University of Kentucky
UKnowledge

Continuing Legal Education Materials | Kentucky Legal History

7-2001

Estate Litigation in Kentucky

Office of Continuing Legal Education at the University of Kentucky College of Law

Follow this and additional works at: https://uknowledge.uky.edu/uky_cle

Part of the Estates and Trusts Commons, and the Litigation Commons

Right click to open a feedback form in a new tab to let us know how this document benefits you.

Repository Citation
Office of Continuing Legal Education at the University of Kentucky College of Law, "Estate Litigation in Kentucky" (2001). *Continuing Legal Education Materials*. 51.
https://uknowledge.uky.edu/uky_cle/51

This Book is brought to you for free and open access by the Kentucky Legal History at UKnowledge. It has been accepted for inclusion in Continuing Legal Education Materials by an authorized administrator of UKnowledge. For more information, please contact UKnowledge@lsv.uky.edu.

UK CLE

ESTATE LITIGATION IN KENTUCKY

July 2001

UK
CLE

ESTATE LITIGATION IN KENTUCKY

July 2001

Presented by the
OFFICE OF CONTINUING LEGAL EDUCATION
UNIVERSITY OF KENTUCKY COLLEGE OF LAW

FROM THE LAW LIBRARY OF: _____

_____

Written materials and oral presentations offered through the University of Kentucky College of Law Office of Continuing Legal Education (UK/CLE) are designed to assist lawyers in maintaining their professional competence. The Office of Continuing Legal Education and its volunteer speakers and writers are not rendering legal or other professional services by their participation in continuing legal education activities. Attorneys and others using information obtained from UK/CLE publications or seminars must also fully research original and current sources of authority to properly serve their or their client's legal interests. The forms and sample documents contained in our continuing legal education publications are intended for use only in conjunction with the professional services and advice of licensed attorneys. All parties must cautiously consider whether a particular form or document is suited to specific needs. The legal research presented herein is believed to be accurate, but is not warranted to be so. These written materials and the comments of speakers in presentation of these materials may contain expressions of opinion which do not necessarily reflect the views of the Office of Continuing Legal Education, the University of Kentucky, the Commonwealth of Kentucky, or other governmental authorities. UK/CLE strives to make its written materials and speaker presentations gender-neutral; however, gender-specific references may remain where it would otherwise be awkward or unclear. It should be understood that in such references the female includes the male, and vice-versa.

Copyright 2001 by the University of Kentucky College of Law,
Office of Continuing Legal Education.
All rights reserved.

Printed in the United States of America

UNIVERSITY OF KENTUCKY
COLLEGE OF LAW

OFFICE OF CONTINUING LEGAL EDUCATION

Suite 260 Law Building
Lexington, Kentucky 40506-0048

Phone
(859) 257-2921

Facsimile
(859) 323-9790

Web Address
www.uky.edu/Law/CLE

PRESIDENT, UNIVERSITY OF KENTUCKY: Lee T. Todd, Jr.

DEAN, COLLEGE OF LAW: Allan W. Vestal

DIRECTOR OF CLE: Kevin P. Bucknam

ADMINISTRATIVE/BUSINESS MANAGER: Melinda E. Rawlings

EDITORIAL/MARKETING MANAGER: William G. Nims

UK/CLE: A Self-Supporting Entity

The University of Kentucky Office of Continuing Legal Education (UK/CLE) is an income-based office of the University of Kentucky College of Law. As such, it is separately budgeted and financially self-supporting. UK/CLE operations are similar to not-for-profit organizations, paying all direct expenses, salaries and overhead solely from revenues. No public funds or tax dollars are allocated to its budget. Revenues are obtained from registrant enrollment fees, and the sale of publications. Our sole function is to provide professional development services. In the event surplus funds become available, they are utilized to offset deficits or retained in our budget to improve the quality and variety of services we provide.

ESTATE LITIGATION IN KENTUCKY

TABLE OF CONTENTS

LITIGATION ASPECTS OF THE CLAIMS STATUTE: CLAIMS AGAINST THE DECEDENT'S ESTATE ..... **SECTION A**
Garnie Cliff Stidham

EFFECTIVE HANDLING OF A WILL CONTEST IN KENTUCKY ..... **SECTION B**
Homer J. Parrent III

SUITS ALLEGING FIDUCIARY BREACHES ..... **SECTION C**
David Tachau

ESTATE SETTLEMENT SUITS ..... **SECTION D**
Wayne F. Wilson

DEALING WITH THE INSOLVENT ESTATE ..... **SECTION E**
Chris Meinhart

SPECIFIC EVIDENTIARY ISSUES IN ESTATE LITIGATION ..... **SECTION F**
Thomas W. Miller

VALUATION: COMMON BATTLEGROUND ISSUES & CASE SCENARIOS ..... **SECTION G**
Scott D. Hakala

LITIGATION ASPECTS OF THE CLAIMS STATUTE
[Claims Against The Decedent's Estate]

*G. Cliff Stidham **
Stidham & Associates, P.S.C.
Lexington, Kentucky

** Many thanks to Mark Noel, UK College of Law Class of 2003, for his contribution to this outline.*

Copyright 2001, G. Cliff Stidham

SECTION A

LITIGATION ASPECTS OF THE CLAIMS STATUTE

(CLAIMS AGAINST THE DECEDENT'S ESTATE)

". . . forgive us our debts, as we forgive our debtors."

1. Introduction A-1

2. Claims Against Living Persons A-1

2.1 Statutes of Limitations A-1

2.2 Choice of Forum A-2
2.2.1 Personal Jurisdiction A-2
2.2.2 Subject Matter Jurisdiction A-3
2.2.3 Venue A-4

2.3 Pre-Judgment Remedies A-4
2.3.1 Lis Pendens A-4
2.3.2 Pre-Judgment Attachment A-5

2.4 Enforcing a Judgment A-6
2.4.1 Marital Property Rights A-7
2.4.2 Exemptions A-9
2.4.3 Fraudulent Conveyances A-10
2.4.4 Disclaimers A-12
2.4.5 Spendthrift Trusts A-13
2.4.6 Self-Settled Trusts A-14

3. Claims Against Decedent's Estate A-14

3.1 Survival of Claim A-14

3.2 Statutes of Limitations A-15

3.3 Does the Claim Arise Before, At or After Death? A-18

3.4 Claims That Arose Prior to Death That Are Not Secured, Covered by Insurance or Government Claims A-19
3.4.1 Presentment Within Six Months of Appointment of Personal Representative or Within Two Years of Death of Decedent If No Personal Representative Appointed A-19

SECTION A

3.4.2 Presentment of Claim A-20
3.4.2.1 Suit Not Filed Before Death A-20
3.4.2.2 Actions Pending At Death A-20
3.4.2.3 Presentation Where No Personal Representative Appointed A-20
3.4.3 Due Process: Actual Notice to Known and Reasonably Ascertainable Creditors A-21
3.4.4 Verification of Claim A-23
3.4.5 Contingent or Unliquidated Claim A-24
3.4.6 Deduction of Counterclaim A-24
3.4.7 Compromise of Claim A-24
3.4.8 Waiver of Defense of Limitations A-24
3.4.9 Allowance/Disallowance of Claim A-24
3.4.10 Disallowed Claims - Suit Within Sixty Days A-25
3.4.10.1 Extension of Sixth Day Period for Filing Suit A-25
3.4.10.2 Proper Forum A-25
3.4.10.3 Proving the Claim A-26
3.4.10.4 Judgment As Allowance of Claim A-27

3.5 Claims That Arose At or After Death, Secured Claims, Claims Covered By Insurance, and Government Claims A-27

3.5.1 Presentment A-27
3.5.2 Action Barred Two Years After Discharge of Personal Representative A-27
3.5.3 Proper Forum, Proving the Claim, and Judgement as Allowance of Claim . A-28

3.6 Priority of Claims/Exemptions/Dower A-28

3.6.1 Community Property of Surviving Spouse A-29
3.6.2 Secured Claims A-29
3.6.3 Exemption for Surviving Spouse/Children A-30
3.6.4 Costs and Expenses of Administration A-30
3.6.5 Funeral Expenses A-30
3.6.6 Debts and Taxes With Preference Under Federal Law and Laws of Kentucky A-31
3.6.6.1 Medicaid Claims A-31
3.6.7 Other Claims A-32
3.6.8 Dower and Curtesy A-32

3.7 Payment of Allowed Claims A-33

3.7.1 Contingent, Unliquidated or Future Claims A-33
3.7.2 Interest A-33
3.7.3 Secured Claims A-34
3.7.4 Compelling Payment of Allowed Claim A-34
3.7.5 Liability of Personal Representative A-34

SECTION A

3.7.6 Recovery of Overpayment A-35
3.7.7 Payment When Multi-State Administration A-35
3.7.7.1 Creditor Instituting Ancillary Administration A-36

3.8 Enforcement of Claims Against Other Parties A-36

3.8.1 Individual Liability of Personal Representative A-36
3.8.2 Liability of Distributees A-36
3.8.3 Liability of Decedent's Revocable Trust A-37

3.9 The Relationship Between Bankruptcy Proceedings and Probate A-37

1. Introduction

The law regarding claims against a decedent's estate is primarily found in KRS Chapter 396 (also known as the "claims statute"). Other statutes and case law (discussed below) provide some of the missing pieces of the puzzle not found in KRS 396.

In 1988, the General Assembly revised KRS 396 (effective July 15, 1988) in its entirety as well as amending other statutes which affect claims against a decedent's estate. The 1988 revisions expedite the claims process as compared to prior Kentucky law. The revisions are also much more similar to Part Eight of the Uniform Probate Code (hereinafter "UPC") governing claims against a decedent's estate. KRS 396, however, deviates in many respects from the UPC. A thorough review of KRS 396 is in James R. Merritt, Kentucky Practice: Probate Practice and Procedure (2d ed. 1984) and in James E. Hargrove and Walter R. Morris, Jr., Claims Against the Estate, Kentucky Estate Administration (3d ed. 2000).

2. Claims Against Living Persons

In order to appreciate the litigation aspects of claims against a decedent's estate, it is helpful to first review certain litigation aspects of claims against a living person. Many of the rules and strategies for claims against living persons are modified or have special significance when prosecuting claims against the decedent's estate.

2.1 Statutes of Limitations

One of the most important consequences of the death of the actual or potential defendant or debtor will be the shortening (or, in rare cases, the lengthening) of the statute of limitations for prosecuting the claim. The statute of limitations for the most common claims against living persons are as follows. KRS 413.120(6) imposes a five year limitations period on "an action for an injury to the rights of the plaintiff, not arising on contract and not otherwise enumerated." For actions on a written contract there is a fifteen year limitations period. KRS 413.090(2). Parties may contract around this period, but an agreed upon period that is impermissibly brief, such as one year, has been invalidated by Kentucky Courts. Gordon v. Kentucky Farm Bureau Insurance Company, 914 S.W.2d. 331 (Ky. 1995). An action on a contract not in writing must be instituted within five years. KRS 413.120. An action for malpractice must be brought within one year of the occurrence of the event or when it was discovered or reasonably should have been discovered. KRS 413.245. An action on the ground of fraud or mistake must be instituted within five years after the cause of action accrued. KRS 413.120(11).

The statute of limitations applicable to an action upon judgment, contract or bond, including actions to foreclose or enforce a mortgage is fifteen (15) years after the cause of action first accrued. KRS 413.090 . This section applies to the enforcement of the security of the mortgage only and not the personal obligation of the note. Yeiser v. Webb, 187

S.W.2d 831 (Ky. 1945). The expiration of personal liability on a note does not prohibit the enforcement of the mortgage lien. Id.

2.2 Choice of Forum

Another important aspect of the claims statute is whether it limits the prospective plaintiff as to where suit may be brought when the prospective defendant has died. A quick review of the law regarding choice of forum in suits against living persons may be helpful.

2.2.1 Personal Jurisdiction

For a defendant to be held amenable to suit in any jurisdiction without violating the Due Process Clause of the Fourteenth Amendment, she must have minimum contacts with the forum state such that institution of the suit does not offend traditional notions of fair play and substantial justice. International Shoe v. Washington, 326 U.S. 310 (1945). The International Shoe test is only one of two criteria for obtaining personal jurisdiction over the nonresident defendant. The state long-arm statute must also confer upon the potential claimant the statutory authority to subject to the potential defendant to suit in Kentucky courts. Under Kentucky's liberal long-arm statute, KRS 454.210, there are numerous ways a nonresident defendant may be subject to process, including where the defendant 1) transacts any business in the state; 2) contracts with this state; and 3) causes a tort in this state. If the minimum contacts required by International Shoe are established, the long-arm statute will confer personal jurisdiction.

The Kentucky long arm statute provides that, "as used in this section, 'person' includes an individual, his executor, administrator, or other personal representative." KRS 454.210(1). This clause allows Kentucky claimants to retain a remedial right in their forum even though the potential defendant has died. In Williams v. Carter Brothers Company, 390 S.W.2d 873 (Ky. App. 1965), the plaintiffs sued a nonresident personal representative for damages arising out of an automobile accident where the nonresident decedent was killed in Kentucky. The court upheld the statutory authority allowing the resident claimants to secure personal jurisdiction over the non-resident personal representative. Id. at 874. The Court further held that such jurisdiction did not violate the mandates of due process. Id. at 874.

The long-arm statute of Kentucky, and its application to personal representatives, appears to be a weapon for Kentucky claimants to sue in Kentucky courts over a non-resident decedent's tortious acts. An interesting question is whether the nonresident plaintiff must first present his claim? There is no case on point after the 1988 revisions to Chapter 396. The Williams case relied upon the explicit language of KRS 396.020 which read that nonresidents do not have to first file verified claims with the personal representative. Since this provision has been repealed, and no such language has been added to a new section, by implication it appears that presentation may be required by

nonresidents. As discussed below, all claims appear to have to be first presented to the personal representative under KRS 396.

2.2.2 Subject Mater Jurisdiction

To be held bound by a judgment, the court in its adjudication must have the legal authority to render that judgement. To initiate or remove an action in federal court based on diversity, the amount in controversy must exceed $75,000 and the suit must be between citizens of different states. 28 U.S.C. 1332. There also must be complete diversity, i.e. no plaintiff is a citizen of the same state as any defendant. Carden v. Arkoma Associates, 494, U.S. 185 (1990).

Diversity is dependant upon the citizenship of the relevant parties. Johnson v. Smithsonian Institution, 80 F.Supp.2d 197 (S.D.N.Y. 2000). When an executor sues in his representative capacity on behalf of the decedent, it is the citizenship of the decedent, not the executor, that is pertinent for diversity purposes. However, when a statute gives a personal representative the right to sue on their own behalf for the wrongful death of the decedent, the citizenship of the representative applies. Deposit Guaranty Bank & Trust Company v. Burton, 380 F.2d 346 (6th Cir. 1967). An analysis of which party's citizenship applies depends upon which is the relevant party as defined by the courts.

In Kentucky, KRS 24A.120 confers upon the district court exclusive jurisdiction, with some enumerated exceptions, in civil cases where the amount in controversy does not exceed $4,000. The Kentucky Circuit Court is a court of general jurisdiction with original jurisdiction of all justiciable causes not exclusively vested in some other court. KRS 23A.010.

KRS 24A.120 provides that the district court shall also have exclusive jurisdiction in "matters involving probate, except matters contested in an adversary proceeding. Such adversary proceeding shall be filed in circuit court." KRS 24A.120 (1)(b). The statute does not tell us what constitutes an adversary proceeding. Kentucky courts have ruled that the district court had proper jurisdiction in an action to remove an executor when the facts supporting removal of the executor were not in dispute. Morris v. Brien, 712 S.W.2d 347 (Ky.App. 1986). In addition, an "adversary proceeding" is not "created by the mere opposition of a party to the admission to probate of a will, and that such opposition does not therefore divest the district court of its jurisdiction." Mullins v. First American Bank, 781 S.W.2d. 527 (Ky.App. 1989). Finally, the renunciation of a will was not an "adversary proceeding." McElroy v. Taylor, 977 S.W.2d. 929 (Ky. 1998). Therefore, it appears that at the very least there must be more than a facial showing of an adversarial action to constitute an "adversary action" within the meaning of the statute.

2.2.3 Venue

Jurisdiction relates to the power of the court to hear the subject matter of the case. Britton v. Davis, 103 S.W.2d 665 (1937). Venue, however, relates to the site of the particular court located in the forum state where the action may or must be brought. Stewart v. Sampson, 148 S.W.2d 278 (1937). Therefore, if a state has jurisdiction over the defendant, venue is merely the state's choice, usually statutorily, of where the suit may be instituted.

KRS 452.400 provides that certain actions concerning real property are to be brought in the county where the land is situated. These actions include; 1) For the recovery of real property, or of an estate or interest therein; 2) For the partition of real property except as is provided in KRS 452.420; 3) For the sale of real property under a mortgage, lien, or other encumbrance or charge, except for debts of a decedent; and 4) For an injury to real property. Id. KRS 452.460 governs where an action for injury to person, property or character must be brought. These "must be brought in the county in which the defendant resides , or in which the injury is done." The requirements for where a tort or contract action against a corporation may be brought are governed by KRS 452.450. KRS 452.480 governs where transitory action may be brought. It provides that an action that is not required to be brought in some other county by KRS 452.400 to 452.475 "may be brought in any county in which the defendant, or in which one (1) of several defendants, who may be properly joined as such in the action, resides or is summoned." Breach of contract actions are covered by this section of the venue statute. Wood v. Downing's Administrator, 62 S.W. 2d 487 (1901).

2.3 Pre-Judgment Remedies

Even before judgment is obtained against a living person, the plaintiff may take action against the defendant's property to help ensure the successful enforcement of any judgment obtained. How are these pre-judgment remedies affected by the death of the defendant?

2.3.1 Lis Pendens

One method employed to ensure the recovery of an expected judgment is the filing of a lis pendens. Lis Pendens is a notice "to warn all persons that certain property is the subject matter of litigation, and that any interests acquired during the pendency of the suit are subject to the outcome of the litigation." Black's Law Dictionary, 943 (7th ed 1999). The purpose of a lis pendens is to protect a subsequent bona fide purchaser of the property in question by placing a notice on that property that the pending litigation may limit its transferability. Leonard v. Farmers and Trader Bank, 605 S.W.2d 770 (Ky.App. 1980). Also, where a lis pendens is properly filed during litigation, a subsequent bona fide purchaser is put on constructive notice of the cloud upon title and may, depending on the

outcome of the litigation, lose their interest in the subject property. Roberts v. Cardwell, 157 S.W. 711 (Ky.App. 1913).

KRS 382.440 governs a notice of lis pendens. The statute provides that no action of any kind, except actions for forcible detainer or forcible entry or detainer, "commenced or filed in any court of this state ... shall affect the right, title or interest of any subsequent purchaser, lessee, or encumbrancer of such real property," or interest for value, "except from the time there is filed, in the office of the county clerk of the county in which such real property or the greater part thereof lies, a memorandum." This memorandum shall state: a) The action's number, the style of the proceeding, and the court in which it is commenced; b) The name of the person whose title, right, or interest in real property is affected; and c) A description of the real property in the county thereby affected. KRS 382.440. This notice "may be filed by any party in interest. Id. A separate notice shall be filed in each county where property is affected. Id.

The recent Supreme Court case of Greene v. McFarland, 43 S.W.3d. 258 (Ky. 2001) addressed the proper use a lis pendens. "[A]ctions for general debt do not give rise to a valid lis pendens because there is no actual lien or interest in the real property." Id. at 260. Therefore, a claimant for general debt may not validly cause a lis pendens to be issued simply because it seeks a general remedy out of this property. "It is not sufficient that the property be the source out of which the plaintiff will be compensated." Levin v. George Fraam & Sons, Inc., 585 N.E.2d. 527 (Ohio.App.9th Dist. 1990).

An interesting situation could occur when an action and a valid lis pendens are filed against a defendant and the defendant dies prior to judgment for the plaintiff. Would the property that was lawfully encumbered by the lis pendens remain subject to it and the plaintiff recover as if he were a secured creditor following judgment after the death of defendant property owner? Or would the lis pendens be invalidated and the plaintiff be treated as any other unsecured creditor? While KRS 396.135 provides that no execution or levy may be made against the property of a decedent, the statute also provides that it is not intended to prevent the enforcement of a lien upon real property in an appropriate proceeding.

2.3.2 Prejudgment Attachment

KRS 425.301 allows the plaintiff, at or after the commencement of the action, to attach the property of the defendant as security for the satisfaction of the contemplated judgment for money damages. The statute permits such an attachment if the defendant a) is a foreign corporation or nonresident; b) has been absent from the state for four months; c) has departed from the state to avoid his creditors; d) has left his resident county to avoid service; e) so conceals himself that a summons cannot be served upon him; f) is about to remove, or has removed, a material portion of his property out of state while leaving an insufficient amount to satisfy creditors; g) has conveyed his property with fraudulent intent to hinder or delay his creditors; or h) is about dispose of his property

with such intent. KRS 425.301(1). Attachment is "tantamount to an involuntary dispossession of the property of the defendant prior to any adjudication of the rights of the plaintiff." Placer Coal, Inc. v. Rhondale Coal Services Company, 684 S.W.2d 25 (Ky.App. 1984). Attachment "may only be had in satisfaction of the debt." Id. 30. In addition, a defendant who has been subjected to a wrongful attachment may collect damages for such wrongful attachment. Id.

KRS 396.135 (discusses below) disallows an execution pursuant to a judgment against a decedent or personal representative (with the exception of the enforcement of a secured debt). This prohibition would seem to logically disallow a prejudgment attachment after the decedent's death. The prejudgment attachment would be superfluous due to the fact that it may not be validly executed upon once a judgment is entered after the decedent's death. Also, the personal representative of the estate has the fiduciary duty to creditors of the estate to see that estate assets are not dissipated.

2.4 Enforcing a Judgment

Once a personal judgment is obtained, KRS 426.010 allows an execution to be made against the property of the defendant. In Kentucky, "a court has the authority to enforce its own judgments." Shelby Petroleum Corporation v. Croucher, 814 S.W.2d. 930 (Ky.App. 1991). KRS 426.120 provides that an execution shall bind the estate of the defendant only upon its delivery to the proper officer to execute. The law gives preference to the first execution that comes into the hands of the appropriate officer. KRS 426.120. In addition, the effect of an execution under KRS 426.120 is to create a lien for its payment from the time the execution has been delivered. Credit Trust Co. v. Daniel Boone Coal Corporation, 58 F.2d 305 (6th. Cir. 1930).

Absent a statutory provision permitting it, "attachment or garnishment proceedings will not, at the instance of a creditor of a decedent or a decedent's estate, lie against an administrator or an executor to reach property or debts of the decedent, at least prior to an order of distribution." American States Insurance Company v. Citizens Fidelity Bank & Trust Company, 662 S.W.2d. 851 (Ky.App. 1983). Kentucky had no statutory provision permitting execution against an estate and now has a statute prohibiting it. KRS 396.135 disallows an execution pursuant to a judgment "against a decedent or personal representative." This makes it advisable to obtain a judgment and execution prior to the defendant's death. The rationale for disallowing an execution or post-judgment attachment pursuant to a judgment against the estate of the decedent is clear. If courts that are not involved in the probate process allow executions on various judgments against the decedent, then the statutory priority of claims paid may be altered if the debtor has insufficient assets to pay all debts.

However, KRS 396.135 also provides that the statute shall not be construed to prevent to the enforcement of "liens upon real or personal property in an appropriate proceeding." KRS 396.135. Kentucky law allows a final judgment to act as a lien on

realty with certain notice requirements. KRS 426.720. The creditor must file with the clerk a notice of judgment lien as well as send a copy of the notice to the creditor's last known address. Also, if an execution can be obtained pursuant to a judgment against a living person, it should be treated as a secured claim following the defendant's death with priority over other claimants of the estate upon distribution. In McCook National Bank v. Bennett, 537 N.W.2d 353 (Neb. 1995) the Court held that a judgment lien was not a "claim" against the decedent's estate subject to the presentation requirements and the judgment lienholder could institute a proceeding in the trial court on the lien without filing a claim in probate proceedings. The remedial nature of obtaining and enforcing a judgment presents a great advantage to the claimant who successfully sues the debtor while alive rather than against her estate.

2.4.1 Marital Property Rights

In executing upon a judgment against a married debtor, a very important question is who within the marriage actually owns the assets. This issue of marital property rights is resolved by looking at the domicile of the spouses when the property in question was acquired. See Restatement of the Law (Second) of Conflict of Laws §§ 233-234, 257-259. (1971 & 1988 Rev.) There are two basic forms of marital property rights. Kentucky and forty other states are common law property states. Nine states (Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin) are community property states.

In common law states, ownership of property is generally determined by how record title to the property is held. However, the spouse of the record title holder has inchoate rights in the property (unless waived by agreement or forfeited by misconduct, e.g., killing the spouse or living in adultery) that become choate upon entry of a divorce decree or the death of the record title holder. Kentucky law provides that upon divorce the parties' "marital property" is divided in "just proportions" as determined by the court based upon all the circumstances. KRS 403.190(1). Marital property is, generally, all property acquired during the marriage other than by gift, bequest, devise or inheritance. KRS 403.190(2). A spouse is awarded his or her separate or non-marital property which is, generally, any property acquired prior to the marriage and all property acquired during the marriage that is not marital property. KRS 403.190(1) & (2).

Upon the death of a spouse, Kentucky law provides that the surviving spouse receives in fee one-half of the deceased spouse's "surplus" personalty and one-half of the deceased spouse's "surplus" real estate, as well as a life estate in one-third of any real estate owned in fee simple during the marriage and conveyed during the marriage without the surviving spouse's interest being relinquished, barred or forfeited. KRS 392.020. Upon the death of a spouse testate, the surviving spouse may elect against the will and receive what she would have received had the other spouse died intestate, except that the surviving spouse receives only a one-third interest in fee in the deceased spouse's

"surplus" real estate. KRS 392.080. The distinctions of marital and separate or (non-marital) property are irrelevant.

The term "surplus" with respect to the deceased spouse's personal property means such spouse's personal property remaining after payment of her debts (including estate administration and funeral expenses) and the surviving spouse's $7,500 exemption. Mattingly v. Gentry, 419 S.W. 2d 745 (Ky. 1967); KRS 391.030(1)(c). The term "surplus" with respect to real estate means the real estate remaining after the payment of the decedent's debts. Mattingly v. Gentry at 747. The life estate of the surviving spouse in one-third of the real estate conveyed by the deceased spouse during the marriage without the surviving spouse's interest being released, barred or forfeited comes before the debts of deceased spouse. Id.

In community property states, generally, property "earned" during the marriage is "community property". Norvie L. Lay, Multi-State Problems In Estate Administration, Kentucky Estate Administration (3rd ed. 2000) at 26. Community property does not include "separate property" which is, generally, property acquired by a spouse before the marriage or after the marriage by gift, bequest, devise or inheritance. Community property is owned one-half by each of the spouses regardless of which spouse earned it and regardless of how title to the property is held. Id. at 26. This ownership is choate, not inchoate. Community property rights are not forfeited when the married couple moves from the community property state to Kentucky, and this is true even if community property is sold after they are domiciled in Kentucky and the proceeds reinvested in Kentucky real estate in the name of only one of the spouses (assuming the non-record owner spouse did not intend to make a gift of her community property interest to the other spouse). Id. At 27.

In Kentucky, a common law property state, an unsecured creditor could execute upon the personal property in titled in the name of a living spouse without concern for the inchoate rights of the other spouse in the personal property. The same is true for real estate except for the inchoate right of the non-debtor spouse to a life estate in one-third of the real estate owned and conveyed by the debtor spouse during the marriage without release of this interest. Mattingly v. Gentry, at 746. Presumably, this one-third life estate interest could be valued and execution sale proceeds set aside for her interest. See Mattingly.

In a community property state a creditor of only one of the spouses could not execute upon the community property (real or personal and regardless of how title was held) without respecting the other spouse's interest in the property. Estate of O'Conner, 23 P.2d 1031 (1933). Since the ownership right in community property is a vested property interest, these interests cannot be lost as a result of their change in domicile to Kentucky. Lay, Supra. at 27. Accordingly, in Kentucky, with respect to the community property brought into the state, the creditor of the debtor spouse should have to respect the community property interest of the non-debtor spouse in executing upon the property

(whether real or personal and regardless of how title was held). Clearly the non-debtor spouse would have to assert her interest in the community property to protect it from her spouse's creditors.

2.4.2 Exemptions

In executing upon a judgment against the property of a living person, KRS Chapter 427 exempts certain property of an individual debtor such that it is immune from attachment to satisfy her debts.

KRS 427.060 allows a maximum $5,000 homestead or burial plot exemption to be exempt from execution. This exemption differs from the other exemptions of KRS 427 in that the exemption applies to the property that "such debtor or a dependent of such debtor uses as a permanent residence in this state, or in a burial plot for such debtor or a dependent of such debtor. Id. KRS 427.070 provides that the homestead exemption shall be "for the use of the widow so long as she occupies it, and the unmarried infant children are entitled to joint occupancy with her until the unmarried child arrives at full age. The termination of the widow's occupancy shall not affect the rights of the children." Id. Therefore, it is clear that the statutory intent is to make this exemption available to the surviving spouse and children.

A search of Kentucky cases reveals that there is not a great deal of recent controversy concerning homestead. In fact, almost all cases reported were decided prior to 1960. One possible reason for this is that Kentucky case law provides that the homestead exemption for the surviving spouse is not absolute. The surviving spouse is required to elect between her dower interest and her interest in homestead. Berger v. Berger, 94 S.W.2d 618 (1936). Since the right in homestead is so small, the election of the widow is normally in favor of dower. Harrison v. Taylor's Administrator, 51 S.W. 193 (1899). Another reason why there have not been many reported cases regarding homestead is that many decedents own no real property. Frederick R. Schneider, Recommendations for Improving Kentucky's Inheritance Laws, 22 N.Ky.L.Rev. 317 (Spring 1995).

The remaining exemptions under KRS 427 apply only to the debtor and not her spouse or dependents. Some of the exemptions are as follows. KRS 427.010 provides an exemption to the individual debtor of $3000 for household furnishings, jewelry, personal clothing, and ornaments; tools equipment, and livestock of farmers not to exceed $3000; and one motor vehicle not to exceed $2500. Id. The professional library, office equipment, instruments and furnishings of a professional, necessary in the practice of such profession, are exempt up to $1000. KRS 427.040. Police and firefighters' pension funds are exempt in some cases. KRS 427.120. "Any money to be paid or rendered by a ... life or casualty insurance company is exempt from execution." KRS 427.110. This statute creates some ambiguity as to whether only the cash value of the insurance policy is exempt or if their paid proceeds are also exempt. In Thompson et al. v. Latimer, 273 S.W. 65 (Ky.App. 1925) the court held that the insured may designate his children as beneficiaries

to a life insurance policy and its proceeds were exempt from the decedent's estate and therefore not part of the probate estate but an asset of the children. However, it was also held that the proceeds of an insurance payment were not exempt after they were invested in real estate, except to the extent of homestead and other statutory exemptions. Merrell Drug Co. v. Dixon, 115 S.W. 179 (Ky.App. 1909).

KRS 427.150 allows exemptions for reasonably necessary alimony, support, or separate maintenance payments as well as total exemptions for a) an award under a crime victim's reparation law; b) a wrongful death payment reasonably necessary for support; c) A payment, not to exceed $7500, on account of personal bodily injury; d) a payment in compensation of loss of future earnings of the debtor; e) assets, payments, and accounts payable under statutorily exempt pensions; f) "the right or interest of a person in an individual retirement account or annuity, deferred compensation account, tax sheltered annuity, simplified employee pension, pension, profit-sharing, stock bonus" or other tax deferred retirement account. This exemption does not apply to any amounts contributed to the above accounts within 120 days of filing bankruptcy. KRS 427.150. This exemption also does not apply to the extent that the interest is subject to a court order for the payment of maintenance or child support. Id.

