



IN THE SUPREME COURT OF THE STATE OF DELAWARE

JESSE FREDERICK-CONAWAY,)
Appellant)
)
v.) No. 359, 2016
)
KEVIN M. BAIRD, COURT-) ON APPEAL FROM THE COURT
APPOINTED EXECUTOR OF THE) OF CHANCERY C.A. NO. 8379-
ESTATE OF EVERETT T.) VCG
CONAWAY AND COURT-)
APPOINTED TRUSTEE OF THE)
EVERETT T. CONAWAY)
REVOCABLE TRUST,)
Appellee)
)
And)
JANICE M. RUSSELL-CONAWAY,)
Appellee.)

**ANSWERING BRIEF OF APPELLEE, KEVIN M. BAIRD, COURT-
APPOINTED EXECUTOR OF THE ESTATE OF EVERETT T.
CONAWAY AND COURT-APPOINTED TRUSTEE OF THE
EVERETT T. CONAWAY REVOCABLE TRUST**

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NATURE OF PROCEEDINGS

Appellee, Kevin M. Baird, Court-Appointed Executor of the Estate of Everett T. Conaway and Court-Appointed Trustee of the Everett T. Conaway Revocable Trust (“Mr. Baird”), submits that Appellant, Jesse Frederick-Conaway’s (“Jesse”) statement of the Nature of Proceedings is adequate.

This is Mr. Baird’s Answering Brief responding to Jesse’s Opening Brief.

SUMMARY OF ARGUMENT

I. **ADMITTED** in Part; **DENIED** in Part. Mr. Baird agrees with Jesse that the Court of Chancery erred by ruling that Janice properly received the two payments of \$75,000 from Harry Cook, LLC related to the sale of Mr. Conaway's 100 shares of Conaway Development Industries, Inc. stock. Mr. Conaway's Trust sought to bequest the right to those payments to Janice. However, Mr. Conaway personally, not his Trust, was contractually entitled to those payments. Thus, those payments were property of Mr. Conaway's estate and subject to creditor claims before pouring over into the Trust through Mr. Conaway's pour-over will.

Mr. Baird disagrees with Jesse's position that the Trust's assets could not be used to pay the Estate's debts. Delaware law permits a fiduciary to use the assets of a decedent's revocable trust to pay the debts of that decedent's insolvent estate. To hold otherwise would allow decedents to be completely absolved of all lifetime debts by simply transferring assets to a revocable trust.

II. **DENIED.** The Court of Chancery properly ruled that the Trust's limited partnership interest in EJKC, Partnership, L.P. is subject to the Trust's bequests and debts before it passes to Jesse through the residuary clause. Jesse's law of the case argument is based on a ruling in a different case that was self-described by the Court of Chancery as "sloppy" which was properly corrected. The law of the case does not prevent this legally correct result.

STATEMENT OF FACTS

A. Introduction – Mr. Baird’s Role, Generally and on Appeal.

In the years after Mr. Conaway’s death, his Estate and Trust were handled by its co-fiduciaries Jesse and Janice.¹ Mr. Baird was appointed by the Court of Chancery to bring neutrality to the matter, but disputes persisted.² Mr. Baird’s Petition for Instructions gave the Court of Chancery the messy task of unscrambling the egg that was Mr. Conaway’s estate planning and administration.³ The Court of Chancery considered the Petition and the parties’ arguments and then issued bench rulings.⁴ Both Jesse and Janice have appealed the Rule 54(b) order.

Mr. Baird owes fiduciary duties to all of the beneficiaries of Mr. Conaway’s Estate and Trust. And while Jesse and Janice’s interests have been protected by able counsel, the interests of the Other Beneficiaries (defined below) have been largely ignored and relegated to the sidelines.⁵

Mr. Baird’s primary goals are to satisfy the specific bequests to the Other Beneficiaries, properly apportion the remaining assets between Jesse and Janice, and close out the administration of the Estate and Trust. Mr. Baird asks that this

¹ See A101 - 102

² *Id.*; A100.

³ A101 – 119.

⁴ OB Exhs. D – G.

⁵ See OB Ex. D at 11-12 (Mr. Baird describing his role at hearing), 21-22 (certain Other Beneficiaries raising their concerns with the Court).

Court provide a clear disposition of the issues so that he can complete his duties as Court-appointed successor executor and trustee in a fair and proper manner.

Mr. Conaway died on May 11, 2010.⁶ Mr. Baird joined the fray in August 2013, when he was appointed by the Court of Chancery as successor executor and trustee.⁷ Therefore, Mr. Baird leaves it to Jesse and Janice to describe the facts from before his appointment and instead focuses on the facts arising after his appointment; particularly those directly related to his Petition and how this matter proceeded below.

