Commonwealth Of Kentucky
Supreme Court Of Kentucky
2011-SC-277-DG

TAX EASE LIEN INVESTMENTS 1, LLC, APPELLANT

On Appeal From Court Of Appeals, No. 2010-CA-00595-MR
v. **And Shelby Circuit Court, No. 09-CI-00823**

COMMONWEALTH BANK & TRUST COMPANY
and
TERETHA M. MURPHY, APPELLEES

Brief Of Appellee, Commonwealth Bank & Trust Company

M. Thurman Senn
MORGAN & POTTINGER, P.S.C.
601 West Main Street
Louisville, Kentucky 40202
Phone: (502) 589-2780
Fax: (502) 585-3498
Email: mts@morganandpottinger.com
Co-Counsel for Appellee, Commonwealth Bank & Trust Company

Donald T. Prather
MATHIS, RIGGS & PRATHER, P.S.C.
500 Main Street, Suite 5
Shelbyville, Kentucky 40065
Phone: (502) 633-5220
Fax: (502) 633-0667
Email: dprather@iglou.com
Co-Counsel for Appellee, Commonwealth Bank & Trust Company

Certificate of Service

I hereby certify that a true copy of this Brief Of Appellee, Commonwealth Bank & Trust Company, was served by first-class mail, postage prepaid, this 18th day of May, 2012, on the following: (1) **Hon. Charles R. Hickman**, Judge, Shelby Circuit Court, 501 W. Main Street, Suite 15, Shelbyville, KY 40065; (2) **Samuel Givens, Jr.,** Clerk, Kentucky Court of Appeals, 360 Democrat Drive, Frankfort, KY 40601; (3) **Teretha M. Murphy k/n/a Teretha M. Beckley**, 925 College Street, Shelbyville, KY 40065; and (4) **R. Eric Craig and P. Blaine Grant,** Hayden, Craig & Grant, PLLC, 718 W. Main Street, Suite 202, Louisville, KY 40202, Counsel for Appellant.

M. Thurman Senn, Co-Counsel For Appellee

Statement Concerning Oral Argument

This case involves the extent to which a mortgage lienholder in a real property foreclosure lawsuit is entitled to notice and opportunity to be heard before a Circuit Court enters an agreed judgment adjudicating the existence and amount of a competing party's lien on the subject real property. It also involves the extent to which a Circuit Court should review the reasonableness of an award of attorney's fees and other fees where an objection to the award is made. It also involves the extent to which the judicial system will supervise the authority of a tax bill purchaser to add $2,541.67 in additional fees to ad valorem tax bills which were purchased for a total of $1,436.10, particularly when none of those fees will be received by the taxing authorities.

Appellant, Tax Ease Lien Investments I, LLC, believes that there is no need for judicial supervision of the extent to which its attorneys can "persuade" an individual property owner who is not represented by counsel to agree to a judgment which adds thousands of dollars of fees and costs to its claim and adjudicates those sums as a valid lien on her home.

Appellee, Commonwealth Bank & Trust Company, disagrees and believes that oral argument on these important issues is both appropriate and desirable.

Counterstatement of Points and Authorities

Counterstatement Of The Case

This case involves fundamental issues of due process and the appropriate judicial review of awards of attorneys' fees and litigation expenses. The case does not arise out of a private transaction. It arises from the sale by the government of its ad valorem taxing power to a private, for profit, business. Because of that sale, Appellant, Tax Ease Lien Investments 1, LLC ("Tax Ease"), claims a lien for unpaid 2006 and 2007 ad valorem taxes against the home of Appellee, Teretha M. Murphy ("Ms. Murphy"), which she had previously mortgaged in 2004 to Appellee, Commonwealth Bank & Trust Company ("Commonwealth Bank").

In a 2-1 decision, the Court of Appeals held that Commonwealth Bank was entitled to notice and an opportunity to be heard before the Circuit Court entered an "Agreed Judgment" which (i) was not reviewed or approved by Commonwealth Bank, (ii) was signed by Ms. Murphy without benefit of counsel, (iii) was presented to the Circuit Court by Tax Ease without any actual or attempted notice to Commonwealth Bank, and (iv) which adjudged that Tax Ease had a lien against the subject property and that this lien included an additional $2,541.67 in attorney's fees and litigation expenses beyond the $1,436.10 that Tax Ease paid to purchase the underlying tax bills.

1. Tax Ease Files A Lien Foreclosure Lawsuit To Collect The Unpaid 2006 And 2007 Ad Valorem Real Estate Taxes It Purchased And Joins Commonwealth Bank As A Mortgagee Lienholder.

This case began on October 30, 2009, when Tax Ease filed a "Complaint" in Shelby Circuit Court against Ms. Murphy, Commonwealth Bank, and Perry & Sickmeiers, Inc. ("P&SI") seeking a monetary judgment against Ms. Murphy for unpaid ad valorem real estate taxes for 2006 and 2007 plus additional fees and costs that Tax Ease had added to the

tax bills. See "Complaint", Record On Appeal at pp. 1-7 (hereinafter "R.A."). The ad valorem taxes were imposed against Ms. Murphy's home at 925 College Street, Shelbyville, Kentucky. See Complaint ¶2-¶3.

Commonwealth Bank was joined as a Defendant because Tax Ease sought more than a monetary judgment against Ms. Murphy. Tax Ease also sought "[t]hat it be adjudged to have a lien on the real property described herein and that this Lien be adjudged prior and superior to all other Liens set forth herein." See Complaint, Prayer for Relief ¶(b) [R.A. p. 4]. Tax Ease also sought that "the Master Commissioner of this Court sell the real property described herein" and that the proceeds of sale "be applied in accordance with the priority rights of the parties herein." Id. at Prayer for Relief ¶(d) and ¶(e) [R.A. p. 4].

