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Nebraska Bankruptcy Court Holds Chapter 7 Debtors Not Individually Liable for Damages from Their Alleged Fraud in Conduct of Their Non-Debtor Business

EIGHTH CIRCUIT BANKRUPTCY MONITOR

In *Lund-Ross Constructors, Inc. v. Buchanan (In re Buchanan)*, the Bankruptcy Court for the District of Nebraska (Judge Saladino) denied an objection to discharge on the basis that tort claims against a non-debtor business were not enforceable against the husband-and-wife chapter 7 debtors who owned the business. The opinion warrants careful consideration by counsel representing property owners and general contractors in Nebraska, because it suggests Nebraska law limits the liability of corporate principals, even when they participate actively in allegedly actionable misrepresentations.

The debtors owned and operated an electrical business called Signature Electric. Signature served as a subcontractor to the plaintiff, Lund-Ross Contractors, on several projects. As is typical, Signature would provide Lund-Ross with periodic pay applications, which included signed lien waivers representing that all amounts owed to suppliers and sub-subcontractors had been paid in full. According to Lund-Ross, it turned out at least some of those representations were false. In July 2019, Electric told Lund-Ross that it would be discontinuing operations. Afterwards, a number of unpaid suppliers began filing liens against the projects.

Lund-Ross sued the debtors and Signature in state court. The debtors filed their bankruptcy case, but the state court action proceeded against Signature and resulted in a default judgment against the company for several hundred thousand dollars. Lund-Ross filed a proof of claim in the bankruptcy case for the amount of the judgment. The chapter 7 trustee succeeded in objecting to the claim, on the basis that the underlying debt was not owed by the debtors but rather by Signature.

Undeterred, Lund-Ross commenced an adversary proceeding under section 523(a)(2)(A) to have the debt excepted from discharge. Lund-Ross argued that the representations in the payment applications that all suppliers and sub-subcontractors had been paid were fraudulent, and that the debtors were individually liable on that debt. The debtors moved for summary judgment on a host of theories, including that the debt was owed by Signature rather than the debtors, and that any representations the debtors made were made on behalf of Signature.

The Court granted summary judgment for the debtors. The Court noted that the underlying invoices and lien claims referenced Signature rather than the debtors, that there was no evidence the debtors guaranteed the debts, and that in Nebraska members of a limited liability company like Signature typically are not individually liable for company debts. The Court further found that the "only way" Lund-Ross could prevail would be to pierce the corporate veil, but that Lund-Ross had not sought to do so.

Lund-Ross argued that case law supports that individuals who make false statements in lien waivers are personally liable for resulting damages. The Court distinguished those cases—from Ohio and North Carolina—on the basis that the applicable law in those states specifically provided for personal liability, whereas no similar statute applied in Nebraska.

Ultimately, the Court concluded that while "the plaintiff claims [debtor] Jay Buchanan knowingly and intentionally made fraudulent representations that proximately caused it damage, the plaintiff has not demonstrated how the Buchanans can be held personally liable for their business's debts." Because the debtors were not liable for the debts, there was no need to discuss whether they should or should not be discharged.

Conspicuously absent from the Court's discussion—presumably because it was not raised by the parties—is that Nebraska law, like the law of most jurisdictions, holds that "where fraud is committed by a corporation, it is time to disregard the corporate fiction and hold the persons responsible therefor liable in their individual capacities." *Huffman v. Poore*, 569 N.W.2d 549, 557 (Neb. App. 1997), citing seven cases from the Nebraska Supreme Court for that proposition. Further, Nebraska specifically rejects the argument that a plaintiff must first pierce the corporate veil to hold a corporate officer individually liable for his personal, active participation in a fraud by the corporation. *Id.*

The Court's decision here is unremarkable as to the issues it reached—plainly, an objection to the discharge of a debt will fail if the debtor is not liable for the debt in the first place. But, the opinion underscores the importance of explaining clearly why it is that a corporate officer may be held individually liable for the fraud in which he or she participates personally, even if he or she committed the fraud as a corporate officer. The factual scenario presented here is in no manner unusual for a distressed contractor, and those dealing with distressed contractors would do well to keep this opinion in mind.

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