The only remedy an insolvent debtor has with regards to exemptions from creditors in Kentucky is that of KRS 427. The federal bankruptcy exemptions, contained in 11 U.S.C. 522, may not be claimed by Kentucky residents because Kentucky has opted out of these exemptions and replaced them with there own. In Re Raymond, 103 B.R. 846 (W.D. KY 1989). KRS 427.170 illustrates the clear intention of the state legislature to opt out of the federal exemptions and replace them with there own. Consequently, the Federal Bankruptcy court must apply the Kentucky state exemption statute (KRS 427) in bankruptcy cases. In re Raymond.

While KRS 427 enumerates many very specific and detailed exemptions that only the individual debtor may claim (with the exception of the homestead exemption), Kentucky law only allows a $7,500 spousal or children's exemption of personal property that is not subject to claimants of the probate estate. KRS 391.030. As discussed above, dower and curtesy now come only after payment of all creditors from surplus property (with the exception of the one-third life estate in property conveyed during the marriage without release of the dower). See Mattingly.

2.4.3 Fraudulent Conveyances

A debtor may attempt to render herself judgment proof by gifts, discounted sales or full value sales of assets to family members or other persons before the plaintiff/creditor can obtain a judgment and execute upon it. Such transfers may be voided by the judgment creditor and the transferred asset recovered for satisfaction of the judgment, if it can be shown that the transfer violated Kentucky's fraudulent conveyance statutes. KRS Chapter

378 contemplates and provides remedies for three different types of fraudulent conveyances.

KRS 378.020 provides that all transfers that are not for valuable consideration are void as to then existing creditors. KRS 378.020. This section has no application to conveyances executed prior to creation of the debt being sued upon. Cornett v. Brashear, 9 S.W.2d 302 (Ky. App. 1928). However, under this section, every transfer without any real or valuable consideration may be void as to the grantor's then existing creditors regardless of the grantee's knowledge that the gift or conveyance was executed with the intent to defraud creditors. Walker v. First National Bank, 111 S.W. 328 (Ky. App. 1908). Since the grantee in this section has given no valuable consideration, the law favors the rights of the defrauded creditors.

Even where valuable or even full consideration is given, KRS 378.010 renders transfers made "with the intent to delay, hinder, or defraud creditors" void, except as to purchasers for valuable consideration without knowledge of the transferor's fraudulent intent. Therefore, a creditor may sue to set aside a conveyance for valuable consideration only if the grantee had actual knowledge of the grantor's intent. James v. Stokes, 261 S.W. 868 (Ky. App. 1924). This provides protection for bona fide purchasers for value in that his purchase will not be overturned. This section applies not only to existing creditors but subsequent creditors as well. Id.

When a conveyance is attacked as fraudulent and badges of fraud are shown, the burden of proof to show good faith is shifted to the grantee. Trent v. Carroll et al., 380 S.W.2d 87 (Ky.App. 1964). A transfer of property in anticipation of a lawsuit or during a pending lawsuit has been found to be a badge of fraud. Id. At 89. Inadequacy of consideration is another badge. Id. "When there are badges of fraud the purchaser is put on inquiry, and his good faith depends on the sufficiency and reasonableness of his inquiry." Id. at 90. Therefore, when the purchaser knew of the conveyance prior to a suit, and was told by the grantor that it had been settled, evasive answers when the purchaser was asked in court if he knew that it had not been settled illustrate a lack of good faith on the part of the purchaser. Id. at 90. One may not color a transaction showing badges of fraud with good faith simply by performing a title search and relying on the representations of the grantor. Id. Therefore, even if valuable consideration is paid, inquiry notice is a weapon a creditor can use to establish the purchaser's knowledge of the seller's fraudulent intent and set aside the conveyance.

A final method of overturning a conveyance as fraudulent is by attacking a payment to a specific creditor as preferential. The effect of the transfer can be abrogated if it is made "in contemplation of insolvency and with the design to prefer one or more creditors to the exclusion, in whole or part, of others." KRS 378.060.

With knowledge of failing health or impending death, a debtor may be tempted to rid his estate of certain property in order to keep it out of the hands of his creditors after

his death. Under KRS 378.030, the personal representative or transferees of a deceased debtor may be sued to set aside a conveyance as fraudulent. The statute allows any aggrieved party, such as a creditor, to sue to set aside the transfer. Id. For example, a father, who loaned his son a sum of money prior to his son's death, could sue to recover that amount which was allegedly fraudulently conveyed by the son prior to death. McMurry v. McMurry, 410 S.W.2d 139 (Ky.App. 1966). A mortgage from brother to brother-in-law was found to be an invalid conveyance in fraud of creditors and therefore part of decedent's estate and subject to claims. Hardy v. Peoples State Bank & Trust Co. Et al., 229 S.W.2d 771 (Ky. App. 1950). Also, a widow successfully sued, individually and as administrator of her late husbands estate, to have a trust which was entered into on the eve of the wedding naming the late husbands children beneficiaries set as a fraud on the dower. Mathias v. Martin, 2000 WL 1479595 (Ky.App.).

2.4.4 Disclaimers

An interesting situation occurs when an actual or potential defendant/debtor is to receive a gift, bequest, devise or inheritance. Once the property is actually or constructively received, it will be subject to the claims of the recipient's existing and future creditors. To avoid this result, the debtor may wish to disclaim the gift so it will pass to the alternate takers (who are often family members) under the deed or will, the lapsed legacy statute or the laws of intestate succession.

KRS 394.035 (nontestamentary instruments) and KRS 394.610 (transfers at death) provide that a living person or his legal representative may disclaim in whole or in part the right of transfer or succession to such person in any property or interest therein, including a future interest. To disclaim the property, the person (or his legal representative) must file a written disclaimer with the transferor (in the case of a nontestamentary transfer) or district court (in the case of a testamentary transfer) within nine months of the effective date of the nontestamentary instrument or death of the decedent transferor, as the case may be. The right to disclaim survives the death of the person having it and may be exercised by the personal representative. Id. The property or interest disclaimed devolves as if the disclaimant had predeceased the donor. Id. In addition, a disclaimer relates back to the death of the decedent. Id.

But how are a creditor's rights affected by this statute? Does the statute intend that creditors of the disclaimant shall have no right of recovery as to the disclaimed property even if the disclaimant intended to disclaim the property solely to protect the inheritance from creditor's claims? The relation back provision and legal effect of the disclaimant predeceasing the decedent arguably make that intention evident. However, a recent Supreme Court case interpreting the Arkansas disclaimer statute makes this less clear. Drye v. United States, 528 U.S. 49 (1999). In this case, the Court held that the right of the appellant to disclaim an inheritance was a "right to property" and thus subject to a federal tax lien. In its decision, the Supreme Court relied heavily on the language of the statute authorizing a federal tax lien. Id. at 60.

Can this rational be applied to an individual creditor of the disclaimant? Would a security interest in all property and rights to property of a disclaimant reach the right to disclaim? What if such right were specifically mentioned as being subject to the security interest? What about using the fraudulent conveyance statutes to void the disclaimer? Kentucky's fraudulent conveyance law covers "every gift, conveyance, assignment or transfer" of property.

A federal bankruptcy court has ruled (subsequent to Drye) that the Oregon fraudulent conveyance statute would not void a disclaimer made by a debtor. In re Nistler, 259 B.R. 723 (D.Ore 2001). The Court held that debtor's disclaimer of inheritance was not a transfer of any "interest of the debtor in property." Id. at 725. This was because the disclaimer related back in time and debtor was treated as never legally having possessed an interest in the inheritance. Id. Because a disclaimer includes a relation back provision, the effect of a disclaimer is the same as if the disclaimed interest had never been created and the disclaimant never had an interest in the estate. Frances Slocum Bank and Trust Co. v. Estate of Martin, 666 N.E.2d 411 (Ind.App. 1996). The Supreme Court of Illinois also entertained a suit where a creditor attempted to attack a disclaimer as a fraudulent conveyance. Thompkins State Bank v. Niles, 537 N.E.2d 274 (Ill. 1989). It held that a disclaimer "is not a voluntary conveyance and is not subject to attack by creditors." Id. at 227. The Illinois fraudulent conveyance statute the court interpreted was very similar to Kentucky's in that it covered "every gift, grant, conveyance, assignment or transfer." Ill.Rev.Stat.1985, ch. 59, par. 4.

2.4.5 Spendthrift Trusts

In executing upon her judgment, a creditor may attempt to reach the interest of the debtor in a trust. KRS 381.180 covers estates in trust that are subject to the debts of the beneficiary. Unless a trust is a "spendthrift trust", estates of every kind that are held in trust shall be subject to the debts and charges of the beneficiaries. KRS 381.180(1). The definition of a spendthrift trust is "a trust in which by the terms of the instrument creating it a valid restraint on the voluntary and involuntary alienation of the interest of a beneficiary is imposed. KRS 381.180(2). The creation of a spendthrift trust is not contingent upon any specific language but, rather, a manifest intention to create a spendthrift trust. KRS 381.180(3). If the instrument creating the trust provides that a beneficiary is entitled to receive income of the trust or principal of the trust at a future time, and that his interest shall not be alienable by him and shall not be subject to alienation by operation of law or legal process, the restraint on the voluntary and involuntary alienation of his right to income and principal is valid. KRS 381.180 (4) $& (5).

Even if the trust is a valid spendthrift trust, the interest of the beneficiary shall be subject to the satisfaction of an enforceable claim against the beneficiary: a) by a spouse or child for support or a spouse for maintenance; b)by providers of necessary services rendered to the beneficiary or necessary supplies furnished to him; c) by the Federal or

State government for taxes due on account of the beneficiary's interest or income from the trust. KRS 381.180(6).

While the provisions of this statute appear fairly unambiguous, the one provision that seems to leave the door open for interpretation is the subjecting of interests in trusts assets to claims by providers of "necessary services rendered to the beneficiary or necessary supplies furnished to him". KRS 382.180(6)(b). In one case, necessaries were described as board, lodging, clothing, and doctor bills. Newland v. McNeill, 126 S.W.2d. 127 (Ky. 1939).

2.4.6 Self-Settled Trusts

If a person creates a trust for his own benefit restraining alienation of his interest, "his interest nevertheless shall be subject to alienation by operation of law or legal process. KRS 381.180(7). Nonetheless, one may create a trust for his own benefit with a provision restraining voluntary or involuntary alienation if it is an interest in "an individual retirement account or annuity, tax sheltered annuity, simplified employee pension, pension, profit-sharing, stock bonus, or other retirement plan described in Internal Revenue Code of 1986 ... which qualifies as a deferral of current income tax." KRS 381.180(7)(b). This is consistent with the exemption under KRS 427.150.

Alaska and Delaware in 1997, and Nevada and Rhode Island in 1999, have adopted legislation designed to permit what are referred to as "domestic asset protection trusts". The legislation provides that a settlor's retained interest in a self-settled trust are not reachable by the settlor's creditors except in rare circumstances. To my knowledge, this legislation has not yet been tested in the courts by motivated creditors.

3. Claims Against Decedent's Estate

3.1 Survival of Claim

To maintain an action against a decedent's estate, that action must survive at law. Under common law, tort claims died with the tortfeasor but contract claims survived the death of the obligor and could be enforced against her estate. Merritt. at 247. KRS 411.140 modifies the common law rule regarding tort claims by providing that "no right of action for personal injury or for injury to real or personal property" is extinguished by the death of the injured or injuring person, "except actions for slander, libel, criminal conversion, and so much of the action for malicious prosecution as is intended to recover for the personal injury." The statute further provides that actions for any other injury may be brought by or against the personal representative in the same manner as contract actions. While the statute has narrowed the types of tort claims that do not survive the death of the tortfeasor (at common law no tort claims survived the tortfeasor's death), the statute now extinguishes certain tort claims upon the death of the injured party (i.e.,

slander, libel, criminal conversion and malicious prosecution to extent recovery for personal injury) which did not occur at common law.

Payments for alimony and support may not survive the death of the decedent, depending on the provisions of the divorce decree. Shepard v. Shepard, 521 S.W.2d 74 (Ky.1975).

In light of the above, a claimant who is concerned about a possible compulsory or permissive counterclaim being attached to his suit may wish to bring the action after the potential defendant has died, depending on whether the counterclaim survives at law. Conversely, if a potential plaintiff's claim will not survive his death, the action should not be postponed in the absence of any other good reason for delay.

3.2 Statutes of Limitations

As noted above, death brings into play additional statutes of limitations that supplement or override the statutes of limitations for claims against a living person. Most of the post-death statutes are summarized below and discussed in greater detail in the following sections.

The first and most important statute is KRS 396.011(1), which provides that a claim against a decedent's estate "which arose before the death of the decedent", if not barred earlier by another statute of limitations, must be -

- "presented" within six months of the appointment of the personal representative, or
- or "presented" within two years of the death of the decedent where no personal representative is appointed,

or the claim will be barred against the estate, the personal representative, and the heirs and devisees of the decedent. This limitation does not apply to secured claims (but only to the extent of the security); claims for which the decedent (or his personal representative) is protected by liability insurance (but only to the extent of the insurance protection); claims of federal, state or local government; or claims that arose at or after the death of the decedent. KRS 396.011(1) and (2).

KRS 396.035 provides that an action shall not be brought against a personal representative on a claim against the decedent's estate unless the claimant first "presents" his claim in the manner described in KRS 396.015. KRS 396.015 provides a method of presentation (discussed below) but not a time limit for the presentation. KRS 396.035 does not appear to limit its application to claims that arose before the decedent's death, as does KRS 396.011.

KRS 396.055 provides that if the personal representative disallows a claim which was "presented" in the manner described in KRS 396.015 within the time limit provided in

KRS 396.011 (the six-month rule), the claim will be barred unless the claimant "commences an action" against the personal representative within sixty days after the mailing of the notice of disallowance, provided the notice of disallowance warns the claimant of the impending bar. KRS 396.055 appears to limit its application to claims that arose before the decedent's death (other than secured, insured and government claims), given its reference to KRS 396.011. The statute does not specify in which court the action is to be commenced.

KRS 396.205 provides that -

- not withstanding any other statute to the contrary,
- if a cause of action is not otherwise barred by -
  - KRS 396.011 (the six-month rule),
  - KRS 396.055(1) (the 60-day rule), or
  - any other applicable statute of limitations,
- it may not be "brought" against the personal representative or against any distributee after the expiration of two years from the date of the order of discharge of the personal representative. However, this rule does not apply to an action based on fraud of the personal representative or a distributee. KRS 396.025.

KRS 396.205 appears to apply to all claims, including claims that arose at or after the decedent's death, and all claims that arose prior to the decedent's death, including secured claims, insured claims and government claims. There are no annotations or court interpretations of this section. The language bars actions that are not "brought" after the expiration of two years from the discharge of the personal representative. Since the personal representative has been discharged and the term "brought" is used rather than "presented", one would infer that the procedure for this type of action would be in the form of an original action filed in some court (not specified by this statute) rather than first presenting the claim as required by KRS 396.035 (which says all claims must first be presented).

KRS 396.045(1) provides that a claim shall not be barred by a statute of limitations (other than a statute of limitations contained in KRS 396) that expires during the six-month period beginning with the decedent's death, if the claim is presented within six months after the decedent's death. The proper presentment of a claim under KRS 306.015 is deemed to be a commencement of an action on the claim for purposes of any statute of limitations. KRS 396.045(2).

The personal representative must have some time to familiarize himself with the assets and liabilities of the estate. Accordingly, no action may be brought against a personal representative of a decedent's estate until two months after the appointment of the personal representative. KRS 395.270. This prohibition, however, does not apply to an executor de son tort (i.e., a person who assumes to act as executor of an estate without authority to do so), or to an alleged creditor whose claim has been denied in writing by the

personal representative. Id. Any action brought in violation of this rule will be dismissed with costs. Id.

KRS 395.278 provides that an application to revive an action in the name of the personal representative or successor of a plaintiff, or against the representative or successor of a defendant, must be made within one year after the death of the deceased party. Actions by or against a person who later dies do not continue unless a party applies to the court to revive the action within one year of the decedent's death. See Snyder v. Snyder, 769 S.W.2d 70 (Ky. Ct. App. 1989).

KRS 413.160 provides that an action for relief not otherwise provided for by statute can only be commenced within ten years after the cause of action accrues. This catch-all limitation period was held to apply to a claim for the inheritance of personalty, which began to run upon the death of the decedent. Wood v. Wingfield, 816 S.W.2d 899 (Ky. 1991).

KRS 413.170 provides for an extension of the limitations period applicable for actions under KRS 413.090 to 413.160 that accrue during the minority or "unsound mind" of the claimant. Once the minor or disabled person dies, however, the statute of limitations begins to run and the action must be brought (except for a penalty or forfeiture) within the same number of years as a person without a disability would have to file the action. KRS 413.170(1).

KRS 413.180 covers an action by or against a personal representative under the limitations period governed by KRS 413.090 to 413.160. Subpart one declares that if a person who is entitled to bring such an action dies before the expiration of the applicable limitations period and the cause of action survives, the personal representative may bring the action after the period has run, as long as the action is commenced within one year after the qualification of the representative. Subpart two covers situations where a personal representative is appointed more than one year after the death of the decedent and the decedent dies before the limitations period in KRS 413.090 to 413.160 has run. If this is the case, for the purposes of this chapter, the personal representative will be deemed to have qualified on the last day of the one year period. This means that, regardless of when a personal representative is qualified, the longest an applicable statute of limitations may be extended under this section is two years. Note once again that this section encompasses any person entitled to bring an action in this chapter. It is applicable to both suits by and against the personal representative.

KRS 395.010 provides that "original administration shall not be granted after the expiration of ten (10) years from the death of the testator or intestate and if made after that time, it shall be void."

3.3 Does the Claim Arise Before, At or After Death?

The time limitation and method for pursuing a claim against a decedent's estate may turn on whether the claim arose before, at or after the decedent's death. The six months limitation period to present a claim after the appointment of the personal representative under KRS 396.011(1) only applies to "claims which arose before the death of the decedent", excluding secured claims (but only to the extent of the security); insured claims (but only to the extent of the insurance coverage) or claims of federal, state or local government. KRS 396.011(1) and (2).

The Kentucky Supreme Court has defined a claim against a decedent's estate that is governed by KRS 396.011(1) as "debts or demands against the decedent that might have been enforced in his lifetime." Underwood v. Underwood, 999 S.W.2d. 716 (Ky.App. 1999). This is the rule whether the claim is due or to become due, liquidated or unliquidated, or founded on any legal basis. KRS 396.011(1). The fact that a claim may not be due until after the statute of limitations under Chapter 396 has run does not insulate the claimant from the presentment requirements of Chapter 396.

The question arises as to whether a claim based on a promise to bequeath something in a will, or founded on an agreement prior to, or upon the dissolution of, marriage, arises before death. While one could argue that in these cases the decedent promisor had an affirmative duty to provide for this in a will prior to death and the claim is one that arises prior to death, another argument could be made that such a claim necessarily cannot arise until the decedent has died and leaves a will that breaches the contract. The latter interpretation will likely be the most plausible given the fact that an actual breach would not occur until the time has come for the distributees to obtain their interests in the will.

In Underwood, the court clarified this question by declaring that "if the decedent took no action during his lifetime which could have prompted litigation, then the claim cannot be said to have arisen during the decedent's lifetime." Id. at 719. The Court held that husband's failure to take steps to ensure that his former wife would receive survivor benefits from his national Guard pension, as required by the dissolution decree, was a breach of that duty prior to his death and subject to the six-month presentation requirements. Id. at 719. However, a divorced wife's claim for the continuance of maintenance after the husband's death, as provided by the dissolution decree, was not subject to the six-month statute of limitations because the cessation of maintenance occurred after death. Id. In Ellis v. Ellis, 752 S.W.2d. 781 (Ky. 1988) the Court held that expected heirs do not have a claim arising prior to the death of the decedent. Also, a valid contract to devise property in a will does not deprive the parties thereto of complete control of their respective properties ... unless a plain intention to this effect is set out in the will or in the contract pursuant to which it was executed." Boner's Administratrix v. Chesnut's Executor, 317 S.W.2d. 867 (Ky. App. 1958). The reading of these cases together suggests that a claim for the contractual obligation to devise property in a will is

not enforceable prior to death, and therefore not subject to the six-month presentation requirements, without express and unambiguous language to the contrary in the document.

When the executor commits an act which gives rise to a claim after the decedent has died, the claim clearly arises after the decedent's death. Batson v. Clark, 980 S.W.2d 566 (Ky.App. 1998).

3.4 Claims That Arose Prior to Death That Are Not Secured, Covered by Insurance or Government Claims

3.4.1 Presentment Within Six Months of Appointment of Personal Representative or Within Two Years of Death of Decedent If No Personal Representative Appointed

Claims arising before the decedent's death that are not barred by another applicable statue of limitations, and that are not secured, covered by insurance or government claims, are barred unless "presented" within six months of the personal representative's appointment or within two years after the decedent's death if no personal representative is appointed. KRS 396.011(1). If the claim would be barred by a statute of limitations outside of Chapter 396 that expires during the six month period beginning after the decedent's death, then the claim will be timely if it is "presented" within six months after the decedent's death (not six months after the appointment of the personal representative). KRS 396.045(1). The "proper presentment" of a claim under KRS 306.015 is deemed to be a commencement of an action on the claim for purposes of any statute of limitations. KRS 396.045(2).

KRS 396.011(1) also provides that claims "where no personal representative has been appointed" are barred against the estate "within two (2) years after the decedent's death". This statute seems to be self-executing in that it is not triggered by a court action but on the death of the decedent. Such statutes have been held not to require notice under Pope to reasonably ascertainable creditors. Therefore, where no personal representative has been appointed within two years of the decedent's death and the claim governed by KRS 396.011 is not filed by that time, the claim will be barred and not subject to a notice attack.

If one has a secured claim or a claim that is covered by insurance and the security or insurance may prove to be insufficient to cover the entire claim, a "protective presentment" of the unsecured or uninsured portion of the claim should be made.

KRS 396.085(1) governs the payment of interest on claims where interest is not provided for by contract or judgment. On a claim not based on contract making provision for interest, interest will be allowed only if it is requested in the presentment of the claim. Even then, interest will only start to accrue at the legal rate beginning sixty days after the end of the six-month period for presenting claims. Id. If interest was not demanded in the

presentment of the claim, the claimant is not entitled to any interest. Accordingly, the claimant should always demand interest in her presentment of the claim.

3.4.2 Presentment of Claim

3.4.2.1 Suit Not Filed Prior to Death

A proper presentation of a claim may be in two forms. The first method is a written notice from the claimant to the personal representative. KRS 396.015(1). This statement must include the basis of the claim, the name and address of the claimant, the amount claimed, the due date of the claim if it is not yet due, the nature of any uncertainty if the claim is contingent or unliquidated, and the nature of the security, if any. Id. Failure to correctly describe the security, the nature of any uncertainty, and the due date of a claim not yet due does not invalidate the presentment. Id. The alternative method of presentment allows the claimant to file a written statement of the claim, in the form prescribed by rule, with the clerk of the court, but the claimant must also certify as provided in the rules of civil procedure that a copy of the written statement was given or mailed to the personal representative and his attorney. Id. The claim is deemed presented when the first of the recipients is in receipt of the claim. Id. The latter option, filing a claim with the clerk and serving a copy on the personal representative and attorney, is advisable, especially if the claim is close to being barred by a statute of limitations.

3.4.2.2 Actions Pending At Death

If litigation was instituted on the claim prior to the decedent's death, KRS 396.011(1) appears to nevertheless require that it be presented within six months of the appointment of the personal representative, assuming the claim survives. Substitution of the personal representative for the decedent, or a motion therefor, constitutes presentment of the claim as of the date of substitution or motion. KRS 396.015(2). This six month requirement is in conflict with KRS 395.278, which requires an application to revive an action within one year of the death of a deceased party. The time limitation of KRS 395.278 was affirmed in Snyder v. Snyder, 769 S.W.2d 70 (Ky. Ct. App. 1989). CR 25.01 provides that if a party dies during the pendency of an action and the claim is not thereby extinguished [it survives at law], the court, within the period allowed by law, may order substitution of the proper parties." Such a substitution may by effectuated by motion by any party.

3.4.2.3 Presentation Where No Personal Representative Appointed

Given the specifications of KRS 396.015 for presentation of a claim (discussed above), how does one present a claim within two years (where no action was pending) or within six months (in a pending action by substitution) of the decedent's death where no personal representative is appointed? KRS 396 does not tell us, but KRS 395.015 permits

a claimant to petition for appointment of a personal representative and commence administration of the estate of the debtor/defendant. After this is accomplished, presentment can be made.

This could become a pressing issue if the regular statute of limitations for a claim expires during the six month period beginning with the decedent's death and there is no estate administration begun during this time. Presenting the claim after the six month period but within two years of the decedent's death (in the event of there being no personal representative) would be of no avail, since the regular statute of limitations would have expired. However, if the claimant whose claim is to expire within the six months after the decedent's death institutes estate administration proceedings on behalf of the decedent and presents his claim during the six month period, his claim would be timely.

3.4.3 Due Process: Actual Notice to Known and Reasonably Ascertainable Creditors

Kentucky requires that creditors be notified by newspaper of the appointment of a personal representative and the time period within which claims must be presented. KRS 424.340. The statute mandates the clerk of the probate court to publish at least monthly, in a newspaper meeting the requirements of KRS 424.120, a notice setting forth all fiduciary appointments made since the last publication. KRS 424.340. The publication must include the following: 1) the decedent's name and address; 2) the fiduciary's name and address; 3) the date of the fiduciary's appointment; 4) the name and address of the fiduciary's attorney, if any; and 5) the date by which creditor's claims must be presented. Id. There is no requirement under Kentucky statutes or case law that the personal representative or the clerk of the court actually notify claimants of the decedent.

Such statutory notice requirements which only mandate publication notice will inevitably result in some potential claimant being precluded from asserting her claim due to a lack of actual knowledge of the decedent's death. However, two fundamental requirements of procedural due process are that the person have notice and an opportunity to be heard before property rights are forfeited. According to the United States Supreme Court, statutory notice requirements such as those in Kentucky may not be sufficient to satisfy the requirements of the Due Process Clause of the Fourteenth Amendment to the United States Constitution. Tulsa Professional Collection Services v. Pope, 485 U.S. 478 (1987). The holding of Pope establishes that notice by publication, which is all that is required in Kentucky, is insufficient to satisfy the due process rights of creditors who are "known or reasonably ascertainable." Id. Therefore, the Constitutional mandate requires the personal representative to actually notify known or reasonably ascertainable claimants before their suits can be barred by an expedited statute of limitations such as the one found in KRS 396.011. For claimants who could not be ascertained through reasonable efforts, it appears that mere publication notice will suffice. Id. The concern of notice is especially true for out of state claimants who presumably have no way of obtaining notice through

publication. In a case prior to Pope, the New Mexico Supreme Court held publication notice is insufficient to satisfy due process requirements with respect to known potential tort claimants who reside out of state and said publication notice was merely in a local newspaper. Re Estate of Engbrock, 565 P.2d. 662 (N.M. 1977).

The Pope decision was based on prior United States Supreme Court precedent outlining the requirements for procedural due process. For instance, Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306 (1950), held that a creditor's claim against an estate is a property interest protected by the Fourteenth Amendment and state action is subject to notice requirements. Also, Mennonite Board of Missions v. Adams, 462 U.S. 791 (1983), held that actual notice is a minimum constitutional requirement in a proceeding that will adversely affect liberty and property interests of a party whose name and address are reasonably ascertainable. The application of these cases resulted in Pope's holding that reasonably ascertainable claimants must be actually notified.

However, the court in Venturi v. Taylor, 41 Cal.Rptr.2d 272, 277 (Cal.App. 1995) ruled that a claimant who had actual knowledge of the estate pendency could not attack the constitutionality of the lack of formal notice given to him. Therefore, the actual knowledge rather than the likelihood of obtaining such knowledge seems to be an important distinction to some courts. However there is not uniformity in these cases. For instance, in Foster v. Cianci, 773 So.2d 1181,1182 (Fl.App. 2000) the Court held that even though the potential claimant was aware that the estate was being probated, the personal representative, who had knowledge of the potential claimant, was not relieved of the responsibility under due process of giving actual notice of the necessity of filing a claim prior to the expiration period.

It is important to note that this notice requirement imposed by Pope does not apply to "self-executing" statutes of limitations. Pope at 486. These are regular statutes of limitations that are not contingent upon an event (such as the appointment of a personal representative). Self-executing statutes of limitations involve no state action beyond legislative enactment of the period. Id. at 487. The aspect on nonclaim statutes that make them not self-executing and subject to due process concerns is that the time bar is never activated without the involvement of the probate court, a state institution. Id. Accordingly, state nonclaim statutes, such as KRS 396.011, that expedite the limitations period upon the occurrence of an event in a probate proceeding (such as the appointment of a personal representative) are not self-executing and are subject to the Pope due process notice requirements.

While it is evident that the six month presentation requirement of KRS 396.011(1) is not self-executing and thus subject to the Pope requirements, there is a question as to whether KRS 396.205 (a limitation for claims filed within two years after the discharge of the personal representative) is self-executing. For instance, many states have limitations statutes barring claims after a certain number of years after the decedents death. Hargrove and Morris. at 12. Courts universally hold these to be self-executing. Id. For instance, in

a recent decision, the Colorado Court of Appeals held that the nonclaim statute requiring publication notice of when claims would be barred was not self executing and the reasonably ascertainable creditor could assert a claim after this publication date but before the termination of a statute requiring claims to be filed within one year of the decedent's death. Estate of Russo v. Sunrise Healthcare Corporation, 994 P.2d 491 (Co.App. 1999). Therefore, the statute requiring claims to be filed within one year of the decedent's death was ruled to be self-executing and not subject to Pope while the statute barring claims from a certain period of time after the appointment of the personal representative was not self-executing. Id. In addition, the court in Burnett v. Villaneuve, 685 N.E.2d 1103 (Ind.App. 1997) ruled that a statute barring claims one year after the death of the decedent was self executing, in that, unlike the statute in Pope, in was not triggered by a probate proceeding. Id. at 1111.

This presents an interesting problem of Kentucky statutory construction. The Kentucky provision only deals with a decision of the Probate Court in its determination of when the personal representative is discharged. Therefore, there is an interpretation issue with regard to whether or not KRS 396.205 is self-executing or also subject to Pope. Since KRS 396.205 more closely resembles statutes that are not self-executing but triggered by a probate proceeding, claims barred by it may be subject to a constitutional attack with respect to notice.

It would appear that the provision of KRS 396.011(1), which bars claims arising prior to the death if not presented within two years of the decedent's death, would be self-executing and not subject to the Pope actual notice requirement. But this provision only applies where no personal representative is appointed.

3.4.4 Verification of Claim

Prior to the 1988 revisions to Chapter 396 there were fairly rigid verification requirements a claimant had to make in order to have properly submitted her claim. Some of these requirements are no longer compulsory but at the option of the personal representative. Now, the personal representative, when presented with a claim, may request by written request mailed to the claimant an affidavit or other satisfactory evidence which establishes that: 1) The claim is justly due; 2) No payments have been made; 3) There are no set offsets; and 4) If there were any payments or offsets, their amount and nature. KRS 396.026.

In presenting an affidavit under current law to the personal representative, cases decided under the old law are instructive. The claimant's affidavit should state the relevant facts and not merely assert legal conclusions. McBride v. McBride, 90 S.W.2d 736 (Ky. 1936). An affidavit merely asserting a conclusion that a claim is due seems to be insufficient absent any factual or evidentiary proof for that assertion. Depositions that fully establish the debt satisfied the requirement of being other satisfactory evidence.

