

Commonwealth Of Kentucky

Court of Appeals

NO. 2003-CA-001818-MR

LOU MAY RICHARDSON

APPELLANT

v. APPEAL FROM MARION CIRCUIT COURT
HONORABLE ALLAN RAY BERTRAM, JUDGE
ACTION NO. 02-CI-00057

JULIANNE MAY YOUNG; PHIL M. ORR, JR.;
SAM C. MAY; PHILIP S. GEORGE, JR.,
CONSERVATOR FOR SAM C. MAY;
MANEESSE WALL; CHARLES ORR; CHRISTIE
ORR; CLAYTON ORR; AND BUENA
VISTA, LLC.

APPELLEES

AND

NO. 2003-CA-001848-MR

PHIL M. ORR, JR.; CHARLES ORR;
CHRISTIE ORR; CLAYTON ORR;
AND BUENA VISTA, LLC.

APPELLANTS

v. APPEAL FROM MARION CIRCUIT COURT
HONORABLE ALLAN RAY BERTRAM, JUDGE
ACTION NO. 02-CI-00057

LOU MAY RICHARDSON;
JULIANNE MAY YOUNG;
SAM C. MAY, PHILIP S.
GEORGE, JR., CONSERVATOR
FOR SAM C. MAY; AND
MANEESSE WALL

APPELLEES

AND

NO. 2003-CA-001849-MR

BUENA VISTA, LLC.

APPELLANT

v.

APPEAL FROM MARION CIRCUIT COURT
HONORABLE ALLAN RAY BERTRAM, JUDGE
ACTION NO. 02-CI-00057

LOU MAY RICHARDSON; PHIL M.
ORR, JR.; JULIANNE MAY
YOUNG; SAM C. MAY; PHILIP S.
GEORGE, JR., CONSERVATOR FOR
SAM C. MAY; MANEESSE WALL;
CHARLES ORR; CHRISTIE ORR;
AND CLAYTON ORR

APPELLEES

OPINION
AFFIRMING

** ** * * *

BEFORE: SCHRODER, TAYLOR, AND VANMETER, JUDGES.

SCHRODER, JUDGE: These appeals were consolidated to determine whether the trial court erred in determining the May family assets should be managed through trusts rather than through a limited liability company. The court's ruling had undesirable tax consequences to the estate. Unfortunately for the estate, the trial court rulings were correct, therefore we affirm.

The facts of this case are worthy of an academic discussion on estate planning and on trusts. In 1991, Sam and Julia May each created revocable living (*inter vivos*) trusts with essentially identical provisions. Although revocable and

amendable by the settlor, amendments affecting the powers and duties of the trustee(s) had to be approved in writing by the trustee(s). Each trust provided for two separate funds. Fund A was what is commonly known as a "marital trust" for the benefit of the surviving spouse during his or her lifetime. Fund B was a "credit shelter trust", which was intended to contain a sum equal to the largest amount that could pass free of federal estate tax by reason of the unified credit, subject to certain adjustments. When the marital trusts were created, Sam and Julia May were identified as the trustees of their respective trusts. Thus, Sam May was the initial trustee of his trust, and Julia May was the trustee of her trust. The trusts provided that upon the death of the trustee, the surviving spouse would become the successor trustee. The May's three daughters, Lou Richardson, Julianne Young, and Martiele Orr were appointed successor trustees, in the event of their parents' inability or desire not to act as trustee.

The beneficiary of Fund A was the surviving spouse during his/her lifetime, with the power to consume both the income and principal. The surviving spouse also had a power of appointment that permitted him/her to transfer any or all assets of Fund A to anyone, including his/her estate. Upon the death of the surviving parent, the trust property (A and B) passed to the three daughters, per capita, or their heirs, per stirpes.

One half of each beneficiary's share was to be distributed in fee and the other half remained in trust, with income benefits payable quarterly, with the power to consume the principal for the health or education of said children or their children per stirpes upon the death of the settlors' children.

Following the creation of the May Trusts, the following events occurred:

1. On November 30, 1993, Sam and Julia May each amended their respective trusts to provide that if their three daughters were called upon to act as their successor co-trustees, approval of two of the three of them was required for the successor co-trustees to act on any matter;

2. On December 29-30, 1994, Sam and Julia May each amended their respective trust so as to name their three daughters, rather than each other, as their immediate successor co-trustees. In the same instruments, Sam and Julia May resigned as trustees of their respective trusts. Although these amendments were signed by both Martiele Orr and Lou Richardson, Julianne Young did not sign either amendment;

3. On March 9, 1995, Sam and Julia May amended their respective trusts, again noting their resignation and their three daughters as their immediate successor co-trustees. The effect of this amendment was to delete the requirement of the November 30, 1993, amendment that allowed two of the three co-

trustees to act (thereby requiring consent by all three for exercising a power). Julianne Young agreed to this March 1995, amendment and agreed to serve as a trustee. However, Martiele Orr and Lou Richardson never signed the March 1995, amendment. Thereafter, none of the daughters exercised any control over the trusts or the assets of the trusts.

