No. 21-908

In The
Supreme Court of the United States

KATE MARIE BARTENWERFER,

Petitioner,

v.

KIERAN BUCKLEY,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

AMICUS CURIAE BRIEF OF THE HON. JUDITH FITZGERALD (RET.), THE HON. ROBERT GERBER, (RET.), THE HON. EUGENE WEDOFF (RET.), AND LAW PROFESSORS INGRID HILLINGER, GEORGE KUNEY, JULIET MORINGIELLO, NANCY RAPOPORT, WALTER TAGGART, RAY WARNER, AND JACK WILLIAMS IN SUPPORT OF THE PETITIONER

DAVID R. KUNEY
Counsel of Record
DAVID KUNEY LAW
9200 Cambridge Manor Court
Potomac, Maryland 20854
301-299-4336
Davidkuney@dkuney.com

Attorney for Amici Curiae

COCKLE LEGAL BRIEFS (800) 225-6964
WWW.COCKLELEGALBRIEFS.COM

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

Page

OTHER AUTHORITIES

TABLE OF AUTHORITIES—Continued

Page

INTEREST OF *AMICI CURIAE*[1]

Your *amici curiae* are the Honorable Judith Fitzgerald (Bankruptcy Judge, Western District of Pennsylvania, ret.), the Honorable Robert Gerber (Bankruptcy Judge, Southern District of New York, ret.), the Honorable Eugene Wedoff (Bankruptcy Judge, Northern District of Illinois, ret.), and Professors Ingrid Hillinger (Boston College), George Kuney (University of Tennessee College of Law), Juliet Moringiello (Widener University Commonwealth Law School), Nancy Rapoport (William S. Boyd School of Law, University of Nevada), Walter Taggart (Charles Widger School of Law), Ray Warner (St. John's University School of Law) and Jack Williams (Georgia State University).

The *amici* have taught courses on bankruptcy and commercial law, conducted research, and been frequent speakers at seminars and conferences throughout the United States. Each is highly regarded in this field, and each has made substantial contributions to bankruptcy scholarship and jurisprudence.

The question presented on this appeal is whether an individual debtor may be denied a discharge for "actual fraud" under 11 U.S.C. § 523(a)(2)(A) of the Bankruptcy Code solely "by imputation" where it was

---

[1] Pursuant to this Court's Rule 37.3(a), the Petitioner and Respondent have consented to the filing of *amicus* briefs. Pursuant to Rule 37.6, *amici* affirm that no counsel for a party authored this brief in whole or in part, and that no person other than *amici* or their counsel contributed any money to fund its preparation or submission.

determined that the debtor was innocent of any act, fraud, omission, intent, or knowledge of her own. Pet. i.

The Ninth Circuit denied Ms. Bartenwerfer a discharge despite a finding that she was free of any wrongdoing or fraud. The court applied a rule of imputed liability of a partner for the torts of a co-partner, and did so on a strict liability basis, with no exception for innocence or honesty. “Mrs. Bartenwerfer’s debt is nondischargeable regardless of her knowledge of the fraud.” App. 6a. It did not matter, said the court, whether she “knew or should have known” about the fraud. *Id*. Instead, the court ruled that a partner is responsible “for a tortfeasor/partner’s fraud when the fraud was performed ‘on behalf of the partnership and in the ordinary course of the business of the partnership.’ ” App. 6a.

Our interest in filing this *amicus* brief arises from our concern that the decision by the Ninth Circuit may cause a denial of a discharge to other individual debtors who have done no wrong, and who are entitled to such relief under the express terms of 11 U.S.C. § 523(a)(2)(A). The impact of this decision may be widespread. “One in ten adult Americans have turned to the consumer bankruptcy system for help.[2] Over

[2] Pamela Foohey, Robert M. Lawless, Deborah Thorne, *Portraits of Bankruptcy Filers* (March 18, 2021), Georgia L. Rev., Vol. 56, Forthcoming, 15, available at https://dx.doi.org/10.2139/ssrn.3807592.

310,000 individuals filed for Chapter 7 in 2021.[3] Of those who file for Chapter 7, approximately five percent will not receive a discharge.[4] The inability to obtain a discharge has been correctly recognized as the economic death penalty.[5]

Mrs. Bartenwerfer was an honest debtor and was entitled to a discharge. She was denied a discharge of a claim held by Respondent, solely because of the wrongdoing of her husband—who the circuit court deemed to be her "partner." The case arose in connection with the sale of a home the couple was remodeling and intended to sell. Mr. Bartenwerfer was solely in charge of the construction work. He was found to have misrepresented to Respondent several items concerning the construction. Mrs. Bartenwerfer was not. As the Bankruptcy Appellate Panel noted, she was employed elsewhere, was absent from the project, did not engage the professionals handling the remodel, was unaware of the day-to-day activities at the property and was not involved in obtaining permits. App. 15a. "Mrs. Bartenwerfer never interacted with or gave instructions to laborers or contractors; never met with or gave instructions to architects; never wrote checks to contractors; etc." App. 39a.

---

[3] United States Courts, *Bankruptcy Filings Continue to Fall Sharply*, https://tinyurl.com/bd97wfne.

[4] Pamela Foohey, *Portraits of Filers*, at 15.

[5] *In re Rabinowitz*, 508 B.R. 874, 879 (Bankr. S.D.N.Y. 2014); *Yankowitz Law Firm v. Tashlitsky*, 492 B.R. 640 (Bankr. E.D.N.Y. 2013).

Nor did Mrs. Bartenwerfer have knowledge of her husband's fraud. The Bankruptcy Appellate Panel stated the parties "no longer seriously dispute that Mrs. Bartenwerfer had no actual knowledge of Mr. Bartenwerfer's fraud." App. 16a and 47a.

