

ORDERED.



Dated: July 02, 2010

*Eileen W. Hollowell*

EILEEN W. HOLLOWELL  
U.S. Bankruptcy Judge

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF ARIZONA

In re:	)	Chapter 11
	)	
CHARLES R. ROSE,	)	Case No. 2:07-bk-05284-EWH
	)	
Debtor.	)	
<hr/>		
DERRICK COLLINS,	)	
	)	Adv. No. 2:08-ap-00033-EWH
Plaintiff,	)	
v.	)	<b>MEMORANDUM DECISION</b>
	)	
CHARLES R. ROSE,	)	
	)	
Defendant.	)	
<hr/>		

**I. INTRODUCTION**

The Debtor entered into a payment obligation with no intent of repaying it because he believed it would be paid by another. However, the Debtor did not disclose that fact to the lender and also failed to disclose his knowledge about the uncertain status of title to property which purportedly secured the obligation. As a result, the Debtor may not discharge the obligation in his bankruptcy case.

1 II. FACTS

2 Debtor, who works as a construction consultant specializing in post-disaster  
3 projects, was owed money by one of his clients. According to the Debtor, he was asked  
4 to do work for the client's property acquisition division, Gibraltar Properties LLC  
5 ("Gibraltar"), to expedite payment on what he was owed. It was Debtor's efforts to assist  
6 Gibraltar that led Debtor to incur an obligation to the Plaintiff, Derrick Collins ("Collins").  
7 In late 2006, Gibraltar was seeking to obtain title insurance on land in Imperial County,  
8 California, so that it could use the property as collateral for a loan. To complete the title  
9 insurance process and to pay obligations the insurance division owed to the Debtor and  
10 another party, Emmanuel Illuminardi ("Illuminardi"), Gibraltar needed cash.

11  
12  
13 Illuminardi is in the business of real estate and construction development. In late  
14 2006, he approached a Mr. McDaniels ("McDaniels") about raising \$100,000 for  
15 Gibraltar. In addition to raising private investment for real estate deals, McDaniels also  
16 does tax preparation work. Collins was one of his tax clients. In doing Collins' tax work,  
17 McDaniels learned that Collins had recently inherited several hundred thousand dollars  
18 from his grandfather. McDaniels approached Collins about making a \$100,000 loan to  
19 raise the money Illuminardi was seeking. After first resisting, in late 2006, Collins  
20 decided to make the loan McDaniels suggested.

21  
22 On December 14, 2006, Collins delivered to McDaniels' office a cashier's check  
23 ("Check") for \$100,000 made out to Gibraltar. Collins testified the Check was made out  
24 to Gibraltar per McDaniels' instruction. In return, Collins was given a promissory note  
25 ("Note") dated December 14, 2006 and executed by the Debtor and Illuminardi. The  
26 Note promised to pay Collins \$150,000.00 on or before April 14, 2007. The Note also  
27

1 states it is secured by a parcel of real property located in Imperial County, California  
2 (“Property”). The Property was one of the parcels that Gibraltar was trying to insure.  
3 Collins was also given two deeds (“Deeds”). The first deed purported to transfer the  
4 Property from Gibraltar to Illuminardi. The second deed purported to transfer the  
5 Property from Illuminardi to Collins. Neither deed was recorded. Collins was told  
6 (presumably by McDaniels) that the Deeds were the collateral for the Note.<sup>1</sup>

8 The Debtor and Illuminardi each received \$25,000.00 from Gibraltar after the  
9 Check was negotiated by Gibraltar. Both the Debtor and Illuminardi testified that those  
10 payments were made for past work they did for Gibraltar. The Debtor and Illuminardi  
11 also testified that they believed, at the time they executed the Note, that Gibraltar would  
12 obtain insurable title to the Property and that neither one of them would be called upon to  
13 pay the Note because Gibraltar would do so as soon as it obtained title insurance.  
14 Debtor testified that he believed Gibraltar held good title to the Property (and the rest of  
15 the Imperial parcels) because he had been “doing leg work” for a title examiner and  
16 because of the assurances he received from the title examiner that a title policy would be  
17 issued to Gibraltar.  
18