B. Summary of Trust and Will Terms

Mr. Conaway's Will and Trust agreement, both dated September 21, 2009, are in Jesse's Appendix. A brief summary of the documents' basic principles may be helpful.

i. Mr. Conaway's Last Will and Testament⁸

Mr. Conaway's Will was a typical "pour-over" will, directing the executor to administer the estate with a revocable trust as the ultimate beneficiary, with the trust containing the testator's dispositive provisions. In traditional fashion, the Will directed the executors to:

- First: Pay last illness, funeral, and burial expenses

⁶ A1.

⁷ A100.

⁸ A2-6.

- Second: Section 212 tangible personal property bequest to TBD legatees⁹
- Third: Balance of household furnishings and tangible personal property to Janice.
- Fourth: Residue to Trust

Pour-over wills are commonly used in estate planning to ensure that all of a decedent's assets are transferred into their trust, which contains the ultimate dispositive provisions. It is often preferable, however, to title assets directly into the trust during the testator's lifetime.

ii. Amended and Restated Revocable Trust Agreement¹⁰

Mr. Conaway's revocable trust contains his ultimate testamentary wishes. And before his death he did manage to transfer certain assets directly to his trust. These assets included: 32,486 shares of Fulton stock; a Morgan Stanley account; 69% interest in EJKC Partnership, L.P.; and 50% interest in Confam, Inc.¹¹

Section Three of the trust is the key section which outlines how the Trust's estate shall be distributed upon Mr. Conaway's death. That is:

- A. 10,000 Fulton shares to Janice, plus 1,000 shares for each year she was married to Mr. Conaway; resulting in 23,000 shares.
- B. 1,000 Fulton shares to each of the following:
 - Mary Linda Brodie
 - Kevin Bodie
 - Carolyn Conaway

⁹ There is no Section 212 document in the record.

¹⁰ A18-31. Mr. Conaway previously created a revocable trust dated September 3, 1993. *See* A18.

¹¹ A104 (chart of Trust assets at time of death).

Virginia Conaway
Jack Knowles
Carolyn Knowles
Nikolas Karbelnikoff

- C. 200 Fulton shares to Seaford Historical Society
- D. To Janice: a Morgan Stanley account; 100 shares of CDI Stock or the proceeds of any sale of same; the Trust’s partnership interest in EJKC Partnership, L.P.
- E. Janice given right to live in Seaford home for 6 months
- F. Balance of corpus and income to Jesse.

The beneficiaries named in Section Three, sub-sections B and C, shall be referred to in this brief as the “Other Beneficiaries.”

C. The Estate’s and Trust’s assets and liabilities upon death.

It is important to have a basic understanding of the financial condition of the Estate and Trust upon Mr. Conaway’s death. The Trust held the following assets:¹²

Morgan Stanley Active Assets Account	\$36,088.24
69% interest in EJKC Partnership	\$814,131.00
50% interest in Confam, Inc.	\$5,899.50
Fulton Financial Stock (32,486 shares)	\$336,230.10
Total	\$1,192,348.80

¹² A104; A125.

According to the inventory, the Estate had the following assets:¹³

Delaware National bank account	\$6,022.41
PNC bank account	\$4,300.33
Fulton Financial Stock (3,592 shares)	\$36,013.39
Heinz Corporation stock (300 shares)	\$15,750.00
Del Monte Stock (133 shares)	\$2,525.67
Pernix Therapeutics Stock (50 shares)	\$155.99
Golf Trust (100 shares)	\$179.00
Tangible Property	\$35,750.00
Total	\$100,696.79

In addition, Mr. Conaway (not his Trust) was owed at least \$150,000 in deferred payments from the sale of his 100 shares of stock in Conaway Development Industries, Inc. (“CDI”) to Harry Cook, LLC (*see* I.D.ii. below).¹⁴ Those payments were made directly to Janice during the course of administration, and the parties dispute whether that was appropriate.¹⁵

The Estate had one large liability and a few smaller liabilities. Mr. Conaway personally owed Fulton Bank about \$261,000 on an unsecured personal line-of-

¹³ A104; A125. *See* A7-17.

¹⁴ A105; A125; A148-152.

¹⁵ A105.

credit.¹⁶ Funeral expenses were about \$10,000 and other minor expenses were about \$3,000.¹⁷ Accordingly, the Estate had a significant shortfall in assets.¹⁸

D. Petition for Instructions; Parties' Positions; Court's Rulings.

Following Mr. Baird's appointment, he was unable to achieve a resolution of the parties' disputes, so he filed a verified Petition for Instruction on January 20, 2015 (the "Petition").¹⁹ The Petition requested instructions from the Court of Chancery on four issues. The parties' positions and the Court of Chancery's ruling on each issue are summarized below.

i. Sale of Trust's Fulton stock to pay Estate debt.