Quinn v. Quinn, 259 S.W.2d 23 (Ky. 1953). It appears that any sworn testimony establishing the debt will suffice as "other satisfactory evidence."

3.4.5 Contingent or Unliquidated Claim

Even contingent or unliquidated claims that arose before the death of the decedent must be presented within six months (assuming they are unsecured and not covered by insurance and not government claims) of the appointment of the personal representative or be forever barred. KRS 396.011(1).

3.4.6 Deduction of Counterclaim

In allowing a claim, the personal representative may deduct any counterclaim the estate has against the claimant. KRS 396.125. The counterclaim, liquidated or unliquidated, may arise out of a transaction other than that on which the claim is based. Id.

3.4.7 Compromise of Claim

The personal representative may compromise any claim, if it appears to be in the best interest of the estate. KRS 396.145. This places broad discretion on the personal representative in her decision as to whether or not to seek a settlement or continue in litigation.

3.4.8 Waiver of Defense of Limitations

If an estate is solvent, the defense of limitations may be waived by the personal representative, and thus allowance or payment made, only if the personal representative obtains the consent of all successors of the decedent whose interests would be affected. KRS 396.065.

3.4.9 Allowance/Disallowance of Claim

The personal representative decides whether or not to allow a properly presented claim. KRS 396.055. This is done by a mailed written notice form the personal representative to the creditor. Id. An allowance means the claim will be paid without litigation. In the event of a notice of disallowance, the claimant will have to resort to filing a complaint with the court and securing a judgment before she will collect.

A personal representative may change his or her decision regarding allowance or disallowance of claims with notice to the claimant. KRS 396.055. However, a disallowance may not be changed after the time to commence an action has run and the claim has been barred. Id.

If the personal representative does not mail notice disallowing a claim within sixty days after the six month period for the initial presentation of the claim has expired, the claim is deemed to be allowed. KRS 396.055(1). However, the personal representative may petition the court with notice to the claimant at any time before payment of the claim, and the court may "for cause shown" permit the personal representative to disallow the claim.

3.4.10 Disallowed Claims - Suit Within Sixty Days

If the claim is disallowed the claimant must commence an action within sixty days after notice of disallowance or else the claim will be barred, provided the personal representative warned the claimant of the impending bar. KRS 396.055(1). A disallowance with warning effectively creates a sixty day statute of limitations on the claim from the date of the mailing of the disallowance. If the disallowance does not warn of this bar, then an action may be brought after this sixty days, but before the first to occur of the expiration of the claim's regular statute of limitations or two years of the discharge of the personal representative (KRS 396.205). Thus the burden with respect to having knowledge of the limitations period and conveying the information to the other party is placed on the personal representative who presumably has greater knowledge of this law than the claimant would.

3.4.10.1 Extension of Sixty Day Period for Filing Suit

Where a claim is disallowed that has not matured or which is contingent or unliquidated, the personal representative may extend the sixty day period for filing suit on the claim, but any such extension may not run beyond the regular statue of limitations for the claim. KRS 396.055(3). The extension is advisable if time is not of the essence in closing the estate and there is a fair degree of uncertainty as to whether the contingent claim will be due and/or its amount. Such an extension allows the parties to wait for the claim to come due, if at all, and therefore not speculate as to its value. Also, upon petition, the court may order an extension of the sixty-day period for filing suit to avoid injustice, but again any such extension may not run beyond the regular statue of limitations. Id.

3.4.10.2 Proper Forum

Chapter 396 does not tell us where suit must be filed within sixty days if the claim is disallowed. KRS 24A.120, however, provides that the district court shall have exclusive jurisdiction in "matters involving probate, except matters contested in an adversary proceeding. Such adversary proceeding shall be filed in circuit court." KRS 24A.120 (1)(b). This statute raises two important interpretation questions. First, what is considered an "adversary proceeding." The second is what is a "matter involving probate". It appears that a contested action regarding the estate's liability on a claim would be an adversary proceeding. But if the action merely involves the decedent's liability on a bank note for $3,500, does the matter "involve probate" within the meaning of the statute. Clearly the

claim arose in the contest of an administration of an estate, but does the statue intend to divest the district court of subject matter jurisdiction over this type of adversary proceeding if the suit is for an amount within its jurisdictional requirements on a type of claim the district court entertains every day.

In Vega v. Kosair Charities Committe, Inc., 832 S.W.2d. 895 (Ky.App 1992) the Court of Appeals held that "the district court lacks jurisdiction to decide a contested matter [in a probate proceeding], or matters provided by statute to be commenced in circuit court. In holding this, the Court of Appeals held that the district court lacked jurisdiction in an action to determine whether or not a person was the beneficiary of the decedent's will. Id. The case and statutory law seem to conclude that if the case is truly adversarial, then a claimant is precluded from bringing any claim, regardless of the amount in controversy, in district court. But in Kosair, the nature of the claim clearly involved probate.

Since most claims against a decedent's estate will be made pursuant to state law, federal question jurisdiction should not normally be an issue. However, suppose the claimant is alleging that the decedent violated the claimant's federal statutory civil rights. Also, suppose a creditor who was barred by the claims statute in bringing his action wants to institute an action in federal court claiming the statute violates his federal constitutional right to due process. Or suppose a claimant demands payment on a note in an amount in excess of the $75,000 jurisdictional requirements of federal court in diversity actions, and there is complete diversity among the parties. Since there are federal statutes granting an unambiguous right to federal diversity jurisdiction in these type of actions, there is a federal statutory right to have such claims heard in Federal District Court.

3.4.10.3 Proving the Claim

A normal obligation, such as a mortgage or written contract, is provable by verification of the instrument. However, suppose that a creditor seeks to testify as to what the decedent said, alleging an oral contract or an oral modification of a written contract. This presents problems as to the admissibility of evidence.

Until 1992, Kentucky had a "Dead Man's Statute" which governed the admissibility of statements of the deceased. KRS 421.210 (Repealed). Therefore, evidence of an oral contract modification was inadmissible under the "Dead Man's Statute" without a disinterested witness. Cox v. Venters, 887 S.W.2d 563 (Ky. 1994). However, this statute was repealed in 1992 with the advent of the Kentucky Rules of Evidence.

KRE 802 renders hearsay inadmissible, subject to the exceptions provided by the rules. KRE 801 defines hearsay as "a statement other than one made by the declarant while testifying at trial or hearing, offered in evidence to prove the truth of the matter

asserted." Therefore, testimony attempting to prove the oral statements made by the decedent falls under the KRE definition of hearsay.

KRE 803 provides twenty-three exceptions to the hearsay rule where the availability of the declarant is immaterial. Some of the more notable are the excited utterance, recorded recollection (where the decedent leaves a memorandum documenting the statement), and numerous exceptions dealing with the declarant's reputation..

In addition to the twenty-three exceptions to the hearsay rule enumerated in KRE 803, KRE 804 provides that death is obviously one of the situations where the declarant is unavailable. This section gives four additional exceptions to the hearsay rule only when the declarant is unavailable, as in the case of death. They are: 1) Former testimony; 2) Statement under belief of impending death; 3) Statement against interest; and 4) Statements of personal or family history. The statement against interest exceptions seems to be the most expansive exception where the declarant is unavailable for testimony. It allows a statement that was "so far contrary to the declarant's pecuniary or proprietary interest, or so far tended to subject the declarant to civil or criminal liability ... that a reasonable person in the declarant's position would not have made the statement unless believing it to be true. These additional exceptions create leeway for a claimant who is attempting to prove the statements of the decedent in a court proceeding.

3.4.10.4 Judgment As Allowance of Claim

A judgment against the personal representative to enforce a claim against the decedent's estate constitutes an allowance of the claim. KRS 396.055(2). In adjudicating a claim against the estate, the court must reduce the amount allowed by any successful counterclaim, and if the amount of the counterclaim exceeds the claim, render a judgment against the claimant. KRS 396.125. The counterclaim, liquidated or unliquidated, may arise from a transaction other than that upon which the claim is based and may give rise to relief different from that sought in the claim. Id.

3.5 Claims That Arose At or After Death, Secured Claims, Claims Covered By Insurance, and Government Claims

3.5.1 Presentment

Even claims that are not subject to the six month presentment rule, still must be presented. KRS 396.035. The six-month presentment requirement of KRS 396.011(1) does not apply to claims that arise at or after the decedent's death or a to claim that is secured by a mortgage or other security instrument to the extent of the security. KRS 396.011(1) & (2). Also to the extent of the amount of the claimant's claim that is protected by liability insurance, the six-month presentment requirement is not applicable. KRS 396.011 (2); Gailor v. Alasabi, 990 S.W.2d. 597 (Ky. 1999). The rationale behind limiting the time and manner claims against the decedent's estate may be filed is to balance

the interest of the claimants with the interest in an efficient and equitable termination of the estate. Therefore, insurance protection does not fall into this concern and creditors are given more protection for claims which are backed by insurance coverage. "The purpose of the statute is to protect the personal estate of the decedent, not his insurance company." Id. However, any portion of the claim amount above the insurance coverage is subject to the six-month presentment rule. KRS 396.011 (2)

In addition, Federal and state governmental claims are not subject to the six month presentment rule under KRS 396.011. A state nonclaim statute cannot prevent the federal government from collecting. Re Estate of McBride, 249 N.E.2d 266 (Ill. App. 1969).

3.5.2 Action Barred Two Years After Discharge of Personal Representative

As discussed earlier, KRS 396.205 bars suits that were not otherwise barred from being brought against the personal representative or her heirs after two years from the date of the discharge of the personal representative. However, there is an exception to this limitations period for actions by claimants against the personal representative or a distributee for fraud. KRS 396.205. It appears claims that arose at or after death, secured claims, claims covered by insurance, and governmental claims, must be instituted before the two year limitations period after the discharge of the personal representative under KRS 396.205, if the decedent's estate is to be charged. This section should not bar a purely in rem action asserting enforcement of a property right in a mortgage or lien.

As discussed above, however, KRS 396.205 does not appear to be a self-executing statute and may be subject to actual notice to the claimant of the impending bar under Pope. If so, a creditor without notice may not be barred until the regular statute of limitations has run on the action or the ten-year statute under KRS 413.160 (discussed above).

3.5.3 Proper Forum, Proving the Claim, and Judgement as Allowance of Claim

See discussion in 3.4.10.2-4

3.6 Priority of Claims/Exemptions/Dower

If the "applicable assets" of the estate are insufficient to pay all claims in full, the claims must be paid in the following order: (1) costs and expenses of administration; (2) funeral expenses; (3) debts and taxes with preference under federal and state law; and (4) all other claims. KRS 396.035(1). "Applicable assets" presumably refers to assets other than those subject to prior security interests. Between claims within the same class, no preferences shall be given, even with respect to unmatured claims. KRS 396. 095(2).

Accordingly, it appears that property of the decedents estate should be set aside, distributed and disbursed in the following order of priority.

3.6.1 Community Property of Surviving Spouse

Since the property earned in a community property state and brought into Kentucky with a change of domicile remains a legally vested one-half interest in both spouses, it is important to determine how this will affect the rights of claimants at the death of a spouse. Kentucky has adopted the Uniform Disposition of Community Property Rights at Death Act. KRS 391.210-391.260. This Act applies to a) personal property acquired in a community property state; b) income from rents, issues, or proceeds from that community property; and c) real property or rents, issues, process, etc. therefrom that came from community property states. This act evidences no intent on the part of the legislature to recharacterize the interest of this community property once the property owner is domiciled in Kentucky. Lay, Norvie. Multi-State Problems in Estate Administration. Kentucky Estate Administration (3rd Ed). 2000. at 29. KRS 391.220 clarifies that when a married person dies with property applicable under this act, one-half of that property is property of the surviving spouse and not subject to testate or intestate distribution. Upon death, the community property interest of the surviving spouse in estate assets may be perfected by an order of the probate court (assuming the spouse did not relinquish or forfeit such interest). KRS 391.225. Likewise, a personal representative, heir, or devisee has the same right to perfect the community property interest of the estate in assets held by the surviving spouse (assuming the decedent did relinquish or forfeit such interest). KRS 391.230. In addition, a creditor of the decedent may make a written demand obligating the personal representative to discover whether any property held by the surviving spouse is property governed by the Act. Id.

The term "claims" does not include disputes regarding title to specific assets alleged to be in the estate. Such a dispute is not subject to the nonclaims statute. Murphy v. Murphy, 596 N.W.2d 571 (N.D. 1999).

3.6.2 Secured Claims

The death of the secured debtor does not result in an extinguishment of the lien. Avey v. Stearman, 140 S.W. 1055 (Ky. App. 1911). A secured claim is superior to the spousal exemption of Chapter 391. Graham v. Graham's Adm'r, 306 S.W.2d 831 (Ky. 1957). They are also superior to the homestead exemption. Meader v. Meader, 10 S.W. 651 (Ky. App. 1889). Secured claims have priority over funeral expenses. Graham. They also are superior to costs of administration. Milward v. Sheilds, 43 S.W. 184 (Ky. App. 1897). It is important to keep in mind that these priorities are only to the extent of the secured interest. After the amount of security, the claim is subject to the requirements for unsecured claims. The secured creditor is not entitled to a preference from the estate's general assets. Miller's Executors v. Miller's Heirs and Creditors, 189 S.W. 417 (Ky. App. 1916).

A lien filed to secure a judgment should be treated as a secured claim giving the creditor priority to the extent of that secured asset. Kentucky law allows a final judgment to act as a lien on realty with certain notice requirements. KRS 426.720. The creditor must file with the clerk a notice of judgment lien as well as send a copy of the notice to the creditor's last known address. In addition, KRS 376.460 authorizes a lien for attorney's fees that are either agreed or reasonable. These tools are incentive to institute a claim prior to death if possible and securing a judgment lien. Therefore, the judgement lienholder should have security and thus payment priority that claimants who present their claims after death do not.

3.6.3 Exemption For Surviving Spouse/Children

Statutorily, the surviving spouse, or children if there is no surviving spouse, is entitled to $7,500 of personal property that is exempt from estate distribution. KRS 391.030. This exemption is absolute regardless of whether or not the spouse dies intestate or whether there is a renunciation of the will. This spousal right is an exemption rather than a claim. It therefore has priority over unsecured claims such as funeral expenses. Blades v. Blades Administrator, 159 S.W.2d 407 (Ky. 1942). However, the exemption is inferior to a secured debt such as a mortgage. Graham v. Graham's Administratrix, 306 S.W.2d 831 (Ky 1957). As long as all secured debts have been paid, the surviving spouse has an absolute right to this $7,500 exemption prior to any unsecured claim, even claims arising from the cost of estate administration from the personal representative.

3.6.4 Costs and Expenses of Administration

Costs and expenses of administration are to be paid prior to other unsecured claims because they are for services that would not be undertaken if the personal representative were placed in competition with other creditors. International Harvestor v. Dyer's Administrator, 178 S.W.2d 966 (Ky. 1944). Costs of Administration are charges that are necessarily incurred by the personal representative in the settlement of the estate. Brown's Executor v. United States, 215 S.W. 815 (Ky. 1919). These include court costs, attorney's fees, the personal representative's compensation, and other expenses relating to the personal representative's fiduciary capacity. Id. Attorney's fees are included as priority debts in this category only as to those fees incurred by the personal representative in the administration of the estate. Other attorney's fees, such as those incurred by an estate beneficiary, are in the final priority of claims. Tillman v. Smith, 533 So.2d 928 (FL. App. 1988).

3.6.5 Funeral Expenses

Chapter 396 gives the reasonable costs of funeral expenses second priority. KRS 396.095. Therefore, a claim against the estate may be filed by the funeral administrator and take precedence over lower unsecured claims and estate administration costs and expenses. Terrill's Administrator v. Davis, 199 S.W.2d 130 (Ky. 1947). It is important to

note that the statute only provides priority for funeral expenses and not those associated with the deceased's last illness of or hospitalization. These are given last priority. The pre-1988 statute did give such services priority but that priority was abolished in 1988 due to the amendments.

3.6.6 Debts and Taxes With Preference Under Federal Law and Laws of Kentucky

31 U.S.C. 3713 gives the statutory authority for claims of the United States to have priority over other unsecured claims. However, they are not given priority over funeral expenses or administration costs. Abrams v. United States, 274 F.2d 8 (8th Cir. 1960). This category only applies where a statute confers priority for unsecured governmental claims to take precedence over other unsecured claims. As between governments, local laws may not be given priority over laws of the United States. Kentucky Department of Revenue ex. rel. Luckett v. United States, 383 F.2d 13 (6th Cir. 1967).

Federally, 26 U.S.C.A. 6321 grants the United States a lien over the property of the decedent for all taxes after demand. The tax lien is entitled to priority over a mortgage or other lien only if the tax lien were filed prior in time to the other lien. International Harvestor v. Dyer's Adm'r, 178 S.W.2d 966 (Ky 1944). The state of Kentucky and local governments have a lien on property assessed for taxes for ten years following the date of delinquency. KRS 134.420. The lien shall not be defeated by alienation except to a bona fide purchaser. Id. Prior recorded tax liens have priority over subsequent mortgages. Liberty National Bank & trust Co. v. Vanderkraats, 899 S.W.2d 511 (Ky.App. 1995).

3.6.6.1 Medicaid Claims

42 U.S.C.A. 1396 imposes a requirement on states that receive federal funds for local Medicaid programs to collect, in certain situations, from the estates of recipients who received certain types of care.

KRS 205.520(4) expresses the state statutory authority to comply with the above federal statute regarding Medicaid claims against the decedent's estate.

The substance of the recovery guidelines is promulgated in 907 KAR 1:585. The legislature gives the Cabinet for Human Resources, Department for Medicaid Services the authority, through administrative regulation, "to comply with any requirement that may be imposed or opportunity presented by Federal law for the provision of Medical Assistance to Kentucky's indigent citizenry."

907 KAR 1:585 provides that recovery applies to "institutionalized individuals" (an individual age fifty-five or older who received Nursing Facility Services, Intermediate Care Facility for the Mentally Retarded and Developmentally Disabled Services, Home

and Community Based Services or Alternative Intermediate Services for the Mentally Retarded with payment for these services made, wholly or in part, by the Medicaid program) or "permanently institutionalized individuals" who have been Medicaid recipients for two or more years and received the above services.. Id. at 1(4) and (6). The recovery received by Medicaid shall not exceed benefits paid during institutionalization. Id. at 2(2).

There are several exemptions to the Medicaid estate recovery guidelines under 907 KAR 1:585. First, recovery will be made only if there is no surviving spouse or child under twenty-one years of age. Id. at 3(1). Second, recovery shall not be made against the portion of a blind or disabled child's inheritance. Id. at 3(2). Third, recovery will be waived upon the occurrence of any of the following five conditions: a) the estate is valued at $5000 or less; 2) the asset is the sole income producer under $50,000 annually for a decedent within the third degree on consanguinity; 3) there is a homestead exemption of $50,500 or less ($50,500 of a homestead is exempt property); 4) the cost of recovery exceeds the estate's value; or 5) the recipient's estate is granted a case by case exemption granted by the Department. Id. at 3. The case by case exemption may be granted "if circumstances exist which shall be directly related to a surviving family member within the third degree of consanguinity for continuing educational needs, health care needs or the needs of a person with a disability. Id. at 3(4).

Medicaid claims against the decedent's estate are not secured claims but rather prioritized unsecured claims. The 907 KAR 1:585 does not authorize a lien on the decedent's property. Therefore, secured claims, the costs of administration, and funeral expenses have a priority over Medicaid claims. However, KRS 205.520(5) establishes that state Medicaid claims "shall be superior to any right of reimbursement, subrogation, or indemnity of any liable third party." Therefore, it appears that Medicaid claims are superior to any other unsecured claims that are not given statutory priority in Kentucky. Accordingly, the personal representative and any claimants should be aware that such Medicaid Estate Recovery claims by the state government, if the above services were rendered and the property is not exempt, will take precedence over the claims of general creditors without a priority.

3.6.7 Other Claims

These are given final priority and are the vast majority of claims. They are composed of all unsecured claims that are not costs of administration, funeral expenses, and claims with governmental statutory priority.

3.6.8 Dower and Curtesy

This right is not generally considered a claim against the decedent's estate but rather a statutory right held by the surviving spouse to "surplus" property. The statute provides that if the spouse dies intestate the surviving spouse is entitled to "an estate in fee

of one-half of any surplus realty or personality." KRS 392.080. However, to obtain the dower interest when the spouse dies testate, the surviving spouse must renounce the decedent's will. Upon such a renunciation, the spouse will be entitled to half of the surplus realty and one third of the surplus personality of the decedent's estate. Id. However, dower and courtesy have little if any effect on claims against the decedent's estate. The Supreme Court of Kentucky has interpreted the dower interest to be surplus property "after the payment of funeral expenses, charges of administration, and debts." Mattingly v. Gentry, 419 S.W.2d 745, 747 (Ky. 1967)(see discussion above). Therefore, this right will occur only after all debts and exemptions are paid, if at all, and do not affect claimant's rights for recovery.

3.7 Payment of Allowed Claims

Even if the personal representative feels that the claim is justly due, for the purposes of considering other claimants, the statute does not permit her to pay those allowed claims immediately. KRS 396.075. The personal representative may commence the payment of claims after six months from the date of her appointment. Id. While proceeding to pay the claims, she must make appropriate provisions for claims that have been timely presented but not allowed, as well as any claims that are not subject to the requirements of Chapter 396. Id. An example of such a claim would be a claim sought by the federal government.

3.7.1 Contingent, Unliquidated or Future Claims

If a claim will mature prior to the distribution of the estate, it is to be paid in the same manner as other matured claims of the same class. KRS 396.115. Where the claim will not mature prior to the distribution of the estate, either the claimant or the personal representative may petition the court to provide for payment. Id. Upon consent of the claimant, the court may award payment of the present or agreed value of the claim. Id. The court may alternatively arrange for future payment on the happening of a contingency through a trust, mortgage, bond, or other form of security. Id.

3.7.2 Interest

KRS 396.085 governs the payment of interest on allowed claims. A claim based on a contract providing for interest shall bear interest from the date of death in accordance with the contract. If interest was provided for in a judgment against the personal representative, it shall be paid according to the judgment. Id. On a claim not based on a contract making provision for interest, interest will be allowed only if it is requested in the presentment of the claim. Id. Even then, interest will only start to accrue at the legal rate beginning sixty days after the end of the six-month period for presenting claims. Id. If interest was not demanded in the presentment of the claim, the claimant is not entitled to any interest.

3.7.3 Secured Claims

If the creditor surrenders his security, the payment is simply on the amount allowed. KRS 396.105. If the creditor does not surrender his security, there are two options. Id. First, if the security is exhausted the personal representative should pay the claim based on its amount less the value of the security. Id. If the security has not been exhausted, payment should be made based on the amount of the claim minus the value of the security. This value may be determined by compromise, judicial decision, arbitration, etc. Id.

These situations arise when assets of the estate are encumbered by a mortgage or other secured interest. In these situations, the personal representative may: 1) Pay all or part of the encumbrance; 2) Renew or extend any obligation secured by the encumbrance; 3) If in the best interest of the estate, in satisfaction of the lien, the personal representative may convey or transfer the assets to the creditor. KRS 396.155.

Payment of an encumbrance on an asset does not increase the share of the distributee entitled to the asset unless the distributee is entitled to exoneration.

3.7.4 Compelling Payment of Allowed Claim

On petition, a claimant with an allowed but unpaid claim may obtain an order directing payment by the court. KRS 396.075. This would occur where a notice of allowance was sent but no payment is given as well as when no response to a properly presented claim is timely given. To be valid, the claimant must receive an order from the court directing the personal representative to pay the claim to the extent that funds of the estate are available for the payment. Id.

Kentucky law gives the creditor a right to bring suit for the settlement of an estate. KRS 395.510 authorizes such a creditor of a deceased person to "bring an action in circuit court for the settlement of his estate provided that no such suit shall be brought ... until the expiration of six months after the qualification of such representative." Id. Therefore, after the six months claims period has elapsed, a creditor has to power to institute an action to settle an estate. This action has been permissibly used by creditors to sue for the estate's settlement and join as defendants other creditors who had allegedly been wrongfully paid. Peoples National Bank v. Guier, 145 S.W.2d. 1042 (Ky.App. 1940). In addition to creditors, the personal representative and distributees may sue to settle the estate. KRS 395.510.

3.7.5 Liability of Personal Representative

The personal representative will be individually liable to claimants who are injured by payment of claims in two instances. KRS 396.075(2). The first situation is where the personal representative paid a claim prior to the date of six months after the date of his

appointment and did not obtain adequate security from that claimant. KRS 396.075(2)(a). In this situation the personal representative may be sued to collect the balance of any money owed by a valid claimant who was injured. The second situation where the personal representative is liable for payed claims is when a payment is made, either negligently or willfully, to deprive the injured claimant of his priority. KRS 396.075(2)(b). For instance, this would occur if the personal representative paid a normal unsecured claim, which is given final priority, ahead of funeral expenses.

3.7.6 Recovery of Overpayment

If, under a mistake as to the estate's solvency, the personal representative pays an undue share to a particular claimant, he may recover the amount in excess with interest. KRS 396.165. This is generally done by the personal representative instituting an action against the claimant who received the undue benefit. If the personal representative fails to sue to recover an overpayment, creditors who were underpaid or unpaid may bring an action for recovery. Johnson v. Dodd's Admx, 37 S.W.2d 26 (Ky. 1931).

3.7.7 Payment When Multi-State Administration

Payment issues arise when a decedent has assets and/or liabilities in multiple states. This may allow one state to tailor its laws in order to prefer its citizens over the other state's citizens.

All assets located in Kentucky are "subject to all claims, allowances and charges existing or established against the personal representative wherever appointed" regardless of which state the personal representative is appointed. KRS 396.175(1). When the domiciliary and ancillary estate is insufficient to pay all claims, charges, and exemptions under the law of the decedent's domicile, Chapter 396 provides that each claimant is entitled to an equal proportion of his claim. KRS 396.175(2). If there is a preference or security that is not allowed in Kentucky but lawful in another state, nonresident creditors that are benefitted by this preference shall receive payment out of Kentucky assets only after the deduction of said preference. Id.

When Kentucky is not the state of the decedent's domicile and the decedent's's domiciliary estate assets are insufficient to meet all claims, exemptions, allowances, and prior charges, local assets, if adequate, will be paid proportionately to all in-state allowed claims first, with the remainder being transferred to the domiciliary estate. KRS 396.175(3). The statute provides that claims allowed in this state shall be paid their proportion if local assets are adequate for the purpose and the remainder will be transferred to the domiciliary personal representative. Id. If local assets are insufficient to pay all allowed claims in this state, after taking into account payments made on claims from Kentucky by assets from other jurisdictions, the local assets shall be marshalled so that each claim in Kentucky will be paid in its proportion, sop far as possible. Id.

3.7.7.1 Creditor Instituting Ancillary Administration

In an increasingly mobile society, it is often the case that a decedent who is domiciled in another state will have assets within Kentucky that are subject to probate. May a Kentucky claimant institute ancillary administration in Kentucky in order to present his claim in Kentucky instead of proceeding in the foreign jurisdiction under the domiciliary administration of the non-resident decedent? KRS 394.140 allows the district court venue to probate a will 1) where the testator resides; 2) where land lies; 3) where he died: 4) where his estate is located; or 5) where there is a debt or demand owing him. KRS 395.030 provides that when a person dies intestate, the district court which would have had jurisdiction to probate his will, had he made a will, shall have jurisdiction to grant administration on his estate. Kentucky has anciently settled authority "that jurisdiction to appoint an ancillary representative in Kentucky is dependant upon two factors (1) the existence of assets and (2) the location of these assets within the state. Merritt. Kentucky Practice: Probate Practice and Procedure, sect. 874 (1984). Kentucky case law is clear that to have ancillary administration, the decedent need not have left real property assets. For instance, debts due to the decedent are assets located in Kentucky if owned by Kentucky residents. Hyatt v. James' Administrator, 71 Ky. 9 (1871). Also, a wrongful death claim of the decedent killed in Kentucky has been held a local asset giving rise to ancillary administration. Whisler v. Allen, 380 S.W.2d 70 (Ky. 1964). This "ancillary administration" may be undertaken even if no domiciliary administration has been embarked upon. Payne v. Payne, 39 S.W.2d. 205 (Ky.App. 1931).

3.8 Enforcement of Claims Against Other Parties

3.8.1 Individual Liability of Personal Representative

Unless otherwise provided in the contract, the personal representative is not personally liable with respect to contracts entered into under his fiduciary capacity, unless he fails to reveal that capacity. KRS 396.185(1). The personal representative is personally liable for "obligations arising from ownership or control of the estate" or tort associated with the estate for which he is at fault. KRS 396.185(2). The above claims may be proceeded against the estate by a "proceeding against the personal representative in his fiduciary capacity." This is regardless of the personal representative's individual liability. KRS 396.185(3). The liability disputes between the personal representative and the estate may be determined by appropriate judicial proceedings. KRS 396.185(4).

3.8.2 Liability of Distributees

Claims which the statute of limitations does not bar may be brought against distributees. KRS 396.195. This liability only extends to the amount of the distributee's's distribution minus any statutory exemptions he may have. Furthermore, each distributee against whom a judgment has been procured has the right to contribution if they give other distributees timely notice. Id. This applies to land inheritances of the beneficiary of a will

when a creditor sues asserting a non-barred claim. Griffith's Administratrix v. Miller, 149 S.W.2d 11 (Ky. 1941).

3.8.3 Liability of Decedent's Revocable Trust

An estate planning method that is utilized often is the revocable trust. These allow the grantor to transfer all or a substantial portion of his assets into a trust and retain benefits from it. The Restatement (Second) of Trusts 156 (1959) states "where a person creates for his own benefit a trust with a provision restraining the voluntary or involuntary transfer of his interest, ... creditors can reach [the trust estate]."

The law is much less clear however when it comes to the question of may creditors reach the assets of the revocable trust after the settlor has died. The Ohio Supreme Court answered this question in the negative in Schofield v. Cleveland Trust Co., 21 N.E.2d 119 (Ohio 1939). Kentucky law does not appear to have broached this subject. However, recent cases in other jurisdictions have declined to follow the Schofield holding and reflect a view that public policy is shifting on this point. Kruse, Clifton. Revocable Trusts: Creditors' Rights After Settlor-Debtor's Death. Probate and Property. Nov.-Dec. 1993.

Courts have declared revocable trusts with benefits retained in the settlor to be reachable by the decedent's creditors in two ways. One popular method is to attack the trust under the state fraudulent conveyance or transfer statute. In Johnson v. Commercial Bank, 588 P.2d 1096 (Or. 1978) the Oregon Supreme Court held that, under the fraudulent conveyance statute, the transfer into the revocable trust was void as to creditors of the decedent where the decedent retained an interest. It is important to note that the Kentucky Fraudulent Conveyance statute, KRS Chapter 378, which uses broad language subjecting to the statute "every gift, conveyance, assignment, transfer or charge made by a debtor," may be an effective tool for a creditor to make an argument attacking a decedent debtor's revocable trust. KRS 378.020.

The second method of attack on the assets of a revocable trust after the death of a settlor is a public policy argument. In United States v. Ritter, 558 F.2d 1165 (4th.Cir. 1977). Declared that where the settlor reserved to himself income for life and general power of appointment over remainder, it was contrary to public policy to allow him by such formal change to prevent creditors from reaching the property. Id. at 1168. In Ritter, a the conveyance was equitably disallowed as constructive fraud to the extent that the grantor has unsatisfied creditors. Whether the attack on the revocable trust is by public policy, fraudulent conveyance, or both, it is an important possibility for estate planners, potential settlors, potential beneficiaries, and creditors to consider.

