In the United States Bankruptcy Court

for the Northern District of Iowa

SHIRLEY SUE HINDE *Debtor(s).*	Bankruptcy No. 95-60300KW Chapter 7
AT&T UNIVERSAL CARD SERVICES *Plaintiff(s)* vs. SHIRLEY SUE HINDE *Defendant(s)*	Adversary No. 95-6088KW

ORDER

On March 28, 1996, the above-captioned matter came on for trial pursuant to assignment. Plaintiff AT&T Universal Card Services appeared by its representative Sherrill Jean Vawter and its attorney Mark D. Reed. Debtor/Defendant Shirley Sue Hinde appeared in person with her attorney Michael Dunbar. Evidence was presented after which the Court took the matter under advisement. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I). The April 12 deadline for filing briefs has now passed and this matter is ready for determination.

STATEMENT OF THE CASE

Plaintiff filed this complaint objecting to discharge pursuant to 11 U.S.C. § 523(a)(2)(A). It asserts that Debtor received an AT&T credit card and knew or should have known that she was approaching the limits of her ability to pay. Plaintiff also asserts that Debtor continued to use the credit card with no intention of paying the debts and with reckless disregard of her ability to pay. Finally, Plaintiff asserts that Debtor used the credit card for purposes not authorized by the contract.

Debtor asserts that the charges she incurred on the credit card obtained from Plaintiff were made for legitimate purposes consistent with the cardholder agreement. She maintains that she made the charges with the intent to pay when loans from the Small Business Administration and local banks were approved.

FINDINGS OF FACT

Debtor is 39 years old, has a high school education, and has completed some college courses. By August 1994, Debtor was debt free and had money in her bank account. She also had a good credit history.

Despite having no prior experience operating a business, Debtor started "Reality Based Transportation Services" as a sole proprietorship on October 17, 1994. The business purpose was to provide transportation for physically and mentally handicapped individuals. In setting up this business, Debtor acquired five vehicles, a small office, and some office furniture.

To finance her venture, Debtor used her own funds and money borrowed from her grandmother. Debtor also applied for business loans from several banks in the Waterloo area and sought funds from the Small Business Administration (SBA).

Debtor received a pre-approved credit card application from AT&T Credit Card Corporation during the time she was applying for these business funds. She could accept the credit card either by returning the written application or by telephone. Debtor accepted the credit card by phone.

Plaintiff sent Debtor the credit card and included a document called "Cardmember Agreement." This document, introduced into evidence as "Exhibit 1", sets out the terms of the contract between Plaintiff and Debtor. Paragraph three of the Agreement states that the contract between Plaintiff and the cardholder becomes effective once the cardholder uses the card or account. Paragraph four admonishes the cardholder not to exceed the credit limit. Paragraph five states as follows:

> You can use your Account and your Card for personal, family, or household purposes only. Your Card can be used to purchase or lease goods and services from participating establishments. You may also use the Card to obtain a loan from your Account, by presenting it to any institution that accepts the Card for that purpose, or to make a withdrawal of cash at an Automated Teller Machine (ATM).

Debtor began using the credit card almost immediately. She was low on funds because she had generated only a few accounts receivable and had not yet obtained additional funds through either the SBA or the banks. Debtor made her first charge on the credit card on November 1, 1994 at Wal-Mart for $709.65. The second charge, in the form of a cash advance of $5500, was incurred November 8 at the National Bank of Waterloo. A second cash advance was made from Norwest Bank of Iowa on November 28 in the amount of $200. The remainder of the charges were to hotels, gas stations, and Wal-Mart.

In total, Debtor used the card issued by Plaintiff for six purchases totaling $1077.94 and two cash advances totaling $5700. Exhibit 3 evidences that the card had a credit limit of $6500 which Debtor exceeded on December 4. At the time of trial, the total amount due from charges, cash advances, penalties, and interest was $7203.54.

Debtor made one payment by check to Plaintiff on November 21, 1994. This check, however, was returned for insufficient funds. Plaintiff did not resubmit the check for payment. Debtor made no further payments on the account.

Plaintiff initially contacted Debtor on December 19, 1994 concerning the NSF check with additional contacts on January 4, 1995 and January 18, 1995. The financing which Debtor sought never materialized and she first met with an attorney for the purpose of filing bankruptcy on January 18, 1995. This visit subsequently led to her filing a chapter 7 petition on February 24, 1995.

