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Commonwealth of Kentucky

Court of Appeals

NO. 2010-CA-000620-MR

CHRIS GORMAN APPELLANT

v. APPEAL FROM JEFFERSON CIRCUIT COURT
HONORABLE ANN O'MALLEY SHAKE, JUDGE
ACTION NO. 07-CI-001798

STITES & HARBISON, PLLC APPELLEE

OPINION
AFFIRMING

** ** ** ** **

BEFORE: MOORE AND STUMBO, JUDGES; LAMBERT,[1] CHIEF SENIOR JUDGE.

STUMBO, JUDGE: Chris Gorman appeals from a summary judgment entered in favor of Stites & Harbison. The underlying case is an action for malicious prosecution, defamation, and abuse of process. Gorman argues that the trial court

[1] Chief Senior Judge Joseph E. Lambert sitting as Special Judge by assignment of the Chief Justice pursuant to Section 110(5)(b) of the Kentucky Constitution and Kentucky Revised Statutes (KRS) 21.580.

erred when it granted summary judgment. We find that there was no error and affirm.

In 1999, Gorman joined the law firm of Sheffer Hutchison Kinney (hereinafter the Sheffer Firm) as a non-equity partner. A few years later, the Sheffer Firm fell behind on rent payments under a commercial lease agreement. The lease holder, a company called GSMS, sought to collect past rent due to it and hired Stites & Harbison to handle the collection efforts.

Stites & Harbison then filed suit against the Sheffer Firm and its three partners. Because the Sheffer Firm was a partnership, Stites & Harbison sought to impose liability on the named partners under the Kentucky Uniform Partnership Act, KRS 362.220, which provides that each partner is jointly and severally liable for the liabilities of the partnership. During the pendency of this action, the equity partners became insolvent and sought bankruptcy protection.

In the course of the collection litigation, Stites undertook extensive discovery, deposing Sheffer and gaining access to the firm's books and records. No specific questions were asked about Appellant but the discovery revealed that the non-equity partners were paid a set salary, bonuses if warranted, and that contributions to a 401(k) were matched by the firm.

Stites & Harbison then discovered that there was a number of so called "non-equity" partners associated with the Sheffer Firm. These partners were named as partners for the purposes of the firm, but owned no actual stake in the firm. They were paid a set salary, plus bonuses earned through individual

performance. Gorman was one such non-equity partner. Stites & Harbison believed these partners might also be held liable for the debt if they were actual equitable partners of the Sheffer Firm. It sent letters to each of these partners requesting information as to why they should not be held liable for the debt of the Sheffer Firm.

Gorman responded stating that he was a non-equity partner who owned no part of the Sheffer Firm and that he was only an employee. Similar responses were sent to Stites & Harbison from the other twenty-two (22) non-equity partners. Disregarding this correspondence, Stites & Harbison brought action against these partners alleging that the Sheffer Firm's tax returns listed these non-equity partners as general partners and that they were each described as having received profit sharing.[2] All of the non-equity partners moved for summary judgment.

Prior to a ruling on the motions for summary judgment, GSMS settled the claims against the non-equity partners pursuant to a settlement and agreement. In exchange for ending the litigation, the non-equity partners would agree not to bring any future claim against GSMS or Stites & Harbison. All but Gorman agreed to this settlement and agreement. Instead, Gorman executed a different settlement in which he would release GSMS from any future action, but would reserve his right to pursue an action against Stites & Harbison.

[2] KRS 362.180(4) states that if one receives a share of the profits from a business, it is prima facie evidence that he or she is a partner in the business.

On February 20, 2007, Gorman brought this suit against Stites & Harbison arguing that there was no reason he should have been named in the GSMS suit because there was no evidence that he owned any part of the Sheffer Firm or that he was a partner liable for any of the firm's debts. Stites & Harbison moved for summary judgment on September 3, 2008. Gorman responded that Stites & Harbison's motion was premature in that little discovery had been completed. The trial court permitted more discovery before considering the motion.

After further discovery, Gorman filed a supplemental response to the pending motion on August 11, 2009. Stites & Harbison then filed its supplemental memorandum, followed by a final reply by Gorman. After hearing arguments, the trial court entered an opinion and order granting summary judgment in favor of Stites & Harbison. In its opinion, the court articulated the six elements required for a successful claim of malicious prosecution, or wrongful use of civil proceedings.[3]

The court focused on two elements: 1) that the initial cause of action, the GSMS action, must terminate in Gorman's favor, and, 2) that there was no probable cause for bringing the action. The trial court found that the GSMS action did not terminate in Gorman's favor because it was brought about by a settlement and not based on the merits. It also found that Stites & Harbison had probable cause to bring the suit. The court also found that since there was probable cause to

[3] Malicious prosecution is a term used in criminal proceedings. The civil equivalent is called wrongful use of civil proceedings.

bring the GSMS action, Gorman's defamation and abuse of process actions must also fail. This appeal followed.

