

## Holder in Due Course...in Layman's Terms

Holder in Due Course (HIDC) is part of the Uniform Commercial Code (UCC) that significantly impacts an organization's liability for check fraud and the checks it issues. After learning about HIDC claims, prudent companies are often motivated to use high security checks and change check disbursement procedures to protect themselves. The following is a brief, understandable explanation of Holder in Due Course.

In simple terms, a Holder in Due Course is anyone who accepts a check for payment. On the face of the check there cannot be any evidence of fraud, nor can the person accepting the check have knowledge of any fraud related to it. Under the UCC, the recipient of the check is an HIDC and is entitled to be paid for the check. The statute of limitations for an HIDC to sue the check's maker for its face value is 10 years from the issue date, or three years from the date the check was deposited and returned unpaid, whichever comes first. An HIDC can assign, sell, give, or otherwise transfer its rights to another party, who becomes the new HIDC with the same legal rights as the original Holder.

The following Federal Appellate Court cases illustrate the far-reaching power of Holder in Due Course.

### **ROBERT J. TRIFFIN V. CIGNA INSURANCE COMPANY**

**Issue: Placing A Stop Payment Does Not Eliminate Your Obligation To Pay A Check**

In July 1993, Cigna Insurance issued James Mills a Worker's Compensation check for \$484. Mills falsely claimed he did not receive it due to an address change, and requested a replacement. Cigna placed a stop payment on the initial check and issued a new check. Mills nevertheless cashed the first check at Sun's Market, and Sun presented the check for payment through its bank.

Cigna's bank dishonored the check, stamped it with "Stop Payment," and returned the check to Sun's bank. Had Sun's Market filed a claim against Cigna as the issuer of the check, Sun would have been entitled to be paid because of its status as a Holder in Due Course. However, Sun either did not know about the law or chose not to pursue it, because it merely tacked the check up on its bulletin board.

Robert J. Triffin obtained the check from Sun's Market, became the new HIDC, and filed this lawsuit against Cigna in August 1995, over two years after the check was returned unpaid. The Court ultimately ruled in favor of Robert Triffin, and Cigna had to pay him \$484, plus interest.

**Recommendation:** Make a check "expire" before replacing it, or you can be held liable for both checks. Print an expiration statement on the face of checks such as, "THIS CHECK EXPIRES AND IS VOID 20 DAYS FROM ISSUE DATE." If a check is lost, wait 20 + 2 days from the initial issue date before reissuing. Many companies print "Void After 90 Days" or longer, but cannot reasonably wait that long before re-issuing a check. A party that accepts an expired check has no HIDC basis if the check is returned unpaid.

While the above case clearly illustrates what a Holder in Due Course is, the case does not deal with check security features, or the lack thereof. The following two cases do.

### **ROBERT J. TRIFFIN V. SOMERSET VALLEY BANK AND HAUSER CONTRACTING CO.**

**Issue: You May Be Responsible For Checks You Did Not Issue or Authorize**

Hauser Contracting Co. used ADP for payroll services. A thief obtained check stock that looked identical to ADP's checks and created 80 counterfeit payroll checks identical to Hauser Contracting Co.'s, and cashed them all over town.

A retailer who knew Mr. Hauser became suspicious and called him. Somerset Valley Bank also called. Mr. Hauser reviewed the checks, which looked just like his, and confirmed the checks were unauthorized and the payees were not his employees. The bank returned the checks marked as "Stolen Check - Do Not Present Again."

Mr. Triffin bought 18 of these checks totaling \$8800 from four check cashing agencies, claimed HIDC status, and sued both Mr. Hauser and his bank for negligence for not safeguarding the payroll checks and facsimile stamp. Because the counterfeit and authentic checks looked identical, the lower court ruled for Triffin. Hauser appealed, but the Federal Appellate Court upheld the lower court. The Court said the counterfeit check met the definition of a negotiable instrument, and because the check and signature were identical to an authentic check, the check cashing agency could not have known it was not authentic.

Recommendation: Use a controlled check stock, which means using checks that are uniquely designed or customized for your organization and are not available blank to others. SAFEChecks and the Abagnale SuperBusinessCheck, manufactured and sold by SAFEChecks, are both strictly controlled check stock.

### **ROBERT J. TRIFFIN V. POMERANTZ STAFFING SERVICES, LLC**

#### **Issue: High Security Checks May Protect You From Some Holder in Due Course Claims**

Pomerantz Staffing Services used high security checks that included heat sensitive (thermochromatic) ink on the back and a warning banner on the front that said, "THE BACK OF THIS CHECK HAS HEAT SENSITIVE INK TO CONFIRM AUTHENTICITY." Someone made copies of Pomerantz's checks, but without the thermo ink on the back. They cashed 18 checks totaling \$7000 at Friendly Check Cashing Company. Friendly's cashiers failed to heed the warning on the check face, and did not look for the thermo ink. All 18 checks were returned unpaid, likely caught by Positive Pay.

Mr. Triffin bought the checks, claimed Holder in Due Course status, and sued Pomerantz. Pomerantz counter-sued and won! The judge correctly asserted that if Friendly had looked for the thermo ink as instructed, they could have determined the checks were counterfeit. Because they were provided a means to verify authenticity and failed to do so, they were not an HIDC and had no rights to transfer to Mr. Triffin.

This case clearly illustrates the value of check security features, a properly worded warning band, and a controlled check stock. Pomerantz was protected by his checks.

Recommendation: Use high security checks with overt and covert security features, including explicitly worded warning bands. Such security features will also help prevent other kinds of check fraud.

**(For an in-depth article, read "Holder in Due Course and Check Fraud," written by Frank Abagnale and Greg Litster. The article can be found at [www.fraudtips.net](http://www.fraudtips.net) or from SAFEChecks at [info@safechecks.com](mailto:info@safechecks.com).)**

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The Abagnale **SuperBusinessCheck** has 16 security features and **SAFEChecks** have 12 security features, including heat sensitive ink, a dual-tone true watermark and explicit warning bands. Both are strictly controlled, high security check stock that were designed with Frank Abagnale, one of the world's foremost authorities on fraud prevention, and are manufactured and sold by SAFEChecks.