Plaintiff does not make any specific allegations of fraudulent misrepresentation. Ms. Sherrill Jean Vawter, the investigating manager for AT&T Corporate Security, testified that AT&T obtains a potential cardholder's credit history before sending the pre-approved application. Concerning Debtor's acceptance of the card by telephone, Ms. Vawter testified that the usual information obtained in the phone conversation is the applicant's name, address, social security number, income, and a secret code. Mrs. Vawter testified further that she was not aware of any statements made by Debtor other than the statement of personal income. There is no testimony in this record that any of the information provided over the telephone was inaccurate or fraudulent in any way.

Debtor testified that while she had no previous experience operating a business she remained optimistic about the business' initial chances for success. Once the business started, she was confident that the business would continue when additional infusions of funds became available from loans, her grandmother, and future business receipts.

Debtor testified that she provided her previous year's income in response to Plaintiff's inquiry of her annual income. She also testified that upon taking out the $5500 cash advance, she deposited $5000 in her business account and recorded it as a personal loan from herself to the business. Debtor used the remaining $500 from this $5500 cash advance for personal expenses. She maintains that all of the charges on the card were incurred with the intent that they would be paid once her loans were approved and the funds made available to Debtor.

CONCLUSIONS OF LAW

Plaintiff filed this complaint objecting to discharge of its claim under § 523(a)(2)(A). A debt is excepted from discharge pursuant to § 523(a)(2)(A) if it is incurred through "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) (1996).

Before a debt will be excepted from discharge pursuant to § 523(a)(2)(A), a test comprised of five elements must be satisfied. In re Stanton, Adv. No. 95-2031KD, slip op. at 3 (Bankr. N.D. Iowa Jan. 10, 1996). These five elements provide that: (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, Field v. Mans, 116 S. Ct. 437, 446 (1995); 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). Plaintiff must prove these elements by a preponderance of the evidence. Grogan v. Garner, 111 S. Ct. 654, 659 (1991).

Contract law governs credit card obligations. In re Walderbach, Adv. No. 92-1135LC, slip op. at 3 (Bankr. N.D. Iowa Aug. 31, 1993). A contract between the credit card issuer and the cardholder is not formed by receipt and return of a credit card application; the potential cardholder gives no consideration by just providing information. Id. Neither is a contract formed once the cardholder receives the credit card; this is merely an offer to extend credit. Id. A contract between the credit card issuer and the cardholder is formed through the cardholder's use of the credit card or the account. Id. Once a charge is incurred, the credit card issuer promises to pay the charge and the cardholder reciprocates by promising to repay the credit card issuer the charge incurred in the transaction. Id. Promises made in good faith are not misstatements or misrepresentations of fact. In re Cox, 161 B.R. 667, 670 (Bankr. W.D. Ark. 1993). The charges incurred are not rendered nondischargeable under §523(a)(2)(A) when a cardholder's good faith promise is not carried out. Id.

A § 523(a)(2)(A) misrepresentation can occur at the start of the relationship, or impliedly upon first use of the credit card. Stanton, slip op. at 4. Use of a credit card serves as an implied representation to the card issuer that the cardholder has incurred the charges with both the ability and the intention to pay for them. In re Stewart, 91 B.R. 489, 495 (Bankr. S.D. Iowa 1989). Once this representation as to the cardholder's ability and intention to pay is implied by the law, the first three elements of the test under § 523(a)(2)(A) interlock. Walderbach, slip op. at 4. These three elements (debtor's false representations, debtor's knowledge that these representations were false, and debtor's intention and purpose of deceiving the creditor) are jointly decided in the affirmative or negative once the Court determines whether Debtor had the ability and the intention to pay for the charges incurred. Id.

Plaintiff has not alleged that Debtor made explicit misrepresentations to Plaintiff. However, Plaintiff has asserted numerous allegations of implied misrepresentation. Plaintiff asserts that at the time the Debtor received the card, she did not have the ability or the intention to pay the charges made. Secondly, Plaintiff asserts that Debtor continued to use the credit card after it became apparent, or should have been apparent, that she did not have the ability to pay those charges. Finally, Plaintiff asserts that Debtor used the credit card for business purposes which were not authorized by the underlying contract.

The first two allegations are essentially the same in that Plaintiff asserts that a credit cardholder makes an implied representation when she uses the credit card that she has both the ability and the intention to pay them. Plaintiff asserts that Debtor did not have the ability nor the intention to pay these charges. Debtor, however, testified that she believed, at the time that she incurred the charges, that she would have the ability to pay for charges incurred once the additional funding for her business was approved by the SBA and/or local banks and once her accounts receivable began to be paid.