> The standard of review on appeal of a summary judgment is whether the trial court correctly found that there were no genuine issues as to any material fact and that the moving party was entitled to judgment as a matter of law. Kentucky Rules of Civil Procedure (CR) 56.03 . . . . "The record must be viewed in a light most favorable to the party opposing the motion for summary judgment and all doubts are to be resolved in his favor." *Steelvest, Inc. v. Scansteel Service Center, Inc.,* Ky., 807 S.W.2d 476, 480 (1991). Summary "judgment is only proper where the movant shows that the adverse party could not prevail under any circumstances." *Steelvest,* 807 S.W.2d at 480, *citing Paintsville Hospital Co. v. Rose,* Ky., 683 S.W.2d 255 (1985). Consequently, summary judgment must be granted "[o]nly when it appears impossible for the nonmoving party to produce evidence at trial warranting a judgment in his favor . . . ." *Huddleston v. Hughes,* Ky. App., 843 S.W.2d 901, 903 (1992).

Scifres v. Kraft, 916 S.W.2d 779, 781 (Ky. App. 1996).

As the trial court correctly discussed, there are six elements of the tort of malicious prosecution or wrongful use of civil proceedings:

> (1) the institution or continuation of original judicial proceedings, either civil or criminal, or of administrative or disciplinary proceedings, (2) by, or at the instance, of the plaintiff, (3) the termination of such proceedings in defendant's favor, (4) malice in the institution of such proceeding, (5) want or lack of probable cause for the proceeding, and (6) the suffering of damage as a result of the proceeding.

Raine v. Drasin, 621 S.W.2d 895, 899 (Ky. 1981).

We find that the issue of probable cause is dispositive. Stites & Harbison had probable cause to bring the suit.

> The question of probable cause is related not to whether the facts exist to prove a lawsuit, but whether it was reasonable to believe that the client's claim is tenable. In the context of probable cause, tenable "depends not on the actual state of the case in point of fact, but upon the honest belief of the person instituting it. It may flow from a belief that turns out to be unfounded as long as it is not unreasonable." *Ammerman v. Newman,* 384 A.2d 637, 640 (D.C. 1978).

Prewitt v. Sexton, 777 S.W.2d 891, 896 (Ky. 1989).

> The question of probable cause underlying the tort of wrongful use of civil proceedings does not turn on whether a court subsequently decides the attorney erred in his view of the law, any more than it turns on whether he was subsequently unable to prove his client's claims regarding the facts, so long as his views were tenable at the outset.

Id. at 897.

> What facts and circumstances amount to probable cause is a question of law. Whether they exist or not, in any particular case where the evidence is conflicting, is a question of fact, to be determined by the jury. But where there is no conflict in the evidence, whether the facts shown amount to probable cause, is ordinarily a question of law for the court.

Craycroft v. Pippin, 245 S.W.3d 804, 806 (Ky. App. 2008) (citing *F.S. Marshall Co. v. Brashear,* 238 Ky. 157, 37 S.W.2d 15, 17 (Ky. 1931)).

In the case at hand, Stites & Harbison had sufficient evidence when suit was filed for it to reasonably believe Gorman to be an actionable party. When Stites & Harbison first brought suit against Gorman, it had information that Gorman held himself out to be a partner in the Sheffer Firm and that on the schedule K-1's issued to Gorman, he was listed as a general partner. There were

also notations on his tax records, and those of the Sheffer Firm, that he received some type of profit sharing. As noted above, profit sharing is prima facie evidence of partnership. It was not until after the suit was filed that Gorman produced an employment contract stating that he would be a non-equity partner and not be entitled to any firm assets nor be responsible for any liabilities. It was also not until after the filing of the suit that the profit sharing listed on his K-1 was discovered to be the Sheffer Firm's contribution to Gorman's 401(k) plan. Based on these tax documents, it was not unreasonable for Stites & Harbison to initiate the action against Gorman.