4. Julia May (a settlor) died on March 24, 1998, and her husband, Sam May, became the executor of her estate.

5. In September of 1998, Sam May signed a disclaimer of all his rights to Julia May's Trust Fund A, and disclaimed his general power of appointment. Said disclaimer was filed with the probate court. Within two weeks, Sam May and his counsel decided that the first disclaimer contained fundamental errors which essentially defeated the entire intent of Sam and Julia May's estate planning. As a result, Sam May executed a second disclaimer on October 9, 1998. The second disclaimer differed from the first in that Sam May did not "specifically disclaim either the remaining principal of Fund A of the Julia C. May Trust or his general power to appoint any assets of Fund A remaining at his death." This second disclaimer was filed in the probate court on October 13, 1998.

The events which gave rise to this action began on October 27, 1999. Sam May created a limited liability company, Buena Vista, LLC. The operating agreement of that company,

which was executed on the day the company was formed, identified Sam May as the sole member and named Martiele Orr and Lou Richardson as the managers. Two days later, on October 29, 1999, pursuant to a power of appointment, Sam May transferred the assets within the Julia C. May Trust, and particularly an Advest brokerage account which was in Fund A of the Julia C. May Trust, to Buena Vista, LLC. On the same day, Sam May also transferred title to two farms which were held in the Sam C. May Trust to Buena Vista, LLC. Five days later, on November 4, 1999, Sam May transferred his entire interest in Buena Vista, LLC to his three daughters in equal shares.¹

Martiele Orr passed away in April 2000, and Phil M. Orr, Jr. was appointed her executor. Sam May's health began to fail, and on October 26, 2001, Philip S. George, Jr. was appointed as Sam May's conservator.

Two months later, in December 2001, Julie Young for the first time attempted to act as a trustee with respect to her parent's assets, specifically attempting to get the Advest accounts transferred to her mother's trust. Those efforts caused Philip Orr and Lou Richardson to file a declaratory judgment action against Julie Young, and Buena Vista, LLC was joined as a third party defendant. The heart of the controversy

¹ Either way, the three daughters, or their heirs, end up with the assets. The decision affects the tax consequences and whether any of the assets are subject to the trust restrictions.

was whether or not Sam May had the right to direct the transfer of assets from Fund A of the Julia C. May Trust by power of appointment to Buena Vista, LLC, on October 29, 1999, which he did as trustee of the Julia C. May Trust on October 30, 1999; and whether he was the trustee of the Sam C. May Trust when he executed the deed conveying real property to Buena Vista, LLC on October 29, 1999.

The circuit court granted partial summary judgment which was entered on April 11, 2003. The circuit court analyzed the events and concluded that:

The power of appointment granted to Mr. May does not permit *inter vivos* exercise thereof. To the contrary, Mr. May was permitted to exercise the power of appointment granted under Paragraph 5.4 of the Julia C. May Trust Agreement only in his Will. Therefore, Mr. May's purported exercise thereof on October 29, 1999, and October 30, 1999, to transfer all of the securities contained in Fund A of the Julia C. May Trust to Buena Vista, LLC and his own Trust was clearly unauthorized and without legal effect.

Furthermore, Mr. May's efforts to make an *inter vivos* exercise of that power of appointment also fail because he specifically and irrevocably disclaimed his right to exercise that power of appointment under his First Disclaimer.

and

Upon the execution and filing of his First Disclaimer, Mr. May no longer had the right to withdraw from Fund A of the Julia C. May Trust or to testamentarily appoint assets of Fund A at his death. Although Mr.