The decision by the Ninth Circuit is not supported by the text of the controlling statutory provision. Section 523(a)(2)(A) provides that a discharge can be denied based on "actual fraud." The phrase "actual fraud" was first introduced in the 1978 Bankruptcy Code and was based on the well-established meaning of the term "fraud," which required culpable misconduct and scienter by the debtor. *See, e.g.*, *Neal v. Clark*, 95 U.S. 704 (1877). Prior versions of American bankruptcy law on which § 523(a)(2)(A) is based excepted from discharge acts "of a bankrupt" that is, "by the debtor" and not by another.[6] It is undisputed that no such showing by Mrs. Bartenwerfer was made here. These textual underpinnings are plain and leave no fair doubt that vicarious liability was not seen by Congress as a basis to deny a discharge.

Not only is the text of the Code decidedly inconsistent with the notion of vicarious liability as a grounds to deny discharge, but so too are the longstanding and critical theories that are at the heart of bankruptcy law. Bankruptcy law for individuals is based on the principle that the "honest debtor" is

---

[6] For example, the Bankruptcy Act of 1898 excepted from discharge debts of "a bankrupt" which were "created by *his fraud*." 30 Stat. 544, 550. (emphasis added).

entitled to a discharge. The principle has its roots not just in the humanitarian objectives, but in the long-recognized conclusion by this Court that society at large benefits from the discharge of debt for those who are overburdened. This Court has recognized that the discharge is not only a matter of "personal liberty" but also a matter of "great public concern" because it restores the financially distressed debtor to being a productive member of society. *Local Loan Co. v. Hunt*, 292 U.S. 234, 245 (1934). The decision by the Ninth Circuit, however, now denies an honest debtor a discharge on the basis that the debtor's spouse engaged in wrongdoing and on the sole basis that husband and wife were "deemed" to be partners.

Respondent essentially asks this Court to disregard the central thrust of *Local Loan*. One of Respondent's core arguments is that the exceptions to discharge embodied in § 523 were meant to serve primarily as compensation to a creditor for wrongdoing—as opposed to ensuring that the honest debtor is discharged from debt. *See* Cert. Opp. 14. Respondent makes light of the debtor's economic plight: "Protecting fraud victims over fraudsters' head-in-the sand partners also makes good sense." Cert. Opp. 13. Thus, Respondent argues that the key issue here is "not the debtor's entitlement to a discharge, but rather the creditors entitlement to have its claim carved out of the discharge." Cert. Opp. 14.

This theory, however, is entirely contrary to the conclusion reached by a leading scholar of bankruptcy history, Charles Jordan Tabb, who in his survey of the development of the discharge in the United States concluded that, "a strong pro-debtor policy has been a linchpin of the national bankruptcy laws for more than ninety years." Charles J. Tabb, *The Historical Evolution of the Bankruptcy Discharge*, 65 Am. Bankr. L.J. 325 (1991).

Respondent is thus urging nothing less than a sea-change on the law of discharge and wants this Court to eliminate the protection of the honest debtor, and instead to interpret § 523's primary goal as being protection of a creditor from fraud. He reads *Grogan v. Garner*, 498 U.S. 279 (1991) as diluting the importance of *Local Loan* and the one-hundred-plus years of jurisprudence on its importance. *Id.*

The principal case upon which the Ninth Circuit relied was *Strang v. Bradner*, 114 U.S. 555 (1885). The decision in *Strang* has been widely criticized, ignored by some courts, and apologetically but reluctantly used by other courts; causing a leading commentator to urge its outright reversal.[7] *Strang* has since been superseded by key Congressional changes to § 523(a)(2)(A) and the case law from this Court emphasizing that the relevant exceptions to discharge in § 523 require culpable conduct by the debtor herself.[8]

---

[7] *See* Steven H. Resnicoff, *Is it Morally Wrong to Depend on the Honesty of your Partner or Spouse—Bankruptcy Dischargeability of Vicarious Debt*? 42 Case W. Rsrv. L. Rev. 147, 154, n. 17 and 155, n. 20 (1992).

[8] Some exceptions to discharge, such as those for domestic support or taxes, are excepted from discharge even if the debtor lacked the ability to make the payments.

The only other case upon which the Ninth Circuit relied was *Impulsora Del Territorio Sur v. Cecchini (In re Cecchini)*, 780 F.2d 1440, 1443 (9th Cir. 1986. This case has been vigorously challenged and frequently disregarded. *See* Resnicoff, *Vicarious Debt*, 155, n. 20. Justice Kennedy, then writing for the Ninth Circuit, expressed serious doubt about *Cecchini*, stating that "absent some culpability" a debt under § 523(a)(2) could be dischargeable. *See In re Lansford*, 822 F.2d 902, 904 (9th Cir. 1987).

The potential harm from the decision by the Ninth Circuit is substantial. Of particular concern in the context of this case is the unwarranted loss of the discharge in the case of transactions by married persons. The Ninth Circuit's decision could transmute virtually all spousal transactions into partnerships, when, like here, there is nothing remotely resembling a true commercial enterprise.[9] Even the law review article Respondent relies upon acknowledges that applying vicarious liability to establish fraud has no rightful place when applied in the spousal relationship.[10]

---

9. The Petitioner has accepted for purposes of this appeal that the Bartenwerfers were "deemed partners" in the remodeling and sale of their home and is not asking that this Court revisit the factual determination of partnership.

10. "To the extent that *Strang* is read as authority for imputing the fraud of one marital partner to the other, I would agree with Professor Resnicoff's dubious assessment of the continuing viability of the case and join in his criticism of Strang as exacerbating gender discrimination." Lawrence Ponoroff, *Vicarious Thrills: The Case for Application of Agency Rules in Bankruptcy Dischargeability Litigation*, 76 Tul. L. Rev. 2515, 2536 (1996).

