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U.S. BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA**

In re:)	Chapter 11
)	
THE VILLAS AT HACIENDA)	Case No. 4-05-bk-1482-EWH
DEL SOL, INC.,)	
)	
Debtor.)	
)	MEMORANDUM DECISION

INTRODUCTION

The Villas at Hacienda Del Sol, Inc. ("Villas" or "Debtor") filed a Chapter 11 bankruptcy petition on March 28, 2005. Louis Cohen ("Cohen") asserts a claim for \$1.25 million against the Debtor, based upon a promissory note ("Note") in that amount issued in his favor by the Debtor. Equity shareholders, David Mason and Manchester Development Company (collectively, "Mason"), object to Cohen's claim. Mason asserts that Cohen is not a Holder in Due Course ("HIDC") under Uniform Commercial Code ("UCC") §3-302¹ because he took the Note with notice of a claim for breach of fiduciary duty.

On October 19, 2006, the Court held an evidentiary hearing on the objection filed by Mason. The parties agreed that the hearing was limited to the question of whether Cohen is a HIDC of the Note.

¹ Hereafter, all citations to the UCC will be referenced by section only.

1 Because the evidence demonstrates that Cohen is a HIDC and that he
2 took the Note without any notice of a breach in fiduciary duty,²
3 Mason's objection is overruled.

4 **FACTS**

5 Cohen invested money in a project known as Country Village Road.
6 Albert Gersten ("Gersten") and Martin Collier ("Collier") were
7 involved in this project. Cohen had invested or been involved with
8 other projects of Gersten and Collier, having known both men for
9 many years. Country Village Road was going to be sold. Cohen
10 wished to invest his proceeds from that project, up to \$1.25
11 million, in another Collier and Gersten project -- the Debtor.

12 Gersten and Collier have a company called GC Enterprises. Before
13 the closing of the sale of Country Village Road, GC Enterprises
14 agreed to advance funds to the Debtor on Cohen's behalf. The
15 parties understood that upon the closing of Country Village Road,
16 the amount advanced would be reimbursed to GC Enterprises and a Note
17 would be issued from the Debtor for the amount advanced. The
18 agreement between Cohen and GC Enterprises was memorialized in a
19 letter dated May 1, 2003, and signed by Cohen and Collier. (Cohen
20 Exhibit C-2.)

21 Country Village Road sold, and the Debtor issued a Note to Cohen
22 in the amount of \$1.25 million, dated November 18, 2004. (Cohen
23 Exhibit C-1-A.) The Note was signed by Collier as President of the
24

25 ² For purposes of this ruling, the Court does not decide
26 whether there was, in fact, a breach of any kind.

1 Debtor. When the Debtor filed for bankruptcy, it scheduled Cohen's
2 claim as undisputed.

3 **ISSUE**

4 Is Cohen a Holder in Due Course?

5 **STATEMENT OF JURISDICTION**

6 The Court has jurisdiction over this matter pursuant to 28 U.S.C.
7 §1334 and General Order 128 of the United States District Court for
8 the District of Arizona. Venue is proper under 28 U.S.C. §1409.

9 **DISCUSSION**

10 Mason alleges that Collier breached his fiduciary duty by issuing
11 the Note from the Debtor to satisfy a debt owed to Cohen by GC
12 Enterprises. Mason further alleges that Cohen took the Note with
13 notice of the breach of fiduciary duty, which thereby prevents him
14 from being a HIDC.

15 **STATUTORY BACKGROUND**

16 This issue involves several sections of the UCC. Under §3-306, a
17 person taking an instrument is subject to a claim to the instrument
18 or its proceeds, unless the person is a HIDC under §3-302. Under
19 §3-302(a)(2)(v), the taker cannot be a HIDC if the instrument was
20 taken with notice of a claim under §3-306.

21 A claim under §3-306 includes a claim of a "represented person"
22 under §3-307(b)(iii) (the represented person makes a claim to the
23 instrument or its proceeds on the basis that the transaction of the
24 fiduciary is a breach of fiduciary duty). Section 3-307 specifies
25 rules for determining when a person taking an instrument has notice

26

1 of the claim, which will prevent assertion of his rights as a HIDC
2 because of §3-302(a)(2)(v).

