



Jack Rose Law



RAY QUINNEY
& NEBEKER

80 YEARS
1940-2020

VICARIOUS LIABILITY

Jack J. Rose
David H. Leigh

WHAT IS VICARIOUS LIABILITY?

- **Bartenwarfer**
- Supreme Court Decision on Vicarious Liability
- Section 523(a)(2) Of the Bankruptcy Code
- (a) A discharge under section [727](#), [1141](#), [1192](#) [1] 1228(a), 1228(b), or 1328



WHAT IS VICARIOUS LIABILITY?

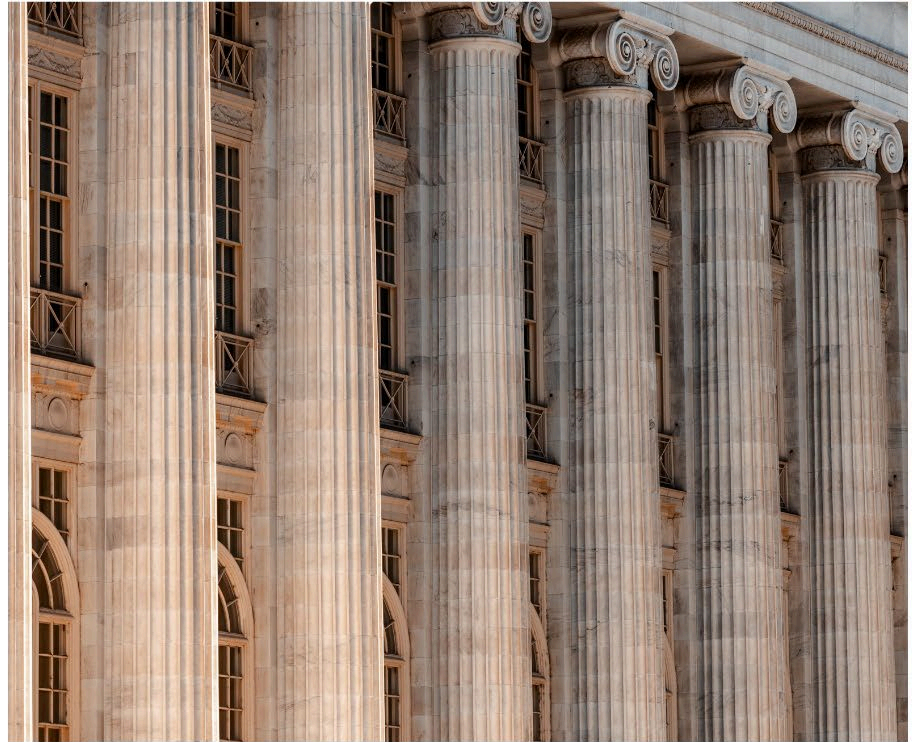
- **Section 523(a)(2) Of the Bankruptcy Code**

- (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; or



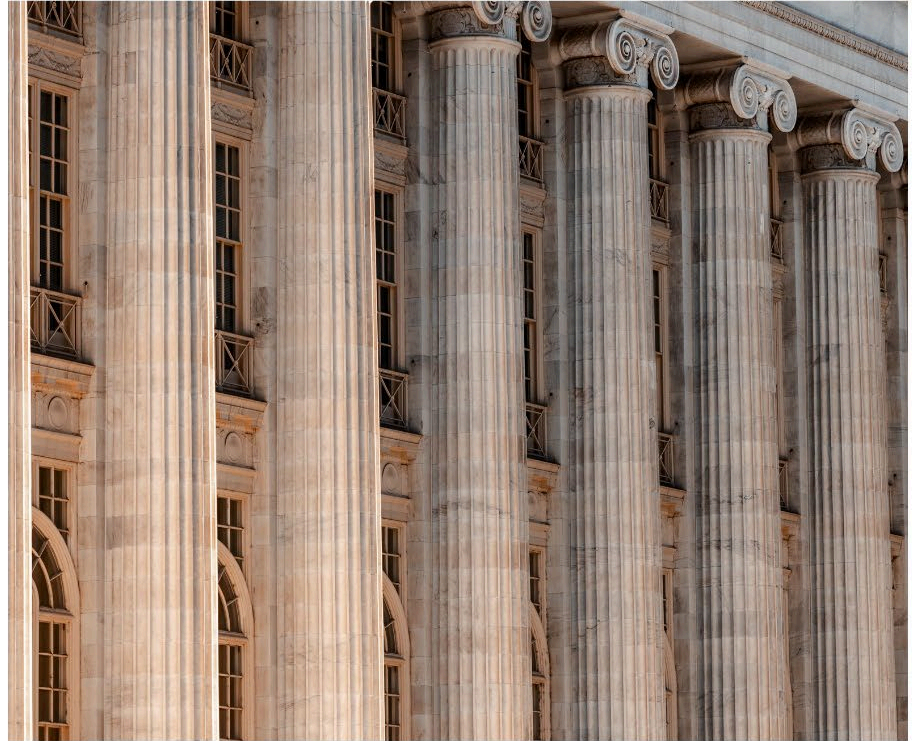
WHAT IS VICARIOUS LIABILITY?

