

COMMONWEALTH OF KENTUCKY
SUPREME COURT OF KENTUCKY
CASE NO. 2014-SC-000324-D
(2012-CA-002218)

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SUPREME COURT

JOHN WESLEY BAYS,

APPELLANT

v.

KNOX CIRCUIT COURT
2007-CI-00631, 2008-CI-00371, AND 2009-CI-00246

KRISTIE D. KIPHART, INDIVIDUALLY
AND AS TRUSTEE, OF THE DEMAND
RIGHT IRREVOCABLE TRUST FOR
BRYCE A. BAYS,

APPELLEE.

APPEAL FROM DECISION OF THE COURT OF APPEALS
REPLY BRIEF ON BEHALF OF APPELLANT,
JOHN WESLEY BAYS

CERTIFICATE OF SERVICE

This is to certify that a true and correct copy of the foregoing Appellant's Reply Brief was transmitted, all expenses pre-paid, on this the 12th day of June 2015 to the following persons in accordance with CR 76.12(5) and 76.12(6): Clerk of the Kentucky Court of Appeals, 360 Democrat Drive, Frankfort, Kentucky 40601; Hon. Robert W. McGinnis, Special Judge, Knox Circuit Court, 775 Johns Road, Butler, KY 41006; Hon. Travis A. Rossman, P.O. Box 209, Barbourville, KY 40906; Hon. Dave R. Collins, 203 Knox Street, Ste. 1, Barbourville, KY 40906; and on the same date an original and nine (9) true and exact copies were transmitted via Federal Express Delivery to the Clerk of the Kentucky Supreme Court, Room 209, State Capitol, 700 Capital Ave., Frankfort, Kentucky 40601-3488. The record on appeal was not withdrawn by the Appellant.

Respectfully submitted,



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**I. WHEN FRAUD ON THE SPOUSAL SHARE IS FOUND
LIFE INSURANCE SHOULD BE SUBJECT TO KRS 392.020.**

The Appellee, Kiphart, argues that the Court of Appeals correctly determined that life insurance proceeds are not subject to the curtesy interest afforded by KRS 392.020.

With this case the Supreme Court can clarify that life insurance may be considered an asset like any other personal asset owned by a decedent spouse and does not hold some special protection or status in the event a surviving spouse is compelled to seek his or her statutory share, pursuant to KRS 392.020¹. Life insurance should not be immune from being considered personalty of the estate for the purpose of calculating the statutory share of the surviving spouse when fraud on the dower has occurred. Life insurance is an asset possessed by the owner of the policy with a known value even though that value may not be paid until the owner's death.² The owner of the insurance policy, usually by contract with the insurance company, dictates who or what the beneficiary or beneficiaries of the policy are. In the event that the estate is named the beneficiary or if no beneficiary is named, the death benefit is, and will necessarily be, surplus personalty of the decedent's estate.

This case is not about an insurance contract or the right to change a named beneficiary. This case concerns multiple acts of deception and fraudulent

¹ In his dissenting opinion, Justice Vanmeter characterized the status of life insurance as "magic". (p. 14).

² Both the American General Insurance Policy and the Prudential Life Insurance policy had terminal illness riders whereby the payment of all or part of the death benefit could be accelerated and paid prior to the death of Carole Bays.

behavior of Carole Kiphart Bays, with the assistance of her sister, Kristie Kiphart, to disinherit her husband, John Wesley Bays. There has been no evidence offered by the Appellee to rebut the multiple allegations of fraud in this matter.

It is important to remember that the two (2) life insurance policies were not the only assets of Carole Bays which were brought back into the estate for the purposes of calculating the statutory share of John W. Bays. The trial court also ordered that John Bays shall receive a sum of money equal to one-half of all the personalty of the Estate of Carole Bays identified as a Certificate of Deposit at National City Bank in the sum of \$90,891.01, jewelry valued at \$11,900.00, a Sept IRA valued at \$25,643.11, a tractor and 2005 Ford truck with a combined value of \$30,000.00.

In this case, Carole Bays' assets had a value in excess of \$1,213,000.00. The two (2) insurance policies constituted \$875,000.00 of that sum or seventy-two percent (72%) of her estate. Of her total assets Carole Bays left her husband, John Bays, "personal and household effects of every kind including but not limited to furniture" ³ He did not receive cash of any kind until he received payment of the \$15,000.00 spousal exemption and one-half of an IRS income tax refund in the amount of \$4,851.50 after the estate was probated. In addition, it is also worth repeating that John W. Bays is the father and natural guardian of Bryce Bays who was six (6) years old when his mother died. Bryce is now thirteen (13) years of age and has always resided with his father. The Appellee,

³ See Last Will of Carol Kiphart-Bays, Item III, Appendix 5 to Appellant Brief to Supreme Court.

who is the Trustee of the Demand Right Irrevocable Trust for Bryce Bays, now and has always resided in Ohio.