3 Section §3-307 provides in pertinent part:

4 (a) In this section:

5 (1) "Fiduciary" means an agent, trustee, partner, corporate
6 officer or director, or other representative owing a
7 fiduciary duty with respect to an instrument.

8 (2) "Represented person" means the principal, beneficiary,
9 partnership, corporation, or other person to whom the duty
10 stated in paragraph (1) is owed.

11 (b) If (I) an instrument is taken from a fiduciary for
12 payment or collection or for value, (ii) the taker has
13 knowledge of the fiduciary status of the fiduciary, and
14 (iii) the represented person makes a claim to the instrument
15 or its proceeds on the basis that the transaction of the
16 fiduciary is a breach of fiduciary duty, the following rules
17 apply:

18 (1) Notice of breach of fiduciary duty by the fiduciary is
19 notice of the claim of the represented person. . . .

20 (4) If an instrument is issued by the represented person or
21 the fiduciary as such, to the taker as payee, the taker has
22 notice of the breach of fiduciary duty if the instrument is
23 (I) taken in payment of or as security for a debt known by
24 the taker to be the personal debt of the fiduciary, (ii)
25 taken in a transaction known by the taker to be for the
26 personal benefit of the fiduciary, or

17 MASON'S OBJECTION

18 Mason asserts that Cohen had notice of a breach of fiduciary duty
19 for purposes of §3-307, which prevents him from being a HIDC. Mason
20 argues that Cohen knew that Collier was the Debtor's President and
21 that the transaction was for the personal benefit of Collier.

22 Mason's argument makes two assumptions. First, it assumes that
23 Mason satisfies §3-307(b)(iii) as the represented person making a
24 claim. However, Mason may not qualify as "the represented person"
25 under §3-307, which is defined as the principal, beneficiary,
26 partnership, corporation, or other person to whom the fiduciary duty

1 with respect to the instrument is owed -- this would be the Villas.
2 It is worth noting that, at the Hearing, Mason's counsel stated that
3 "Villas is the representative person." (Hearing Transcript at 110,
4 11. 24-25.) The Debtor, however, is not making a claim to the
5 instrument based on a breach of fiduciary duty, having scheduled the
6 debt as undisputed.

7 Second, Mason's argument assumes monies advanced by GC
8 Enterprises on behalf of Cohen constitute a "personal debt" of
9 Collier or that the repayment of the advance is for the "personal
10 benefit" of Collier. There has been no showing that Collier and GC
11 Enterprises are legally fungible.

12 For purposes of this ruling, however, the Court will decide the
13 issue without challenging these assumptions. The Court finds that
14 Cohen is a HIDC because he did not take the Note in a transaction
15 known by him to be for the personal benefit of Collier. The
16 evidence demonstrates that Cohen believed his loan was for the
17 benefit of the Villas, pursuant to his agreement with GC
18 Enterprises.

19 Mason's argument ignores the fact that, pursuant to the agreement
20 memorialized in the letter dated May 1, 2003, Cohen understood that
21 GC Enterprises had advanced the proceeds from the sale of Country
22 Village Road to the Villas on behalf of Cohen -- it was a two-step
23 transaction.³

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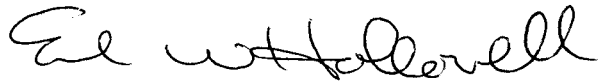
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³ At the hearing, Counsel for Mason conceded that the personal benefit element argument would be eliminated if the loan had been accomplished in one step. (Hearing Transcript at 121 l. 25; 122, 11. 1-8.)

CONCLUSION

1 Because Cohen has demonstrated that he is a HIDC under §3-302 and
2 that his status is not defeated by §3-307 because he took the Note
3 without any notice of a breach in fiduciary duty, he is entitled to
4 have his claim paid. A separate Order will be entered overruling
5 the objection and allowing his claim.
6

7 Dated this 27th day of November, 2006.
8

9 

10 EILEEN W. HOLLOWELL
11 UNITED STATES BANKRUPTCY JUDGE

12 Copies of the foregoing
13 mailed this 27th day of
14 November, 2006, to:


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