



IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

B.A.S.S. GROUP, LLC, and)
JOSEPH H. WEBB, III,)
)
Plaintiffs,)
)
v.) Civil Action No. 3743-VCP
)
COASTAL SUPPLY CO., INC. and)
JOHN M. BURKETT,)
)
Defendants.)

MEMORANDUM OPINION

Submitted: March 2, 2009
Decided: June 19, 2009

Basil C. Kollias, Esquire, Eric M. Andersen, Esquire, COOCH AND TAYLOR, P.A.,
Wilmington, Delaware; *Attorneys for Plaintiffs*

Seth J. Reidenberg, Esquire, THE CHARTWELL LAW OFFICES, LLP; *Attorneys for
Defendant Coastal Supply Co., Inc.*

Mr. John M. Burkett, Milford, Delaware; *Pro Se Defendant*

PARSONS, Vice Chancellor.

This action involves a disloyal employee who embezzled funds from his employer, formed a limited liability company with a friend, and used the embezzled funds to purchase a property on behalf of the LLC. After the employer discovered the embezzlement, it fired the employee and entered into a restitution agreement with him, which included transferring the real estate in question to the employer. The other member of the LLC then commenced this action, individually and derivatively on behalf of the LLC, to void that transfer and to obtain other relief for alleged breaches of fiduciary duties by the member who transferred the property. The employer has counterclaimed for, among other things, unjust enrichment and conversion, and seeks restitution in the form of a constructive trust over the property or some form of monetary judgment.

Both sides in the litigation have filed motions for partial summary judgment. The LLC and the ostensibly innocent member seek summary judgment on their claims to void the transfer of the property to the former employer and for breach of fiduciary duty against the other member of the LLC. The employer requests summary disposition of its counterclaims for unjust enrichment and conversion, including imposition of a constructive trust, if necessary, on the disputed property. For the reasons discussed in this memorandum opinion, I deny the motion of the LLC and its member and grant the employer's motion for judgment in its favor and against the LLC on its unjust enrichment and conversion claims.

I. BACKGROUND

A. The Parties

Plaintiff B.A.S.S. Group, LLC (“BASS”) is a Delaware limited liability company formed by Plaintiff Joseph H. Webb, III and Defendant John M. Burkett on October 22, 2007 to “acquire, own, hold, manage, operate, improve, develop, lease and otherwise deal” with property.¹ Webb and Burkett had been childhood friends and were next-door neighbors during the period relevant to this opinion.² From January 2003 through April 2008, Burkett worked as the controller of Defendant Coastal Supply Co., Inc. (“Coastal”).³ Coastal is a Delaware corporation that manufactures and bags bulk lawn and garden products.⁴ Joseph Kollock, III is the CEO of Coastal and, with his father and brother, Joseph Kollock, Jr. and Jamie Kollock, controls Coastal. The Kollocks are not parties to this action.

¹ Affidavit of Dawn M. Jones in Supp. of Coastal’s Mot. for Summ. J. (“Jones Aff.”) Ex. 5 (“LLC Agreement”).

² Jones Aff. Ex 3, Webb Dep., at 16, 31.

³ Jones Aff. Ex. 2, Burkett Dep., at 4, 60-61.

⁴ Jones Aff. Ex. 1, Deposition of Steven W. Liffers (“Liffers Dep.”), at 16. Liffers is the President of Coastal. *Id.* at 14.

B. Facts

1. The embezzlement

During his tenure as controller of Coastal, Burkett admittedly embezzled over \$2 million from the company.⁵ As Coastal's controller, Burkett was responsible for approving new supply vendors, approving and reviewing payables to vendors and other suppliers, monitoring and adjusting pre-paid vendor accounts,⁶ and replenishing pre-paid accounts as their pre-paid balances were depleted.⁷ Burkett also was responsible for reconciling the actual inventory with the accounting reports.⁸

At some point, Burkett opened a bank account in the name of A & S Services ("A&S") at the Wilmington Trust Company ("Wilmington Trust").⁹ In the spring of 2004, Burkett set up A&S as a pre-paid vendor of Coastal and established an internal account at Coastal to pay A&S.¹⁰ A&S seemingly would perform services for or supply goods to Coastal, and an accounts payable clerk would issue payment to A&S.¹¹ Instead of mailing the checks to A&S, however, Burkett personally would pick up the checks and

⁵ Burkett Dep. at 44, 60.

⁶ *Id.* at 9-10, 41-42, 115.

⁷ Liffers Dep. at 43-44.

⁸ *Id.* at 60-61.

⁹ Burkett Dep. at 40-42, 115.

¹⁰ *Id.* at 41.