Gorman also sued Stites & Harbison for defamation. Defamation has four elements: defamatory language, about the plaintiff, which is published, and which causes injury to reputation. *Columbia Sussex Corp., Inc. v. Hay*, 627 S.W.2d 270, 273 (Ky. App. 1981). However, because the alleged defamatory statements in this case were published in judicial pleadings in good faith, they are privileged. *Schmitt v. Mann*, 291 Ky. 80, 163 S.W.2d 281 (Ky. 1942).

Finally, Gorman's claim of abuse of process was also properly dismissed.

> Generally stated, one who uses a legal process, whether criminal or civil, against another primarily to accomplish a purpose for which that process is not designed, is subject to liability to the other for harm caused by the abuse of process. There is no liability where the defendant (usually a plaintiff in the underlying action) has done nothing more than carry out the process to its authorized conclusion. (Citations omitted).

Sprint Communications Co., L.P. v. Leggett, 307 S.W.3d 109, 113 (Ky. 2010). Here, Stites & Harbison had probable cause to bring suit against Gorman. It cannot therefore be said that the judicial process was wrongfully used.

Based on the above, we find that the trial court properly granted summary judgment in favor of Stites & Harbison.

LAMBERT, CHIEF SENIOR JUDGE, CONCURS.

MOORE, JUDGE, CONCURS IN PART, DISSENTS IN PART AND FILES SEPARATE OPINION.

MOORE, JUDGE, CONCURRING IN PART AND DISSENTING IN PART: I concur with the results reached by the majority on the issues raised in this appeal except for that portion of the majority's opinion that affirms the trial court's summary dismissal of Gorman's claim against Stites for wrongful use of civil proceedings.

The majority's sole basis for affirming the trial court's order was the element of probable cause. Specifically, the majority opinion holds that Stites was entitled to summary judgment because the evidence of record only supports that Stites had probable cause to sue Gorman for the outstanding balance of the Sheffer Firm's lease. Respectfully, I disagree. I believe that the majority opinion overlooks evidence that materially conflicts with that proposition, *i.e.*, there are factual issues to be resolved by a jury.

In *D'Angelo v. Mussler*, 290 S.W.3d 75, 80 (Ky. App. 2009), this Court recently elaborated upon what "probable cause" is within the context of this tort:

> A plaintiff must prove that the proceeding was initiated or continued without probable cause. Restatement (Second) of Torts § 662(c), comment (f) states:
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> > The question of probable cause is to be determined in the light of those facts that the accuser knows or reasonably believes to exist at the time when he acts. His subsequent discovery of exculpatory facts does not indicate a lack of probable cause for initiating the proceedings, although he may make himself liable by subsequently taking an active part in pressing the proceedings.
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> *See also Id*. at § 675, comment (c) (adapting this comment to wrongful civil proceedings).
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> In a civil proceeding, the quantum of necessary probable cause is less than that required in a criminal action:
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> > [W]hen the proceedings are civil, while the person initiating them cannot have a reasonable belief in the existence of the facts on which the proceedings are based if he knows that the alleged facts are not true and his claim is based on false testimony, it is enough if their existence is not certain but he believes that he can establish their existence to the satisfaction of court and jury.

With this in mind, it is necessary to examine the evidence that the majority opinion relied upon to support its conclusion that Stites indisputably had probable cause to sue Gorman for the outstanding balance of the Sheffer Firm's lease.

First, the majority opinion emphasizes that Gorman's 1999 and 2000 tax returns included an IRS Form K-1; that the top of the K-1 included the term "general partner;" and that Gorman put a check mark in that box. In a similar vein, where the majority opinion states that Gorman "held himself out to be a partner in the Sheffer Firm," the majority opinion is referring to Gorman's listed status as a "partner" on an internet legal directory website.

However, the issue in this matter was whether Gorman could have been liable for the outstanding balance of the Sheffer Firm's lease as a general partner, not as a partner by estoppel; as Stites itself admits, Gorman was not even employed by the Sheffer Firm at the time that its lease was executed. This being the case, Kentucky law, rather than an IRS form or a website, defines what a partnership is. And, KRS 362.180, entitled "Rules for determining the existence of a partnership," does not include "described as a general partner in a tax return or website" as one of its rules. *See also*, *Purchase Transp. Services v. Estate of Wilson*, 39 S.W.3d 816, 819 (Ky. 2001) (holding that administrative law judge, in determining whether an employment relationship existed, properly disregarded that decedent considered herself to be an independent contractor for the purpose of her income tax returns).