While the record is somewhat murky as to the exact dates that Debtor learned that she would not receive additional funds, it is the ultimate conclusion of this Court that Debtor incurred these credit card obligations prior to learning that additional funds for her business would not be forthcoming. Without the additional funds, Debtor was not able to remain in business and generate the anticipated revenue with which she testified she intended to pay off the credit card obligations. It is the conclusion of this Court that the use of the credit card by this Debtor did not constitute either overtly or impliedly a misrepresentation on the part of this Debtor. While technically true that at the time the charges were incurred, Debtor did not have the cash available to pay the entire amount due, Debtor did have a reasonable

expectation that funds would be shortly forthcoming with which to pay these charges. It is ultimately the conclusion of this Court that Plaintiff has failed to establish that Debtors use of the credit card constituted a misrepresentation of her ability to pay the obligations when they became due.

The final allegation made by Plaintiff relates to Plaintiff's claim that Debtor incurred charges on this credit card for purposes contrary to those set out in the cardholder agreement. Specifically, Plaintiff asserts that Debtor fraudulently violated paragraph 5 of the cardholder agreement by using the credit card for business purposes when the stated purpose was for personal, family, or household purposes only. The record establishes that Debtor did use $5,000 from a cash advance for business purposes. Debtor, however, asserts that the language when construed properly does not limit cash advances to personal, family, or household purposes only.

The parties have not submitted to the Court any authority that establishes that use of the card, in this context, constitutes a misrepresentation, even if the language is properly construed as Plaintiff interprets it. The law provides that these types of contracts must be interpreted in such a manner that ambiguities are interpreted against the party drafting the contract. Johnson Controls, Inc. v. City of Cedar Rapids, Iowa, 713 F.2d 370, 375 (8th Cir. 1983); Rector v. Alcorn, 1241 N.W.2d 196, 202 (Iowa 1976). It is the conclusion of this Court that, in this case, the language is sufficiently ambiguous that the strict interpretation sought by Plaintiff is inappropriate.

Even assuming that the construction sought by Plaintiff is correct, it is difficult to perceive the precise nature of the misrepresentation alleged. Debtor commenced this business as a sole proprietorship. She was personally responsible for payment of all of the obligations incurred by the business. It is difficult in this context to distinguish between personal use or business use. Regardless, the Court finds it inappropriate to conclude that use of the credit card for a purpose not specifically provided in the cardholder agreement constitutes an implied misrepresentation.

It is the general rule that where a lender assumes that the loan is given for a specific purpose and the borrower does not mention the purpose for the loan, the fact that the borrower uses the loan for another purpose, does not in and of itself preclude dischargeability of the debt. In re Watson, 22 B.R. 938, 940 (Bankr. M.D. Fla. 1982) (dictum). If the purpose of the funds were critical to the transaction, a borrower could possibly acquire the loan under false pretenses. There is nothing in this record, however, which establishes that Plaintiff relied on this type of misrepresentation in extending the credit. Ultimately, it is the conclusion of this Court that the use of the card for a purpose other than that specifically set out in the contract, even if applicable here, would not in and of itself constitute a misrepresentation. At best, it would constitute a breach of the underlying cardholder contract.

Such a breach could have relevance in the determination of whether or not Debtor intended to pay the obligation, the next element Plaintiff must prove. Debtor's intent is a critical component in the combined analysis of the first three elements of the test under § 523(a)(2)(A). Walderbach, slip op. at 5. In assessing intent, most courts, including the Northern and Southern Districts of Iowa, have adopted the totality of the circumstances approach. In re Davis, No. X91-01771F, slip op. at 7 (Bankr. N.D. Iowa Aug. 21, 1992); Stewart, 91 B.R. at 495.

This approach considers the following nonexclusive list of factors to find the lack of intention to pay creditors under § 523(a)(2)(A): (1) the length of time between the charges and the bankruptcy filing; (2) whether the debtor consulted an attorney about filing bankruptcy before the debtor made the charges; (3) the number of charges made; (4) the amount of the charges; (5) the financial condition of the debtor at the time of the charges; (6) whether the charges exceed the limit of the account; (7) whether the debtor made multiple charges on one day; (8) whether the debtor was employed; (9) what the debtor's prospects were for employment; (10) the debtor's financial sophistication; (11) whether there was a sudden change in the debtor's buying habits; and (12) whether the debtor purchased luxuries or necessities. Davis, slip op. at 7. Despite the recognition "that misconceived optimism [to pay] is not uncommon to the financially distressed," Stewart, 91 B.R. at 495, this Court previously has found the lack of an intent to pay a creditor based on the sole factor that there was no realistic possibility that the debtor could repay the indebtedness. Davis, slip op. at 7-9.

