

UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

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U.S. DISTRICT COURT
WESTERN DISTRICT MICH
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MICHAEL J. QUILLING, Receiver for
Hammersmith Trust, L.L.C., Hammersmith
Trust, Ltd., Microfund, L.L.C. and B.
David Gilliland,

Plaintiff,

v.

Case No.: 1:00-CV-826

THE WOLCOTT LIFETIME TRUST,
JACK W. HIGGINS, TRUSTEE,
MELODY WOLCOTT GILLILAND,
JEFFREY D. SAXON, JR.,
OPTION ONE MORTGAGE
CORPORATION, NORWEST BANK
MINNESOTA (now known as WELLS
FARGO BANK MINNESOTA), and
NORTHPOINTE BANK,

HON. GORDON J. QUIST

Defendants.

OPINION

Plaintiff, Michael J. Quilling ("Quilling"), the Receiver for Hammersmith Trust, L.L.C., Hammersmith Trust, Ltd., Microfund, L.L.C., and B. David Gilliland, filed this action against Defendants, The Wolcott Lifetime Trust, Jack W. Higgins, Trustee, Melody Wolcott Gilliland, Jeffrey D. Saxon, Jr., Option One Mortgage Corporation, Norwest Bank Minnesota, n/k/a Wells Fargo Bank Minnesota, and Northpointe Bank, seeking: (1) a declaratory judgment that equitable title to certain real property located in Ottawa County, Michigan, is vested in him and that his interest is superior to the interests of the Wolcott Lifetime Trust and Melody Wolcott Gilliland; and (2) the imposition of a constructive trust in his favor over the Wolcott Lifetime Trust's interest in the property. Now before the Court is Quilling's motion for summary judgment against the Wolcott Lifetime Trust and Melody Wolcott Gilliland.

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Facts

David Gilliland ("Gilliland") and Melody Wolcott Gilliland ("Melody Gilliland") were married until October 7, 1995, when their divorce became final. From approximately 1997 to 1999, Gilliland controlled the day-to-day operations of Hammersmith Trust, LLC and Microfund, LLC (the "Funds"). The Funds were represented to investors as offering high-yield investments through which investors could receive huge returns with no risk of principal. In reality, the investments offered by the Funds were fraudulent pyramid schemes which were perpetuated by paying funds received from subsequent investors to prior investors.

During the course of the fraudulent scheme, Gilliland diverted approximately \$3.5 million received by the Funds from investors to entities owned and controlled by him, including Covent Garden, LLC, Tactical Capital Placement, LLC, Paladin Consulting, and the Wolcott Lifetime Trust. Gilliland had complete control over these entities and was solely responsible for moving funds into and out of them. The only monies ever placed into these entities came from defrauded investors through the Funds.

Gilliland caused the Wolcott Lifetime Trust (the "Trust") to be created on July 31, 1998. Jack Higgins ("Higgins"), a business associate of Gilliland, was appointed trustee of the Wolcott Lifetime Trust. Melody Gilliland was the lifetime beneficiary of the Trust, and the remainder beneficiaries were Gilliland's daughters, Devon Lee Gilliland and Ashley Waldron Gilliland. The Trust was established for the sole purpose of acquiring the property located in the Township of Port Sheldon, County of Ottawa, and State of Michigan, more commonly known as 9047 Lakeshore Drive, West Olive, Michigan 49460, and legally described as:

A part of the North $\frac{1}{2}$ of the Southwest fractional $\frac{1}{4}$ of Section 4, Town 6 North, Range 16 West, described as commencing at a point 1100 feet West and 999 feet South of the Northeast corner of the said Southwest fractional $\frac{1}{4}$ of said Section; running thence South 110 feet; running thence West to the margin of Lake Michigan; running thence North along the margin of Lake Michigan 110 feet to a point directly West of place of beginning; running thence East to place of beginning. Including an unrecorded right of ingress and egress from the Public highway over the presently established roadway.