3.9 The Relationship Between Bankruptcy Proceedings and Probate

Suppose that a debtor dies while in the process of taking bankruptcy. In this situation, are the assets of the estate administered through state probate proceedings or do

they remain within the jurisdiction and control of the Bankruptcy Court? This question will have a large impact on the claims of the creditors of the deceased because if the Bankruptcy Court retains jurisdiction over the deceased person's assets, there is an entirely different system to follow for the purposes of presenting claims as well as how much, if any, of that claim will be paid. Bankruptcy cases and rules demonstrate that there are no set answers to this question.

Where the decedent filed Chapter 7 Bankruptcy and then died prior to liquidation, the Court in In Re Gridley, 131 B.R. 447 (So.Div.S.D. 1991) held that the debtors estate could continue in the bankruptcy proceeding and the only assets subject to probate were those gained after Chapter 7 petition was filed. In holding this, the Court relied upon Rule 1016 of the Bankruptcy Rules of Procedure that allowed the "estate to be administered and the case concluded in the same manner, so far as possible, as though the death ... had not occurred." The Gridley court came to a conclusion that, under Rule 1016, it was required to continue the administration in a Chapter 7 proceeding, but not under Chapters 11 or 13.

In a 2000 case, In Re Lucio, 251 B.R. 705 (W.D.Tex. 2000) the Court had a slightly different interpretation. It read Rule 1016 to mean that a Chapter 7 case can continue notwithstanding the death of the debtor, however, there is no requirement that the case must proceed, and a deceased debtor's Chapter 7 case is still subject to dismissal. Id. at 708. If dismissed, presumably the debtors assets would be turned over to the probate court and administered under state probate laws.

A Texas bankruptcy Court dismissed a Chapter 13 petition once the debtor had passed away despite a request of the personal representative to convert debtor's case to Chapter 7. In Re Spiser, 232 B.R. 669 (N.D.Tex. 1999). It held that since the decedent had passed away, it would obviously have no future earnings or income needed to fund the plan. Id. 673. It relied upon language of Rule 1016 declaring that administration may proceed after death if possible and "in the best interest of the parties." Thus, the Court held that dismissing the bankruptcy proceedings due to the death of the decedent was in the best interest of the parties. Id. at 674.

Therefore, it is apparent that Bankruptcy courts retain some discretionary power in determining whether to hold the estate of a decedent who recently filed proceedings in Bankruptcy court or to dismiss and defer to state probate courts. It appears that there is a greater propensity for the Bankruptcy Court to retain control over Chapter 7 proceedings than Chapter 13 proceedings. This process is important to all parties who are affected by the death of the decedent in the determination of the proceeds, if any, of his estate.

EFFECTIVE HANDLING OF A WILL CONTEST IN KENTUCKY

Homer J. Parrent III
Parrent & Vish
Louisville, Kentucky

Copyright 2001, Homer J. Parrent III

SECTION B

EFFECTIVE HANDLING OF A WILL CONTEST IN KENTUCKY

INTRODUCTION **B-1**

I. ASSESSING THE CASE **B-1**

II. GROUNDS **B-3**

III. PARTIES **B-4**

A. Which Defendants To Sue B-4

B. Which Plaintiffs Should Be Named B-6

IV. PLEADING STRATEGY **B-6**

A. Grounds To Set Aside The Will B-6

B. Joinder Of Inter Vivos Claims B-7

V. DISCOVERY **B-8**

A. Timing And Method Of Discovery B-8

B. Production Of Financial Records B-8

C. Production Of Medical Records B-9

VI. SUBSTANTIVE LAW **B-9**

VII. EVALUATION OF THE CASE FOR SETTLEMENT PURPOSES **B-9**

VIII. EVIDENCE ISSUES **B-11**

A. Use Of Experts B-11
1. Medical Experts B-13
2. Disputed Document Experts B-14
3. Accounting Experts B-14
4. Legal Experts B-14

B. Proving Lack Of Testamentary Capacity B-14

C. Proof Of Undue Influence B-16

SECTION B

D. Declarations Of The Deceased B-16

E. Testimony By Counsel For Defendants B-17

F. Evidence Post-Dating The Contested Will B-18

CONCLUSION B-19

EXHIBIT: Bye v. Mattingly, 975 S.W.2d 451 (Ky. 1998) B-21

SECTION B

INTRODUCTION

Will contest litigation is significantly different than most other forms of civil litigation. It frequently involves disputes that are as heated and emotionally charged as domestic relations or custody cases, yet present the trial advocate with the additional difficulty of trying such a case to a jury. The issues involved frequently relate to state of mind, intent, purpose, motive, and capacity. These are often difficult concepts to convey to a jury unlike, for example, more concrete situations such as are predominant in automobile accident cases or other personal injury or property damage litigation.

The measure of counsel's effectiveness in will contest litigation in the simplest terms, of course, means successfully obtaining a verdict overturning a will, in the case of a Plaintiff, or obtaining a verdict sustaining the will, in the case of a Defendant. However, it does not always follow that the losing side has not presented an effective case. As will be discussed below, will contest cases tend to be unpredictable, volatile, and frequently surprising, if not on occasion shocking in terms of the result.

For purposes of this paper, effectiveness as an advocate in a will contest case will be defined as proper preparation of the facts, evidence, and documents, and sufficient knowledge of the applicable law to permit those facts to be presented to the jury in the most favorable way possible. In order to do this, an attorney handling will contest litigation must be familiar with a whole series of relatively unique substantive and procedural rules, as well as possess a good litigator's instinct for what works. This paper will attempt to address some of these issues.

I. Assessing the Case

As with any form of litigation, a seasoned litigator knows that one does not accept every case which is offered. This is a lesson which all of us, usually as a young lawyer, have learned

the hard way. However, assessing the validity and strength of will contest litigation is particularly difficult, especially for a Plaintiff's case.

The client who is consulting the attorney about prosecuting a will contest case usually has a tenacious belief, held to a moral certainty, that the testator was incapacitated mentally and was completely over-reached in the preparation and execution of the complained of will. Of course, CR 11 does not permit an attorney to simply accept those assertions at face value without some investigation. However, as a practical matter, that investigation may be difficult if not impossible to conduct thoroughly. For example, it is likely impossible to have the decedent's physicians discuss the testator's mental status in the absence of an authorization from the Executor, or for the same reason, to have access to medical records. Frequently, the executor is alleged to be one of the primary wrongdoers, or, regardless may have no incentive to cooperate. Therefore, one may be left to interviewing lay witnesses to ascertain the extent of testamentary incapacity. With respect to undue influence, a number of the badges of undue influence (discussed below) may be inherent in the fact pattern, e.g., an unnatural disposition, an aged, or weak testator. However, information about a number of the other badges, e.g., who possessed the will, the degree of control of testator's business affairs, and participation by the beneficiary in the preparation of the will, may not be obvious or easily obtainable.

On the other hand, counsel consulted about possible defense of a will has few of those hurdles to overcome. Normally the Executor (if not the party actually seeking representation) is friendly to the client's interests, and hence, defense counsel will have full access to medical opinions and records as well as to financial and other data relating to financial affairs. Defense counsel will also have the ability, probably more freely than Plaintiff's counsel, to discuss the circumstances of the will's execution and preparation with the scrivener thereof.

Hence, while it is impossible to state a universal rule, the conclusion suggested is that evaluation and assessment of a potential Plaintiff's case probably requires a higher threshold and more initial investigative sleuthing, than is required in most cases for the defense.

II. Grounds

As noted above, the usual grounds for setting aside a testamentary instrument are lack of testamentary capacity, undue influence, and fraud.

The elements of testamentary capacity are often stated to be:

A. The ability to know the nature and extent of one's bounty;
B. The ability to know the nature objects of one's bounty and the obligations to them;
C. The ability to appreciate the nature of the testamentary act; and
D. The ability to formulate a fixed plan of one's own for disposition of one's estate. [1]

The level of capacity sufficient to execute a will is far less than the level of capacity necessary to enter into inter vivos transactions such as contracts (Bye v. Mattingly, Ky., 975 S.W.2d 451 (1998)).

Undue influence is defined as that influence obtained over the mind of the testator to such a degree as to compel the testator to do that which he/she would otherwise not do, and is sometimes described as depriving the testator of free agency. Fischer v. Heckerman, Ky. App., 772 S.W.2d 642 (1989). Undue influence is a nebulous and indefinite thing, highly dependent on the individual facts, and frequently proven by resort to badges of undue influence which are discussed below.

Fraud, like in other civil matters, is a misrepresentation of a material fact upon which the testator relies in such a fashion as to alter the testamentary plan from what it otherwise would

[1] These elements are occasionally expressed in a some what different manner, and are sometimes referred to as three in number rather than four. For example, compare the three elements discussed in Fischer v. Heckerman, Ky. App., 772 S.W.2d 642 (1989) with the four elements expressed in Bye v. Mattingly, Ky., 975 S.W.2d 451 (1998).

have been. The fraud can be in the factum, i.e., going to the actual testamentary intent or in the inducement, i.e., going to an intention which is thwarted or perverted by the wrongdoer's deceit.

Other grounds of undue influence also exist, these however are more rare. These include mistake, forgery, lack of proper execution of the testamentary execution, or an assertion that the testamentary instrument was revoked by some event, circumstance or transaction.

In order for counsel to effectively advise a client, it is essential that the client be aware that mere dissatisfaction with the will, assertions that it is "unfair", or that it does not represent the testator's true wishes do not have any weight unless supported by further facts tending to establish cognizable grounds. A frequent complaint is that the potential Plaintiff "deserved" better treatment than the will provided. However, the mere circumstance that one individual was disproportionately benefited or disadvantaged, as the case may be, does not, of itself, state grounds for a will contest.

III. Parties

A. Which Defendants to Sue. Until 1992, the Plaintiff had little choice in who should be named as a party defendant in a will contest case. KRS 394.260 required that "...all necessary parties should be brought before the court by the Plaintiff". That phrase had been uniformly determined by the courts of Kentucky to refer to all beneficiaries, e.g., Security Trust Company vs. Swope, Ky., 118 S.W.2d 200 (1938); McComas v. Hull, Ky., 118 S.W.2d 540 (1938); Russell vs. Grumbley's Executor, 160 S.W.2d 321 (1942). However, in West vs. Goldstein, Ky., 830 S.W.2d 379 (1992), the Supreme Court in a 4-3 decision by Justice Leibson, departed from the previous rule. In Goldstein, Plaintiffs had elected, presumably for strategic reasons, not to join as parties defendant to the action, two elderly ladies who were the recipients of relatively small specific bequests under the will which Plaintiffs contested. The Plaintiffs'

main strategy was to make out the Defendant as a greedy and controlling presence in the testatrix life. Apparently they felt that joining the two elderly specific legatees would tend to dilute that strategy. Defendant made a motion to dismiss based on the absence of necessary parties; the trial court overruled the motion. A jury trial resulted in a verdict against the will. On appeal, the Court of Appeals reversed and held, pursuant to the then existing precedent, that the omission of the specific legatees as defendants was fatally defective. On discretionary review, the Supreme Court reversed the Court of Appeals and reinstated the Circuit Court judgment, holding that, at least in the circumstances presented, the specific legatees were not necessary parties. In dissent, Justice Lambert commented:

> "By omitting certain parties, the contestant can, in effect, permit the jury to rewrite the will invalidating those bequests which it deems inappropriate, safe in the knowledge that proper bequests have been or will be satisfied."

Following Goldstein, it was unclear exactly how far this logic would be extended. However, in Kesler vs. Shehan, Ky., 934 S.W.2d 254 (1996), the Supreme Court seemed to offer some clarification. One of the issues in Kesler was whether an appeal was defective when some of the parties adversely affected by a judgment against the will were not named as parties to the appeal. In holding the appeal defective, the Court noted the rule in Goldstein did not apply because the omitted parties were residuary beneficiaries rather than specific legatees and because there was no waiver of rights as against the omitted legatees. It would therefore appear that the rule in Goldstein will likely only apply where the omitted beneficiaries are recipients of specific bequests and where the Plaintiff affirmatively waives all claims against those beneficiaries. Nevertheless, the rule does clearly give a Plaintiff a leg up, in that as favorable parties such as charities, elderly people, small children, grandchildren or close friends who receive only specific bequests under a challenged document will not have to be sued. This clearly enables the Plaintiff

to focus the case (and the subject of the jury's inquiry) solely on the party or parties that the Plaintiff feels are the most attractive targets.

B. Which Plaintiffs Should Be Named. Unlike the parties named as beneficiaries in a challenged will, the parties who elect to file suit are not required to be an all inclusive class. That is, any one or more of the persons aggrieved by the action of a District Court in admitting to probate an allegedly defective will has the right to sue individually. See Security Trust Company, supra (holding that the trial court committed no error in failing to require the contestants to join all other heirs of the testator as parties). However, as a practical matter, it is seldom advantageous for a family unit not to speak as one mind on the issue of contesting the will. That is, it is hard to think of circumstances in which it is more advantageous for fewer than all of the aggrieved parties to participate in the litigation. Indeed where fewer than all of the potential will contestants are parties, some interesting questions arise in the context of potential settlement of the case. Will a Defendant be willing to settle with some of the heirs while other potential contestants remain in the wings? If a Defendant insists upon a release from persons who are not parties to the suit, can the Plaintiffs obtain such releases, or will they necessarily dilute the available pool of settlement money if they do so? If that problem can be overcome, what happens if, in fact, other contestants do bring another suit?

IV. Pleading Strategy

A. Grounds to Set Aside the Will. Obviously, the pleader will ordinarily set forth as many grounds to challenge the will as the limits of Rule 11 will permit. There is seldom any advantage in failing to include any potential ground if there is reasonable basis for it to be pleaded. In this regard two matters deserve note. The great bulk of will contest cases are pleaded on the basis of both lack of testamentary capacity and undue influence. Even when one

or the other of those grounds appears somewhat weak, it is usually advantageous to assert both grounds, as a relatively small amount of evidence is then required to submit both grounds to the jury. The rule, as frequently noted, is that where there is some evidence of undue influence and some evidence of lack of capacity, the quantum of proof sufficient to take the case to the jury is less than would be the case for either grounds standing alone. See Burke vs. Burke, Ky. App., 801 S.W.2d 691 (1990). The second matter is the provision of Civil Rule 9.02 which requires averments of fraud or mistake to be pleased with particularity as to the circumstances constituting same. It is a frequent defense strategy to attempt to compel the Plaintiff to specifically aver the acts of undue influence. Since undue influence, as the cases noted below reflect, is seldom practiced in the open, to require the Plaintiff to plead it with particularity can be burdensome if not impossible. A recitation of the colorable badges of undue influence which the pleader reasonably believes to exist should suffice.

B. Joinder of Inter Vivos Claims. Frequently the party benefited by a challenged will has also benefited from inter vivos transactions with the decedent. These may include outright gifts during the testator's lifetime, the creation of joint survivorship interests, or questionable transactions made by the wrongdoer while holding a power of attorney for the deceased. The issue frequently raised is whether causes of action challenging these transactions may be joined with the will contest case, and perhaps more significantly, if they can be simultaneously tried with the issues of the will contest. Again, until the Goldstein case it was not at all clear that the Plaintiff could join the inter vivos claims or try them simultaneously with will contest claims. However, Goldstein, supra, relying on KRS 24A.120 and CR 18.02, dealing with dependent claims, held that the trial court properly conducted a combined trial covering all of such issues between the parties. And from a strategic point of view, it is almost always to the

Plaintiff's benefit to include all of the claims against the Defendant that one might have. In the normal undue influence case, Plaintiff desires to paint a picture of the wrongdoer which portrays him/her as a pervasively self-aggrandizing person. The more the questionable or suspicious transactions that one can point to, the greater the odds of prevailing on the entire case. Another aspect of the Goldstein decision which is significant is its approval of submitting for decision in the Circuit Court action, the validity or invalidity of other wills which were not presented to the District Court. A defensive strategy where numerous testamentary documents have been executed is to simply fall back to each earlier document in time in which the Defendant still may participate as a beneficiary. If it is desired to attack all of those documents, it is much easier to do so in one trial than to have a series of trials over each respective prior document. Under Goldstein, Circuit Courts now clearly have jurisdiction to entertain a contest of prior wills which were not acted on by the District Court.

V. Discovery

A. Timing and Method of Discovery. There is no one set formula for the timing, nature and sequence of discovery. That is a matter which depends on the individual case and upon the individual preference of counsel. It is believed, however, that in most cases it makes more sense to obtain financial and medical records in advance of depositions as those materials may furnish the grounds for important lines of inquiry. However, there are certainly circumstances under which a quick deposition of the adverse party may be desirable to lock in certain testimony before Defendant's counsel has full knowledge of the circumstances.

B. Production of Financial Records. In undue influence cases, the Defendant is almost always involved to some degree in handling money before the testator's death. To the extent that one can demonstrate inappropriate, inadequately documented, unauthorized or

otherwise suspicious transactions, the Plaintiff's case is enhanced. However, it is not unusual for the Defendant to have discarded those records as he/she is usually in possession of them at the time of testator's death. Thus, relatively expensive and slow recovery of microfilm records from banks may be necessary.

C. Production of Medical Records. If the testator had been hospitalized or regularly saw a physician, it is essential to obtain those records in advance of any medical depositions. It may also be necessary to obtain such records if one seeks to utilizes the services of an expert witness on the subject of the testator's mental state at the time of the will. These records would include not only hospital but private physician records, and a review of such documents is essential in any case in which the testator's mental state is at issue.

VI. Substantive law

At least insofar as cases involving testamentary capacity and undue influence are concerned, the Supreme Court decision in Bye v. Mattingly, supra, summarizes and expounds the applicable law and discusses most of the significant precedents as well or better as any secondary source. Because of the breadth of the Bye case, a copy is appended hereto. It is the most recent Kentucky Supreme Court case on will contests, and is, therefore, required reading for any attorney handling a will contest case.

VII. Evaluation of the Case for Settlement Purposes

With today's emphasis on mediation and alternate dispute resolution mechanisms, it is appropriate for counsel to consider settlement in virtually every case. Obviously, as a general rule, only cases where the parties are significantly at odds should be taken to trial. However, the reasons underlying the desirability of settlement in will cases is even stronger than in other types of legal actions, e.g. damage suits. In an action for money damages, the jury is entitled to fix the

elements of damages, and frequently compromises between the Plaintiff's demand and the Defendant's plea for exoneration. That is not generally possible in a will contest case. The instructions submitted to the jury by the court allow only for the jury to find for or against the challenged will. The Plaintiff will win everything or will take nothing. Settlement thus holds benefits for everyone. However, before entering into mediation or other efforts to settle the case it is obviously important for counsel to evaluate the case as accurately as possible. Attorneys not familiar with this type of litigation frequently undervalue will cases. Defense counsel may believe that there is no solid evidence in support of the claims made, that juries are fundamentally conservative, that the Plaintiff – usually family members – were insufficiently attentive to the deceased or that they may be easily portrayed as undeserving or greedy. Obviously it is the job of Plaintiff's counsel to dispel those notions if possible and if not, then to point out the extent of the Defendant's exposure. Plaintiff's counsel and defense counsel may somewhat more frequently be able to agree in an evaluation of a case of testamentary incapacity but may have great difficulty in evaluating claims of undue influence. Defendants will simply assert that there is no proof of undue influence, that the attorney who wrote the will and witnesses to the instrument adequately sustain that it was the voluntary act of the testator and generally that the Plaintiff's case is all smoke and mirrors. On the other hand, Plaintiffs have an exceedingly powerful weapon in their arsenal – the concept of "badges of undue influence". The concept has been around for a long time. The case most frequently cited is Belcher vs. Somerville, Ky. 413 S.W.2d 620 (1967). However, the principal has been restated and reaffirmed as lately as the 1990 case of Burke vs. Burke, supra. In general, the badges of undue influence are said to be:

1. A physically weak, mentally impaired testator;

2. An unnatural will;

3. A lately developed close relationship between the testator and the principal beneficiary

4. Participation by the beneficiary in the preparation of the will;

5. Possession of the will by the beneficiary after it is written;

6. Efforts by the beneficiary to restrict contacts between the testator and the natural objects of his/her bounty; and

7. Absolute control of testator's business affairs.[2]

These factors – each of which is merely a circumstance – essentially enables Plaintiff's counsel to make out a case of undue influence based purely upon circumstantial evidence. In fact, it is frequently stated in the law that merely the circumstance of an unnatural disposition when coupled with slight evidence of the exercise of undue influence is sufficient to take the case to the jury. See Williams vs. Vollman, Ky. App. 738 S.W.2d 849 (1987) and cases cited therein. Logically, one can conclude that a Defendant may be objectively innocent of overreaching and yet found culpable given the right set of circumstances. While that may be true, it does not lessen the legal exposure of the Defendant and for purposes of settlement, exposure is the crucial point which Plaintiff's counsel will want to hammer on. Again, exposure can mean the Defendant loses everything, unlike other civil cases where the issue of the degree of exposure may be the heart of the dispute.

VIII. Evidence Issues

A. Use of Experts. The use of expert witnesses in will contests is subject to the identical rules and other forms of civil action. Under Kentucky Rules of Evidence, Section 702,

[2] The "badges" were formulated in nearly identical terms in Bye.

an expert witness's testimony is admissible if the expert's "specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue..." and if the witness is "...qualified as an expert by knowledge, skill, experience, training or education..." Expert testimony in will contest cases usually involves medical experts, disputed document experts, accountants or attorney experts. Occasionally in will contest cases, a question has arisen as to whether the testimony of a proposed expert is objectionable because it goes to the "ultimate issue". For example, an expert, most likely a physician, could be asked if the testator was of sound mind at the time of the execution of the will. Similarly, a psychologist or other expert might be asked if, in the expert's opinion, the testator was unduly influenced in executing the will. Traditionally, questions of this nature, framed in that fashion might elicit an objection from opposing counsel that the question went to the ultimate issue and usurped the province of the jury. Two recent criminal cases decided in the Kentucky Supreme Court have substantially eroded the viability of such an objection although, arguably, it might be going too far to say that an expert can offer an opinion on the ultimate issue in all circumstances.

In Stringer v. Commonwealth, Ky., 956 S.W.2d 883 (1997), the Supreme Court held that a physician could testify that observed trauma was consistent with the history of sexual abuse and that it was not an inappropriate opinion to the ultimate issue to proffer such testimony. Later, in Commonwealth v. Alexander, 5 S.W3d 104 (1999), the Supreme Court held admissible an accident reconstructionist's opinion that the cause of a collision was excessive speed. Although both opinions indicated that the Court was in essence abandoning the ultimate fact rule, the criminal context of both cases cannot be overlooked, and the Court took pains to point out that an opinion as to the ultimate question of guilt or innocence would probably still be held inadmissible in Kentucky. How this translates into will contest litigation, is, of course,

problematic. Perhaps analogizing to the residual inadmissibility of "guilt vs. innocence" opinions, one could assume that an expert can opine in will contest case upon any issue short of one tantamount to the issues framed in the jury instructions, i.e., is the will the product of undue influence; did the testator lack testamentary capacity?. Accordingly, the exact parameters and application of the rule in any civil litigation is probably yet to be fleshed out in subsequent opinions; however, one can safely conclude that most opinions of qualified experts will be received except where framed in the terms which are virtually synonymous with the issues as submitted to the jury for decision.

1. Medical Experts. Use of medical testimony in will contest cases is common. However, most medical experts are treating physicians who have actual knowledge of the testator's condition. Unless the issue of incapacity is clear-cut, most treating physicians are reluctant to opine as to testator's testamentary capacity on a given date unless they actually saw the testator on that date. Therefore, medical experts, generally psychiatrists or neurologists, are frequently utilized to offer an opinion based upon the other medical evidence admissible in the case as to whether testator possessed testamentary capacity on the date of the will. Even though the "ultimate fact" rule may not be a substantive problem any longer, it generally is more effective to elicit from the physician sub-elements of testamentary capacity, i.e., whether the testator in the opinion of the expert possessed sufficient mind to know the natural objects of his/her bounty, the nature and extent of his/her bounty, and was able to formulate a fixed plan to dispose of the estate. Obviously, the strength of a medical expert's testimony is no greater than the medical records and other facts upon which the opinion is based. However, in most cases a medical expert's opinion is well received by a jury.

2. Disputed Document Experts. If forgery or the substitution of pages in a will is at issue, a disputed document examiner may be not merely desirable but necessary for both Plaintiff and Defendant.

3. Accounting Experts. In cases in which undue influence is demonstrated among other ways, by evidence of the amount of control of the testator's business affairs, or if there are a large number of apparently unauthorized or inappropriate transactions, it is not uncommon to utilize the services of a CPA to schedule all of the transactions and testify regarding his/her findings. Such an expert can also be helpful if tracing of funds is necessary as is sometimes required if the wrongdoer has attempted, consciously or subconsciously, to launder the funds removed from the decedent's estate prior to death.

4. Legal Experts. A legal expert may be called to clarify for the jury the process of executing the will and the scrivener's duties with respect thereto. This evidence is sometimes objected to as irrelevant and most trial courts will not permit Plaintiff's counsel to get into the area of whether the scrivener met the standard of practice in connection with the preparation of the contested will. However, under the authority of Kesler vs. Shehan, supra, it is clearly appropriate for such evidence to be used to rebut testimony offered by the scrivener of the will that he/she was careful about ascertaining whether the will was the product of undue influence.

B. Proving Lack of Testamentary Capacity. In order to prove testamentary capacity it is not necessary to adduce evidence from either the testator's treating physician or physicians or from an expert medical witness. Rather, lay persons who have had an opportunity to observe the testator's conduct may give opinions as to testator's mental capacity. This has been the rule in Kentucky since at least the case of Murphy's Executor vs. Murphy, 142 S.W. 1018 (1912). The view is also consistent with the Kentucky Rules of Evidence, Section 701,

which permits opinion testimony by lay witnesses which are rationally based on the witness' perceptions and are helpful for a clear understanding of the matter in controversy. Therefore, counsel will need to investigate, locate and discover individuals who have some foundation or background of knowledge about the testator and who are willing to express their opinion that based on their perceptions that the testator did or did not have the requisite elements of testamentary capacity. On the other hand, expert opinion alone unsupported by either medical records or supporting testimony of factual witnesses is insufficient to sustain the Plaintiff's burden of proof. Fischer vs. Heckerman supra. A further difficulty for the Plaintiff in making out a case of testamentary incapacity is the so-called "lucid interval" rule. Restated in the recent Bye decision, supra, the lucid interval rule holds that a generalized or non-specific dementia or condition of mental impairment is not of itself sufficient to demonstrate that testator lacked testamentary capacity if the testator had lucid intervals, i.e., periods of time in which the mental impairments abated and testator could interact, think, reason and speak relatively normally. Anyone with exposure to individuals suffering from dementia, senility or related neurological deficits is aware that mental acuity is not a static thing, but frequently varies significantly from day to day and even from hour to hour. The Plaintiff will frequently have difficulty finding witnesses, lay or expert, who have knowledge of the testator's precise mental state at the time of execution of a will. The Defendant, however, will usually have the scrivener of the will, its subscribing witnesses, and probably others to attest that the will was executed in a lucid interval. The issue normally devolves to an inquiry as to whether the testator ever had lucid intervals after a given point in time. Other than testimony of witnesses, other frequently employed techniques to demonstrate lack of capacity involve medical records, particularly hospital or nursing home records, which reflect disorientation, confusion, forgetfulness, dementia or conduct or activities

inconsistent with normal mental functioning, i.e. aggressive behavior, wandering, inability to perform simple mental tasks, etc. Nurses' notes and observations from medical charts are frequently full of these sorts of episodes which can be most helpful to the Plaintiff's case. Defendants may rely obviously, on the absence of such notations, especially at or about the crucial time.

C. Proof of Undue Influence. As discussed above, proof of undue influence is normally based upon evidence tending to establish the presence of one or more of the badges of undue influence. Another aspect of undue influence which is usually found is the existence of a confidential, i.e. fiduciary or quasi fiduciary, relationship between the Defendant and the testator. Undue influence is never presumed, however, no matter how strong the relationship between the parties, as the Bye case has re-emphasized. However, the reliance, dependence and vulnerability components of the relationship are strong evidence, if coupled with other aspects of overreaching. As the cases recite, undue influence is a species of fraud and is rarely practiced in daylight; e.g. see McKinney vs. Montgomery, Ky., 248 S.W.2d 719 (1952). Furthermore, each component relied upon to establish the undue influence may well be insufficient standing alone; however, it is the effect of all the circumstances taken together which show the undue influence. Walls vs. Walls, Ky. 99 S.W. 969 (1907). Other aspects or components of proof of undue influence are discussed in Section V above. The usual mode of refuting such charges is to show testator's declarations of intent consistent with the will, especially at a time and place when the Defendant was absent, and by demonstrating that the testator had the benefit of independent advice, i.e., normally a disinterested attorney, about the will.

D. Declarations of the Deceased. It is uniformly held that direct declarations of the deceased, whether offered by interested parties or not, are admissible in a will contest in order to

demonstrate the relationship between the parties, the susceptibility of the decedent to undue influence, the testator's state of mind, and possible other relevant issues. Hall vs. Childress, Ky., 420 S.W.2d 398 (1967); Welch's Administrator vs. Clifton, Ky., 1725 S.W.2d 221 (1943). Under the Kentucky Rules of Evidence such declarations are an express exception to the hearsay rule.[3] However, the authorities hold that such declarations while admissible, are not themselves direct evidence of undue influence. Hence, a case cannot be pitched solely upon the statement that for example the testator said, "Momma made me write that will". However, such testimony would be admissible for the purpose of showing susceptibility to undue influence and, in one Kentucky case, the testimony that the testator had made a will to "keep down the hell at home" was held admissible; Powell vs. Powell's Administrator, Ky., 78 S.W.2d 152.

E. Testimony by Counsel for Defendants. A rather interesting problem which occurs with amazing frequency is where the scrivener of the will represents the Defendant executor in the probate proceeding in District Court, and also represents the Defendant in the will contest action in the Circuit Court. Thus, the attorney, who is clearly a material witness, is also actively defending the Circuit Court action. This would appear to be a violation of Rule 3.7(a) of the Kentucky Rules of Professional Conduct, which requires that a lawyer not act as advocate at a trial in which the lawyer is likely to be a necessary witness. While the Rule states several exceptions, none would appear to be applicable. Nevertheless, many attorneys rely on Adams vs. Flora, 445 S.W.2d 420 (1969), as grounds to remain in the role of attorney for the Defendant in the will contest case. The Adams case has not been overruled and whether its holding has been abrogated by the above cited disciplinary rule is yet to be determined by the Supreme Court. That point aside, however, counsel for Plaintiff will also need to consider the practical aspect of the situation. Is it better to make a motion to disqualify Defendant's counsel or is it

[3] Ky. Rules of Evidence, Sec. 803(3).

more advantageous to Plaintiff's case to put the adversary in the unseemly position of being crossed-examined during a trial at which defense counsel is serving as an active advocate? That is a decision which, in consultation with the client, will need to be made on a case by case basis.

F. Evidence Post-dating the Contested Will. As a general and broadly stated rule, evidence of events or circumstances which occur after the date of the challenged will is not relevant. However, this rule must be taken in context of the nature of the case. For purposes of testamentary capacity, clearly the testator's condition at a remote time after the will was executed has no bearing on the condition at the time of the will. However, some cases have permitted medical evidence of circumstances within a brief time after the execution of the will, i.e. days or weeks, as likely indicating mental condition as of the date of the will. The point is buttressed if the medical expert is able or willing to state that the condition could not have changed to any great degree in the interim. In an undue influence case, however, there is somewhat more latitude and a greater probability of admission of evidence occurring after the date of the will. This is because one must differentiate between direct evidence of undue influence on one hand and circumstances on the other hand, some of which occur after the date of the will, which nonetheless may indicate that undue influence existed at the time of the will's making. For example, at least two of the commonly stated badges of undue influence clearly imply conduct or actions after the date of the will – possession of the will by the undue influencer and keeping the testator in seclusion. At least one foreign case has held that evidence of a spouse's indifference to the testator's welfare and her disposition to exercise undue influence (which occurred more than two years after the will was admissible). See Neill vs. Brackette, Mass., 135 N.E. 690 (1922).

