



THE REPORTER

Published by the Kansas Bar Association • Real Estate, Probate, and Trust Law Section

President's Message

The torch has passed from Fred Farmer to me as president of the REPT Section. I look forward to serving as president and expect the section will continue to be active in its endeavors. The success of the committee the last couple of years has in large part been due to the efforts of Fred Farmer, and I would be remiss if I did not thank him for the outstanding leadership he has provided the section while serving as president. At the same time, there are a number of other executive committee members that have contributed in making this section one of the most active, and in my opinion, the best of the KBA. Cal Karlin steadfastly works as editor of the section newsletter and has graciously agreed to continue to serve in this capacity. Karlin is fortunate to have Mark Andersen and Dan Peare as contributing authors. If you do not read the newsletter, you are missing one of the section member benefits. Scott Jensen has agreed to serve as legislative liaison, and Dan will continue to serve as CLE liaison. If you have any suggestions on proposed legislation or CLE program ideas please pass it on to Scott or Dan.

A revision of the Kansas Estate Administration Handbook has begun in earnest. Nancy Schmidt Roush, editor emeritus, and Charles Andres and D. Michael Dwyer, co-editors, met at the KBA Annual Meeting with individuals who have agreed to be chapter authors to provide preliminary direction. This is a project that has been long overdue, and if all goes as expected, the new handbook should be published by Lexis Nexis in the spring of 2007.

Section President



Robert M. Hughes
Bever Dye LC,
Wichita

Finally, our section has always tried to keep its members informed regarding changes in the law in the areas in which we practice. I encourage all of us to become more active, whether it is by submitting an article to be published in the newsletter, suggesting new legislation, or becoming actively involved with the executive committee. One thing that all of us can do is to encourage our fellow lawyers that are not members of the KBA or this section to join. After all, it is the support that we receive from our members that allow us to provide CLE programs, newsletters, and sponsor legislation that helps all of us and our clients. ■

About the Author:

Robert M. Hughes practices in the areas of taxation, trusts and estates, wills, probate, asset protection, succession planning, and business planning. Hughes also represents individuals in the preparation of pre-marital and post-marital agreements. He is admitted to practice in the U.S. Supreme Court, 10th U.S. Circuit Court of Appeals, U.S. Tax Court, U.S. District Court for the District of Kansas and Kansas state courts.

Hughes is a member of the National Academy of Elder Law Attorneys and the Wichita Estate Planning Council. He frequently lectures on estate planning, asset protection planning, charitable tax planning, and will and trust drafting to other professionals and organizations.

He graduated from Washburn University School of Law, in 1982, and Southern Methodist University, Dallas, LL.M. in taxation in 1983. He received his undergraduate degree from the University of Kansas in 1978.

He is a member of the American, Kansas, and Wichita bar associations. He serves on the American Bar Association, Wichita Estate Planning Council, and National Academy of Elder Law Attorneys.

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He received his J.D. from the University of Kansas School of Law and his MBA and BBA in finance from Wichita State University (WSU).

He is a member of the KBA Executive Committee of the REPT Section and serves as the committee's liaison to the KBA Continuing Legal Education Committee. He is a member and past director of the Wichita Estate Planning Council and the Wichita Estate Planning Forum. He is on the WSU Foundation Board of Directors, where he serves as chairman of the Foundation's Giving Committee, and is a member of the National Advisory Council for WSU. Peare is also a member and past chairman of WSU Foundation's Planned Giving Professional Advisory Committee.

He provides a regular report on selected estate planning topics for the segment "Eye on Your Money," for KWCH-TV Channel 12, Wichita. Peare can be reached via e-mail at dpeare@hinklaw.com.

Estate Tax Notes

TAX CASES AND RULINGS AFFECTING THE ESTATE AND BUSINESS SUCCESSION PLANNER

ESTATE INCLUSION

1. P.L.R. 200604028 – WIFE'S ASSETS OVER WHICH HUSBAND HOLDS TESTAMENTARY GENERAL POWER OF APPOINTMENT INCLUDIBLE IN HUSBAND'S GROSS ESTATE

A husband and wife each have revocable living trusts they propose to amend. Under the amended trusts, the trustee would be directed to pay to the grantor such portion of the income and principal as the grantor may request. In addition, the trustee may distribute to either spouse so much of the income and principal to maintain them as nearly as possible in their accustomed manner of living. Upon the grantor spouse's death, all assets other than personal property are to be distributed outright to the surviving spouse. If the surviving spouse disclaims the assets, they will be held in trust for the surviving spouse's benefit. During that time the surviving spouse would be entitled to quarterly distributions of income and discretionary distributions of principal for health, education, maintenance, and support. Upon the death of the second spouse, the remaining assets would be held in trust for their children until the youngest child attains the age of 25. The wife's trust would also provide that if she is living at the time of her husband's death, he would have a testamentary general power of appointment equal to his remaining applicable exclusion amount less the value of his taxable estate. The husband proposes to execute a new last will and testament under which he will exercise the testamentary general power of appointment granted to him under the wife's trust.

The IRS held that if the husband predeceases the wife, the value of the wife's trust assets over which the husband holds a testamentary general power of appointment will be included in the husband's gross estate. Further, on the death of the husband during the wife's lifetime, if the husband exercises the testamentary general power of appointment, the wife will be treated as relinquishing her dominion and control over the property. Accordingly, on the death of the husband during the wife's lifetime, if the husband exercises the power of appointment, the wife will be treated as making a completed gift to the husband under Code Section 2501,

which will qualify for the federal gift tax marital deduction under Code Section 2523. The husband will then be treated as the owner of such appointed assets, so the wife will not be treated as making gifts to the beneficiaries of the husband's trust.

2. P.L.R. 200617008 – LIFE INSURANCE POLICY ON WIFE'S LIFE NOT INCLUDED IN WIFE'S GROSS ESTATE UNDER CODE SECTIONS 2042(O) OR 2035(A)

A husband created an irrevocable trust, the terms of which provided for discretionary distributions to his wife and issue during his lifetime. Following the husband's death, a percentage of the trust corpus will be used to create Trust A for the benefit of the wife, and the balance of the assets will be distributed to the husband's then-living issue. With respect to Trust A, the trustees are directed to pay to the wife the entire net income and may make discretionary distributions of principal. Trust A will terminate upon the wife's death, and the remaining corpus will be distributed to the husband's then-living issue. The trust provides that if any person currently eligible to receive distributions of principal or income is acting as a trustee, such trustee shall have no power to make or participate in making decisions involving the disposition of income or principal to himself or herself. Following the husband's death, the wife and the husband's father are co-trustees of Trust A. The wife proposes to resign as co-trustee. Following the resignation, the father will apply for and purchase a policy of life insurance on the wife's life. Trust A will be the owner and beneficiary of the policy, and the principal of Trust A will be used to pay the premiums on the policy.

Under the facts presented, the IRS held the wife would never possess or have the power to exercise any incidents of ownership in the policy to be acquired by Trust A, or would she relinquish or transfer any incidents of ownership in the policy by resigning as co-trustee prior to the acquisition of the policy. In addition, the wife had not transferred any assets to Trust A, and she would not pay any premiums with respect to the policy to be held as an asset of Trust A. Accordingly, the IRS concluded that the proceeds of the life insurance policy to be acquired by Trust A would not be includible in the wife's gross estate under Code Section 2042(2) and would not be includible under Code Section 2035(a) if the wife died within three years of resigning as co-trustee.

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GENERATION SKIPPING TRANSFER (GST) TAX

3. P.L.R. 200618004 – COURT’S CONSTRUCTION OF TRUST AGREEMENT DOES NOT DEPRIVE TRUSTS OF GRANDFATHERED EXEMPTION FROM GST TAX, DOES NOT RESULT IN TAXABLE GAIN TO TRUST BENEFICIARIES

The grantor created a revocable inter vivos trust that became irrevocable upon his death, a date prior to Sept. 25, 1985. At his death, the trust assets were divided into two equal shares, Trust 1 and Trust 2, one for each of his children. The two children and a bank serve as the co-trustees of each trust. No contributions have been made to the trusts since the grantor’s death.

Upon formation of the revocable trust, the grantor transferred shares of stock to the trust. The company’s stock is divided into two classes: Class B voting and Class A nonvoting. Shares of Class B voting stock are not readily marketable but are convertible into shares of publicly traded Class A at the ratio from time to time determined by the company. A dividend may be declared on the Class A shares and not on the Class B shares. However, if a dividend is declared on the Class B shares, the Class A shares are automatically entitled to a dividend at a significantly reduced rate. The trust agreement states the purpose of the trust is to create and preserve unified ownership and control of the company and requires the trustees to maintain and preserve ownership of all the Class B stock.

The child beneficiary of each trust will receive the income from his or her trust quarterly. The beneficiary may withdraw all of the trust principal other than the Class B stock. Upon the death of a beneficiary, the remaining trust principal other than the Class B stock will be distributed as its beneficiary appoints by will. The Class B stock and any unappointed assets will be further held in trust for the beneficiary’s spouse and then for the benefit of the child’s children. Each trust must terminate on the first to occur of the sale or other disposition of all of the company’s stock, or the expiration of 21 years after the death of the survivor of all of the grantor’s descendants who were living at the grantor’s death. Each of the two trusts holds 38 percent of the Class B stock. The administrative expenses of each trust routinely exceed the income produced by the Class B stock. Because the trust agreement prohibits the sale or disposition of the Class B stock, the trusts have insufficient assets to pay expenses, including the compensation of the corporate trustee.

The grantor’s two children have agreed on a plan to generate the cash needed to pay trust expenses, and the court has approved the plan and construed the trust agreement to allow the sale of Class B stock pursuant to the plan in order to pay the trusts’ routine expenses while advancing the trusts’ purpose of preserving unified and centralized control of the company within the grantor’s family. An appeals court held that the lower court’s construction of the trust agreement was a sound reflection of the grantor’s intent, and the state supreme court denied a petition for appeal.

Under the plan, the trustees would periodically determine the amount of the excess expenses of each trust and the smallest whole number of Class B shares that if converted to Class A shares and sold on the open

market would generate enough cash to pay the expenses. The trusts, however, must at all times own in the aggregate at least 51 percent of the then outstanding Class B shares. Two voting shares would be created under the plan. Prior to conversion of any Class B shares, the beneficiary of each trust and that beneficiary’s descendants would have the option of purchasing voting trust certificates representing beneficial ownership interests in the Class B shares. Upon exercise of such option, the option holder would transfer consideration into his or her respective voting trust. Consideration for the shares could consist of Class A shares or cash. The trustees of the voting trusts would always be the same as the trustees of the trusts created under the trust agreement, and they would be required to vote the Class B shares held in the voting trusts in the same manner as the trustees voted the Class B shares held in the trusts created under the trust agreement. Class B shares would be converted as necessary to pay expenses, in the event they are not transferred to a voting trust, and the Class A shares will be sold as needed to pay trust expenses. Excess proceeds from the sale of Class A shares would be reserved for payment of future trust expenses and could not be distributed to the beneficiary.

The IRS recognized that the inability of the trusts to pay trust expenses expressly authorized by the trust agreement without violating the express prohibition against selling Class B shares presented a bona fide issue to be resolved by a court. It held that the court’s construction of the trust agreement was consistent with the applicable state law. Accordingly, the construction of the trust agreement and the implementation of the proposed funding plan would not cause the trusts to lose their status as exempt from the GST tax. The IRS further held that because the proposed construction of the trust agreement and implementation of the funding plan would not change the interests of the beneficiaries, no transfer of property would be deemed to occur that would result in gift tax liability. Further, the proposed construction of the trust agreement would not result in a disposition event for purposes of Code Section 1001 and would not result in the recognition of gain or loss to the trusts or their beneficiaries. Because there would be no gain or loss recognition, the basis and holding period of the trusts’ assets would remain the same after the construction as before.

