

Commonwealth of Kentucky

Court of Appeals

NO. 2016-CA-001415-MR

SAMUEL VARNER

APPELLANT

v.

APPEAL FROM FAYETTE CIRCUIT COURT
HONORABLE THOMAS L. CLARK, JUDGE
ACTION NO. 16-CI-02312

KINGFISH CAPITAL PARTNERS I,
LP

APPELLEE

OPINION
AFFIRMING

** ** * ** * ** *

BEFORE: KRAMER, CHIEF JUDGE; DIXON AND NICKELL, JUDGES.

KRAMER, CHIEF JUDGE: Samuel Varner appeals the summary judgment of the Fayette Circuit Court to the extent that it dismissed a claim of unjust enrichment he asserted against the appellee, Kingfish Capital Partners I, LP (“Kingfish”). For the reasons discussed below, we affirm.

Varner filed his complaint against Kingfish on June 22, 2016, asserting claims of breach of contract and unjust enrichment based upon the following general allegations which Kingfish admitted for purposes of the instant appeal:

7. Kingfish was formed on or about November 13, 2013. It was to be operated as a hedge fund, the primary purpose of which was to invest in energy related investment and growth opportunities.

8. As the entity name implies, Kingfish was formed as a Limited Partnership in Texas by a General Partner, Kingfish Capital Management, LLC, (“KCM”) with the intent that KCM would manage the fund and operate the limited partnership, with the help of capital raised from outside investors, who would become limited partners in the venture.

9. Pursuant to a Private Placement Memorandum (“PPM”) dated August 25, 2014 and attached to this Complaint as Exhibit A, Kingfish and/or KCM began offering Class A limited partnership interests for sale pursuant to the PPM or terms agreed to by them and limited partnership investors.

10. In late 2014, the Defendants entered into an oral contract with the Plaintiff, Varner, by which the Plaintiff would act as an agent for selling subscriptions for Class A limited partnership interests.

11. It was expressly understood by and between Varner and Kingfish that he would earn and be paid a placement fee equivalent to 8.5% of the subscriptions placed by him.

12. Pursuant to his contract with Kingfish, Varner was solely responsible for the investment of \$725,000.00, investments which were converted into Class A limited partnership interests pursuant to the PPM. He invested

\$25,000 himself, and successfully solicited investments from others in an additional amount of \$700,000.00.

13. All of the investors Varner sold subscriptions to, including himself, were either individuals residing in or companies primarily doing business in the Commonwealth of Kentucky.

14. Kingfish was aware that Varner was located in Lexington Kentucky when it solicited him to assist in the sale of Limited Partnership interests and was aware when it accepted investments from Kentucky investors that it was granting these interests to individuals and entities located in Kentucky.

15. Varner has not been paid by Kingfish for the work performed on its behalf despite numerous demands.

Shortly after Varner filed his complaint, Kingfish moved for summary judgment. Its argument was in relevant part as follows:

A. The Contract Which Varner Alleges in this Case is Illegal.

Varner, who was not registered as a broker or agent with the Kentucky Division of Securities or any other licensing authority during the relevant period, claims that he contracted to act as an agent for selling Kingfish's securities and to receive an 8.5% commission for effectuating these sales. Varner acknowledges, as he must, that such activities subject him to the reach of KRS^[1] 292.330(3), which makes it "unlawful for any person to transact business in this state as an agent [FN] unless the individual is registered under this chapter as an agent or is exempt from registration under subsection (4) of this section."

[FN] Pursuant to KRS 292.310(1), an "agent" is "an individual . . . who represents . . . [an] . . . issuer in effectuating or

¹ Kentucky Revised Statute.

attempting to effectuate purchases or sales of securities.”

