

Casino Debtors Will Not Find a Haven from Nevada's Bad Check Statute in Bankruptcy



By Vernon Nelson

In the past year, two cases have reaffirmed the now well-established notion that Bankruptcy Courts are not a haven from criminal prosecution. They also established that the longheld sovereign right of states to formulate and enforce their own penal statutes is paramount to a debtor's need for a fresh-start. Thus, neither a Bankruptcy Court nor any other federal court can enjoin the State of Nevada from prosecuting defendant-debtors under NRS § 205.130. Likewise, a defendant's obligation to pay criminal restitution cannot be discharged in bankruptcy.

In Ravani v. Wolfson (In Re: Ravani), Adv. No. 1-12-ap-01303-GM, the United States Bankruptcy Court for the Central District of California denied the Debtor's motion for a temporary restraining order that would have enjoined the prosecution of the Debtor in Nevada. The Debtor executed credit instruments at Hard Rock and Treasure Island casinos in Las Vegas in 2009; which were about 20 months before he filed his Chapter 7 Petition. The Debtor failed to repay the credit instruments, The Hard Rock and Treasure Island casinos, in turn, filed complaints with the Clark County District Attorney's office. The Debtor filed his Chapter 7 Petition in the United States Bankruptcy Court for the Central District of California in February 2011. The Bankruptcy Court granted Debtor's discharge on February 7, 2012, and closed the bankruptcy case. A Clark County Grand Jury indicted the Debtor on February 22, 2012. The Debtor filed a Petition for

Writ of Habeas Corpus and a Motion to Dismiss for Violation of Nevada's Equal Protection Clause and For Selective Prosecution. The Debtor also sent communications to the Clark County District Attorney, the Nevada Attorney General, the Clark County Clerk, and the Justice Court of Las Vegas Township demanding that these parties cease any further prosecution of the Debtor. The Debtor claimed that the criminal prosecution violated 11 USC § 524, because the criminal action was an effort to collect a discharged debt. The Debtor's efforts were for naught and the criminal case was set for trial in September 2012.

Thereafter, the Debtor successfully moved to reopen his bankruptcy case and he filed an Adversary Complaint against representatives of the Clark County District Attorney Office, representatives of the Nevada Attorney General's Office, the Hard Rock and Treasure Island casinos. The complaint requested injunctive relief and damages. The Debtor also filed a motion for a temporary restraining order that would have enjoined the parties from continuing with the criminal prosecution while the Adversary Case was proceeding. Counsel for Hard Rock was able to file a brief opposition to the motion for the temporary restraining order.

The Bankruptcy Court denied the Debtor's motion and entered an order which adopted the position as set forth in the Bankruptcy Court's posted "tentative ruling." The Court's written order cites and follows several cases decided by the United States Court of Appeal for the 9th Circuit and other courts within the Circuit. Most prominently, the Bankruptcy Court followed the decisions of: (1) the Bankruptcy Appellate Panel in *Nash v. Clark County District Attorney's Office*, (In re Ryan Nash), 464 B.R. 874 (9th Cir. BAP 2012); and (2) *Gruntz v. County of Los Angeles*, 202 F.3d 1074 (9th Cir. 2000).

In *Nash*, the Bankruptcy Appellate Panel ("BAP") for the 9th Circuit upheld the Bankruptcy Court's order denying sanctions against the Clark County District Attorney. Like Ravani, Nash had insufficient funds in his bank account to pay for \$12,500 in credit instruments that he issued to the Hard Rock casino. The District Attorney commenced a criminal action against Nash prior to March 26, 2009, and an arrest warrant was issued. Nash filed a bankruptcy petition several months later in August 2009. Neither the Hard Rock casino nor the District Attorney appeared in the bankruptcy action and Nash was granted a discharge in January 2010. Nash was arrested on March 22, 2010. He successfully moved to reopen his bankruptcy action and filed an adversary complaint against the District Attorney and the Hard Rock casino. Neither the District Attorney nor the Hard Rock casino appeared in the adversary action and Nash moved for a default judgment. The Bankruptcy Court refused to enter a default judgment against the Hard Rock casino, because it found that any collection efforts that it undertook occurred before Nash filed for bankruptcy. The Bankruptcy Court also refused to enter a default judgment against the District Attorney based on the principles set forth in *Gruntz v. County of Los Angeles* (In Re Gruntz), 202 F.3d 1074 (9th Cir. 2000) (en banc),

and refused to interfere with the Nevada criminal proceedings. The 9th Circuit's decision in *Gruntz* essentially overturned the earlier 9th Circuit decision in *Hucke v. Oregon*, 990 F.2d 950 (9th Cir. 1993). In *Hucke*, the court held that if "a criminal proceeding" has the collection of a debt as its underlying aim, then the automatic stay imposed by § 362(a)(6) would enjoin the criminal action. In determining the "underlying aim," the *Hucke* Rule required the court to determine whether the "primary motivation" of the prosecution was debt collection.