GIFT TAX

4. P.L.R. 200612002 – TRANSFER TO TRUST INCOMPLETE GIFT DUE TO RETAINED POWERS

The taxpayer created and funded an irrevocable trust during his lifetime. Under the terms of the trust, the class of beneficiaries eligible to receive distributions during the taxpayer’s lifetime were the taxpayer, the taxpayer’s sibling, the taxpayer’s descendants, a third-party individual, and a named private foundation. Distributions to any such persons were to be made in such amounts and in such proportions as appointed by unanimous agreement of the power of appointment committee, or by unanimous agreement of the taxpayer and one member of the power of appointment committee. The taxpayer’s sibling and a descendant of the taxpayer were named the initial members of the power of appointment committee. If either ceased serving during the taxpayer’s lifetime, the third-party individual

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NEWSLETTER

To be successful and informative, a section newsletter needs articles or ideas that reflect the needs of its membership. If you would like to contribute to the newsletter, contact Calvin J. Karlin at ckarlin@barberemerson.com.

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would become successor on the power of appointment committee. In the event of any other vacancy during the taxpayer's lifetime, the eldest living descendant of the taxpayer not already serving would become successor on the power of appointment committee. The terms of the trust directed the exercise of the power to appoint trust assets by a member of the power of appointment committee was to be exercised only in a nonfiduciary capacity. Upon the taxpayer's death, the taxpayer had a broad limited power to appoint any remaining trust assets. In the absence of appointment, the private foundation was to receive the lesser of 10 percent or \$2 million. The balance was to be divided into separate, equal shares for the taxpayer's spouse, if living, each living child of the taxpayer, and the collective descendants of any child of the taxpayer not then living.

The IRS first held that the taxpayer would not be treated as the owner of any portion of the trust under Code Sections 673, 674, 676, or 677. However, the IRS stated the issue of administrative controls under Code Section 675 was a question of fact, the determination of which must be deferred until the federal income tax returns of the parties involved had been examined by the office with responsibility for such examination. The IRS next ruled the taxpayer's transfer of property to the trust would not be a completed gift subject to the federal gift tax because of the taxpayer's retained testamentary limited power of appointment and the taxpayer's lifetime power to appoint assets to himself with the consent of one member of the power of appointment committee. The IRS noted the members of the power of appointment committee were individuals who would not have a substantial adverse interest in the disposition of the transferred property for purposes of Code Section 2511. The taxpayer would be treated as making a taxable gift at such time as trust assets were distributed to persons other than the taxpayer, or if, during the taxpayer's lifetime, he released the testamentary limited power of appointment. Finally, the IRS held the members of the power of appointment committee would not be treated as having a general power of appointment, because their power to appoint assets to themselves could be exercised only with the consent of the other. Accordingly, the members of the power of appointment committee would not be treated as making a taxable gift if trust assets were distributed to the taxpayer under the terms of the trust.

5. *ESTATE OF FOCARDI v. COMM.*, T.C. MEMO 2006-56 – SPOUSAL INTERESTS IN GRANTOR RETAINED ANNUITY TRUSTS NOT QUALIFIED INTERESTS

In October 1996, the decedent transferred 817,500 shares of Great Bay Distributors Inc. into a two-year grantor retained annuity trust (GRAT). On the same day, he transferred another 817,500 shares in the same company to a four-year GRAT. The two GRATs were identical in all material respects, except for the annuity term and the percentage used to calculate the amount of the first annuity payment. Each GRAT provided that during the term of the respective GRAT, the trustee was to pay to the decedent an amount equal to a percentage of the initial fair market value of the assets contributed to the trust as finally determined for federal tax purposes (51.2535 percent for the two-year GRAT and 22.9876 percent for the four-year GRAT). The annuities were to increase by 20 percent each year during the annuity terms. If the decedent died prior to expiration of the annuity terms, the trustee would pay to his estate any part of the annuity accrued and undistributed at his death, based on a daily proration. In the event of the decedent's death prior to expiration of the annuity terms, his wife (provided she survived the decedent) was to receive the remaining annuity amounts for the balance of the annuity terms unless the decedent revoked all or a portion of his wife's interest under the GRATs. If his wife failed to survive him, or if the decedent revoked her interest, the assets were to be distributed as the decedent appointed by will. In the absence of appointment, the assets were to be distributed to his estate. Upon expiration of the annuity terms, the remaining trust assets were to be distributed outright to the decedent's children, in equal shares. In the event a child was not then living, such child's share would be distributed to his or her estate.

On his 1996 federal gift tax return, the decedent calculated the value of the gifts by reducing the value of his transferred shares by the actuarially determined value of a two-life annuity under Code Section 7520 for himself and his wife. However, the IRS determined the value of the gifts must be calculated by reducing the value of the decedent's transferred shares by the value of a single-life annuity based on the decedent's life and determined a gift tax deficiency.

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In general, the value of a gift in trust where the donor retains an interest in the property is the value of the property transferred less the value of the donor's retained interest. However, when the gift in trust is to a family member, the value of the gift must be determined by reference to Code Section 2702(a)(2), which provides that the value of a retained interest that is not a qualified interest is zero, resulting in a gift of the entire property transferred. A qualified annuity interest is generally a qualified interest under Code Section 2702, but the qualified annuity interest must fix the term of the annuity interest for the life of the term holder, for a specified term of years, or for the shorter of those periods. The IRS argued the spousal interests at issue were not qualified interests, because the spousal interests were contingent on the grantor's failing to survive the applicable GRAT term, meaning the interests were not fixed and ascertainable, and the spousal interests were not payable for the life of the term holder, for a term of years, or for the shorter of those periods. It argued the decedent's retained annuity was a qualified interest to the extent payable for a term of years or the decedent's earlier death, but not to the extent it continued for the surviving spouse for the remainder of the term or until the surviving spouse's earlier death. The decedent's estate argued the spousal interests were qualified interests in that they were fixed and ascertainable interests existing for a specified term of years, for the life of the term holders, or for the shorter of the two.

The court agreed with the IRS that the spousal interests at issue were not qualified interests, stating the decedent's wife would have received no payments from the GRATs had the decedent survived the GRAT terms. As a result, the spousal interests were not fixed and ascertainable upon the inception of the trusts as required by the treasury regulations.

The estate alternatively argued language contained in the trust agreements whereby no power, right, or duty contained under the trust agreement would be effective or exercisable to the extent it would cause the decedent's retained annuity interest, or his wife's interest, if any, to fail to qualify as a qualified annuity interest under the Code operated to invalidate the spousal interests in the GRATs, because they were not qualified interests. The estate concluded the GRATs were each for a term of years and should be treated as such. However, the court rejected the argument, stating the estate was not entitled to treat each GRAT as one for a term of years simply because the terms of the GRATs stated the court's determination that the spousal interests were not qualified interests essentially meant the spousal gifts were revoked. Such a savings clause, the court held, was ineffective for federal transfer tax purposes.

6. P.L.R. 200617002 – UNAUTHORIZED TRANSFER OF RESIDENCE FROM QUALIFIED PERSONAL RESIDENCE TRUST DOES NOT CREATE TAXABLE GIFT

The decedent and spouse each created a qualified personal residence trust (QPRT) and each conveyed a one-half interest in their personal residence to his or her respective QPRT. Each QPRT provides that if the grantor is unable to serve as trustee, the other spouse will become the successor trustee. If neither spouse is able to serve as trustee, one of their daughters will become the successor trustee. Under the provisions of each QPRT, until the first to occur of the eighth

anniversary of the creation of the QPRT or the death of the grantor, the grantor will be paid the net income of the QPRT at least annually, will be entitled to exclusive use of the residence, and will be required to pay all expenses relating to the residence. Upon expiration of the trust term if the grantor is then living, the trustee is to distribute the principal of each trust in equal shares to the grantor's then-living daughters.

Subsequent to creation of the QPRTs, the spouse developed severe health problems and became distressed over the loss of the residence upon termination of the QPRTs. Eight months prior to expiration of the eight-year term of each QPRT, the decedent and spouse executed deeds conveying the interests in the residence held by their respective QPRTs to revocable trusts created by them. Their four daughters were not consulted, advised of, or aware of such actions and did not become aware of the conveyances until several years later when the parties began the process of selling the residence. The four daughters, on the advice of counsel, made a demand against the decedent and spouse for the sale proceeds based on fraud, breach of fiduciary duties, and tortious interference with their interests in the residence. Subsequent to the closing of the sale of the residence and the demand, the proceeds had been held in escrow pending the determination of the rights of the parties and resolution of the conflict. The decedent subsequently died. To avoid the costs of litigation with the daughters, the decedent's estate and the spouse offered to deliver all of the proceeds of the sale to the daughters, in equal shares, in settlement of the matter. The daughters agreed to accept the sale proceeds in full settlement of all claims against the decedent's estate and spouse.

The IRS held the payment of the sales proceeds of the residence to the daughters in settlement of their claims that residence would not constitute a taxable gift by the spouse or the beneficiaries of the decedent's revocable trust or the beneficiaries of his estate. The IRS further held at the time of the sale of the residence, the daughters were the owners of the residence. Therefore, the gain on the sale of the residence should be reported by the daughters. Finally, the IRS held the basis of the residence in the hands of the daughters was determined by reference to its basis in the hands of the decedent and spouse and was used in determining the gain on the sale of the residence.

CHARITABLE GIVING

7. NOTICE 2006-15, 2006-8 I.R.B. 501 (02/03/2006) – IRS TO RECONSIDER SAFE HARBOR RULE REGARDING EFFECT OF STATE LAW RIGHT OF ELECTION ON QUALIFICATION OF CHARITABLE REMAINDER TRUSTS

The IRS previously issued Rev. Proc. 2005-24 (2005-16 I.R.B. 909), which provided certain safe harbor provisions to prevent the disqualification of a charitable remainder trust (CRT) in circumstances where a state law right of election could be satisfied from the assets of the CRT. Commentators asserted Rev. Proc. 2005-24 placed an undue burden on taxpayers and trustees seeking to comply with the safe harbor rule. Due to such adverse public comment, the IRS issued a Notice extending the June 28, 2005, grandfather date until it issues further guidance. Consequently, until further guidance is published, the IRS will disregard the existence of such a state law right of election, even without a waiver, only if the surviving spouse does not exercise the right of election.

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RETIREMENT BENEFITS

8. REV. RUL. 2006-26, 2006-22 I.R.B. (05/04/2006) – INCOME INTEREST QUALIFIED WHERE SPOUSE HAS POWER TO COMPEL WITHDRAWALS OF IRA INCOME

The IRS issued guidance regarding different circumstances under which a surviving spouse will be considered to have a qualifying income interest for life in an individual retirement account (IRA) or other qualified retirement plan where a marital trust is named beneficiary of such account. The decedent died in 2004, at age 68, survived by his spouse. Prior to death, the decedent established an IRA. The decedent's will created a testamentary marital trust (trust) funded with assets from his probate estate. Prior to death, the decedent named the trust as beneficiary of all amounts payable from the IRA after his death. The IRA is currently invested in productive assets, and the decedent's spouse has the right to compel the investment of the IRA in assets productive of a reasonable income. The executor of the decedent's estate elected to treat the IRA and the trust as qualified terminable interest property. Under the terms of the trust, all income is payable annually to the spouse for her life, and the spouse has the power, exercisable annually, to compel the trustee to withdraw from the IRA, an amount equal to all the income of the IRA for the year, and to distribute that income to the spouse. On the death of the decedent's spouse, the trust principal is to be distributed to the decedent's children who are younger than the spouse. No persons other than the decedent's spouse and children have a beneficial interest in the trust, including any contingent beneficial interest. The IRS determined the beneficiaries of the trust may be treated as designated beneficiaries of the IRA, and the IRA must be distributed over the spouse's life expectancy.

In Situation 1, the trust is governed by the laws of a state that has adopted a version of the Uniform Principal and Income Act (UPIA), including a provision authorizing adjustments between income and principal to fulfill the trustee's duty of impartiality between the income and remainder beneficiaries. With regard to a payment made from an IRA to a trust, the state law provides (i) if no part of the payment is characterized as interest, a dividend, or an equivalent payment, and all or part of the payment is required to be distributed currently to the beneficiary, the trustee must allocate 10 percent of the required payment to income and the balance to principal; and (ii) if no part of the payment made is required to be distributed from the trust or if the payment received by the trust is the entire amount to which the trustee is contractually entitled, the trustee must allocate the entire payment to principal. State law further provides that if in order to obtain an estate tax marital deduction (more of a payment must be allocated to income) the trustee is required to allocate to income the additional amount necessary to obtain the marital deduction. Accordingly, the trustee annually determines the total returns separately for the assets held in the trust (exclusive of the IRA, and for the assets held in the IRA) and determines the respective portion of the total returns allocated to principal and to income under state law. If the spouse exercises her withdrawal power, the trustee withdraws from the IRA the greater of the amount allocated to income or the required minimum distribution and distributes to the spouse the amount allocated to income of the IRA.

