>THERESA BELLE FAUST,</b>	:	
	:	
	:	
<b>Defendant.</b>	:	

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**ORDER—COMPLAINT TO DETERMINE DISCHARGEABILITY OF DEBT**

On March 30, 1999, trial was held on the Plaintiff's Complaint to Determine Dischargeability of Debt. Plaintiff, Universal Bank, N.A (AT&T), was represented by attorney Mark D. Reed; Defendant, Theresa Belle Faust, was represented by attorney Paul D. Gandy. At the conclusion of the trial, the Court took the matter under advisement upon a briefing schedule. Plaintiff filed a post-trial brief. No brief was filed by Debtor. The Court now considers the matter fully submitted.

The Court has jurisdiction of this matter pursuant to 28 U.S.C. § 157(b)(1) and § 1334. This is a core proceeding. 28 U.S.C. § 157(b)(2)(I). The Court, upon review of the briefs, pleadings, evidence, and arguments of counsel, now enters its findings and conclusions pursuant to Fed. R. Bankr. P. 7052.

## FINDINGS OF FACT

1. The Plaintiff is a creditor of the debtor as the result of credit card account number 5396-4300-0041-6495 with AT&T Universal Card Services (AT&T account). The account was opened on August 8, 1995.

2. The Defendant is Theresa Belle Faust (the debtor), who along with her husband, Roy Clinton Faust, Jr., filed a joint chapter 7 bankruptcy petition on February 17, 1998.

3. The terms and conditions of the AT&T account are provided in a comprehensive Cardmember Agreement. The agreement provides for the reevaluation of credit. Section 26 states: "We may reinvestigate any information you provided on your credit application at any time, and in the course of doing so, we may ask you for additional information, request credit bureau reports and/or otherwise verify your current credit standing." (Exh. 13, P. 5).

4. At least back to March of 1997, the debtor was carrying an account balance averaging \$6,600.00 per month.

5. In July of 1997, the debtor acquired a Providian VISA card. A July 10, letter from the issuer welcomed her to Providian. The letter's heading stated:

Now You've Got It All !!  
0% APR For the First Three Months  
A Powerful Credit Line To Meet Your Needs!  
Guaranteed Savings on Balance Transfers!

The letter encouraged her to transfer balances to her Providian account. The initial credit limit of \$5,000.00 would be automatically raised to \$8,500.00 once the balance transfer checks had cleared. (Exh. 4a, P. 1).

6. Sometime in July, the debtor used her Providian credit card to pay down the balance on the AT&T account with a transfer of approximately \$6,500.00.

7. On or about October 20, 1997, the debtor received a letter from AT&T Universal Card with three enclosed convenience checks. The letter began with the statements: "Imagine being able to use your credit card to pay any kind of bill. That's the idea behind your AT&T Universal Card Convenience Checks." It continued by encouraging the debtor to use Convenience Checks to pay, among other things, "other credit card bills." The first check was already made out for "something everyone needs – cash." No cash advance fees were charged when the Convenience Checks were used. (Exh. 3, P. 2).

8. On or about October 22, 1997, the debtor used a convenience check to obtain \$7,000.00 cash. The convenience check was made payable to cash. She then paid \$6,390.00 to Providian, leaving her with an account credit of \$66.99. The debtor testified that she transferred the balance back to AT&T because the interest rate was lower. Providian charged 21.90% on cash advances and AT&T charged 15.5% on cash advances.

9. The debtor made the minimum required payment in November and a payment of \$150.00 in December.

10. Roy Faust Jr. worked for Southeastern Community College (SCC) in West Burlington, IA from 1987 – 1996. He taught classes in electronics technology, computer technology, robotics technology, automotive technology, and design engineering. While employed, he was covered by the Iowa Professional Public Employees' Retirement System (IPERS). In 1995 he earned \$38,375.88 at this position. In 1996 he earned \$24,869 from SCC. In August of 1996, his employment at SCC terminated. He withdrew \$12,952.00 from his IPERS account that year. His total income from 1996, including unemployment compensation, was \$36,882.00. (Exhs. 8a,11).

11. On January 27, 1997, Roy started Metal Detectors of Iowa. He would take orders for metal detectors and supply them to customers. The detectors were used for security, industrial, and professional purposes.

12. On April 4, 1997, Roy started a vending business. He purchased some vending machines and was selling Tic-Tacs through them.

13. The debtors' income for 1997 was \$4,259.61. For the time in 1998 leading up to their petition on February 17, 1998, their income was \$0.00. (Pet.).

14. On November 1, 1997, Roy was arrested for disorderly conduct, interference with official acts, and going armed with intent. (Exh. D). He was subsequently convicted of only the disorderly charge.