When Mr. Conaway died he owed Fulton Bank approximately \$261,000 for an unsecured personal line-of-credit.²⁰ The Estate did not have the assets to pay the debt when Mr. Conaway died.²¹ With advice of estate counsel, Janice and Jesse sold the Trust's 32,486 shares of Fulton stock for \$326,420.76.²² The proceeds were used to pay off the Fulton Bank line of credit, as well as \$10,355.46 in funeral expenses and \$3,118.64 expenses.²³ The above transactions had the effect of converting a substantial Trust asset, 32,486 shares of Fulton stock,

¹⁶ A50-55, 105-107.

¹⁷ A106.

¹⁸ A104-106; *see* A7-18.

¹⁹ A101-119.

²⁰ A50-55, 105-107.

²¹ A105-107

²² *Id.*

²³ *Id.*

entirely to the use of the Estate without any compensation paid by the Estate to the Trust.²⁴ It also disposed of trust assets that were earmarked as specific gifts to Janice and the Other Beneficiaries.²⁵

Mr. Baird sought instruction on whether the sale of the Trust's Fulton stock was proper to pay the Fulton Bank loan, and, if so, whether the payment of that Estate debt loan should have been treated as a loan by the Trust to the Estate. He also asked what should be done if the Estate is unable to pay the Trust back.²⁶

Mr. Baird: The sale was improperly handled and should be considered a loan from the Trust to the Estate.²⁷

Jesse: The sale was improper and should be considered a loan from the Trust to the Estate. Fulton should not have been paid immediately. Instead, Fulton's demand should have been considered a creditor's claim to be paid in the course of estate administration.²⁸

Janice: The sale was proper at the time it was done because the Trust's assets were available to be used for Estate debts.²⁹

²⁴ *Id.*

²⁵ *Id.*

²⁶ A102, 107-108.

²⁷ A105-107.

²⁸ A127-130.

²⁹ A146-147.

Court ruling: The sale was proper so Jesse and Janice could pay the debts of the insolvent Estate.³⁰ The Court deferred ruling on whether the sale proceeds should be considered a loan from the Trust to the Estate.³¹

ii. Proceeds of sale of CDI stock – Janice’s or the Estate’s?

The second issue raised in the Petition was whether Janice properly received two payments of \$75,000 that were deferred payments from Mr. Conaway’s sale of 100 shares of CDI stock (the “CDI Payments”). Was it proper for the CDI Payments to go directly to Janice, or should the payments have been made to the Estate and used to pay Estate debts?³²

In December 2009 Mr. Conaway entered into a stock purchase agreement with Harry Cook, LLC to sell his entire interest in CDI.³³ Mr. Conaway executed the agreement in his name, not in the name of the Trust.³⁴ Harry Cook, LLC was obligated to pay Mr. Conaway three payments of \$75,000, along with an additional contingent payment of up to \$775,000.³⁵ The first of the required \$75,000 payments was paid at closing in 2009, and the other two payments were due on the first and second anniversary of the closing.³⁶

³⁰ OB Ex. F at pgs. 5-8.

³¹ *Id.*

³² A102.

³³ A62-85.

³⁴ A62, 84.

³⁵ A66-67.

³⁶ *Id.*

By the time the second CDI Payment of \$75,000 became due in December 2010, Mr. Conaway had already passed away (May 2010). Harry Cook, LLC timely made the second and third CDI Payments directly to Janice rather than to the Estate.³⁷

Under the Trust Janice was specifically bequeathed Mr. Conaway's 100 shares of CDI stock or the proceeds of any sale of that stock.³⁸ There is no evidence, however, that Mr. Conaway's 100 shares of CDI stock, or his individual interest in the stock purchase agreement, was ever retitled, assigned, or otherwise transferred to the Trust.³⁹

Therefore, Mr. Baird sought instruction on whether the CDI Payments were assets of the Estate available to pay Estate debts before pouring-over to the Trust; and, if so, whether Janice should account for those payments.⁴⁰

Mr. Baird: The CDI Payments should have gone to the Estate to be available to pay Estate debts.⁴¹

Jesse: The CDI Payments should have gone to the Estate to be available to pay Estate debts.⁴²

³⁷ A109.

³⁸ A21.

³⁹ A109.

⁴⁰ A110.

⁴¹ *Id.*

⁴² A130-132.