19  
20 Debtor testified he knew when he executed the Note that he could not pay it. He  
21 testified he was relying on Gibraltar to pay the Note because he knew he could not do  
22 so. Debtor’s counsel asked, “You had 100 percent complete confidence that Gibraltar  
23 would timely pay back this obligation when it became due?” To which the Debtor  
24

25 \_\_\_\_\_  
26 <sup>1</sup>Illuminardi testified he did not meet or speak to Collins on December 14, but Collins  
27 testified he met Illuminardi on that date. McDaniels was not called as a witness. All parties  
agree that the Debtor did not meet Collins until after the loan went into default.



1 **III. ISSUE**

2 Is Debtor’s obligation to Collins non-dischargeable under 11 U.S.C.  
3 § 523(a)(2)(A)?  
4

5 **IV. STATEMENT OF JURISDICTION**

6  
7 Jurisdiction is proper under 28 U.S.C. §§ 1334(8) and 157(b)(2)(J).  
8

9 **V. DISCUSSION**

10 **A. Introduction**

11 Money, property, services, or an extension, renewal, or refinancing of credit  
12 obtained by a debtor can be excepted from the debtor’s discharge if a debtor obtains it  
13 through “false pretenses, false representation or actual fraud.” 11 U.S.C. § 523(a)(2)(A).  
14 The terms “false pretenses” and “false representation” both involve intentional conduct  
15 intended to create and foster a false impression. *In re Patten*, 225 B.R. 211, 215 (Bankr.  
16 D. Or. 1998) *citing* Collier on Bankruptcy ¶ 523.08[1][d] (15th Ed. 1998). The distinction  
17 between the two terms is that a false representation typically involves a statement, while  
18 a claim of false pretenses typically involves misleading conduct without an explicit  
19 statement. *Id.* In this case, because there was no contact between the Debtor and  
20 Collins before the Note was executed, there is no issue regarding the Debtor’s conduct.  
21 Instead the court must determine whether the Note was a false representation.  
22 In order to prevail on his non-dischargeability complaint, Collins must establish by a  
23 preponderance of the evidence, *Grogan v. Garner*, 498 U.S. 279, 291 (1991), that (1) the  
24  
25  
26  
27  
28

1 Debtor knew he made a misrepresentation, (2) the Debtor knew it was false at the time,  
2 (3) the Debtor intended to deceive Collins, (4) Collins relied upon the false  
3 representation, and (5) the false representation was the proximate cause of damage to  
4 Collins. *In re Cossu*, 410 F.3d 591, 596 (9th Cir. 2005) *citing In re Britton*, 950 F.2d 602,  
5 604 (9th Cir. 1991).  
6

7 B. Misrepresentation and knowledge

8 At the evidentiary hearing, the parties focused on whether the Debtor's  
9 representation that the Note was secured by the Property was a fraudulent  
10 misrepresentation. The Debtor testified that, when he executed the Note, he believed  
11 that Gibraltar would be successful in obtaining title insurance for the Property and that,  
12 therefore, the representation that the Note was secured was not fraudulent. However,  
13 the Debtor knew when he signed the Note that Gibraltar did not yet have insurable title to  
14 the Property because he was doing "leg work" with a title examiner so Gibraltar could  
15 obtain title insurance. Nothing in the Note or the Deeds disclosed that information to  
16 Collins. Silence or omissions regarding a material fact can constitute a false  
17 representation under § 523(a)(2)(A) when there is a duty to disclose. *In re Eashai*,  
18 87 F.3d 1082, 1089 (9th Cir. 1996). There is a duty to disclose when the other party to a  
19 contract is ignorant of material facts which he does not have an opportunity to discover.  
20 *Apte v. Japra, M.D., F.A.C.C., Inc. (In re Apte)*, 96 F.3d 1319, 1324 (9th Cir. 1996).  
21 The failure to disclose the Property's status was not the only misrepresentation the  
22 Debtor made. The Debtor knew he could not repay the Note at the time he signed it.  
23 While not every broken promise is a false representation under § 523(a)(2)(A), if the  
24 creditor can prove a debtor did not intend to perform or could not perform when the debt  
25  
26  
27  
28