The *Gruntz* court rejected the *Hucke* Rule and stated that prosecutorial discretion was the primary concern. The *Gruntz* court recognized notions of "cooperative federalism" and that "Congress has specifically subordinated the goals of economic rehabilitation and equitable distribution of assets to the states' interest in prosecuting criminals." In this regard, the *Gruntz* court added that, "[o]nce the state has made an independent decision to file criminal charges; the prosecution belongs to the government, not the complaining witness." The *Gruntz* court emphasized that once the prosecutor has probable cause to believe a crime has been committed; the decision whether not to file charges lies within the prosecutor's discretion. The *Gruntz* court pointed to the Supreme Court's decision in *Wayte v. United States*, 470 U.S. 598 (1985), to illustrate that the "decision to prosecute is particularly ill-suited for judicial review. Based on the foregoing analysis, the *Gruntz* Court held that the automatic-stay provisions of the bankruptcy code did not void the state criminal judgments against *Gruntz*.

The *Gruntz* Court also relied heavily on the principles set forth by the Supreme Court in *Kelly v. Robinson*, 479 U.S. 36, 47 (1986), and stated that, "[w]e maintain the deep conviction that Federal Bankruptcy Courts should not invalidate the results of state criminal proceedings." The *Kelly* Court recognized that "the right to formulate and enforce penal sanctions is an important aspect of the sovereignty retained by the States."

Once again, in *Nash* the 9th Circuit BAP followed the principles set forth in *Gruntz* to determine that the strong public policy expressed in *Gruntz* prohibited the Bankruptcy Court from interfering in the state court criminal action. Accordingly, the BAP Court affirmed the Bankruptcy Court decision to refuse to interfere in the criminal case that the District Attorney filed against *Nash*.

As it's mentioned above, the *Ravani* Court followed the principles set forth in *Nash* and *Gruntz*. While *Ravani* tried to provide evidence that he was not guilty of the crimes alleged, the Bankruptcy Court correctly noted that it was not the court that would determine *Ravani's* guilt or innocence. Further, *Ravani* did not allege that the criminal action violated any other federal or state law. Accordingly, the Bankruptcy Court refused to interfere with the Nevada criminal proceedings and denied *Ravani's* motion. *Ravani* eventually entered in to a plea bargain and the adversary case was dismissed.

The cases above demonstrate that Bankruptcy Courts cannot enjoin pending state criminal matters. The other side of the coin is the defendant/debtor's attempts to discharge restitution obligations in bankruptcy.



It is common for debtor-defendants to be ordered to make restitution as part of their criminal case sentencing. On several occasions, debtor-defendants have unsuccessfully filed bankruptcy in an attempt to avoid their restitution obligations.

Most recently, in *United States v. Colasuonno*, 697 F.3d 164 (2d. Cir. 2012), the Second Circuit Court of Appeals held that: (1) court ordered restitution, imposed as a condition of probation; and (2) proceedings related to the payment of restitution and its impact on probation are a continuation of the criminal action against the defendant. As a result, such proceedings are not stayed by the automatic stay provisions of 11 USC § 362(a). Instead, these proceedings fall squarely within 11 USC § 362(b); which provides that a debtor cannot stay the commencement or continuation of a criminal action against the debtor by filing for bankruptcy. In reaching

this decision, the 2nd Circuit cited several of the principles set forth in *Kelly* and *Gruntz*.

In its decision, the 2nd Circuit examined 11 USC § 362(b) and the meaning of a criminal proceeding. In so doing, the 2nd Circuit favorably cited the *Gruntz* court's contention that "Congress specifically subordinated the goals of economic rehabilitation and equitable distribution of assets to the states interest in prosecuting criminals. In *Kelly*, the 2nd Circuit also noted out that, the Supreme Court had recognized that "[a]lthough restitution does resemble a judgment 'for the benefit' of the victim, the context in which it is imposed," a criminal proceeding, "undermines that conclusion." The 2nd Circuit also recognized that in *Gruntz*, the 9th Circuit rejected the prior reasoning of *Hucke*. The 2nd Circuit agreed with *Gruntz's* holding that the plain language of § 362(b)(1) prohibits the enjoining of all criminal proceedings, including those pertaining to the non-payment of restitution.

With the guidance of *Gruntz* and *Kelly* in mind, the 2nd Circuit stated:

With this understanding of the language of 362(b)(1), we easily conclude that Colasuonno's criminal prosecution for bank fraud and tax crimes constituted a criminal action. We further conclude that, for purposes of § 362(b)(1), the criminal action did not end when the judgment of conviction became final. Rather, the action continued through satisfaction of the judgment because all duties imposed on the defendant, as well as the court's authority to hold the defendant to account for those duties, derive from, and in that respect continue, the original criminal action. To hold otherwise would be to ignore the fact that the purpose of a criminal action is not simply to charge a defendant with criminal conduct or to try him on such charges. It is to punish the defendant for offenses committed against the public.

