

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA
CASE NO: 07-22204-CIV-GOLD/TURNOFF (LEAD CASE)

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

CHARLES O. MORGAN, JR., as Personal Representative
of the ESTATE OF FREDERICK J. KUNEN,

Defendant.

_____ /

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

TERRY E. PROVENCE, and DT CAPITAL, LLC,

Defendant.

_____ /

ORDER GRANTING PLAINTIFF AND RECEIVER'S MOTION FOR IMPOSITION OF
CONSTRUCTIVE TRUST ON CERTAIN FUNDS, ASSETS, AND RECORDS OF THE
ESTATE OF FREDERICK J. KUNEN

THIS CAUSE comes before the Court on the Securities and Exchange Commission ("SEC") and Scott M. Dimond's, Court-appointed Receiver for the Estate of Frederick J. Kunen, Motion for Imposition of Constructive Trust on Funds, Assets, and Records of the Estate of Frederick J. Kunen [DE 46]. Neither Defendant nor any of the probate estate creditors upon which a copy of the Motion was served have filed an opposition to the

Motion.¹ I held a hearing on the Motion on Monday, February 11, 2008. Having considered the Motion, the record and relevant case law, and noting that no opposition has been filed, I conclude that the Motion shall be granted.

I. Background

On August 23, 2007, the SEC brought a civil injunctive action against Charles O. Morgan, Jr., as the Personal Representative of the Kunen Probate Estate. (See Complaint, DE 1). In its Complaint, the SEC alleged that from approximately December 2006 until his death on July 11, 2007, Kunen lured primarily inexperienced investors into a risky options trading program by falsely representing the program had a successful ten-year track record, and baselessly promising 10 to 20 percent monthly returns. According to Plaintiff, Kunen spent investor funds on a variety of personal expenses, and lost a significant amount of the remainder of their money in his risky options trading while Kunen profited by approximately \$1 million of the \$2.5 million raised. The Complaint describes Kunen's elaborate scheme of defrauding investors into transferring funds to him as compensation by misrepresenting he had made a profitable return on their behalf. The Complaint also alleges that Kunen failed to disclose to investors that he had been convicted of securities fraud, and subsequently incarcerated for violating his probation by committing bank fraud.

At the time the Complaint was filed, approximately \$751,702 of investor funds

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One of the probate creditors upon which the Motion was served is the Internal Revenue Service ("IRS"). According to Movants, the IRS has filed a tax lien against the Probate Estate in the amount of \$1,726,945.36, which Defendant, the Estate's Personal Representative, has accepted. If the Court does not impose a constructive trust, Movants are concerned that funds that do not properly belong to the Probate Estate will be used to pay the IRS's claim. Despite having been served with the instant Motion, the IRS has not opposed the imposition of the constructive trust.

remained in an E*Trade account under Kunen's name. Plaintiff alleges that Defendant had contacted E*Trade and inquired about the money for the benefit of the Kunen Estate. In order to prevent the further dissipation of investor assets, the SEC sought emergency relief in the form of an asset freeze, and order appointing a Receiver. On August 23, 2007, I issued an Order Appointing Receiver [DE 10], and an Order Freezing Assets and Other Emergency Relief [DE 11]. The order temporarily freezing assets scheduled a Show Cause Hearing on September 4 as to why the Court should not enter an Order Freezing Assets as requested. (See Order Freezing Assets, DE 11 at p. 3).

Prior to the Show Cause Hearing, Defendant filed a Motion to Vacate *Ex Parte* Order Appointing Receiver and *Ex Parte* Order Freezing Assets and Other Emergency Relief [DE 16]. At the September 4 Hearing, Defendant did not defend the allegations of violations of the federal securities laws as alleged in the Complaint, and the parties stipulated that there were no factual disputes as to the affidavits and exhibits filed in this matter. At the conclusion of the hearing, I instructed the parties to file supplemental briefs on the issues raised in the pleadings and at the hearing. In an Order Following Oral Argument [DE 22], I further requested that the parties confer as to how the August 23 Order temporarily freezing assets could be narrowed. Ultimately, upon request by the parties, resolution of Defendant's Motion to Vacate was stayed, and the order temporarily freezing assets remains in full effect.