By reinstating the Judgment of the Knox Circuit Court in this case, the Supreme Court can provide protection to a surviving spouse who has been disinherited so that he/she may assert a claim for his/her statutory spousal interest pursuant to KRS 392.020.

Kentucky courts have historically refused to honor a testator's intentions when an intent to defraud the surviving spouse of his or her spousal interest is found⁴.

Kentucky case law has long held that assets which were not technically part of the decedent's estate may be used or "brought back into the estate" for the purposes of calculating the surviving spouse's statutory share. However, before KRS 392.020 would be used by a surviving spouse, there must have necessarily been a bequest, gift or transfer of assets of the decedent which substantially deprived the surviving spouse of his or her statutory share.

Justice Vanmeter, in a well-reasoned dissenting opinion in the underlying Court of Appeals decision, correctly pointed out that several Kentucky cases brought property back into the estate that were not actually part of the decedent's probate estate but which were transferred in fraud of the spousal share.⁵

⁴ See, Elizabeth S. Muyskens, Married in Kentucky: A Surviving Spouse's Dower Right in Personalty, Volume 96, Kentucky Law Journal, 99, (2007 – 2008) page 106., Citing, *Martin v. Martin*, 138 S.W.2d 509 (Ky. 1940); *Payne v. Tatem*, 33 S.W.2d 2 (Ky. 1930); *Goff v. Goff's Ex'rs*, 193 S.W. 1009 (Ky. 1917); *Fennessey v. Fennessey*, 2 S.W. 158 (Ky. 1886).(Appendix 14). This Note by Ms. Muyskens is included in the annotations to KRS 392.020.

⁵ *Harris v. Rock*, 799 S.W.2d 10 (Ky. 1990), certificates of deposit; *Benge v. Barnett*, 217 S.W.2d 782 (Ky. App. 1949), *gifts of personalty*; *Redmond's Adm'x vs. Redmond*, 66 S.W.745 (Ky. App. 1902) and *Petty v.*

Pursuant to KRS 392.020 the surviving spouse has an absolute right to one-half (1/2) of the personal assets and a one-half (1/2) interest in the real estate⁶. However, this claim **only** comes into play when and **if** the surviving spouse believes that he or she has been left less than his or her statutory share and chooses to make a claim under the statute. When the claim is made by the surviving spouse, a rebuttable presumption of fraud is created. Thereafter, a Court must find that the acts of the testator's transfer or disposition of assets constituted "intent to defraud" in order for the surviving spouse to prevail.

With its opinion in this case, the Court of Appeals has carved out an exception to KRS 392.020, the dower/curtesy statute, which will exempt life insurance from being challenged by a surviving spouse as a mechanism to commit fraud on the dower. Such an exception is contrary to KRS 392.020 and the Kentucky case law as set forth above.

**II. CHAOS WOULD NOT BE CREATED IN ESTATE PLANNING
NOR WOULD INSURANCE COMPANIES BE PLACED IN AN
UNTENABLE POSITION BY REINSTATING THE JUDGMENT OF
THE TRIAL COURT.**

The Appellee, Kiphart, argues that the Court of Appeals correctly held that insurance companies would be burdened if life insurance proceeds were considered for the purpose of calculating the statutory share of the surviving spouse when fraud on the dower has occurred. The Court of Appeals stated as follows, "We are of the opinion that to adopt the trial court's rationale would not

Petty 43 Ky. (4 B. Mon) 215 (1843), real property placed in another's name; and *Anderson v. Anderson*, 583 S.W.2d 504 (Ky. App. 1979) money deposited into a joint account with children.

⁶ In a testate death and the surviving spouse renounces the will, the surviving spouse takes one-third (1/3) of the fee simple real estate of the decedent. KRS 392.080.

only create chaos in the realm of estate planning but would also place insurance companies in an untenable position of honoring the contract of an insured in the face of a dower or curtesy claim by a surviving spouse.”⁷

It is difficult to conceive of a situation where an insurance company would be placed in “. . . [A]n untenable position of honoring the contract of an insured in the face of a dower or curtesy claim by a surviving spouse.” The recipient of the bequest or inter vivos transfer is subject to the spouse's claim if fraud occurs, not the insurance company or other payor of the asset. In this case, the insurance companies which paid the benefit on Carole Bays' policies were not parties to the litigation and were not exposed to any claims as a result of the litigation. The fact that there is sparse case law dealing with spousal claims regarding personalty is further testament that litigation would not be generated by this Court upholding the Knox Circuit Court's Judgment.