- **Section 523(a)(2) Of the Bankruptcy Code**
- (C) (i) for purposes of subparagraph
 - (A)—(I) **consumer** debts owed to a single creditor and aggregating more than \$500 [2] for luxury goods or services incurred by an individual debtor on or within 90 days before the order for relief under this title are presumed to be nondischargeable; and
 - (II) cash advances aggregating more than \$750² that are extensions of **consumer** credit under an **open end credit plan** obtained by an individual debtor on or within 70 days before the order for relief under this title, are presumed to be nondischargeable; and



WHAT IS VICARIOUS LIABILITY?

- (ii) for purposes of this subparagraph—
 - (I) the terms “consumer”, “credit”, and “open end credit plan” have the same meanings as in section 103 of the Truth in Lending Act; and
 - (II) the term “luxury goods or services” does not include goods or services reasonably necessary for the support or maintenance of the debtor or a dependent of the debtor;



INNOCENT SPOUSE DEFENSE (RECOGNIZED BY THE IRS)

- **The Innocent Spouse Defense**

- Who recognizes the Innocent Spouse Defense
 - The IRS
- Ninth Circuit BAP applies the Innocent Spouse Defense.
 - "As the panel saw it, "§523(a)(2)(A) barred her from discharging the debt only if she knew or had reason to know of David's fraud."
- Supreme Court
 - "'We start where we always do: with the test of the statute'" . . .



CASE SUMMARY: *BARTENWERFER V. BUCKLEY*

- **Parties Involved:**

- Kate Bartenwerfer (and her husband David) were the debtors, while Kieran Buckley was the creditor.

- **Background:**

- The case originated when Bartenwerfer and her husband purchase a house.
- David undertook a renovation of the house the details of which Kate had no knowledge.
- Unbeknownst to Kate there were a number of latent defects in the house.
- David and Kate sold the house to Buckley making certain representations regarding the condition of the property.
- Upon learning of the defects, Buckley sued the Bartenwerfers alleging among other things fraud. The court found in favor of Buckley and awarded him damages.
- The Bartenwerfers subsequently filed for bankruptcy.



CASE SUMMARY: *BARTENWERFER V. BUCKLEY*

- **Legal Issue:**

- The question before the Court was whether Kate Bartenwerfer, who had no knowledge of the fraud committed by her husband, could have the debt discharged.
- Put another way, does Section 523(a)(2)(A) of the Bankruptcy Code, bar the discharge of Kate Bartenwerfer's debt notwithstanding she had no actual knowledge of the fraud or any of the acts obtained by "false pretenses, a false representation, or actual fraud."
- Answer -> **YES IT DOES!**



COURT'S DECISION: *BARTENWERFER V. BUCKLEY*

- The U.S. Supreme Court ruled that a debt incurred through fraud cannot be discharged in bankruptcy, even if the debtor had no personal knowledge of the fraud.
- The Court emphasized that the Bankruptcy Code's language focuses on the nature of the debt itself, rather than the knowledge or intent of the debtor. Thus, even if Bartenwerfer was unaware of her husband's fraudulent actions, the debt to Buckley could not be discharged in bankruptcy.



CASE SIGNIFICANCE: *BARTENWERFER V. BUCKLEY*

- This case clarifies that the dischargeability of a debt in bankruptcy due to fraud does not depend on the debtor's personal involvement, intent or knowledge.
- This could potentially have broad implications beyond personal unions and could extend to partnerships and other joint actions where one party is unaware of the actions taken by another either under the guise of agency or some other form of authority.



BARTENWERFER'S PROGENY

- Imputed Knowledge Being Applied to the Good Faith Exception in Fraudulent Conveyances
- On August 24th from the 5th Circuit Decided a case where investors appointed an agent to take action on their behalf. Much like our friends the Bartenwerfers, the agent took certain unexpected actions resulting in the investors finding themselves subject to unexpected liability.



SCHMIDT V RECHNITZ

- Oil & Gas Deal.
- A couple, Shlomo & Tamar Rechnitz, makes a \$10 million dollar investment in a transaction in an affiliate of a debtor.
- As part of the transaction, they appoint an affiliate of the debtor as their agent.
- Over the Course of the investment, the investors receive certain distributions.
- The investors claim their distributions were received in “good faith” and fell under the “good faith” exception to fraudulent conveyance.
- **Section 550 of the Bankruptcy Code provides in relevant part,**
 - (b)The trustee may not recover under section [1] (a)(2) of this section from—
 - (1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or
 - (2) any immediate or mediate good faith transferee of such transferee.



SCHMIDT V RECHNITZ

- The Court looks to the law of Agency in analyzing the Rechnitz's position
- The Rechnitzs on the other hand argue they were innocent recipients of distributions
- Relying on Agency law and the holdings in the Madoff cases, the Fifth Circuit finds the transfers to the Rechnitzs are avoidable under Sections 548 and 550 of the Bankruptcy Code
- Notably, the Court also cites *Bartenwerfer v Buckley* in its decision.



DRIVETRAIN

- Brief Discussion of Facts of Case
- Discussion of Director Vicarious Liability
- *Drivetrain, LLC v DDE Partners, LLC*
- How Far is Too Far



GET IN TOUCH

Jack Rose Law

RQ & N RAY QUINNEY
& NEBEKER | **80 YEARS**
1940-2020



Jack J. Rose

jrose@jrlpllc.com | (914) 649-8892



David H. Leigh

DLeigh@rqn.com | (801) 323-3382