In Situation 2, the trust is governed by the laws of a state providing that if the trust instrument specifically provides or the interested parties consent, the income of the trust means a unitrust amount of 4 percent of the fair market value of the trust assets valued annually. In accordance with the state's statutes, all interested trust parties authorize the trustee to administer the trust and to determine withdrawals from the IRA in accordance with such provision. The trustee distributes an amount equal to 4 percent of the trust assets, exclusive of the IRA, to the spouse annually. If the spouse exercises her withdrawal power, the trustee withdraws from the IRA the greater of the required minimum distribution or the amount equal to 4 percent of the value of the IRA assets and distributes to the spouse at least the amount equal to 4 percent of the value of the IRA assets.

In Situation 3, the trust is governed by the laws of a state that has not adopted UPIA. In determining the amount of IRA income the spouse can compel the trustee to withdraw from the IRA, the trustee applies state law regarding the allocation of receipts and disbursements to income and principal, with no power to allocate between income and principal. The income of the trust is determined without regard to the IRA, and the income of the IRA is separately determined based on the assets of the IRA.

For each of the three situations, the IRS concluded the spouse had a qualifying income interest for life, because she had the power to unilaterally access all of the IRA income, and she annually received the income of the trust. The IRS further held the result would be the same if the terms of the trust directed the trustee to annually withdraw all of the income from the IRA and to distribute to the spouse at least the income of the IRA, rather than granting the spouse the power, exercisable annually, to compel the trustee to do so.

PARTNERSHIPS

9. ESTATE OF DISBROW V. COMM., T.C. MEMO 2006-34 – VALUE OF RESIDENCE TRANSFERRED TO FAMILY PARTNERSHIP INCLUDIBLE IN DECEDENT'S GROSS ESTATE

In December 1993, at almost 72 years of age, the decedent created a general partnership called Funny Hats (partnership). The partners were as follows: the decedent with a 28.125 percent interest; the decedent's only unmarried son, David, with a 14.375 percent interest; and the decedent's other four children and their spouses each with a 7.1875 percent interest. None of the partners contributed any asset to the partnership upon formation. The decedent later transferred her entire interest in her residence to the partnership for no consideration. On Jan. 1, 1994, the decedent gave her partnership interest to her children and their spouses, such that David had a 20 percent interest, and the decedent's other four children and their spouses each had a 10 percent interest. The partnership agreement stated the partnership was created to establish and conduct the business of real estate ownership and management. The only assets of the partnership were the residence and a checking account. The checking account had the following activities: \$69,250 of transfers from the decedent; a \$6,774 loan from the decedent; \$1,712 in interest; \$348,600 in proceeds from a sale of the residence to David at the end of 2000; contributions from each partner of \$1,000 and \$800 in 1995 and 1997, respectively; a contribution from David of

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Real Estate Cases

Kansas Supreme Court

CITY OF ROELAND PARK V. JASAN TRUST ET AL.

JOHNSON DISTRICT COURT

— AFFIRMED

NO. 94,897 — APRIL 28, 2006

Eminent domain and contracts

ATTORNEYS: Sherwin L. Epstein and Marcus G. Abbott, Sherwin L. Epstein & Associates, Kansas City, Mo., for appellant. W. Joseph Hatley and Melissa Hoag Sherman, Lathrop & Gage L.C., Overland Park, for appellee.

FACTS: City condemned shopping center for proposed redevelopment. District court apportioned condemnation award between fee owner of parcel of land (Jasan Trust) and leasehold interest (BCB). It then apportioned BCB's award between BCB and a subtenant (Payless), awarding Payless \$502,991 in damages for lost profits as provided in lease agreement. BCB appealed, arguing lost profits are not recoverable in Kansas condemnation action, and district court lacked jurisdiction to award lost profits. Appeal transferred to Supreme Court.

ISSUES: (1) Payment for lost profits out of condemnation proceeds and (2) jurisdiction

HELD: As general rule under Kansas law, a tenant is entitled to compensation if leasehold interest is damaged by exercise of eminent domain. However, parties are free to contract around eminent domain rules. Here, condemnation provision in lease agreement is clear and should be enforced as agreed upon, and Payless proved through expert testimony that it had suffered lost profits. District court correctly apportioned BCB's award to cover that loss. If various parties in interest cannot agree as to division of appraisers' award in condemnation proceeding, the court allocates the award pursuant to K.S.A. 26-517. District court had jurisdiction to apportion the award in accord with lease agreement.

STATUTES: K.S.A. 26-501 *et seq.*, -504, -513, -517

BOARD OF LEAVENWORTH COUNTY COMMISSIONERS V. WHITSON

LEAVENWORTH DISTRICT COURT

— AFFIRMED

NO. 95,193 — APRIL 28, 2006

Sexually violent predators, county zoning, and special use permits

ATTORNEYS: Gregory A. Lee, Cooper & Lee LLC, Topeka, for appellant. David C. Van Parys, county counselor, for appellee. C. William Ossman, Kansas Department of Social and Rehabilitation Services (SRS), for amicus curiae Secretary of SRS.

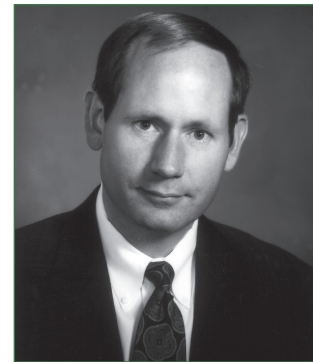
FACTS: Leroy Hendricks was in sexually violent treatment and moved into a house owned by the Whitsons' company. The Whitsons had contracted with SRS to provide housing for similar sexually violent predator treatment. When Hendricks moved into the residence, the Whitsons had neither obtained an SRS license nor a special use permit. The operation of a group home in Leavenworth County required a special use permit. The Board of County Commissioners of Leavenworth County (county) filed and obtained a temporary restraining order based on the Whitsons' failure to obtain an SRS license. After the Whitsons' obtained a license, they moved to vacate the restraining order. The county adopted a resolution adding an adult care facility, detention facility, or post release facility to the list of uses requiring a special use permit. The county filed for a permanent injunction based on the Whitsons' failure to obtain a permit. The district court granted the permanent injunction because the Whitsons failed to obtain a permit.

ISSUES: Did the county fail to provide evidence that county residents would suffer irreparable harm if injunctive relief was denied? Did the district court err in concluding that K.S.A. 12-736(e) did not apply? Is the county's resolution requiring a special use permit unconstitutional?

HELD: Court affirmed. The county presented evidence that Hendricks was a sexually violent predator. There was uncontroverted evidence that he was likely to re-offend if at large. Despite his reduced risk of re-offending because of his poor health and the structure and safeguards of the planned facility, the district judge implicitly determined the Board had made a sufficient showing of probability of irreparable injury when he granted the injunction it sought. Court held the district

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Author



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Andersen is admitted to the bar in Kansas and Missouri. Andersen is a fellow of the American College of Real Estate Lawyers and a member of the Kansas Society of Farm Managers and Rural Appraisers. His practice includes real estate, like-kind exchanges, and construction. Andersen can be reached via e-mail at mandersen@barberemerson.com.

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court did not abuse its discretion in granting the injunction. Court held K.S.A. 12-736(e) does not apply to group homes for disabled transitioning sexually violent predators. Court stated the Legislature could not have been more clear about its desire to incapacitate sexually violent predators when it enacted the civil commitment process. Court did not address the constitutionality of the county's resolution finding the district court had not relied on the resolution in granting the county's injunction.

STATUTES: K.S.A. 12-736(b)(1), (3), (c)(1), (2), (e) and K.S.A. 59-29a01 *et seq.*

CONCURRENCE: Justice Rosen concurred with the majority's conclusion that pre-existing Leavenworth county zoning regulations apply and affirmed the district court's decision enforcing those regulations.

**HAWLEY ET AL. V.
KANSAS DEPARTMENT OF AGRICULTURE
REPUBLIC DISTRICT COURT — REVERSED
NO. 93,690 — APRIL 28, 2006
*Water rights and abandonment***

ATTORNEYS: Brett W. Berry, Kansas Department of Agriculture, Division of Water Resources, Topeka, for appellant. Larry G. Michel, of Kennedy Berkley Yarnevich & Williamson Chtd., Salina, for appellees.

FACTS: In 1953, E.E. Conzelman obtained a permit from the Division of Water Resources, Kansas Department of Agriculture (DWR) to appropriate water for beneficial use from the Republican River through use of a pump and sprinkling system. Upon his death, Conzelman's son, Max, took over operation of the farmland subject to the water right. After Max's death in 2000, the water right passed to his daughter, Karen Hawley. In 2000, DWR asserted that according to water-use reports, the water right had only been exercised once in more than 40 years. In 2003, DWR initiated proceedings for abandonment and termination of Hawley's water right. A DWR hearing officer found no due and sufficient cause for the nonuse for 11 successive years (1959-1969) and for 31 successive years (1971-2001). The DWR hearing officer proposed an order of termination of water right. Hawley timely petitioned the secretary of agriculture for review based on lack of notice, but review was denied finding the DWR is not required to send notice to holders of water rights for which five or more successive years of nonuse had occurred prior to July 1, 1999. The district court entered judgment in favor of Hawley finding that compliance with the notice provisions of the termination statute was a condition precedent to an abandonment and termination proceeding, that the DWR had failed to provide Hawley with the required notice, and that the DWR's termination of Hawley's water right should be set aside.

ISSUE: Whether DWR erroneously interpreted K.S.A. 2005 Supp. 82a-718 when it concluded that one of the notice provisions of the statute, subsection (b), was not a condition precedent to termination of water right pursuant to subsection (a).

HELD: Court reversed. Court stated that the DWR's interpretation of the statute was correct and the decision declaring the Hawley's water right to be "abandoned and terminated" is affirmed. The district court's order reversing the decision of the hearing officer is reversed. Court held that under the fact of this case, the DWR was correct in not providing notice under K.S.A. 2005 Supp. 82a718(b) to holders of water rights who, without due and sufficient cause, had not beneficially used the water for 31 successive years.

STATUTES: K.S.A. 3-316; K.S.A. 2005 Supp. 8-1021; K.S.A. 20-3018; K.S.A. 21-3401; K.S.A. 2005 Supp. 21-3436(a), (b); K.S.A. 55-1,120(a)(3), (b)(2); K.S.A. 58-3935(a)(15); K.S.A. 60-236; K.S.A. 61-3101(b); K.S.A. 2005 Supp. 66-1,129a(d); K.S.A. 72-6433, -8801; K.S.A. 77-621(a)(1), (c)(4); K.S.A. 82a-701 *et seq.*, -702, -703a, -706a, -707(b), (c), -718; and K.S.A. 2005 Supp. 82a718(b), -1901(a), (b)

**BOTKIN V. SECURITY STATE BANK
SUMNER DISTRICT COURT — JUDGMENT OF THE
COURT OF APPEALS REVERSING THE DISTRICT
COURT IS AFFIRMED IN PART AND REVERSED IN PART.
JUDGMENT OF THE DISTRICT COURT IS REVERSED,
AND THE CASE IS REMANDED WITH DIRECTIONS
NO. 92,380 — MARCH 17, 2006**

Guaranty, statute of frauds, waiver, and public policy

ATTORNEYS: Martin J. Peck, Hyndman & Peck LLP, Wellington, for appellant. W. Thomas Gilman, Redmond & Nazar LLP, Wichita, for appellees.

FACTS: Security State Bank loaned money to Botkin. In return, 34 individuals and entities executed separate three-page guaranty agreements securing the loan. After Botkin defaulted on the loan, Botkin and the other guarantors filed a declaratory judgment action to determine whether their signed guaranty agreements were enforceable under the statute of frauds. The district court granted summary judgment to the guarantors finding the guaranties were incomplete and therefore unenforceable under the statute of frauds. The Court of Appeals reversed finding the guaranties satisfied the statute of frauds and that any escape of the guarantors from liability would not be consistent with the statute of frauds to prevent fraud and injustice.