¹¹ Liffers Dep. at 64-66; Burkett Dep. at 41-42, 58.

hand-deposit them into the A&S account at Wilmington Trust.¹² Burkett continued this activity until his termination in April 2008.¹³

Burkett embezzled approximately \$2 million via the A&S artifice and, through other methods, such as using Coastal's company credits cards and causing Coastal to write checks directly to Burkett's personal creditors, purloined additional funds from Coastal, allegedly amounting to another \$1 million or so.¹⁴ There is no evidence that any money deposited in the A&S account at Wilmington Trust came from anywhere other than Coastal.¹⁵ Funds from the A&S account were transferred periodically to one of two of Burkett's personal accounts, one at Wilmington Trust and the other at Wilmington Savings Fund Society or WSFS.¹⁶

2. The formation of BASS and the property purchase

In October 2007, Burkett and Webb formed BASS and executed the LLC Agreement.¹⁷ Burkett and Webb agreed to each contribute \$100 in exchange for 100

¹² Liffers Dep. at 64-66; Burkett Dep. at 41-42, 58.

¹³ Burkett Dep. at 115.

¹⁴ Liffers Dep. at 74-76, 87-88; Kollock Dep. at 37, 47-48; Burkett Dep. at 59-60.

¹⁵ *See* Burkett Dep. at 58.

¹⁶ *Id.* at 44, 58.

¹⁷ LLC Agreement § 3.2.

units of ownership interest.¹⁸ Burkett opened a bank account for BASS at WSFS, funding it with \$2,500 from a personal account Burkett maintained at WSFS.¹⁹

Burkett and Webb agreed to have BASS acquire a parcel of land located in Harrington, Delaware (the “Property”), and that Burkett would supply the funds to purchase it. Webb was to handle the development of the Property going forward.²⁰ Further, Burkett and Webb agreed that, upon the sale of the Property, the LLC would repay Burkett for his investment before distributing any profits equally between Webb and Burkett.²¹

On November 21, 2007, Burkett executed an agreement of sale to buy the Property on behalf of BASS.²² The same day Burkett provided the seller with a \$1,000 deposit check (the “Deposit Check”) drawn from his and his wife’s personal checking account at Wilmington Trust.²³ Burkett testified that the money making up the deposit “most likely came out of the A & S account.”²⁴ On January 23, 2008, Burkett delivered a WSFS cashier’s check (the “Cashier’s Check”) to the seller for \$411,972.52, which represented

¹⁸ *Id.* §§ 3.2, 3.3.

¹⁹ Burkett Dep. at 34-35.

²⁰ Webb Dep. at 32; Burkett Dep. at 46.

²¹ Burkett Dep. at 47, 49-50; LLC Agreement §§ 4.4(b), 10.5(a).

²² Burkett Dep. at 27, 35; Webb Dep. at 46.

²³ Burkett Dep. at 36, 38; Jones Aff. Ex. 6 (“Deposit Check”); Webb Dep. at 44.

²⁴ Burkett Dep. at 37-38.

the remaining balance on the purchase price of the Property.²⁵ Burkett funded the Cashier's Check from the same personal Wilmington Trust account from which the Deposit Check was drawn.²⁶ When asked about the source of the \$411,972.52 used to fund the Cashier's Check, Burkett responded: "It all came from the A & S Services account."²⁷ In addition, Webb admitted that he did not contribute any of his own funds to the purchase price of the Property.²⁸

3. Burkett transfers the property to Coastal

On April 8, 2008, after receiving notice from WSFS of suspect activity in the A&S account,²⁹ Coastal discovered that Burkett had been stealing the company's money³⁰ and immediately terminated him.³¹ At a meeting later the same day, Burkett explained his embezzlement scheme to Joseph Kollock III.³² Burkett told Kollock what he did with Coastal's money, and drove Kollock to the Property.³³ Burkett offered to repay Coastal the amount he had stolen by, among other things, transferring the Property purchased by

²⁵ *Id.* at 36, 39-40.

²⁶ *Id.* at 39-40.

²⁷ Burkett Dep. at 39.

²⁸ Webb Dep. at 47, 49, 88.

²⁹ Kollock Dep. at 44-45.

³⁰ Burkett Dep. at 60-61.

³¹ Liffers Dep. at 66.

³² Kollock Dep. at 46; Burkett Dep. at 62-64.

³³ Kollock Dep. at 46-47; Burkett Dep. at 62-64.

BASS to Coastal.³⁴ On April 9, 2008, Burkett and Coastal executed an agreement to transfer the Property from BASS to Coastal as partial restitution for the embezzlement (the “Restitution Agreement”).³⁵ On April 11, 2008, in accordance with the Restitution Agreement, Burkett purported to execute a deed on behalf of BASS transferring the Property to Coastal (the “Deed”).³⁶

Webb and BASS note that, although an attorney for Coastal drafted the Deed,³⁷ neither Coastal nor its attorney examined the LLC Agreement to verify that Burkett had authority to execute such a deed.³⁸ Further, the only consideration referred to in the Deed, which was recorded on April 14, 2008,³⁹ is ten dollars (\$10.00) to be paid from Coastal to BASS.⁴⁰

³⁴ Burkett Dep. at 62-65.

³⁵ Jones Aff. Ex. 8 (“Restitution Agreement”).

³⁶ Jones Aff. Ex. 9 (“Deed”); Burkett Dep. at 71.

