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SUPERIOR COURT OF ARIZONA

MARICOPA COUNTY

ML SERVICING CO., INC., an Arizona 10 corporation; and ML LIQUIDATING TRUST, 11 Plaintiffs, 12 13 GERALD K. SMITH, as Trustee for 14 THE COLES CHILDREN'S TRUST; HALEY BROOKE COLES, an 15 individual; FRANCINE COLES, individually and as conservator for Z.A. 16 COLES and S.B. COLES, minors; JOHN AND JANE DOES 1-30; BLACK 17 CORPORATIONS 1-30; WHITE PARTNERSHIPS 1-30; and GRAY 18 TRUSTS 1-30, 19 Defendants. 20

No. CV2011-005890

COMPLAINT

(Unjust Enrichment, Fraudulent Transfer, Constructive Trust, Wrongful Distribution, Aiding and Abetting Conversion, Aiding and Abetting Breach of Fiduciary Duty)

For their Complaint, Plaintiffs, ML Servicing Co., Inc. and ML Liquidating Trust

alleges as follows:

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GENERAL ALLEGATIONS

- 1. Plaintiff, ML Servicing Co., Inc. ("Plaintiff") is an Arizona corporation that was formerly known as Mortgages, Ltd. ("ML").
- 2. Plaintiff ML Liquidating Trust is a liquidating trust that is organized under the laws of Arizona and the owner of Plaintiff.
- ML Liquidating Trust was created as part of the Chapter 11 Plan of Reorganization for ML, which was approved by the United States Bankruptcy Court for the District of Arizona on May 20, 2009.
- 4. Pursuant to the Chapter 11 Plan of Reorganization for ML, ML Servicing Co., Inc. and ML Liquidating Trust are authorized to prosecute the claims asserted herein.
- 5. Upon information and belief, each of the Defendants received proceeds from life insurance policies in which Scott Coles was the insured party.
- 6. Upon information and belief, Defendant Gerald K. Smith is the Trustee for The Coles Children's Trust and he resides in Maricopa County, Arizona.
- 7. Upon information and belief, The Coles Children's Trust is a trust created by Scott Coles for the benefit of his children.
- 8. Upon information and belief, Defendant Haley Coles is a single woman residing in Maricopa County, Arizona.
 - 9. Defendant Haley Coles is Scott Coles' daughter.
- 10. Upon information and belief, Defendant Francine Coles is a single woman residing in Maricopa County, Arizona.
- 11. Upon information and belief, Defendant Francine Coles is the mother of and the conservator for Z.A. Coles and S.B. Coles, who are Scott Coles' children.
- 12. The true names of all John Doe, Jane Doe, Black Corporation, White Partnership, and Gray Trust Defendants are unknown to Plaintiff at the time of the filing of this Complaint,

and Plaintiff, therefore, sues them through fictitious names. Plaintiff will ask leave of Court to amend this Complaint to reflect the true names of these unknown Defendants if and when they have been ascertained.

13. Jurisdiction is proper pursuant to A.R.S. § 12-123.

THE LIFE INSURANCE POLICIES

- 14. For more than 40 years, ML was a private mortgage broker and lender before an involuntary petition for relief under Chapter 11 of the United States Bankruptcy Code was filed by some of ML's creditors in 2008.
 - 15. In the years prior to ML's bankruptcy it was owned by SMC Revocable Trust.
- 16. Before 2006, Scott Coles became ML's Chief Executive Officer and he continued to serve in that capacity until his death on June 2, 2008.
- 17. By no later than 2008, ML's financial condition had deteriorated to the point that it was insolvent and lacked sufficient funds to pay its investors and to fund substantial loans that ML had committed to fund.
- 18. In the wake of ML's imminent collapse, on or about June 2, 2008, Scott Coles committed suicide.
- 19. In the two years preceding Scott Coles' suicide, with ML's financial condition rapidly deteriorating and during a time when ML was insolvent, SMC Revocable Trust caused ML to transfer funds to SMC Revocable Trust, for the purpose of paying life insurance premiums on life insurance policies under which Scott Coles was the insured ("the Life Insurance Policies").
- 20. Upon information and belief, the SMC Revocable Trust was established by Scott Coles.
 - 21. SMC Revocable Trust was at all relevant times, a shareholder of ML.

- 22. Upon information and belief, Scott Coles falsely represented to ML that he was purchasing "key man" or other life insurance policies on himself for the benefit of ML.
- 23. By accepting the transfer of funds for the purpose of paying premiums on the Life Insurance Policies, SMC Revocable Trust was taking funds from an insolvent or soon to be insolvent corporation for the benefit of the Defendants who were the beneficiaries of those Life Insurance Policies.
 - 24. ML was not a beneficiary under any of the Life Insurance Policies.
- 25. The annual premiums for the Life Insurance Policies exceeded \$130,000 and those premiums were paid using money that SMC Revocable Trust caused ML to transfer to SMC Revocable Trust for the purpose of paying those premiums.
- 26. Upon information and belief, the proceeds of the Life Insurance Policies totaled over \$60 million.
- 27. Upon information and belief, some or all of the \$60 million in proceeds from the Life Insurance Policies was paid to Defendants.
- 28. Plaintiffs did not receive any proceeds from the Life Insurance Policies even though ML's money was used to pay the premiums for the Life Insurance Policies.
- 29. Plaintiffs did not and reasonably could not have discovered as a result of the Defendants receiving any payments under the Life Insurance Policies until mid-2009.