Second, the majority opinion emphasizes that Gorman's 1999 and 2000 K-1's included a notation that he received "some type of profit sharing" and, on that basis, determined that *prima facie* evidence supported that he was a general partner. What the majority opinion is referencing is the last line of each of

Gorman's K-1's, which note: "PROFIT SHARING: 1,800." There is no further explanation of this notation in either K-1. Stites argues that when it filed this collection action against Gorman, it had no understanding of what the term "profit sharing" meant within the context of Gorman's K-1's and simply made an assumption that seized upon this language.

Yet, in spite of this notation, the very same K-1's actually *contradict* the notion that Gorman received profits from the Sheffer Firm, or owned any equity in that entity, or shared in any of its losses. In the upper left-hand corner of these two-page documents, immediately underneath where the "general partner" box is checked, Gorman's K-1's list Gorman's percentages of profit sharing, loss sharing, and ownership of capital as "0%." The Sheffer Firm's 1999 and 2000 partnership tax returns also reflected that Gorman had these "0%" interests, and, for further clarity, contrasted Gorman's "0%" interest with the equity partners' respective interests of 49.17% (belonging to Ronald G. Sheffer); 10.66% (belonging to Peter B. Lewis); 22.61% (belonging to John A. Sheffer); and 17.56% (belonging to Mark R. Hutchinson).

Moreover, the Sheffer Firm's 1999 and 2000 tax returns, which Stites had in its possession and had thoroughly examined before filing suit against Gorman,[4] reflected that the Sheffer Firm was a *profitless entity*. As *Stites itself* describes in its appellate brief, "Sheffer Hutchison Kinney was not profitable.

[4] Indeed, on April 5, 2005, Stites detailed parts of the Sheffer Firm's federal tax returns and Gorman's accompanying K-1 schedules in a memorandum it submitted to the Kentucky Bar Association.

According to the firm's 1999 Federal tax return, it was $4,992,000 in debt at the beginning of the 1999 taxable year and it was $8,325,161 in debt by the end of 2000." During oral argument before this Court, Stites again cited to each of these returns and reiterated that the Sheffer Firm "had no profits to distribute. It was simply an entity that owed money to the bank."

In sum, when Stites filed suit against Gorman, it did so only upon the strength of the phrase, "PROFIT SHARING: 1,800." And, apparently Stites understood that phrase was contradicted by 1) the very K-1 it was written on; and 2) the cold reality that the Sheffer Firm had no profits to share.

It is true that

> [i]n many cases civil proceedings, to be effective, must be begun before all of the relevant facts can be ascertained to a reasonable degree of certainty. To put the initiator of civil proceedings to a greater risk of liability would put an undesirable burden upon those whose rights cannot be otherwise effectively enforced.

D'Angelo, 290 S.W.3d at 80 (quoting Restatement (Second) of Torts § 675, comment (d)). This rule simply presumes the obvious—namely, that a party cannot be aware of all of the relevant evidence, exculpatory or otherwise, until it conducts discovery and that discovery is not ordinarily permitted until a suit has been filed.

But, the case at bar is not the ordinary case. Stites filed this suit against the Sheffer Firm on November 5, 2003. Stites had already amassed a considerable amount of discovery, including all of the evidence previously

referenced, *prior* to when Stites added Gorman as a defendant on April 28, 2005. Prior to April 28, 2005, the Sheffer Firm had already made all of its records and files available for Stites' review. The record reveals nothing that would have prevented Stites, prior to filing this suit, from contacting any of the Sheffer Firm's accountants who had prepared the K-1's in question for further clarification regarding the phrase "PROFIT SHARING: 1,800." Indeed, prior to when Stites filed the underlying collection action, even one of Stites' own attorneys, Jim Seiffert, suggested that Stites could contact the Sheffer Firm's accountants for an explanation of that phrase.

In this light, I respectfully believe that the majority opinion misapplied the applicable legal standard in holding that "it was not unreasonable for Stites & Harbison to initiate the action against Gorman" because it was "not until after the filing of the suit that the profit sharing listed on his K-1 was discovered to be the Sheffer Firm's contribution to Gorman's 401(k) plan." I believe that the correct standard is whether it was reasonable for Stites, in light of the access it was given and the evidence it had already amassed through discovery, to not understand or investigate this prior to filing suit. And, in light of that evidence and access, I believe that this is a factual question best suited for a jury.