Nor is there any perceived need for the shift in emphasis on discharge exceptions urged by Respondent. This Court itself has noted that Congress has even modified the exceptions because it was shown that it was creditors who were abusing the discharge law, and not debtors. *See, e.g.*, *Field v. Mans*, 516 U.S. at 76-77, describing the conduct of finance companies that were encouraging fraud to insulate themselves from discharge. *See also Midland Funding, LLC v. Johnson*, 137 S. Ct. 1407, 1418 (2017), where Justice Sotomayor noted in her dissent the "common practice" among debt collectors who had "deluge[d]" the bankruptcy courts with claims "on debts deemed unenforceable under state statutes of limitations."

We urge this Court to confirm that the text and context of § 523(a)(2)(A) preserve the core principles that protect honest debtors who should not be denied a discharge where they have not engaged in fraud or other wrongdoing, and neither knew or should have known of a fraud perpetrated by a "partner."

SUMMARY OF ARGUMENT

The decision of the Ninth Circuit should be reversed for the reasons set forth in Petitioner's brief, and for the following as well.

The decision by the Ninth Circuit is inconsistent with the jurisprudence of this Court from *Neal v. Clark*, 95 U.S. 704 (1877) through *Husky Int'l Elecs., Inc. v. Ritz*, 136 S. Ct. 1581 (2016). This Court's decisions reflect a consistent requirement that in order to justify denial of a discharge there must be misconduct *by the debtor* which is tantamount to unscrupulous conduct, or which involves moral turpitude or intentional wrong and "not implied fraud or fraud in law." *Neal*, 95 U.S. at 709. As the law review article cited by Respondent notes, vicarious liability falls within the notion of implied fraud or fraud in law.[11]

The decision by the Ninth Circuit is inconsistent with the statutory language of § 523(a)(2) and the surrounding provisions, as well as prior bankruptcy law upon which § 523 is based. The Bankruptcy Acts of 1898 and 1867 both stated that a debt could be excepted from discharge based on the culpable conduct *by the bankrupt* (that is, by the debtor under modern terminology).[12] This principle was carried forward when Congress enacted the 1978 Code. Congress expressly stated that § 523(a)(2)(A) was intended to codify *Neal v. Clark* and gave no indication that it was intending to depart from historical origins by inserting a new theory of vicarious liability. The text of the 1978 Code inserted the phrase "actual fraud" to signify that loss of the discharge required misconduct by the debtor, and not implied fraud. The surrounding

---

[11] Ralph Brubaker, *The Dischargeability of "Control Persons" Liability for Federal Securities Fraud: Actual Fraud, Vicarious Nondischargeability, and the Vacillating Objects of the § 523(a)(2)(A) Discharge Exception*," Bankruptcy Law Letter No. 5, 9 (May 2002).

[12] *See* Act of Mar. 2, 1867, ch. 176, 14 Stat. 517 (the ("1867 Act"), repealed by Act of June 7, 1878, ch. 160, 20 Stat. 99; Act of July 1, 1898, ch. 541, 30 Stat. 544 (the "1898 Act").

provisions in § 523 likewise required a showing of misconduct by the debtor and gave no basis to conclude that Congress had intended to deny a discharge based on vicarious fraud.

The decision by the Ninth Circuit that denial of a discharge for an honest debtor can be based upon theories of vicarious liability is directly counter to the Court's long-standing view that the discharge is central to the functioning of the American bankruptcy system and not only addresses a private need of the debtor but is a public necessity. *Local Loan*. Respondent seeks a sea-change in these foundational concepts. It relies on a misreading of *Grogan v. Garner*, 498 U.S. 279 (1991) which he sees as undoing the central thrust and meaning of *Local Loan.* But as Professor Tabb pointed out, the bankruptcy discharge remains the "linchpin" of modern bankruptcy law. Tabb*, Bankruptcy Discharge*, at 370. Respondent's view is entirely out of keeping with this Court's jurisprudence and the text and legislative history of § 523.

LEGAL ARGUMENT

I. The decision by the Ninth Circuit is inconsistent with the jurisprudence of this Court from *Neal v. Clark*, 95 U.S. 704 (1877) through *Husky Int'l Elecs., Inc. v. Ritz*, 136 S. Ct. 1581 (2016).

For over 145 years, the Court has consistently held that the statutory exceptions to when an individual may be denied a discharge required a showing of intentional wrongdoing and culpability. *See, e.g.*, *Neal v. Clark*, 95 U.S. 704 (1877); *Field v. Mans*, 516 U.S. 59 (1965); *Kawaauhau v. Geiger*, 523 U.S. 57 (1998); *Bullock v. Bankchampaign*, *N.A.*, 569 U.S. 267 (2013); *Husky Int'l Elecs., Inc. v. Ritz*, 136 S. Ct. 1581 (2016).

In *Neal v. Clark* the question of what is "fraud" for purposes of the denial of a bankruptcy discharge was squarely before the Court. William Fitzgerald left a will in which he directed his executor to sell his estate and distribute the proceeds. Certain bonds were sold by the estate to Griffith Neal. It was argued that the sale of the bonds to Neal was wrongful (a "devastavit" of the estate—that is mismanagement of the estate). Neal filed for bankruptcy and an objection to his discharge was based on the sale of the notes.

The Supreme Court of Appeals of Virginia ruled that while Neal had not engaged in any "actual fraud" he had committed "constructive fraud" which thus implicated him in the mismanagement of the estate and was a basis to deny his discharge.

The Court reversed, holding that Neal should not be denied his discharge based on implied or constructive fraud. Justice Harlan wrote the opinion, stating that the case "involves the meaning of the word 'fraud' as used in the thirty-third section of the bankrupt law of 1867 [14 Stat. 517]." 95 U.S. at 706. Section 33 provided that "no debt created by the fraud or embezzlement *of the bankrupt*, or by defalcation as a public officer, or while acting in a fiduciary capacity, shall be discharged under this act." *Id*. (emphasis added).