KRS 292.330(4)(c)7 provides for the exemption claimed by Varner, the so-called “issuer exemption” (which Varner’s trial counsel refers to as the “partnership exemption”). According to that exemption provision, an agent representing an issuer in effectuating transactions is only exempt “if the agent’s compensation is not based, directly or indirectly, on the transactions.” KRS 292.330(4)(c)7. Thus, by the plain terms of the statutory exemption claimed by Varner, his alleged contract to receive compensation equal to 8.5% of the sales he claims to have effectuated in this case precludes him from relying on the “issuer exemption.” [FN]

[FN] Similarly, KRS 292.330(4)(c)5, which applies to transactions relating to Regulation D private offerings like that at issue in this case, exempts agents from registration only if they do not “receive[] a commission or other remuneration based, either directly or indirectly, on the transaction.”

Federal law similarly precludes Varner from charging a fee for acting as Kingfish’s agent in the sales of its securities. Section 15 of the Securities Exchange Act of 1934, 15 U.S.C.^[2] § 78o, provides that all individuals who broker securities transactions in interstate commerce must register as a broker with the Securities Exchange Commission. While 17 C.F.R.^[3] § 240.3a4-1 (the federal version of the “issuer exemption”) permits an individual affiliated with an issuer to participate, under certain limited circumstances, in the sale of the issuer’s securities without registering under § 78o, that provision only applies where the individual “is not compensated in connection with his participation by the payment of commissions or other remuneration based either directly or indirectly on transactions in securities”

² United States Code.

³ Code of Federal Regulations.

In sum, under the facts alleged by Varner, *i.e.*, that he acted as Kingfish's agent in the sales of Kingfish's securities and contracted for an 8.5% commission in connection with those sales, Varner is not exempt from the registration requirements of either the Kentucky or the federal securities laws. As a result, and as a matter of law, Varner violated those laws under his sworn factual allegations in this case.

B. Varner Cannot Recover On an Illegal Fee Contract.

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Pursuant to Section 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc(b): “[e]very contract made in violation of any provision of this chapter or of any rule or regulation thereunder. . . shall be void. . . as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract” Because, as established above, the contract which Varner alleges in this case would violate the provisions of Section 15 of the Securities Exchange Act of 1934, 15 U.S.C. § 78o, which prohibits engaging in securities brokerage activities without a license, Section 29(b) of the Securities Exchange Act of 1934 prohibits the enforcement of that contract.

.....

KRS 292.480(6) similarly provides that contracts in violation of the provisions of the Kentucky Securities Act are void: “[n]o person who has made or engaged in the performance of any contract in violation of any provision of this chapter or any rule or order hereunder . . . may base any suit on the contract.” Thus, as Varner's alleged contract to act as Kingfish's agent in the sales of its securities and to recover an 8.5% commission for those services violates KRS 292.330, KRS 292.480(6) provides an independently sufficient basis for barring Varner's claim.

Upon consideration, the circuit court ultimately adopted Kingfish's reasoning as its bases for summarily dismissing Varner's breach of contract and unjust enrichment claims. This appeal followed.

Summary judgment serves to terminate litigation where "the pleadings, depositions, answers to interrogatories, stipulations, and admissions on file, together with the affidavits, if any, 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." Kentucky Rule of Civil Procedure (CR) 56.03. It should be granted only if it appears impossible that the nonmoving party will be able to produce evidence at trial warranting a judgment in his favor. *Steelvest, Inc. v. Scansteel Serv. Ctr., Inc.*, 807 S.W.2d 476 (Ky. 1991).

Varner has not appealed the dismissal of his breach of contract claim against Kingfish. His sole argument on appeal is that *even if* his contract with Kingfish was illegal and violated public policy, the circuit court incorrectly dismissed his claim against Kingfish for restitution under his alternative theory of unjust enrichment. We disagree.

Based upon the reasoning quoted and adopted above, we agree with the circuit court's determination that Varner's contract with Kingfish *was* illegal and violated public policy. And, by failing to appeal the circuit court's dismissal of his breach of contract claim--a dismissal the circuit court based solely upon that determination--Varner has also effectively conceded the point. *See, e.g., Osborne*

v. Payne, 31 S.W.3d 911, 916 (Ky. 2000) (“Any part of a judgment appealed from that is not briefed is affirmed as being confessed.”).