³⁷ PAB at 3, citing Deed. DOB, PAB, and DRB refer to the opening, answering, and reply briefs, respectively, related to Defendant Coastal’s motion for summary judgment. Similarly, POB, DAB, and PRB refer to the briefs regarding Plaintiffs’ motion for summary judgment. The Deed appears from its face to have been drafted by Young Conaway Stargatt & Taylor, LLP, the firm which represented Coastal in this action.

³⁸ Liffers Dep. at 78.

³⁹ POB at 3, citing Compl. ¶ 6.

⁴⁰ Deed at 1.

C. Procedural History

On May 6, 2008, Webb filed his Complaint in this action. Count I seeks to void the April 11, 2008 transfer of the Property from BASS to Coastal. Count II alleges Burkett breached his fiduciary duty by participating in that transfer. Count III accuses Coastal of aiding and abetting Burkett's breach of fiduciary duty.

On May 30, 2008, Coastal answered and brought several counterclaims against Plaintiffs. Counts I to IV assert claims against at least BASS and arguably Webb for unjust enrichment, conversion, civil conspiracy and aiding and abetting conversion, respectively. Count V seeks an equitable accounting. Based on its Counterclaims, Coastal requests the imposition of a constructive trust over the Property, restitution in the amount of \$412,972.52 plus interest, a declaration that legal title to the Property remains with Coastal, and an accounting for all money used by BASS with respect to the Property.⁴¹

On January 23, 2009, Webb and BASS brought a Motion for Partial Summary Judgment on Counts I and II of their Complaint, which challenge the validity of the transfer and assert a breach of fiduciary duty. By way of remedy, Webb and BASS seek

⁴¹ On June 16, 2008, BASS and Webb filed their reply to the Counterclaims. On August 7, 2008, Burkett filed a "Reply to Complaint," in which he requested that Webb be allowed a "[r]easonable period of time to obtain financing to reimburse Coastal." Reply to Complaint at 2. As to the competing motions for summary judgment presently before the Court, Burkett has been proceeding pro se, and did not submit any papers in connection with either of them.

(i) to void the transfer of the Property to Coastal, (ii) to have Burkett removed as a member of BASS, and (iii) to have Burkett's contributions to BASS forfeited.

Also on January 23, 2009, Coastal filed a Motion for Summary Judgment on Count I of its Counterclaim for unjust enrichment and Count II for conversion. Coastal urges the Court to impose a constructive trust over the stolen funds or the Property. On March 3, I heard argument on the cross-motions for summary judgment. During the argument, I requested supplemental submissions on Coastal's status as a bona fide purchaser for value, which the parties promptly supplied.

D. Parties' Contentions

Coastal seeks summary judgment on two counts of its Counterclaim. Count I alleges Webb and BASS have been unjustly enriched and Count II charges that Webb and BASS converted Coastal property. By way of remedy, Coastal seeks the imposition of a constructive trust over the stolen funds and any property that can be traced to those funds.

Webb has moved, in his personal capacity and on behalf of BASS, to void the transfer of the Property to Coastal that was effected pursuant to the Restitution Agreement between Burkett and Coastal. Coastal counters that, among other things, there are issues of fact regarding Burkett's authority to transfer the Property that would preclude summary judgment. Webb also seeks to have Burkett removed as a member of BASS and to have Burkett's contributions to BASS forfeited.

II. ANALYSIS

A. Standard

“Summary judgment is granted if the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.”⁴² When considering a motion for summary judgment, the evidence and the inferences drawn from it are to be viewed in the light most favorable to the nonmoving party.⁴³ The Court also “maintains the discretion to deny summary judgment if it decides that a more thorough development of the record would clarify the law or its application.”⁴⁴ Thus, for example, summary judgment will be denied when the legal question presented needs to be assessed in the “more highly textured factual setting of a trial.”⁴⁵

The procedural posture here is somewhat unusual in that there are competing motions for summary judgment, but the motions technically are not cross-motions of the

⁴² *Twin Bridges L.P. v. Draper*, 2007 WL 2744609, at *8 (Del. Ch. Sept. 14, 2007) (citing Ct. Ch. R. 56(c)).

⁴³ *Judah v. Del. Trust Co.*, 378 A.2d 624, 632 (Del. 1977).

⁴⁴ *Tunnell v. Stokley*, 2006 WL 452780, at *2 (Del. Ch. Feb. 15, 2006) (quoting *Cooke v. Oolie*, 2000 WL 710199, at *11 (Del. Ch. May 24, 2000)).

⁴⁵ *Schick, Inc. v. Amalgamated Clothing & Textile Workers Union*, 533 A.2d 1235, 1239 n.3 (Del. Ch. 1987) (citing *Kennedy v. Silas Mason Co.*, 334 U.S. 249, 257 (1948)).

type contemplated by Court of Chancery Rule 56(h).⁴⁶ Nevertheless, the disposition of one side's motion may impact the other's. Accordingly, I proceed by first examining Webb and BASS's motion for summary judgment as to the property transfer from BASS to Coastal, challenged in Counts I and II of Plaintiffs' Complaint. I then address Coastal's motion as to Counts I and II of its Counterclaims, regarding Plaintiffs' alleged unjust enrichment and conversion.