The Court noted that the term "fraud" was used in the same section with debts created by embezzlement. From this the Court concluded that the term "fraud" means "positive fraud" and not fraud implied in law. This association of the two words justified "if not imperatively require, the conclusion that the 'fraud' referred to in that section means positive fraud, or fraud in fact, involving moral turpitude or intentional wrong, as does embezzlement; and not implied fraud, or fraud in law, which may exist without the imputation of bad faith or immorality." 95 U.S. at 709.

Implied fraud and vicarious fraud are one and the same. Professor Brubaker has noted that "a debtor's vicarious liability for the fraud of another could also be characterized as "implied" or "constructive" fraud, as the legal fiction of vicarious liability attributes the conduct of one person to another such that the debtor is treated as if he/she had perpetrated the fraud for purposes of the debtor's liability therefor."[13]

The Court in *Neal* also held that its ruling was consistent with the over-arching purposes of bankruptcy law, thus grounding the discharge in principles relating to rehabilitation of the debtor and not, as Respondent now urges, compensating creditors for wrongdoing. "Such a construction of the statute is consonant with equity, and consistent with the object and intention of Congress in enacting a general law by which the honest citizen may be relieved from the burden of hopeless insolvency." 95 U.S. at 709. "A different construction would be inconsistent with the liberal spirit which pervades the entire bankrupt system." *Id.*[14]

In *Field v. Mans*, 516 U.S. 59 (1995) the question presented was the level of a creditor's reliance on a fraudulent misrepresentation necessary to justify denial of a discharge under § 523(a)(2)(A). The Court reviewed the legislative history of this section and the changes over time in its wording. Section 523(a)(2)(A) does not mention reliance, while § 523(a)(2)(B) does. The Court refused to apply the principle of a "negative

---

[13] Brubaker, *"Control Persons,"* at 9. Professor Brubaker, however, is more closely aligned with the notion that § 523 may embrace vicarious liability.

[14] *Neal* also implicitly rejects the view advanced by Respondent that the purpose of the discharge exception found in § 523(a)(2)(A) is compensatory (based on creditor protection) as opposed to "punitive" (designed to provide relief for the honest, but not the dishonest debtor); see discussion below. *See* Brubaker, "*Control Persons*," at 8.

pregnant" and found that justifiable reliance was required for reasons that pertain here: "If the negative pregnant is the reason that § 523(a)(2) (A) has no reasonable requirement, then the same reasoning will . . . eliminate scienter from the very notion of fraud." *Field*, at 67-68. The Court held that reading § 523(a)(2) without a requirement of "intentionally" would cause "common sense [to] balk." *Field*, at 68.

The Court was firm that intent (and hence scienter) is required to make fraud grounds for an exception to discharge. "If Congress really had wished to bar discharge to a debtor who made unintentional and wholly immaterial misrepresentations having no effect on a creditor's decision, it could have provided that. It would, however, take a very clear provision to convince anyone of anything so odd, and nothing so odd has ever been apparent to the courts that have previously construed this statute, routinely requiring intent, reliance and materiality before applying § 523(a)(2)(A)." *Field*, at 68.

In short, while the decision in *Field* began with a search for the level of reliance required, the Court embraced the related notion of scienter (intent) and in several statements made it abundantly clear that to strip out intent would both defy common sense and would be "odd." *Field* is fairly read as being focused on the debtor's state of mind, and not merely on the nature of the debt when considering dischargeability.

The Court's decision in *Kawaauhau v. Geiger*, 523 U.S. 57 (1998) followed. The Court held that only acts with intent to cause injury are sufficient for non-dischargeability under § 523(a)(6) and that "reckless" and "negligent" acts are not. *See In re Shart*, 505 B.R. 13 (Bankr. C.D. Cal. 2014). "This echoes the Supreme Court holdings that intent and fault are essential factors for non-dischargeability (at least for § 523(a)(2)(4) and (6)."

In *Bullock v. Bankchampaign, N.A.*, 569 U.S. 267 (2013) the Court addressed the issue of whether the term "defalcation" when used in § 523(a)(4) includes a culpable state of mind requirement akin to that which accompanies application of the other terms in the same statutory phrase." *Id* at 269. "We describe the state of mind as one involving knowledge of, or gross recklessness in respect to, the improper nature of the relevant fiduciary behavior." *Id*. at 269. That is, defalcation requires scienter—knowledge of the wrongdoing.

The Court stated that embezzlement requires a wrongful intent and that "fraud" must be read to require an equivalent showing. 569 U.S. 275. This was the rule from *Neal* which "has been the law for more than a century." *Id*. at 275. Here the Court suggested that the terms "defalcation," "fraud" and "embezzlement" should be read in a similar fashion (569 U.S. at 277) and that this similarity included a "scienter standard." Again, the focus was on the debtor's state of mind, and not on the nature of the debt.

In 2016, this Court in *Husky Int'l Elecs., Inc. v. Ritz*, 136 S. Ct. 1581, 1586, restated that the notion of fraud under § 523(a)(2) requires moral turpitude or an intentional wrong, citing *Neal v. Clark*. The court added that "anything that counts as fraud and is done with wrongful intent is "actual fraud."" *Id.*

This judicial history refutes the core notions advanced by Respondent. As one court noted, "[t]he *Geiger* and *Bullock* decisions appear to cut strongly against applying imputed fraud under § 523(a)(2)(A) to except a debt from discharge in the absence of a showing of culpability on the part of the debtor." *Sachan v. Huh (In re Huh)*, 506 B.R. 257, 267 (B.A.P. 9th Cir. 2014). "In light of the Supreme Court's recent rulings in *Grogan, Geiger*, and especially *Bullock*, I am certain that given the opportunity today, the Supreme Court would not impute fraud to preclude dischargeability to an otherwise innocent partner who had no culpability other than being a partner." *Haig v. Shart* (*In re Shart)*, 505 B.R. 13 (Bankr. C.D. Cal. 2014).