Seeking this relief, Tax Ease was required by KRS 426.006 to "state in his petition the liens held thereon by others, making them defendants." Tax Ease did so in Paragraph 8 of its Complaint in which it acknowledged that "Defendant, Commonwealth Bank & Trust Company, may be claiming an interest in the above-described real property by virtue of that certain Mortgage dated April 1, 2004, recorded in Book M587, Page 491, in the Office of the Shelby County Clerk." See Complaint ¶8 [R.A. p. 3]. This date was almost exactly three years before the date when Tax Ease purchased the 2006 unpaid ad valorem tax bill. See Complaint ¶4(A) (alleging purchase date of April 16, 2007) [R.A. p. 2]. Tax Ease alleged it purchased the 2007 unpaid ad valorem tax bill on April 22, 2008. See Complaint ¶4(B) [R.A. p. 2].[1]

Commonwealth Bank properly filed its Answer And Crossclaim on November 13, 2009, asserting its mortgage lien interest in Ms. Murphy's home. See R.A. pp. 14-26.

---

[1]Tax Ease also named as a Defendant, Perry & Sickmeier, Inc., alleging that it purchased an unpaid 2008 ad valorem tax bill. See Complaint ¶9 [R.A. p. 4].

2. Tax Ease Persuades Ms. Murphy To Sign An Agreed Judgment Adjudicating It To Have A Lien And Setting Out The Lien Amounts And Files The Agreed Judgment With The Circuit Court Without Notice To Commonwealth Bank.

The next activity in the case that Commonwealth Bank was aware of occurred on December 28, 2009, when counsel for Commonwealth Bank received in the mail an "Agreed Judgment" which had been entered by the Shelby Circuit Court on December 23, 2009, and mailed by the Court's clerk that same day. See Agreed Judgment [R.A. pp. 28-31]. See also Record on Appeal Index (captioned "Case History") listing the docket entries for the case.[2] A copy of this Agreed Judgment is attached hereto as part of Commonwealth Bank's Appendix. It is undisputed that this Agreed Judgment was prepared and tendered to the Circuit Court without any prior notice to or involvement by Commonwealth Bank. Indeed, Tax Ease vehemently (and unabashedly) contends that it had no obligation to give Commonwealth Bank any notice of, or opportunity to object to, the Agreed Judgment.

3. The Lien Adjudged And Sums Awarded Tax Ease In The Agreed Judgment.

Paragraph 1 of the Agreed Judgment awards Tax Ease a monetary judgment against Ms. Murphy, and the amounts so awarded are the subject of the dispute before this Court. Paragraph 2 declares that "to secure the payment of" the sums awarded in Paragraph 1, Tax Ease "is adjudged to have a valid enforceable lien against the property owned by the Defendant(s), Teretha M. Murphy, ..." Paragraphs 3 and 4 provide for an installment payment schedule by Ms. Murphy of the judgment awarded Tax Ease. Under this

[2]The first page of the Agreed Judgment has a "Tendered" stamp in the upper right corner of the first page of "12/21/09" but the date on the third page above the Circuit Court Judge's signature is December 7, 2009. Commonwealth Bank believes that handwritten "7" and "Dec" on the date line is not the date the Circuit Court Judge signed the Agreed Judgment but the date when either Ms. Murphy or Tax Ease's attorney signed the Agreed Judgment.

installment payment schedule, Ms. Murphy was to pay at total of $3,123.90. Paragraph 5 reflects that "Plaintiff agrees that it will not execute on the Judgment or take any additional steps to enforce its lien in and to Defendants' [sic] real property" if Ms. Murphy complies with the Agreed Judgment. Paragraph 6 provides that if Ms. Murphy fails to comply with the Agreed Judgment, then Tax Ease "will be entitled to proceed to enforce its lien and move the Court for an Order of Sale against Defendants' real property, with proceeds there from applied to the full unpaid balance of this Judgment." Paragraph 6 does not state that the proceeds will be used to pay any other potential creditor. Thus, the Agreed Judgment granted Tax Ease a first lien position for the full amount of the sums set forth in the Agreed Judgment.[3]

Regarding the specific sums, Tax Ease was awarded in the Agreed Judgment the following:

---

[3]In this case, Commonwealth Bank has not challenged the position of Tax Ease that the lien of a purchaser of a tax bill has "superpriority" over even a prior recorded mortgage. However, Commonwealth Bank would advise the Court that there is currently pending in the Franklin Circuit Court a lawsuit challenging this view of the statutory scheme. The case is Farmers National Bank, et al. v. Commonwealth of Kentucky, Department of Revenue, Franklin Circuit Court, No. 10-CI-1745. That lawsuit challenges the constitutionality, on several grounds, of the state selling its taxing power and taxing authority to private, for profit businesses. In addition, Count VIII of the Complaint in that lawsuit further alleges that superpriority exists only to the extent of the sums actually paid to the taxing entities and that the additional fees and expenses added on by the private purchasers are not entitled to superpriority. This argument is based upon the specific language of KRS 134.420, KRS 134.546, KRS 134.551, and KRS 382.270. It is also based upon an "unconstitutional takings" argument. This constitutional argument notes that if superpriority exists, then the equity of a preexisting lien is being given to a private tax bill purchaser as an incentive to purchase the tax bill and without any compensation being paid to the preexisting lienholder whose equity is consumed by the additional fees added by the tax bill purchaser (particularly when those additional fees are not received by the taxing entities). These issues are not before the Court in this case, but Commonwealth Bank is concerned that this Court not craft a written decision that inadvertently forecloses these arguments when they have not been briefed in this case.

a. $718.05 (being the "Principal Amount" of the 2006 tax bill made the basis of this suit), plus interest upon the Principal Amount from the date of Plaintiff's purchase of said tax bill, April 6, 2007, until paid (pursuant to KRS 134.500), Administrative Fees (pursuant to KRS 134.452(1)(d)) of $100, Pre-Litigation Fees (pursuant to KRS 134.452(1)(c)(1)) of $464.00,

b. $718.05 (being the "Principal Amount" of the 2007 tax bill made the basis of this suit), plus interest upon the Principal Amount from the date of Plaintiff's purchase of said tax bill, April 22, 2008, until paid (pursuant to KRS 134.500), Administrative Fees (pursuant to KRS 134.452(1)(d)) of $100, Pre-Litigation Fees (pursuant to KRS 134.452(1)(c)(1)) of $271.00,

c. Actual and reasonable attorney's fees (pursuant to KRS 134.452(1)(c)(3)) in the amount of $957.00, Legal Expenses for Title Search of $400.00 and Court costs and filing fees of $249.67.