ISSUE: Are the guaranties valid under the statute of frauds?

HELD: Court affirmed the Court of Appeals reversal. As a matter of law, Court held that some tension existed in the guaranty between liability to "my proportional ownership share" and "if no amount is stated, the Undersigned shall be liable for all indebtedness without any limitation to amount." Court held that because the parties did not leave blank the amount of the limitation on liability, but instead agreed that liability would be based upon the phrase the bank typed there, "my proportional ownership share," the parties' intent to limit liability is evident. Court strictly resolved any tension against the bank as drafter of the guaranty. Court clarified that its remand was only to determine what was meant by "my proportional ownership share." Court found the rest of the issues raised in the case were moot.

STATUTES: K.S.A. 33-106

**PANKRATZ IMPLEMENT CO. V.
CITIZENS NATIONAL BANK
RENO DISTRICT COURT — JUDGMENT OF THE COURT
OF APPEALS REVERSING THE DISTRICT COURT IS
AFFIRMED. JUDGMENT OF THE DISTRICT COURT IS
REVERSED AND REMANDED WITH DIRECTIONS
NO. 91,721 — MARCH 17, 2006**

Security interest and incorrect debtor's name

ATTORNEYS: John K. Pearson and J. Scott Pohl, Hinkle Elkouri Law Firm LLC, Wichita, for appellant. Charles D. Lee, Arlyn Miller, and John B. Swearer, Martindell, Swearer & Shaffer LLP,

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Hutchinson, for appellee. Mary Patricia Hess, Redmond & Nazar LLP, Wichita, amicus curiae for Kansas Bankers Association. Melissa A. Wangemann, legal counsel, deputy assistant secretary of state, amicus curiae for Kansas Secretary of State.

FACTS: Pankratz Implement Co. attempted to perfect its security interest in equipment sold to Rodger House. In filing with the secretary of state, Pankratz spelled the debtor's name as Roger House. Citizens National Bank later attempted to secure the same property using the debtor's correct name, Rodger House. Rodger House filed for bankruptcy; Pankratz obtained relief from the bankruptcy stay order and filed suit against Citizens in order to realize its security interest. The district court determined in accordance with recently enacted amendments to the Kansas Commercial Code that Pankratz was entitled to summary judgment because use of the debtor's incorrect name was a minor error and not seriously misleading. The Court of Appeals reversed, concluding that the use of the debtor's incorrect name was seriously misleading.

ISSUE: Whether the filing of a financing statement, which misspells the debtor's name is insufficient to render a filed financing statement seriously misleading under the Uniform Commercial Code (UCC).

HELD: Court affirmed the Court of Appeal's reversal of the district court. Court held that Pankratz failed to satisfy the requirement of using the correct name of the debtor and this did not satisfy the name requirements of the UCC. Nevertheless, minor errors will not destroy the effectiveness of that statement unless the errors make the statement seriously misleading. Court held that Pankratz's failing to meet the naming requirements is seriously misleading except in the case where a search using the debtor's correct name discloses the defective financing statement. In this case, it did not and therefore remains seriously misleading. Also, the Court found Pankratz failed to raise the issues in the trial court concerning the new revisions to the UCC and is precluded from raising it on appeal.

STATUTES: K.S.A. 2003 Supp. 84-9-101 *et seq.*, -9-502(a)(1), -9-503, -9-506, -9-705(c).

Kansas Court of Appeals

**BOARD OF JEFFERSON COUNTY COMMISSIONERS V.
ADCOX ET AL.**

**JEFFERSON DISTRICT COURT — AFFIRMED IN PART,
REVERSED IN PART, AND REMANDED**

NO. 94,894 — APRIL 28, 2006

Tax foreclosure, notice, and sheriff's sale

ATTORNEYS: Vernon L. Jarboe and Martha A. Peterson, Sloan, Eisenbarth, Glassman, McEntire & Jarboe LLC, Topeka, for appellants. Steven C. Montgomery, county counselor, for appellees.

FACTS: In January 2003, the Board of Jefferson County Commissioners filed a tax foreclosure action that involved delinquent real estate taxes on more than 200 parcels of land, two of the many owners were the Schrages and the Hummers. In the Schrages' case, Jefferson County officials relied upon service by publication after an attempt to personally serve the couple in Douglas County failed. The Schrages lived on the real estate tract in question and had been served with process seven times in the three years prior to the tax sale. In the Hummers' case, Terry Hummer was the president of RVH Inc, a corporation that was the title owner of the mobile home park in Jefferson County, but

the Hummers live in Topeka. Shawnee County officers tried twice to serve them at their Topeka home. Terry Hummer called the Shawnee County officers and advised that he or an employee would pick up the papers. An RVH maintenance worker received the foreclosure petition and summons at the sheriff's office after telling them he had been sent to pick up the papers. Both the Schrages' and the Hummers' property was sold at a sheriff's sale. The district court denied both the Schrages' and the Hummers' motions to set aside the sheriff's sale claiming they did not receive legally sufficient notice.

ISSUE: Legally sufficient notice of a sheriff's sale

HELD: Court affirmed in part, reversed in part, and remanded. Court reversed the district court's denial of the motion to set aside the sheriff's sale regarding the Schrages. Court held because the Jefferson County Sheriff's Department could have reasonably ascertained the Schrages' address, the publication of notice was insufficient and denied them due process of law. Regarding the Hummers, the court affirmed the sheriff's sale of their property. The court held the worker that Jerry Hummer sent to pick up the petition and summons was clothed with the apparent authority to receive process and that personal service was achieved in their case.

STATUTES: K.S.A. 60-260(b)(4), -304(e), -307(e) and K.S.A. 79-2804(b)

**R.H. GUMP REVOCABLE TRUST ET AL.
V. CITY OF WICHITA
SEDGWICK DISTRICT COURT — AFFIRMED
NO. 94,312 — APRIL 14, 2006**

Telecommunication towers and conditional use permit

ATTORNEYS: Robert W. Kaplan, Kaplan, McMillan & Harris, Wichita, for appellants. Joe Allen Lang and Jay C. Hinkel, assistant city attorneys, and Gary E. Rebenstorf, county attorney, for appellee.

FACTS: Gump filed a request seeking a conditional use permit to construct a "stealth flagpole" tower for use by Cricket Communications on the real property owned by Gump. The planning department found the proposed tower conformed to code and the Wireless Communication Master Plan and recommended approval of the conditional use permit subject to certain conditions. The planning commission and the District Advisory Board also recommended approval. The city council denied the conditional use permit finding overwhelming opposition, adverse visual impact, and eight other adverse factors. The district court remanded to the city council for clarification on the apparent finding that the council denied the permit based entirely on the aesthetic impact or visual impact of the tower. After further findings by the city, the district court concluded that the city could make its determination based on visual impact and aesthetics of the proposed tower and the city had balanced the benefits and harms.

ISSUES: (1) Sufficiency of the evidence, (2) open meetings, and (3) conditional use permit

HELD: Court affirmed. Court stated that while aesthetic considerations may not be as precise as more technical measures and must be carefully reviewed to assure they are not just a vague justification for arbitrary and capricious decisions, they may be considered as a basis for zoning rulings. Court found substantial evidence to support the city's denial of Gump's conditional use application, although reasonable persons might have found otherwise. Court rejected Gump's argument on open meetings. Court stated Gump does not dispute that it was able

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to present city with additional evidence at the remand hearing. There was no evidence city would not have examined any additional evidence Gump would have submitted as well. After deliberations in executive session, city took up the remand order on its agenda and made additional findings as directed by the district court. Court found no violation of due process concerning city's actions on the court's remand order.

STATUTE: K.S.A. 12-755

**MISSOURI BANK & TRUST CO. V. GAS-MART
DEVELOPMENT CO. ET AL.**

**JOHNSON DISTRICT COURT — AFFIRMED
NO. 93,662 — MARCH 10, 2006**

Arbitration and motion for judgment

ATTORNEYS: S. W. Longan III, and Patricia L. Lear-Johnson, Longan & Associates, Leawood, for appellants. Thomas J. Fritzlen, Jr., of Martin, Leigh, Laws & Fritzlen P.C., Kansas City, Mo., for appellee.

FACTS: Gas-Mart contracted with Cherry & Associates to construct a "Conoco Breakplace" in Leavenworth. Cherry filed for arbitration alleging payments due under the contract in the amount of \$192,808.75. Gas-Mart responded with claims totaling \$270,000, based on allegations that construction costs had either not been properly documented or were inflated. Cherry assigned its right, title, and interest in the arbitration to Missouri Bank & Trust. The district court found a valid assignment and denied a stay of the arbitration. The arbitrator awarded Cherry \$122,569.97 after setting off some of Gas-Mart's claims. Missouri Bank filed a motion for judgment on the pleadings or alternatively for summary judgment. The district court confirmed the arbitration award, which was modified to adjust the rate of interest.

ISSUES: (1) Procedural error in motion for judgment and (2) assignment of arbitration rights

HELD: Court affirmed. Court disagreed with the district court's characterization of Missouri Bank's motion as one for summary judgment. Rather, court found Missouri Bank's motion was properly considered as a motion for judgment on the pleadings. Court held the district court committed no procedural error in granting the motion for judgment on the pleadings and declined Gas-Mart's request to remand for discovery and rehearing. Court also held prior decisions of a different district judge concerning the construction contract's express prohibition on assignment were res judicata or law of the case. Last, the court held Cherry's assignment of its right, title, and interest in its arbitration claims was not prohibited by the contract provisions and was valid. The arbitration claims were fully assignable, and the district court did not err in refusing to stay the arbitration.

STATUTES: K.S.A. 5-412, -413 and K.S.A. 60-212(c), -256

BERGMAN V. COMMERCE TRUST CO. ET AL.

**JOHNSON DISTRICT COURT — AFFIRMED
NO. 93,936 — MARCH 10, 2006**

Contracts and right of first refusal

ATTORNEYS: Bruce F. Landeck, Overland Park, for appellants. Leonard B. Rose and Amy L. Allen, Lathrop & Gage L.C., Kansas City, Mo., for appellees.

FACTS: In June 1995, Crispan Richardson and Bradley and Elizabeth Bergman executed Declarations of Restrictions and Reservations, which granted both parties the right of first refusal on specified adjacent

properties owned by each of the parties. Richardson executed a will and trust leaving all his personal and real property, including the 10 acres in question, to Christa Park. Richardson executed a deed conveying the property to the trust. After Richardson's death, Richardson's sister contested the will and trust. Park settled with the estate and the 10 acres was transferred to Richardson's sister. Before the deed of distribution was executed, Bergman made a written offer to purchase the 10 acres for \$106,000. The Bergmans sued Commerce and Richardson's sister. The district court granted summary judgment to Commerce and Richardson's sister finding the qualifying conditions for triggering the right of first refusal had never occurred.

ISSUE: Did the district court err in finding the right of first refusal was not triggered?

HELD: Court affirmed. Court stated two separate conditions precedent would have had to occur before triggering the Bergmans' right of first refusal: (1) Richardson or Commerce would have had to form a specific intent to sell, transfer, or convey the 10-acre tract and (2) Richardson or Commerce would have had to receive a bona fide written offer for the purchase of the 10-acre tract that Richardson and Commerce would have accepted. Court held the Bergmans' failed to show these conditions precedent were satisfied and the Bergmans' right of first refusal never ripened into an enforceable right to purchase the property.

STATUTES: No statutes cited.

CONCURRENCE: Judge McAnany concurred in the ultimate decision, but used a different rationale to affirm the district court.

PHILLIPS V. TYLER

**SEDGWICK DISTRICT COURT — REVERSED AND
REMANDED**

NO. 93,146 — MARCH 10, 2006

Negligent misrepresentation and contracts

ATTORNEYS: Alvin D. Herrington and Scott E. Sanders, McDonald, Tinker, Skaer, Quinn, & Herrington P.A., Wichita, for appellants. Nicholas S. Dailey and Randall K. Rathbun, Depew Gillen Rathbun & McInteer L.C., Wichita, for appellees.