Janice: Janice properly received the CDI Payments because she was specifically bequeathed those payments under the Trust agreement, and the Will does not provide for the payment of debts and expenses so those obligations should be funded by the Trust.⁴³

Court ruling: The CDI Payments properly went to Janice to effectuate Mr. Conaway's intended specific bequest. But Janice received the payments before she was entitled to them because the CDI Payments should have remained in the Trust until final distribution, so she owes the Trust interest.⁴⁴

iii. Did the Trust's interest in EJKC already pass to Jesse, or did it remain subject to Trust administration?

The third issue raised in the Petition was the status of the Trust's 69% interest in EJKC Partnership, L.P. ("EJKC").⁴⁵

The Trust's interest in EJKC was the subject of prior litigation in the Court of Chancery and this Court.⁴⁶ The interpretation of the Court of Chancery's rulings in that litigation led to this particular problem: did the Trust's interest in EJKC pass to Jesse upon Mr. Conaway's death, or did it remain subject to Trust

⁴³ A148-150.

⁴⁴ OB Ex. E at pgs. 5-6, 9, 17, 23-27; OB Ex. G at ¶¶(b), (c).

⁴⁵ A111-113. The EJKC limited partnership agreement is found at A32-45. Mr. Baird also raised the issue of the Trust's ownership of the 50% interest in Confam, Inc., but that interest has minimal relative value and was not focused upon below.

⁴⁶ OB Exhs. A, B, & C. C.A. No. 6056; No. 194, 2012.

administration? Jesse took the former position, relying upon the following statement in the Court of Chancery's March 13, 2012 opinion denying reargument:

I found that the ownership interest in EJKC Partnership, L.P. [], held by the Everett T. Conaway Revocable Trust [] passed to Jesse Conaway, or to the Jesse Frederick Conaway Trust, upon the death of Everett Conaway.⁴⁷

Based upon the above language, Jesse, then still a co-fiduciary of the Estate and Trust, took personal control of the Trust's EJKC interest, valued in excess of \$800,000.⁴⁸

The parties disputed whether the direct transfer of the Trust's EJKC interest to Jesse was proper, or if the Trust's EJKC interest should have passed to him under the residuary of the Trust only after all specific bequests and Trust expenses were satisfied. Mr. Baird, therefore, sought instruction on whether Jesse's removal from the Trust of its 69% interest in EJKC was proper, and, if not, how Jesse should account for the removal of that Trust asset.⁴⁹

Mr. Baird: Jesse's removal of the Trust's interest in EJKC was improper, and those assets should be returned to the Trust and subject to administration.⁵⁰

⁴⁷ OB Ex. B at 1.

⁴⁸ A111.

⁴⁹ A111-113.

⁵⁰ *Id.*

Jesse: Jesse properly removed and took control over the Trust's interest in EJKC pursuant to the EJKC partnership agreement and the Court of Chancery's prior ruling stating that the interest transferred when Mr. Conaway died.⁵¹

Janice: Jesse's removal of the Trust's interest in EJKC was improper, and those assets should be returned to the Trust and subject to administration.⁵²

Court ruling: The Trust's interest in EJKC did not pass to Jesse upon Mr. Conaway's death. Rather, it passes to Jesse through the Trust's residuary clause, but only after other bequests and expenses are paid. The Trust's interest in EJKC is subject to Trust administration including specific bequests and estate expenses.⁵³

iv. Janice's removal of funds during Estate administration.

During the course of estate administration, the records show that Janice removed at least \$77,986.82 from the Estate account; transactions Janice was unable to justify to Mr. Baird.⁵⁴ Mr. Baird sought instruction on whether Janice's removal of Estate funds was improper, and, if so, how she should account for those funds.⁵⁵ Both Mr. Baird and Jesse took the position that the funds were improperly removed and that Janice should be held liable.⁵⁶ Janice essentially admitted that

⁵¹ A132-136.

⁵² A143-146, 152-156.

⁵³ OB Ex. E at pgs. 3-5, 9; OB Ex. F at pgs. 10, 13-15, 19; OB Ex. G at ¶(a).

⁵⁴ A113-115.

⁵⁵ *Id.*

⁵⁶ *Id.*; A136-138. Jesse totaled a higher amount of improper removals by Janice.

the funds were improperly removed, though she sought some minor offsets.⁵⁷ The Court ruled that Janice was liable for the removed funds and entered an order stating the Janice was liable to the Trust for each removal of funds with interest accruing at the legal rate from the date of removal.⁵⁸

⁵⁷ OB Ex. D at pgs. 8-9; A156-157.

⁵⁸ OB Ex. D at pg. 29; OB Ex. G at pg. 6; OB Ex. G at ¶(f).

ARGUMENT

The Petition presented four issues, but the parties and the Court of Chancery focused on two: the CDI Payments and the status of the Trust's interest in EJKC. Jesse has continued this approach on appeal.