II. The decision by the Ninth Circuit is inconsistent with the statutory language of § 523(a)(2)(A) and the surrounding provisions, as well as prior bankruptcy law upon which § 523 is based.

A. Section 523(a)(2)(A) codified *Neal v. Clark* and its plain meaning excepts from discharge only debts obtained by "actual fraud" which requires a showing of misconduct or moral turpitude by the debtor.

Neal v. Clark was codified in the 1978 Bankruptcy Code, embedding the requirement for actual fraud in the Code. This codification was preceded by earlier iterations of American bankruptcy law reflecting the principle that denial of the discharge must be based on the debtor's misconduct, and on actual intent, not on theories of imputed or vicarious liability.[15] Further, from the time of the enactment of 1898 Bankruptcy Act, through the enactment of the 1978 Code, one of Congress's principal concerns has been protection of the discharge for individual debtors, and much less so as a means of compensating creditors for wrongdoing, as Respondent now argues.

Both *Strang* and *Neal* were decided when the Bankruptcy Act of 1867 was in effect. Act of Mar. 2, 1987, ch. 176, 14 Stat. 517. In *Neal v. Clark* the Court relied upon section thirty-three of that Act which

[15] The statutory evolution of § 523(a)(2)(A) and § 523(a)(2)(B) is partially described in *Field v. Mans*, 516 U.S. at 65-66.

provided that "no debt created by the fraud or embezzlement *of the bankrupt* or by his defalcation as a public officer or while acting in any fiduciary character, shall be discharged" (emphasis added). 14 Stat. 33. *See* 96 U.S. at 706. *Neal* was thus true to the statutory text. *Strang* noted this language, but then failed to see the textual requirement that the fraud be "of the bankrupt." *See Strang*, 114 U.S. at 556.[16] As noted below, *Strang* has been superseded by the changes in the Code.

Following the repeal of the 1867 Act, Congress enacted the Bankruptcy Act of 1898.[17] Section 17(a)(2) was the "precursor" to current § 523. *Field v. Mans*, 516 U.S. at 64-65. Section 17(a) stated that a discharge shall release a "bankrupt" [e.g., the debtor] from all of his provable debts" other than those listed in the sections that followed. Section 17(a)(2) made nondischargeable debts that were "judgment in actions for frauds, or obtaining property by false pretenses or false representations, or for willful and malicious injuries to

---

[16] Section 29 of the 1867 Act provided for loss of the discharge in general (as opposed to a specific debt) and focused primarily on misconduct that related either to the filing of the case, the making of fraudulent transfers, failing to keep adequate records and making preferential transfers. Section 29 more closely tracks 11 U.S.C. § 727.

[17] Bankruptcy Act of 1898, ch. 541, 30 Stat. 544 (1898) (repealed 1978). "The Bankruptcy Act of 1898 marked the beginning of the era of permanent federal bankruptcy legislation. The 1898 Act remained in effect for eighty years until being replaced by the Bankruptcy Reform Act of 1978." Charles J. Tabb, *The History of the Bankruptcy Law in the United States*, 3 Am. Bankr. Inst. L. Rev. 5, 23 (1985).

the person or property of another." Section 17(a)(4) made non dischargeable debts that "were created *by his fraud*, embezzlement, misappropriation, or defalcation while acting as an officer or in any fiduciary capacity." 30 Stat. 544, 550-51 (emphasis added). Again, the pertinent fraud was that of the bankrupt ("his fraud").

The 1898 Act occurred at a "watershed" moment in American history—the legal and political attitude toward bankruptcy shifted and unlike English law now "favored debtors' interests in many respects," including changes in the discharge provisions.[18] The legislative history to the 1898 Act gave full voice to the principle that the discharge served a social-economic goal of helping debtors to become economically productive. House Report of 1897, H.R. Rep. No. 65, 55th Cong., 2d Sess. 30-32 (1897). In addressing "who is a debtor" the House Report noted the public benefit from the discharge as well as for the "honest men" who seek a discharge:

> [T]his vast number [of debtors] constitute an army of men crippled financially—most of them active, aggressive, honest men who have met with misfortune in the struggle of life, and who if relieved from the burden of debt, would reenter the struggle with fresh hope and vigor and become active and useful members of society.

---

[18] David A. Skeel, *The Genius of the 1898 Act*, 15 Bankr. Devs. J. 321 (1998).

> [T]he passage of a bankrupt law . . . will lift these terrible and hopeless burdens, and restore to the business and commercial circle of the country, the active and aggressive elements that have met with misfortune and are now practically disabled for the battle of life.

Professor Tabb points out that the 1898 Act rejected the view now espoused by Respondent that the exceptions to the discharge were meant to provide compensation for creditors who were defrauded—but rather to ensure that only the honest debtors received a discharge. That is, the exceptions were viewed as "punitive" and not "compensatory." The 1898 Act rejected "the notion that the debtor's entitlement to a discharge rests solely on the impact on the interests of the immediately affected creditors." Tabb, *Bankruptcy Discharge*, at 364.

Thus, the 1898 Act made a significant change from the law in effect when *Strang* was decided. The 1898 Act recognized formally for the first time the overriding *public interest* in granting a discharge to the "honest but unfortunate debtors." Tabb, *Bankruptcy Discharge*, at 364. "The theory is that society as a whole benefits when an overburdened debtor is freed from the oppressive weight of accumulated debt . . . the debtor then is able to resume his or her place as a productive member of society." *Id*. at 364-65. At the same time the new bankruptcy act made clear that the exception to the discharge was to be based on intentional wrongdoing—nothing in the law suggested that a theory of vicarious liability could be grounds to deny a discharge.

