

RENDERED: January 8, 1999; 2:00 p.m.
NOT TO BE PUBLISHED

Commonwealth Of Kentucky

Court Of Appeals

NO. 1996-CA-003492-MR

TOMMY E. PACE AND DONNA PACE

APPELLANTS

v. APPEAL FROM FRANKLIN CIRCUIT COURT
HONORABLE ROGER L. CRITTENDEN, JUDGE
ACTION NO. 94-CI-01492

COMMONWEALTH OF KENTUCKY,
NATURAL RESOURCES AND
ENVIRONMENTAL PROTECTION
CABINET

APPELLEE

OPINION

REVERSING AND REMANDING

** ** * * *

BEFORE: GARDNER, JOHNSON and MILLER, JUDGES.

MILLER, JUDGE: Tommy and Donna Pace (hereinafter referred to collectively as "the Paces") appeal from an order of the Franklin Circuit Court entered on December 13, 1996, which denied the Paces' motion to set aside a default judgment in favor of the Natural Resources and Environmental Protection Cabinet (the Cabinet). We reverse and remand.

The Paces were shareholders, officers, and directors of K.O.K. Contractors, Inc. (KOK), which was involved in surface

mining. KOK had its charter administratively dissolved on November 11, 1991. Following administrative proceedings, the Cabinet filed an order on June 2, 1992, which dismissed the Paces "as parties hereto without prejudice on the part of the Cabinet to bring an action in the future against the individuals", and imposed upon KOK a civil penalty of \$23,200 for failure to submit water quality reports. The Cabinet filed another order on July 7, 1992, which named only KOK as the defendant and fined KOK a civil penalty of \$121,580 for environmental violations. The Paces were not mentioned in the second order. KOK did not make any payments on the fines.

On September 30, 1994, the Cabinet filed a complaint in the Franklin Circuit Court listing KOK and the Paces, individually, d/b/a KOK, as defendants and seeking to enforce the previous orders. The relevant language of the complaint is as follows:

1. This action is brought pursuant to KRS Chapter 350.

. . .

3. Defendants Tommy E. Pace and Donna G. Pace, were shareholders, officers and directors of . . . [KOK], from charter to administrative dissolution.

4. Defendant . . . [KOK] is the alter ego of the Defendants, Tommy E. Pace and Donna G. Pace, and they have conducted, managed, and controlled the affairs of the Corporation as though it were their own business, and they have used Defendant Corporation to defraud Plaintiff and others similarly situated.

5. On June 2, 1992, the Secretary of the

Natural Resources and Environmental Protection Cabinet filed a Final Order . . . requiring Defendants to pay a civil penalty of twenty-three thousand two hundred thirty dollars [sic] (\$23,200) within thirty days after entry of the Order. . . .

6. Defendants have failed to pay Plaintiff the civil penalty of twenty-three thousand two hundred thirty dollars [sic] (\$23,200) and that amount is now due and owing.

The complaint made similar allegations regarding the \$121,580 civil penalty and requested that "the Defendants, jointly and severally, be ordered to pay" the civil penalties, costs, and an additional \$10,000 civil penalty for failure to heed the earlier orders. The Paces were served with the complaint, yet failed to appear.

On January 22, 1996, the Cabinet filed a motion for default judgment which the trial court granted two days later. In April 1996, the Paces' bank accounts were unsuccessfully garnished but in October 1996, garnishment began on Donna's wages. In early November 1996, the Paces filed a motion to set aside the default judgment. The Paces argued that since the Cabinet's first order dismissed them, only KOK could be held liable. The Cabinet noted that under Kentucky Rules of Civil Procedure (CR) 55.02 the Paces were required to show good cause to set aside the default judgment; that the defense asserted by the Paces was without merit; and that the motion to set aside was not brought in a reasonable amount of time. The Paces responded that they merely had to make the motion within a year of the

judgment under CR 60.02(a) since it was based on "mistake, inadvertence, surprise or excusable neglect . . ." and that the Cabinet would not be unduly prejudiced by setting aside the judgment. The Franklin Circuit Court denied the Paces' motion to set aside the judgment. This appeal followed.

The Paces argue that the trial court erred in refusing to set aside the default judgment under CR 55.02 and CR 60.02. CR 55.02 states: "For good cause shown the court may set aside a judgment by default in accordance with Rule 60.02." CR 60.02 states, in part:

On motion a court may, upon such terms as are just, relieve a party or his legal representative from its final judgment, order, or proceeding upon the following grounds: (a) mistake, inadvertence, surprise or excusable neglect; . . . The motion shall be made within a reasonable time, and on grounds (a), (b), and (c) not more than one year after the judgment, order, or proceeding was entered or taken.