B. Are Webb and BASS Entitled to Summary Judgment Voiding the Transfer to Coastal?

Plaintiffs maintain that the transfer from BASS to Coastal is void or voidable, because (i) Burkett did not have authority to transfer the Property, (ii) BASS did not receive any consideration for the transfer, and (iii) the Deed is defective on its face.

1. Authority

Webb maintains that Burkett had no authority to transfer the Property to Coastal, so the transfer should be voided. This case involves both actual and apparent authority. "Actual authority is that authority which a principal expressly or implicitly grants to an agent."⁴⁷ When an agent commits acts with actual authority, the "principal is bound by

⁴⁶ Under Rule 56(h), where the parties have cross moved for summary judgment and have not presented argument that there is an issue of fact material to the disposition of either motion, "the Court shall deem the motions to be the equivalent of a stipulation for decision on the merits based on the record submitted with the motion." Ct. Ch. R. 56(h).

⁴⁷ *Albert v. Alex. Brown Mgmt Servs., Inc.*, 2005 WL 2130607, at *10 (Del. Ch. Aug. 26, 2005) (citation omitted).

the legal consequences of the agent's action."⁴⁸ Here, Webb maintains that to transfer the Property the LLC Agreement required the consent of both Webb and Burkett.⁴⁹ Section 7.1 of the BASS LLC Agreement states, in relevant part:

Except with the consent of a majority of the Members, in terms of their Company interests, no Member shall be authorized and empowered, on behalf of the Company to:

- (a) Borrow (from any Member or third party); or (b) lend money; or (c) make, deliver, or accept any commercial papers; or (d) execute any mortgage, bond or lease (for a period in excess of one (1) month including rights of renewal or extension), deed or release; (e) purchase or contract to purchase, or sell or contract to sell any property; or (f) compromise or release any of the Company's claims or debts
-

Webb did not consent; therefore, Webb argues, Burkett had no actual authority to transfer the Property.

Webb also maintains that nothing in § 7.3 of the LLC Agreement confers authority on Burkett to transfer the Property. Section 7.3 states in relevant part:

7.3 Power of Attorney. Each of the Members constitutes and appoints John Matthew Burkett (hereinafter "Authorized Person") his true and lawful attorney, in his name, place and stead, to make, execute, acknowledge, deliver and record the following:

- a. Any certificate or other instrument which may be required by any governmental authority, or which the Authorized Person may deem necessary or appropriate for purposes of the Company, including, but not limited to, the Certificate and any amendments or modifications thereto;

⁴⁸ *Restatement (Third) of Agency* §4.01 Introductory Note (2006).

⁴⁹ LLC Agreement § 7.1.

b. All instruments which the Authorized Person deems necessary or appropriate to implement any amendment, change or modification of the Company in accordance with the terms of this Agreement

. . .

Each Member agrees to be bound by any representation made by the Authorized Person, acting in good faith pursuant to such power of attorney, and each Member waives any and all defenses which may be available to contest, negate or disaffirm the action of the Authorized Person taken in good faith under such power of attorney.

Webb admits that Burkett was an “Authorized Person” within § 7.3, but contends that Burkett did not act in “good faith,” because he transferred the Property solely for his own benefit, rather than for the benefit of BASS. In response, Coastal contends that Burkett did act in “good faith,” because he “protected BASS from potential liability for the tort of conversion and from potential criminal prosecution for retaining stolen property.”⁵⁰

Hence, whether Burkett had actual authority depends on whether he acted in good faith in transferring the Property to Coastal. In Delaware, much ink has been spilt analyzing the concept of good faith.⁵¹ The parties, and in particular BASS and Webb,

⁵⁰ DAB at 14.

⁵¹ See, e.g., 8 *Del. C.* § 102(b)(7); *Lyondell Chem. Co. v. Ryan*, 970 A.2d 235, 240 (Del. 2009); *Stone v. Ritter*, 911 A.2d 362, 367-371 (Del. 2006); *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 62-67 (Del. 2006); 6 *Del. C.* § 1-201(20) (defining good faith for Delaware’s Uniform Commercial Code as “honesty in fact and the observance of reasonable commercial standards of fair dealing”); 12 *Del. C.* § 3580 (defining “good faith” in the trust context as “honesty in fact and observance of reasonable standards of fair dealing”); see also R. Franklin Balotti et al., *Loyalty’s Core Demand: The Defining Role of Good Faith in Corporation Law* (Widener Law Sch. Legal Stud. Res. Paper No. 09-13, 2009), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1349971; David Rosenberg,

have provided little guidance as to the meaning of “good faith” in this context. Borrowing from the corporate realm, for example, I note that a fiduciary “does not act in good faith if the [fiduciary] acts with a subjective belief that her actions are not in the best interest of the corporation, such as when she is acting for the benefit of a related person at the expense of the company.”⁵² In this case, there are disputed issues of fact concerning Burkett’s state of mind, as well as the reasonableness of his actions with respect to the Property transfer to Coastal, that preclude summary judgment.⁵³ The fact that a more contextually specific definition of “good faith” possibly should apply further supports the denial of Plaintiffs’ motion for summary judgment, because “a more thorough development of the record would clarify the law or its application.”⁵⁴