May filed a Second Disclaimer approximately twenty (20) days later which did not include the provisions of paragraph 7 of his First Disclaimer, the Second Disclaimer did not have the effect of revising, revoking or amending the First Disclaimer. . . .

and

It is clear that Mr. May is not the Trustee of the Sam C. May Trust and has not been the Trustee since his resignation as Trustee on December 30, 1994. At that time he substituted his three daughters as successor Co-Trustees. He affirmed that resignation on March 9, 1995. Therefore, Mr. May was without legal authority to convey the Brady Farm and the Ellis Farm from the Sam C. May Trust to Buena Vista, LLC on October 29, 1999.

and

The 1995 Amendment affirmed Mr. and Mrs. May's resignation as Trustees.

and

It is fundamental trust law that the settlor may amend the Trust he or she created so long as the Trust Agreement expressly reserves to the settlor the power of amendment. Therefore, where pursuant to paragraph 2.1 of the Trust Agreements, Mr. and Mrs. May expressly reserved the right to amend the Agreements, they were perfectly within their rights to do so without approval of their three daughters. In this light, there is no question that the 1993 Amendments were fully effective. Although paragraph 2.1 of the Trust Agreements restrict the settlor's ability to alter the "compensation, powers or duties" of the Trustee without the Trustee's written approval, on November 30, 1993, Mr. and Mrs. May were acting as the Trustees of their respective Trusts and executed the

Amendments both individually and as Trustees.

and

The Trust Agreements themselves require no formality on the part of the successor Trustees in the acceptance of their appointments. In fact, the acceptance of the trust by a trustee is ordinarily presumed until the trustee declines the position. Therefore, the lack of Young's signature on the 1994 written resignation by Mr. and Mrs. May does not render the resignations ineffective. To the contrary, the signatures of Richardson and Martiele on the 1994 Amendments and Young's signature on the 1995 Amendments is potent evidence that all three daughters knew of their parents' resignations and that each willingly accepted their office as a successor Co-Trustee.

and

After his resignation as Trustee of the Sam C. May Trust on December 30, 1994, Mr. May was wholly lacking in authority to thereafter execute the duties of Trustee. Therefore, he had no legal authority to execute a deed on October 29, 1999, some four years after his resignation, purporting to transfer the Brady Farm and the Ellis Farm from the Sam C. May Trust to Buena Vista, LLC.

Having concluded that Sam May was acting as trustee without authority, the trial court attempted to undo each of his transfers since his resignation as trustee, and to void the transfers pursuant to the testamentary power of appointment, and imposed a constructive trust on the assets in order to transfer all of the assets back to their respective trusts. Lou

Richardson, filed the first appeal, followed by Phil M. Orr, Jr., the Orr heirs, and Buena Vista, LLC. A third appeal was filed by Buena Vista, LLC. By Order entered January 15, 2004, these appeals were consolidated.

On appeal, appellants contend the trial court erred in deciding that: the attempted resignations of the parents were effective, even though the successor trustees did not accept the appointments; Sam May's first disclaimer of interest could not be amended in the face of a clear mistake; and that the various transfers of assets to Buena Vista, LLC were invalid.

Appellants remind us that regardless of our decision, the beneficiaries remain the same. However, the tax consequences motivate this appeal.

The first issue, the attempted resignation of the trustees and the acceptance by the successor trustees, is actually two issues. Neither the December 29-30, 1994, resignations nor the March 9, 1995, resignations were contingent upon the successor trustees accepting the positions. Neither did the trust agreements require such a result. To the contrary, the trust agreements dictate how a trustee is to resign and how to select successor trustees, including successor trustees when a trustee does not accept. Paragraph 9 of the trust agreements provides:

P. Resignation of Trustee. To resign at any time by giving written notice, specifying the effective date of resignation to those specified in the following order: (1) to a Co-Trustee who will then either serve alone or a successor will be appointed as provided herein; (2) to a successor Trustee if one is named herein or has otherwise been selected; (3) to me; (4) to the advisory committee if one is named herein and then active; (5) to the then current income beneficiary(ies) of the trust. Thereafter, if a successor Trustee needs to be appointed, the one or ones receiving notice will, by majority vote, appoint as successor Trustee an independent Trustee as such. . . .

Therefore, we agree with the trial court that Sam and Julia May effectively resigned with their written notice to themselves and the successor trustees with the December 29-30, 1994, resignations. Two of the daughters signed acceptances of their appointments as successor trustees. Julianne did not sign an acceptance, but she also did not disclaim the trustee position. Even if Julianne disclaimed the trustee position, the resignations of Sam and Julia May were not contingent and were effective according to the terms of the trust. See Saunders v. O'Bannon, 27 Ky. L. Rptr. 1166, 87 S.W. 1105 (1905).

Also, at this point, two of the three successor trustees accepted their appointments. Under the terms of the trust, if only two accept, or if only one accepted, the surviving trustee(s) are authorized to act. See also KRS 386.825. Julianne did not immediately accept or disclaim the

trustee position in writing. Therefore she would have a reasonable time to accept or disclaim her appointment.

