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RESTITUTION-CONSTRUCTIVE TRUST ON RECISSION FOR FRAUD WILL NOT DISPLACE LIEN FOR REPAIRS ON VESSEL

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RESTITUTION—CONSTRUCTIVE TRUST ON RESCISSION FOR FRAUD WILL NOT DISPLACE LIEN FOR REPAIRS ON VESSEL—The Maryland Dry Dock Company sued to enforce its statutory maritime lien for converting a cargo vessel owned by the Republic Steamship Corporation into a passenger ship, and the International Refugee Organization contested the action on the ground that the money used to purchase the vessel was obtained by Republic from IRO by fraud. IRO argued that Republic did not have authority to bind the vessel because the vessel was impressed with a constructive trust in IRO's favor, and that if Republic did have authority the trust took preference over the lien.¹ *Held*, a constructive trust on rescission for fraud is a remedy which does not

¹The statute gives a lien for repairs to any vessel if the owner or a person authorized by the owner orders the repairs. The following section declares that no person tortiously or unlawfully in possession of a vessel shall have authority to bind the vessel. 41 STAT. L. 1005, §30 (1920), 46 U.S.C. (1946) §§971, 972, 973.

affect the ownership of the wrongdoer, and any claim the defrauded person has will not displace the valid maritime lien. *International Refugee Organization v. Maryland Dry Dock Co.*, (4th Cir. 1950) 179 F. (2d) 284.

Although the courts are in general agreement as to allowing a constructive trust on rescission for fraud,² there is a conflict as to the legal relationship created between the defrauded party and the defrauder. There is some authority for the proposition that the defrauded person is still the legal owner. This may be partly due to the fact that the courts are prone to talk of rescission as revesting the legal title in the original owner.³ However, the majority of the cases hold that the one acquiring the property is the legal owner.⁴ This would appear to be the correct view, as the defrauded person intended to give up the legal title. There is a greater conflict in the cases as to whether the wronged party has any equitable title. Statements may be found to the effect that the wronged person has the equitable title and as equitable owner has the same rights that are present in an express trust.⁵ The result of this in some cases is that the wronged party takes priority over subsequent equitable interests.⁶ The report of the principal case does not give a clear view of IRO's contentions, but IRO seems to have argued, first, that Republic was not the true owner and could not bind the vessel under the statute, and second, that if Republic were the owner, IRO had the equitable title which took free of the lien.⁷ The court denied all the contentions of IRO and agreed with the authorities which state that the constructive trust does not create "ownership" automatically but is merely a remedial device which the court may impose in order to return the property to the defrauded party, giving him greater satisfaction of his claim than he would get at law. The court accordingly held that the ownership of the wrongdoer was

² CORPUS JURIS., Trusts §220 (1933); *Rice v. Allen*, 318 Mich. 245, 28 N.W. (2d) 91 (1947); *Fresh v. Dunakin*, 306 Ky. 87, 206 S.W. (2d) 203 (1947).

³ *Missouri Brown Mfg. Co. v. Guymon*, (C.C.A. 8th, 1902) 115 F. 112; *Hall v. Miller*, (Tex. Civ. App. 1941) 147 S.W. (2d) 266; *Williams v. Logue*, 154 Miss. 74, 122 S. 490 (1929). 4 POMEROY, EQ. JURIS. §1058: "Equity regards the cestui que trust . . . as the real owner and entitled to all the rights and consequences of such ownership."

⁴ *Meier v. Geldis*, 148 Neb. 304, 27 N.W. (2d) 215 (1947); *Binford v. Snyder*, 144 Tex. 134, 189 S.W. (2d) 471 (1945); *Frink v. Commercial Bank of Emmetsburg*, 195 Iowa 1011, 191 N.W. 513 (1923).

⁵ *Shearer v. Barnes*, 118 Minn. 179, 136 N.W. 861 (1912), stating that the constructive trust is an equitable estate arising immediately upon the act of the wrongdoer; *Raasch v. Lund Land Co.*, 103 Neb. 157, 170 N.W. 836 (1919); 3 BOGERT, TRUSTS AND TRUSTEES §472 (1946).

⁶ The wronged party took free of a mortgage placed on the land by the defrauder in *Cann v. Barry*, 298 Mass. 186, 10 N.E. (2d) 88 (1937); *Brennan v. Perselli*, 353 Ill. 630, 187 N.E. 820 (1933).

⁷ IRO may have also contended that even if Republic were the owner, Republic still had possession wrongfully or tortiously and was unable to bind the vessel. IRO could find ample authority to the effect that the defrauder had wrongfully taken or was wrongfully holding the property. Almost all of the cases speak of the defrauder in such words. The court refused to so construe the statute and said that the decreeing of a constructive trust did not mean the title of the owner was defective or his possession tortious. Principal case at 827.

not defective, and that he had power to bind the vessel.⁸ The court did use language which could be construed to mean that IRO had an equitable interest which did not take preference because it was pitted against a superior lien, but the more reasonable interpretation is that the court refused to enforce a remedy which would defeat the statutory security interest deemed desirable to commerce.⁹ In classifying and discussing constructive trusts with express trusts, there is a tendency to mix the remedial aspects with substantive rules, and this in turn may create a new substantive relationship between individuals. It is submitted that the constructive trust should be considered solely as a remedy for the wronged party against the wrongdoer which will not affect innocent third parties' substantive rights in the property.¹⁰

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⁸ *American Sugar Ref. Co. v. Fancher*, 145 N.Y. 552, 40 N.E. 206 (1895); *Falk v. Hoffman*, 233 N.Y. 199, 135 N.E. 243 (1922); Pound, "The Progress of the Law," 33 HARV. L. REV. 420 (1920); 46 MICH. L. REV. 116 (1947); Morehead, "Constructive Trust as a Remedy For Fraud," 14 TEX. L. REV. 252 (1936). See also 31 MICH. L. REV. 826 (1933).

⁹ "Origin of the Maritime lien is the need of the ship." Principal case at 288.

¹⁰ The RESTITUTION RESTATEMENT §160 (1936) treats the constructive trust as setting up two property interests, making it more than a remedy. However in the same work at §172 it states that a bona fide purchaser takes free of the constructive trust and that the same is true of transfers for security, of mortgages, pledges, and liens created by the fraudulent party. This theory would reach the same result as was reached in the principal case.