The ubiquitous Bye case also speaks to this issue, by reiterating the general rule that the undue influence must be at or before the will's execution. Therefore, the Rule might be able to be stated as follows: the undue influence must affect the will and therefore must have occurred on or before its making, but the evidence that undue influence was exercised may be based upon circumstances which exist or occur after the date of the will's making.

CONCLUSION

As stated in the Introduction, the premise of this paper is that "effective handling of a will contest" is not equivalent to victory, regardless of which side of the case counsel represents. No litigator can ever guarantee results in any case no matter how seasoned, prepared, and effective he or she is at trial. This is particularly true in will contest cases. Nevertheless, no one can dispute the premise, however, that when all other things are equal, the more effective advocate will more often succeed.

FOR EDUCATIONAL USE ONLY
Copr. © West 2001 No Claim to Orig. U.S. Govt. Works

975 S.W.2d 451
(Cite as: 975 S.W.2d 451)

Supreme Court of Kentucky.

Mary Ruth BYE, Appellant,
v.
Sylvia Ann MATTINGLY, Successor Administratrix Cum, Testamento Annexo, of the Estate of William Louis McQuady, Richard Keith McQuady, and Acracia G. Beavin, Appellees.

No. 97-SC-208-DG.

Sept. 8, 1998.

Testator's former housekeeper brought action against executor of testator's estate and beneficiaries, challenging validity of will on grounds of undue influence and lack of testamentary capacity. The Breckinridge Circuit Court, Ronnie C. Dortch, J., upheld will. Former housekeeper appealed. The Court of Appeals, 1996 WL 531751, affirmed. After granting discretionary review, the Supreme Court, Stephens, C.J., held that: (1) pursuant to presumption arising under lucid interval doctrine, testator had requisite testamentary capacity; (2) will was not result of undue influence; and (3) any error resulting from permitting judge for same circuit to testify as rebuttal character witness for attorney, after former housekeeper sought to discredit will by discrediting attorney as drafter, was harmless.

Affirmed.

Wintersheimer, J., concurred in the result.

West Headnotes

[1] Wills k52(3)
409k52(3)

Pursuant to presumption arising under lucid interval doctrine, testator who suffered from Alzheimer's disease and had been adjudged partially disabled had requisite testamentary capacity at time he executed contested will, given failure of party challenging will's validity to show that testator did not have lucid period at will execution.

[2] Wills k52(1)
409k52(1)

There is a strong presumption in favor of a testator possessing adequate testamentary capacity which can only be rebutted by the strongest showing of incapacity.

[3] Wills k53(2)
409k53(2)

Testamentary capacity is only relevant at the time of execution of a will.

[4] Wills k21
409k21

Any order purporting to render a person per se unable to dispose of property by will is void ab initio, as such a ruling on testamentary capacity would be premature.

[5] Wills k53(1)
409k53(1)

Kentucky is committed to the doctrine of testatorial absolutism, whose practical effect is that the privilege of citizens to draft wills to dispose of their property is zealously guarded by the courts and will not be disturbed based on remote or speculative evidence.

[6] Wills k31
409k31

Degree of mental capacity required to make a will is minimal.

[7] Wills k31
409k31

Minimum level of mental capacity required to make a will is less than that necessary to make a deed or a contract.

[8] Wills k50
409k50

To validly execute a will, a testator must (1) know the natural objects of her bounty, (2) know her obligations to them, (3) know the character and value of her estate, and (4) dispose of her estate according to her own fixed purpose.

[9] Wills k31
409k31

[9] Wills k32
409k32

[9] Wills k47
409k47

Merely being an older person, possessing a failing memory, momentary forgetfulness, weakness of mental powers or lack of strict coherence in conversation does not render one incapable of validly executing a will.

[10] Wills k316.2
409k316.2

Every man possessing the requisite mental powers may dispose of his property by will in any way he may desire, and a jury will not be permitted to overthrow it, and to make a will for him to accord with their ideas of justice and propriety.

[11] Wills k24
409k24

While a ruling of total or partial disability is evidence of a lack of testamentary capacity, it is not dispositive of the issue.

[12] Wills k52(3)
409k52(3)

Under "lucid interval doctrine," when a testator is suffering from a mental illness which ebbs and flows in terms of its effect on the testator's mental competence, it is presumed that the testator was mentally fit when the will was executed.

[13] Wills k52(1)
409k52(1)

Burden is placed upon those who seek to overturn a will to demonstrate the lack of testamentary capacity.

[14] Wills k52(3)
409k52(3)

Presumption of testamentary capacity created under lucid interval doctrine is a rebuttable one, so that evidence which demonstrates conclusively that the testator lacked testamentary capacity at the time of the execution of the will results in nullifying that will.

[15] Wills k156
409k156

[15] Wills k158
409k158

Testator's will was not result of undue influence; although testator suffered from partial disability when will was executed and beneficiary, as testator's limited conservator and guardian, had complete control of testator's affairs, no other indicia of undue influence existed.

[16] Wills k155.1
409k155.1

"Undue influence" is a level of persuasion which destroys the testator's free will and replaces it with the desires of the influencer.

[17] Wills k155.2
409k155.2

In discerning whether influence on a given testator is "undue," courts must examine both the nature and the extent of the influence.

[18] Wills k155.2
409k155.2

[18] Wills k155.4
409k155.4

To be "undue" influence, influence on testator must be of a type which is inappropriate; influence from acts of kindness, appeals to feeling, or arguments addressed to the understanding of the testator are permissible.

[19] Wills k155.3
409k155.3

Influence on testator from threats, coercion and the like are improper and not permitted by the law.

[20] Wills k159
409k159

To be "undue" influence on testator, influence must be of a level that vitiates the testator's own free will so that the testator is disposing of her property in a manner that she would otherwise refuse to do.

[21] Wills k155.1
409k155.1

Essence of undue influence inquiry is whether the testator is exercising her own judgment.

[22] Wills k155.1
409k155.1

In addition to demonstrating that undue influence was exercised upon the testator, a contestant asserting undue influence must also show influence occurring prior to or during the execution of the will; undue influence exercised after the execution of the will has no bearing whatsoever upon whether the testator disposed of her property according to her own wishes.

[23] Wills k159
409k159

To support undue influence claim, influence must operate upon the testator at the execution of the will; if the influence did not affect the testator, then such conduct is irrelevant.

[24] Wills k159
409k159

Even if undue influence occurred many years prior to the execution of the will, but operates upon the testator at the time of execution, it is improper and will render the will null and void.

[25] Wills k155.1
409k155.1

[25] Wills k156

409k156

To determine whether a will reflects the wishes of the testator, the court must examine the indicia or badges of undue influence, including a physically weak and mentally impaired testator, a will which is unnatural in its provisions, a recently developed and comparatively short period of close relationship between the testator and principal beneficiary, participation by the principal beneficiary in the preparation of the will, possession of the will by the principal beneficiary after it was reduced to writing, efforts by the principal beneficiary to restrict contacts between the testator and the natural objects of his bounty, and absolute control of testator's business affairs.

[26] Wills k163(1)
409k163(1)

When a contestant seeks to claim that undue influence was employed upon a testator, the burden is upon the contestant to demonstrate the existence and effect of the influence.

[27] Wills k163(1)
409k163(1)

Merely demonstrating that the opportunity to exert undue influence existed is not sufficient to sustain the burden of proving that such influence was exerted.

[28] Wills k156
409k156

When undue influence and a mentally impaired testator are both alleged and the mental impairment of the testator is proven, the level of undue influence which must be shown is less than would normally be required since the testator is in a weakened state.

[29] Wills k163(2)
409k163(2)

No presumption of undue influence arises from a bequest by a testator who has a confidential relationship with the beneficiary.

[30] Wills k163(2)
409k163(2)

When a testator has a confidential relationship with one who receives a benefit under a will, such a transaction should be examined and placed into evidence before the jury, but no presumption of wrongdoing is created.

[31] Guardian and Ward k69
196k69

Contract between a guardian and ward creates a presumption against the transaction which must be rebutted by the guardian with clear and convincing evidence.

[32] Wills k393.1
409k393.1

Supreme Court is particularly disinclined to set aside a jury's decision in which it has found a will to be valid.

[33] Wills k163(4)
409k163(4)

Presumption of undue influence arising from grossly unreasonable will in which principal beneficiary actively participated in will's execution did not apply to will in which beneficiary's participation was merely to drive testator to and from lawyer's offices.

[34] Wills k163(4)
409k163(4)

In those instances in which a will is grossly unreasonable and the principal beneficiary actively participated in its execution, a presumption of undue influence arises.

[35] Wills k163(4)
409k163(4)

If the will contestant can offer evidence that will is grossly unreasonable and principal beneficiary actively participated in its execution, then the burden of persuasion on undue influence claim shifts to the proponents of the will, but it does not relieve the contestants of the continuing burden of proof.

[36] Wills k400
409k400

Any error resulting from permitting judge for same circuit to testify as rebuttal character witness for attorney, after will contestant sought to discredit will by discrediting attorney as drafter, was harmless, given that judge was subpoenaed by will proponents, and thus his testimony was permissible under ethical rules, and testimony was relatively brief and limited in scope. Sup.Ct.Rules, Rule 4.300, Code of Jud.Conduct, Canon 2, subd. B.

***453** O. Grant Bruton, Louisville, Kentucky, for appellant.

Kenton R. Smith, Steven R. Crebessa, Brandenburg, Kentucky, for appellees.

STEPHENS, Chief Justice.

The testator, William Louis McQuady, and Alberta Beavin McQuady were married for forty-five years prior to Ms. McQuady's death on March 23, 1989. In October of 1988, the McQuadys executed identical wills ***454** which left the surviving spouse in possession of the entire estate. In the event that there was no surviving spouse, all realty was to pass to Richard Keith McQuady, a second cousin once removed to William McQuady, and all personalty was to pass to Samuel Thomas Beavin, brother of Alberta Beavin McQuady. Accordingly, on Ms. McQuady's death, the entire estate passed to Mr. McQuady.

Following his wife's death, Mr. McQuady retained Mary

Ruth Bye, appellant in this matter, to act as his housekeeper. Mr. McQuady was unable to see and required assistance to overcome this disability. During their marriage, Ms. McQuady had performed all tasks related to maintaining the household and Ms. Bye was to perform these tasks as part of her duties. Ms. Bye assumed her position as housekeeper in May of 1989.

On July 17, 1989, Mr. McQuady, accompanied by Ms. Bye, visited Herbert O'Reilly of Hardinsburg who had drafted the 1988 wills the McQuadys had executed. Mr. McQuady executed a new will that left his entire estate, save a hundred dollar bequest to St. Mary of the Woods Church, to Ms. Bye.

Subsequent to the execution of the 1989 will, Ms. Bye arranged for a garage to be constructed on Mr. McQuady's property. Following completion of the garage Mr. McQuady's car was never actually stored in the garage. However, at trial Ms. Bye testified that her car was periodically parked inside the garage. The relevance of this event was that it sparked concern in Mr. Beavin and Mr. Richard McQuady with regard to the use of Mr. William McQuady's money by Ms. Bye. The construction of the garage concerned Mr. Beavin and Richard McQuady as the McQuadys had lived in a frugal fashion during their forty-five year relationship and Mr. McQuady possessed an older automobile which had never been garaged in the past.

On May 18, 1990, the petition of Mr. Beavin and Mr. Richard McQuady to appoint a guardian/conservator for William McQuady was heard. As a result of that hearing the Breckinridge District Court appointed Mr. Beavin as a Limited Conservator and Limited Guardian for Mr. McQuady. Following the hearing, Mr. McQuady's health declined and he was admitted to the hospital on September 21, 1990. Mr. McQuady was diagnosed as suffering from Alzheimer's disease. It should be noted that the effects of Alzheimer's disease can be accentuated by poor health and/or poor treatment.

After Mr. McQuady was diagnosed with Alzheimer's disease, a petition seeking to permit Mr. McQuady to marry Ms. Bye was filed with the Breckinridge District Court. On May 17, 1991, a hearing was held in Breckinridge District Court to determine whether the petition of William McQuady to marry Ms. Bye should be granted. At that hearing Mr. McQuady testified that although he had signed the petition, he was misled in regard to the nature of the document. Mr. McQuady stated that he was told by the Byes not to worry about it and just sign it. The document was prepared by Ellen Bye, daughter of appellant.

During the course of this hearing, Mr. McQuady emphatically stated that he did not want to get married to Ms. Bye. He also stated that he was afraid of Ms. Bye. The court denied the petition to marry. Ms. Bye's services as housekeeper were subsequently terminated.

Five months after the hearing on the petition to marry, Mr. McQuady executed a new will. The net effect of the will executed October 29, 1991, was to re- enact the will he had executed in 1988, in effect leaving his personalty to Mr. Beavin and his realty to Mr. Richard McQuady. The 1991 will was drafted by Alton Cannon and was executed in his office. Richard McQuady drove William McQuady to Mr. Cannon's Law Offices, but Richard McQuady never participated in any discussion or activities regarding the will. William McQuady and Mr. Cannon privately discussed the will that Mr. McQuady desired. When the will was actually executed Mr. Cannon, Mrs. Sheila Cannon and William McQuady were the only three persons present.

On August 7, 1992, William McQuady died. Mr. Beavin was appointed executor of McQuady's estate. Appellant then brought ***455** the instant action, challenging the validity of the 1991 will on grounds of undue influence and lack of testamentary capacity. Mr. Beavin died on October 5, 1993 and Sylvia Mattingly, Mr. Beavin's daughter, was appointed by the Breckinridge Circuit Court to serve as a party-defendant in place of Mr. Beavin in his capacity as executor.

Following a five day trial, a jury returned a unanimous verdict for appellees. During the course of the trial Judge Samuel Monarch, a sitting judge on the Breckinridge Circuit Court, was called by appellees to testify as a witness. Judge Monarch had not been listed by appellees on their witness list. Judge Monarch testified as to the honesty and veracity of his former partner in legal practice, Alton Cannon. Appellants appealed the verdict to the Court of Appeals. A divided panel upheld the trial court. *Bye v. Mattingly,* Ky.App., 97-CA-1874-MR (Sept. 20, 1996). This Court granted discretionary review. We now affirm the Court of Appeals.

There are several issues which the parties have brought before this Court. First, whether a partial disability judgment against an individual removes that person's testamentary capacity. Second, whether a partial disability judgment creates a presumption that a testator lacks testamentary capacity. Third, whether a fiduciary relationship between a limited conservator/guardian and his ward creates a burden on the limited conservator/guardian to demonstrate the non-existence of undue influence. Fourth, whether it is proper for a circuit judge who sits in the same court as the instant trial to testify as a character witness. We shall respond to each of these issues in turn.

I. JUDGMENT OF DISABILITY PURSUANT TO KRS 387.500 ET SEQ. AND TESTAMENTARY CAPACITY.

[1] On July 9, 1990, pursuant to KRS 387.500 *et seq.,* William McQuady was adjudged partially disabled in the Breckinridge District Court. Appellants urge this Court to rule that the effect of such judgment was to remove McQuady's capacity to draft a will or in the alternative that a presumption against testamentary capacity was created by the judgment. We decline to make either such ruling.

[2][3][4] In Kentucky there is a strong presumption in favor of a testator possessing adequate testamentary capacity. This

presumption can only be rebutted by the strongest showing of incapacity. *Williams v. Vollman,* Ky.App., 738 S.W.2d 849 (1987); *Taylor v. Kennedy,* Ky .App., 700 S.W.2d 415, 416 (1985). Testamentary capacity is only relevant at the time of execution of a will. *New v. Creamer,* Ky., 275 S.W.2d 918 (1955). Thus any order purporting to render a person per se unable to dispose of property by will is void *ab initio,* as such a ruling on testamentary capacity would be premature. This is not to say that such an order is irrelevant, but rather it is not dispositive of the issue of testamentary capacity.

[5][6][7] "Kentucky is committed to the doctrine of testatorial absolutism ." J. Merritt, 1 Ky.Prac.--Probate Practice & Procedure, § 367 (Merritt 2d ed. West 1984). *See New v. Creamer,* Ky., 275 S.W.2d 918 (1955); *Jackson's Ex'r v. Semones,* 266 Ky. 352, 98 S.W.2d 505 (1937). The practical effect of this doctrine is that the privilege of the citizens of the Commonwealth to draft wills to dispose of their property is zealously guarded by the courts and will not be disturbed based on remote or speculative evidence. *American National Bank & Trust Co. v. Penner,* Ky., 444 S.W.2d 751 (1969). The degree of mental capacity required to make a will is minimal. *Nance v. Veazey,* Ky., 312 S.W.2d 350, 354 (1958). The minimum level of mental capacity required to make a will is less than that necessary to make a deed, *Creason v. Creason,* Ky., 392 S.W.2d 69 (1965), or a contract. *Warnick v. Childers,* Ky., 282 S.W.2d 608 (1955).

[8][9][10] To validly execute a will, a testator must: (1) know the natural objects of her bounty; (2) know her obligations to them; (3) know the character and value of her estate; and (4) dispose of her estate according to her own fixed purpose. *Adams v. Calia,* Ky., 433 S.W.2d 661 (1968); *Waggener v. General Ass'n of Baptists,* Ky., 306 S.W.2d 271 (1957); *Burke v. Burke,* Ky.App., 801 ***456** S.W.2d 691 (1990); *Fischer v. Heckerman,* Ky.App., 772 S.W.2d 642 (1989). Merely being an older person, possessing a failing memory, momentary forgetfulness, weakness of mental powers or lack of strict coherence in conversation does not render one incapable of validly executing a will. *Ward v. Norton,* Ky., 385 S.W.2d 193 (1964). "Every man possessing the requisite mental powers may dispose of his property by will in any way he may desire, and a jury will not be permitted to overthrow it, and to make a will for him to accord with their ideas of justice and propriety." *Burke v. Burke,* Ky.App., 801 S.W.2d 691, 693 (1991) (*citing Cecil's Ex'rs. v. Anhier,* 176 Ky. 198, 195 S.W. 837, 846 (1917)).

[11] In the instant case Mr. McQuady executed wills in 1988, 1989 and 1991. Appellant seeks to have the 1991 will declared invalid as it was executed following the 1990 adjudgment of partial incapacity. While a ruling of total or partial disability certainly is evidence of a lack of testamentary capacity, it is certainly not dispositive of the issue. This Court has upheld the rights of those afflicted with a variety of illnesses to execute valid wills. *Tate v. Tate's Ex'r,* Ky., 275 S.W.2d 597 (1955) (testator suffered deafness and retarded speech); *Bush v. Lisle,* 89 Ky. 393, 12 S.W. 762 (1889) (testator was blind); *In re: McDaniel's Will,* 25 Ky. 331 (1829) (testator was paralyzed); *Bodine v. Bodine,* 241 Ky. 706, 44 S.W.2d 840 (1932)(testator was an epileptic). We have not disturbed the testatorial privileges of those who believed in witchcraft [FN1], spiritualism [FN2] or atheism. [FN3] While none of these cases absolutely parallels the instant case, we recite them here to demonstrate how this Court has always taken the broadest possible view of who may execute a will no matter what their infirmity.

FN1. *Schildnecht v. Rompf's Ex'x,* 9 Ky.Law Rep. 120, 4 S.W. 235 (1887)

FN2. *Compton v. Smith,* 286 Ky. 179, 150 S.W.2d 657 (1941).

FN3. *Woodruff's Ex'r v. Woodruff,* 233 Ky. 744, 26 S.W.2d 751 (1930).

[12] When a testator is suffering from a mental illness which ebbs and flows in terms of its effect on the testator's mental competence, it is presumed that the testator was mentally fit when the will was executed. This is commonly referred to as the lucid interval doctrine. *Warnick v. Childers,* Ky., 282 S.W.2d 608, 609 (1955); *Pfuelb v. Pfuelb,* 275 Ky. 588, 122 S.W.2d 128 (1938). See *In re Weir's Will,* 39 Ky. 434 (1840); *Watts v. Bullock,* 11 Ky. 252 (1822). Alzheimer's is a disease that is variable in its effect on a person over time. It is precisely this type of illness with which the lucid interval doctrine was designed to deal. By employing this doctrine, citizens of the Commonwealth who suffer from a debilitating mental condition are still able to dispose of their property.

[13][14] The lucid interval doctrine is only implicated when there is evidence that a testator is suffering from a mental illness; otherwise the normal presumption in favor of testamentary capacity is operating. The burden is placed upon those who seek to overturn the will to demonstrate the lack of capacity. *Warnick,* 282 S.W.2d at 609; *Pfuelb,* 275 Ky. at 588, 122 S.W.2d at 128. The presumption created is a rebuttable one, so that evidence which demonstrates conclusively that the testator lacked testamentary capacity at the time of the execution of the will results in nullifying that will.

In the present case there is no question that Mr. McQuady suffered from Alzheimers disease. However, under the doctrine he is presumed to have been experiencing a lucid interval during the execution of the will. The wisdom of this doctrine is demonstrated by Mr. McQuady's testimony during the hearing on the petition for marriage in Breckinridge District court. During that hearing Mr. McQuady was very lucid and demonstrated a complete grasp of the circumstances in which he found himself. Appellant has failed to offer this Court evidence which demonstrates that the testator did not have a lucid interval during which he executed the 1991 will.

In sum, let it suffice to say that in the instant case a presumption of a lucid interval of testamentary capacity was appropriate.

***457** Given this Court's consistent attitude toward the virtually absolute right of the citizens of the Commonwealth to make wills, it would be incongruous for us now to announce a new rule of law which restricted these rights

which we have held in such high regard for so long. While the clear policy of the Commonwealth is that our citizens who are no longer able to fully care for themselves must be protected from the various societal predators, we will restrict their testamentary rights only when it is absolutely necessary and even then only to the degree required to defend their interests.

II. FIDUCIARY RELATIONSHIPS AND THE PRESUMPTION OF UNDUE INFLUENCE.

[15][16][17][18][19][20][21] Undue influence is a level of persuasion which destroys the testator's free will and replaces it with the desires of the influencer. *Nunn v. Williams,* Ky., 254 S.W.2d 698, 700 (1953); *Williams v. Vollman,* Ky.App., 738 S.W.2d 849, 850 (1987). In discerning whether influence on a given testator is "undue", courts must examine both the nature and the extent of the influence. First, the influence must be of a type which is inappropriate. Influence from acts of kindness, appeals to feeling, or arguments addressed to the understanding of the testator are permissible. *Nunn,* 254 S.W.2d at 700; *Fischer v. Heckerman,* Ky.App., 772 S.W.2d 642, 645 (1989). Influence from threats, coercion and the like are improper and not permitted by the law. *Lucas v. Cannon,* 76 Ky. 650 (1878). Second, the influence must be of a level that vitiates the testator's own free will so that the testator is disposing of her property in a manner that she would otherwise refuse to do. *See v. See,* Ky., 293 S.W.2d 225 (1956); *Rough v. Johnson,* Ky., 274 S.W.2d 376 (1955). The essence of this inquiry is whether the testator is exercising her own judgment. *Mayhew v. Mayhew,* Ky., 329 S.W.2d 72 (1959); *Copley v. Craft,* Ky., 312 S.W.2d 899 (1958).

[22][23][24] In addition to demonstrating that undue influence was exercised upon the testator, a contestant must also show influence prior to or during the execution of the will. Undue influence exercised after the execution of the will has no bearing whatsoever upon whether the testator disposed of her property according to her own wishes. *Bennett v. Bennett,* Ky., 455 S.W.2d 580 (1970); *Wallace v. Scott,* Ky.App., 844 S.W.2d 439 (1992); *Fischer v. Heckerman,* Ky.App., 772 S.W.2d 642 (1989). The influence must operate upon the testator at the execution of the will. If the influence did not affect the testator, then such conduct is irrelevant. *Bodine v. Bodine,* 241 Ky. 706, 44 S.W.2d 840 (1932); *Walls v. Walls,* 30 Ky.Law Rep. 948, 99 S.W. 969 (1907). However, even if the influence occurred many years prior to the execution of the will, but operates upon the testator at the time of execution, it is improper and will render the will null and void. *Id.*

[25] To determine whether a will reflects the wishes of the testator, the court must examine the indicia or badges of undue influence. Such badges include a physically weak and mentally impaired testator, a will which is unnatural in its provisions, a recently developed and comparatively short period of close relationship between the testator and principal beneficiary, participation by the principal beneficiary in the preparation of the will, possession of the will by the principal beneficiary after it was reduced to writing, efforts by the principal beneficiary to restrict contacts between the testator and the natural objects of his bounty, and absolute control of testator's business affairs. *Belcher v. Somerville,* Ky., 413 S.W.2d 620 (1967); *Golladay v. Golladay,* Ky., 287 S.W.2d 904, 906 (1955).

Applying these badges to the 1991 will, it is clear that no undue influence was present. Given the fact that a partial disability order was in place when the will was executed, there is no question that the testator was physically and mentally weak. Similarly, since a disability order was in place, Mr. Beavin had complete control of the testator's business affairs. However, none of the other badges are present with respect to the 1991 will.

[26][27][28] When a contestant seeks to claim that undue influence was employed upon a testator, the burden is upon the contestant to demonstrate the existence and effect of the influence. *Nunn v. Williams,* Ky., 254 ***458** S.W.2d 698, 700 (1953). Merely demonstrating that the opportunity to exert such influence is not sufficient to sustain the burden of proof. *Id.* When undue influence and a mentally impaired testator are both alleged and the mental impairment of the testator is proven, the level of undue influence which must be shown is less than would normally be required since the testator is in a weakened state. *Creason v. Creason,* Ky., 392 S.W.2d 69 (1965); *Sloan v. Sloan,* 303 Ky. 180, 197 S.W.2d 77, 80 (1946).

[29][30] In Kentucky no presumption of undue influence arises from a bequest by a testator who has a confidential relationship with the beneficiary. *Palmer v. Richardson,* 311 Ky. 190, 197, 223 S.W.2d 745, 749- 50 (1949); *McAtee v. McAtee,* 297 Ky. 865, 874, 181 S.W.2d 401, 405 (1944); *Kiefer's Ex'r v. Deibel,* 292 Ky. 318, 166 S.W.2d 430, 433-34 (1942); 1 Ky. Prac.--Probate Practice & Procedure, § 555 (Merritt 2d ed.1984). There is no question when a testator who has a confidential relationship with one who receives a benefit under a will, such a transaction should certainly be examined and placed into evidence before the jury, but no presumption of wrongdoing is created. In fact, it is not uncommon or inappropriate for a testator to make such a bequest to one who has provided comfort and support to the testator. *Ecken's Ex'x v. Abbey,* 283 Ky. 449, 141 S.W.2d 863 (1940); *Karr v. Karr's Ex'r,* 283 Ky. 355, 141 S.W.2d 279 (1940).

[31] We wish to note that in making this ruling we are not disturbing the well-settled rule that a contract between a guardian and ward does indeed create a presumption against the transaction which must be rebutted by the guardian with clear and convincing evidence. *Meade v. Fullerton's Adm'x,* 266 Ky. 34, 98 S.W.2d 1, 2 (1936). The distinction between a bequest in a will and a transaction between two parties is that a will gift does not involve conflicting interests. However, in a transaction, the parties are placed in an adversarial relationship in which each party is attempting to maximize his or her own benefit without regard to the other. Accordingly, all contracts between a ward and guardian are due a much higher level of scrutiny and thus the presumption against them is created.

[32] Accordingly, since no presumption against the validity of the 1991 will exists, the burden was on the appellant to show that the 1991 will was procured through undue influence. A jury unanimously found that the 1991 will was not procured by undue influence. Nothing appellant has offered this Court even comes close to rising to the level necessary to set the jury's verdict aside. This Court is particularly disinclined to set aside a jury's decision in which it has found a will to be valid. *Rodgers v. Cheshire,* Ky., 421 S.W.2d 599 (1967).

Appellant's argument, based on the idea that because the testator had been adjudicated as mentally infirm, he was more susceptible to undue influence, is indeed an interesting one. However, for some reason appellant urges this Court not to examine the 1989 will, procured under suspicious circumstances (under which she benefitted) but rather only apply its undue influence analysis to the 1991 will. We decline her invitation to do so. If testator was in a mentally feeble condition in July of 1990, then it is certainly possible--in fact likely--that he was in a similar condition one year earlier when he willed his entire estate to appellant. We find appellant's argument unpersuasive. However, as we find no undue influence in the execution of the 1991 will, we have no occasion to fully review the circumstances surrounding the enactment of the 1989 will.

[33][34][35] There is a presumption which has some potential application to the instant case. In those instances in which a will is grossly unreasonable and the principal beneficiary actively participated in its execution, a presumption of undue influence arises. *Hollon's Ex'r v. Graham,* Ky., 280 S.W.2d 544 (1955); *Gay v. Gay,* 308 Ky. 539, 215 S.W.2d 92 (1948). If the contestant can offer evidence of such activities, then the burden of persuasion shifts to the proponents of the will, but it does not relieve the contestants of the continuing burden of proof. *Gay,* 308 Ky. at 539, 215 S.W.2d at 92; *Kiefer's Ex'r v. Deibel,* 292 Ky. 318, 166 S.W.2d 430 (1942).

***459** The executions of the 1989 and 1991 wills are virtually identical in their facts. In 1989, Ms. Bye drove the testator to a lawyer and Ms. Bye was not privy to the drafting nor execution of the will. Following the execution ritual, Ms. Bye drove the testator home. In 1991, the same circumstance was repeated with Mr. Beavin driving testator to and from the lawyer's offices. Under neither of these circumstances can we say that Ms. Bye nor Mr. Beavin actively participated in the execution of the respective wills. Accordingly, this presumption does not apply in the instant case.

III. APPEARANCE OF SITTING CIRCUIT JUDGE AS A WITNESS AT TRIAL IN HIS OWN COURTHOUSE.

[36] During the course of the trial, appellant sought to discredit the 1991 will by discrediting its drafter, Alton Cannon. Appellant now complains that she was unfairly surprised when appellees were permitted to call Circuit Judge Samuel Monarch, who sits in the Breckinridge Circuit Court where this case was tried, as a character witness to rebut appellant's attacks on Mr. Cannon. Appellant asserts, *inter alia,* that it was improper for Judge Monarch to be permitted to testify as a witness in the very courthouse in which he was then sitting as a Circuit Judge. Appellant further complains that he had presided over the same panel of veniremen and at least two of the jurors had been jurors in a previous trial which Judge Monarch had conducted. It should be noted that Judge Monarch recused himself from participating in the instant case due to his previous relationship with Alton Cannon.

Obviously it is preferable that a sitting jurist never be called upon to testify in a trial, particularly within the jurisdiction over which he presides and very particularly in front of a panel of veniremen over which he originally presided. While this Court does not agree with appellant's characterization of appellees conduct as the "ultimate Home Cookin" ' ploy, we are in general agreement that this was a very unfortunate situation which should be avoided whenever possible. However, we find singularly uncompelling appellant's argument that she was "blind-sided" by Judge Monarch's surprise appearance, particularly after she placed Mr. Cannon's credibility in issue in the first place.

As the trial record clearly reflects, appellant decided to attempt to denigrate Mr. Cannon's reputation in an attempt to cast the execution of the 1991 will into doubt. This was a perfectly permissible trial strategy. However, appellant cannot now speak out of the other side of her mouth and say that she had no idea that a character witness might be called to rebut her assault. Appellees are under no obligation to warn appellant of their possible response to appellant's every conceivable course of action.

Under Canon 2(b) of the Code of Judicial Conduct, codified at SCR 4.300, a "judge should not ... testify voluntarily as a character witness." Judge Monarch was served with a subpoena by appellees. Accordingly, he did not testify voluntarily within the meaning of Canon 2(b). Since Judge Monarch's testimony was permissible, given its relative brevity and limited scope, any error which may have occurred was certainly harmless.