In the instant motion, the SEC and Receiver (collectively, the "Movants") inform me that the Receiver, the SEC, and Defendant have worked cooperatively to discover, marshal, and preserve funds and assets derived from investors whom Kunen deceived into providing him money by means of misrepresentations and baseless projections. According

to Movants, the parties' joint efforts have lead to the discovery of more than 100 investors who may have a claim on the funds in the Receivership and Probate Estates. To determine the origin of the funds and assets at issue in this case, the SEC retained Andrew R. Kaplan, C.P.A., a forensic account expert to: (1) trace all money in Kunen's financial accounts, as well as all funds that were transferred to and from those various accounts as part of the fraudulent scheme; and, (2) analyze the trades Kunen made on behalf of his investors and the resulting profits and losses from those trades. According to Movants, because Mr. Kaplan's investigation and analysis reveals that certain funds and assets were derived from the defrauded investors for whose benefit the Court created the Receivership, this property is subject to a constructive trust in favor of the Receivership Estate. As noted, neither Defendant nor any of the probate estate creditors have opposed the instant Motion, nor have they objected to the findings of Mr. Kaplan's investigation and analysis.

II. Analysis

In their Motion, Movants seek a constructive trust of approximately \$1.4 million in cash in six bank accounts, nine watches with an approximate value of \$100,000, and a car (collectively, the "Property"), all of which the Movants have traced back to funds from investors Kunen defrauded through a fictitious index options trading program. The six bank accounts have been identified as: (1) E*Trade Account No. 3131-3181; (2) Bank of America Account No. 229005349291; (3) Wells Fargo Account No. 505-1476082; (4) Citibank Gold Checking Account No. 3196006388; (5) Windward Islands Bank, Ltd. Account No. 22589207; and, (6) Deutsche Bank Account No. 4930030110. Movants have also identified nine luxury watches and a car as property that was bought with funds traced to Kunen's fraud. Eight of these watches have been shipped to the Receiver, and are

being held in a Safety Deposit Box.

Movants also seek a declaration that the assets they have shown Kunen took from defrauded investors never properly became part of the Probate Estate. According to Movants, the Receiver is entitled by law to the imposition of a constructive trust over the Property because the Property is the direct proceeds of Kunen's fraudulent options trading scheme. Further, because Kunen was only able to procure the investor proceeds that allowed him to secure the Property by fraud committed before he died and before his Probate Estate arose, Kunen's Probate Estate has no legitimate claim to the Property. The Personal Representative has not opposed the Motion.

A. Jurisdiction

Plaintiff has invoked the Court's federal question jurisdiction. Specifically, this case is before the Court pursuant to Sections 20(b), 20(d) and 22(a) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. §§ 77t(b), 77t(d) and 77v(a); and §§ 21(d) and 27 of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§ 78u(d) and 78aa. As such, the so called Probate Exception to this Court's jurisdiction does not apply. See *Glickstein v. Sun Bank/Miami, N.A.*, 922 F.2d 666, 672 n. 13 (11th Cir. 1991) ("We note that the probate exception is an exception to diversity jurisdiction and has no application to the federal RICO claims."); *Goerg v. Parungao (In re Goerg)*, 844 F.2d 1562, 1565 (11th Cir. 1988) (holding that the Probate Exception only relates to diversity jurisdiction, and has no bearing on federal question jurisdiction).