Even in the absence of actual authority, however, Coastal maintains that Burkett still had apparent authority to transfer the Property. “Apparent authority is that authority which, though not actually granted, the principal knowingly or negligently permits an

Making Sense of Good Faith in Delaware Corporate Fiduciary Law: A Contractarian Approach, 29 Del. J. Corp. L. 491 (2004); John L. Reed & Matt Neiderman, *Good Faith and the Ability of Directors to Assert § 102(b)(7) of the Delaware General Corporation Law as a Defense to Claims Alleging Abdication, Lack of Oversight, and Similar Breaches of Fiduciary Duty*, 29 Del. J. Corp. L. 111 (2004).

⁵² *Kahn v. Portnoy*, 2008 WL 5197164, at *7 (Del. Ch. Dec. 11, 2008).

⁵³ For the same reasons, I deny summary judgment as to Webb and BASS’s claim for breach of fiduciary duty.

⁵⁴ *Tunnell v. Stokley*, 2006 WL 452780, at *2 (Del. Ch. Feb. 15, 2006) (quoting *Cooke v. Oolie*, 2000 WL 710199, at *11 (Del. Ch. May 24, 2000)).

agent to exercise, or which he holds him out as possessing.”⁵⁵ To find apparent authority, the party seeking to show the existence of such authority must “show reliance on indicia of authority *originated by the principal*, and such reliance must have been reasonable.”⁵⁶ Where a “third party relies on the agent’s apparent authority in good faith and is justified in doing so by the surrounding circumstances, the principal is bound to the same extent as if actual authority had existed.”⁵⁷

Whether the current record provides a sufficient basis for a finding of apparent authority is debatable. Perhaps, Coastal reasonably could have thought that Burkett had authority, but that argument only goes half way. It is less clear whether the record indicates that Coastal relied upon anything BASS (or even Webb) did or did not do in forming its arguably reasonable belief that Burkett had authority to transfer the Property. Indeed, Coastal maintains it did not know that Webb was a member of BASS and did not ask for or examine a copy of the LLC Agreement until after it obtained the Deed. To some degree, at least, Burkett controverts that assertion. Accordingly, Coastal may have a difficult time proving a defense of apparent authority at trial. Still, because there is a factual dispute precluding summary judgment on the issue of actual authority and factual

⁵⁵ *Alex. Brown*, 2005 WL 2130607, at *10 (citations omitted).

⁵⁶ *Id.* (emphasis added).

⁵⁷ *Old Guard Ins. Co. v. Kimmy’s Grille, Inc.*, 860 A.2d 811, 2004 WL 2154286, at *3 (Del. Sept. 21, 2004) (TABLE).

disputes appear to exist on the issue of apparent authority, as well, I conclude that the question of Burkett's authority cannot be resolved at the summary judgment stage.

2. Valid consideration

Webb and BASS also maintain that the Property transfer is void for invalid consideration. The Deed states that Coastal paid ten dollars for the Property, but Webb claims the ten dollars never made its way to BASS. A court of equity, however, often looks past the terms of an agreement and gives effect to the actual intent of the parties.⁵⁸ Taking all inferences in favor of the nonmoving party, as I must, it is possible the consideration for the Property transfer involved not only the ten dollars, but also consideration flowing from the Restitution Agreement, to which BASS was a putative party.⁵⁹ Thus, this argument implicates some of the same considerations as the actual

⁵⁸ See, e.g., *Justice v. D & R Builders*, 1978 WL 2513, at *3 (Del. Ch. Jan. 18, 1978) (holding that extrinsic evidence supported view that consideration consisted of more than that described in deed).

⁵⁹ Webb also contends the Deed is defective in that it lists the grantor as "B.A.S.S. Group, LLC as Trustee under a constructive trust agreement U/A/D/ April 9, 2009" Deed at 1. Webb asserts: "Private persons cannot create constructive trusts." POB at 7 (citing *Nash v. Schock*, 1997 WL 770706 (Del. Ch. Dec. 3, 1997), *aff'd and remanded*, 737 A.2d 217 (Del. 1999)). Neither of the cited opinions, however, directly states such a rule of law. Webb also offers some technical objections to the existence of a trust or trustee based on, among other things, the lack of a trust instrument. Nevertheless, a constructive trust is not really a trust at all, but rather a concept that uses trust language metaphorically and by analogy. See 1 Dobbs *Law of Remedies* § 4.3 (2d ed. 1993). Likewise, whether a constructive trust automatically arises when the property involved is wrongfully acquired or arises solely upon a court's imposition of it as a remedy remains an unsettled point of law. See George Gleason Bogert et al., *The Law of Trusts and Trustees* § 472 (2008).

authority issue discussed in Part II.B.1 *supra*. Accordingly, I deny Plaintiffs' motion for summary judgment on the basis of invalid consideration.