The Court went on to note:

While we think the plain meaning of the text, viewed in context, is sufficient to reach this conclusion, it is reinforced by the legislative history of § 362(b), which emphasizes that "bankruptcy laws are not a haven for criminal offenders, but are designed to give relief from financial over-extension." S. Rep. 95-989, at 54 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5840. A failure to recognize enforcement of the conditions of a probationary sentence or proceedings to address violations of probation as a "continuation" of the criminal action that resulted in such a sentence would allow the bankruptcy laws to become a haven for criminal offenders, allowing them to interrupt, if not completely frustrate, their criminal punishment.



The United States Bankruptcy Court for the Eastern District of North Carolina reached a similar conclusion in the case of *In Re: Byrd*, 256 B.R. 246 (Bankr. E.D.N.C. 2000). In *Byrd*, the Debtor delivered credit instruments to Caesars Palace and Circus Circus casinos in April 1998. When the credit instruments were returned unpaid, the casinos notified the Clark County District Attorney. The Debtor filed bankruptcy in September 1998. In October 1998, the District Attorney notified Debtor that it would proceed with criminal charges against *Byrd*. In May 2000, *Byrd* was involved in an automobile accident and the police discovered that a warrant had been issued for *Byrd's* arrest in Clark County and that bail had been set at \$32,000 (approximately the amount of the unpaid credit instruments). *Byrd's* wife gathered enough money to pay the bail. Upon receipt of the bail amount, the District Attorney undertook efforts to withdraw the warrants and dismiss the case.

Byrd filed a motion for an order to show cause to require the casinos and the District Attorney to show cause why they had not violated the automatic stay and the discharge provisions of the United States Bankruptcy Code § 362(a) and § 524 (a)(2). The Court found that these sections of the Code had not been violated.

Like the 2nd Circuit in *Colasuonno*, the *Byrd* Court cited with approval the rationale underlying the 9th Circuit's decision in *Gruntz*. The *Byrd* Court also recognized the federalism principles set forth by the Supreme Court in *Kelly*. Furthermore, the *Byrd* Court explicitly rejected the "principal motivation" test as described in *In Re Wise*, 25 BR 440, 442 (Bankr. E.D. Va. 1982).

The *Byrd* Court recognized that, pursuant to 11 U.S.C. § 362(b)(1), the filing of a bankruptcy petition does not stay "the commencement or continuation of a criminal action or proceeding against the debtor." As a result, the *Byrd* court held that this section authorized the commencement or continuation of the criminal action by Clark County against *Byrd*.

The *Byrd* Court went on to hold that Clark County's recovery of the discharged debts for the purpose of providing restitution to the casinos was also authorized under 11 USC § 362(b)(1) and 11 USC § 523(a)(7). Section 523(a)(7) provides that a discharge under chapter 7 does not discharge a debtor from any debt "to the extent

such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss."

The *Byrd* Court correctly identified NRS § 205.130 as a penal statute and concluded "that under *Kelly v. Robinson*, 479 U.S. 36, 93 L. Ed. 2d 216, 107 S. Ct. 353 (1986), and related precedent, that the State of Nevada was entitled to commence or continue a criminal prosecution against a debtor even if the prosecution is based upon a debt that could be discharged in bankruptcy, and even if the prosecuting entity intends to pass recovered monies on to the complaining victim/creditor in the form of restitution."

Like the 2nd Circuit, the *Byrd* Court recognized *Kelly's* admonition that "[a]lthough restitution does resemble a judgment 'for the benefit of' the victim, the context in which it is imposed undermines that conclusion." The *Byrd* Court went on to recognize that *Byrd* was not required to pay restitution and that he was entitled to "judicial overview and discretion," had he chose to defend himself against the charges in Nevada. Based on these factors, the Court concluded: "the fact that the restitution was paid by *Byrd* on short notice and without the exercise of judicial oversight is the price *Byrd* paid for sending in payment rather than staying in jail pursuant to a lawful warrant."

The *Byrd* Court went on to recognize Nevada's right to require restitution as part of a criminal sentence. The *Byrd* Court also noted that *Kelly* held that restitution ordered as part of a criminal sentence squarely fits within the non-dischargeability provisions of 11 U.S.C. § 523(a)(7). Based on the foregoing considerations, the *Byrd* Court held that the restitution and fines *Byrd* paid were, pursuant to the Nevada statute, within the "fine, penalty or forfeiture" language of 11 U.S.C. § 523(a)(7).

In summary, these cases illustrate how debtor-defendants may not be able to avoid their obligations under credit instruments by filing for bankruptcy.¹ The automatic-stay does not stay criminal prosecutions under NRS § 205.130. Furthermore, bankruptcy does not discharge debtor-defendants' obligations to pay court-ordered restitution.

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¹ There is some *dicta* in *Byrd* that seems to indicate that a creditor can violate the stay by filing a bad check complaint *after* a debtor has commenced a bankruptcy proceeding. Casinos should consult with legal counsel before filing a complaint after a debtor has commenced a bankruptcy proceeding.