Accordingly, for the foregoing reasons the judgment of the Court of Appeals is affirmed.

COOPER, GRAVES, JOHNSTONE, LAMBERT and STUMBO, JJ., concur.

WINTERSHEIMER, J., concurs in result only.

END OF DOCUMENT

SUITS ALLEGING FIDUCIARY BREACHES

David B. Tachau
Tachau Maddox Hovious & Dickens PLC
Louisville, Kentucky

Copyright 2001, David B. Tachau

SECTION C

ESTATE LITIGATION: SUITS ALLEGING FIDUCIARY BREACHES

David Tachau
TACHAU MADDOX HOVIOUS & DICKENS PLC
200 S. Fifth St., Suite 200N
Louisville, Ky. 40202-3200
(502) 588-2000
fax: (502) 588-2020
email: dtachau@tmhd.com

July 12, 2001

28th Annual Midwest/Midsouth
ESTATE PLANNING INSTITUTE
University of Kentucky College of Law
Lexington, Ky.

SUITS ALLEGING FIDUCIARY BREACHES

I. ELEMENTS OF FIDUCIARY DUTY CLAIMS: WHO? WHAT? WHICH? .. C-1

A. ***Who*** Is A Fiduciary In Kentucky Law? C-1

B. ***What*** Duties Are Owed By A Fiduciary? C-1

C. ***Which*** Parties Are Owed Fiduciary Duties? C-3

D. ***What*** Remedies Are Available For Fiduciary Duty Breaches? C-3

II. SPECIAL PROBLEMS IN FIDUCIARY LITIGATION C-5

A. What If Fiduciary Duties Conflict: How Are Conflicts Resolved? C-5

B. Removal Of A Breaching Fiduciary: Jurisdictional Puzzle C-6

C. Attorney-Client Privilege C-7

ESTATE LITIGATION:
SUITS ALLEGING FIDUCIARY BREACHES

I. ELEMENTS OF FIDUCIARY DUTY CLAIMS: WHO? WHAT? WHICH?

A. *Who* Is A Fiduciary In Kentucky Law?

1. *Steelvest, Inc. v. Scansteel Service Center, Inc.*, Ky., 807 S.W.2d 476, 485 (1991):

   "[B]ecause the circumstances which may create a fiduciary relationship are so varied, it is extremely difficult, if not impossible, to formulate a comprehensive definition of it that would fully and adequately embrace all cases. Nevertheless, as a general rule, we can conclude that such a relationship is one founded on trust or confidence reposed by one person in the integrity and fidelity of another and which also necessarily involves an undertaking in which a duty is created in one person to act primarily for another's benefit in matters connected with such undertaking. This Court in the case of *Security Trust Co. v. Wilson*, 307 Ky. 152, 210 S.W.2d 336 (1948), quoted with approval the following definition of a fiduciary relationship:

   > 'The relation[ship] may exist under a variety of circumstances; it exists in all cases where there has been a special confidence reposed in one who in equity and good conscience is bound to act in good faith and with due regard to the interests of the one reposing confidence.' 307 Ky. at 157, 210 S.W.2d at 338."

2. *Who* is a fiduciary in estate matters

   - *See* KRS 395.001: "The term 'fiduciary' as used in this chapter means any person, association, or corporation meeting the requirements of KRS 395.005 … appointed by, or under the control of, or accountable to, the District Court, including executors, administrators, administrators with the will annexed, testamentary trustees, curators, guardians and conservators."

B. *What* Duties Are Owed By A Fiduciary?

1. *Steelvest, Inc. v. Scansteel Service Center, Inc.*, Ky., 807 S.W.2d 476, 484 (1991) ("the tendency of the law, both legislative and common, has been in the direction of enforcing increasingly higher standards of fairness or commercial morality in trade.") (citation omitted).

2. *Bryan v. Security Trust Co.*, 296 Ky. 95, 99, 176 S.W.2d 104, 106 (1943):

"The first duty is with respect to the relationship existing between the trustee and the beneficiary. This duty is, in effect, that of uberrima fides, or utmost fidelity. As trenchantly stated by the distinguished jurist, Chief Judge Cardozo, in *Meinhard v. Salmon*, 249 N.Y. 458, 164 N.E. 545, 546, 62 A.L.R. 1: 'Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior.'

"The duty has been defined and described in many ways. It is well expressed in 26 Bogert, *Trusts and Trustees*, § 543, as follows: 'One of the most fundamental duties of the trustee is that he must display throughout the administration of the trust complete loyalty to the interests of the cestui que trust. He must exclude all selfish interest and also all consideration of the welfare of third persons.'"

3. *See also Curtis v. Drybrough*, 70 F. Supp. 151, 153 (W.D. Ky. 1947), *also quoting Meinhard v. Salmon*, 164 N.E. 545 (N.Y. 1928):

   "Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions. ... Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court."

4. *See also* KRS 287.277 (establishing "standards for bank or trust company acting as fiduciary" in connection with prudent and diversified investments, in conformity "to fundamental fiduciary duties of loyalty and impartiality" and "with prudence in deciding whether and how to delegate authority and in the selection and supervision of agents" and "incur[ring] only costs that are reasonable in amount and appropriate to the investment responsibilities of the account").

C. *Which* Parties Are Owed Fiduciary Duties?

1. *Lucas v. Mannering*, Ky. App., 745 S.W.2d 654, 656 (1987) ("the executrix represents the testatrix and to a very great extent, the heirs, legatees, or distributees, for whose benefit probate proceedings are had."); *Carpenter v. Planck*, 304 Ky. 644, 201 S.W.2d 908 (1947) (administrator's duty is "to protect and preserve the Estate for the benefit of all of the heirs"); *Allen v. Foth*, 210 Ky. 343, 275 S.W. 804, 805 (1925) ("The widow as a distributee is vitally interested in the settlement of the estate.").

2. KRS 395.195 enumerates certain transactions authorized for personal representatives, and states that the personal representative may take those actions as long as the representative is "acting reasonably for the benefit of interested persons."

D. *What* Remedies Are Available For Fiduciary Duty Breaches?

1. Compensatory damages

   - *See Smith v. McMillan*, Ky., 841 S.W.2d 172, 175 (1992), *quoting with approval Paducah Area Public Library v. Terry*, Ky. App., 655 S.W.2d 19, 23 (1983) ("The object of tort law is to, so far as possible with money, place the injured party in the position he would have been if no tort had been committed. It is to provide full recompense but nothing more.").

2. Punitive damages

   - The General Assembly has attempted to restrict the availability of punitive damages, and limit them to circumstances where there was "fraud," "oppression" or "malice" as defined in KRS 411.186, but the Kentucky Supreme Court has asserted that state constitutional guarantees are more expansive. As defined in the statute:

     - "Fraud" means an intentional misrepresentation, deceit or concealment of material fact known to defendant, and made with the intention of causing detriment to plaintiff;

- "Malice" means conduct that was specifically intended, or done with reckless disregard of plaintiff's rights, to cause tangible or intangible injury to plaintiff. Malice may be implied from outrageous conduct and need not be expressed so long as the conduct is sufficient to evidence conscious wrongdoing. *Bowling Green Municipal Utilities v. Atmos Energy Corp.*, Ky., 989 S.W.2d 577 (1999); and

- "Oppression" means conduct specifically intended to subject plaintiff to cruel and unjust hardship.

- The Kentucky Supreme Court has not squarely invalidated these restrictions, but arguably has accomplished the same result by holding that punitive damages must be available more liberally, in circumstances where there is:

  - "Gross negligence" meaning wanton or reckless disregard of the consequences to plaintiff. The jury does not need to find that defendant intended to do the harm, nor have actual knowledge of the result. *Williams v. Wilson*, Ky., 972 S.W.2d 260, 264 (1998).

- *See also Banks v. Fritsch*, Ky. App. , 39 S.W.3d 474, 481 (2001) ("In false imprisonment cases, punitive damages are not justified absent 'a showing that the acts were either willful or malicious or that they were performed in such a way as would indicate a gross neglect or disregard for the rights of the person wronged.'"), *quoting Horton v. Union Light, Heat & Power Co.*, Ky., 690 S.W.2d 382, 389 (1985).

3. Equitable relief:

   - *Bryan v. Security Trust Co.*, 296 Ky. 95, 99, 176 S.W.2d 104, 107 (1943) ("Want of fidelity in the administration of a trust forfeits the trustee's right to compensation. This embraces dishonesty, negligence or wilful or gross misconduct.") (citation omitted).

II. SPECIAL PROBLEMS IN FIDUCIARY LITIGATION

A. What If Fiduciary Duties Conflict: How Are Conflicts Resolved?

- *See Wiggins v. PNC*, Ky. App., 988 S.W.2d 498, 501 (1998) (holding trustee liable for breach of fiduciary duty when it encroached on principal of one trust instead of a second trust without having obtained court authorization; "Generally, a trustee owes the duty of 'uberrima fides, or utmost fidelity' to the beneficiaries of a trust. *Bryan v. Security Trust Co.*, 296 Ky. 95, 99, 176 S.W.2d 104, 107 (1943). According to Black's Law Dictionary 299 (6th ed.1990), a conflict of interest exists in '[a] situation in which regard for one duty tends to lead to disregard of another.'").

  - At that time, KRS 386.820(2) provided:

    "If the duty of the trustee and his individual interest or his interest as trustee of another trust, conflict in the exercise of a trust power, the power may be exercised only by court authorization (except as provided in KRS 386.810, subsections (3)(a), (d), (f), (r), and (x) upon petition of the trustee."

  - Without amending KRS 386.820(2), the 2000 General Assembly enacted SB 309, which appears to have been aimed directly at reversing the holding of *Wiggins v. PNC Bank, Kentucky, Inc.*, *supra*, and created a new provision codified at KRS 287.220(3):

    "(3) A bank or trust company serving as a trustee of multiple trusts having one (1) or more common beneficiaries or remainder beneficiaries, need not obtain court approval for performance or execution of its duties, and it shall not be considered a conflict of interest solely because all beneficiaries or remainder beneficiaries of the trusts are not identical."

B. Removal Of A Breaching Fiduciary: Jurisdictional Puzzle

1. KRS 395.160(1) provides, in part: "If a personal representative moves out of the state and fails to designate a process agent as required by KRS 395.015(1), becomes insane or *otherwise incapable to discharge the trust*, goes bankrupt or insolvent or is in failing circumstances, the District Court shall remove him ... ."

    - Additional grounds for removal may include hostility toward beneficiaries, particularly where the fiduciary's own interests may create conflict. *See Price's Adm'r. v. Price*, Ky., 163 S.W.2d 463, 466 (1942) (affirming removal of the decedent's son as administrator where he had misled the widow into relinquishing her right to be appointed and then omitted certificates of deposit from the estate inventory in order to enhance his personal claim to own them; where conflicting claims involving a personal representative were made, "the personal representative should occupy a strictly neutral position and be in an attitude to advocate and obtain justice to all parties, and not be influenced by seeking to assert an adverse claim in favor of himself.").

    - *See also Barnett's Adm'r v. Pittman*, 282 Ky. 162, 137 S.W.2d 1098, 1100 (1940) ("Mere personal hostility toward a distribute[e] does not necessarily disqualify one to act as personal representative of an estate."); *Rieke's Adm'r v. Rieke*, 183 Ky. 131, 208 S.W. 764, 765 (1919) (even the "severest friction" will not furnish cause to remove an executor).

2. *Priestley v. Priestley*, 949 S.W.2d 594, 597 (Ky. 1997) ("upon the filing of a claim pursuant to KRS 395.510 where acts of mismanagement, fraud or deception are alleged, the circuit court has jurisdiction to settle the estate and adjudicate all claims associated therewith. KRS 24A.120. Even though KRS 387.210 confers exclusive jurisdiction upon the district court to appoint, remove and require accounting of committees and provides further for appeal to the circuit court from such acts or failure to act there appears to be no power to entertain actions involving such a fiduciary where mismanagement, fraud or deception is involved.").

C. Attorney-Client Privilege

1. In Kentucky:

- Kentucky's attorney-client privilege is contained in Ky. Rules of Evidence 503, which has been codified by statute, KRS 422A.0503. KRE 503(c) provides "The privilege may be claimed by the client, the client's guardian or conservator, the personal representative of a deceased client, or the successor, trustee, or similar representative of a corporation, association, or other organization, whether or not in existence." The commentary accompanying KRE 503(c) states: "KRE 503(c) makes it clear that the client is the holder of the privilege, that a fiduciary or other representative may claim the privilege, and that the attorney at the time of the communication may claim the privilege on behalf of the client … ." *See also* KRE 1104: "The commentary accompanying the Kentucky Rules is intended to explain its provisions and to aid in interpreting them. It should be emphasized, however, that the language of rules themselves constitute the law."

- There is no "fiduciary exception" to the attorney-client privilege in the Kentucky Rules of Evidence, although five other specific exceptions are enumerated; *see also* Kentucky Bar Association Ethics Opinion E-401 (1997) ("In representing a fiduciary the lawyer's client relationship is with the fiduciary and not with the trust or the estate, nor with the beneficiaries of a trust or estate," and "The lawyer's obligation to preserve client[] confidences under Rule 1.6 is not altered by the circumstance that the client is a fiduciary).

- *See generally* Robert G. Lawson, *The Kentucky Evidence Law Handbook*, § 5.10, at 40-41 (3d ed. Supp. 1999) (discussing judicial exception to attorney-client privilege created in *Garner v. Wolfinbarger*, 430 F.2d 1093 (5th Cir. 1970)).

2. Some authorities would restrict attorney-client privilege:

   - *See, e.g.,* Edna Selan Epstein, *The Attorney-Client Privilege and the Work Product Doctrine* (4th ed. 2001), at 113: "A particular complexity arises when a person serving as a fiduciary, such as a corporate officer, seeks legal advice respecting his or her fiduciary duties. When a fiduciary seeks legal advice with respect to his or her fiduciary role or duties, that fiduciary may not necessarily be able to claim the privilege in his or her individual capacity. Furthermore, developing case law suggests the fiduciary cannot, in that fiduciary capacity, assert the privilege in litigation against the fiduciary as an individual. ... The fiduciary will be deemed to be acting in a fiduciary, and not individual, capacity until such point as the beneficiary questions the action and an adversary relationship is thereby established. At that point in time, the fiduciary is free to consult an attorney in his or her individual capacity and assert the privilege on his or her own behalf."

   - IIA A. Scott and W. Fratcher, *The Law of Trusts* § 173 at 465 (1987), *relying on Talbot v. Marshfield*, 2 Drew & Sm. 549, 62 Eng. Rep. 728 (Ch. 1865): "A beneficiary is entitled to inspect opinions of counsel procured by the trustee to guide him in the administration of the trust. It is held, however, that where there is a conflict of interest between the trustee and the beneficiaries and the trustee procures an opinion of counsel for his own protection, the beneficiaries are not entitled to inspect the opinion."

3. Is Kentucky's statutory privilege better established?

   - *Prudence-Bonds Corp. in re Guaranty Trust Co. of New York*, 76 F. Supp. 643 (E.D.N.Y. 1948) (refusing to order disclosure of legal opinions which had been paid for out of trust funds in order to protect the right of the "corporate trustee, with its large responsibility, to seek legal advice and nevertheless act in accordance with its own judgment" as well as the attorney's right to give what he "then believed to be proper legal advice without being influenced by fear that in some subsequent litigation such opinions or advice so rendered, may be generally gone over with a biased eye and bring him before a court to explain why he gave same.").

- *Wells Fargo Bank, N. A. v. Superior Court*, 990 P. 2d 591, 594 (Cal. 2000) (daughter who was dissatisfied with the administration of a testamentary trust established by her father requested documents between trustee and counsel concerning allegations of misconduct; appellate court reversed trial court's ruling compelling production of documents, holding that California's statutory attorney-client privilege contained no "fiduciary" exception: "[T]here is no authority in California law for requiring a trustee to produce communications protected by the attorney-client privilege, regardless of their subject matter.").

- *Huie v. DeShazo*, 922 S.W.2d 920, 921 (Tex. 1996) (daughter who was beneficiary of a testamentary trust created under her mother's will sued her father, who was executor of her mother's estate and trustee of the trust, accusing him of self-dealing, diverting opportunities, commingling and converting property, and other forms of mismanagement. Daughter sought discovery from a lawyer who represented her father as executor and trustee, and had been compensated from estate and trust funds. Trial court held that attorney-client privilege did not prevent trust beneficiary from discovering pre-lawsuit communications between the executor/trustee and his lawyer, but did prevent discovery of communications made once "a litigious dispute existed" if the communications were to protect the executor/trustee and were paid for by him from his own funds. Texas Supreme Court reversed: "[N]otwithstanding the trustee's fiduciary duty to the beneficiary, only the trustee, not the trust beneficiary, is the client of the trustee's attorney. The beneficiary therefore may not discover communications between the trustee and attorney otherwise protected under Texas Rule of Civil Evidence 503."); *id.*, at 924:

  "The attorney-client privilege serves the same important purpose in the trustee-attorney relationship as it does in other attorney-client relationships. A trustee must be able to consult freely with his or her attorney to obtain the best possible legal guidance. Without the privilege, trustees might be inclined to forsake legal advice, thus adversely affecting the trust, as

disappointed beneficiaries could later pore over the attorney-client communications in second-guessing the trustee's actions. Alternatively, trustees might feel compelled to blindly follow counsel's advice, ignoring their own judgment and experience."

- *Barnett Banks Trust Company, N. A. v. Compson*, 629 So. 2d 849, 851 (Fla. App. 1993) (trustee agreed to produce documents "with regard to the administrative matters of the trust" but sought to protect documents "involving" a lawsuit with the settlor's widow. Trial court ordered production of the documents, partially because of prior case law and partially because of a Florida statute requiring trustees to "provide any vested beneficiary with relevant information about the assets of the trust and the particulars relating to administration." Appellate court reversed, and observed that under Florida law, "The real client of the law firms is the trustee," not a beneficiary like the widow. Court did not consider it determinative that the law firms were paid from trust assets because "the trustee has the burden of demonstrating that the expense was reasonably necessary and was incurred for the benefit of the trust.").

1000:mscother:FiduciarySeminarJuly01

ESTATE SETTLEMENT SUITS

Wayne F. Wilson
Goldberg & Simpson, P.S.C.
Louisville, Kentucky

Copyright 2001, Wayne F. Wilson

SECTION D

Prepared for the UK/CLE 28th Annual Midwest/Midsouth Estate Planning Institute

By:

Wayne F. Wilson
Goldberg & Simpson, P.S.C.
3000 National City Tower
Louisville, Kentucky 40202-3118
502-589-4440
Wayne@gsatty.com

ESTATE SETTLEMENT SUITS IN KENTUCKY

I. ORIGIN AND PURPOSE OF THE SETTLEMENT SUIT STATUTE D-1

A. History D-1

B. Traditional Probate Procedures D-2

C. A Potential Increase In Insolvent And Contentious Estates D-3

D. Instances Where Traditional Probate Remedies May Be Inadequate D-4

1. A Means of Selling Real Property in Insolvent Estates D-4
2. Consolidating Multiple Actions D-5
3. Forcing a Correct and Expeditious Settlement of the Estate D-6

II. MECHANICS OF THE STATUTE D-7

A. Petitioner / Plaintiff (KRS 395.510) D-7

B. Necessary Parties (KRS 395.510) D-7

C. Contents Of Petition (KRS 395.515) D-8

D. What May Be Adjudicated (KRS 395.515) D-8

E. Sale Of Realty (KRS 395.515) D-9

F. Presentation Of Claims (KRS 395.520) D-9

G. Effect Of Creditor Presenting Claim (KRS 395.530) D-10

H. Effect Of Creditor Failing To Present A Claim (KRS 395.535) D-11

I. Enjoinment Of Collateral Actions (KRS 395.550) D-12

III. ATTORNEY FEES D-13

I. Origin and Purpose of the Estate Settlement Suit

A. History

The origin of the estate settlement suit statute[1] in Kentucky dates back at least as far as 1880. Although the settlement suit statute was historically more restrictive, the purpose of the statute has always been to provide a neutral venue for interested parties of an estate when traditional probate proceedings are inadequate for the settlement of the estate.

Formerly, the settlement suit statute existed primarily for interested parties of an estate to have a means of selling real property where the personalty was insufficient to pay the debts of the estate.[2] In 1964, the statute which spelled out the grounds for filing an estate settlement suit was expanded to specifically include other issues which may be adjudicated by the court.[3]

The modern statutory scheme consists of five chapters all of which have been subject to amendments at varying times. Thus, much of the language appears disjointed and often incomplete. Nonetheless, a review of old the Civil Code of Practice reveals that the settlement suit statutes remain largely unchanged since their inception.[4]

By comparison, the Uniform Probate Code ("UPC") does not contain any provisions quite like the format set forth in the settlement suit statutes. This is not surprising as the argument has been made that a comprehensive framework of probate procedures should obviate the need for an estate settlement suit outside of true adversarial proceedings such as a suit to remove the personal representative. Nonetheless, the UPC contains provisions for a personal representative or other interested party in an estate to petition the probate court for a "complete settlement of the estate".[5] This section allows the probate court to consider the final account of the personal representative and to adjudicate matters regarding a distribution of the estate.[6] However, this section is not specifically set up to accommodate multiple claims of creditors or to liquidate real estate where the personal estate is insufficient for the payment of debts.[7]

The intent of this writing is to provide the practitioner with an understanding of the purpose and benefits of the estate settlement suit statute, to set out a practical guide for use of the settlement suit, and to provide practice tips for the unwary personal representative and creditor.

---

[1] Former Civil Code of Practice Section 428.
[2] KRS 395.515 as it existed prior to its amendment by 1964 Ky. Acts c.105 § 1.
[3] KRS 395.515.
[4] Old Civil Code of Practice Sections 428 – 434.
[5] UPC 3-1001 (1969 Act).
[6] Id.

Lastly, it is intended to demonstrate that the settlement suit statute serves to provide the personal representative with a shield that can offer protection from creditors and beneficiaries or as a sword to be used by creditors and beneficiaries to obtain a proper and expeditious settlement of the estate.

Every insolvent or contentious estate is not a proper candidate for an estate settlement suit. To invoke the formal proceedings of such a suit, the estate will have to be of sufficient size or complexity to warrant the additional time which must be spent on matters relating to the suit. In the long run, however, a settlement suit is the most expeditious approach as it will conclude with the close of the estate.

B. Traditional Probate Procedures

Kentucky's current statutory framework for personal representatives and creditors would appear to offer most of the remedies necessary for thorough estate settlement. The personal representative is given authorization to take most actions necessary to settle the estate[8], the discretion to sell the personalty unless directed otherwise[9] and the power to sell land when authorized by the Will.[10] The personal representative is directed to file an inventory[11] and is further directed to file settlements with the probate court.[12] Creditors are generally given ample opportunity to present their claims to the personal representative and are permitted to commence an action against the personal representative upon the disallowance of a claim.[13] Lastly, there are adequate provisions contained in the statutory scheme to remove a personal representative who is not carrying out his or her duties in a prudent manner.[14] Nonetheless, there will be instances when the circumstances of an estate will require the personal representative to exercise more than a comfortable amount of discretion, to defend a multiplicity of law suits, or to ask or answer questions which are clearly adversarial in nature and which belong in circuit court. Conversely, there will be instances when creditors and beneficiaries of an estate must resort to litigation to realize their share of the estate and the format of the settlement statute will best allow them to attain their goal.

---

[7] Id.
[8] KRS 395.195.
[9] KRS 395.200.
[10] KRS 395.220.
[11] KRS 395.250.
[12] KRS 395.600.
[13] KRS 396.005 et. seq.
[14] KRS 395.160

The purpose of the settlement statute is to provide a forum for the court to resolve genuine issues regarding creditors' claims or about what constitutes a correct and lawful settlement of the estate. Once the suit is filed the estate is essentially removed from district court for settlement purposes. The settlement suit will conclude with a commissioner's report recommending a distribution scheme, the discharge of the personal representative and the close of the estate. Upon court approval of the Commissioner's report, an order will be entered binding all interested parties and closing the estate. Thus, when the settlement suit concludes, there will be nothing left to do for probate purposes. This consolidation offered by the settlement suit statute is also one of its biggest benefits.

C. A Potential Increase in Insolvent and Contentious Estates

Even though the traditional probate and claims statutes have been fine tuned by the legislature over the years, it seems likely that the instances where a Decedent's probate estate will be insolvent or will be subject to adversarial type issues which belong in circuit court are going to increase. More and more the financial services industry is offering products which by-pass probate by paying to a named beneficiary upon the death of the account owner. These non-probate transfers include IRAs, life insurance, annuities and payable on death accounts. Many couples still use joint tenancy with right of survivorship to pass assets upon the death of the first spouse. Furthermore, the estate planning techniques of attorneys and other professionals such as revocable and irrevocable trusts serve to pass assets outside of probate. All of these non-probate transfers can leave behind a significant amount of personal property but a probate estate which is insufficient to satisfy the claims of all creditors.

Another factor which may lead to the increase in insolvent estates is the enormous health care costs which face many families during a final illness. As the baby boomer generation continues to mature, insolvent estates due to extraordinary medical expenses may become more prevalent.

Estate settlement suits are often filed when the estate is solvent but a contentious relationship exists between the personal representative and the other interested parties (i.e., surviving spouse, personal representative v. step-children, beneficiaries).[15] As the number of

[15] For actual examples, see, Priestley v. Priestley 949 S.W. 2d. 594 (Ky. 1997) and Ray v. Ray 182 S.W. 2d. 664 (Ky. 1944)

estates increase where a "non-traditional" family exists, the number of these contentious relationships among the parties will rise in direct proportion.

D. Instances where Traditional Probate Remedies may be Inadequate

The estate settlement statute does not specifically set out the necessary criteria for filing a suit. Rather, the statute which sets out the necessary contents of the petition merely gives direction about what issues may be adjudicated by the Court. This vague direction is a result of the statute being revised in 1964 and the newer language being inserted directly into the middle of the statute.

1. A Means of Selling Real Property in Insolvent Estates

The Kentucky statutes provide three methods by which real estate may be sold or divided pursuant to a court order. One statute[16] allows for a party seeking a division or sale of land to file an action in circuit court to determine whether the land may be divided without materially impairing its value. If the court finds that the land is not divisible, it may order its sale and the proceeds distributed to all parties in interest. Under this scenario, a court appointed commissioner will determine the divisibility of the land and will further determine how the land is to be divided upon distribution. This statute primarily exists for a surviving spouse and/or heirs to divide inherited land or to sell that land which is not divisible.

Another statute[17] provides for the sale of real property by a fiduciary pursuant to a court order. This action may be brought in district court and is often used by trustees and executors to dispose of realty, the sale proceeds from which are necessary to maintain beneficiaries, or where the realty is a burdensome asset of the trust or estate.

The third method by which real property may be sold by a personal representative or other interested party pursuant to a court order is through utilization of the settlement suit statute. While it is not necessary that the personal estate of a decedent be insufficient to pay his debts and administration expenses before a settlement suit is filed, it is most often the case.[18] Filing an estate settlement suit will provide parties with a means of selling real estate when the settlement is ongoing and there are insufficient personal assets to satisfy all debts and expenses of

---

[16] KRS 381.135.
[17] KRS 389A.010.
[18] But See, Smith v. Louisville Trust Co., 237 S.W.2d 836 (Ky. 1951) which stated that "[o]ne of the basic requirements for [a settlement] suit is that there be not sufficient personal estate for payment of the debts.

administration. In this instance, the settlement suit statute is the preferred method of selling real estate over the other two statutes for several reasons.[19]

First, is the stated intent of the statute allowing the personal representative to sell so much of the realty as is necessary for the payment of debts.[20] Next, is the benefit which accrues to the personal representative by having a forum where all creditors must prove their claims to a trial court commissioner. If there are any questions about the priority or validity of any claims or expenses they may be decided by the commissioner prior to settlement. For example, if there is a question about whether a payment by the personal representatives constitutes a valid funeral expense[21], then this dispute may be heard by the court and settled prior to distribution. Lastly, is the benefit of a statutory framework which is set out to allow the complete settlement of the estate in one venue. Under the first two methods, settlement of the estate must still proceed in district court pursuant to the traditional probate procedures. However, under the settlement suit statute, all matters will be consolidated before the commissioner who will ultimately make a report to the court regarding the sale of real property and the distribution of the proceeds therefrom.

2. Consolidating Multiple Actions

Under the district court procedure for claims against a decedent's estate, creditors have six months from the date of the personal representative's qualification to present their claim.[22] If it is necessary for the personal representative to disallow a claim in whole or in part, the claimant must commence an action on the claim against the personal representative no later than 60 days after the mailing of the notice of disallowance.[23]

In an estate with multiple creditors, it may be necessary for the personal representative to disallow a multitude of claims based on their validity or the fact that they are being exaggerated so that the creditor can obtain a higher proportionate share of the estate upon distribution, as is often the case in an insolvent estate. In these instances, the settlement suit statute can be used to

---

[19] See, Johnson v. Dodd's Adm'x, 37 S.W.2d 26 (Ky. 1931) where it was stated that "[I]t is his duty if it reasonably appears to the administrator that his decedent's estate is insolvent...to institute an action to settle his estate as authorized by the Code provisions."
[20] KRS 395.515.
[21] See, Oster's Ex'r v. Ohlman, 219 S.W. 187 (Ky. 1920) where the court held that thank you cards to sympathetic friends and lunches served to those sitting up with the decedent were valid funeral expenses to be paid from the estate.
[22] KRS 396.011.
[23] KRS 396.055.

preempt the filing of separate actions by creditors to collect the debt, or if such actions have already been filed, the suit may be used to temporarily enjoin, or as is more likely, consolidate, such actions all in one venue designed toward settlement of the estate. Furthermore, once the suit is filed, creditors will be put to the task of proving their claims to the commissioner and to the other creditors who will be sure to review other claims to make certain they are not being exaggerated in an effort to increase a distributable share. Under regular probate proceedings, other creditors would not ever receive a copy of other claims unless they file a demand for notice. This has the effect of placing a check on all the creditors and lifting some of the burden on the personal representative to closely scrutinize every claim.

3. Forcing a Correct and Expeditious Settlement of the Estate

In 1964, the settlement suit statute was revised to allow the filing of a settlement suit "if it appears that there is a genuine issue concerning the right of any creditor, beneficiary or heir at law to receive payment or distribution, or if it appears that there is a genuine issue as to what constitutes a correct and lawful settlement of the estate, or a correct and lawful distribution of the assets".[24] In practice, the settlement suit has long been used by creditors and beneficiaries to enforce their rights in an estate.[25]

Subject to certain restrictions discussed herein, any party who has an interest in a decedent's estate may file a petition that institutes an action pursuant to the settlement suit statute.[26] A survey of the case law in this area reveals that creditors and beneficiaries of an estate are often the petitioners in an estate settlement suit. A creditor or a beneficiary may use a settlement suit to realize their share of an estate where the personal representative is uncooperative or delaying distribution or who may be mismanaging the estate.

An estate settlement suit is more attractive than traditional litigation because it brings all aspects of the estate under one umbrella. A suit in circuit court to remove an executor may be successful but the estate must still be settled. Likewise, a suit by a creditor against a personal representative to enforce a claim may yield a judgment in favor of the creditor. But that judgment must still be paid out of the probate estate. Only through the institution of an estate

---

[24] KRS 395.515.

[25] Straton v. Wilson 182 S.W. 858 (Ky. 1916); Oster's Ex'r v. Ohlman 219 S.W. 187 (Ky. 1920); Bailey's Adm'r v. Hampton Grocery Co. 224 S.W. 1067 (Ky. 1920); Johnson v. Dodd's Adm'x 37S.W. 2d. 26 (Ky. 1931); Ray v. Ray 182 S.W. 2d. 664 (Ky. 1944); Priestley v. Priestley 949 S.W. 2d. 594 (Ky. 1997).