C. Is Coastal Entitled to Summary Judgment on its Claim for Unjust Enrichment?

Coastal has moved for summary judgment on Count I of its Counterclaim for unjust enrichment. By way of remedy, Coastal seeks the imposition of a constructive trust or money damages. The elements of unjust enrichment are: "the unjust retention of a benefit to the loss of another, or the retention of money or property of another against the fundamental principles of justice or equity and good conscience."⁶⁰ In other words, courts look for: (1) an enrichment; (2) an impoverishment; (3) a relation between the enrichment and the impoverishment; (4) the absence of justification; and (5) the absence of a remedy provided by law.⁶¹

The claim that BASS was unjustly enriched when Burkett supplied embezzled funds to it requires little discussion. BASS was enriched by Burkett's wrongful actions.

⁶⁰ *Schock v. Nash*, 732 A.2d 217, 232 (Del. 1999).

⁶¹ *Oliver v. Boston Univ.*, 2000 WL 1091480, at *9 (Del. Ch. July 18, 2000) (citations omitted). In the circumstances of this case, where subject matter jurisdiction exists over the unjust enrichment claim under at least the clean-up doctrine, the existence or absence of the fifth element, an adequate remedy at law, is immaterial. Depending on the circumstances, unjust enrichment can be thought of as either a legal or an equitable claim. In *Crosse v. BCBSD, Inc.*, the Delaware Supreme Court held that the Superior Court could award relief for an unjust enrichment claim, when unjust enrichment served as an alternate theory of recovery for a contract claim. 836 A.2d 492, 496-97 (Del. 2003); *see also Testa v. Nixon Uniform Serv., Inc.*, 2008 WL 4958861, at *3 n.23 (Del. Ch. Nov. 21, 2008) (embracing the proposition that a claim for unjust enrichment by itself does not invoke this court's subject matter jurisdiction).

Coastal suffered impoverishment as a result of those same actions. In addition, there was no justification for BASS's enrichment or Coastal's impoverishment.

At the core of his argument, Webb contends that he and BASS were innocent parties and, thus, should not be penalized for Burkett's acts.⁶² I find that argument unpersuasive for two reasons. First, the knowledge of an officer, director, or manager of a business entity generally is imputed to the entity.⁶³ Second, the Delaware Supreme Court has held that "[r]estitution is permitted even when the [party] retaining the benefit is not a wrongdoer."⁶⁴

The remaining question is what remedy should be imposed to rectify BASS's unjust enrichment.⁶⁵ Plaintiffs urge this Court to impose a constructive trust over the

⁶² The evidence presented on the pending motions is not sufficient to support summary judgment as to whether Webb personally was unjustly enriched, in part because Webb never owned the Property. Webb had, at best, an indirect interest in the Property through his ownership interest in BASS. Depending on the surrounding circumstances, Webb's ownership interest conceivably could make him personally liable for any benefit he personally received as a result of Burkett's contribution or loan of over \$412,000 to BASS. The facts and law related to that issue will need to be developed further at trial.

⁶³ *Triton Constr. Co. v. E. States Elec. Servs.*, 2009 WL 1387115, at *16 n.94 (Del. Ch. May 18, 2009) (citations omitted).

⁶⁴ *Schock*, 732 A.2d at 232.

⁶⁵ Webb suggests in his papers that a charging order upon Burkett's units in BASS for the benefit of Coastal would be adequate. PAB at 8, citing 6 *Del. C.* § 18-703. Section 18-703 provides that a judgment creditor "may charge the limited liability company interest of the judgment debtor to satisfy the judgment." According to Webb, that would enable him to develop the property, and Coastal could participate in any income generated by his efforts. Because BASS was unjustly enriched, I do not consider a charging order in favor of BASS on Burkett's units

embezzled funds contributed to BASS and any property, including the Property, into which those funds have been converted. For the most part, I agree with Coastal.⁶⁶ The typical remedy for unjust enrichment is restitution.⁶⁷ A constructive trust is simply a form of restitution in specie.⁶⁸

alone to be an adequate remedy. Moreover, a charging order would leave Coastal as a holder of at least fifty-percent of the economic interest in BASS but without any voting rights and at the mercy of a controlling member who Coastal has been engaged in litigation with for several years. *See* 6 *Del. C.* § 18-703 (providing that with a charging order a judgment creditor would have rights of an assignee); 6 *Del. C.* § 18-702 (“[A]n assignee of a member’s limited liability company interest shall have no right to participate in the management of the business and affairs of a limited liability company . . .”). In the circumstances of this case, that prospect is objectively unattractive and untenable.

⁶⁶ The posture of this case vis-à-vis a constructive trust is somewhat unusual. Typically, a wronged plaintiff would seek a constructive trust over property held by a defendant who was unjustly enriched. Here, Coastal currently holds title to the disputed Property and has possession over it. If that situation continues, Coastal may not need a constructive trust over the Property. That is, if the Court upholds the transfer of the Property from BASS to Coastal, addressed *supra* Part II.B, then Coastal may be able to keep the Property. Conversely, if the Court voids the transfer for any of the reasons Webb advanced, I likely would impose a constructive trust over the Property in the possession of BASS based on my finding of unjust enrichment.