See Agreed Judgment ¶1 [R.A. 28].

These paragraphs of the Agreed Judgment cite to several subsections of KRS 134.452. This statute provides that "Notwithstanding any other provisions of this chapter, a third-party purchaser of a certificate of delinquency shall be entitled to collect only the following ... [listing the permissible fees]."

As a preliminary matter, KRS 134.452 was amended during the 2009 regular session of the Kentucky General Assembly by Section 14 of House Bill 262. See 2009 Ky. Acts ch. 10 §14. The amendments took effect on January 1, 2010. See 2009 Ky. Acts ch. 10 §73. This was 9 days after the Agreed Judgment was entered. The changes to the sections referred to in the Agreed Judgment were stylistic (changing the numbering and cross-referencing sections therein). The 2009 legislation did not changes the substantive requirements and limits on permissible fees involved in this case. Thus, for purposes of this Appellee's Brief, Commonwealth Bank will cite to the language of the statute in effect on December 23, 2009 (the date of the Agreed Judgment).

A. The "Administrative Fee" Award.

First, Tax Ease's tendered Agreed Judgment awarded it $100 as an "Administrative Fee" for each of the 2006 and 2007 tax bills and recites this "was pursuant to KRS 134.452(1)(d)" which at that time provided that a purchaser of an unpaid tax bill (referred to in the statutes as a "Certificate of Delinquency") could collect "Administrative fees incurred for preparing, recording, and releasing an assignment of the certificate of delinquency in the county clerk's office, not to exceed one hundred dollars ($100.00)." Tax Ease did not present to the Circuit Court or to the Court of Appeals any evidence of the "administrative fees" it actually "incurred" for "preparing, recording, and releasing an assignment of the certificate of delinquency in the county clerk's office."

B. The "Pre-Litigation Fees" Award.

Second, Tax Ease's tendered Agreed Judgment awarded it "Pre-Litigation Fees" "pursuant to KRS 134.452(1)(c)(1)" in the amount of $464 for the 2006 tax bill and in the amount of $271 for the 2007 tax bill. The statutory citation in the Agreed Judgment is incorrect because Tax Ease owns two tax bills and it alleges having paid more than $701 for each, and this triggers a special limit on the fee contained in KRS 134.452(1)(c)(2). The relevant statutory provisions in effect on December 23, 2009, were the following:

> (c) Attorneys' fees as provided in this paragraph:
> 1. Attorneys' fees incurred for collection efforts prior to litigation as follows:...
> c. If the amount paid for a certificate of delinquency is above seven hundred one dollars ($701), actual reasonable fees incurred up to seventy percent (70%) of the amount of the certificate of delinquency, not to exceed seven hundred dollars ($700).
> 2. If a purchaser is the owner of more than one (1) certificate of delinquency against the same taxpayer, actual and reasonable prelitigation attorneys' fees for all certificates of delinquency against the same taxpayer shall not exceed one and one-half (1.5)

> times the maximum amount permitted in subparagraph 1. of this paragraph for the largest tax bill owed by the taxpayer.

Applying these statutory provisions is a three step-process:

- First, under KRS 134.452(1)(c)(1), the owner of the certificate of delinquency must show certain proof of the nature of the charges: that the charges are for "attorneys' fees" which were "incurred for collection efforts prior to litigation" and they must be "actual" and "reasonable" No such showing was presented to the Court when the Agreed Judgment was presented.
- Second, under KRS 134.452(1)(c)(1)(c), there is a dollar cap on the attorneys' fees that meet the requisite showing for each single tax year. Since Tax Ease alleges it purchased both the 2006 and 2007 tax bills for more than $700, that cap is "seventy percent (70%) of the amount of the certificate of delinquency, not to exceed seven hundred dollars ($700)." The statute is unclear if this 70% is based upon the "amount of the certificate of delinquency" at the time of the purchase or at some later time (possibly the date the owner files a lawsuit). If it is based upon the purchase price (the smallest possible number), it would be $502.63 for each year. This is calculated as follows: (a) for 2006, $502.63 (70% of $708.15); and (b) for 2007, 502.63 (70% of 708.15).
- Third, since Tax Ease owns two tax bills, under KRS 134.452(1)(c)(2), there is a total cap on "attorneys' fees incurred for collection efforts prior to litigation" which is "one and one-half (1.5) times the maximum amount permitted in subparagraph 1. of this paragraph for the largest tax bill owed by the taxpayer." Applying this aggregate cap, Tax Ease could only collect 1.5 times $502.63 for its actual, reasonable, pre-litigation attorney's fees or $753.95. The Pre-Litigation fees that Tax Ease persuaded Ms.

Murphy to pay in the Agreed Judgment total $735 ($464 for 2006 and $271 for 2007) which was within the cap.

Since the dollar amounts awarded for "Pre-Litigation Fees" are within the statutory cap, the real issue in this case is the right of Commonwealth Bank to require that Tax Ease demonstrate that $735 is for "attorneys' fees" which were "incurred for collection efforts prior to litigation" and that are "actual" and "reasonable". It is undisputed that no evidence of this was presented to the Circuit Court prior to entry of the Agreed Judgment.[4]

C. The Post-Litigation Award.

Third, Tax Ease's tendered Agreed Judgment awarded three different amounts citing KRS 134.452(1)(c)(3): (1) "Actual and reasonable attorney's fees" of $957.00; (2) "Legal Expenses for Title Search" of $400; and (3) "Court costs and filing fees of $249.67".