(the "Michigan Property"). Gilliland agreed to cause the Trust to purchase the Michigan Property for the benefit and use of Melody Gilliland in exchange for a release by Melody Gilliland to Gilliland's mother of Melody Gilliland's equity interest in property located in Memphis, Tennessee (the "Memphis Property"). On August 11, 1998, the Trust purchased the Michigan Property by warranty deed (the "Trust Deed") from John and Nancy Carlyle for \$385,000.00. All of the funds used to purchase the Michigan Property, including closing costs and attorney fees, came from monies acquired from the fraudulent schemes perpetrated by the Funds. The total amount paid by the Trust in connection with the transaction was \$389,290.53.

Quilling became the Receiver for the Funds as of July 22, 1999.¹ After learning that the monies used to purchase the Michigan Property were diverted from the Funds, Quilling demanded that Higgins cause the Trust to convey the Michigan Property to Quilling. Higgins agreed to the demand, and on February 9, 2000, signed a warranty deed on behalf of the Trust conveying the Michigan Property to Quilling as Receiver for the Funds (the "Receiver's Deed").

II. Standard of Review

Summary judgment is appropriate if there is no genuine issue as to any material fact and the moving party is entitled to a judgment as a matter of law. Fed. R. Civ. P. 56. Material facts are facts which are defined by substantive law and are necessary to apply the law. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S. Ct. 2505, 2510 (1986). A dispute is genuine if a reasonable jury could return judgment for the non-moving party. Id.

The court must draw all inferences in a light most favorable to the non-moving party, but may grant summary judgment when "the record taken as a whole could not lead a rational trier of fact to find for the non-moving party." Agristor Financial Corp. v. Van Sickle, 967 F.2d 233, 236 (6th Cir. 1992)(quoting Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574, 587, 106 S. Ct. 1348, 1356 (1986)).

¹Quilling was initially appointed Receiver in the matter captioned Securities and Exchange Commission v. Funding Resource Group, a/k/a FRG Trust, et al., Case No. 3:98-CV-2689-M, on November 13, 1999. The receivership was subsequently expanded to include the Funds.

Discussion

In the present motion, Quilling requests that the Court declare that a constructive trust is imposed upon the Trust's title to the Michigan Property in favor of Quilling as Receiver, that equitable title is vested in Quilling, that the Receiver's Deed is valid, enforceable, and vests equitable title in Quilling, and that the Trust Deed is null and void.

Under Michigan law,

[a] constructive trust may be imposed "where such trust is necessary to do equity or to prevent unjust enrichment. . . ." Hence, such a trust may be imposed when property "'has been obtained through fraud, misrepresentation, concealment, undue influence, duress, taking advantage of one's weakness, or necessities, or any other similar circumstances which render it unconscionable for the holder of the legal title to retain and enjoy the property. . . ." Accordingly, it may not be imposed upon parties "who have in no way contributed to the reasons for imposing a constructive trust." The burden of proof is upon the person seeking the imposition of such a trust.

Kammer Asphalt Paving Co. v. East China Township Sch., 443 Mich. 176, 188, 504 N.W.2d 635, 641-42 (1993)(citations omitted). See also McCreary v. Shields, 333 Mich. 290, 52 N.W.2d 853 (1952)(en banc)(holding that a constructive trust was properly imposed to prevent the defendant from being unjustly enriched by a mistake common to all parties). See id. at 294-95, 52 N.W.2d at 855-56.

Although actual fraud will certainly support the imposition of a constructive trust under Michigan law, it is not a prerequisite. "Fraud in the inception [is] not require[d], nor deceit, nor chicanery in any of its valied [sic] guises, for it is not necessary that property be wrongfully acquired. It is enough that it is unconscionably withheld." Kent v. Klein, 352 Mich. 652, 657, 91 N.W.2d 11, 14 (1958)(en banc).