<u>COUNT I – UNJUST ENRICHMENT</u>

- 30. Plaintiffs reallege and incorporate by reference the allegations set forth in the preceding paragraphs as if fully set forth herein.
- 31. ML was impoverished as a result of Scott Coles causing ML to pay the premiums on the Life Insurance Policies instead of purchasing key man or other life insurance policies, under which ML was the beneficiary.

- 32. ML received no benefit as a result of SMC Revocable Trust causing ML to pay the premiums on the Life Insurance Policies and as an insolvent corporation, ML owed fiduciary duties to its creditors and investors to refrain from making transfers to Scott Coles or other insiders.
- 33. Because SMC Revocable Trust caused ML to transfer the funds that were used to pay the Life Insurance Policy premiums, ML did not gratuitously or voluntarily pay those premiums for the benefit of Scott Coles or any of the Defendants.
- 34. Defendants were unjustly enriched by receiving the proceeds from the Life Insurance Policies.
- 35. Defendants gave no value to ML in exchange for the benefits they received from the Life Insurance Policies.
 - 36. ML's impoverishment and Defendants' enrichment are directly connected.
- 37. As a direct and proximate result of Defendants' unjust enrichment, Plaintiffs have sustained damages in an amount to be proven at trial.
- 38. Plaintiff is entitled to have the Court impose a constructive trust on the proceeds from the Life Insurance Policies that were received by Defendants.

COUNT II - FRAUDULENT TRANSFER

- 39. Plaintiffs reallege and incorporate by reference the allegations set forth in the preceding paragraphs as if fully set forth herein.
- 40. SMC Revocable Trust caused ML to transfer assets to SMC Revocable Trust for the purpose of purchasing life insurance policies that would benefit Defendants and which would not benefit ML.
- 41. At the time of the transfers, ML had a right of payment against Scott Coles and SMC Revocable Trust for the funds that were transferred for the purpose of purchasing life insurance policies that would benefit Defendants.

- 42. At the time of the transfers, ML was either insolvent or became insolvent as a result of the transfers.
 - 43. ML did not receive reasonably equivalent value in exchange for the transfers.
- 44. Scott Coles and SMC Revocable Trust engaged in those transfers with the actual intent to hinder, delay, and defraud ML and ML's creditors and investors.
- 45. Scott Coles and SMC Revocable Trust were insiders with respect to ML at the time when the transfers were made.
- 46. Scott Coles, SMC Revocable Trust, and the Defendants concealed the transfers from ML and its creditors and investors.
- 47. The transfer of ML's assets for the benefit of Defendants constitutes a fraudulent transfer pursuant to A.R.S. §§ 44-1004 and 44-1005.
- 48. As a direct and proximate result of the fraudulent transfers for the benefit of Defendants, Plaintiffs have been damaged in an amount to be proven at trial.

COUNT III - CONSTRUCTIVE TRUST

- 49. Plaintiffs reallege and incorporate by reference the allegations set forth in the preceding paragraphs as if fully set forth herein.
 - 50. At all relevant times, Scott Coles owed ML a fiduciary duty.
- 51. Scott Coles represented to ML that he had purchased or would purchase key man or other life insurance policies for the benefit of ML.
- 52. Scott Coles expressly or impliedly led ML to believe that some or all of the funds that were being transferred to SMC Revocable Trust for the purpose of paying insurance premiums on key man or other life insurance policies that were for the benefit of ML.
 - 53. ML reasonably relied on Scott Coles' representations.
- 54. Defendants will be unjustly enriched at Plaintiff's expense unless a constructive trust is imposed on the proceeds of the Life Insurance Policies.

55. Plaintiff is entitled to have the Court impose a constructive trust on the proceeds from the Life Insurance Policies that were received by Defendants.

<u>COUNT IV – WRONGFUL DISTRIBUTION – VIOLATION OF A.R.S. § 10-640</u>

- 56. Plaintiffs reallege and incorporate by reference the allegations set forth in the preceding paragraphs as if fully set forth herein.
- 57. When SMC Revocable Trust caused ML to transfer funds to SMC Revocable Trust for the purpose of paying the Life Insurance Policies, he directed ML to treat those and other transfers as shareholder distributions.
- 58. When SMC Revocable Trust transferred funds to the SMC Revocable Trust for the benefit of Defendants, ML was unable to pay its debts as they came due in the ordinary course of business.
- 59. Upon information and belief, at the time when SMC Revocable Trust transferred funds to the SMC Revocable Trust for the benefit of Defendants, ML's assets were less than the sum of its total liabilities.
- 60. The transfers of funds from ML to SMC Revocable Trust for the purpose of paying premiums on the Life Insurance Policies violated A.R.S. § 10-640.
- 61. As a direct and proximate result of the improper distributions to SMC Revocable Trust, ML has been damaged in an amount to be proven at trial.
- 62. Because the funds that were used to pay the premiums on the Life Insurance Policies were obtained in violation of A.R.S. § 10-640, ML is entitled to a constructive trust on the proceeds of the Life Insurance Policies.