As quoted above, KRS 134.452(1)(c)(3) only permits Tax Ease to collect "actual, reasonable attorneys' fees and costs that arise due to the prosecution of collection remedies."

It is undisputed that no evidence justifying these amounts awarded Tax Ease was presented to the Circuit Court prior to entry of the Agreed Judgment.

---

[4]On February 23, 2010 (two months after the Agreed Judgment was entered), Tax Ease tendered to the Circuit Court the "Affidavit of Billy W. Sherrow of the law firm Sherrow, Sutherland & Associates advising that his firm had invoiced Tax Ease and been paid the sums alleged in the Complaint "in exchange for its attempts to collect the amounts due". See Affidavit Of Pre-Litigation Attorneys Fee" [R.A. at pp. 68-69]. Mr. Sherrow is not an attorney with the same law firm that filed Tax Ease's Complaint. The attorney signing Tax Ease's Complaint was employed at the Dallas, Texas law firm of Wilensky & Jones, LLP. [R.A. at p. 5]. Mr. Sherrow's affidavit does not give any details about his work such as the work performed, the dates and time it was performed, or the method by which the fee was calculated (flat fee, hourly, contingent, or something else). Cf. Meyers v. Chapman Printing Co., Inc., 840 S.W.2d 814 (Ky. 1992) (approving the "lodestar" approach to determining a reasonable attorney fee award in civil rights cases). Also, it is Commonwealth Bank's experience switching lawyers "midstream" often results in duplicative and greater attorneys' fees, a circumstance that Commonwealth Bank was denied the opportunity to investigate.

4. The Circuit Court Rejects Commonwealth Bank's Efforts To Set Aside The Agreed Judgment And Require Tax Ease To Prove It Is Entitled To A Lien On The Property In The Amount Of The Sums Awarded To It.

The same day that Commonwealth Bank's counsel received the entered Agreed Judgment, Commonwealth Bank filed two motions in the Circuit Court. It filed a motion to set aside the Agreed Judgment. See "Motion To Vacate Agreed Judgment" [R.A. pp. 45-47]. It also filed a "Motion" requesting the Circuit Court review payoff quotes provided by Tax Ease for compliance with KRS 134.452 and order that Tax Ease accept those sums if tendered by Commonwealth Bank as a protective advance under its mortgage from Ms. Murphy. See "Motion" [R.A. pp. 32-44].

Commonwealth Bank's motions were noticed for and heard at the Circuit Court's regular motion hour on January 6, 2010. At that time, Ms. Murphy personally appeared *pro se* and also orally requested the Circuit Court set aside the Agreed Judgment and review the appropriateness of the fees Tax Ease was claiming. Commonwealth Bank argued that the entry of the Agreed Judgment without the agreement of, or prior notice to Commonwealth Bank, was improper. Commonwealth Bank also argued that the sums demanded were excessive and that Tax Ease should be required to demonstrate as a factual matter that it satisfied the statutory requirements under KRS 134.152(1).

By an Opinion And Order entered on February 25, 2010, the Circuit Court denied both Commonwealth Bank's and Ms. Murphy's motions. See "Opinion And Order" [R.A. 73-75].[5] The Circuit Court held that Commonwealth Bank did not have standing to object to the Agreed Judgment. The Circuit Court focused on Commonwealth Bank's willingness to voluntarily pay a Circuit Court-approved amount as a protective advance under its mortgage

[5]The Circuit Court's Opinion And Order at pp. 1-2 recites that Ms. Murphy's oral motion was made at the motion hour. See R.A. 73-74.

from Ms. Murphy. The Circuit Court did not consider the fact that Commonwealth Bank was harmed by the Agreed Judgment since it purported to establish Tax Ease's entitlement to a lien superior to the Bank's mortgage, thereby reducing the Bank's property interest in the real property mortgaged to it.

Commonwealth Bank then filed a motion under CR 60.02 asking the Circuit Court to reconsider its decision that Commonwealth Bank did not have standing to object to the entry of the Agreed Judgment and to have the Agreed Judgment set aside. See "Motion" [R.A. 81-83]. Commonwealth Bank argued that entry of the Agreed Judgment without prior notice to Commonwealth Bank was an unconstitutional taking of its property without due process of law, and that the Court's action was taken based upon an improper *ex parte* communication with the Court by Tax Ease and Ms. Murphy since their tendering of the Agreed Judgment was done without notice to or participation by Commonwealth Bank.

By an Opinion And Order entered March 11, 2010, the Circuit Court denied this motion on the ground that it was a second post-judgment motion which was not permissible as a procedural matter. See "Opinion And Order" [R.A. 91-94].

Commonwealth Bank then appealed.

5. The Court Of Appeals Reverses, In Part, The Circuit Court And Directs That Tax Ease Prove That It Has Satisfied The Statutory Requirements For Recovery Of The Amounts To Which It Claims To Be Entitled.

By an "Opinion Affirming In Part, Reversing In Part And Remanding" rendered on April 15, 2011 (hereafter, the "Court of Appeals' Opinion"), the Court of Appeals held that Commonwealth Bank had standing to object to entry of the Agreed Judgment. It found that Commonwealth Bank "was negatively impacted by the agreed judgment, and has standing under well-established constitutional analysis". See Court of Appeals' Opinion at p. 5.