FACTS: Phillips purchased a house from Tylers. Based on later found defects, Phillips sued the Tylers for negligent misrepresentation, negligent failure to repair, fraud, and nuisance. District court dismissed nuisance and negligent failure to repair claims, and denied summary judgment on remaining claims. Jury found no fraud, but awarded almost \$1 million to Phillips for repairs and loss of use of home. Tylers appealed.

ISSUE: Negligent misrepresentation

HELD: Tort of negligent misrepresentation is discussed. Contract provisions between buyers and sellers can defeat a claim of negligent misrepresentation. Here, buyers cannot sustain negligent misrepresentation claim where they, by express contract provisions, agreed that statements of sellers were not warranties, that sellers were not experts concerning building defects, and that buyers were relying upon own judgment and own inspections of property and not statements of sellers. Because buyers agreed they did not rely upon any representation of the sellers in making the purchase of the house, district court erred in denying summary judgment on the negligent misrepresentation claim. Judgment is reversed and case is remanded with instructions to enter judgment on behalf of Tylers.

STATUTES: No statutes cited.

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TRADESMEN INTERNATIONAL INC. V. WAL-MART REAL ESTATE BUSINESS TRUST ET AL.

JOHNSON DISTRICT COURT — AFFIRMED IN PART AND REVERSED IN PART

NO. 93,410 — MARCH 3, 2006

Mechanic's lien, bond claimant, and attorney's fees

ATTORNEYS: Leslie A. Bailey and Thomas M. Moore, Moore & Hennessy P.C., Kansas City, Mo., for appellants/cross-appellees. Samuel P. Logan and James D. Oliver, Foulston Siefkin LLP, Overland Park, for appellee/cross-appellant.

FACTS: Wal-Mart contracted with Merit Construction for construction of an Overland Park Wal-Mart Supercenter Store. Merit subcontracted with Construction Services Corp. (CSC) to complete the concrete work. Merit eventually terminated CSC from its subcontract with \$168,031.04 remaining due and owing from CSC to Tradesmen International for the skilled laborers supplied to the Wal-Mart project. After Tradesmen's claims were refused by Merit and Centennial Insurance Co., Tradesmen filed a subcontractor's mechanic's lien against the Wal-Mart property. The lien statement failed to correctly name the contractor as Merit General Contractors Inc., and instead named Merit Construction Co. Inc., as the contractor. The trial court later allowed Tradesmen to amend its lien statement to reflect the correct name for Merit after the statutory period for filing a valid lien had expired. The trial court granted summary judgment in favor of Tradesmen, but denied Tradesmen's request for attorneys fees.

ISSUES: Was the mechanic's lien valid? Was Tradesmen the proper bond claimant?

HELD: Court affirmed in part and reversed in part. Court held the trial court erred in granting summary judgment to Tradesmen. Court stated that a mechanic's lien statement filed by a subcontractor that fails to correctly name the contractor is vitally defective and the correct name of the contractor is an essential step for a valid lien. Court held the trial court may not exercise its authority to allow the amendment of a mechanic's lien, and the trial court erred in allowing Tradesmen to amend its mechanic's lien statement. Court also held that Tradesmen was a proper bond claimant under Centennial's payment bond because Tradesmen provided skilled laborers that were used in the prosecution of work under the general contract between Wal-Mart and Merit. Court affirmed summary judgment in that regard. Court also affirmed the trial court's refusal to grant attorney fees to Tradesmen because it was unable to find that no reasonable person would take the view of the trial court that Centennial had just cause or excuse in refusing to pay Tradesmen's payment bond claim based upon the obligation of a surety to a subcontractor of a subcontractor.

STATUTES: K.S.A. 40-201, -254(b), -256; and K.S.A. 60-1102, -1103(a)(1), -1105(b)

ALLIANCE STEEL V. PILAND ET AL.
FINNEY DISTRICT COURT — REVERSED AND REMANDED

NO. 94,245 — MAY 19, 2006

Mechanic's liens, foreign corporation, and Kansas actions

ATTORNEYS: Douglas M. Crotty III, Crotty Law Office P.A., Garden City, and Ross A. Plourde, McAfee & Taft, Oklahoma City, for appellant. William I. Heydman, Heydman Kliever LLP, Garden City, for appellees Troy Piland and Terrance Piland. Gerald O. Schultz, Law Offices of Gerald O. Schultz, Garden City, for appellee Robert D. Dunlap, d/b/a Dunlap Construction.

FACTS: Piland owned real estate in Garden City. Piland entered into a contract with Dunlap for the construction of a pre-engineered metal building on the property. Dunlap subcontracted with Grooms for the purchase and erection of the metal building. Grooms in turn contracted with Alliance to furnish the materials and supplies necessary for construction of the building. Piland paid Dunlap, Dunlap paid Grooms, but Grooms did not pay Alliance. Alliance filed a lien on Piland's property through the Kansas mechanic's lien statutes and then filed a petition to foreclose the lien. The petition stated that Alliance was an Oklahoma corporation authorized to do business in Kansas. Piland filed a motion to dismiss for the lien being tardy and also invalid in Kansas. In both amended petitions, Alliance again stated it was an Oklahoma corporation authorized and doing business in Kansas. Alliance filed another motion to dismiss stating that Alliance claimed to be authorized in Kansas but was not actually registered in Kansas. Alliance filed a motion for leave to amend its petition to clarify that it was not doing business in Kansas. The district court granted Piland's motion to dismiss holding that Alliance was not authorized to bring a cause of action in Kansas without being registered with the secretary of state.

ISSUE: Did the district court properly apply the corporation statutes to the foreign corporation?

HELD: Court reversed and remanded. Court found the district court erred in granting Piland's motion to dismiss. Viewing the facts in the light most favorable to Alliance, Court found that the district court should have denied the motion to dismiss. Court stated these types of cases are extremely fact specific and the district court's decision was not supported by substantial competent evidence and does not support the application of whether a foreign corporation was doing business in Kansas. Court held that Alliance was not doing business in Kansas and was not required to register as a foreign corporation and was not prohibited from bringing the present action.

STATUTES: K.S.A. 17-7303, -7307 and K.S.A. 60-212(b)(6)

SEWARD COUNTY BOARD OF COMMISSIONERS V. NAVARRO ET AL.

SEWARD DISTRICT COURT — REVERSED AND REMANDED WITH DIRECTIONS

NO. 94,598 — MAY 19, 2006

Injunctive relief, agricultural use, and race horse training

ATTORNEYS: Daniel H. Diepenbrock, Miller & Diepenbrock P.A., Liberal, for appellant. J. Gregory Swanson, Swanson Law Office, Liberal, for appellees.

FACTS: In 1992, the Navarros acquired a 40-acre tract of land outside of Liberal and used it to breed, raise, and train horses. They

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also constructed a racetrack with a four-horse starting gate to train the racehorses. In 1997, Seward County created and approved the first ever zoning and subdivision for Seward County. The Navarros' land was zoned agricultural. In February 2003, the Navarros graded out another racetrack. In March 2003, the Navarros applied for a special use permit to operate a horse-training track on their land. The board denied the permit or special use concluding that horse training is not an agricultural use and was not exempt from planning and zoning requirements. The Navarros did not appeal the board's decision. After several Sunday afternoons where the Navarros allowed friends and family to train horses on the track, the county requested a permanent injunction. The district court denied the injunction finding the county had failed to prove that the Navarros' horse training facility was not an agricultural pursuit or that the use was not for agricultural purposes, the Navarros were not bound by the board's decision because their use was exempt, and the county should address the problem as a nuisance.

ISSUES: Did the county pursue a proper remedy? Is racehorse training an agricultural purpose? Was there a pre-existing use?

HELD: Court reversed and remanded with directions. Court held the county was within its statutory right to file the petition for injunctive relief and there was nothing improper about the remedy the county pursued. Court also held that a landowner's use of property as a facility to train racehorses does not constitute an agricultural purpose within the meaning of Kansas zoning statutes and regulations. However, the court held that the burden should have been placed on the Navarros to establish whether there was a pre-existing use of the property. Court stated that to the extent the Navarros fail to prove a pre-existing use of their property, then the county's request for injunctive relief should be granted.

STATUTES: K.S.A. 2-3203(a); K.S.A. 12-741(a), -758; K.S.A. 2005 Supp. 12-761(a), (b), (c); and K.S.A. 47-414(b), -1001(b), -1402(c), -1501(c)

DISSENT: Judge Green dissented based on analysis that the county failed to establish that it lacked an adequate remedy at law and that this case does not fit with the criteria for obtaining injunctive relief and the trial court correctly so held.

Kansas 2006 Legislative Highlights

House Sub. for SB 35 — *Sexually-oriented business signs.* The provisions in House Sub. for SB 35 were originally contained in HB 2854. The bill regulates signage for sexually-oriented businesses, as follows: (i) prohibit signs or outdoor advertising for adult cabaret or sexually-oriented business from being located within one mile of any state highway; (ii) provide if the business is located within one mile of a state highway, the business could display a maximum of two exterior signs, one identifying the business and the other stating the business is off limits to minors; (iii) stipulate the identification sign could be no larger than 40 square feet in size and could include only the name, street address, telephone number, and operating hours of the business; (iv) provide if a nonconforming sign exists on the effective date of the act, it would be allowed to continue in existence until July 1, 2009; (v) provide any owner of a business whose signs are regulated, and who violates the provisions of the bill, would be guilty of a class C misdemeanor, and each week the owner remained in violation would be a separate offense; (vi) provide that the provisions of the bill are

intended to mitigate adverse secondary effects of sexually-oriented businesses, improve traffic safety, limit harm to minors, and reduce prostitution, crime, juvenile delinquency, deterioration in property values, and lethargy in neighborhood improvement project efforts; and (vii) authorize the attorney general to represent the state in all actions and proceedings that arise from passage of this bill, and provide that all costs of defending or prosecuting these actions and proceedings would be paid for from the State General Fund.

SB 55 (Sub. for HB 2023) — *Sales taxes and excise taxes prohibited.* The bill is intended to restore uniformity to local sales tax provisions relating to cities by reducing the number of classes of cities to one. All cities in that class would be granted authority to levy sales taxes of up to 2 percent for general purposes and up to 1 percent for special purposes (for a maximum rate of 3 percent). Any special purpose taxes levied would be required to sunset after 10 years. Additional language would provide a grandfather clause clarifying sales taxes imposed by cities as of July 1, 2006, pursuant to the exercise of home rule authority would remain in effect. Cities not levying development excise taxes as of Jan. 1, 2006, would be prohibited from doing so. Moreover, cities already levying such taxes on that date would be prohibited from increasing the tax rates. Finally, all cities would be granted authority to levy excise taxes on tickets for admissions to concerts, theatrical performances, sports contests, or other similar performances which occur on property owned by the cities.

House Sub. for SB 196 — *Protection of certain personal information.* The bill enacts new law by allowing for protection and restriction of the use of certain personal information and amends existing identity theft law and the Fair Credit Reporting Act. Unless required by federal law, a document that is available for public inspection or copying shall not contain an individual's social security number if such document contains an individual's personal information (i.e., name, address, phone number, or e-mail address). The bill also creates associated penalties and remedies for violations of the use of personal information. Specifically, the bill creates new law for the illegal possession or use of scanning devices, protections for personal identifying information and notification requirements associated with a breach of security of computerized data, allowances for the use of and protections associated with security freezes on consumer reports, and procedures for the destruction of data.

SB 271 — *Real estate brokers and salespersons; license act; and real estate validation questionnaires.* The bill amends the Real Estate Broker and Salesperson Act. The amendments add five additional fees the Kansas Real Estate Commission may charge for services that require staff time as follows (1) additional branch offices an amount not to exceed \$100, (2) primary office an amount not to exceed \$100, (3) certification of educational history an amount not to exceed \$25, (4) licensure of a professional corporation an amount not to exceed \$25, and (5) special branch offices an amount not to exceed \$50. The bill also includes a definition for the term "primary office" as the broker's principal place of business. Finally, the bill also amends KSA 79-1437f, to provide that the contents of real estate sales validation questionnaires shall be made available to, inter alia, "a person licensed pursuant to the real estate brokers' and salespersons' act for purposes of fulfilling their fiduciary duties to clients and providing information on market value of property to clients."