1 is incurred, then the debt may be excepted from discharge under § 523(a)(2)(A).  
2 *McCrary v. Barrack (In re Barrack)*, 217 B.R. 598, 606-07 (B.A.P. 9th Cir. 1997). The  
3 inability or lack of intent to perform usually needs to be proven through circumstantial  
4 evidence, *In re Carlson*, 426 B.R. 840, 855 (Bankr. D. Idaho Mar. 19, 2010), but in this  
5 case, the Debtor testified that he knew he was not able to perform at the time he signed  
6 the Note.  
7

8       The fact that the Debtor expected Gibraltar to pay the Note does not rescue the  
9 Debtor from his misrepresentation. It is simply another material fact which was not  
10 disclosed. Nothing in the Note alerts Collins that Gibraltar is supposed to pay the Note.  
11 Debtor testified that he told McDaniels that Gibraltar would have to pay the Note  
12 because he could not, but Collins denied being told by McDaniels that the “real” borrower  
13 was Gibraltar. Debtor has not established that McDaniels was anything more than a  
14 facilitator to all of the parties in the transaction. Absent proof that McDaniels was Collins’  
15 agent, notice to McDaniels cannot be treated as notice to Collins. Accordingly, Debtor’s  
16 testimony is simply an admission by the Debtor that he signed the Note knowing he  
17 could not perform.  
18

19  
20       C.     Intent to Deceive

21       The court, as finder of fact in this case, must “consider all of the facts and  
22 circumstances of the case to determine if the debtor lacked the requisite intent to  
23 perform.” *E.g., Mandalay Resort Group v. Miller (In re Miller)*, 310 B.R. 185, 196 (Bankr.  
24 C.D. Cal. 2004). The Debtor testified that he knew he could not perform and that he  
25 never intended to be in a position where he would have to perform because he believed  
26 Gibraltar would do so. Thus, the direct evidence shows that the Debtor did not intend to  
27

1 perform. This is not a case where a debtor has a good faith belief or hope when she  
2 writes a check that the bank will honor it. In such cases, courts have found there is no  
3 intent to deceive. *In re Elibuyuk*, 163 B.R. 75, 76 (Bankr. E.D. Va. 1993); *In re Pike*,  
4 79 B.R. 41, 43-44 (Bankr. N.D. Ala. 1987). While the Debtor may have had a good faith  
5 belief that Gibraltar would pay the Note, that does not change the fact the Debtor knew  
6 *he* could not perform when he signed the Note.  
7

8 D. Reliance

9 Collins must establish that he reasonably relied on the representations in the Note  
10 and Deeds. *Cossu*, 410 at 596. A person is entitled to rely on a representation even if  
11 the falsity of that representation could have been ascertained had the person  
12 investigated. *Eashai*, 87 F.3d at 1090-91. While the Check was made out to Gibraltar  
13 and one of the Deeds is from Gibraltar to Illuminardi, those two facts are not enough to  
14 have put Collins on notice that Gibraltar was the “real” borrower. The Debtor had  
15 information about the true nature of the transaction, and the Debtor did not provide that  
16 information to Collins. Instead, the Debtor accommodated Gibraltar’s apparent desire to  
17 be an undisclosed party to the transaction by executing the Note which does not mention  
18 Gibraltar.  
19  
20

21 A misrepresentation or omission about a material term of an agreement  
22 constitutes a fraudulent representation within the meaning of § 523(a)(2)(A). *Apte*,  
23 96 F.3d at 1323-24. One party to a business transaction is under a duty to exercise  
24 reasonable care to disclose to the other party facts basic to the transaction if she knows  
25 the other party will be mistaken about those facts. *Id.* The Debtor knew he did not intend  
26 to pay, knew only his name and Illuminardi’s appeared on the Note, and he, therefore,  
27