The subsequent (March 9, 1995) resignation and amendments of the trusts had limited effect. The settlors had already resigned and successor trustees were appointed (and at least two out of the three accepted), so the subsequent resignations were a nullity. The attempted amendments (which would change the powers of the trustees to require unanimous consent of the trustees) were exercised according to the terms of the trust which allowed the settlors to amend at any time. The trust did however, require the trustees to accept amendments to changes in the powers of the trustees to become effective. See KRS 386.805. At this point, Julianne did sign the acceptance as a trustee, and acceptance of the change. The acceptance as a trustee was effective. However, the amendment to the powers of the trustee failed for a lack of a majority of trustees accepting the amendment. Per the terms of the trust, and KRS 386.825, a majority was needed to amend the trust to require unanimous consent of the trustees. Now, we have three trustees and a trust agreement that requires two out of three trustees to agree on any action, and a written notice requirement if a trustee resigns. There are no written resignations in the record.

Appellants' second allegation of error was that the trial court erred in finding Sam May's first disclaimer could not be amended. This argument relates back to Julia May's death. Sam was the designated beneficiary of Julia May's trust, Fund A, and a power of appointment. On September 23, 1998, Sam executed a disclaimer in which he irrevocably disclaimed all of his right, title and interest in certain nontestamentary property he received upon the death of Julia May, including his right to withdraw all or any portion of the remaining principal of Fund A of the Julia C. May Trust. Moreover, Sam May disclaimed his general power to appoint (under Article 5, paragraph 5.4) any of the assets of Fund A remaining at his death. The disclaimer, pursuant to KRS 394.035 (Uniform disclaimer of transfers under nontestamentary instruments), was filed with the Marion District Probate Court. Approximately 20 days later, October 9, 1998, Sam May attempted to amend his disclaimer by filing a second disclaimer, in which he did not disclaim the remaining principal of Fund A or the power of appointment in the Julia C. May Trust. Whether a disclaimer can be revoked or amended has not been addressed by either the General Assembly or a reported Kentucky case. However, the first disclaimer does contain language that it was made "in compliance with Section 2518 of the Internal Revenue Code of 1986, as amended," §2518(b) of the IRS code defines a

qualified disclaimer as "an irrevocable and unqualified refusal by a person to accept an interest in property. . . ."

(emphasis added). Also, the disclaimer itself provides (paragraph 6, 7, and 8) the disclaimer is irrevocable. Therefore, we agree with the trial court that the first disclaimer was irrevocable.

Appellants' next to last contention is that even if Sam May's disclaimer were binding, he still had authority, as trustee, to transfer the assets to Buena Vista, LLC, per paragraph 5.3 of the trust agreements (which provides that the trustee(s) can disperse principle to allow the beneficiary to maintain a certain standard of living). There are two problems with this logic. First, Sam May's transfer was as a trustee, which he was not (in either trust). Secondly, the attempted transfer was not to himself as a beneficiary, but to a third person - Buena Vista, LLC.

As part of their argument, appellants contend that even if Sam May lost all control over the Julia C. May Trust, he retained control over the Sam C. May Trust, and as settlor, he retained the right (under section 2.1 of the trust) to revoke or amend the trust and he could transfer the assets (two farms) in his trust to Buena Vista, LLC. Again, there are two problems with this logic. First, Sam May's transfer was as a trustee, which he was not. Secondly, an attempted transfer as a trustee

does not amount to a revocation of the trust by the settlor. Sam May could have revoked his trust as settlor and could have had the trustees transfer the assets back to him. Sam May could then have subsequently transferred those assets to Buena Vista, LLC. His attempt to transfer the assets directly to Buena Vista, LLC, as a trustee, did not revoke the trust. See Gamage v. Liberty National Bank & Trust Co., 598 S.W.2d 463, 464 (Ky.App. 1980). Therefore, the assets technically remained in the trust.

Appellants' final contention is that Julianne Young is estopped by her inaction to deny Sam May's trusteeship because she never took any action as a co-trustee until after her father was declared incompetent in October of 2001. This argument was not addressed in the partial summary judgment and we will not discuss it for the first time on appeal. Charash v. Johnson, 43 S.W.3d 274 (Ky.App. 2000)

Therefore, for the foregoing reasons, the judgment of the Marion Circuit Court is affirmed.

ALL CONCUR.

BRIEF FOR APPELLANTS
LOU MAY RICHARDSON, PHIL M.
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