With that in mind, Varner’s unjust enrichment claim is untenable. As to why, it is evident from his complaint that Varner is asking the Court to compel, through equity, restitution for performance he rendered in return for Kingfish’s purported illegal promise to compensate him for his unlicensed sale of Kingfish’s securities. But:

In general, if a court will not, on grounds of public policy, aid a promisee by enforcing the promise, it will not aid him by granting him restitution for performance that he has rendered in return for the unenforceable promise. Neither will it aid the promisor by allowing a claim in restitution for performance that he has rendered under the unenforceable promise. It will simply leave both parties as it finds them, even though this may result in one of them retaining a benefit that he has received as a result of the transaction.

Restatement (Second) of Contracts § 197, cmt. a.

In other words, equity cannot indirectly compel a remedy that a statute or constitution directly forbids. *See S.J.L.S. v. T.L.S.*, 265 S.W.3d 804, 821 (Ky. App. 2008); *see also Miller v. Miller*, 296 S.W.2d 684, 688 (Ky. 1956) (“Any conduct or contract of an illegal, vicious or immoral nature cannot be the proper basis for a legal or equitable proceeding.”); *Cougler v. Fackler*, 510 S.W.2d 16, 18 (Ky. 1974) (explaining where “an otherwise *legal* contract is unenforceable [. . .] the remedy of restitution to prevent unjust enrichment is available *unless* the statute that makes the contract unenforceable prohibits the remedy, or if the

purpose of the statute would be nullified by granting such a remedy.” (Citations omitted; emphasis added)).

Compelling Kingfish to compensate Varner under the circumstances would nullify the purposes of the above-cited securities statutes--statutes which, by their plain terms, flatly prohibited Varner from receiving payment of commissions or other remuneration based either directly or indirectly upon his participation in transactions in Kingfish’s securities.⁴ To quote another appellate tribunal that resolved a similar situation involving an unregistered broker who sought equity to compel otherwise illegal compensation connected with the sale of securities,

If the broker who has performed can recover his commission despite non-registration, then the prohibition is a toothless tiger.

The illegality of the transaction precludes the recovery of damages for breach and any other judgment aimed at enforcement of the tainted contract. Thus, persons who perform services without obtaining a required

⁴ Varner cites *Kennoy v. Graves*, 300 S.W.2d 568, 569 (Ky. 1957), for the proposition that, under the common law, “a contract for services” can be enforced where “an unlicensed member of a profession or trade seeks to recover from a licensed member for services rendered or labor performed pursuant to a contract entered into by them.” To the extent that this constitutes an exception to the general rule prohibiting the enforcement of illegal promises, it does not apply here for at least three reasons. First, Varner is seeking *equity*, not to enforce “a contract for services.” Second, Varner cites nothing indicating Kingfish had any kind of license or that a fund that issues securities is necessarily in the same trade or profession as a broker of securities transactions. See *Regional Props., Inc. v. Financial & Real Estate Consulting Co.*, 752 F.2d 178, 185, n. 4 (5th Cir. 1985) (explaining “[a]n issuer that effects the distribution of its own securities is not engaging in transactions for the account of others but is instead selling securities for its own account. Thus an issuer is not subject to the [Securities Exchange] Act’s broker registration requirements.”) Lastly, *Kennoy* applied this exception only because the reviewing court determined, from its interpretation of the statute at issue in that matter, “that the technical requirements of the licensing statute play[ed] no part in the determination of just claims between persons in the same business . . . who have contracted with knowledge of each other’s respective professional qualifications.” *Kennoy*, 300 S.W.2d at 570. Here, by contrast, the brokerage licensing statutes unequivocally prohibited the claims Varner asserted against Kingfish.

occupational license have been denied recovery either on their contract or in quasi-contract.

Regional Props., Inc. v. Financial and Real Estate Consulting Co., 678 F.2d 552, 564 (5th Cir. 1982) (citation omitted).

In short, the circuit court did not err in dismissing Varner's unjust enrichment claim against Kingfish. Accordingly, we AFFIRM.

ALL CONCUR.

BRIEF FOR APPELLANT:

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BRIEF FOR APPELLEE:

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