

CONSUMER BANKRUPTCY

Did Santa Leave the Debtor Some Gift Cards?

By **Craig D. Robins**

Now that the holidays have just passed, it's a perfect time to discuss whether consumers can load up with gift cards before filing for bankruptcy relief, and then exempt them. As gift cards have become especially popular over the past several years, many potential debtors not only own a small treasure trove of unredeemed cards, but some have even purchased them to spend down their non-exempt cash before filing their bankruptcy case.

This is exactly what a Kansas couple recently did before filing their Chapter 7 petition. They had more cash than what the Kansas exemption statute permitted them to protect, so they purchased several gift cards from local retailers, including Target, Costco and a gas station chain, totaling \$4,000. They were candid and honest about it as they listed the gift cards as assets in their petition, which they also exempted pursuant to the Kansas statute exempting "household furnishings and supplies." Kansas has its own exemption statutes and has opted out of using the federal exemptions.

The trustee quickly filed a motion objecting to this exemption by arguing that the gift cards were "essentially cash," and therefore did not qualify as household furnishings or supplies. Prior to the hearing on the motion, the parties stipulated to various facts including that the gift cards can be used by anyone in possession of the cards; the cards can be

sold on the secondary market; and there are websites that exist for that purpose.

Kansas Bankruptcy Judge Dale L. Somers issued a decision on this motion two weeks before Christmas. *In re Parks*, 18-40736 (Bankr. D. Kan. Dec. 12, 2018). The judge began his discussion by pointing out two basic elementary law principles: the party objecting to an exemption has the burden of proving that the debtor did not properly claim the exemption; and exemption statutes are to be liberally construed for the benefit of the debtor.

The court then looked at the express language of the exemption statute (which is similar to New York's personal property exemption). The statute protects "furnishings, equipment and supplies, including food, fuel and clothing," and it applies to what "is in the person's present possession," and to what "is reasonably necessary at the principal residence . . . for a period of one year."

The judge then noted that on their face, gift cards do not appear to fall within the statute's contours as they are not furnishings, equipment or supplies that are in the debtor's current possession. "At best, a gift card is a 'purchase instrument' that can buy a future furnishing or supply." However, the judge stated that this raises an important issue: How is a gift card different than cash?

The debtors argued that a gift card is a tangible device which promises to provide



Craig Robins

the bearer merchandise of equal value to the remaining balance of the device. The debtors also pointed out that Kansas statutes treat a gift card differently than a "prepaid bank card," which is essentially an "electronic payment device" issued by a bank. The state statute specifically states that a gift card "does not include a prepaid bank card."

The debtors also argued that the gift cards created a binding sales contract with the applicable retailers for the exchange of goods that the retailers sell, and therefore, the cards were "equitably converted" into merchandise at the time the gift cards were activated.

Unfortunately for the debtors, despite their clever and creative persuasive arguments, the judge concluded that they could not exempt the gift cards. The judge found that gift cards were similar to prepaid bank cards in that both can be sold for cash despite the fact that use of the gift cards can be limited to a variety of retailers.

The judge also took judicial notice that even though the gift cards can only be redeemed for merchandise, this could easily include flat screen televisions, dirt bikes, or jewelry that can then be given as gifts. "Just because something is a 'good' does not mean that it is a good that is reasonably necessary at a person's household for the year."

Finally, the court found two other cases with similar issues, both from Arizona, which

held that the gift cards were not exempt, pointing out that they were the "functional equivalent to cash." So, these debtors received coal in their stockings for Christmas.

Here are some practice tips. Many debtors may own gift cards but may not think to disclose that fact to their attorney, which could then result in a petition that does not fully disclose all of their assets. Since a subsequent discovery of the gift cards by the trustee can have profound consequences on the debtor's ability to obtain a discharge, it would be wise to remind your clients about the importance of revealing all assets.

In addition, some debtors who have judgments against them may consider purchasing gift cards to get cash out of their names so that it cannot be restrained. However, consider whether an aggressive creditor can make an argument that such conduct constitutes an attempt to hinder or delay the legitimate collection remedies of the judgment creditor, which could be grounds for objecting to discharge.

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