⁶⁷ 1 Dobbs, *Law of Remedies* §4.1(1) at 553 (2d ed. 1993) (“One whose money or property is taken by fraud or embezzlement, or by conversion, is entitled to restitution.”); *see also* *Adams v. Jankouskas*, 452 A.2d 148, 152 (Del. 1982) (“[A] constructive trust does not arise from the presumed intent of the parties, but is imposed when a defendant’s fraudulent, unfair or unconscionable conduct causes him to be unjustly enriched at the expense of another to whom he owed some duty.”); *Jackson Nat. Life Ins. Co. v. Kennedy*, 741 A.2d 377, 394 (Del. Ch. 1999) (“Having pleaded sufficiently the allegations . . . that [defendant] aided and abetted [an] alleged breach of fiduciary duty to a degree sufficient to defeat this motion, it is axiomatic that Plaintiffs have likewise pleaded sufficiently the allegations that Defendants were enriched by their actions If Plaintiffs succeed on the merits of their breach of fiduciary duty and aiding and abetting

A constructive trust may be imposed “upon specific property [or] identifiable proceeds of specific property, and even money so long as it resides in an identifiable fund to which the plaintiff can trace equitable ownership.”⁶⁹ If the unjustly obtained funds can be traced into specific property, then a constructive trust can be imposed on the property, regardless of the culpability of the party possessing the property, provided that the person or entity that received the funds was not a bona fide purchaser for value.⁷⁰

claims, it is likely they will also be able to prove that neither Kennedy nor Fort James can retain any benefit resulting from the disputed transaction ‘justifiably’ or in accordance with ‘the fundamental principles of justice or equity and good conscience.’ Plaintiffs, therefore, properly state an actionable claim for unjust enrichment and imposition of a constructive trust.”); *Nash v. Schock*, 1998 WL 474161, at *2 (Del. Ch. July 23, 1998) (“Constructive trusts are regularly imposed by courts of equity to remedy unjust enrichment.”), *aff’d* 732 A.2d 217 (Del. 1999); *Restatement (Second) of Restitution* § 1 (Draft 1983) (“A person who receives a benefit by reason of an infringement of another person’s interest, or of loss suffered by the other, owes restitution to him in the manner and amount necessary to prevent unjust enrichment.”).

⁶⁸ Wolfe and Pittenger, *Corporate and Commercial Practice in the Delaware Court of Chancery* §12.07(a) (2008) (“Constructive and resulting trusts are appropriate where, *in the absence of a valid, written agreement of trust*, equity requires a judicially imposed trust to remedy unjust enrichment.”) (emphasis added); 2 Dobbs *Law of Remedies* § 6.1(3) (2d ed. 1993) (“The idea is that the plaintiff’s property has been found in the hands of the defendant and must be restored to the plaintiff, even if legal title has passed, and even if the property has undergone a change in form by reason of exchange or otherwise.”).

⁶⁹ Wolfe and Pittenger, *supra* note 69, § 12-7[b] at 12-75, 76.

⁷⁰ *See Schock*, 732 A.2d at 232 (“Restitution is permitted even when the defendant retaining the benefit is not a wrongdoer.”); *Smith v. Smitty McGee’s, Inc.*, 1998 WL 246681, at *7 (Del. Ch. May 8, 1998) (“In a court of equity even if the [the former wife of defendant] may be free of wrongdoing, she can be ordered to make restitution to [the injured plaintiff] of any assets [her former husband, the defendant] obtained through his wrongdoing and then transferred to her.”); *see*

Here, the funds embezzled from Coastal can be traced directly to the Property. Burkett testified that the money went from Coastal to the A&S account at Wilmington Trust to his personal account at Wilmington Trust and then to a Cashier's Check Burkett caused to be furnished to the seller of the Property on behalf of BASS. In addition, Webb and BASS have not disputed that the funds can be traced to the Property.

Moreover, BASS was not a bona fide purchaser for value of the embezzled funds. As the Delaware Supreme Court recently stated, a "bona fide purchaser is one who acquires legal title to property in good faith, for valuable consideration, and without notice of any other claim of interest in the property."⁷¹ Admittedly, a factual dispute appears to exist as to the proper characterization of the transfer of the embezzled funds from Burkett to BASS. The dispute centers on whether BASS paid any valuable consideration for the funds and whether the funds were made as a loan or a capital contribution to BASS. I need not decide those issues, however, because they are largely

also Schock, 732 A.2d at 233-34 (permitting the imposition of a constructive trust on the car belonging to the daughter of the wrongdoer because "the proceeds of the constructive trust placed on the annuity that was illegally cashed in by [the wrongdoer] were used to purchase the automobile"); Austin Wakeman Scott & William Franklin Fratcher, *Scott on Trusts* § 470 (4th ed. 1989) ("Where a person holding property transfers it to another in violation of his duty to a third person, the third person can reach the property in the hands of the transferee, unless the transferee is a bona fide purchaser The cases involving transfers of property in fraud of creditors of the transferor are legion The transferee in these cases will not be permitted to retain the property as against the defrauded creditors unless he is in the position of a bona fide purchaser. The transferee holds the property upon a constructive trust for the creditors.").

