

**UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF FLORIDA
ORLANDO DIVISION**

**SECURITIES AND EXCHANGE
COMMISSION**

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Plaintiff

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**CIVIL ACTION FILE NO:
6:06-cv-137-Orl-19 KRS**

v.

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EDWARD S. DIGGES, JR., et al.,

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Defendants

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**MEMORANDUM IN SUPPORT OF DEFENDANT’S
MOTION FOR RELIEF FROM INJUNCTION**

Defendant Edward S. Digges, Jr. (“Digges”), through the limited appearance of counsel for purposes of Defendant’s Motion for Relief from Injunction only, submits this Memorandum in support of said Motion.

INTRODUCTION

Digges is destitute, without income, blocked by the Court’s injunction from access to any assets, and in desperate need of funds to meet basic needs and pay attorneys’ fees in this case. He seeks relief from the injunction to permit a family-owned corporation to sell four parcels of land in Charles County, Maryland to raise money so that he may survive and defend himself in this case. The relief is warranted because the four parcels have no connection to the activity which forms the basis of Plaintiff’s complaint. Rather, the parcels originally were acquired by members of Digges’ family more than 50 years ago and passed to the family-owned corporation by bequest and gift over the years.

Digges has meritorious defenses to Plaintiff's claims. He consented to the entry of the injunction in this case in order to show his good faith and avoid costly and time-consuming proceedings relative to Plaintiff's request for an injunction. However, without the ability to raise money for attorneys' fees through the sale of this family-owned property, no full and fair examination of these issues will be possible.

Plaintiff and the Receiver have cast a wide net to recover assets allegedly transferred improperly by Defendants. In doing so, however, they have inadvertently or mistakenly ensnared property that is wholly separate and unrelated to the actions complained of in this action. Because the Receiver has no legitimate claim to this property, and Digges has a paramount need for the proceeds from its sale, the interests of justice require that this property be released from the scope of the injunction.

STATEMENT OF FACTS

This SEC enforcement action was commenced on February 1, 2006 with the filing of a Complaint alleging violations of the Securities Act of 1933, the Securities Exchange Act of 1934, and Rule 10b-5 promulgated thereunder. On February 15, 2006, the Court issued an Order (the "Order") (with Defendant's consent) that, inter alia, froze "all assets of, or under the control of" Digges as well as restraining Digges from, directly or indirectly, transferring, selling, or disposing of any assets "owned by, controlled by, or in [his] possession." Order ¶ IV at p. 5. The Order also appointed a Receiver to administer and manage the Receiver Estate and to pursue claims for the recovery of assets for the benefit of investors. Order ¶¶ VII, VIII at pp. 7-9.

On March 7, 2006, the Receiver commenced a separate action in this Court, James Silver v. Edward S. Digges, Jr., et al., Civil Action No. 6:06-cv-290-18-DAB (the "Receiver Action"), seeking to recover for the benefit of investors and the Receiver Estate assets allegedly

fraudulently transferred to other persons or entities. In an Amended Complaint filed in the Receiver Action on April 28, 2006, the Receiver named as defendants Digges, his wife Katherine Anne Kerr (“Kerr”), various children, family members, or associates of Digges and Kerr, and as well as two family-owned ventures, KBK Partnership, LLP (“KBK”), a Maryland limited liability partnership, and Chilham, LLC (“Chilham”), a Maryland limited liability corporation. In that Amended Complaint, the Receiver correctly alleges that Chilham owns several parcels of land in Charles County, Maryland (the “Property”), but further alleges “upon information and belief,” the Property “was acquired with monies belonging to the Receiver Estate’s defrauded investors” (Amended Complaint ¶ 19), and that “misappropriated investor funds were used to purchase and/or pay the mortgages, in whole or in part, directly or indirectly,” on the Property (Amended Complaint ¶ 24).