Two facts impact adversely upon the Debtor. First, the majority of the charges were created in one month and Debtor filed bankruptcy within 90 days of incurring the last charge. These facts admittedly give the initial impression that Debtor was "loading up" her credit card in anticipation of receiving a discharge on the debt. Stewart, 91 B.R. at 495. Secondly, Debtor sent Plaintiff payment by check dated November 21, 1994 which was returned for insufficient funds.

The evidence, when considered as a whole, adequately addresses and resolves these adverse impressions. As to the first adverse fact, while it is true that Debtor incurred all of the charges within a short period of time prior to bankruptcy, the record is compelling that Debtor did not do so for the purposes of inappropriately using this credit card. Going into her new venture, Debtor had a good credit rating, she had few, if any, outstanding obligations, and she was paying all of her debts as they became due. She had just commenced a new business venture and was optimistic about its success. Such a factual determination negates the conclusion that this Debtor was in financial difficulty and was using her credit card for an inappropriate purpose immediately prior to filing bankruptcy.

Secondly, pursuant to § 523(a)(2)(A), a debtor's attempt to pay the plaintiff is not rendered fraudulent by the later discovery that there were insufficient funds to cover the check. In re Stockdale, Adv. No. 82-0177, slip op. at 4 (Bankr. N.D. Iowa Jan. 31, 1984). Therefore, the NSF check does not, by itself, negate a finding that Debtor in good faith intended to repay her obligations to Plaintiff.

Debtor testified that she intended to repay her credit card debts once the SBA and the local banks approved her business loans and the funds became available to her. Predictions of future events may be fraudulent under §523(a)(2) if a debtor does not really hold these predictions as true or they are made recklessly. In re Pallo, 65 B.R. 101, 104 (Bankr. W.D. Ky. 1986). However, there is nothing in this record to support a conclusion that Debtor was untruthful or reckless in her belief that the debt to Plaintiff would be repaid from future resources.

While self-serving expressions of good intentions standing alone may not enable a court to find a debt dischargeable, a debtor's demeanor is a legitimate factor in the court's decision. Davis, slip op. at 9. In Davis, the debtor testified that she intended to repay her credit card obligations but bad luck prevented repayment. The court did not believe the debtor and subsequently found the debt nondischargeable because her "uncooperative ... , almost belligerent" demeanor at trial contradicted her testimony. Id. However, in this case, the Court concludes that Debtor's demeanor matched the intent she voiced during her testimony.

Ultimately, it is the conclusion of this Court that while Debtor may have been naive in commencing a business of this magnitude prior to acquiring guaranteed financing, Debtor's use of this card did not constitute a misrepresentation of her ability or intention to pay the credit card obligations which she incurred. As such, Plaintiff has failed to establish by a preponderance of evidence the first three elements of the test under § 523(a)(2)(A).

Reliance and causation remain unresolved under § 523(a)(2)(A). The Court has concluded that there were no misrepresentations upon which Plaintiff could or should have relied. As such, the element of justifiable reliance is not present. Additionally, as there was no misrepresentation or reliance, the charges incurred and the injuries allegedly suffered by Plaintiff were not causally related to any misrepresentations.

CONCLUSION

A debt is excepted from discharge pursuant to § 523(a)(2)(A) if a card issuer establishes each element of the five part test by a preponderance of evidence. This Court concludes, based upon the record made, that Debtor did not make any actual or implied misrepresentations to Plaintiff. While the commencement of Debtor's business may have been naive under all of the circumstances present, this Court concludes that Debtor did not misrepresent her position to Plaintiff and it was her intent to pay the charges made against this credit card. As there were no misrepresentations, there was nothing upon which Plaintiff could rely to its detriment. Finally, any alleged injury did not occur as a proximate result of any representations made by Debtor. As such, it is the finding of this Court that Plaintiff has failed to establish by a preponderance of evidence the requisite elements excepting this obligation from discharge under § 523(a)(2)(A). The obligation is therefore dischargeable.

WHEREFORE, Plaintiff has failed to establish its claim of nondischargeability pursuant to § 523(a)(2)(A) by a preponderance of evidence.

FURTHER, the debt incurred by Debtor to Plaintiff AT&T Universal Card Services is dischargeable.

SO ORDERED this 19th day of April, 1996.

Paul J. Kilburg
U.S. Bankruptcy Judge