The application of KRS 392.020 to the inter vivos transfer of any assets owned and controlled by a testator has not been used by Kentucky Courts to nullify or void the transfer. However, this statute has been applied when such inter vivos transfers leave the surviving spouse with less than his or her statutory share of those assets and a proper and timely action was thereafter initiated by the spouse. Even after such an action has been filed by the surviving spouse seeking his/her spousal share, the fraudulent transfer of the testator is not voided but rather the transferee is subject to the statutory claim of the spouse. (See, KRS 392.070).

⁷ Opinion of the Court of Appeals, Appendix 1, to Appellant Brief to Supreme Court.

This case is not about the decedent's authority to change the beneficiary on her life insurance policies. She had that right. However, when she makes such a change to the detriment of her spouse, KRS 392.020 provides a remedy for him.

Life insurance is an asset like any other personal asset owned by the decedent spouse and does not hold some special protection or status⁸ in the event that a surviving spouse seeks his or her statutory share, pursuant to KRS 392.020. Life insurance should not be immune from being challenged by the surviving spouse when fraud on the interest of the surviving spouse has occurred. Life insurance may not be part of the liquid assets at the time of death but it is an expectation of the proceeds of the estate and is frequently used in estate planning to fund potential taxes as well as other estate expenses.

With respect to concerns about estate planning, practitioners are normally cautious when advising clients about large transfers of personal property to individuals other than their spouse because of the prohibition of doing so by KRS 392.020. It is seldom that this scenario ever arises. In this case, the attorney who drafted the Trusts and Last Will of Carole Kiphart Bays was apparently well aware that the documents he drafted were contrary to the statutory rights of John Bays and of the potential statutory claims that Mr. Bays could assert.⁹ Cases

⁸ In his dissenting opinion, Justice Vanmeter characterized life insurance as "magic" because of the status given to it by the opinion of the Court of Appeals labeling it as a nonprobate asset. (Court of Appeals Opinion p. 21).

⁹ The drafting attorney included the following language in the Last Will and Testament of Carole Kiphart Bays at page 8 "The provisions made in this Will for my husband are in lieu of and a bar to dower and all statutory marital rights he may have in my estate." See Item III, Appendix 5 to Appellant Brief to Supreme Court. See also language he included in the Trust Agreement of Carole Kiphart Bays, "The

such as this are uncommon because spouses rarely bypass each other as beneficiaries unless they together have other plans for the use of the life insurance asset.

The case of *Farley v. First National Bank*, 61 S.W.2d 1059 (1933) is relied upon by the Appellee here as being dispositive of the issue of insurance proceeds not being subject to spousal interest. However, upon a close reading of *Farley* one clearly sees that it is most distinguishable from the case before this Court.

The primary issue of the appeal by the administrator of the estate of O.B. Farley and his widow was that the change of beneficiaries was in fraud of the rights of the insured's creditors and of the marital rights of his wife.

The *Farley* Court, in 1933, made its decision applying the then Sections 654 and 655 of the Kentucky Statutes which allowed ". . . [O]nly premiums on a life insurance policy paid by an insured in fraud of creditors . . . may be recovered as an asset of his estate." (Id. p. 1061). Presently, KRS 304.14-340 protects against fraud on creditors by the payment of insurance premiums.

The *Farley* Court further stated, "The right of the insured to make the change is absolute ***unless equities have intervened, which is not the case here . . .***" (emphasis ours). Clearly, unlike the present case, in *Farley* there was not a claim of fraud on the spousal share as contemplated by KRS 392.020 which provides an equitable remedy.

provision made in this Trust for the Settlor's husband are in lieu of and a bar to dower and all statutory marital rights he may have in the Settlor's estate. " See Article XX, page 12, Appendix 12 to Appellant Brief to Supreme Court.

The Appellees belief that upholding the Trial Court's judgment would be problematic and have widespread consequences is simply conjecture. For all of the reasons set forth hereinabove, the Appellee's concerns about Kentucky being at odds with law in other jurisdictions, creating uncertainty in the law, the generation of litigation, overruling prior decisions, subjecting life insurance policies to the claims of creditors, damaging the interests of surviving spouses and placing a burden on life insurance companies are unfounded.

The rationale set forth in the Trial Court's Judgment, when applied to the proceeds of life insurance death benefits, would only come into play when, as here, there is unrebutted proof presented of fraud on the spousal interest.

CONCLUSION

For all of the reasons set forth above the Appellant, John Wesley Bays, respectfully requests this Court to reverse the opinion of the Court of Appeals entered on March 21, 2014 with directions to reinstate the Judgment of the Knox Circuit Court entered December 21, 2011.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "W. Patrick Hauser", is written over a horizontal line. The signature is enclosed in a large, hand-drawn oval.

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