The Receiver is wrong. The land records of Charles County, Maryland (attached hereto as Exhibits A, B and C) establish that the four parcels of land which comprise the Property were acquired by family members of Digges more than 50 years ago and have passed to Chilham over the years by bequest and gift. At no time were any investor funds used to acquire, improve, or maintain these parcels. See Exhibits A – C, hereto; Declarations of Edward S. Digges, Jr. (“Digges Declaration”) and his wife Katherine Anne Kerr (“Kerr Declaration”) (Exhibits D and E).

1. The Digges Family

Digges is the only child of Edward S. Digges, Sr. Digges Sr. was the youngest of four Digges siblings including, Eleanor Digges (later Eleanor Digges Harrington), Dudley Digges, and Walter Mitchell Digges. Eleanor and Digges Sr. were the only Digges siblings to marry and have children; Eleanor married Calvin Harrington and had three children (the “Harrington cousins”), and Digges Sr. married Maria Janie McHugh on November 11, 1943 and had one child. Dudley and Walter never married nor had children. Digges Declaration ¶ 6. Digges and Kerr were married on June 12, 2004. Kerr Declaration ¶ 1.

2. Chilham

Chilham is a Maryland limited liability corporation established by Digges Sr. in 2000 as an estate planning vehicle. Digges Declaration ¶ 3. Prior to Digges Sr.’s death in 2002, he transferred various assets to Chilham including interests in property acquired by Digges Sr. over the years through purchase or bequest. All of this property has been sold by Chilham, except for four parcels comprising the Property. Chilham’s only remaining assets are these four parcels of land and stock (currently valued at approximately \$10,000) that was also transferred by Digges Sr. prior to his death to Chilham as part of his estate planning. Digges Declaration ¶¶ 3, 5.

Chilham is owned 99% by KBK and 1% by Kerr, individually. KBK in turn is owned 99% by Kerr with the remaining 1% split between two trusts established for the children of Digges and Kerr by prior marriages. Digges Declaration ¶ 4, Kerr Declaration ¶ 2.

Chilham’s ownership interest in the Property consists of (a) a 25% share of three parcels of approximately 20 acres of undeveloped commercial property on or near Route 301 in La Plata, Maryland (the “La Plata Parcels”); and (b) a 50% share of one parcel of 201.418 acres of

undeveloped agricultural land off of Route 225 near Ripley, Maryland (the “Ripley Parcel”). Digges Declaration ¶ 5, Kerr Declaration ¶ 3.

3. The La Plata Parcels

The La Plata Parcels were originally acquired by Dudley Digges in the early 1950’s, along with two other Charles County families. Dudley Digges owned 50% of all three La Plata Parcels with 50% of one parcel being owned by the Mudd family and 50% of the two remaining La Plata parcels being owned by the Viering family. The 50% owned by the Mudd and Viering families has remained in those families through bequests and/or gifts over the years. Digges Declaration ¶ 7.

Upon Dudley Digges’ death in 1983, his 50% interest in all three La Plata Parcels passed by bequest in equal shares to his three surviving siblings, Eleanor, Walter, and Digges Sr. Upon the death of Walter Digges in 1993, his share of the La Plata Parcels passed equally to his two surviving siblings, Eleanor and Digges Sr. Thus, after the deaths of Dudley and Walter Digges, Digges Sr. and his sister Eleanor Harrington each owned 25% of the La Plata Parcels. Digges Declaration ¶ 8.

Digges Sr.’s share of the La Plata property was later gifted to Chilham prior to his death. Eleanor Harrington’s share of the La Plata Parcels passed by bequest upon her death in 2001 to her three children, the Harrington cousins. Thus, currently the three La Plata Parcels are owned 25% by the Harrington cousins, 25% by Chilham, and 50% by either the Mudd or Viering families. Digges Declaration ¶ 9. See Exhibits A and B.