Because Tax Ease claimed a first lien position and because Commonwealth Bank did not challenge the interpretation of KRS 134.420(3) that a tax lien held by a private purchaser is superior to the lien of a prior recorded mortgage, Judge Thompson recognized that the Agreed Judgment gave Tax Ease a lien that reduced the amount of the proceeds from any sale of the mortgaged property that could be used to repay Commonwealth Bank. Id. at pp. 5-6.[6] Judge Thompson recognized the obvious point that "if a creditor's security interest is supplanted by the entry of an agreed judgment, it necessarily follows that its ability to recoup its prior loan is diminished and, in some cases, may even be rendered impossible." He concluded that, reducing a party's security interest is a real and substantial harm warranting constitutional standing." Id. at p. 6.

Court of Appeals' Judge Clayton dissented. See Court of Appeals' Opinion at pp. 7-13. In his view, Ms. Murphy's signature on the Agreed Judgment was an acceptance by her of the reasonableness of the fees Tax Ease was seeking, and Commonwealth Bank should not be allowed to challenge her acceptance of the fees. He viewed the Agreed Judgment as merely a "separate contract" between Ms. Murphy and Tax Ease. Id. at p. 12. He also viewed the amounts at issue as having only a "slight 'ripple effect'" on Commonwealth Bank's lien position which did not justify giving it standing to object to them. Id.

Argument

1. Standard Of Review.

Commonwealth Bank agrees with Tax Ease's position that this Court's review concerns questions of law for which *de novo* review is the appropriate standard.

[6]As discussed in Footnote 3, there is a pending lawsuit in Franklin Circuit Court challenging this view of KRS 134.420(3) on both statutory construction and constitutionality grounds. However, that issue and those arguments have not been raised in this proceeding.

2. The Circuit Court Erred In Entering An Agreed Judgment Finding Tax Ease Had A Lien Upon The Subject Property And Setting The Lien Amount Without Giving Commonwealth Bank Notice And An Opportunity To Be Heard.

A. Failing To Give Notice To Commonwealth Bank Violated The Applicable Rules Of Civil Procedure.

Tax Ease contends that it is entirely permissible for some parties to a lien enforcement lawsuit to tender an "Agreed Judgment" to a Circuit Court without giving notice to the other parties in the case who are not in default and who are claiming a competing lien. This is not the proper reading of this Court's Rules of Civil Procedure.

Civil Rule 5.01 unequivocably states:

> ....every written motion other than one which may be heard ex parte, and every written notice, appearance, demand, offer of judgment, ... and similar papers shall be served upon each party except those in default for failure to appear. [Emphasis added]

The "Agreed Judgment" tendered by Tax Ease and Ms. Murphy is either a "motion" requesting the court to enter the judgment, an "offer of judgment", or a "similar paper". As such, the rule requires that it "shall be served" upon Commonwealth Bank. There is no dispute that the Agreed Judgment was not served upon Commonwealth Bank.

Under Civil Rule 5.03, since the Agreed Judgment was required to be served, "proof of the time and manner of such service shall be filed before action is to be taken thereon by the court or the parties." There is no dispute that no proof of service upon Commonwealth Bank was filed, and certainly not before the Circuit Court entered the Agreed Judgment.

Commonwealth Bank believes that technically the "Agreed Judgment" is best viewed as a proposed order which, under Civil Rule 7.02, should be accompanied by a written motion as it was not made at a hearing or trial. Under Civil Rule 7.02, that motion

"shall state with particularity the grounds therefor." Where all parties not in default are in agreement, the common practice is to dispense with a motion and simply tender the agreed judgment. Obviously, the key point is that all of the parties not in default review, approve and join in the tendered agreed judgment.

Indeed, the Circuit Court attempted in its March 11, 2010, order to rely upon its local rules regarding agreed orders to justify its action. Local Rule of Practice 5(f) for the 53rd Judicial Circuit states that "if an agreed order, signed by counsel for all parties affected, relating to a motion appearing on the motion docket, is submitted to the Clerk prior to the call of the motion docket, counsel need not attend the call of the motion docket. See Circuit Court's Opinion And Order (entered March 11, 2010) [R.A. at p. 93].

There are two glaring errors in using the rule to justify refusing to set aside the Agreed Judgment. First, Commonwealth Bank was a party "affected" by the Agreed Judgment as it eliminated any ability of Commonwealth Bank to challenge the existence of a lien claim by Tax Ease or to question the amount of the fees that Tax Ease could receive from a Commissioner's Sale of the subject property. As an affected party, the local rule required the signature of Commonwealth Bank's attorney on the Agreed Judgment, but this did not occur so the rule does not apply. Second, the Agreed Judgment did not "relat[e] to a motion appearing on the motion docket." In fact, no motion of any kind was filed with respect to the Agreed Judgment.

As explained more fully below, the requirements in the Civil Rules of making written motions with service on opposing counsel is a fundamental requirement of due process. It also avoids the appearance of impropriety and prevents improper *ex parte* contacts. See SCR 3.130(3.5(b)) (prohibiting *ex parte* communications with judges except

as permitted by law or court order).

Tax Ease has presented no persuasive reason why it could not either (a) attempt to obtain Commonwealth Bank's consent to the Agreed Judgment or (b) file the Agreed Judgment with the Court along with an appropriate motion and notice to Commonwealth Bank. Tax Ease argues that doing either of these will "make it less likely for third-party purchasers to settle with delinquent taxpayers...." See Appellant's Brief at p. 8.

As a preliminary matter, there is nothing that precludes Tax Ease and Ms. Murphy from agreeing to an installment payment plan outside of a court proceeding. However, when Tax Ease wishes to use the enforcement mechanisms of the judicial system to put pressure on a taxpayer to settle, those mechanisms come with certain safeguards, including the service and notic provisions of the Civil Rules, that protect the integrity of the entire system and the rights of the others involving in those judicial proceedings. Each year, thousands of cases are settled throughout the Circuit Courts of this Commonwealth in compliance with these safeguards. There is no reason why Tax Ease should not similarly follow them.