⁷¹ *Fletcher v. City of Wilm. UDAG*, 905 A.2d 746, 2006 WL 2335237, at *2 (Del. Aug. 11, 2006) (TABLE) (citation and internal quotation marks omitted).

immaterial. There is no dispute that Burkett purchased the Property with the embezzled funds on behalf of BASS. Thus, BASS and Burkett are equally culpable in this situation. Burkett was acting for and on behalf of BASS in purchasing the Property; therefore, Burkett's state of mind can be imputed to BASS.⁷² Thus, even if Webb had no notice that the funds had been embezzled, BASS did have notice. Consequently, BASS cannot be a bona fide purchaser for value.

On this basis, even if the Property transfer from BASS to Coastal were voidable, principles of unjust enrichment and constructive trust would dictate that the Property either should be transferred to Coastal or held by BASS subject to a constructive trust for the benefit of Coastal at least until such time as Coastal has been made whole. There is, however, a question of who should capture the upside of the Property, assuming there is any upside after repayment to Coastal of the full amount Burkett contributed to BASS plus interest. The parties did not address that issue in any detail in the context of the pending motion. Further, the Court's decision on the precise parameters of a constructive trust may depend on additional facts likely to be the subject of the parties' evidence at trial on the issues not resolved or not even addressed in the pending motions for partial summary judgment.

⁷² Delaware courts consistently have imputed to a corporation the knowledge of an officer or director of the corporation when acting on its behalf. *See, e.g., Teachers' Retirement System of La. v. Aidinoff*, 900 A.2d 654, 671 n.23 (Del. Ch. 2006) (citing *Carlson v. Hallinan*, 2006 WL 771722, at *21 (Del. Ch. Mar. 21, 2006); *In re HealthSouth Corp. S'holders Litig.*, 845 A.2d 1096, 1108 n.22 (Del. Ch. 2003)). I see no reason why the rule would be any different for a member of an LLC who has management rights.

D. Is Coastal Entitled to Summary Judgment on its Claim for Conversion?

Coastal also seeks summary judgment on its conversion claim. Conversion is defined as the “act of dominion wrongfully exerted over the property of another, in denial of his right, or inconsistent with it.”⁷³ Coastal ultimately must prove that: it had a property interest in equipment or other property; it had a right to possession of the property; and the property was converted.⁷⁴ For reasons discussed in connection with Coastal’s claim for unjust enrichment, Coastal also is entitled to summary judgment on its claim for conversion of the embezzled funds contributed to BASS, and then used to purchase the Property. The remedy would include, at least, a damage award against BASS of \$412,972.52 plus interest at the legal rate from the date those funds were contributed to BASS.⁷⁵

III. CONCLUSION

For the reasons stated in this memorandum opinion, I hold that Coastal is entitled to summary judgment at least against BASS on the unjust enrichment and conversion counts of Coastal’s Counterclaims. Such a result entitles Coastal to the imposition of a

⁷³ *McGowan v. Ferro*, 2004 WL 2423570, at *19 (Del. Ch. Oct. 8, 2004) (quoting *Arnold v. Soc’y for Sav. Bancorp, Inc.*, 678 A.2d 533, 536 (Del. 1996)).

⁷⁴ *Facciolo Constr. Co. v. Bank of Del.*, 514 A.2d 413, 1986 WL 17356, at *2 (Del. Aug. 12, 1986) (TABLE).

⁷⁵ As with the claim for unjust enrichment, whether or not Webb would be liable jointly and severally or whether he might be liable for any deficiency should the Property not satisfy the judgment involves issues of fact and law that can best be determined after a more thorough development of the record at trial.

constructive trust over the funds and the Property at least until such time as it has been paid back the \$412,972.52 in embezzled funds used by BASS plus interest at the legal rate, compounded quarterly.⁷⁶ In all other respects, I deny Coastal's motion for partial summary judgment without prejudice. Hence, the propriety of any additional relief against BASS, Webb, or both will have to be addressed after trial in connection with the remaining claims and counterclaims in this action. I also deny Webb's motion for partial summary judgment, because there are genuine issues of material fact with respect to Burkett's authority to act on behalf of BASS and whether he breached any fiduciary duty to BASS or Webb.

IT IS SO ORDERED.

⁷⁶ See *In re PNB Holding Co. S'holders Litig.*, 2006 WL 2403999, at *33 (Del. Ch. Aug. 18, 2006). There may be a question as to who should capture the upside of the Property, assuming there is any upside, after repayment to Coastal of the full amount Burkett contributed to BASS plus interest. Of course, there may not be any such upside at all. If there is, however, the parties have not yet addressed the precise mechanics of how the upside would be distributed. Therefore, I express no opinion on that issue here, and will consider it further, if necessary, in the context of the trial.