15. On August 27, 1998, the Fausts filed a complaint in the Iowa District Court for Des Moines County naming police officers Michael Charles Swore, John Willis, and the City of Burlington as defendants. The Fausts claimed police misconduct in relation to Roy's arrest in November. They requested compensatory and punitive damages. (Exh. F).

## **DISCUSSION**

The Bankruptcy Code provides that a debt is not dischargeable to the extent that it was obtained by "false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition." 11 U.S.C. § 523(a)(2)(A). The plaintiff has the burden of proving the debtor's deceit by a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279, 286-87 (1991). The Eighth Circuit has adopted a five-part test to determine whether a debt will be excepted from discharge under § 523(a)(2)(A). The court asks whether: (1) the debtor made false representations; (2) the debtor knew these representations

were false at the time they were made; (3) the debtor made these representations with the intention and purpose of deceiving the creditor; (4) the creditor justifiably relied on the representations; and, (5) the creditor sustained the alleged injury as a proximate result of the representations having been made. In re Van Horne, 823 F.2d 1285, 1287 (8th Cir. 1987), as modified by Field v. Mans, 516 U.S. 59, 74-75 (1995) (holding that § 523(a)(2)(A) requires "justifiable, but not reasonable, reliance").

"The first, second, and third elements can be considered together by asking whether the debtor made false representations knowingly and with the intent to deceive the creditor." AT&T Universal Card Services v. Broerman (In re Broerman), No.97-2569-CH, Adv. No. 97-97203 at 5 (Bankr. S.D. Iowa Jan. 19,1999). The use of a credit card serves as an implied representation that the cardholder has the intention and ability to repay the debt. Id., see also, In re Stewart, 91 B.R. 489, 494 (Bankr. S.D. Iowa 1989). "*However*, insolvency alone does not establish intent to deceive." Id., see also, In the Matter of Cron, 241 B.R. 1, 5 n. 7 (Bankr. S.D. Iowa 1999). In order to prevail, AT&T must prove that the debtor, Theresa Faust, had neither the intention nor the ability to pay the charges at the time that they were made.

Intent to deceive may be proven by circumstantial evidence. In re Broerman, No. 97-2569-CH, Adv. No. 97-97203 at 5. The following nonexclusive list of factors are considered by the court:

- 1) the length of time between making the charges and filing bankruptcy;
- 2) whether an attorney had been consulted concerning filing of bankruptcy before the charges were made;
- 3) the number of charges;
- 4) the amount of charges;
- 5) whether multiple charges were made on the same day;
- 6) whether the charges were above the credit limit on the account;
- 7) whether the purchases were for luxuries or necessities;
- 8) a sharp change in the buying habits of the debtor;
- 9) the debtor's financial sophistication;
- 10) the financial condition of the debtor when the charges were made;
- 11) the debtor's employment circumstances; and
- 12) the debtor's prospects for employment.

Id. at 6. In considering these and additional factors in their totality, the court finds that Theresa Faust did not intend to deceive AT&T when she made the charges on her account.

First, the court finds Theresa Faust to be a credible witness. It accepts her statement, at least subjectively, that she intended to pay the charges that she made. Second, the factors that weigh in favor of the court's findings include: an attorney had not been contacted concerning filing bankruptcy before the charges were made; the credit limit was not exceeded on this account or any of the Fausts' other accounts; the purchases were for necessities not luxuries (contrary to AT&T's claim of a sybaritic lifestyle, the Fausts apparently lived quite modestly with their four children in a \$40,000.00 home and drove a 1990 Plymouth Grand Voyager); there was no sharp change in the debtor's buying habits shortly before bankruptcy was filed; there are not a significant number of charges nor excessive charges in one day; and importantly there is no evidence that the debtor is financially sophisticated. It is true that the debtor is a housewife and not employed in the conventional sense of the word. However, that was her situation when the account was approved. AT&T has not contended that the debtor falsely represented her situation in acquiring the card. The court assumes that this is a case where the household was considered in determining credit worthiness.

The court finds the following facts persuasive. First, as far back as March 1997, the debtor had a balance of \$6,600.00 with AT&T. In July of 1997, in response to a solicitation offering 0% interest for 3 months, she transferred the balance of \$6,420.00 (which was costing around 15.30% APR. or .0419% daily) from AT&T to Providian. In late October, as the introductory rate was about to end, the debtor received a letter from AT&T with enclosed convenience checks. The letter encouraged the debtor to use the convenience checks to pay off other credit cards. The first check was made to cash. The debtor used a convenience check to acquire \$7,000.00 in cash and pay off the Providian account. In this respect the debtor was doing exactly what AT&T encouraged.