4. The Ripley Parcel

The Ripley Parcel was originally purchased in the early 1950’s by Walter Mitchell Digges. When he died in 1993, the Ripley Parcel passed by bequest in equal 50% shares to his

two surviving siblings, Eleanor and Digges Sr. Eleanor Harrington's 50% share passed by bequest upon her death to her three children, the Harrington cousins. Digges Sr.'s 50% share of the Ripley Parcel was later gifted to Chilham prior to his death as part of his estate planning. Thus, currently, the Ripley Parcel is owned 50% by Chilham and 50% by the Harrington cousins. Digges Declaration ¶ 10. See Exhibit C.

5. No Investor Funds Were Used to Acquire, Improve, or Maintain the Property

At no time has any money or proceeds from any enterprise or venture that are the subject of this SEC enforcement action been used to acquire, improve, or maintain any of the Property. Digges Declaration ¶¶ 3, 12. To the contrary, Chilham has been a source of capital to these ventures over the years through the sale of property and the loan of the proceeds of those sales to KBK. KBK has used this money to make capital infusions into the ventures. All of these transactions, i.e., the loans from Chilham to KBK and the capital infusions into the ventures, are evidenced by interest-bearing notes and/or reflected in respective financial statements as conversions to capital accounts. Digges Declaration ¶ 12. Thus, rather than being a recipient of investor funds from these ventures, Chilham has been a provider of funds to these ventures.

There has never been a mortgage on any of the four parcels comprising the Property. Digges Declaration ¶ 11. See Exhibits A, B, and C. The only income received by Chilham from the Property over the years has been from the leasing of the Ripley Parcel to a neighbor of Digges for \$500 per year for hunting privileges. That \$500 annual hunting fee is used to pay the yearly taxes on the Ripley Parcel. Digges Declaration ¶ 11. In addition, Chilham has on occasion used payments by KBK on its loans to Chilham to pay property taxes on the La Plata Parcels of approximately \$6,250 per year. Digges Declaration ¶ 14.

ARGUMENT

I. THE COURT MAY RELEASE PROPERTY FROM THE ASSET FREEZE TO PROVIDE FOR LIVING EXPENSES AND/OR ATTORNEYS' FEES

It is well-settled that, as a corollary to the Court's power to issue an order freezing a defendant's assets in an SEC enforcement action, the Court may modify the asset freeze to permit a defendant to pay for necessary living expenses and attorneys' fees. See S.E.C. v. Asset Recovery and Management Trust, S.A., 340 F.Supp.2d 1305, 1311 (M.D. Ala. 2004) (defendants may seek modification of asset freeze to pay for living expenses); S.E.C. v. Duclaud Gonzalez de Castilla, 170 F.Supp.2d 427, 429-30 (S.D.N.Y. 2001) (asset freeze modified to permit payment of legal fees and disbursements); S.E.C. v. Schiffer, 1998 WL 307375 at *7 (S.D.N.Y. 1998) (funds released from asset freeze to pay for living expenses and attorneys' fees subject to court's careful monitoring).

The Court may also release personal assets from the scope of an asset freeze where there is no proof that those assets are tainted by the alleged fraud. See S.E.C. v. International Loan Network, Inc., 770 F.Supp. 678, 697 (D.D.C. 1991), aff'd 968 F.2d 1304 (D.C. Cir. 1992) (asset freeze lifted as to personal assets of defendants where SEC failed to produce evidence of improper diversion or secreting of assets); S.E.C. v. Grossman, 1997 WL 231167 at *16 (S.D.N.Y. 1997) (proof that defendant had no interest in joint accounts held with wife and daughter would warrant modification of asset freeze to release funds in such accounts).

In the instant case, both of these grounds exist for relief from the Order freezing Digges' assets. As more fully discussed infra, Digges has an immediate need for, and a constitutional right to, legal counsel to assist in the defense of this case. Without modification of the Order to permit sale of the Property to raise funds for attorneys' fees, he will be denied that right. In addition, as set forth infra, the Property is untainted by money or proceeds from the alleged fraud

at issue in this action. Thus, the Court may release it from the scope of the Order so that Digges may use such untainted, personal assets for living expenses and attorneys' fees.