B. Imposition of a Constructive Trust

Equity recognizes the doctrine of constructive trusts "to right a wrong committed and to prevent unjust enrichment of one person at the expense of another either as a result

of fraud, undue influence, abuse of confidence or mistake in the transaction.” *Kozyak v. Levy (In re Fin. Federated Title & Trust, Inc.)*, 273 B.R. 706, 717-718 (Bankr. S.D. Fla. 2001) (affirmed and adopted by *Levy v. Kozyak (In re Fin. Federated Title & Trust)*, 347 F.3d 880, 881 (11th Cir. 2003)). “The reason for imposing a constructive trust is to avoid unjust enrichment to the recipient of the windfall, and to do equity for the party whose property has been misused.” *Id.* at 718. “The essence of the equitable remedy of imposing a constructive trust ... is the concept that the very property in question can be returned to its rightful owner.” *Id.*

To impose a constructive trust, “there must be an identifiable *res* on which the trust can be impressed.” *Id.* A constructive trust may be imposed both on the original property fraudulently acquired, as well as on the proceeds of the original property. *Id.* Where the original *res* has been transformed into a different form, the party seeking the imposition of the constructive trust bears the burden of tracing the property to specific funds. *Id.* A constructive trust arises in favor of a defrauded party at the time of the fraud, and not at the time of judgment on the party’s fraud claim. *In re Gen. Coffee Corp.*, 828 F.2d 699, 703 (11th Cir. 1987); *Sarasota v. Dixon*, 146 Fla. 369, 378-379 (Fla. 1941) (holding that a constructive trust arose during decedent’s lifetime, and that decedent’s personal representative held the property in trust subsequent to decedent’s death); *Mayer v. Ciancolo*, 463 So.2d 1219, 1221 (Fla. 3d DCA 1985) (finding a constructive trust in favor of son arose when he quitclaimed his joint interest in real property for the sole reason of facilitating its sale by his mother).

Here, imposition of a constructive trust is appropriate to right the fraud committed by Kunen. Through a constructive trust, the Property can be returned to its rightful owners:

the defrauded investors. *Cf. Kozyak*, 273 B.R. at 718. The Movants have identified the specific *res* as funds in six bank accounts, nine luxury watches, and a BMW car. Through a forensic accountant, Movants have traced the funds in the six bank accounts and have established that they were proceeds from Kunen's fraud. In addition, the watches and car should be held in a constructive trust because Movants have demonstrated that these items were purchased with proceeds from Kunen's fraudulent scheme. *Cf. id.* Finally, there is no dispute that the probate estate has no legitimate claim to this Property. Under Florida law, a constructive trust in favor of the defrauded investors was impressed upon the Property at the time that the fraud was committed. *Cf. In re Gen. Coffee Corp.*, 828 F.2d at 703. Since the fraud occurred prior to Kunen's death and the formation of the Probate Estate, the Probate Estate does not have a legitimate claim to funds and assets traceable to Kunen's fraudulent options trading scheme.


III. Conclusion

For the reasons discussed in this Order and at the February 11 Hearing, it is hereby ORDERED AND ADJUDGED:

1. The SEC and Receiver's Motion [DE 46] is GRANTED.
2. A Constructive Trust for the benefit of Kunen's defrauded investors is imposed over all funds derived from Kunen's investors that were ever, or are still, held in:
 - a. E*Trade Account No. 3131-3181;
 - b. Bank of America Account No. 229005349291;
 - c. Wells Fargo Account No. 505-1476082;
 - d. Citibank Gold Checking Account No. 3196006388;

- e. Windward Islands Bank, Ltd. Account No. 22589207; and,
 - f. Deutsche Bank Account No. 4930030110.
3. A constructive trust is further imposed over all other funds or assets purchased with funds derived from defrauded investors whether held, individually or jointly, in the name of Kunen, Kunen's family, his Estate, or the Personal Representative, including the nine (9) watches, and the BMW purchased for Kunen's son.
4. The Receiver shall not distribute the Property without further Order of this Court.

ORDERED AND ADJUDGED in Chambers in Miami, Florida this 11 day of February, 2008.



THE HONORABLE ALAN S. GOLD
UNITED STATES DISTRICT JUDGE

cc:
U.S. Magistrate Judge William C. Turnoff
All counsel of record