B. Failing To Give Notice To Commonwealth Bank Violated Its Right To Due Process.

"An elementary and fundamental requirement of due process in any proceeding which is to be accorded finality is notice reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections." Mullane v. Central Hanover Trust Co., 339 U.S. 306, 314 (1950). "The fundamental requirement of procedural due process is simply that all affected parties be given 'the opportunity to be heard at a meaningful time and in a meaningful manner.'" Hilltop Basic Resources, Inc. v. County of Boone, 180 S.W.3d 464, 468 (Ky. 2005) (quoting

Matthews v. Eldridge, 424 U.S. 319, 333 (1976)).

In Mullane, the Supreme Court noted that it is "interested parties" that are entitled to notice and an opportunity to be heard." Plainly, Commonwealth Bank is "interested" in the existence and amount of a competing lien against property on which it claims a mortgage lien. Indeed, the existence alone of a lien, prior or subordinate, is a sufficient interest since a junior lienholder can force a judicial sale which can have adverse implications on the mortgage lender. For example, a judicial sale of the borrower's house at the demand of a junior lienholder can result in numerous adverse consequences to the borrower which can spill over to affect Commonwealth Bank. A judicial sale will require a competing lienholder to decide whether or not to attend, and bid, at the sale. Even the amount of a competing lien, junior or senior, can be of interest to a mortgagee lienholder since the amount can affect whether or not the mortgagor can pay the lien claim and also afford to continue to make payments on the loan secured by the lender's mortgage. Indeed, it was to prevent such adverse consequences that Commonwealth Bank was interested in obtaining a judicial review of Tax Ease's fees so it could decide if it wished to pay those fees itself (as a protective advance under its mortgage) so that Ms. Murphy could be in a better position to repay her loan to Commonwealth Bank.[7]

It is obvious that the General Assembly recognized that a competing lienholder is always "interested" in the validity, priority, and amount of another person's competing lien

[7] For example, a tax lien accrues interest at 12% per annum and a judicial sale by the tax lien purchaser will add master commissioner fees and other costs and expenses. If Commonwealth Bank were prepared to charge a lower interest rate and agree to a longer repayment period that Tax Ease proposed in its Agreed Judgment, this could put Ms. Murphy in a better position to repay Commonwealth Bank's loan. However, Commonwealth Bank is entitled to know the details of how Tax Ease calculated and justified its fee claims before making such a decision.

claim. That recognition is expressly reflected in the enactment of KRS 426.006 which required Tax Ease to join Commonwealth Bank in its lawsuit.

The rule that a junior lienholder may raise as against a prior lienholder any defense which a debtor could raise is a very old established rule in Kentucky. At least as far back as 1883, Kentucky's highest court held that the defense of usury (which affects the amount of a payoff) can be raised by a junior lienholder as against a prior lien. Levi Sloss' Exr. v. Adolph Levi, 5 Ky.L.Rptr. 431, 12 Ky.Op. 346 (Ky. 1883). This rule was recognized by the Sixth Circuit Court of Appeals stated in Kaye v. MacMillan, 60 F.2d 7, 10 (6th Cir. 1932). In that case, the Court of Appeals acknowledged that "in Kentucky a contest between parties asserting liens upon the same property owned by a common debtor, either party may make any defense with the common debtor could make." As Ms. Murphy certainly could raise (and in fact attempted to raise at the motion hour on January 6, 2010), the reasonableness of the amount of Tax Ease's fees, so can Commonwealth Bank.

The failure to give prior notice to Commonwealth Bank and to force Commonwealth Bank to try to set aside the Agreed Judgment was improper from a due process perspective. Commonwealth Bank had no prior notice that its property interest (the equity in the property available to satisfy its mortgage) was going to be taken, there was no hearing at the time of the taking, nor was there in place a process for an early post-seizure hearing. This type of violation was expressly ruled unconstitutional by Fuentes v. Shevin, 407 U.S. 67 (1972). See also Farmers Deposit Bank v. Ripato, 760 S.W.2d 396, 400-401 (Ky. 1988).

The United States Supreme Court's decision in Armstrong v. Manzo, 380 U.S. 545 (1965), illustrates the flaw in forcing Commonwealth Bank to try to set aside the Agreed Judgment after it was entered. In that case, a divorced father was not given prior notice of

efforts by his ex-wife and her new husband to adopt his child based upon the ex-wife's filing an affidavit that the ex-husband was not paying child support. After the decree of adoption was entered, he was then notified. As Commonwealth Bank did in this case, the ex-husband promptly filed a motion to vacate the ruling and require the ex-wife to restart the proceedings. Rather than doing that, the trial court forced the ex-husband to show that the ruling should be set aside. The United States Supreme Court held that placing the burden on the ex-husband to set aside a court order about which he had received no prior notice was a due process violation. In an unanimous opinion, Justice Stewart explained that the subsequent hearing was insufficient because it improperly placed the burden of proof on the ex-husband when it was the burden of the ex-wife to prove that the ex-husband should suffer the loss of his parental rights. Justice Stewart explained:

> The trial court could have fully accorded this right [the opportunity to be heard] to the petitioner [the ex-husband] only by granting his motion to set aside the decrees and consider the case anew. Only that would have wiped the slate clean. Only that would have restored the petitioner to the position he would have occupied had due process of law been accorded to him in the first place. His motion [to vacate] should have been granted.

See Armstrong v. Manzo, 380 U.S. at 552.

The exact same result is required in this case, and the Court of Appeals correctly so held. Its opinion should be affirmed.

C. Tax Ease's Arguments That Commonwealth Bank Lacks Standing To Object To The Agreed Judgment Are Incorrect.

i. Tax Ease Fails To Advise This Court Of Controlling Kentucky Precedent That Commonwealth Bank Has Standing To Raise Any Defense Ms. Murphy Could Raise.