[26] KRS 395.510.

settlement suits will creditors and beneficiaries realize their share of the estate at the close of the proceedings.

II. Mechanics of the Statute.

A. Petitioner/Plaintiff (KRS 395.510)

The first of the five settlement suit statutes states that the personal representative, legatee, distributee, or creditor of a deceased person may bring an action for the settlement of an estate which must be initiated in Circuit Court. However, no party but the personal representative may bring the settlement suit until the six month claim period has expired after the date of the representative's qualification.[27]

When the personal representative initially qualifies in probate court, the claims statutes bar a creditor's suits so long as the creditor's claim is not disallowed. The personal representative is not put to a decision about a creditor's claim until 60 days from the expiration of the claims period.[28] Once the personal representative makes the decision to disallow claims he may be forced to defend a multitude of lawsuits. One example is where the decedent was the "key person" in a business and also a guarantor on the business debts. After death, creditors will want to pursue both the company and the decedent. Thus, the settlement suit becomes a shield for the personal representative to use when he must disallow a number of claims and be subject to multiple suits in Circuit Court.

B. Necessary Parties (KRS 395.510)

The personal representative, the beneficiaries, persons having a lien upon estate property, creditors of the decedent, so far as known to the plaintiff, and "all persons having an interest in the property left by a decedent" must all be made parties to the action.[29] In practice, bringing all parties before the court may result in a somewhat humorous case styling (e.g. Emily Lawrence, Executor v. Emily Lawrence, Trustee).[30] Nonetheless, it is of the utmost importance that all parties having interest in the estate be made respondents in the suit. As with Will contest

---

[27] KRS 395.510.
[28] KRS 396.055
[29] KRS 395.510.
[30] See, White v. White where the court found that the Administrator's suit was defective because he didn't name himself as a defendant in his individual capacity as an heir. White v. White, 883 S.W. 2d 502 (Ky. App. 1994).

actions, a failure to bring all necessary parties before the court can result in a fatal flaw to the proceedings.[31]

If the estate contains any real property which is to be sold, the spouse of any beneficiary must also be made a party to the suit so that such spouse may release his or her dower/curtsey interest in the property.[32]

C. Contents of Petition (KRS 395.515)

The statute appears only to require that the petition state the amount of the debts as far as known to the petitioner and the nature and value of the real and personal property.[33] Of course, proper pleading requires the petitioner to provide the court with the statutory jurisdiction, (i.e., "this action is pursuant to KRS 395.510"), a general averment describing the issues which prompted the petitioner to file the settlement suit (i.e., "the Executor is uncertain as to what constitutes a correct and lawful settlement of the estate") and a prayer for relief.

D. What may be Adjudicated (KRS 395.515)

It is interesting to note that the statute states only that "if it shall appear that the personal estate is insufficient for the payment of all debts, the court may order the real property descended to the heirs of devisees or order the sale of so much as shall be necessary to pay debts of the estate."[34] Clearly, the statute contemplates the filing of estate settlement suits for reasons other than insolvency. Other issues which may be adjudicated by the court include a genuine issue concerning the right of any creditor, beneficiary or heir at law to receive payment or distribution, or a genuine issue as to what constitutes a correct and lawful settlement of the estate, or a genuine issue as to the correct and lawful distribution of the assets.[35]

The personal representative may bring a settlement suit to consolidate multiple actions which have been filed against the estate in circuit court. By consolidating these actions with the settlement suit, the settlement process can proceed and the case will ultimately conclude with a distribution of the assets rather than a mere judgement against the estate. The petitioner in a settlement suit may also wish the court to adjudicate other issues such as a Will construction or a

---

[31] See, Hackett v. State Bank and Trust Co, 159 S.W. 952 (Ky. 1913) (widow failed to name children as parties or even state if decedent had children; presumed he had children since widow only asked for dower interest). West v. Goldstein, 830 S.W.2d 379 (Ky. 1992).
[32] Barry v. Fain's Adm'r 189 S.W. 220 (Ky. 1916)
[33] KRS 395.515. However, the Court will insist that the assets and debts of the decedent be listed. Smith v. Louisville Trust Co. 213 S.W.2d 987 (Ky. 1948)
[34] KRS 395.515.
[35] KRS 395.515.

determination of heirship.[36] This is acceptable since adversarial actions involved in an estate are to be brought in Circuit Court. Obviously, a personal representative may bring the settlement suit to obtain a court order directing the sale of real property where the estate's personal property is insufficient for the payment of debts and administration expenses. Creditors may bring estate settlement suits in place of a traditional circuit court action when their claim has been disallowed by the personal representative. Both creditors and beneficiaries may wish to bring the suit as a way of combating a perceived problem with the personal representative (whatever that problem may be) without having to bring an action for the removal of the fiduciary.[37]

E. Sale of Realty (KRS 395.515)

Once all issues concerning the distribution of claims of creditors and the distribution of estate assets have been resolved, the court may order the distribution or sale of as much of the real property as is necessary for the payment of estate debts.

F. Presentation of Claims (KRS 395.520)

The statute provides that the court shall appoint a commissioner who shall give notice of the suit by publication and require all creditors of the decedent to appear before the commissioner and prove their claims before a bar date to be named in the order.[38] According to the language of the statute it is up to the court to set the bar date for claims to be presented to the commissioner.

This brief statute is possibly the most important statute in the entire estate settlement suit scheme. It is also a most incomplete statute. First the statute directs that the court shall make an order for the creditors of a decedent to appear before a commissioner appointed by the court. However, the statute does not state whether the court shall appoint the commissioner upon its own initiative or whether the commissioner must be appointed upon motion by the petition or other party.[39]

The statute also states that the creditors' claims must be presented to the commissioner before a date to be named in the court's order. However, no direction is provided with respect to the duration of the period for filing claims with the commissioner. Should the court set the bar

---

[36] See, INFRA note 15.
[37] Priestley v. Priestley 949 S.W. 2d. 594 (Ky. 1997).
[38] KRS 395.520.
[39] In practice, the commissioner will be appointed upon motion of the petitioner unless some other party has already initiated litigation type discovery.

date to reconcile with the six month period set out in the probate code? What if the estate has already been open for two years? Then should the period for filing claims be only 30 days?

It is clear that if there is a failure to comply with the direction that a creditor's claim be presented directly to the commissioner, such creditor will be barred from participating in the distribution.

Almost always, upon filing a petition, each of the named respondents will file an answer to the petition along with a counter-claim stating the Respondent's claim to the estate. The answer, regardless of its content, will be insufficient for purposes of satisfying the statutory requirements for presenting the creditor's claim to the commissioner. Thus, even though a creditor may file an answer and counter claim with the court, it will still be necessary for the creditor to prove his claim to the commissioner. This harsh result is illustrated in the often cited case of First Nat. Bank of Louisville v. Prestonburg Nat. Bank, 567 SW 2d., (Ky. App. 1978).[40]

Considering the foregoing, an argument might be made that it is not even necessary to file an answer to an estate settlement suit petition. In practice, this will rarely, if ever, happen. The more likely scenario is that before the court has had an opportunity to refer the matter to a commissioner as is called for by the statute, the creditors' attorneys will proceed in a litigious manner not contemplated by the statute. Once the petition is filed, the petitioner's attorney must be prepared for the type of discovery requests more commonly found in traditional law suits. One of the benefits of filing an estate settlement suit is to consolidate other actions which have been filed in Circuit Court into an action designed with the goal of estate settlement. However, this goal of the statute will have to be communicated to the other parties involved in the suit.

G. Effect of Creditor Presenting Claim (KRS 395.530)

This statute states that where a creditor appears before the commissioner and presents his claim he thereby becomes a party to the estate settlement suit and is thus bound by the final judgment of the court allowing or rejecting his claim.[41]

If the petitioner filing the settlement suit is, as in most case, the personal representative, he will likely know who most of the creditors of the estate are. These debts will be set out in the petition. Certainly, it is possible that the petitioner will not be the personal representative or if it

---

[40] Although it must be noted that the facts of First National Bank of Louisville v. First National Bank of Prestonsburg do not squarely address the question of whether an answer and counterclaim to estate settlement suit petition are sufficient to set up a creditors claim.

[41] KRS 395.530.

is the personal representative he may not be aware of certain creditors. In any case, the court will set a bar date for claims to be presented by the commissioner. Each creditor who is already a party must once again prove his claim to the commissioner. In addition, any other creditors who become a party as a result of the commissioner's notice must also prove their claims with the commissioner. These additional creditors will not need to file an answer to the petition or otherwise enter a formal appearance as parties respondent to have their claims included in the settlement. By proving their claims with the commissioner, the creditors will automatically become a parties to the action and be bound by the court's judgments regarding distribution, and validity and priority of claims.[42]

In the past, it has been argued that because a creditor was not made an actual party respondent to the suit, the creditor was not bound by the court's decree regarding the distribution of the assets. The courts have repeatedly held, however, that where a creditor is required to appear before the commissioner and prove claim, he is bound by the court's decree in an action to settle a decedent's estate.[43]

H. Effect of Creditor Failing to Present Claim (KRS 395.535)

Creditors who fail to appear before the commissioner and prove their claims pursuant to the circuit judge's order, shall be barred from participating in the distribution of the estate.[44] The statute further states that where the creditor fails to present their claim, such creditor shall have no claim against the personal representative who has paid out the estate, the other creditors or beneficiaries of the estate.[45]

A creditor may timely file his claim in probate court and may also file an answer and counterclaim with the Circuit Court upon being served with the settlement suit petition. However, the statute makes clear that where the creditor does not present his claim to the commissioner he will be barred from participating in the distribution of the assets and shall have no recourse against the personal representative, the other creditors or the beneficiaries of the estate.[46] One of the purposes of the estate settlement suit is to provide the creditors and

---

[42] U.S. v. Buckley, 264 S.W.2d 65, (Ky. 1954).
[43] Massie v. Paul, 292 S.W.2d 11, (Ky. 1936): Combs v. Allen, 271 S.W. 598, (Ky. 1925).
[44] KRS 395.535.
[45] KRS 395.535.
[46] However, under prior law creditors were only barred from pursuing the personal representative. A statute in the old Civil Code allowed a creditor who had not received payment from the estate to pursue his claim, to the extent of the estate assets distributed, against a beneficiary so long as the claim could have been brought against the decedent, if living. Section 434 of the Old Civil Code.

beneficiaries with a measure of finality regarding the distribution of assets. This statute is consistent with that purpose by preventing further collection actions once the Judge has approved the final settlement.

I. Enjoinment of Collateral Actions (KRS 395.550)

This statute states that upon the institution of an estate settlement suit an order may be made enjoining the prosecution of actions against the personal representative, by creditors, for their demands.[47] The statute further states that collateral actions will not be enjoined unless the settlement suit has been commenced within three years after the qualification of the personal representative.[48]

On its face, this statute offers a welcome respite to the personal representative who is faced with defending multiple actions for the collection of debts. In reality it may seldom be appropriate to request that a Judge issue an Order enjoining collateral actions by estate creditors because the other matters need to proceed to judgment before the estate can be settled.

For example, where the decedent is merely a guarantor on a loan and the creditor has instituted action against the primary obligor and the decedent, the adjudication of the rights of the creditor with respect to the primary obligor is first necessary to establish the liability of the decedent. Thus, such creditor's share of the decedent's estate can not be properly established until the collateral action has reached its conclusion. In this instance, it is more appropriate to consolidate the collateral action with the estate settlement suit for inclusion in the commissioner's report and determination by the Judge.

Likewise, where the decedent participated in a debt as co-maker, the personal representative may have a right to contribution against the other co-maker. In this instance, it is the personal representative's duty to assure that the co-maker participates in both the creditor's suit and the settlement suit as the personal representative's right to contribution is an asset of the estate. Again, it is more appropriate to consolidate the two actions rather than to enjoin the creditor's action.

Regardless of whether the personal representative chooses to invoke the provisions of this statute, it is comforting to know of its existence. Furthermore, the personal representative will be

---

[47] KRS 395.550.
[48] KRS 395.550.

in a position to present it to the Judge when stating his position that a separate creditor's action should be joined with the settlement suit for adjudication.

III. Attorney Fees

Of course, if the personal representative of an estate must institute an estate settlement suit, his or her attorney will be compensated out the funds of the estate as an expense of administration. However, an attorney will be denied his fee if its shown that the settlement suit was clearly unnecessary and brought for only a self-serving purpose by the attorney.[49]

For attorney fees to be paid out of the estate, it must be shown that there was some good reason for bringing the estate settlement suit which benefits either the estate or the other beneficiaries.[50] In addition, where a settlement suit is filed by someone other than the personal representative, attorney fees may still be recovered from the estate as long as the purpose of the suit could be accomplished only through litigation or where the benefits of the suit will be shared equally by the distributees of the estate.[51]

---

[49] White v. White, 883 S.W.2d 502 (Ky. App. 1994). An interesting case in this area is Holburn v. Phanmiller's Adm'r, where the court much maligns an administrator and creditor for bringing a fruitless settlement suit. In rendering its opinion, the Court stated ..."This brings us to the consideration of another feature of this suit; that is, the right of the administrator to maintain this action under the circumstances, and especially of the liability of decedent's real estate to the rather extraordinary bill of costs brought about by this suit. No one could have died with less personal estate than Lawrence Phanmiller had, for he had none. The record shows that he had not even a rag, nor was it supposed that he had." Holburn v. Phanmiller's Admin, 71 S.W. 940 (Ky. 1903). Needless to say, the Court elected not to approve the attorney's fees in bringing the estate settlement suit.

[50] Johnson v. Ducobu, 258 S.W. 2d 509 (Ky. 1953).

[51] Gernert v. Liberty Nat. Bank & Trust Co., 145 S.W.2d 522 (Ky. 1940).

DEALING WITH THE INSOLVENT ESTATE

Chris Meinhart
Public Administrator - Jefferson County
Louisville, Kentucky

Copyright 2001, Chris Meinhart

SECTION E

DEALING WITH THE INSOLVENT ESTATE

I. INTRODUCTION E-1

II. DETERMINING AND COMPARING ASSETS/LIABILITIES E-1

A. Assets (Determining Fair Market Value Paramount) E-1

B. Liabilities / Claims E-2

III. AFTER INITIAL ASSESSMENT, CONSIDER PETITION TO DISPENSE WITH ADMINISTRATION - KRS 395.455 ..... E-2

IV. PROBATABLE ASSETS EXCEED DISPENSE OPTIONS BUT INSUFFICIENT TO PAY ALL LIABILITIES - WHAT NOW? E-3

V. ASSETS AND LIABILITIES DETERMINED - ESTATE IS INSOLVENT WHAT NOW? E-3

A. Don't Pay Anything Before Six Months From Appointment E-3

B. KRS 396.095 ..... E-3

C. Priorities E-4

VI. TOO MANY CREDITORS E-4

A. Mediation/Arbitration E-4

B. KRS 395.615 (Court Approval of Proposed Settlement) E-4

C. KRS 395.510 (Circuit Court Action To Settle) E-5

VII. MISCELLANEOUS E-5

A. Auctioneers E-5

B. Overpayment E-5

Dealing With the Insolvent Estate

Chris Meinhart, Public Administrator of Jefferson County
150 South Third Street
Louisville, KY 40202
(502) 589-2700
(502) 589-2825
meinhart@bellsouth.net

I. Introduction

"Dealing with the insolvent estate" for the general practitioner is not an overly complicated area of law. The issues therein are infrequently litigated. West's Kentucky Digest 2nd Edition, which gives key numbers 408-419 under the title "Insolvent Estates" cites a total of only four cases under that section which date between 1931 and 1967.

The few areas to look for in which the practitioner can get him/herself or the personal representative in trouble include, but are perhaps not limited to, a) preferential treatment of creditors; b) premature payment of assets; c) mistakes over priority; or d) miscalculations of payments due.

II. Determining and Comparing Assets/Liabilities (that is solvency)

This is the obvious first step in dealing with the insolvent estate, that is determining whether in fact the estate is solvent or not.

A. Assets (determining fair market value paramount)

i. Beware of PVA assessments, favor appraisals on anything not readily apparent. This will be an administrative expense.

ii. Create industry standard file in office (example NADA, Blue Books, etc.)

iii. Always look for credit life insurance on any assets which

are mortgaged (often times family,
decedent, even creditors are unaware of its existence,
request a statement from lienholder that none exists).

B. Liabilities/Claims.

i. Secured claim is usually self-evident. Request a statement of payoff as of date of death for mortgage or lienholders. Interest payable per contract with decedent.

ii. Check for judgment liens with County Clerk's Office.

iii. Child Support/Maintenance obligations - death does not mean an end to the decedent's child support obligation. KRS 406.041 sets forth that it can be modified upon death. Options include buyout for future obligation, etc. Make sure it gets ratified by the Family Court. Obvious concerns regarding statute of limitations as claim may belong to child who is under a legal disability which tolls the statute.
Child can continue to make claim for fifteen (15) years after emancipation.

iv. Death usually will end decedent's maintenance obligation unless otherwise agreed to in writing. Make sure to seek out and read the divorce Order or Agreement.

III. After Initial Assessment, Consider Petition to Dispense With Administration - KRS 395.455

i. If the $7500 spousal/children's exemption within KRS 391.030 and the preferred claims within 396.095 * which were paid by the widow or widower, exceed the value of probatable assets, the court can order transfer of these assets without a formal administration of the estate. Assets may be transferred to anyone who has paid a claim or to whom the exemption has been assigned.

IV. Probatable Assets Exceed Dispense Options But Insufficient to Pay All Liabilities - What Now?

i. Assess claims as they are presented.
Be aware of creditor's time limitations, KRS 396.011 (six months from appointment or two years from DOD if no appointment).

ii. Hold creditors to prescribed method of presentment. KRS 396.015 (Delivery or mail to personal representative or filing with court with certification of copy to personal representative/attorney). Must contain written statement of claim, indicate basis, name and address of claimant, amount claimed).

iii. Deny if untimely or good faith inquiry shows invalid claim. Always put claimant on notice of sixty day limitation to file suit upon claimant's receipt of denial. KRS 396.055 Request an affidavit from claimant if portions of claim are unclear or if you suspect offsets or credits are due.

V. Assets and Liabilities Determined - Estate is Insolvent. What Now?

A. DON'T PAY ANYTHING BEFORE SIX MONTHS FROM APPOINTMENT (unless you are convinced any and all claims on the same level of priority which exist or may surface won't exhaust assets). But be ready to pay on first day of seventh month following appointment.

B. KRS 396.095 the "insolvency statute" is fairly straightforward.

a) Administration and costs, expenses;

b) Funeral costs;

c) Debts and taxes with preference under state and federal law;

d) All other claims.

C. i. Obviously the insolvency statute doesn't tell you everything regarding priority. For example, where does the spousal exemption within KRS 391.030 fit in. OAG 83-478 states it is beneath the administrative expenses but takes priority over funeral costs.

ii. What about secured claims?

KRS 396.105 deals with this. The language of this statute is convoluted, the portion of the secured asset which is encumbered goes directly to that security holder before any other expense or debt would be paid as if that portion of the asset is not considered part of the probatable estate.

iii. Federal "priority statute" 31USC 3713 says federal law makes the personal representative personally liable for various federal claims regardless of whether a proof of claim is filed against the estate or not. It does not prioritize a federal claim above administrative nor funeral expenses, nor the spousal exemption. The most common federal claim is for unpaid income taxes of the decedent and/or the estate.

VI. Too Many Creditors Fighting, Filing Claims, Filing Suit, Etc. - Can you do a straight pro rata apportionment without exposure?

A. Mediation/Arbitration. Propose arbitration over mediation but get all creditors, heirs, legatees to agree.

B. Seek court approval of proposed settlement per KRS 395.615 (my favorite). Give certified notice of hearing

to all creditors, heirs, legatees, etc. At the hearing, if no exceptions are filed, the proposal shall be accepted and an order of distribution entered. Wait thirty (30) days

thereafter and distribute accordingly. If exceptions are filed, the Court can have a hearing, and accept, reject, or amend the proposed settlement.

C. Circuit Court action to settle per KRS 395.510. KRS 389A (fiduciary sale of real estate) has obviated the necessity to bring this action under most circumstances. This route is still used sometimes by rejected claimants, disgruntled heirs regarding probate of a Will, or when there was existing litigation prior to death on behalf of the decedent. This is an attractive option when there are complicated issues being litigated and you have limited resources with which to fight the various claimants. Basically you are dumping it in the Commissioner's lap and putting the onus on the creditors to prove their claims before the Commissioner.

VII. Miscellaneous

A. When liquidation of assets is necessary, auctioneers are the greatest.

B. Overpayment. KRS 396.165 holds that you may recover from any payee if you have made a mistake on solvency and overpaid one or more creditors, heirs, etc.

SPECIFIC EVIDENTIARY ISSUES IN ESTATE LITIGATION

Thomas W. Miller
Miller, Griffin & Marks, P.S.C.
Lexington, Kentucky

Copyright 2001, Thomas W. Miller

SECTION F

SPECIFIC EVIDENTIARY ISSUES IN ESTATE LITIGATION

I. CHALLENGES BASED ON A TESTATOR'S THOUGHT PROCESSES WHEN EXECUTING A WILL F-1

A. Did The Testator Have Testamentary Capacity? F-1

B. Was The Will A Product Of Undue Influence? F-1

C. Evidence To Consider F-3

D. Documents To Locate/Examine F-5

E. Expert Witnesses F-5

F. Who Can Opine About Mental Capacity/Undue Influence? F-5

G. Case Studies F-5

II. CONFIDENTIAL RELATIONSHIP / BREACH OF FIDUCIARY DUTY F-6

A. Legal Standard F-6

B. Evidence F-7

C. Case Study F-8

III. ESTATE ADMINISTRATION F-8

A. Issues That Can Arise F-8

1. Renunciation F-8
2. Possible Conflict of Interest F-8
3. Validity of Marriage F-8

B. Investigating Disputes Over Personal Property Ownership F-8

C. Investments F-9

D. Identification Of "Children" Born Out Of Wedlock F-9

E. Competing Wills F-9

F. Holographic Wills F-10

I. CHALLENGES BASED ON A TESTATOR'S THOUGHT PROCESSES WHEN EXECUTING A WILL

A. Did the Testator Have Testamentary Capacity?

1. Kentucky is committed to the doctrine of testatorial absolutism and the privilege of citizens to draft wills is zealously guarded by the Courts. The presumptions in favor of upholding wills are some of the strongest under Kentucky law and the contestants' burden of proof is high – only the "strongest showing of incapacity" or evidence which demonstrates incapacity "conclusively" is sufficient to set aside a Will. Bye v. Mattingly, Ky., 875 S.W. 2d 451, 455, 456 (1998); Fischer v. Heckerman, Ky., App., 772 S.W. 2d 642 (1989) (Contestant must overcome presumption of capacity by "substantial evidence"); New v. Creamer, Ky., 275 S.W. 2d 918 (1955) (burden is on contestant to establish incapacity by "substantial evidence").

2. Only minimal testamentary capacity is necessary to make a will. A testator must only (1) know the natural objects of his bounty, (2) understand his obligations to them, (3) know the character and value of his estate, and (4) be able to formulate a plan to dispose of his estate according to his own fixed purpose.

3. If a testator suffers from a mental condition that waxes and wanes, it is presumed that the testator was mentally fit when the will was executed under the "lucid interval doctrine." Bye at 455; see also Warnick v. Childers, Ky., 282 S.W. 2d 608 (1955) (evidence of prior incapacity is insufficient without evidence showing continuity of incapacity down to the time of execution).

B. Was the Will a Product of Undue Influence?

1. The Supreme Court of Kentucky in Bye, Supra, also addressed the issue of undue influence. The Court began with the broad and general definition that undue influence is "a level of persuasion which destroys the testator's free will and replaces it with the desires of the influencer." Id. at 457. The Court went on to establish that there are two elements to this inquiry. The Court held "in discerning whether influence on a given testator is "undue" courts must examine both (1) the nature and (2) the extent of the influence." Id.

2. In discussing the nature of the influence, the Supreme Court held that for influence to be "undue," it must be of a type which is inappropriate." Id. This decision echoes prior cases in Kentucky which emphasized the wrongful nature of "undue" influence.

3. In Combs v. Combs, Ky., 112 S.W. 2d 989, 992 (1938), Kentucky's highest court held that "mere general or reasonable influence over the [testator] is not sufficient to invalidate a Will; to have this effect, the influence must be undue; that is, not right or not proper." Id. (quoting Bailey, Adm'r, et al. v. Bailey, et al., 184 Ky. 455, 212 S.W. 595, 596 (1919)).

4. The Court has similarly held that "[u]ndue influence means a wrongful influence, and influence secured through affection and acts of kindness is not wrongful, therefore, not such as would justify a court of equity in setting aside a conveyance." Seals v. Seals, 213 Ky. 779, 281 S.W. 982, 984 (1926) (quoting Chrisman v. Quick, 174 Ky. 845, 193 S.W. 13 (1919)); see also Huff v. Woosley, 184 Ky 605, 212 S.W. 597 (1919) ("Mere general or reasonable influence over the testator is not sufficient of invalidate a will; to have this effect, the influence must be undue, this is, not right or nor proper"); Palmer v. Richardson, Ky. 223 S.W. 2d 745, 749 (1949) ("There must have been proof of [the exercise of undue influence] – evidence of activity or overt acts or incriminating statements of the person concerned or statements of the testator himself which tend to show that he had been wrongfully influenced or imposed upon to do what he would otherwise not have done in the exercise of free will." McEwen v. McEwen, 529 N.E. 2d 355 (Ind. App. 1988) (expert opinion on susceptibility to undue influence insufficient to create issue of fact as to whether undue influence was practiced).

5. Influence "from acts of kindness, appeals to feeling, or arguments addressed to the understanding of the testator are permissible" and that "undue" influence is influence "from threats, coercion and the like, " which is "improper and not permitted by the law. " Bye, at 457.

6. It is not sufficient to show that there was an opportunity to exercise undue influence, or that there was a possibility that it was exercised, but some evidence must be adduced showing that such influence was actually exercised. Nunn v. Williams, Ky., 254 S.W.2d 698, 700 (1953); Hurley v. Blankenship, Ky., 229 S.W.2d 963 (1950).

7. An influence which is obtained by modest persuasion and argument addressed to the understanding, or by mere appeals to the affection, cannot be properly termed undue influence in a legal sense. Stutilville's Ex'rs. v. Wheeler, Ky., 219 S.W. 411, 416 (1920).

8. Suggestions made by family members are not unduly influential where they are not unreasonable. Faulkes v. Brummett's Admin'r., Ky., 204 S.W.2d 493 (1947).

9. If the evidence merely raises a suspicion of fraud, question of undue influence or uncertainty of mental capacity, it is not sufficient to set aside a deed or other instrument. Young v. Mitchell, Ky., 194 S.W.2d 965 (1946).

10. The power or force imposed must be of such a nature as to destroy the free agency of the maker. Mayhew v. Mayhew, Ky., 329 S.W.2d 72 (1959).

11. In Kentucky, no presumption of undue influence arises from a bequest by a testator who has a confidential relationship with the beneficiary. Bye v. Mattingly, supra.

C. Evidence to Consider.

1. Mental and physical health.

   a. Determine diseases from which testator was suffering, history of injuries, current and former medication and history of hospitalizations.
   b. Obtain all medical records.
   c. Consult with treating physicians.
   d. Determine if testator was ever part of a study (i.e. Sanders Brown, etc.)
   e. Alcohol or substance abuse.
   f. Obtaining records by non-personal representative.

2. Determine relationship with family members.

   a. Time spent together on vacations, holidays and other occasions.
   b. Gifts exchanged.
   c. Cards and letters exchanged.

d. Any history of complaints, criminal or otherwise, against the other.

3. Determine testamentary intent outside of the will.

   a. What did the testator tell others?
   b. What can be gleaned from the letters written to others?
   c. What do prior wills show?

      i. Is the current will consistent?
      ii. Did an incident occur which changed the relationship between the testator and prior named beneficiaries?
      iii. Events that may create a reason to add new beneficiaries.

   d. Conversations with counsel that prepared the will.
   e. Elimination of Deadman's Statute.
   f. Attorney (deceased)-Client privilege.

4. What do persons who were frequently around the testator have to say about her mental capacity, relationship with family members and statements about beneficiaries?

   a. Caregivers/housekeepers.
   b. Neighbors.
   c. Persons with whom he has a business relationship.

5. Execution of the will.

   a. What was her appearance? (clean, clothing choice, etc.)
   b. How much time was spent with the testator by the witnesses and what did they discuss?
   c. Cognitive ability during the execution of the will.
   d. Was a video tape or audio tape made of the will execution?

6. Was an autopsy performed?

   a. Contact coroner.
   b. Provide to forensic psychiatrist.
   c. Coroner's inquest.

7. History of charitable giving if a large bequest to charity in a will is being challenged.

a. Relationship with charity.
b. Solicitations from charity.

8. Cause of death.

a. If suicide, why?
b. Video/photographs of death scene.

i. KRE 402 - Only relevant evidence is admissible.
ii. KRE 403 - Relevant evidence can be excluded if relevance is outweighed by the danger of undue influence.

D. Documents to locate/examine.

1. Physician records.
2. Hospitalization records.
3. Medication records.
4. All prior wills.
5. Income tax returns.
6. Gift tax returns.
7. Records of payments to employees.
8. Cancelled checks evidencing gifts to others.
9. Diaries.
10. Correspondence to and from relatives or parties included in or excluded from the will.
11. Study documents and the results.
12. Video tapes/audio tape made at the execution of the will.
13. Police reports.
14. Social Worker reports.
15. EMS reports.
16. Evidentiary issues on introducing records/reports/video and audio tapes.

E. Expert Witnesses.

1. Forensic Psychiatrists.
2. Social Workers.
3. Treating Physicians.
4. Home Health Care Providers.

F. Who can opine about mental capacity/undue influence?

G. Case Studies.

II. CONFIDENTIAL RELATIONSHIP/BREACH OF FIDUCIARY DUTY

A. Legal Standard.

1. If a person has superior knowledge about a fact and hides it and lies about it to another party, the proper lawsuit is for concealment or misrepresentation. The courts require (a) actual knowledge of facts, which (b) must be either (i) affirmatively concealed or (ii) undiscoverable. Creson v. Carmody, Ky., 222 S.W.2d 935 (1949); Bryant v. Troutman, Ky., 287 S.W.2d 918 (1956); Grant v. Wrona, Ky. App., 662 S.W.2d 227 (1983), Hall v. Carter, Ky., 324 S.W.2d 410 (1959).

2. A fiduciary relationship arises as a matter of law, and a confidential relationship is a matter of fact.

   a. A fiduciary relationship arises only in two situations: (1) where various, disparate duties have been consentually undertaken, as in a partnership, and (2) where the court appoints one individual in a position of superiority over the other. (Hence, the uncle guardian has a fiduciary relationship to his niece not by virtue of their family relationship but by virtue of his role as a court appointed guardian). Alagia, Day, Trautwein & Smith v. Broadbent, Ky., 882 S.W.2d 121 (1994); Walton v. Morgan Stanley & Co., Inc., 623 F. 2d 796 (2nd Cir 1980); Security Trust Co. v. Wilson, Ky., 210 S.W.2d 336 (1948); Steelvest, Inc. v. Scansteel Service Center, Ky., 807 S.W.2d 476 (1991).

   b. Confidential Relationships require proof of actual reliance placed by the Plaintiff on the Defendants' guidance. There must be subjective reliance and special confidence reposed. Caldwell v. Hatcher, Ky., 248 S.W.2d 892 (1952); Coleman v. Geer, Ky., 343 S.W.2d 584 (1961).

3. Superior Knowledge alone Does Not Establish a Fiduciary or Confidential Relationship. Bickel v. Louisville Trust Co., Ky., 197 S.W.2d 44 (1946).