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Probate and Trust Cases

MARSHALL V. MARSHALL

U.S. Supreme Court No. 04-1544
(5-1-06)

The U.S. Supreme Court held that federal courts had jurisdiction of a lawsuit against Pierce Marshall by Vickie Marshall (a/k/a Anna Nicole Smith) for tortious interference with her expected inheritance. During pendency of Texas probate proceedings for J. Howard Marshall II (husband of Vickie and father of Pierce), Vickie filed a Chapter 11 bankruptcy in California. Pierce filed an objection to her discharge alleging willful and malicious injury from defamatory claims that Pierce engaged in forgery, fraud, and overreaching to secure his father's assets. Vickie counterclaimed, and the federal district court (adopting the bankruptcy court's findings) determined Pierce had tortiously interfered with Vickie's inheritance by conspiring to suppress a trust that J. Howard had directed his attorneys to prepare for Vickie and to strip J. Howard of his assets by falsifying documents and information given to J. Howard. Based on overwhelming evidence of Pierce's willfulness, maliciousness, and fraud, the district court awarded Vickie more than \$44 million in compensatory damages and an equal amount in punitive damages. Upon obtaining this ruling, Vickie voluntarily dismissed her challenge to the will's validity and her tortious interference claim in the Texas Probate Court. Following a jury trial, the Texas Probate Court held valid J. Howard's pourover will and living trust (that left nothing to Vickie).

The Supreme Court acknowledged the confusion caused by its prior *Markham* case and sought to elucidate the probate exception to federal court jurisdiction. The Bush administration filed a supporting brief in favor of federal jurisdiction. The Court recognized that probate courts' exercise of *in rem* jurisdiction over a *res*, would not bar federal jurisdiction of a federal claim for an *in personam* judgment against Pierce. A federal court has no jurisdiction to probate a will or administer an estate, but it may entertain suits in favor of creditors, legatees, heirs, and other claimants against an estate to establish their claims, so long as it does not interfere with the probate proceedings or take control of property under control of the state court.

IN RE KESTER REDMOND V. KESTER

Bankruptcy Appellate Panel of the 10th Circuit
(3-13-06)

BAP Nos. 05-095 and 05-107

ATTORNEYS: Christopher J. Redmond and Eric J. Howe, Husch & Eppenberger LLC, Leawood, for trustee/appellant. (Debtors were pro se and did not file a brief.)

The three-judge bankruptcy appellate panel (BAP) unanimously upheld the Bankruptcy Court decision overruling the trustee's objection to a claim of homestead exemption. The debtors transferred legal title of their residence to their self-settled revocable trusts. The trustee objected that the debtors, as trust beneficiaries, could not exempt their residence. Looking to settled law in Kansas that equitable title can support a homestead claim and the expressed policy of liberal construction of the state's homestead provisions, the BAP concluded that the homestead claim by the Kesters was proper.

The BAP recognized the general Kansas rule that has been included in the Uniform Trust Code (UTC), that "during the lifetime of the settlor, the property of a revocable trust is subject to claims of the settlor's creditors." K.S.A. 58a-505(a)(1). They rejected this as applied to debtors' homestead claim, but failed to cite another more specific provision in the UTC that, "The transfer by warranty deed of real property into an intervivos trust ... if the settlor is a beneficiary of such trust at the time of the transfer ... shall not affect any homestead exemption or redemption rights." K.S.A. 58a-1107.

IN RE MATTERN

U.S. Bankruptcy Court Case No. 05-40985
(Judge Somers)
(3-9-06)

ATTORNEYS: Brenda J. Bell, Manhattan, for debtor, and Darcy D. Williamson, Topeka, trustee.

Less than 60 days after debtor filed for Chapter 7 bankruptcy relief, his father died. Bankruptcy Code Section 11 U.S.C. 541(a)(5)(A) provides any interest the debtor acquires within 180 days after filing bankruptcy "by bequest, devise, or inheritance" is to be included in the bankruptcy estate. Somers held that property passing by the father's intervivos trust was excluded from the bankruptcy estate, as not resulting from "bequest, devise, or inheritance." The court also held any property that might pass by the father's pourover will to the intervivos trust would also be excluded (relying upon a particular Arizona statute that property poured over to an intervivos trust shall not be considered held in a testamentary trust). The court also held the debtor had no rights as of the date of filing due to the trust's spendthrift provisions, which are effective under Arizona law. The bottom line was the debtor could keep property that he would have had to turn over to the trustee if it had come to him by his father's will alone.

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Credit Card Claim Alert

Some credit card companies are using agents to file their probate claims. You should carefully check the authority granted by any power of attorney, the corporate capacity of the person(s) signing the claim and any related power of attorney, the verification, and the claim documentation. With a proper written defense you may be able to defeat the claim and help get the credit card companies to file claims that comply with Kansas legal requirements.

New Legislation

SB 40 — This bill shifts the duty to mail notice (within 10 days of the fiduciary's appointment) to a surviving spouse of the possible right to an elective share from the court to the administrator, executor, petitioner, or affiant. The mailing can be avoided if the surviving spouse is the petitioner or affiant and a statement acknowledging awareness of the right is included in the petition or in an affidavit filed within 10 days after the fiduciary's letters are issued. Effective July 1.

SB 355 — This bill changes certain probate appeal deadlines and procedures effective July 1. The deadline to appeal a magistrate judge's final orders and judgments regarding adoption and relinquishment; care and treatment of mentally ill persons; care and treatment of persons with alcohol or substance abuse problems; or guardians and conservators, will now be 10 days. The bill also requires the appeal of these personal type issues to be heard by the district court within 30 days from the notice of appeal. The district court shall conduct the appeal on the record, or, if there is no record, then de novo. Upon motion of any party, the district judge may hold a trial de novo. Parties appealing these personal issues from a district judge to an appellate court will still have 30 days to do so.

The appeal of money type issues is still subject to a 30-day deadline. The list of orders that must be appealed now specifically includes a finding that a spouse's consent to a will is valid, an order regarding requested payments to satisfy a spouse's elective share, and an order regarding the validity of a settlement agreement. The amount of a creditor's claim that must be appealed within 30 days of a ruling thereon, has been raised from \$500 to \$5,000 (and parties disputing such larger claims can request transfer from a magistrate to a district judge). This brings the amount in line with claims that can be paid without a hearing.

Any order appealed from (whether personal or money issues are involved) shall continue in force unless modified by the appellate court. A supersedeas bond will not stay proceedings under an appeal from a district court to an appellate court of personal type issues. The court appealed from may require an appellate bond to ensure that an appeal of personal type issues will be prosecuted without unnecessary delay and to ensure payment of all sums adjudged due.

HB 2607 — This bill makes the following changes to the Kansas Uniform Trust Code (UTC) effective July 1:

1. A "qualified beneficiary" means a beneficiary (charitable or otherwise) who, as of the date in question, either is eligible to receive mandatory or discretionary distributions of income or principal, or

would be so eligible if the trust then terminated. Unless the trustee is furnished with a copy of an instrument exercising a power of appointment, the trustee in determining a "qualified beneficiary," may conclusively presume the power of appointment has not been exercised (or the most recently received copy is proper, unless further notice of modification or revocation is received).

2. The trust terms cannot abrogate the trustee's duties to administer the trust in good faith, in accordance with the trust terms and purposes, the interests of the beneficiaries or the terms of the Uniform Trust Code (UTC).
3. The following factors are now set forth as considerations for a trustee in determining the appropriate place for trust administration: the settlor's designation, the trust purposes, the interests of the beneficiaries, and the manner and costs of trust administration.
4. Nonjudicial settlement agreements are now limited to specified matters (which resolves an inconsistency that previously existed between the wide-ranging authority of K.S.A. 58a-111(b) and the seemingly express limitations of 58a-111(d)).
5. The original UTC authority to modify or terminate a noncharitable trust is retroactively negated (back to the original Jan.1, 2003, UTC effective date). This may avoid unintended inclusion in the settlor's taxable estate.
6. Trusts can be combined or divided after notice to qualified beneficiaries if the interests of each beneficiary are "substantially the same" afterwards.
7. In determining a "mandatory distribution" that a creditor can reach despite a spendthrift clause, clarification is provided that discretionary distributions are excluded.
8. Provisions and procedures have been added so that if the settlor of a revocable trust becomes incapacitated, an interested party can petition the court for directions to the trustee to account, to act properly in the best interests of the settlor, or to be removed.
9. The required trustee's annual report no longer needs to be sent to a beneficiary who received a specific bequest.
10. Instead of being required to provide "the trust's Association of Investment Management and Research (AIMR) compliant rate of return" to requesting qualified beneficiaries, the trustee now must provide, if requested, the trust's investment rate of return and whether the method complies with AIMR standards (so compliance is not required, but just disclosure). This should lessen the burden on individual trustees.
11. Exculpatory terms drafted by trustees can now (in addition to the original provision allowing an exculpation term that was "adequately communicated" and "fair under the circumstances") be upheld if the settlor was represented by an attorney who was not employed by the trustee with respect to the trust and such attorney reviewed and provided independent legal advice regarding such exculpatory term. (This would apparently include even advice that the settlor chooses to ignore.) ■

Estate Tax Notes

(Continued from Page 6)

an additional \$6,714 in 2000; and proceeds of loans of \$450 and \$7,933 in 1995 and 2000, respectively, from unspecified sources. When the decedent was no longer a partner, she wrote on her personal bank account eight checks for rent payable to the partnership that she then endorsed and deposited into the partnership checking account. The partnership had annual lease agreements under which it rented the residence to the decedent for the years 1994 through 2000 for annual rental amounts ranging from \$8,400 to \$10,200. Fair rental value for such years ranged from \$17,280 to \$26,400 annually. The decedent paid most of the expenses connected with the residence, as the partners did not want to incur out-of-pocket costs. Accordingly, they asked the decedent to pay rent greater than that stated in the lease agreements to the extent the stated rent was insufficient to pay expenses connected with the residence. The decedent directly paid all utility expenses associated with the residence while she resided there.

The partnership did not treat the decedent in her capacity as a tenant in the same manner as it would have treated a tenant who was a stranger. The decedent did not regularly pay her rent as required by the lease agreements, she did not always pay the amount of rent stated in the agreements, and she often paid the rent later than the time required under the agreements. However, the partnership never mailed the decedent a notice demanding that she pay the rent or a notice of eviction. The decedent died in February 2000 when the fair market value of the residence was \$400,000. In November 2000, the partnership sold the residence to David for \$350,000, upon his request, and did not attempt to obtain a second bid for the residence or otherwise sell it in the market.

In 2004, the IRS issued a notice of deficiency to the decedent's estate, including the value of the residence in her gross estate under Code Section 2036(a)(1) because she retained until her death the possession and enjoyment of the residence. The court noted the decedent would be treated as having retained an interest in the residence if she transferred it to the partnership with an understanding or agreement, express or implied, that the possession or enjoyment of the residence would be for her benefit. Such a determination would be made from all of the facts and circumstances surrounding both the transfer itself and the subsequent use of the residence. The court held the decedent had express and implied understandings and agreements with the partners and they meant for her to stay at the residence until she died. Such agreements and understandings were memorialized in the lease agreements, which gave the decedent exclusive possession and enjoyment of the residence without the payment of fair rental value. Further, the lease agreements served only to disguise the testamentary nature of the transfer. First, the partnership was not a business operated for profit, but was a testamentary device whose goal was to remove the residence from the decedent's gross estate. Second, the decedent's relationship to the residence following its transfer to the partnership was not treated by any of the parties as that of a tenant to leased property. Third, the decedent transferred the residence to the partnership when she was almost 72 and in poor health. Fourth, the partners wanted the decedent to continue to use and possess the residence as she had before its transfer and wanted the decedent to live at the residence for as long as she could. Finally, the decedent transferred the residence to the partnership on the advice of counsel to minimize the tax on her estate.

Based on the foregoing facts, the court concluded that Code Section 2036(a)(1) applied, and the value of the residence was includible in the decedent's gross estate.