The facts in this case, which are not in dispute², establish that Gilliland diverted fraudulently obtained monies to the Trust and that those monies were the sole source of funds used to purchase the Michigan Property. Although there is no evidence showing that Melody Gilliland participated

²Melody Gilliland states that she does not agree that the source of the monies used to purchase the Michigan Property came from defrauded investors through the Funds. Because Melody Gilliland has not cited any evidence demonstrating that monies came from another source, she has failed to create a genuine issue of material fact.

in any way in the fraudulent schemes, by having the use of the Michigan Property as a result of her status as the lifetime beneficiary of the Trust, she is benefitting from the fraudulently obtained funds. These facts provide a compelling basis for imposing a constructive trust on the Trust's title to the Michigan Property in favor of Quilling as Receiver.

Melody Gilliland raises two arguments for denying Quilling the relief sought. First, she contends that she gave fair consideration for her interest in the Michigan Property, namely, the release of her interest in the Memphis Property. Second, Melody Gilliland (joined by the Trust) argues that Quilling should not be granted equitable relief because the investors must have known that they were not investing in a legitimate investment enterprise and therefore had unclean hands. The Court rejects both arguments.

Melody Gilliland's argument that she gave fair consideration for her interest in the Michigan Property is rejected for two reasons. First, the argument relies on the law of fraudulent conveyances, which is not at issue in this case. Quilling is seeking the equitable remedy of a constructive trust. While payment of fair consideration for the property in question might be germane to consideration of the equities, fair consideration is not dispositive of whether a constructive trust should be imposed. Second, and perhaps more fundamentally, Melody Gilliland cannot claim that she was a purchaser for value because she did not purchase the Michigan Property. Rather, the Trust purchased the Michigan Property. While Melody Gilliland does have an interest in the Michigan Property by virtue of her status as the lifetime beneficiary of the Trust, her interest is derivative of the Trust, which cannot be a purchaser for value because the Trust purchased the Michigan Property with fraudulently obtained funds.

Melody Gilliland's unclean hands argument is rejected because she has failed to cite any authority for the proposition that naivety equates to unclean hands. Although Melody Gilliland suggests that the investors were as culpable as Gilliland in the fraudulent schemes, she fails to cite any evidence showing that the investors were aware that they were being defrauded. The fact that the Funds promised huge returns does not detract from the fact that the investors were the victims

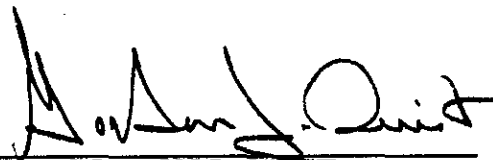
of the fraudulent schemes. Even if the investors were negligent and should have been more wary of an opportunity that promised a return of almost 500% per annum with no risk of principal, the facts remain that Gilliland obtained investors' funds through fraud and Melody Gilliland is a beneficiary of that fraud. See Blachy v. Butcher, 221 F.3d 896, 904 (6th Cir. 2000)(applying Michigan law and holding that a party's negligence would not preclude the remedy of a constructive trust where title was obtained by misleading and deceptive conduct). Moreover, it is the rule in Michigan that "[t]he misconduct which will move a court of equity to deny relief must bear a more or less direct relation to the transaction concerning which complaint is made." McKeighan v. Citizens Commercial & Sav. Bank of Flint, 302 Mich. 666, 671, 5 N.W.2d 524, 527 (1942). "Relief is not denied merely because of the general morals, character or conduct of the party seeking relief." Id. In this case, the investors' conduct did not bear any relationship to the Trust's purchase of the Michigan Property, other than furnishing the funds used in the purchase. Because the Court rejects the arguments raised by Melody Gilliland, the relief sought will be granted.

Conclusion

For the foregoing reasons, the Court will grant Quilling's motion for summary judgment.

An Order consistent with this Opinion will be entered.

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Dated: FEB 28 2002



GORDON J. QUIST
UNITED STATES DISTRICT JUDGE