Setting aside a default judgment is, of course, a matter of discretion with the trial court. See Howard v. Fountain, Ky. App., 749 S.W.2d 690 (1988). The court should adopt a liberal attitude in considering same. See Ryan v. Collins, Ky., 481 S.W.2d 85 (1972). Under the circumstances of this case, we are of the opinion that the court abused its discretion and that the Paces should have been given an opportunity to defend the action in Franklin Circuit Court. Default judgments are not favored. See id.

To set aside the default judgment, the Paces must show,

in a timely manner, good cause for failing to defend and a meritorious defense to the judgment. CR 55.02; see Dant v. Progress Paint Manufacturing Company, Ky., 309 S.W.2D 187 (1958), and Howard, 749 S.W.2d 690. We believe the Paces have met their burden. As to "good cause", the Paces state:

Relying upon the plain language of the Secretary's orders, the Appellant's [sic] were unaware that they were to be held liable, due to the fact that the first Order specifically states that they were dismissed and the second Order does not list the Appellants as Defendants.

The Paces obviously did not believe that they were liable in the circuit court action as they had been individually dismissed as parties in the administrative arena. It is, indeed, easy to understand the confusion of a lay person in this regard.

The Cabinet seeks to impose liability upon the Paces by piercing the "corporate veil." As to a "meritorious defense", we harbor grave doubt about whether the facts of this case justify piercing the corporate veil and imposing personal liability upon the Paces. The use of that doctrine to impose personal liability upon corporate officials is reluctantly utilized. See Holsclaw v. Kenilworth Insurance Company, Ky. App., 644 S.W.2d 353 (1982). We view as specious the claim that KOK was the Paces' "alter ego" and that KOK engaged in fraudulent practices. As such, we think the trial court abused its discretion by refusing to set aside the default judgment. It seems to us that if a civil penalty is to be imposed upon the Paces, it must be in conformance with the precepts enunciated in KRS 350.990(9). See Natural Resources and

Environmental Protection Cabinet v. Williams, Ky., 768 S.W.2d 47 (1989).

For the foregoing reasons, the order of the Franklin Circuit Court is reversed, and this cause is remanded for proceedings consistent with this opinion.

GARDNER, JUDGE, CONCURS.

JOHNSON, JUDGE, DISSENTS AND FILES A SEPARATE OPINION.

JOHNSON, JUDGE, DISSENTING. I respectfully dissent. The trial court has broad discretion in the matter of default judgments; and an appellate court should not disturb the trial court's action except upon a showing of an abuse of discretion. Howard v. Fountain, Ky. App., 749 S.W.2d 690, 692 (1988); Richardson v. Brunner, Ky., 327 S.W.2d 572, 574 (1959). The Court in Richardson, stated as follows:

Let us consider the first motion to vacate under CR 60.02. For the purpose of this discussion we shall assume that the defendant, Richardson, had a valid defense. While highly questionable we shall likewise assume that he properly defined the defense in his motion. This does not of itself entitle the defendant to the relief sought. He must explain why he did not present that defense upon the trial and thus excuse his default.

Id. at 573 (citations omitted and emphasis added). See also Howard, supra; Jacobs v. Bell, Ky., 441 S.W.2d 448 (1969); and Dant v. Progress Paint Manufacturing Co., Ky., 309 S.W.2d 187 (1958).

Thus, the Paces must show both that they had a valid

defense and that their failure to timely assert that defense is excusable. I believe there may have been material issues of fact as to a defense that the Paces could possibly have raised; however, I would hold that the trial court did not abuse its discretion in ruling that the delay in asserting a defense was not excusable.

As to the defense actually raised, the Paces claim that their dismissal in the Cabinet's first order precluded the Franklin Circuit Court from having jurisdiction over them. They claim that the Cabinet cannot rely on its orders to enforce a judgment against them since only KOK was determined to be liable. However, the Cabinet brought the circuit court action to enforce the Cabinet's orders under KRS 350.990; and in an attempt to hold the Paces liable, it alleged the common law "alter ego" method of "piercing the corporate veil." See White v. Winchester Land Development Corp., Ky. App., 584 S.W.2d 56, 61-62 (1979). The Cabinet alleged that the Paces were individually liable for KOK's debt since the corporation was the alter ego of the Paces; the Paces conducted the business of KOK as if it were their own business; and the Paces used KOK to defraud the Cabinet and others. While I have serious questions as to whether the Paces had a valid defense as to the jurisdiction of the circuit court, I recognize that there may have been some factual issues concerning the Cabinet's allegation that KOK was the alter ego of the Paces.

However, even if I were to assume that the Paces may

have had a valid defense, the Paces simply never explained why they did not respond to the complaint and why they should be relieved from the judgment because of "mistake, inadvertence, surprise or excusable neglect." Under these circumstances, I cannot conclude that the trial court abused its discretion in refusing to set aside the default judgment. I would affirm the judgment of the Franklin Circuit Court.

BRIEFS FOR APPELLANTS:

Hon. Otis Doan, Jr.
Harlan, KY

BRIEF FOR APPELLEE:

Hon. Don R. Stephens, Jr.
Frankfort, KY