The 1898 Act was amended in 1903 to include for the first time an exception to discharge based on obtaining property by a materially false statement in writing made for the purpose of obtaining credit. *Field*, 516 U.S. 65. The 1898 Act did not originally include "intent" with respect to written false statements. This was changed by a 1960 amendment which added the requirement that a debtor intend to deceive (as well as reliance). *Field*, at 66. Thus, scienter was expressly added to subsection 523(a)(2)(B). Act of July 12, 1960, Pub. L. 86-621, 74 Stat. 409.

In 1978 Congress adopted the current Bankruptcy Code. The legislative history to § 523(a)(2)(A) stated that it was intended to "codify current case law, e.g., *Neal v. Clark*, 95 U.S. 704 (1887) which interpreted 'fraud' to mean actual or positive fraud rather than fraud implied in law." 124 Cong. Rec. H. 11,095-96 (Sept. 28, 1978); S. 17,412-13 (Oct. 6, 1978); reprinted in 2020 Collier Pamphlet Edition, Bankruptcy Code, Part 1, 461. Nothing in the legislative history evidences any intent to deviate from the basic principle that the denial of a discharge was to be based on the debtor's misconduct.

There is no mention of *Strang* in the legislative history. "Congress had ample opportunity to codify *Strang*, just as they had done for *Neal*, but Congress made no attempt to do so." *In re Shart*, 505 B.R. 13, 17 (Bankr. C.D. Cal. 2014). "[T]here is nothing in the legislative history of 11 U.S.C. § 523(a)(6) to suggest that the nonbankruptcy vicarious liability rules was to be 'appended to the statutory exceptions to discharge in bankruptcy.'" *In re Austin*, 36 B.R. 306, 312 (Bankr. M.D. Tenn. 1984).

The codification of *Neal* reflected that Congress was rejecting the notion that implied fraud could be used as a basis for denial of a discharge. As Professor Brubaker points out, the term "implied fraud" embraces vicarious liability.[19] As another commentator correctly noted, "Congress therefore implicitly rejected the attribution of one party's wrongful conduct to a debtor when determining dischargeability under §523(a)(2)(A)." W. Brian Memory, *Vicarious Nondischargeability for Fraudulent Debts: Understanding the Dual Purposes of § 523(a)(2)(A)*, 20 Emory Bankr. Dev. J. 633, 666, n. 171 (2004).

B. The surrounding provisions in § 523 require that a discharge can be denied only for the fraud by the debtor and not by imputation.

The use of the phrase "actual fraud," first included in the 1978 Code, provides ample support for the view that § 523(a)(2)(A) requires that the denial of a discharge must rest upon the intentional misconduct of the debtor—and not a third party. Further, the surrounding and companion provisions in § 523 likewise

[19] Brubaker, *Control Persons* at 9.

confirm that Congress did not intend to deny a discharge based on vicarious liability.

Professor Resnicoff argues that "the best case against *Strang* begins with the plain language of the exceptions to discharge under sections 523(a)(2)(B), 523(a)(6), and 523(a)(9)." Resnicoff, *Vicarious Debt*, at 196. This is because these sections expressly state that the wrongful acts must be those of the debtor and "there is no policy basis for denying discharge for an innocent debtor's vicariously acquired debt under section 523(a)(2)(A) while allowing discharge for similar debts governed by related sections." *Id*. at 196.

Looking to the companion provisions is consistent with the Court's long-standing views on statutory interpretation. "[T]he meaning of a statute is to be looked for, not in any single section, but in all the parts together and in their relation to the end in view." *Panama Ref. Co. v. Ryan*, 293 U.S. 388, 439 (1935) (Cardozo, J., dissenting). "[I]t is the most natural and genuine exposition of a statute to construe one part of the statute by another part of the same statute, for that best expresseth the meaning of the makers." Antonin Scalia and Bryan A. Garner, *Reading Law: The Interpretation of Legal Texts*, Thomson/West (2012), 167.

The Respondent acknowledges that the requirement that the fraud be "by the debtor" appears in §§ 523(a)(2)(B)(iv), 523(a)(6) and 523(a)(12). Cert. Opp. at 10. And it agrees that in those cases, the "debtor's intent matters." (*Id*.). Debtor's intent "matters" because it is the debtor's intent that governs whether the debtor is discharged, and not the nature of the debt.

Numerous courts agree that the exceptions to discharge in § 523 require that the fraud be "by the debtor" even though § 523(a)(2)(A) does not contain that exact phrase. For example, in *Ghomeshi v. Sabban (In re Sabban)*, 600 F.3d 1219, 1222 (9th Cir. 2010) the court stated that, "[M]aking out a claim of non-dischargeability under § 523(a)(2)(A) requires the creditor to demonstrate [that] *the debtor* made . . . representations." In *Sherman v. SEC*, 658 F.3d 1009, 1014 (9th Cir. 2011), the court stated that "even though the text of the statute does not state that the fraudulent conduct must have been the debtor's, we have nonetheless incorporated that assumption into our understanding of the provision. . . . In fact, we have recently suggested that the debtor's involvement in the fraudulent activity might be the *only* relevant consideration in determining whether the exception applies." *Id*. at 1014.

However, Respondent asks this Court to disregard the surrounding provisions and instead relies on the "negative pregnant" rule to argue that because the phrase "by the debtor" appears in one part of § 523, but not in another, that Congress did not mean that the act of fraud in § 523(a)(2)(A) had to be an act "by the debtor."

