

# Debts for a Partner's Fraud Are Confirmed to be a Nondischargeable Debt According to the Supreme Court's Opinion

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In a unanimous opinion by the Supreme Court, the Court held an innocent partner liable for the fraud of another partner. Should the innocent party declare bankruptcy, the bankruptcy code would bar a discharge of the debt because it was obtained by false pretenses, a false representation or actual fraud.

In Bartenwerfer v. Buckley, prior to their marriage, a couple entered into a partnership to remodel and sell a home. Although the wife was largely uninvolved, there were multiple defects in which the husband failed to disclose to the buyer. The buyer sued in state court and won. The couple was held jointly responsible for damages in excess of \$200,000.00. The couple filed for Chapter 7 Bankruptcy shortly thereafter. The buyer filed an adversary complaint in the bankruptcy court, alleging that the state court judgment constituted a nondischargeable debt. Under the Bankruptcy Code, fraud is an exception to discharge. Pursuant to 11 U.S.C. § 523(a)(2)(A), a discharge under this title does not discharge an individual debtor from any debt "for money... to the extent obtained by false pretenses, a false representation, or actual fraud."

Even though the husband was the person who committed the fraud, his wife was also found liable since the two operated in a legal partnership to renovate and sell the house. The Bankruptcy Appellate Panel disagreed with that determination, stating that the wife should only be held culpable if she knew or had reason to know of her husband's fraud. On remand, the Bankruptcy Court determined that she lacked such knowledge. Both the Bankruptcy Court and the Appellate Panel affirmed the discharge of her debt to the buyer. However, the Ninth Circuit reversed the decision, holding that a debtor is liable for her partner's fraud, regardless of her own culpability. See *Strang v. Bradner*, 114 U.S. 555 (1885).

Here, the Supreme Court looked at the plain language of the statute and noted the passive voice of § 523(a)(2)(A) does not specify an actor. In addition, "when Congress included particular language in one section... but omits it in another section of the same Act, the choice is deliberate." The Court agrees with the common law fraud approach, where fraud liability is not limited to the wrongdoer.

When an agency or partnership relationship is created, the innocent party is also vicariously liable for the fraud of one partner. § 523(a)(2)(A) “takes the debt as it finds it,” therefore, this section is more concerned with how the money was obtained, rather than who committed the fraud to obtain it. As it stands, Congress must balance multiple, competing interests, and innocent people are sometimes held liable for the fraud of their partners.

Members of a partnership should be careful who they enter into a partnership agreement with because they could be held non-dischargeable of their partner’s fraudulent acts even if they did not have knowledge or involvement in the fraud.

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