I. THE COURT OF CHANCERY ERRED BY RULING THAT JANICE IS ENTITLED TO THE CDI PAYMENTS. RATHER, THE TRUST'S BEQUEST OF THOSE PAYMENTS TO HER FAILED, SO THOSE PAYMENTS ARE DUE THE ESTATE.

A. Question Presented

Did the Court of Chancery correctly rule that Janice was entitled to the CDI Payments? Or did the Trust's specific bequest fail because the right to the CDI Payments was never transferred to the Trust, meaning those payments should be considered Estate assets?⁵⁹

B. Scope of Review

The scope of review is *de novo* for legal issues, including interpreting a written agreement.⁶⁰

C. Merits of Argument

The Court of Chancery ruled that Janice was the proper recipient of the two CDI Payments. Mr. Baird agrees with Jesse that this ruling was legal error, but for different reasons.

⁵⁹ Question preserved at A109-110, 130-132, 148-150.

⁶⁰ *Schock v. Nash*, 732 A.2d 217, 224 (Del. 1999).

i. Jesse is correct that the Court of Chancery erred, but his argument is too broad.

Jesse attacks the Court of Chancery's specific ruling about the CDI Payments with a broad argument – the Court of Chancery improperly relied on incorporation-by-reference to merge the Trust and Estate, and thus permit the payment of probate debts with non-probate assets. Jesse further argues that, by permitting this mixing of assets in a merged administration, the CDI Payments improperly passed directly to Janice instead of being subject to the Estate process and the demands of creditors.

Jesse's broad argument is off the mark, for two reasons. First, he conflates the Court of Chancery's narrower ruling with Janice's much broader merger argument.⁶¹ Janice argues that the Trust and Estate merge, with all assets pooled together so that all specific bequests and debts can be paid.⁶² The Court of Chancery expressly stated that it did not fully agree with Janice's argument.⁶³

Second, Jesse appears to argue that the Court of Chancery's ruling was in error because it resulted in using Trust assets to pay Estate debts.⁶⁴ However, as Jesse seems to acknowledge,⁶⁵ the assets of a decedent's revocable trust may be

⁶¹ OB at 17, 19.

⁶² OB Ex. E at 16; *see* A140-159.

⁶³ OB Ex. E at 17, 27.

⁶⁴ OB at Summ. Arg. I; *Id.* at 17, 18, 25,

⁶⁵ OB at 26.

used to pay the decedent's debts after the estate is exhausted.⁶⁶ Fulton Bank, after it was partially paid by the Estate, could have pursued the Trust for the deficiency, so it was reasonable for the Trust to liquidate assets to resolve that claim.⁶⁷ To hold otherwise – that a trust's assets cannot be used to pay an estate's debts – would allow decedents to be completely absolved of all lifetime debts by simply transferring assets to a revocable trust. That is not the law.

ii. The Court of Chancery erred by improperly reviving the Trust's failed bequest of the CDI Payments to Janice. Those payments are Estate assets.

The better view of the Court of Chancery's ruling is that it read the *Arcaro* opinions as permitting the incorporation of a trust's specific bequests into the terms of the pourover will. This in turn provided a basis for the Court of Chancery to revive the Trust's failed bequest of the CDI Payments to Janice by incorporating that bequest into Mr. Conaway's will. From there, the Court of Chancery could fulfill Mr. Conaway's intent to pass the right to the CDI Payments to Janice, even though those payments were Estate assets.

⁶⁶ See 12 *Del. C.* § 3536(c) (rendering a spendthrift clause ineffective as to the trustor, permitting the trustor's creditors to satisfy their claims from the trustor's interest to extent of his contributions); *Uniform Trust Code*, § 505(a)(3) & Comment; RESTATEMENT (SECOND) OF TRUSTS § 156(1) (1959); *cf. Kulp v. Timmons*, 944 A.2d 1023, 1031–33 (Del. Ch. 2002) (discussing ways a creditor can reach a trust's assets to satisfy a claim against the trustor).

⁶⁷ Mr. Baird believes Jesse and Janice should have first made a full distribution to the Other Beneficiaries or reserved sufficient funds to do so, and then they should have booked the Trust's payment to Fulton Bank as a loan to the Estate.

The Court of Chancery's ruling and reasoning on this issue is assembled from the following statements made at the August 17, 2015 hearing:

... the \$150,000 from the sale of CDI. That, to me, is the most difficult question in this estate.

As I read the trust, the intent of Ev. Conaway can be best stated wanting Janice to have the CDI stock itself or the receipts therefrom. The argument is that the cash should have gone, instead of into Janice's pocket, into the estate and used to pay debts, including refund the payment made by the trust to satisfy creditors. But it seems to me that would frustrate even further the intent of Ev. Conaway which clearly was to make a specific bequest of either the certificates themselves or the results of the sale.