Likewise, if Gorman's employment contract with the Sheffer Firm was as exculpatory as the majority opinion apparently implies, I believe that the fact that Stites only received Gorman's employment contract after it added Gorman as a defendant does not automatically exonerate Stites from liability for wrongful

use of civil proceedings. "[S]ubsequent discovery of exculpatory facts does not indicate a lack of probable cause for initiating the proceedings, *although [a party or his attorney] may make [themselves] liable by subsequently taking an active part in pressing the proceedings*." *D'Angelo*, 290 S.W.3d at 80 (quoting Restatement (Second) of Torts § 662(c), comment (f) (emphasis added)). Here, Stites received Gorman's employment contract on April 30, 2005 (merely two days after it added Gorman as a defendant), and took an active part in pressing these proceedings until this action was dismissed on February 21, 2006—nearly one year later.

Moreover, I believe that Gorman's employment contract was cumulative of the evidence already in Stites' possession. Similar to Gorman's K-1's and the Sheffer Firm's 1999 and 2000 tax returns, the employment contract emphasized that Gorman would have no equity in the Sheffer Firm, no entitlement to any firm assets, and no responsibility for any of the firm's liabilities. Similarly, Gorman's employment contract with the Sheffer Firm did not entitle Gorman to share in any of the firm's profits. Rather, it merely structured a plan for Gorman to receive a gradually increasing percentage of the gross returns the firm received originating from business generated by Gorman or services performed by Gorman. This latter detail, by itself, cannot establish the existence of a partnership relationship. *See* KRS 362.180(3).

The trial court's second basis for granting summary judgment in favor of Stites was its conclusion that the evidence in this matter was incapable of

demonstrating another element of Gorman's claim, *i.e.*, that GSMS's underlying collection action against Gorman had terminated in Gorman's favor. In particular, Stites argued, and the trial court found, that the settlement agreement between Gorman and GSMS could not have been favorable to Gorman because it contained an agreement not to sue GSMS. While the majority opinion does not address this part of the trial court's reasoning, I disagree with the trial court's conclusion. Further discussion on this point is warranted.

To begin,

> Civil proceedings may be terminated in favor of the person against whom they are brought by (1) the favorable adjudication of the claim by a competent tribunal, or (2) the withdrawal of the proceedings by the person bringing them, or (3) the dismissal of the proceedings because of his failure to prosecute them. A favorable adjudication may be by a judgment rendered by a court after trial, or upon demurrer or its equivalent. In either case the adjudication is a sufficient termination of the proceedings, unless an appeal is taken.
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> . . .
>
> Whether a withdrawal or an abandonment constitutes a final termination of the case in favor of the person against whom the proceedings are brought and whether the withdrawal is evidence of a lack of probable cause for their initiation, *depends upon the circumstances under which the proceedings are withdrawn*."

Restatement (Second) of Torts § 674, Comment j (1977) (emphasis added).

In short, the analysis set forth in the Restatement contemplates that some dispositions, although not obtained on the merits of the underlying facts, may under certain circumstances give rise to an inference of a lack of probable cause.

And, I believe that Gorman's settlement agreement with GSMS evinces such an inference.

As noted, the trial court concluded that the settlement agreement between Gorman and GSMS could not have been favorable to Gorman because it contained an agreement not to sue GSMS. This conclusion ignores that a suit for wrongful use of civil proceedings can be successful against an attorney prosecuting an action, but unsuccessful against his client. This is because a client might assert a defense altogether unavailable to his attorney, *i.e.*, that the client had probable cause to file the proceedings because, in doing so, he was reasonably relying upon the advice of his attorney. *See, e.g., Kentucky Farm Bureau Mut. Ins. Co. v. Burton*, 922 S.W.2d 385, 389 (Ky. App. 1996) ("Where malice or want of probable cause is an element of the cause of action, acting on advice of counsel is a good defense.").

Here, the settlement between Gorman and GSMS is styled as a "settlement agreement and release," but this agreement had no greater effect than a stipulation that GSMS reasonably relied upon Stites' advice when it added Gorman as a defendant. GSMS collected nothing from Gorman in its suit or settlement. Their agreement contains no stipulation of probable cause. Moreover, Gorman's agreement with GSMS cannot be read to absolve Stites from any liability because, in no fewer than three places, their agreement states that it expressly preserves and does not affect claims that may exist by Gorman against Stites and Stites' employees, partners, members and attorneys. And, the agreement states that it

"shall not be used in any way as a defense to any claim that may be made by [Gorman]" arising out of GSMS's underlying collections lawsuit.

For these reasons, I would reverse the trial court's order of summary judgment as it relates to Gorman's claim of wrongful use of civil proceedings and allow the jury to resolve the factual issues on the merits.

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