4. After employing counsel to assert her adverse rights, one was henceforth dealing at arm's length with other party. Murphy v. Henry, Ky., 225, S.W.2d 662 (1950).

5. The existence of a confidential relationship is a matter of fact. Even where there are objective circumstances which evidence 'a spirit of great trust, confidence' in a family, the existence of such a spirit is merely 'a rebuttable presumption.' Saylor v. Saylor, Ky., 389 S.W.2d 904 (1965).

6. There must be sufficient evidence to support a finding that the defendant occupied a position of trust toward his sister. Savage v. Adams, Ky., 299 S.W.2d 597 (1956).

7. When a party alleging breach of confidential relations employs an attorney to assert her adverse rights, she is thenceforth dealing at arms length with the alleged breacher and his attorney. Murphy v. Henry, Ky., 225 S.W.2d 662 (1950).

B. Evidence.

1. If a family relationship.

   a. How did the parties get along?
   b. Did one of them handle the finances for the other or for the testator.
   c. Describe family gatherings (holidays, weddings, church, etc.)
   d. Were there gifts from the testator to one of the family members and, if so, who arranged for the preparation of the documents, execution of the documents, and delivery of documents.

2. If not a family relationship.

   a. Examine the relationship.
   b. Access to the testator.
   c. Confidence with which testator held accused party.

3. Documents to examine.

   a. Gift tax returns.
   b. Income tax returns.
   c. Payroll records.
   d. Canceled checks.
   e. Deeds.
   f. Family business/firm management.
   g. Writings (diaries, correspondence) of testator.

4. Parties' respective expertise/knowledge.

   a. Impact of retaining attorney.
   b. Financial experience.

5. Mental capacity of testator.

   a. Medical records.
   b. Disease/injury history.
   c. Medication use.

C. Case Study.

III. ESTATE ADMINISTRATION

A. Issues that Can Arise.

1. Renunciation.

   a. Who does the personal representative support?
   b. Ownership of personal property.
   c. Specific bequests under will to renouncing party.
   d. Timing of distribution of personal property.
   e. Form of renunciation and with whom filed.
   f. Estoppel from honoring renunciation.

2. Possible Conflict of Interest.

   a. Financial relationship with adverse party.
   b. Fees received directly or indirectly through investments and mutual funds.
   c. Adverse party serving as director.
   d. Compare management of this estate to previous estates.
   e. Determine events of self-dealing and multiple fees.

3. Validity of Marriage.

B. Investigating Disputes over Personal Property Ownership.

1. Checks/bills/receipts/credit cards for purchase property.
2. Identifying property brought into the marriage.

3. Previous divorce proceedings or estate tax returns if inherited.
4. Gifts during the marriage.
5. Have surviving spouse go through each item of personalty and identify the source.

C. Investments.

1. Comparison to similar type mutual funds/investment portfolios.
2. Is the mix of equities and income producing assets consistent with bank policy?
3. Examine communications from personal representative with:

   a. Beneficiaries.
   b. Adverse Claimants.

D. Identification of "Children" Born out of Wedlock.

1. If no adjudication as to parentage prior to father's death, claimant must prove paternity with clear and convincing evidence. KRS § 391.105.

2. Evidence can include:

   a. DNA Testing.
   b. Testimony from persons who would know to include the natural mother, other children and friends of the decedent.
   c. Establish the nature and duration of the relationship between the decedent and the natural mother.
   d. Birth Certificate.
   e. The relationship between the decedent and the proported child.
   f. Testimony from the alleged child.
   g. Statements made by the decedent.

E. Competing Wills.

1. The Court has jurisdiction to probate a will even where it is subject to objections. Mullins v. First American Bank, Ky. App. 781 S.W.2d 527 (1989).

2. The District Court has jurisdiction until a proceeding is filed in the Circuit Court. 1 J. Merritt, Probate Practice and Procedure §755 (2nd Ed. 1984).

3. Issues of undue influence, capacity and fraud can be litigated in the District Court, and evidence of same can be introduced. KRS 24A.120; OAG 79-81; Merritt at §755.

4. KRS 394.020 requires testator to be over eighteen, of sound mind and under no constraint or undue influence at the time of the execution. The will also must be signed by two witnesses who are in the presence of the Testator. KRS 394.040.

5. A self-proving will merely does away with the obligation of having one of the witnesses appear in court to testify they were present at the execution of the will. KRS 394.255.

6. A lost will can be probated if its contents can be proven and testimony can be introduced it was validly executed and that it had not been revoked. Rowland v. Holt, Ky., 70 S.W.2d 5 (1934); Caudill v. Loar, 168 S.W.2d 757 (1943).

7. Case study of competing wills.

F. Holographic Wills.

VALUATION
Common Battleground Issues & Case Scenarios

Scott D. Hakala, Ph.D., C.F.A.
Principal
Business Valuation Services
Dallas, Texas

Copyright 2001, Scott D. Hakala

SECTION G

VALUATION: COMMON BATTLEGROUND ISSUES AND CASE SCENARIOS

Minimizing Damages In Estate Litigation

INTRODUCTION **G-1**

1. Claims of Breach of Fiduciary Duty and Related Claims G-1
2. Malpractice and Claims Relating to Professional Services G-2

GENERAL BACKGROUND **G-2**

BREACH OF FIDUCIARY DUTY AND MINORITY SHAREHOLDER OPPRESSION CLAIMS **G-3**

1. Theft or usurpation of business opportunities G-3
2. Shareholder oppression claims G-5
3. Fraud in the inducement claims G-9

EXAMPLES OF CASES **G-12**

Case No. 1 ..... G-13
Case No. 2 ..... G-18

Valuation: Common Battleground Issues and Case Scenarios (Minimizing Damages in Estate Litigation)

The theme for this topic arose from a series of situations where our firm was involved as an expert in litigation involving estates. The areas of litigation include:

1. Claims of Breach of Fiduciary Duty and Related Claims

This area covers a lot of different situations that arose as a result of:

(a) Family dissension;

(b) Lack of proper advice or guidance to the executor of the estate or designated controlling person in executing an estate plan;

(c) Failure on the part of the controlling persons to exercise their duties in a prudent and appropriate manner;

(d) Misappropriate or usurpation of business opportunities;

(e) Failure to disclose material information and/or pay a fair price in a purchase of interests from a minority interest holder;

(f) Self-dealing; and

(g) Failure on the part of the controlling person to respect the rights of minority or non-controlling persons (shareholder oppression).

2. Malpractice and Claims Relating to Professional Services

This is a significant and growing problem for attorneys and other professionals advising families, establishing estate plans or advising entities arising out of estate planning. Typical causes of action relate to:

(a) Defective estate planning results in unforeseen or excessive tax liabilities;

(b) Excessive fees;

(c) Aiding and abetting in a breach of fiduciary duty; and

(d) Defective estate planning or legal services results in unforeseen liabilities on the part of estate or controlling person.

General Background

A substantial and increasing portion of my firm's litigation support practice involves analyzing damages in cases of professional malpractice, breach of fiduciary, and defective fairness opinions. Some of the experiences that will be discussed during this session will outline our experiences as experts and the advice that we provide to attempt to reduce or prevent liability and damages to our clients.

Breach of Fiduciary Duty and Minority Shareholder Oppression Claims

One common theme throughout my experiences is the inherent tension between the controlling person's or insider's self interest and the interests of the other beneficiaries of the estate or minority shareholders (including minority or limited partners in a partnership). Often controlling persons are not properly and adequately advised of their rights and responsibilities as fiduciaries. The types of alleged abuses I have observed include:

1. *Theft or usurpation of business opportunities* – This is a surprisingly common claim. For example, a family limited partnership operates oil and gas interests. The general partner identifies additional oil and gas leases and interests that are for sale by a neighbor seeking to avoid bankruptcy. The general partner buys these interests at a discount to their fair value through his own company and does not use the funds of the partnership to acquire these interests. A limited partner brings suit claiming usurpation of corporate opportunities and claims as damages the benefit of the bargain. Similar claims against the controlling or managing fiduciary can arise with entities involved in agriculture, ranching, operating franchise stores, health care services, and managing real estate for rent income.

Often the managing fiduciary is appointed to manage the entity precisely because of prior and separate experience in the relevant business of the entity. It is not surprising, then, that the fiduciary might consider certain opportunities to be separate

from the entity and seek to develop them outside of the entity he is actively managing for the benefit of other parties.

A fiduciary of a partnership or corporation has a general obligation or duty to share any opportunities that may arise with the entity and develop. Controlling persons have a tendency to view opportunities in a narrow sense and ignore the language that might be contained in a partnership agreement or corporate charter. Much of the law in this area was developed in the context of Delaware law. But the legal concepts are generally universal. Under Delaware law (*Guth v. Loft, Inc,* 5 A.2d 503, Del. 1939), in order to find a usurpation of corporate opportunities: (1) the corporation must be financially able to undertake the opportunity; (2) the opportunity must be in the corporation's line of business; (3) the opportunity must be of practical advantage to the corporation; and (4) the opportunity must be one in which the corporation has an interest. Three Delaware cases decided in the mid 1990s include *Broz v. CellularInfo. Sys., Inc.* (673 A.2d 148, Del. 1996), *Thorpe v. CERBCO, Inc.* (No. 345, 1995, Del. April 10, 1996), and *Yiannatsis v. Stephanis* (653 A.2d 275, Del. 1995).

Proactive measures, to avoid claims brought by disaffected family members, one might more narrowly define the scope of the opportunities that the partnership or corporation is entitled to pursue, provide specific provisions for the general partner to separately pursue opportunities defined as outside the narrow scope of the entity being managed, or limit the ability of the entity to actively acquire and pursue opportunities after a specified date in time (such as after the death of the donor and original general partner). Additionally, the fiduciary may obtain consents from a

majority of the equity interest holders or advice from counsel as to the appropriateness of his actions.

2. *Shareholder oppression claims* – These claims are becoming increasingly common. They typically relate to claims of denial or underpayment of dividends, excessive compensation paid to managing or controlling parties, non-arm's length transactions and self-dealing, wrongful termination, and improper management (failure to realize the level of income to the interest holders).

An interesting article on the issue specific to Texas is Moll, "Majority Rule Isn't What It Used to Be: Shareholder Oppression in Texas Close Corporations," *Texas Bar Journal*, May 2000, pp. 434-441. Two specific cases on my resume are *George J. Cortes, Individually and Derivatively on Behalf of MCS/Texas Direct, Inc., v. John W. Windle, Jr., MCS/Texas Direct, Inc. and Alon R. Stephens, v. George J. Cortes, Individually ([Cause No. 352-168681-97]* District Court of Tarrant County, Texas, 352nd Judicial District), tried in 1999 and decided in 2000; and *Tom Limroth and Jean Limroth vs. Scott Killpack, Latrese Killpack, Plastic Magic, Inc., and Killpack & Limroth Plastics, Inc. d/b/a/ Superior Plastics (]Cause No. 352-171839-97]* District Court of Tarrant County, Texas, 352nd Judicial District), hearing in December 1998.

Often these cases arise when an individual becomes disaffected with the majority of the interest holders in a closely held corporation or partnership. The controlling or managing shareholder then uses his power to withhold the payment of dividends and distributions, deny the disaffected person access to the books and records, construct a series of non-arm's length transactions and compensation so as to eliminate

the income of the entity, and deny income to the minority shareholder and/or remove (terminate) the disaffected person from any position of employment, management, or directorship. The withholding of dividends and distributions may be deemed particularly oppressive in pass-through entities, such as partnerships, limited liability corporations and S corporations, because the individual must pay taxes on his share of the income reported by the entity without receiving the funds required to pay the taxes. Courts may additionally find that, despite at will agreements, the denial of employment or compensation denies the minority shareholder a fair and proportionate share of the income of the entity and, therefore, constitutes a form of shareholder oppression to a minority shareholder.

While actions brought against a corporation or partnership by a minority interest holder are typically derivative claims, often (at least in Texas) courts will consider the majority shareholders as having fiduciary duties directly to the minority shareholders and allow for damages to be awarded directly to the damaged individuals. Actions taken by the controlling party or parties may and usually are held to a greater level of legal scrutiny. Oppressed shareholders may be entitled to damages for any loss of value or waste of corporate assets resulting from improper actions, distributions and dividends, and/or (increasingly common) payment for the fair market value or fair value of their respective equity interests. Fair value can be a particularly costly finding in such cases. Fair value may be interpreted as the pro rata share to the value of the underlying assets of the entity and may not include the typical discounts for lack of control and discounts for lack of marketability because the oppression is such that the minority shareholder is entitled to be bought out in a liquidity event and the controlling persons

should not be able to benefit from the buyout. Additionally, shareholder oppression may invalidate buy-sell agreements that might otherwise limit the buyout price to be paid to the minority shareholder. (See the *Windle, et al, v. Cortes* case previously mentioned.)

The tendency for these disputes to become personal and nasty further compounds the problems for the advisor. The person in control is apt to want to "crush" or damage the disaffected person's interest and to so oppress the minority shareholder as to render that person incapable of bringing suit or to force the oppressed shareholder to accept a buyout at a distressed price. This can backfire and compound the liability of the controlling parties. It is essential, therefore, that the advice given be strong, proactive and timely, and that the controlling person be promptly and properly warned as to his/her liability risks. On a number of occasions I have observed, counsel for the controlling person gave the controlling person(s) very bad advice (mostly likely because it was the advice the person wanted to hear) and the counsel ended up being sued for giving improper advice to the entity and the controlling person(s). Thus, attorneys must ensure that they do not become so entangled in these disputes that they become liable for their actions.

Two notable cases on my resume are *James Masters, et al. vs. Hopkins & Sutter et al.* (*[No. 17-143836-92]*; 17th Judicial District, Tarrant County, Texas) tried and settled in 1995; and *Douglas W. Fugate, S. Mark Rippley, James Masters, and Cable Advertising Networks vs. Mark Weisbart; Michael Curran; Akin, Gump, Strauss; Hauer & Feld, L.L.P.; Jonathan V. Leaver; and Cable Advertising Concepts.* (*[No. 17-158151-95]* 17th Judicial District, Tarrant County, Texas) tried and settled in 1997. In the first case, the allegations were that counsel aided and abetted a breach of fiduciary duty, simultaneously

represented multiple individuals that had clear conflicts of interest, committed legal malpractice that resulted in the destruction of a business, and actively assisted in the oppression of the minority shareholders/plaintiffs. In the second case, the plaintiffs alleged that the attorneys acted on behalf of the controlling person to the detriment of the corporation the attorneys claimed to represent, used improper legal claims to deny the plaintiffs the value of their business interests and their rights as shareholders, and misrepresented facts to a court of law. In both cases, the controlling shareholders fled the country or were no longer subject to claims (in the witness protection program) and the attorneys were required to make the plaintiffs whole.

In another case, corporate counsel represented both the defendant officers and directors and the corporation in a derivative shareholder lawsuit involving numerous claims of breach of fiduciary duty, excessive compensation, and self-dealing. The failure on the part of the corporation and the directors to obtain fairness opinions to support a series related party transactions placed the burden of proof on the defendants. The use of corporate funds to defend the defendants in a derivative claim for breach of fiduciary duty was deemed to be improper and counsel was ordered to repay approximately $1 million in legal fees to the corporation.

One of the most important elements in defense in these cases is to obtain credible, independent analyses that support the decisions made by the controlling parties. For example, in the case of *Tom Limroth and Jean Limroth vs. Scott Killpack, et al.,* my testimony on the fairness of affiliated party transactions, the reasonableness of compensation, the adequacy of returns to minority shareholders, and good advice by the attorney representing the defendants allowed the defendants to prevail in a preliminary

hearing and settle the case on very favorable terms. [1] In second example case discussed below, the defendant avoided a finding of breach of fiduciary at trial and achieved a hung jury by obtaining contemporaneous and subsequent expert opinions on the fairness of restructuring transactions and his compensation.

3. *Fraud in the Inducement Claims* – In family disputes involving family partnerships and corporations, it is common for a disaffected minority shareholder to demand and agree to have his/her interest purchased as a settlement of the dispute. Often subsequent events may come to light that suggest that the buyout price paid to the minority shareholder was not fair and/or that the controlling parties did not properly or adequately disclose material information to the minority shareholder during the buyout transaction. The law in this area follows much of the Delaware law on going-private transactions and management buyouts of public companies. Most states have specific provisions requiring a controlling party in a transaction involving securities to fully disclose all material information to minority shareholders.

A case on my resume relating to this duty is *Joe Long, et al. v. Wells Fargo & Company, et al.* (U.S. District Court for the Western District of Texas, Austin Division [Civil Action No. A:98CA751-SS]), settled during trial in 1999. In that case, the seller issued securities to the plaintiff without disclosing material information in the defendant's possession at the time of the transaction. When the material information was disclosed, the plaintiff experienced a loss of approximately 10% of the value of his investment.

---

[1] One reason the court adopted my approach was my testimony on similar issues in U.S. Tax Court and the court's acceptance of my method of analysis. One of my U.S. Tax Court cases addressing issues of reasonable compensation is *Normandie Metal Fabricators, Inc. v. Commissioner of Internal Revenue,* TCM 2000-102, affirmed recently by the Second Circuit. The court, in this decision, outlined the standards for determining reasonable compensation.

I have also been engaged in a variety of smaller, closely held cases. The common situation in these cases is that a minority shareholder demands to have his/her interest in a closely held entity acquired by a controlling or informed party (an insider). Subsequent to the buyout transaction, the entity is sold or engages in a transaction where the value realized by the remaining interest holders in the entity is substantially greater than the amount paid in the buyout. The minority shareholder discovers this information and then brings suit claiming a failure to disclose material information and breach of fiduciary duty. On two occasions, my testimony was that the transaction was fair taking into consideration the fact that the entity was not for sale at the time of the buyout transaction, that the sale of the business or assets was not foreseeable at the time of the buyout transaction, that the minority shareholder demanded and initiated that buy out (which can be important in determining the appropriateness of discounts for lack of control and lack of marketability in the fairness of the transaction) and that the assets of the entity had appreciated considerably or had appreciated more than would have been reasonably foreseeable at the time of the buyout.

In instances where controlling persons or insiders are involved in the buyout of minority shareholders or outsiders, the duties of the controlling persons may require that they pay full value or maximize the value to the outside shareholders. Delaware courts often employ enhanced judicial scrutiny and require entire fairness in evaluating whether the fiduciary was to the corporation and outside shareholders. However, if the transaction is approved by the disinterested shareholders in a vote with adequate disclosure, the burden of proof on fairness may shift to the plaintiff in these cases. (*Weinberger v. UOP*, 457 A.2d 701,710, Del. Super. Ct., 1976; *Michelson v. Duncan*, 407 A.2d 211, 224, Del. Super. Ct.,

1979; *Rosenblat v. Getty Oil Co.,* 493 A.2d 929, 937, Del. 1985). This shift of the burden of proof requires adequate disclosure. A defendant in an engagement I worked on last year (involving the management buyout of Castle & Cooke) specifically disclosed my opinion and another expert's opinion in the proxy as to the value of the company and the unfairness of the transaction. By disclosing everything (practically admitting the deal was unfair and that the minority shareholders should accept the unfair price because of the inability to realize control value due to the actions of the controlling shareholder), the defendant sought to preserve the presumption and gain shareholder approval.

Thus, minimization of the legal risks in transactions where the minority shareholder interests are acquired by insiders or controlling persons includes ensuring that full and adequate disclosure is provided at or immediately prior to the transaction, and obtaining appropriate independent valuation or fairness opinions justifying the transaction price. Valuation and fairness opinions are only of assistance to the defense in these cases when the analyses are performed in compliance with applicable standards (Uniform Standards of Professional Appraisal Practice or USPAP, Business Valuation Standards of the American Society of Appraisers or Standards of Professional Practice of the Association for Investment Management and Research). Many, if not most, investment banking firms routinely (and as a matter of policy) violate these professional standards. They routinely fail to maintain sufficient documentation of their procedures and analyses to demonstrate a "reasonable and adequate basis" for their opinions and/or fail to fully and completely analyze all relevant and material information and to properly evaluate and weight the various valuation methods considered in their analyses. In such instances, the investment

bankers not only fail to provide a presumption to the directors they were engaged on behalf of but become liable, themselves, for their own improper actions.[2]

Examples of Cases

I have increasingly become proactive in advising clients of their duties and risks during estate planning. A donor establishes a gifting vehicle (such as a family limited partnership) and gifts interests in that vehicle to various beneficiaries. Since the donor retains control, a variety of situations can arise (some unseen, many foreseeable) that will result in a loss of the discounts intended to reduce gift and estate taxes, family dissension, unnecessary legal and professional expenses, and further liability. As the assets in the estate increase, the potential for conflicts will increase disproportionately.

Often the donors will seek to limit or designate the individual and individual(s) that will be in control of the entities created to operate or manage the estate's assets. Heirs that are denied control of the assets of the estate (for example, given non-voting interests in the corporate entities and limited partnership interests in the partnership entities) may become dissatisfied with the arrangements due to excessive compensation realized explicitly or implicitly by the controlling person(s), due to a failure to realize their pro rata value of the assets of the estate in a sale or liquidation, or due to an inadequate yield or return from the assets of the estate. Prior grievances (possibly kept hidden) often compound the situation.

---

[2] I have two current engagements where the investment bankers are potentially liable for aiding and abetting breaches of fiduciary duty and/or for destroying their work files. The knowing destruction of working

Case No. 1 (facts altered)

Family X had a substantial amount of wealth in the form of undeveloped real estate. The real estate market was at its peak at the time the grandfather, father, and mother passed away. As a result of the short period of time between the deaths of two generations of the estate, the estate taxes were substantial. Additionally, between the respective dates of death and the filing of the estate tax returns, the real estate market collapsed such that the value of the real estate for estate tax purposes greatly exceeded the value of the real estate. Through effective estate planning (creation of limited partnership interests and gifting at the last minute), the estate tax obligations were reduced sufficiently to allow for the estate to borrow just enough funds to pay the taxes.

There were four children (one son and three daughters) and two other family members that were beneficiaries of the estate. The son had been actively involved in managing the family business and property interests and carried the family name. The other beneficiaries of the estate were adults, married, and not actively involved in the family businesses. Thus, the desire of the donors was that the son be designated as the succeeding general partner and control and manage the family properties on behalf of the estate. The daughters and the two other beneficiaries were made limited partners in the family partnership and were provided with limited partnership interests.

The Internal Revenue Service immediately challenged the discounts claimed by the estate in a series of notices of deficiency. This resulted in a series of Tax Court cases and appeals in which the estate ultimately succeeding in sustaining most, but not all, of

---

files, notes, and analyses tends to shift presumption to the plaintiff and increase the burdens on the defendants to prove overall fairness.

the discounts off of underlying values originally claimed on the estate and gift tax returns. The final resolution of all estate tax issues was not realized until more than ten years after the filing of estate taxes.

Unfortunately, there was a history of resentment by two of the daughters toward the son. Additionally, the beneficiaries of the estate believed the estate to have substantial value and did not appreciate the extent of the estate tax obligations, the legal expenses and liabilities associated with the notices of deficiency, the amount of debt assumed by the estate to pay the estate tax obligations, the loss in the value of the real estate as a result of market conditions and the inability of the property to produce adequate cash flows after debt service. Thus, the daughters demanded an immediate liquidation of the assets of the partnership.

If the estate was liquidated immediately, the values that would have been realized by the beneficiaries would have been minimal relative to the potential value of the estate should the real estate market recover. The estate would have been deprived the necessary resources to fight the notices of deficiency and potentially would have been rendered insolvent if the Internal Revenue Service ultimately prevailed. The general partner sought to maintain the integrity of the family assets and intended to wait until the real estate market recovered and the estate tax issues were resolved before disposing of the underlying properties and liquidating the partnership.

The daughters eventually brought suit against the general partner for breach of fiduciary duty alleging, among other things, a failure on the part of the general partner to liquidate assets in a timely manner, excessive direct and indirect compensation paid to the

general partner, and mismanagement. The daughters requested that their respective limited partnership interests be liquidated at fair value with fair value being the undiscounted value of their pro rata shares of the underlying assets in the partnership.

Three mistakes were made in defending the son in the subject case. First, the attorney defending the son did not engage qualified experts on valuation, taxation, and fiduciary issues. Competent valuation testimony would have established that the partnership was potentially insolvent given the notices of deficiency and expected expenses required to fight the notices. Valuation testimony could have also shown that the compensation realized by the son was not excessive or unreasonable for managing a real estate partnership with the number and type of assets owned by the partnership. Legal and taxation experts should have established the risks and the expenses associated with the notices of deficiency. Second, the son had not obtained contemporaneous expert opinions supporting his decisions. It was reasonably foreseeable that the daughters might question his decisions in litigation. Given the size of the partnership, the son could have easily obtained advisory opinions as to reasonable compensation and valuation that would have provided some protection to him and to the estate in litigation. Third, the case was not well argued. An experienced litigator should have been engaged to argue the case. The son was a tough negotiator and tended to be too strong in his opinions; he was not a sympathetic character and was not necessarily likeable. Therefore, it would have been advisable to prepare the son for trial and to use experts to present evidence and testimony of the difficulties and to explain the issues in a clear and convincing manner to the jury.

This series of mistakes meant that the daughters prevailed in their claims against the son as the general partner. The daughters' experts and claims led the jury to award substantially greater damages than any reasonable calculation of pro rata value could support. The son was forced to settle and make a series of payments to the daughters well in excess of the fair market values of the their respective interests and well in excess of their pro rata share of the partnership in liquidation. The partnership, after payments to the daughters, was nearly insolvent. The only two things that saved the partnership were the turnaround in the real estate markets and a couple of favorable decisions (on appeal) that ultimately reduced the estate tax liabilities.

The attorney representing the son was sued for legal malpractice and ended up having his reputation tarnished and having to pay a sizeable settlement.

The lessons from this (modified) case are as follows:

1. The donors should have established the partnership earlier and made modest gifts at regular intervals during their lifetimes. The last minute estate planning meant that the Internal Revenue Service had stronger arguments and a better chance to unwind the partnership and ignore the discounts.

2. The donors and advisors should have communicated on a regular and consistent basis with the beneficiaries to explain the problems and issues they were attempting to address and the real risks of estate tax deficiencies. Without a full understanding of the issues, the daughters had

unrealistic expectations as to their respective inheritances and, given their personal situations and preferences, were more interested in realizing some consideration immediately than having the patience to wait for a substantially greater amount of value later. A substantial portion of ill will was created when the daughters realized that they were given less than the son and had no control in the distribution or liquidation of the estate.

3. A strong controlling party requires strong advisors. Sometimes, one has to be willing to give advice that is not fully appreciated and risk the loss of the client. The son should have been given advice by counsel to moderate his compensation and related party transactions with the partnership he controlled as the general partner. The son was not counseled to have a realistic appraisal of the risks he faced from litigation brought by the daughters and underestimated the threat of a judgment. Like many strong-willed persons from families of wealth, his management choices often had the appearance of self-interest and he sought to realize compensation from the partnership that, while within the range of compensation observed in the market, was greater than prudence and caution would have advised. The amount of compensation he realized undercut his contentions as to the relatively tenuous state of the partnership's financial situation. The result was an inadequately prepared and presented defense and a substantial liability that almost rendered the son bankrupt and almost wiped out the estate.

4. Advisors and attorneys need to realistically assess their skills, their risks, and advise their clients accordingly. (Our firm has an internal policy of screening and reviewing engagements and requires that our staff be willing to walk away from possible engagements or fees if we feel compromised, uncomfortable, or sense substantial risk.) This may mean admitting to the client the need for outside counsel and assistance in defending the client, convincing the client of the need for greater expenditures (for discovery, on experts and on advisors) to prepare the defense to avoid and reduce liability, and ensuring and documenting that the client has been fully apprised of his risks.

5. A realistic posture would have facilitated a realistic and reasonable settlement at a substantial discount to fair value and closer to fair market value for the limited partnership interests.

Case No. 2

Person X was engaged in a number of risky ventures in the late 1960s and early 1970s and was concerned about his personal liability to creditors. He transferred substantial assets to a trust in the name of four daughters (two by his first marriage and two by his second marriage) designating himself as the trustee. As trustee, he used the assets of the trust to engage in a series of highly speculative, highly leveraged transactions. As a result of luck and his skill the value of the assets in the trust increased substantially. Eventually, the trust acquired control of corporations (of which he was

named Chairman of the Board, an officer or director) and substantial other investments. By virtue of his status as trustee and the nature of the original gifts, only half of the value of the trust was deemed to have been gifted to the daughters and not subject to future gift and estate tax liabilities.

By the early 1990s, the daughters were adults and had their own lives. The dividends and distributions from the trust to the daughters were substantial by ordinary standards but represented a miniscule yield of approximately .2% of the value of the assets owned by the trust. The father remarried and allegedly used the assets of the trust to support his residences, purchase jewelry and personal items, make political and other contributions to causes he favored (but not favored by his daughters), to gain control of corporations, and to pay himself substantial direct compensation from the trust for acting as trustee and substantial indirect compensation by receiving compensation from each of the corporations he controlled through the trust's assets.

The father allegedly sought to carve out a portion of the assets of the trust (that he was deemed to not have gifted for tax purposes) regain outright ownership that portion of the trust assets. He also engaged in a restructuring transaction whereby he issued fixed income (preferred) equity securities to the half of the trust deemed to be gifted to the daughters in return for common equity rights to the half of the trust he was stilled deemed to own and control. The fixed income securities paid a yield but denied the daughters some of the benefits of the future appreciation of the trust.

Two of the daughters (one from each of the first two wives) resented their father's/trustee's control and minimal distributions. They filed suit alleging

mismanagement, excessive compensation, and breach of fiduciary on the part of their father in managing the trust. They demanded that their respective portions of the trust be transferred to separate trusts or entities and placed under the control of independent trustees.

The daughters engaged experts to show that the restructuring transactions resulted in less than fair consideration to the half of the trust they were deemed to own, to opine on breaches of fiduciary duties, to opine on damages, and to advise the trust as to how to minimize estate and gift taxes on the distribution of the half of the trust deemed to be still subject to gift and estate taxes.

The trustee fought back by establishing that his daughters benefited from his investment activities. He further engaged experts to show that, while his compensation was extreme by ordinary standards, his compensation represented a very small percentage of the excess value (the value in excess of equivalent market returns) he created within the trust over the years. He had also engaged a recognized investment bank to perform a fairness opinion on the restructuring transaction.

While the experts engaged by the trustee made a number of statements and reached a number of conclusions that were of questionable validity, they established a presumption in favor of the trustee. In a jury trial, the ultimate outcome was not likely to be decided by a careful application of the facts to the law, but, rather, based on an overall sense of fairness. The jury could not reach a decision on the ultimate issues. Some jurors felt that the daughters were made wealthy by the father and should be grateful for whatever they received. They further found that there was enough evidence of overall

fairness (no matter how weak the evidence was in my opinion) to overcome the daughters' allegations. Other jurors felt strongly that the father had abused his control of the trust to the detriment of the interests of the daughters (especially since the father had originally used the trust to hide or protect assets from potential creditors).

In the end, a settlement was reached whereby the two daughters that brought suit were issued substantial assets carved out from the trust. These assets were then to be independently managed for their individual benefit. The assets they received from the trust were far less (10% of the trust assets each) than they theoretically were entitled to receive from the trust (25% each). However, the future annual cash yields and distributions to the two daughters were projected to be five to ten times the annual dividends and distributions the daughters had historically received from the trust. Thus, even though the two daughters received only 40% of their pro rata rights in the trust, they ended up with substantially greater intrinsic value than they had previously received.

The lessons from this case were as follows:

1. Fairness opinions and expert opinions, even if flawed, provide some level of protection against liability and damage claims.

2. Cases brought against donors for breach of fiduciary are difficult to win. This is because the plaintiffs are viewed as ungrateful and spoiled.