II. THE COURT SHOULD PERMIT THE SALE OF THE PROPERTY SO THAT DEFENDANT CAN RETAIN COUNSEL TO PROVIDE AN EFFECTIVE DEFENSE IN THIS COMPLICATED SECURITIES LAW ACTION.

A civil litigant has a constitutional right to counsel. Potashnick v. Port City Const. Co., 609 F.2d 1101, 1118 (5th Cir.), cert. denied, 449 U.S. 820, 101 S.Ct. 78, 66 L.Ed.2d 22 (1980).¹ See also In re Bell South Corp., 334 F.3d 941, 955 (11th Cir. 2003) (civil litigants have constitutional right to counsel of choice); Texas Catastrophic Property Ins. Ass'n v. Morales, 975 F.2d 1178, 1180-81 (5th Cir. 1992), cert. denied, 507 U.S. 1018, 113 S.Ct. 1815, 123 L.Ed.2d 446 (1993) (same). As the court stated in Potashnick, the right to counsel in civil actions derives from the Due Process Clause of the Fifth Amendment and is analogous to the Sixth Amendment's right to counsel in criminal cases:

[T]he Supreme Court has indicated in its criminal decisions that the right to retain counsel in civil litigation is implicit in the concept of fifth amendment due process. . . . The right develops out of the principle that notice and hearing are preliminary steps essential to the passing of an enforceable judgment and that they constitute basic elements of the constitutional requirement of due process of law.

* * * *

[As with the Sixth Amendment right to counsel in criminal cases], the litigant [in a civil action] usually lacks the skill and knowledge to adequately prepare his case, and he requires the guiding hand of counsel at every step in the proceedings against him. . . . In each instance, the right to counsel is one of constitutional dimensions and should thus be freely exercised without impingement.

609 F.2d 1101 at 1117-18 (citations omitted).

¹ Decisions of the former Fifth Circuit announced prior to October 1, 1981 are binding precedent in the Eleventh Circuit. Bonner v. Prichard, 661 F.2d 1206, 1209 (11th Cir. 1981) (en banc).

Without release of the Property from the scope of the Order, Digges will be unable to avail himself of this right to counsel in either this case or the Receiver Action. The Order froze all of Digges' personal and business accounts, and there is not a single account he can draw upon for attorney's fees or living expenses. He has no income and no savings. Digges and Kerr are living hand-to-mouth, depending on the generosity of family and friends for daily living expenses. The Property is the sole asset available to Digges for funding a defense to this action. Digges Declaration ¶ 3. Release of the Property from the scope of the Order is thus necessary to give force to Digges' Due Process right to counsel in this case.

Digges' right to counsel is even more important because of the extremely complicated nature of the claims leveled against him, involving alleged violations of two different federal securities laws (the Securities Act of 1933 and the Securities Exchange Act of 1934) and one federal regulation (Rule 10b-5 of the Securities and Exchange Commission). In the Receiver Action, the Receiver has alleged violations of Florida statutory and common law, including fraudulent transfers, conversion, and unjust enrichment. These claims all involve complicated fact patterns and mesmerizing statutory and regulatory interpretations. They are not claims that a destitute, pro se litigant can fairly be expected to defend on his own in any sort of meaningful way, particularly given the number of lawyers arrayed against him.² Rather, he desperately needs "the guiding hand of counsel at every step in the proceedings against him." Potashnick, supra.

² Plaintiff, the SEC, lists three attorneys as counsel of record; the Receiver is himself an attorney and thus far has used two attorneys from his firm as counsel of record in this matter

III. THE PROPERTY SOUGHT TO BE RELEASED FROM THE ORDER IS NOT PART OF THE RECEIVER ESTATE NOR SUBJECT TO SEIZURE BY PLAINTIFF.