This Court has rejected the "negative pregnant" argument in a nearly identical context as present here. In construing § 523(a)(2), the Court noted that the section did not contain the word "reliance" or "intent." That it appears in one section but not a nearby section is not, as Justice Souter found in *Field* a sufficient basis to invoke the "negative pregnant" rule. "If the negative pregnant is the reason that § 523(a)(2)(A) has no reasonable requirement, then the same reasoning will . . . eliminate scienter from the very notion of fraud." *Field*, 67-68.

What would be "odd" (as the Court said) would be to require that the discharge only be denied under (a)(6) if the misconduct was "by the debtor" but that an entirely different rule would pertain under (a)(2). Both are directed at nearly identical misconduct; both are generally construed as having the same purpose and goal. The omission of "by the debtor" is just as likely to result from the lack of any need to say what was apparent—that a denial of discharge is measured by the debtor's misconduct and not the misconduct of another party. This Court in *Grogan* found that § 523 should be read as a whole, stating for example that the same standard of proof should govern all of the subsections of § 523, and that "no particular exception is subject to a special standard of proof." *Grogan*, 498 U.S. 287.

III. The Ninth Circuit's decision is inconsistent with the principles of *Local Loan*. *Grogan v. Garner* did not signify diminution in protection of the discharge for the honest debtor.

A. The granting of a discharge to the honest debtor is one of the foundational goals of bankruptcy law: discharge is both a private need and public necessity.

At the core of the Respondent's argument is that the statutory exceptions to discharge are primarily a creditor protection, and that the protection of the discharge for the honest debtor is secondary. By this argument, Respondent means that the exceptions were intended not to punish the dishonest debtor (or to provide a benefit to the honest debtor) but instead to ensure payment to a creditor injured by fraud. Respondent urges a stepping back from *Local Loan* and its progeny. This argument reflects a misunderstanding of what Professor Tabb has correctly labelled the "linchpin" of American Bankruptcy. Tabb, *Bankruptcy Discharge*, at 370.

The discharge provisions are the heart and soul of the bankruptcy process for individual debtors. Over two hundred years ago, Sir William Blackstone wrote that the bankruptcy discharge serves both a private and a public benefit: through the bankruptcy discharge "the bankrupt becomes a clear man again; and by the assistance of his allowance and his own industry, may become a useful member of the commonwealth." 2 WILLIAM BLACKSTONE, COMMENTARIES, *484.

The 1978 Bankruptcy Code carries forward this concept of the central importance of the discharge. "[T]he introduction of the discharge [into modern bankruptcy law] could well be considered the single most important event in bankruptcy history." Charles J. Tabb, BANKRUPTCY ANTHOLOGY, 524 (2002). Other commentators have observed that the bankruptcy discharge "ranks ahead in importance of all others in Anglo-American bankruptcy history." John C. McCoid, II, *Discharge: The Most Important Development in Bankruptcy Discharge*, 70 Am. Bankr. L.J. 163, 164 (1996).

This Court has held much the same, recognizing that the discharge serves both a matter of great public concern and is a private financial necessity. *Local Loan*, 292 U.S. at 245:

> The power of the individual to earn a living for himself and those dependent upon him is in the nature of a personal liberty quite as much if not more than it is a property right. To preserve its free exercise is of the utmost importance, not only because it is a fundamental private necessity, but because it is a matter of great public concern. . . . The new opportunity in life and the clear field for future effort, which it is the purpose of the Bankruptcy Act to afford the emancipated debtor, would be of little value to the wage-earner if he were obliged to face the necessity

> of devoting the whole or a considerable portion of his earnings for an indefinite time in the future to the payment of indebtedness incurred prior to his bankruptcy.

Local Loan recognized that future productivity was the basis for the economic value of the discharge to both debtor and society—and made no reference to the so-called "compensatory" value which Respondent urges. *Local Loan* has been a centerpiece of bankruptcy jurisprudence; decided over 80 years ago, its meaning and stature has increased as the notion of the discharge has become more deeply embedded and understood as a vital goal of bankruptcy law.

Given the above, debts are considered presumptively dischargeable. "American bankruptcy law promotes its principal policy of allowing individuals to escape the financial and emotional burden of past debt by discharging prior economic liabilities. For over a hundred years courts have agreed that debts are presumptively dischargeable and that statutory exceptions to discharge must be narrowly construed in order to afford comprehensive relief to honest debtors." Resnicoff, *Vicarious Debt*, at 149-50.

Respondent now urges a regressive and wholesale shift in bankruptcy principles, asserting in essence that the discharge exceptions are to be read broadly (and not narrowly, as required) and that the primary concern should be to protect creditors from wrongdoing, even if the debtor herself is innocent of any wrongful conduct. Thus, it argues that the key issue here is "not the debtor's entitlement to a discharge, but rather the creditors entitlement to have its claim carved out of the discharge." Cert. Opp. 14. Further, it argues that "in choosing between the victims and the fraudster's partners who pocketed the victim's money, it is perfectly reasonable—and indeed the 'more reflective policy judgment'—for congress to favor the former." *Id*. (citing Ponoroff, at 2652).

But Congress has not adopted this purportedly "more reflective policy" but has held firm to the belief that both the public economic good and the private benefit to the debtor outweigh compensating the creditor for its loss. This Court in *Neal v. Clark* held, and has continued to hold, that denial of the discharge requires unscrupulous conduct and intentional wrongdoing by the debtor. The discharge exceptions carve out the dishonest debtor; they are not, however, designed to compensate the defrauded creditor when the debtor is innocent of all wrongdoing. Mrs. Bartenwerfer was found innocent of all such conduct and was entitled to a discharge of the Respondent's claim.

B. *Strang* failed to consider the key issue of dischargeability under federal bankruptcy as opposed to liability under state partnership law.