OTHER

10. *WOOD v. U.S. BANK N.A.*, 828 N.E.2D 1072 (OHIO APP. 2005) – ABROGATION OF TRUSTEE'S DUTY TO DIVERSIFY MUST BE EXPLICITLY STATED IN GOVERNING INSTRUMENT

John Wood, a prominent Cincinnati attorney with estate planning experience, created a trust worth more than \$8 million, nearly 80 percent of which consisted of stock in Firststar Bank (predecessor to U.S. Bank). The balance of the trust assets consisted of stock in Cincinnati Financial. Wood modified the trust in September 1998 to permit Firststar trustees to retain, manage and invest the stock that was in the trust as they deemed advisable or proper and to include a retention clause to allow Firststar to retain the Firststar stock. Specifically, the trust gave Firststar the power to retain any securities in the same form as when received, including shares of a corporate trustee, even though all of such securities were not of the class of investments a trustee was permitted by law to make. The trust directed the payment of debts and expenses of the estate, followed by distribution of the assets to the beneficiaries following Wood's death. Firststar had custody of the trust assets beginning in early 1998. Shortly after Wood's death, Firststar's trust officers and the beneficiaries met to discuss the estate. Firststar recommended selling some stock to pay the debts and expenses of the estate and retaining the balance pending the eventual distribution to the beneficiaries. The debts and expenses were approximately \$4 million, and the trust contained approximately \$8 million, of which \$6 million was in Firststar stock. Based on Firststar stock's strong earnings momentum at the time, Firststar's plan called for a sale of two-thirds of the Cincinnati Financial stock and only about 10 percent of the Firststar stock to pay the debts and expenses. The trust officers and one of the beneficiaries testified at trial that the parties agreed to the distribution plan.

Because of a Firststar merger, the stock increased from about \$21 per share in October 1998 to almost \$35 per share in early 1999. In April 1999, Wood's wife asked Firststar to sell some of the stock, as did her advisor. The requests were not made in writing, and Firststar did not sell any stock as a result of the requests. By mid-2000, around the time that it made the final distribution to the beneficiaries, Firststar's stock was worth only \$16 per share. According to expert testimony at trial, Firststar's failure to diversify cost Wood's wife more than \$770,000, based on calculations using an average mutual fund as the basis for estimating value.

Wood's wife sued Firststar, asserting that it had violated Ohio law by failing to diversify the assets of the trust. Firststar denied the allegations and raised the affirmative defenses of estoppel, waiver, consent, and ratification. Wood's wife proposed jury instructions based on the Uniform Principal and Income Act (UPIA), which the trial court rejected. Instead, the trial court adopted Firststar's abuse-of-discretion and estoppel instructions. The jury returned a verdict against Wood's wife, and on appeal, she argued the trial court erred in the jury instructions. The appeals court agreed the trial court erred in refusing to instruct the jury in accordance with the UPIA. The court

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recognized Wood's trust granted Firststar the power to retain its own stock even though it would ordinarily not have been permitted to hold its own stock. However, the court held the language in the trust served only to circumvent the undivided loyalty rule, which stated the foremost duty a fiduciary owed to its beneficiary was undivided loyalty. Nevertheless, because a trustee still has the duty to act prudently, and diversification is normally called for, the retention language in the trust did not alter the duty to diversify. Therefore, the court held the language of a trust does not alter a trustee's duty to diversify unless the instrument creating the trust clearly indicates an intention to do so. To abrogate the duty to diversify, the trust must contain specific language authorizing or directing the trustee to retain in a specific investment a larger percentage of the trust assets than would normally be prudent. The UPIA contains an exception to the duty to diversify where special circumstances exist. Due to the trial court's jury instructions, the jury was not allowed to determine whether special circumstances existed to allow Firststar to retain its stock. Therefore, the appeals court ordered a new trial for such determination.

11. CHAWLA v. TRANSAMERICA OCCIDENTAL LIFE INSURANCE, No. 05-1160 (4TH CIR. 2006) – RULING THAT LIFE INSURANCE TRUST LACKED INSURABLE INTEREST IN DECEDENT'S LIFE VACATED

Harald Giesinger was 72 years old in 2000 when the initial life insurance application for a \$1 million policy from Transamerica was completed. He was not in good health. For many years, he had been drinking heavily, developed a meningioma (a hard, slow growing usually vascular tumor invading the dura and skull and leading to erosion and thinning of the skull) and had been suffering memory lapses. In 1999, Giesinger's physicians surgically removed a portion of the meningioma. One month later, the physicians performed serial taps to drain a fluid that had collected in Giesinger's brain following surgery. The following month, he had surgery to insert a shunt in an attempt to drain the excess fluid. During the same period, Giesinger had been diagnosed with chronic alcohol abuse by several physicians and suffered other medical problems as a result.

Giesinger's friend, Vera Chawla, was to own and be the sole beneficiary of the policy. The life insurance application consisted of two parts: Part 1 requested general information about Giesinger, and Part 2 related to his medical history. On the application, Giesinger answered "no" to the following questions: (i) within the past five years, have you had observation or treatment at a clinic, hospital, or sanitarium; (ii) within the past five years, have you had or been advised to have a surgical operation; and (iii) have you ever received treatment or joined an organization for alcoholism or drug addiction. According to Chawla, when Melissa Hadinger, a paramedic for Transamerica, took Giesinger's medical history, Giesinger advised her that a meningioma, or benign cyst, had been removed from his head within the past five years. In response to being asked whether he had been examined or treated by any physician in the past five years, Giesinger answered in the affirmative but disclosed only that he had received a physical examination and a prostate biopsy, both in 2000. In further support of the life insurance application, which was signed by both Giesinger and Chawla, Chawla submitted to Transamerica a letter from her husband, Dr. Chawla, attesting that Giesinger had no history of any disease that he knew of and otherwise was in good health. Dr.

Chawla later testified by deposition that he never examined Giesinger at his office, having only seen him at his home. Neither Giesinger nor Chawla ever disclosed to Transamerica Giesinger's shunt surgery, his multiple hospitalizations, or the nature of his meningioma surgery. However, in at least one previous life insurance application with Transamerica (in 1994, 1995, or 1999), Giesinger had disclosed that he suffered from a meningioma, which was documented in Transamerica's files. The files also contained a scribbled, handwritten report reflecting Giesinger consumed a bottle of wine daily.

Transamerica rejected the initial life insurance application after concluding Chawla, the intended beneficiary, lacked an insurable interest in Giesinger's life. Shortly thereafter, a revised Part 1 was submitted, naming an irrevocable trust created by Giesinger as the proposed owner and beneficiary of the policy. The trust had been created in 1995 and named Giesinger and Chawla as co-trustees. The trust owned Giesinger's residence and provided that during his lifetime, he retained the right to receive all income from the trust and the right to occupy the residence. At his death, the trust property was to be distributed to Chawla. Transamerica approved the revised life insurance application, with coverage in the sum of \$1 million. Soon thereafter, Giesinger was hospitalized because of bouts of unconsciousness physicians believed to be associated with his meningioma and alcohol abuse. After he was released from the hospital, the trust sought to have Transamerica increase the policy's coverage to \$2.45 million. Another life insurance application was completed, and Transamerica issued an endorsement upgrading the policy's coverage, but without receiving additional information concerning Giesinger's hospitalization. Giesinger died of heart failure nearly one year later. Chawla filed a claim for the policy's benefits with Transamerica. After conducting an extensive investigation, Transamerica rescinded the policy on the ground that Giesinger had failed to make full disclosure to it in completion of the life insurance applications. It also refunded to the trust the premiums that had been paid on the policy.

Chawla filed suit in the eastern district of Virginia against Transamerica alleging it had unlawfully rescinded the policy. Transamerica asserted its rescission was justified because material misrepresentations had been made in connection with the life insurance applications and because the trust lacked any insurable interest in Giesinger's life. The district court granted summary judgment to Transamerica, and Chawla appealed. The 4th U.S. Circuit Court of Appeals affirmed the summary judgment award on the basis of misrepresentations in the life insurance applications. It then vacated as unnecessary the district court's alternative ruling that the trust lacked an insurable interest in Giesinger's life. It stated the district court's ruling on such point could be interpreted as concluding under Maryland law, a trust could never possess an insurable interest in a person's life. Because the district court correctly awarded summary judgment to Transamerica on the misrepresentation issue, its alternative ruling unnecessarily addressed an important and novel question of Maryland law. As a general proposition, it stated courts should avoid deciding more than is necessary to resolve a specific case. Accordingly, the court vacated the lower court's alternative ruling.

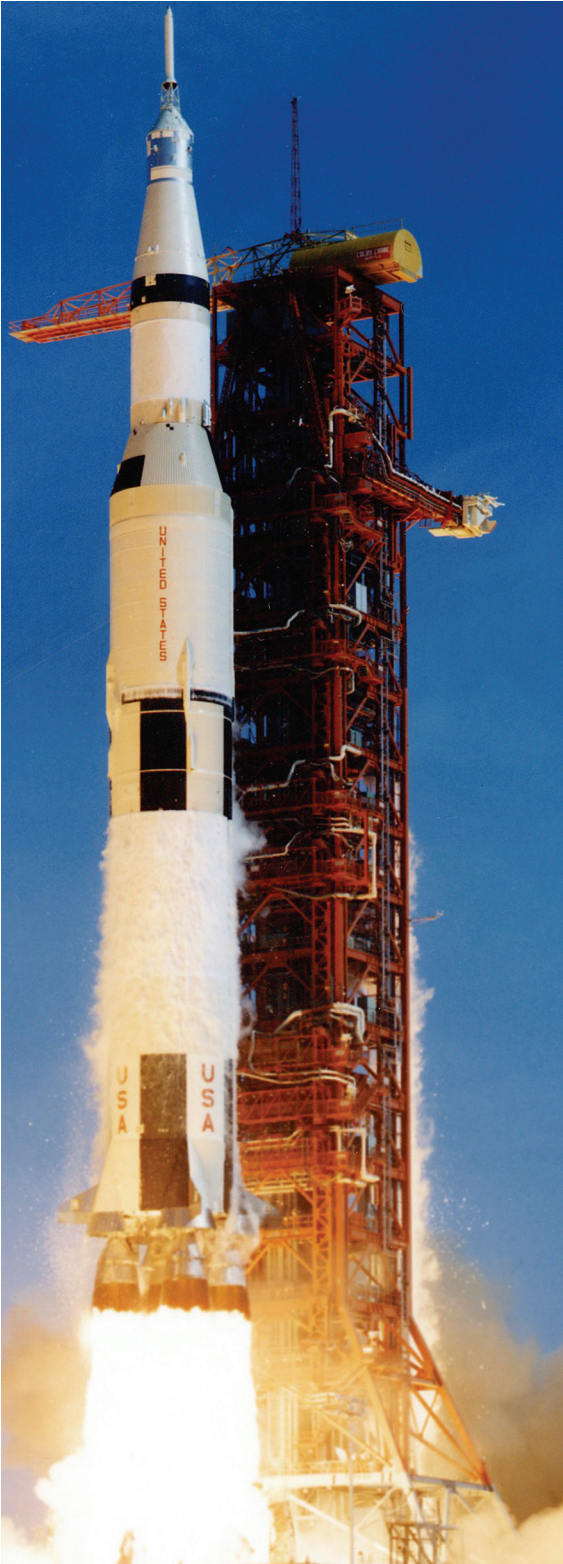
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12. 2006 KANSAS S.B. 365 – KANSAS ENACTS BILL REPEALING ESTATE TAX

Kansas has created a stand-alone estate tax no longer tied directly to federal law, effective for the estates of decedents dying on and after Jan. 1, 2007. The new law creates a set of brackets designed to generate the same amount of revenue as the current estate tax for tax years 2007 through 2009. Estates valued at \$1 million or less would be exempt from the tax. For tax year 2007, the rates range

from 3 percent to 10 percent. For tax year 2008, the rates range from 1 percent to 7 percent. For tax year 2009, the rates range from 0.5 percent to 3 percent. The tax is eliminated for decedents dying on or after Jan. 1, 2010. In determining the value of a decedent's estate, if a decedent is a resident of Kansas on the date of death and owns real property in Kansas that is classified as agricultural property for property tax purposes under K.S.A. § 79-1476, such real property's value for Kansas estate tax purposes will be its most recent valuation pursuant to K.S.A. § 79-1476. ■



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COMING OCTOBER 2006

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Sub. for SB 323 — *Eminent domain and filing fees.* The bill prohibits the use of eminent domain for economic development purposes unless the Legislature approves the taking, and changes certain eminent domain procedures. The bill provides the taking of private property by eminent domain for the purpose of selling, leasing, or transferring it to another private entity is not permitted unless the taking meets any of the following:

- The property is deemed excess real property that was taken lawfully and incidental to the acquisition of right-of-way for a public road, bridge, or public improvement project of Kansas Department of Transportation or a municipality;
- The property is used for the operation of facilities necessary for the provision of services of any privately-owned carrier;
- The private property owner has acquiesced in writing to the taking by any municipality;
- The property has defective or unusual conditions of title or unknown ownership interests in the property and is taken by any municipality;
- The property is unsafe for occupation by humans under the building codes;
- The taking is expressly authorized by the Legislature on or after July 1, 2007, by enactment of law that identifies the specific tract or tracts to be taken.