Second, the court finds that although the Fausts' financial situation has deteriorated since Roy Faust's employment at S.C.C. terminated, they have continually attempted to keep their bills paid and improve their financial situation. Roy Faust invested capital and much effort in starting two businesses. Additionally, he was continuing to work on an educational seminar which they hoped would produce added income. The debtor testified that up until January of 1998, they had not missed any payments. In fact, the Fausts used money from Roy's IPERS account, funds that would normally be exempt in bankruptcy, to pay bills including the credit card debt. The debtor also testified that she received rent and some financial assistance from an adult child and used this money to make credit card payments.

Finally, although AT&T downplays the economic impact of Roy Faust's arrest on November 1, 1997, the court finds that this incident is the proverbial back breaking straw. The debtor testified that the cost of defense and the subsequent fines drained the last of their financial resources. Their homestead was lost to the bank. While the actual impact on Roy's businesses might have been small, the impact to his reputation was greater. Burlington, Iowa is a relatively

small town, and the arrest was published in the paper. More importantly, Roy is an experienced educator. He taught electronics technology, computer technology, robotics technology, automotive technology, and design engineering, all highly desirable subjects. In the wake of the recent violence in the country's educational institutions, the charge of going armed with intent would be particularly damaging to an attempt by him to return to teaching.

AT&T has alleged that the Fausts engaged in a credit card kiting scheme. It points to the fact that the Fausts used cash advances to make payments on the credit cards. Roy Faust testified that cash advances were used to transfer balances from cards with higher interest rates to his card which had a lower rate of interest. As the court has made clear in Broerman, it will not hesitate to deny discharge where this fraudulent behavior is proven. However, in this case, on these facts, the court is not convinced that such a scheme took place.

When a cardholder uses cash advances to make minimum or slightly greater payments on other credit cards, it is not automatically fraudulent credit card kiting. Citibank v. Eashai (In re Eashai), 87 F.3d 1082, 1092 (9th Cir. 1996). As the 9th Circuit has cautioned:

It is well known that credit card issuers compete for new users and a great deal of the marketing effort encourages customers to transfer credit card balances, usually at very low interest, to a new issuer. It is not at all unlikely for a person of average means to receive new credit cards unsolicited. Even where the invitation requires an application before issuance, the inducements may be too attractive to resist by people who should. Mr. Eashai, an unemployed holder of 26 credit cards, may not fit this profile; nevertheless, it would be wrong to conclude that a person who genuinely becomes overextended, perhaps because of the availability of too much free and easy credit, risks nondischargeability. In short, the credit card issuer is not entirely blameless in this equation.

Id. at 1092, see also Anastas v. American Savings Bank (In re Anastas), 94 F.3d 1280 (9th Cir. 1996); Star Bank, N.A. v. Stearns (In re Stearns), 1999 WL 1100873 (D. Minn. 1999); AT&T Universal Card Services, Corp. v. Searle, 223 B.R. 384 (D.Mass. 1998); Hecht's, a Div. of



May Dept. Stores, Inc. v. Valdes (In re Valdes), 188 B.R. 533 (Bankr. D. MD 1995); Citibank (New York State) v. Davis (In re Davis), 176 B.R. 118 (Bankr. W.D.N.Y. 1994).

The Fausts went from having a stable, definite income to a precarious, financial situation. Two new business were started, and the debtor believed that both would succeed. Additionally, Roy Faust was continuing to work on the educational seminar, a long term project, which would provide added income. During this period of reduced income, the Fausts began to rely on the credit cards for more of their necessities. However, they continued to make timely payments. Additionally, they sacrificed a portion of the exempt IPERS fund to pay credit card debt. It is only after Roy's criminal arrest, when the debtors exhausted the last of their resources, that they realized how dire their financial situation was.

Under these facts, the court does not find that the debtor, Theresa Faust, engaged in a credit card kiting scheme. Nor does it find that she intentionally deceived AT&T. The plaintiff has not carried its burden to prove fraud, false pretenses, or misrepresentation. Therefore, the debt is not excepted from discharge.

**ORDER**

IT IS THEREFORE ORDERED, as follows:

(1) The debt of AT&T Universal Gold Mastercard Account Number 5396-4300-0041-6495 in the name of Theresa B. Faust is discharged; and

(2) The Defendant, Theresa Belle Faust, shall have judgment against the Plaintiff, Universal Bank, N.A., dismissing the complaint.

Dated this \_\_\_\_\_ day of January, 2000.

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RUSSELL J. HILL, CHIEF JUDGE  
U.S. BANKRUPTCY COURT