So as I look at this unified estate plan, it seems to me that can best be consummated by finding that the proceeds, the \$150,000, must be paid to Janice. Now, she took that in the past. It should be sitting in the trust estate to be distributed to her. So what she's entitled to is the \$150,000 today which has less value than the \$150,000 that she received sometime ago. So that the time value of that has to be backed out.⁶⁸

....

And the question of whether the \$150,000 should be in the trust or was legitimately taken by Janice, and the answer is it should be in the trust, but it should be available as a specific bequest.⁶⁹

....

I think what Arcaro tells me is that the bequests in the trust have to be looked at as though they are in the estate...⁷⁰

....

I think it follows from my decision on the \$150,000 that the specific bequest of the personalty – because the trust and estate jointly were solvent, that bequest has to be honored as a specific bequest on an equal footing with the specific bequests of the trust. So I think you're correct. There does not need to be an accounting for the \$25,000.⁷¹

⁶⁸ OB Ex. E, 5-6.

⁶⁹ *Id.* at 9.

⁷⁰ *Id.* at 16.

⁷¹ *Id.* at 17.

....

It seems to me that it would frustrate the purpose of the testator/settlor to strip away not only the partnership interest which is stripped away by a contractual obligation that Mr. Conaway entered before he attempted to settle this estate, but also the other specific bequest because of the artificial way that estate debts would accrue against some assets but not others.

I think I agree that Arcaro doesn't specifically say you treat these as one big estate plan, but I think having *imported* the specific bequests of the trust into the estate that it's pretty clear what Mr. Conaway wanted to happen.

I think in this instance it would not be respecting that to cause those specific bequests to lapse, as I say, because of the artificial way that was set up. If I'm wrong, I'm wrong, Mr. Rutt. The Supreme Court won't be shy about telling me so if I am.⁷²

The Court of Chancery's desire to effectuate Mr. Conaway's intent is laudatory and guided by the general legal principle that the decedent's intent controls. And the Court of Chancery's aspiration to revive the specific bequest of the CDI Payments to Janice since she already lost the right to the Trust's EJKC interest has some equitable appeal.

However, in this case, the "importing" of bequests into the Will from the Trust is not supported by *Arcaro* or other law. And by importing a failed Trust bequest into the Will, the Court of Chancery improperly reordered the priority of bequests and payment of debts, which harms Jesse and the Other Beneficiaries.

The Court of Chancery's ruling was legal error, as shown in the following three step analysis.

⁷² *Id.* at 26-27 (emphasis added).

First, the Trust’s specific bequest of the CDI Payments to Janice failed because those payments were due Mr. Conaway personally and his right to those payments was not transferred to his Trust during his lifetime. Section Three, D of the Trust sought to bequest Janice three assets: a Morgan Stanley account, the Trust’s interest in EJKC, and the CDI shares or sale proceeds.⁷³ Only the Morgan Stanley bequest succeeded because it was properly titled in the name of the Trust while Mr. Conaway was alive. The bequest of the Trust’s interest in EJKC failed because of restrictions in the EJKC partnership agreement.⁷⁴ And, unfortunately, Mr. Conaway’s bequest of his interest in CDI to Janice met the same fate because he never transferred or retitled that asset to his Trust during his life.⁷⁵ Therefore, the CDI bequest failed.

Second, the *Arcaro* case does not support the Court of Chancery’s ruling that the Trust’s bequest to Janice of Mr. Conaway’s interest in CDI could be imported

⁷³ A21.

⁷⁴ See OB Exhs. A & B.

⁷⁵ See RESTATEMENT (THIRD) OF TRUSTS § 3 cmt. B (2003) (“Before property can be said to be held in trust by a trustee, the trustee must have legal title. Without legal title the trustee holds nothing in trust.”); *Id.* § 16 (2003) (“(1) If a property owner undertakes to make a donative inter vivos disposition in trust by transferring property to another as trustee, an express trust is not created if the property owner fails during life to complete the contemplated transfer of the property....”).