There is no theory under which Plaintiff can obtain disgorgement of the Property from Chilham in this case, nor is there any theory under which the Receiver can recover the Property for the benefit of investors in the Receiver Action, because the Property is wholly separate from, and untainted by, the conduct alleged to constitute violations of federal securities laws. As set forth above, and confirmed by the land records and Declarations attached hereto, the Digges family's acquisition of the Property predates the conduct at issue in this action by decades. No money or proceeds from any enterprise that is the subject of this action was used to acquire the Property. No such money or proceeds was used to improve or maintain the Property.

Neither Chilham or its members are named as defendants in this action, and thus the Property owned by it is not part of the Receiver Estate. Moreover, the Receiver's filing of the Receivership Order in the District of Maryland pursuant to 28 U.S.C. § 754 only gives this Court jurisdiction over property in that District that is part of the Receiver Estate. Property owned by Chilham, therefore, cannot be used or controlled by the Receiver.

Alternatively, a court in an SEC enforcement action may order equitable relief against a third-party, or "relief defendant," who is not accused of wrongdoing in an SEC enforcement action where that person (1) has received ill-gotten gains from an illegal venture; and (2) does not have a legitimate claim to those funds. See United States v. Cavanagh, 155 F.3d 129, 136 (2d Cir. 1998). This is the theory of liability asserted against Chilham in the Receiver Action, ("the real property owned by Chilham [in Charles County, Maryland] was acquired with monies belonging to the Receiver Estate's defrauded investors;" "[u]pon information and belief, misappropriated investor funds were used to purchase and/or pay the mortgages, in whole or in

part, directly or indirectly, on the Chilham Properties.” See Amended Complaint ¶¶ 19, 24.) However, as established by the land records of Charles County, Maryland (Exhibits A-C) and the Digges and Kerr Declarations (Exhibits D and E), the Property was originally acquired by the Digges family in the early 1950’s and has passed by bequest and gift to Chilham. Not one penny of money or proceeds from the ventures which are the subject of this SEC enforcement action has ever gone into the acquisition, improvement, or maintenance of the Property. The Property has at all times remained entirely separate from the conduct challenged by Plaintiff in this case.³

In sum, the Property is untainted by receipt of money or proceeds from the actions alleged in this case to be in violation of federal securities laws, and the Plaintiff and the Receiver thus have no basis for seizing the Property for the benefit of investors.⁴ Digges has a substantial and immediate need for money to retain counsel in this and the related Receiver Action. The Property is the only possible source for this money. The Property should therefore be released from the scope of the Court’s Order so that the Property can be sold and sale proceeds used for attorneys’ fees and other legitimate expenses. The interests of justice tip decisively in favor of releasing the Property from the scope of the injunction so that Digges can mount an effective defense in these cases.

³ On June 13, Chilham was served with the Receiver Action; however, under the Court’s current Order, it may be prohibited from raising any funds through the sale of the Property in order to retain counsel to defend it in the Action and protect the Property from wrongful acquisition by the Receiver.

⁴ Nor can the Property be seized as a “substitute asset,” a concept reserved for criminal forfeiture actions where specifically authorized by statute. E.g., 21 U.S.C. § 853(p) (forfeiture of substitute assets permitted in drug cases where the property originally subject to forfeiture cannot be located or has been transferred to a third party). There is no provision in Title 15 of the United State Code or elsewhere which gives the SEC authority in a civil enforcement action to seek forfeiture of “substitute assets.”

CONCLUSION

The Court should modify the Order entered on February 15, 2006 to permit Chilham LLC to sell its interest in four parcels of land in Charles County, Maryland.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY certify that I have this 19th day of June, 2006, caused the foregoing to be filed electronically and made available for viewing and downloading from the United States District Court for the Middle District of Florida's CM/ECF system.

/s/ Lee Fugate

Lee Fugate