COUNT V - TRUST FUND DOCTRINE

63. Plaintiffs reallege and incorporate by reference the allegations set forth in the preceding paragraphs as if fully set forth herein.

- 64. Pursuant to the trust fund doctrine, all assets of a corporation immediately upon its becoming insolvent exist for the benefit of all of the corporation's creditors and thereafter, no liens or rights can be created either voluntarily or by operation of law whereby anyone is given an advantage over the corporation's other creditors.
- 65. SMC Revocable Trust caused ML to transfer ML's funds to SMC Revocable Trust for the purpose of paying the Life Insurance Policies that benefitted Defendants.
- 66. The transfers of funds to SMC Revocable Trust for the purpose of paying the Life Insurance Policies that benefitted Defendants were made at times when ML was insolvent.
- 67. The transfer of funds to SMC Revocable Trust for the purpose of paying the Life Insurance Policies preferred SMC Revocable Trust and Defendants to the disadvantage of ML and its creditors.
- 68. As a direct and proximate result of the improper transfers of funds for the benefit of Defendants, Plaintiffs have sustained damages in an amount to be proven at trial.
- 69. Because the transfers of funds for the benefit of Defendants violated the trust fund doctrine, Plaintiff is entitled to have the Court impose a constructive trust on the proceeds from the Life Insurance Policies that were received by Defendants.

<u>COUNT VI – AIDING AND ABETTING CONVERSION</u>

- 70. Plaintiffs reallege and incorporate by reference the allegations set forth in the preceding paragraphs as if fully set forth herein.
- 71. SMC Revocable Trust improperly exercised dominion and control over ML's funds at a time when ML was insolvent or on the verge of becoming insolvent and used those funds to pay the premiums on the Life Insurance Policies for the benefit of Defendants.
- 72. The transfer of funds from ML to SMC Revocable Trust constitutes conversion of ML's assets.

- 73. Upon information and belief, Defendants knew or reasonably should have known that SMC Revocable Trust was converting funds from ML at a time when ML was insolvent or on the verge of becoming insolvent.
- 74. Defendants each acquiesced to the conversion of ML's assets for their benefit and accepted the benefits of the conversion of ML's assets and thereby aided, abetted, and provided substantial assistance in furtherance of the conversion of ML's assets.
- 75. As a direct and proximate result of Defendants' aiding, abetting, and providing substantial assistance in furtherance of the conversion of ML's assets, Plaintiffs have sustained damages in an amount to be proven at trial.

COUNT VII – AIDING AND ABETTING BREACH OF FIDUCIARY DUTY

- 76. Plaintiffs reallege and incorporate by reference the allegations set forth in the preceding paragraphs as if fully set forth herein.
- 77. At all relevant times, Scott Coles and SMC Revocable Trust owed ML a fiduciary duty.
- 78. Scott Coles and SMC Revocable Trust breached their fiduciary duties to ML by among other things, causing ML to transfer funds to SMC Revocable Trust to purchase the Life Insurance Policies at times when ML was insolvent or on the verge of becoming insolvent.
- 79. Upon information and belief, Defendants knew or reasonably should have known that Scott Coles and SMC Revocable Trust were breaching his fiduciary duties to ML by causing ML to transfer funds for Defendants' benefit at a time when ML was insolvent or on the verge of becoming insolvent.
- 80. Defendants each acquiesced to SMC Revocable Trust and Scott Coles' breaches of their fiduciary duties and accepted the benefits of the improper transfers of ML's assets and thereby aided, abetted, and provided substantial assistance in furtherance of SMC Revocable Trust and Scott Coles' breaches of their fiduciary duties.

81. As a direct and proximate result of Defendants' aiding, abetting, and providing substantial assistance in furtherance of SMC Revocable Trust and Scott Coles' breaches of their fiduciary duties, Plaintiffs have sustained damages in an amount to be proven at trial.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs pray for judgment against Defendants and each of them as follows:

- A) For damages in the amount of the proceeds that each Defendant received from the Life Insurance Policies;
- B) For the imposition of a constructive trust in favor of Plaintiff on all of the proceeds that each Defendant received from the Life Insurance Policies;
 - C) For its reasonable attorneys' fees and costs; and
 - D) For such other and further relief as the Court deems appropriate.

RESPECTFULLY SUBMITTED this 25th day of March, 2011.

STINSON MORRISON HECKER LLP

By:

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ORIGINAL filed this Aday of March, 2011:

Clerk of the Court
Maricopa County Superior Court
101/201 West Jefferson
Phoenix, Arizona 85003