It is undisputed that Mr. Conaway signed the Harry Cook, LLC stock purchase agreement in his own name (A62, 84), and there is no evidence that he assigned the rights under that agreement to the Trust (A109).

into the Will. Much was made below of the *Arcaro* case, but the various rulings in that case are not relevant to the issues here.⁷⁶

In *Arcaro I*, a dispute arose between beneficiaries of a trust. The son of the decedent challenged the validity of the trust document, both on technical grounds and for undue influence. Chancellor Marvel deferred until trial a decision on undue influence, but he ruled that the trust was technically valid. The “incorporation by reference” discussion arose in the context of considering the elements of creating a trust.⁷⁷ Specifically, after stating that the transfer of property to a trustee is not required to create a valid trust, he noted that Mr. Arcaro’s will pouring the residue into the trust effectively funded the trust and therefore the trust was valid.⁷⁸ In that context, Chancellor Marvel’s discussion of “incorporation by reference” was directed to the question of whether the pour-over will adequately identified the trust such that the trust was validly funded and created. There is nothing in *Arcaro I* to suggest that a will’s “incorporation by reference” of a trust results in the merger of their administration and bequests.

⁷⁶ Three opinions were issued in the *Arcaro* case: *I/M/O Estate of Arcaro*, 1977 WL 9539 (Del. Ch. Oct. 12, 1977) (*Arcaro I*); *I/M/O Estate of Arcaro*, 1977 WL 176267 (Del. Ch. Oct. 28, 1977) (*Arcaro II*); *I/M/O Estate of Arcaro*, 1977 WL 4530 (Del. Ch. Jan. 10, 1978) (*Arcaro III*).

⁷⁷ *Arcaro I* at *2-3.

⁷⁸ *Id.*; see *Arcaro III* at *1 (describing *Arcaro I* as ruling on whether the trust met “formal legal requirements”).

In *Arcaro III*, the party who was denied summary judgment on the undue influence claim moved for reargument on the basis of estoppel.⁷⁹ Chancellor Marvel framed the question as whether the uncontested probate of the will, the benefits of which the son accepted, meant the son was estopped from challenging the trust which was referenced in the will. In answering that question, the Chancellor built on his “incorporation by reference” concept with broad language about the trust being “inextricably a part of such will” and “an inseparable provision of the will,” and further stating that “the will and deed of trust constitute a single testamentary scheme.”⁸⁰ But, in the end, he ruled simply that the son was estopped from challenging the trust because he failed to challenge the will and actually accepted the will’s benefits.⁸¹

In summary, some of the reasoning and dicta in the *Arcaro* opinions can be read broadly, and out of context, to support Janice’s position and the Court of Chancery’s narrower ruling. But the holdings in *Arcaro* are about a distinctly different issue – the validity of a trust. Those holdings do not address, much less support, merging the administration and bequests of a trust and estate.

⁷⁹ *Arcaro II* merely framed the issue for reargument and set a briefing schedule.

⁸⁰ *Arcaro III* at *2.

⁸¹ *Id.*

Third, the Court of Chancery improperly tried to revive the failed bequest by “importing” the bequest from the Trust to the Estate.⁸² This importation of a bequest defeats the statutory priority scheme to the detriment of Jesse and the Other Beneficiaries.⁸³

The Court of Chancery’s ruling improperly exempts the CDI Payments from the statutory priority scheme that requires estate creditors get paid before beneficiaries.⁸⁴ Under this ruling, Janice’s revived bequest is not subject to the requirement to pay the Estate’s creditors first, which in turn results in the Trust paying more than is required by law. Assuming *arguendo* that this bequest was in the Will (the practical effect of the Court of Chancery’s ruling), that bequest would still be subject to the payment of Estate debts.⁸⁵ To put it in the Court of Chancery’s words, if the Court decides to “import” the bequest into the Will,

⁸² OB, Ex. E at 27.

⁸³ *In re Estate of Farren*, 131 A.3d 817, 840 (Del. Ch. 2016) (describing an executor’s “mandatory duty” to pay demands in a “prescribed order,” with creditors taking precedence over beneficiaries, “who only are entitled to their bequests after the claims of creditors have been paid.”.... “The obligation of an executor to pay legacies only arises when the estate is first able to satisfy the higher priority claims of creditors.”) (citations and quotations omitted) (citing 12 *Del. C.* §§ 2105 & 2312(b)).

Perhaps the Court of Chancery’s ruling – reviving a bequest by importing it into the Will from the Trust – would be permissible if both the Trust and Estate were independently solvent. But that is not the case here.

⁸⁴ 12 *Del. C.* § 2105; *In re Estate of Farren*, 131 A.3d at 840.

⁸⁵ *Id.*

Janice should be required to pay the applicable tariff. To hold otherwise harms both Jesse and the Other Beneficiaries by improperly reducing the Trust's assets.

The legally correct view is that the CDI Payments are general Estate assets that must go towards paying the Estate's debts before pouring over to the Trust. This proper characterization of the CDI Payments would reduce the amount of funds needed from the Trust to pay the Estate's debts, with the favorable adjustment flowing in favor of Jesse and the Other Beneficiaries (whose bequests can be funded).