In its Appellant's Brief, Tax Ease makes the assertion that "[t]here does not appear to

be any case law in the Commonwealth setting forth the test to use to determine when a person has standing to assert the rights of third parties." See Appellant's Brief at p. 9. This assertion is amazing given that Commonwealth Bank's brief to the Kentucky Court of Appeals specifically referred on page 7 to the decisions in Levi Sloss' Exr. and Kaye v. MacMillan discussed in Section 2(A) of this brief. Moreover, the Sixth Circuit in Kaye v. MacMillan expressly refers to a third case, Banta v. Louisville Savings, Loan & Building Co., 59 S.W. 501, 22 Ky. Law Rep. 1045 (1900), as the basis for its finding that "in Kentucky in a contest between parties asserting liens upon the same property owned by a common debtor, either party may make any defense which the common debtor could make." See Kaye v. MacMillan, 60 F.2d at 10.

In Banta, Justice Guffy wrote as follows to affirm the standing of a competing lien creditor to raise the debtor's defenses as against another lien claimant:

> In a contest between parties asserting liens upon the same property, owned by a common debtor, either party may make any defense which the common debtor could make. This doctrine is too well settled to require citation of authorities.

Banta, 59 S.W. at 501 (emphasis added).

Quite simply, Tax Ease's erroneous detour into the realm of federal court decisions about third-party standing is based upon a failure to read the road signs clearly and repeatedly marked by these reported Kentucky decisions.

ii. Tax Ease's Effort To Construe The Agreed Judgment As Merely A Contract Is Equally Untenable.

Tax Ease essentially argues that it reached a private agreement with Ms. Murphy and that Commonwealth Bank does not have standing to challenge that private agreement. The dissenting of opinion of Court of Appeals' Judge Clayton similarly focused on a view of the

Agreed Judgment as being "based on a contractual relationship" between Ms. Murphy and Tax Ease. See Court of Appeals' Opinion at p. 10.

The flaw with this approach is that the Agreed Judgment is much more than a private contract to pay money between Ms. Murphy and Tax Ease.

- First, it is a judicial order which binds Commonwealth Bank both as to the existence of Tax Ease's lien on the same property mortgaged to Commonwealth Bank and the amount of that lien. There is no dispute that this order adjudicates the existence of a lien which the parties in this case do not dispute is prior to the mortgage lien of Commonwealth Bank, permits Tax Ease to obtain a judicial sale, and requires Tax Ease to receive the proceeds of any sale of property also mortgaged to Commonwealth Bank without any provision for making any payment towards Commonwealth Bank's lien claim.
- Second, it is a judicial order applying the provisions of KRS 134.452. This statute expressly provides that Tax Ease "shall be entitled to collect only the following [listing the permitted statutory amounts]." The word "shall" is mandatory, and this statute is an express command by the General Assembly as to what Tax Ease may collect regardless of any contractual agreement. Indeed, KRS 134.990(11)(a) makes it a crime for any third-party purchaser to "knowingly … deman[d] costs or fees in excess of those permitted by KRS 134.452."
- Third, it is a judicial order establishing Tax Ease's right to receive certain attorneys' fees and costs that the General Assembly has expressly required be both actually incurred and also reasonable. Appropriate deference to the General Assembly and appropriate oversight of the legal profession justify this Court reaffirming the

longstanding rule (recognized in Levi Sloss' Exr. v. Adolph Levi) that a competing lien creditor who is a party to the proceeding where the sums are sought has standing to require compliance with these requirements. See also Capital Cadillac-Olds, Inc. v. Roberts, 813 S.W.2d 287, 293 (Ky. 1991) ("... a trial court should require parties seeking attorney fees to demonstrate that the amount sought is not excessive and accurately reflects the reasonable value of bona fide legal expenses incurred."). This Court in Capital Cadillac-Olds further stressed that "[i]t should never be overlooked that any award of an attorney fee is subject to a determination of reasonableness by the trial court." Id. at 293.

- Fourth, the Agreed Judgment is a judicial order entered in a proceeding which Commonwealth Bank is mandated by statute, KRS 426.006, to be joined so it can protect itself.
- Fifth, Tax Ease's argument proves too much. Under its view, Tax Ease could tender an Agreed Judgment signed only by the taxpayer and awarding hundreds (even thousands) of dollars of fees which are plainly in excess of the statutory maximums, but no party could object.

For these reasons, this Court should reject Tax Ease's argument that entry of the Agreed Judgment was merely a contract about which Commonwealth Bank does not have the requisite standing to object.

iii. Commonwealth Bank Has Standing Even Under The Federal Courts' Third-Party Standing Test Urged By Tax Ease.

Even if this Court were to depart from Kentucky's well-established standing rule discussed in Banta and apply the third-party standing test urged by Tax Ease, Commonwealth Bank would still have standing to object to entry of the Agreed Judgment.

The test presented by Tax Ease is the following:

> [T]hird-party standing requires the satisfaction of three preconditions: 1) the plaintiff must suffer injury; 2) the plaintiff and the third party must have a "close relationship"; and 3) the third party must face some obstacles that prevent it from pursuing its own claims.

See Appellant's Brief at p. 9 (quoting Pennsylvania Psychiatric Soc. v. Green Spring Health Services, Inc., 280 F.3d 278, 288-89 (3rd Cir. 2002)).

First, Commonwealth Bank did suffer injury. A competing lien which the parties treat as a prior lien has been adjudged to exist and the amount thereof has been established. If the amounts were only exactly what was paid to the taxing authorities, Commonwealth Bank's injury might be debatable. But Tax Ease has added additional fees and costs that are different from those that the government could charge. Compare KRS 134.452 (fees a third-party purchaser may charge) with KRS 134.504(7) (fees a county attorney may collect).[8]

Second, Commonwealth Bank and Ms. Murphy plainly have a "close relationship" – that of mortgagor and mortgagee. Unlike the relationship with Tax Ease which was created without Ms. Murphy's consent when Tax Ease decided to purchase her unpaid tax bill without her knowledge or consent, Ms. Murphy chose to do business with, and borrow money from, Commonwealth Bank.