Professor Stephen Resnicoff, whose work on this subject is described in the law review article cited by Respondent as the "leading academic treatment on the subject,"[20] has concluded that *Strang* (1) is at odds with *Local Loan* and the jurisprudence of the Court on the importance of the discharge; (b) is based on outdated notions of partnership and agency law and is ill-suited to address the reality of marital relationships today and (c) finds no support in the plain language of the surrounding provisions in §§ 523(a)(2)(B), 523(a)(6) and 523(a)(9).[21]

That *Strang* is inconsistent with the plain language of § 523 and *Local Loan* is discussed above. *Strang* was also decided more than a decade before the enactment of the Bankruptcy Act of 1898 which reflected substantial political and legislative changes concerning both the discharge and involuntary bankruptcy law.[22] The insertion of "actual fraud" into § 523 and the insistence on intent and scienter should lay to rest the notion of vicarious liability.

Strang was essentially a decision that looked to then existing partnership law to determine the issue of "liability" but did not truly analyze the question of whether such liability was dischargeable under bankruptcy law. The two questions are distinct.

In addition, *Strang* is also outdated and out of step with modern notions of partnership and agency law. *Strang* involved a commercial partnership which had been in the business of purchasing wool for several

---

[20] Ponoroff, *Vicarious Thrills*, at 2534-35.

[21] Resnicoff, *Vicarious Debt*, at 196.

[22] *See generally*, Skeel, *The Genius of the 1898 Bankruptcy Act.*

years. 114 U.S. 555, 558. One partner, Strang, made fraudulent misrepresentations to a buyer in connection with a sale, and was denied a discharge on the basis of actual fraud. Two other partners were found to have had no knowledge of the fraud. 114 U.S. at 561. Yet, the Court found that the partners could not escape liability "upon the ground that such misrepresentation were made without their knowledge." 114 U.S. at 561. *Strang* looked to the law of a general partnership, although in today's world, this form has greatly receded from the marketplace—those who are actually engaged in business would almost certainly not elect to do business as a general partnership given the readily available forms of entity business that avoid vicarious liability.

Unlike *Strang* this case does not involve a commercial partnership, but rather treats spouses who engage in a one-time sale of a home as subject to the rules of common law general partnership. Such a rule thus puts at a legal disadvantage the consumer debtor and his or her spouse from the modern outcome in partnership law. Members of a limited partnership or limited liability company can insulate themselves from imputed liability and vicarious liability. While partnership assets can be reached for a tort, individual assets cannot. The general business expectation today is that owners who have not personally guaranteed a firm's debt are immunized from vicarious liability through the widespread use of limited liability companies. Ponoroff, at 2544. Thus, ironically, only those like the Bartenwerfers, who are not truly engaged in a commercial enterprise, and who do not have the formalities of a partnership filing, are exposed to the vicarious liability problem.

While the vicarious liability outcome is improper in general, it is particularly inappropriate when it is applied in the context of a marital relationship. Professor Resnicoff writes that *Strang's* use of vicarious liability to deny a discharge is "pernicious" in the context of a marital relationship.[23] "The pernicious effects of *Strang* are especially evident when the rule is applied in social contexts, such as between spouses, rather than in commercial ones. Social 'partners' are less able to dissolve their 'partnership' or protect themselves against wrongful 'agents.' *Strang* . . . punishes those debtors for wrongs they did not commit. Thus, application of *Strang* condemns those innocent debtors to permanent, or at least indefinite, pauperism. Furthermore, to the extent that financial transactions within a marriage are predominantly controlled by one gender rather than shares, *Strang* exacerbates gender discrimination." Resnicoff, *Vicarious Debt*, at 156.

Even those who support *Strang* in some sense recognize that it should not be applied in the context of a marital relationship, noting it exacerbates gender discrimination.[24] "The reasoning that supports the rule

---

[23] Ponoroff acknowledges that "it is axiomatic that the marital relationship does not alone give rise to either a legal partnership or an agency." Ponoroff. *Vicarious Thrills*, at 2552.

[24] "To the extent that *Strang* is read as authority for imputing the fraud of one marital partner to the other, I would agree with Professor Resnicoff's dubious assessment of the continuing

in Strang does not, however, dictate that we also yield to the expanded proposition for which Strang is sometimes cited as authority, namely, that the fraud of one spouse can be imputed to the other for purposes of determining the dischargeability of a joint debt in the innocent spouse's bankruptcy case. The justification for drawing a distinction between the two kinds of cases is clear." Ponoroff, at 2551.

Ponoroff concludes that the rule of vicarious liability should not be applied in the case of the "morally innocent spouse's bankruptcy case" because the underlying case for vicarious liability is "frail at best." Ponoroff, at 2554. This frailty arises in large measure because husband and wife typically do not have the organizational and legal framework that protects the typical business organization; spouses do not typically arrange their life with regard to formal documentation and legal structures. . . . "In the case of spouse by contrast, the essence of the relationship is personal. Furthermore, even under contemporary societal norms, there are few alternative arrangements available as a practical matter, and in any event, creditors of the 1990s have no business assuming that spouses are obliged by law to come to one another's financial rescue."

Even though the Petitioner has not asked this Court to address the finding that the Bartenwerfers

viability of the case and join in his criticism of Strang as exacerbating gender discrimination." Ponoroff, *Vicarious Thrills*, at 2536.

were deemed partners, the spill-over effect is inevitable, and the Ninth Circuit decision will almost certainly cause creditors to seek to deny a discharge to innocent spouses based on whatever tenuous theory of partnership law may present itself.

CONCLUSION

According, we respectfully request that this Court reverse the ruling of the Ninth Circuit and enter judgment in favor of Ms. Bartenwerfer.

Dated: July 2022

Respectfully submitted,

DAVID R. KUNEY
9200 Cambridge Manor Court
Potomac, Maryland 20854
301-299-4336
Davidkuney@dkuney.com

Attorney for Amici Curiae