In summary, the Court of Chancery's ruling that Janice is entitled to the CDI Payments, while well-intentioned, is contrary to Delaware law. The Trust's specific bequest of Mr. Conaway's interest in CDI failed. Therefore, the CDI Payments are assets of the Estate that must first go to paying the Estate's debts before pouring over to the Trust.

II. THE COURT OF CHANCERY CORRECTLY RULED THAT THE TRUST'S INTEREST IN EJKC IS SUBJECT TO TRUST ADMINISTRATION AND HAS NOT YET PASSED TO JESSE.

A. Question Presented

Did the Court of Chancery properly rule that the Trust's limited partnership interest in EJKC, Partnership, L.P. is subject to Trust administration?⁸⁶

B. Scope of Review

The scope of review is *de novo* for legal issues, including interpreting a written agreement.⁸⁷ "A trial court's application of the law of the case doctrine is [] subject to *de novo* review."⁸⁸

C. Merits of Argument

The Court of Chancery ruled that the Trust's interest in EJKC has not yet passed to Jesse and thus is subject to Trust administration, including specific bequests, creditors, and administration expenses.⁸⁹

This ruling was correct. Recall that the Trust attempted to bequest the Trust's interest in EJKC to Janice.⁹⁰ But that bequest failed because of the contractual limitation on transfers in the EJKC partnership agreement.⁹¹ Therefore, with the transfer to Janice having failed, the Trust retained ownership of its interest

⁸⁶ Question preserved at A111-113, 132-136, 152-156.

⁸⁷ *Schock*, 732 A.2d at 224.

⁸⁸ *Cede & Co. v. Technicolor, Inc.*, 884 A.2d 26, 36 (Del. 2005).

⁸⁹ OB Ex. E at pgs. 3-5, 9; OB Ex. F at pgs. 10, 13-15, 19; OB Ex. G at ¶(a).

⁹⁰ A21.

⁹¹ OB Exhs. A, B, & C.

in EJKC. Consequently, according to the terms of the Trust agreement and Delaware law, that Trust asset would pass to Jesse as residuary beneficiary, but only after all other bequests and expenses are paid.⁹²

Jesse's two arguments for reversal are unpersuasive.

Jesse primarily argues that the Court of Chancery's rulings in the earlier litigation about the EJKC partnership interest, affirmed by this Court, should be considered the law of the case. He advances this argument because the Court of Chancery stated in its opinion denying reargument that the Trust's EJKC interest passed to Jesse upon Mr. Conaway's death.

But the law of the case does not apply in this way, for at least two reasons. First, the law of the case doctrine applies to rulings made in the same case, and the ruling upon which Jesse relies here is from a different and concluded, albeit related, case.⁹³ Second, even if the doctrine applied here, it is flexible enough for the trial court to correct or clarify prior rulings.⁹⁴ Here, the Court of Chancery had the authority to correct its self-described "sloppy" description of the status of the Trust's interest in EJKC.⁹⁵ And the circumstances had changed. The focus of the

⁹² A21; 12 Del. C. § 3595; *In re Estate of Farren*, 131 A.3d at 840.

⁹³ See *Kenton v. Kenton*, 571 A.2d 778, 784 (Del. 1990) ("The 'law of the case' is established when a specific legal principle is applied to an issue presented by facts which remain constant *throughout the subsequent course of the same litigation.*") (emphasis added).

⁹⁴ *Weedon v. State*, 750 A.2d 521, 527 (Del. 2000).

⁹⁵ OB Ex. E at 4-5.

earlier case was the effectiveness of the Trust's bequest of its EJKC interest to Janice. Here, the Petition put the current status of the Trust's interest in EJKC directly at issue. In sum, the law of the case doctrine does not affect the Court of Chancery's correct ruling in this case.

Jesse's back up argument that the Trust's interest in EJKC passed to him upon Mr. Conaway's death per the EJKC partnership agreement is also without merit. Jesse only briefly raises this argument in his opening brief and does not point to any provision of the EJKC partnership agreement that supports his belief.⁹⁶ The EJKC partnership agreement is a contract among a corporation and two trusts. It therefore makes sense that the agreement does not address the death of a trustee of one of the trusts. The future of the Trust's interest in EJKC after Mr. Conaway's death is controlled by the Trust agreement. Under that agreement, Jesse is distributed the Trust's interest in EJKC as residuary beneficiary, but only after Trust administration is complete. Consequently, the Trust is still the owner of its interest in EJKC, not Jesse. Again, the Court of Chancery's ruling on this issue was correct.

⁹⁶ OB at 34.

CONCLUSION

For all of the foregoing reasons, the Court of Chancery's judgment should be reversed in part and affirmed in part as set forth above.

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