---

[8]Indeed, the fact that some taxpayers pay one set of fees to private tax bill purchasers while others pay a different set of fees to county attorneys is part of the challenge being asserted in the Farmers National Bank case currently pending before the Franklin Circuit Court. The Plaintiffs in that case allege that there now exists in Kentucky a dual system of tax collection under which some persons face collection from private, for profit businesses, while others do not. Furthermore, the plaintiffs also contest the ability of different tax purchasers to charge different fees and foreclose at their discretion thereby adding another layer of non-uniformity. Among other arguments, the Farmers National Bank plaintiffs argue that this non-uniformity violates the "general laws" requirement of Kentucky Constitution §171 and §181 as well as the requirement under Constitution §171 that taxes be "collected" in a manner that is "uniform upon all property of the same class". These issues are not currently before this Court in this case.

Third, Ms. Murphy faces real obstacles that prevent her from pursuing her own claims. See Pennsylvania Psychiatric Soc., 280 F.3d at 290 (noting that "[t]his criterion does not require an absolute bar from suit, but some hindrance to the third party's ability to protect his or her own interests."). The major hindrance here is that she is appearing *pro se* (a common situation when an individual faces financial difficulties preventing the payment of ad valorem taxes) and lacks the resources or experience to readily understand and apply the statutory scheme which governs Tax Ease. She certainly has a limited ability to evaluate the reasonableness of an attorney fee claim or the cost of performing a real estate title examination (fees that Tax Ease is claiming).

Even assuming that Commonwealth Bank is acting solely in a derivative manner (which it is not as it is also protecting its own mortgage lien equity in the property), Commonwealth Bank has standing regardless of what test is applied – Kentucky's or that of the federal courts'.

D. This Court Should Appropriately Consider And Address The Reality Of What Occurred In This Case.

"[T]here comes a point where this Court should not be ignorant as judges of what we know as men." Watts v. State of Indiana, 338 U.S. 49, 52, 69 S.Ct. 1347, 1349, 93 L.Ed. 1801 (1949). "[T]here are none so high as to be above the restraints of the law, or so low as to be beneath its protection." Commonwealth v. Wade's Adm'r, 104 S.W. 965, 968 (Ky. 1907).

Commonwealth Bank presents these two quotes because this case deserves to be decided in light of the reality of what occurs in this type of case. Tax Ease filed a foreclosure lawsuit against a homeowner who has failed to pay her taxes. This may be because of oversight, error, financial distress, or something else, but the reason is irrelevant.

Ms. Murphy faces the loss of her home and the expense of hiring a lawyer. The terror of this to an average homeowner should not be underestimated by a panel of Justices whose professional careers involve day-to-day dealings with statutes, courts and lawyers. She is contacted, without the benefit of counsel, by a representative of Tax Ease who presents to her an Agreed Judgment and told that this will save her house from foreclosure and keep Tax Ease from further running up the amount it claims she owes. Ms. Murphy has no experience dealing with the intricacies of what fees are allowed under a statutory schedule like KRS 134.452. She has no experience dealing with what proof she should demand from Tax Ease concerning the required pre-lawsuit notices Tax Ease must send in order to have a valid lien. See KRS 134.490. She has no experience dealing with what proof she should demand to justify the fees Tax Ease claims. She only knows that signing the Agreed Judgment will, according to Tax Ease, save her home from foreclosure even though she will be paying installments totaling $3,123.90[9] for two tax bills that Tax Ease purchased for $1,436.10.

She signs the Agreed Order, and it is presented to the Circuit Court without any prior notice to a competing lien creditor that is a party to the case and who is Ms. Murphy's bank lender. The lawyer for Ms. Murphy's bank learns after the fact of the entry of the Agreed Judgment. The bank, with advice of counsel regularly engaged in this type of legal services, believes the fees awarded are excessive and promptly objects. When Ms. Murphy is finally made aware that perhaps the fees are too high, she joins with her bank and asks the Circuit

[9]The amount of $3,123.90 differs from the $2,541.67 recited by Commonwealth Bank in its Statement Concerning Oral Argument because Tax Ease used the larger figure in Paragraph 3 of the Agreed Judgment for the amount Ms. Murphy would pay for the privilege of paying in installments. The $2,541.67 is the base amount of the judgment (not counting interest) recited in Paragraph 1 of the Agreed Judgment.

Court to review the fees, but she and Commonwealth Bank are told by the Circuit Court that neither can make that request.

This process is not the process required under this Court's Civil Rules. It is not the process or outcome contemplated by the General Assembly when it enacted KRS 134.452. It is not the process contemplated by the constitutional requirement of due process. This Court should preserve the integrity of its Civil Rules, enforce the plain language of KRS 134.452, and give competing lienholders such as Commonwealth Bank the ability to protect themselves and their customers from potential abuses by for-profit businesses that purchase unpaid tax bills.

Conclusion

For all the foregoing reasons, this Court should affirm the Court of Appeals' opinion.

Respectfully submitted,

MORGAN & POTTINGER, P.S.C.

By: _____
M. Thurman Senn
601 West Main Street
Louisville, Kentucky 40202
Phone: (502) 589-2780
Fax: (502) 585-3498
Email: mts@morganandpottinger.com
Co-Counsel for Appellee, Commonwealth Bank & Trust Company

MATHIS, RIGGS & PRATHER, P.S.C.

By: Donald T. Prather by _____
Donald T. Prather
500 Main Street, Suite 5
Shelbyville, Kentucky 40065
Phone: (502) 633-5220
Fax: (502) 633-0667
Email: dprather@iglou.com
Co-Counsel for Appellee, Commonwealth Bank & Trust Company