The Kansas Eminent Domain Procedure Act is amended to set the compensation level at 200 percent of the fair market value; allows a defendant 10 days to remove personal property from the real property that has been taken; and provides that an appeal is deemed perfected upon the filing of a notice of appeal and applying this clarification retroactively to July 1, 2003, which reverses the holding of the Kansas Supreme Court in *In re Condemnation of Land for State Highway Purposes* (*Miller v. Stranger Valley Land Co.*), 123 P.3d 731 (Kan. 2005).

SB 336 — *Uniform real property electronic recording act and formation of electronic recording commission.* The bill enacts the Uniform Real Property Electronic Recording Act. The bill provides the following: (i) if a law requires, as a condition for recording, a document be an original, paper document or other tangible medium, or be in writing, the requirement would be satisfied by an electronic document. Further, an electronic signature would satisfy any law requiring, as a condition for recording, that a document be signed; (ii) creation of a 15-member Electronic Recording Commission to develop electronic recording standards; and (iii) any register of deeds or other recorder shall be authorized to receive, index, store, archive, search, retrieve, and transmit electronic documents in accordance with standards established by the Electronic Recording Commission and any fee or tax may be accepted electronically.

SB 362 — *Solid waste disposal.* The bill amends three statutes that are a part of the act under which solid waste disposal areas are regulated. The bill creates a new category of solid waste disposal area defined as an “industrial facility.” The term includes all operations, processes, and structures involved in the manufacture or production of goods, commodities, materials, or other products located on, or adjacent to, an industrial site. An industrial facility includes all processes and applications generating industrial waste that may be disposed of at a solid waste disposal area. Other provisions of the bill clarify existing

law with respect to requirements for financial assurances for closure and postclosure which must be in place as a condition of the granting of a permit from Kansas Department of Health and Environment (KDHE). New provisions provide more restrictive financial assurance requirements if the permittee does not own the land where the solid waste processing facility or disposal area is located, including a trust fund, a surety bond guaranteeing payment, or an irrevocable letter of credit. Another provision of the bill provides that if the applicant does not own the land, then the applicant is required to have a daily recorded easement to the landfill property and to have the authority to conduct certain landfill activities as outlined in the bill. The easement runs with the land if a transfer occurs and can only be vacated by the secretary of KDHE. Finally, current law is modified to clarify that industrial waste disposed of at a facility is not required to pay the state’s solid waste tipping fee if the facility is either operated by or for an industrial facility.

SB 418 — *Concealed weapons.* The Personal and Family Protection Act authorizes the issuance of licenses to carry concealed weapons to individuals who meet certain criteria. Employers and the owners of real property may prohibit those licensed under the act from bringing weapons onto their property. See SB 418, Section 11. The act defines “weapons” as handguns, pistols, or revolvers. SB 418, Section 2(b). An owner of real property may prohibit licensed persons from carrying weapons onto their property by posting notice “reasonably likely to come to the attention of persons entering the property” that carrying weapons onto the property is prohibited. SB 418, Section 11(a)(2)&(3). The act also prohibits carrying concealed weapons into a host of certain expressly listed properties. SB 418, Section 10(a)(1-21). The list of prohibited properties includes educational institutions, government buildings, commercial establishments, religious buildings, and sporting events not involving firearms. *Id.* The posting requirement does not apply to the listed properties. A licensed individual carrying a concealed weapon onto an expressly prohibited property or onto a property where the owner has properly posted notice prohibiting weapons may be subject to criminal liability. Motion to overrule the governor’s veto passed by the Senate and House on March 22 and 23, 2006, respectively. Kansas 2006 Session Laws, Ch. 32 (SB 418).

SB 505 — *Electronic access of court records.* The bill provides that any county may provide electronic access to district court records that are otherwise publicly available. A county may charge reasonable fees, not to exceed those authorized by law, for providing electronic access to such records.

HB 2125 — *Mortgage releases.* The bill was requested by the Kansas Bankers Association to provide for clarification of payment of the required fee when the satisfaction or cause of satisfaction of a mortgage is entered into the record. The provision allows that the fee may be collected from the mortgagee pursuant to KSA 16-207.

HB 2485 — *Notary public.* The bill enacts certain provisions regarding prohibited acts by notaries public. Prohibited acts include the following: (i) a notary public, not admitted to practice law, and who advertises services in non-English (e.g., Spanish) must include in the same language that “I am not authorized to practice law and have no authority to give advice on immigration law or other legal matters,” and (ii) the notary could not use the term “notario

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publico” or any equivalent, non-English term unless the notary complies with the prior requirement. Violations may result in the loss of notary certification for a lifetime, be deemed deceptive acts or practices punishable under the Kansas Consumer Protection Act, and constitute a class B misdemeanor with a fine and jail sentence.

HB 2582 — *Homeowner’s associations.* The bill addresses homeowner’s association restrictive covenants, budgets, and board meetings. With respect to restrictive covenants, the bill prohibits violations of Kansas laws regarding discrimination based on race, religion, color, sex, disability, familial status, national origin, or ancestry, which is in connection with the sale or rental of real property or real estate loans. These changes must be made within 60 days of the act’s effective date and without seeking approval of association members, the amended document must be recorded within 10 days of the amendment’s adoption (with no fee for recording), and the bill provides for injunctive relief if a violation continues in violation of this law 30 days after a city or county has given written notice to the association. With respect to homeowner’s association budgets and board meetings, the bill requires that all board meetings be open to all homeowners, and requires boards to adopt an annual budget and make a copy available within 30 days to any homeowner who requests one.

HB 2659 — *Title insurance.* The bill defines the phrase “reasonable search and exam and sound underwriting practices” as it relates to companies providing title insurance. The search must cover the lesser span of 25 years or the last time title insurance was obtained on the property. Additionally, the search must include all state, county, and federal offices in the county where the property is located. Sound underwriting practices consist of practices promulgated by an underwriting that has an agency agreement with a title insurance company or that comply with the procedures promulgated by the Kansas Bar Association.

HB 2676 — *Restrictive covenants.* The bill declares as void and unenforceable any provision of a restrictive covenant that requires the use of wood shingles or wood shakes as a roof covering material for any residential dwelling, unless the covenant allows for the use of an alternative material that meets certain criteria (e.g., appearance, flame resistance, building codes). The bill further states the provisions shall not affect the enforceability of a restrictive covenant that regulates or restricts certain aesthetic characteristics of roofing material so long as the restrictive covenant meets the bill’s requirement regarding wood shingles and wood shakes.

HB 2704 — *Small claims court.* The bill increases the number of small claims court actions that an individual may file in any given calendar year from the current 10 to 20 small claims court actions. The fiscal note to this bill states the bill does not specify the funding source to offset the increased financial burden on the judicial system, but it is assumed that it would be the State General Fund.

HB 2709 (Sub. for SB 35) — *Transfer of title by railroads.* Among other things, the bill will allow a railroad company to sell its right-of-way that it owns in fee simple. The owner is entitled to the entire property with unconditional power of disposition. This bill makes law the decision in *Stone v. USD* 222, 278 Kan. 166 (2004).

HB 2720 — *Subdivision regulations and platting.* The bill revises the platting procedure. A planning commission must notify a property owner, in writing, when the plat does not conform to subdivision regulations. The written notice must specify, in detail, the reasons why the plat does not conform with the subdivisions regulations. Additionally, the governing body must give notice to the landowner and the planning commission if it defers or refuses to accept the dedication of land for public purposes related to the plat. If the deferral or refusal of the dedication of land for public purposes is based on noncompliance issues then the notice must specify in detail the nature of the noncompliance.

HB 2735 — *Real estate appraisals.* The bill amends the general definitions provision of the Kansas Consumer Credit Code to expand the definition for the term “appraised value” to include the estimated market value determined through an approved, automated valuation model, in the case of a nonpurchase money real estate transaction. In addition, the bill prohibits a lender or any person acting on behalf of a lender from disclosing to an appraiser or other person engaged to determine the appraised value of real estate, the amount of a proposed real estate loan or the preferred or required value of any real estate intended to secure such loan.

Multi State Issues

**TRENT V. MORTGAGE ELECTRONIC
REGISTRATION SYSTEMS INC.
FOURTH JUDICIAL CIRCUIT OF FLORIDA -
DUVAL COUNTY**

CLASS ACTION COMPLAINT — MARCH 17, 2006

Class action, mortgage foreclosure, and consumer protection violations

ALLEGATIONS: This pending class action lawsuit was recently filed in the state of Florida. Plaintiffs are mortgagors who have been the targets of foreclosure suits by Mortgage Electronic Registration Systems Inc., a Delaware corporation (MERS). MERS is not the plaintiffs’ mortgagee, rather, it is the mortgagees’ Anominee. MERS is owned by its members, consisting mostly of residential mortgage lenders. The members pay annual fees to MERS and pay transaction fees to execute electronic transfers of mortgage loans on the MERS system without recording assignments in registers of deeds. The members also contract with MERS to perform loan servicing and filing of foreclosure actions on mortgage loans owned by its members. The MERS system allows mortgage lenders to avoid the bad publicity of instituting mortgage foreclosures, and to avoid paying local government recording fees for mortgage assignments. The representative class of this action includes all individuals who have been sued in the state of Florida for foreclosure in the preceding four years.

ISSUES: (1) Whether MERS improperly asserted legal and equitable interests in mortgage loans in which it was merely an Anominee, “rather than an Assignee,” of the mortgagee. (2) Whether MERS “is operating as an unlicensed debt collector in violation of Florida law.” (3) Whether MERS’s conduct violates Florida’s consumer protection act by attempting to enforce mortgage obligations without being the record holder of the mortgages.

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FLORIDA LAW: Plaintiffs request a declaratory judgment that MERS has no legal standing to pursue foreclosures in Florida, money damages, attorneys' fees, and injunctive relief prohibiting MERS from seeking further foreclosures.

On May 3, 2006, in a separate, pending Florida foreclosure proceeding, *Mortgage Electronic Registration Systems Inc. v. Miesmer et al.*, No. 16-2004-CA-008651-XX (Fourth Judicial Circuit Court, Duval County, Florida, Division CV-H), the court entered an order dismissing the separate foreclosure proceeding, with prejudice. In the order of dismissal, the circuit judge stated that MERS is not the owner of the claim sued upon, and that a suit cannot be prosecuted to foreclose a mortgage which secures the payment of a promissory note, unless the plaintiff actually holds and owns the original note.

The owner of a note is an indispensable party to a foreclosure action because the owner of the note has an interest in the subject matter of the controversy. MERS is at best an agent and, in Florida, an agent does not have a cause of action against a party allegedly breaching a contract with its principal.

KANSAS LAW: Many of the same issues raised in this Florida class action may be relevant in several residential foreclosure actions filed by MERS, which are currently pending in Kansas. The Kansas statute regarding real parties in interest, KSA 60-217, is even stronger than the Florida statute, and states that every action "shall" be prosecuted in the name of the real party in interest. Accordingly, the judicial proceedings in this Florida class action should be monitored by Kansas attorneys who either file or defend MERS foreclosure actions in Kansas. Between Jan. 1, 2005, and May 1, 2006, MERS filed 74 foreclosure actions in the Douglas County District Court, alone. ■



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