1 should have known that Collins was mistaken about the material fact that Gibraltar was  
2 the party who was expected to pay. Collins' uncontroverted testimony was that he "was  
3 led to believe whatever the Note said, that's who [he] was going after." (Tr. 114,  
4 Ins 22-24.)  
5

6 Debtor also knew that when the Deeds were given to Collins, Gibraltar had not  
7 obtained title insurance for the Property. Debtor entered a letter into evidence from a  
8 title examiner to demonstrate that Debtor had a good faith belief that Gibraltar would  
9 obtain title insurance. However, the letter was not shared with Collins. Therefore, the  
10 letter demonstrates Debtor knew that Gibraltar did not yet have insurable title to the  
11 Property when he signed the Note.  
12

13 E. Proximate Cause of the Damages

14 Collins needs to prove that the Debtor's fraudulent misrepresentation caused his  
15 damages. *Carlson*, 426 B.R. at 856-57. The related doctrine of proximate causation may  
16 relieve a party from liability if damages caused by his or her conduct were unforeseeable  
17 or there was some intervening cause. *Patten*, 225 B.R. at 211.  
18

19 The damage in this case is the money Collins lost. While the Note provides Collins is to  
20 be paid \$150,000, only the money actually obtained through the fraudulent  
21 misrepresentation, which is a tort claim, is nondischargeable. *Carlson*, 426 B.R. at  
22 856-57. Here, Collins lost \$100,000 after he made out the Check, Gibraltar negotiated it,  
23 and nobody repaid it.  
24

25 Collins' damages were foreseeable to the Debtor because the Debtor knew he  
26 could not pay the Note. Debtor also knew, as of the date of the Note, that Gibraltar had  
27 not obtained title insurance for the Property. It was foreseeable, therefore, that Collins  
28

1 might not be able to realize on the collateral for the Note. Collins has demonstrated that  
2 Debtor's fraudulent misrepresentation caused Collins damages

3 F. Calculation of Damages

4 Collins lost \$100,000 when he accepted the Note and Deeds in return for the  
5 Check. At trial, Collins admitted receiving \$25,000.00 from McDaniels.<sup>4</sup> Collins  
6 characterized that payment as either "hush money" or money that McDaniels paid out of  
7 a sense of moral obligation, not as payment on the Note. (Tr. 120, Ins 1-10.) The Debtor  
8 did not call McDaniels as a witness, and the court does not find Collins' testimony  
9 plausible. The Debtor is entitled to a \$25,000.00 credit as a result of the payments made  
10 by McDaniels to Collins.<sup>5</sup>  
11  
12

13  
14 **VI. CONCLUSION**

15 The foregoing constitutes the court's findings of fact and conclusions of law as  
16 required by Rule 7052. A separate nondischargeable judgment will be entered against  
17 the Debtor in the amount of \$75,000.00 with interest to accrue at the federal judgment  
18 rate.  
19

20 Dated and signed above.  
21  
22  
23  
24

---

25 <sup>4</sup> Illuminardi testified that he had given McDaniels \$2,500 to give to Collins. (Tr. 65, Ins 16-22.)

26 <sup>5</sup> The court makes no determination regarding McDaniels' right to make a claim against the Debtor  
27 for sums paid to Collins

1 Notice to be sent through the  
2 Bankruptcy Noticing Center "BNC"  
3 to the following:

4 Charles R. Rose  
5 10022 East Cortez Drive  
6 Scottsdale, AZ 85260

7 Allan D. Newdelman, Esq.  
8 Allan D. Newdelman, P.C.  
9 80 East Columbus Avenue  
10 Phoenix, AZ 85012

11 Christopher J. Pattock  
12 Office of the U.S. Trustee  
13 230 North First Avenue #204  
14 Phoenix, AZ 85003-1706

15 Derrick Collins  
16 2243 N. El Sereno Avenue  
17 Altadena, CA 91001