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Commonwealth of Kentucky

Court of Appeals

NO. 2007-CA-001624-MR

RICHARD WHITE;
VALERIE WHITE — APPELLANT

v.

APPEAL FROM FAYETTE CIRCUIT COURT
HONORABLE THOMAS L. CLARK, JUDGE
ACTION NO. 04-CI-05225

WHITAKER BANK, INC. — APPELLEE

OPINION
AFFIRMING

** ** ** ** **

BEFORE: THOMPSON AND DIXON, JUDGES; HENRY,[1] SENIOR JUDGE.

HENRY, SENIOR JUDGE: Richard and Valerie White appeal from an order granting summary judgment to Whitaker Bank, Inc., in a lawsuit alleging misconduct by the appellee and one of its employees in connection with a construction loan. The Whites contend that the trial court erroneously awarded

[1] Senior Judge Michael L. Henry, sitting as Special Judge by assignment of the Chief Justice pursuant to Section 110(5)(b) of the Kentucky Constitution and KRS 21.580.

summary judgment to the Bank upon their claims alleging fraud and negligent supervision. For the reasons stated below, we affirm.

FACTUAL AND PROCEDURAL BACKGROUND

In December 1997 the Whites organized Cliffview Resort, LLC, for the purpose of developing and operating a recreational project on property located in Wolf and Lee Counties, Kentucky. In February 1998 Cliffview Resort borrowed $1,664,408.00 from Whitaker Bank for the purpose of constructing an inn and conference center on the property. The Whites personally guaranteed the loan. The loan agreement included a provision that the Bank would not make advances under the loan unless it obtained a report by an independent inspector "reflecting a condition of such Collateral [i.e., the inn and conference center] acceptable to the Bank." As the independent inspector, the Bank retained Jonathan C. Skidmore.

Debbie Tipton was the loan officer of the bank originally assigned to oversee the loan. For unrelated reasons the Whites retained her brother, Randy Rose, as the general contractor on the project.

Rose began construction on the project in January 1998. By sometime in April 1998, the Whites were aware of Rose's failure to undertake the initial construction phase of the inn and conference center in a workmanlike manner, as evidenced by narrated video tapes made by Richard on April 29, 1998, and May 6, 1998. The Whites discharged Rose from the project on April 27, 1998.

As previously noted, as part of the loan disbursement process, the Bank retained Skidmore as an independent inspector to monitor the progression of the project for the purpose of confirming that further disbursements were justified. In connection with his inspections, Skidmore produced inspection reports. The first two of the reports, those dated February 22, 1998, and March 10, 1998, were submitted to Tipton. The reports contained negative commentary regarding Rose's performance on the project. Reports subsequent to March 10, 1998, were addressed to Whitaker Bank president Steve Hale. According to Tipton, she, in effect, recused herself from overseeing the loan when problems developed concerning her brother's performance on the project. The Whites allege that in violation of the Bank's normal policies and procedures, Skidmore's inspection reports were not provided to them. As further discussed below, this failure to provide the reports to the Whites' forms the basis for the fraud and negligent supervision claims at issue in this appeal.

Following the Whites' termination of Rose, they retained another contractor to complete the inn and conference center. The project was completed in late 1998. The Whites first defaulted on the loan in the winter of 2000-2001. Cliffview Resort was eventually sold for $2,230,000, with all of those proceeds going to the Bank in full satisfaction of the loan.

In the meantime the Bank had made a second loan to the Whites in the amount of $60,000.00. In 2002 the Bank filed a foreclosure action against the

Whites in Wolf Circuit Court involving the second loan, and the Whites filed various counterclaims against the Bank relating to the transaction.

On September 9, 2004, the Whites initiated the present case by filing a Complaint in Rowan Circuit Court. The parties eventually agreed that Rowan County was not the proper venue for the lawsuit, and agreed to transfer the case to Fayette Circuit Court. Accordingly, on January 25, 2005, the Whites filed an Amended Complaint in Fayette Circuit Court. The Original and Amended Complaints raised various claims relating to the aforementioned $60,000.00 loan. The trial court ultimately granted summary judgment upon those claims based upon the res judicata effect of the Wolf County case. The Whites have not appealed the award of summary judgment upon those issues, and all claims relating to the second loan are not relevant to this appeal.

As discovery progressed in the proceedings below, the Whites learned for the first time of the Skidmore inspection reports filed beginning in February 1998 at the outset of the construction project. The reports, as previously noted, contained adverse conclusions relating to Rose's work. Based upon the Bank's failure to contemporaneously disclose these reports, on January 26, 2007, the Whites filed a Second Amended Complaint alleging counts of fraud and negligent supervision in connection with the 1998 loan. These counts are predicated exclusively upon the Bank's (and Tipton's) failure to contemporaneously disclose the Skidmore reports and to take proper actions based upon the contents of the reports.

On July 11, 2007, the trial court entered an order awarding the Bank summary judgment upon all issues. As relevant here, the trial court awarded summary judgment upon the White's fraud and negligent supervision claims based upon the five-year statute of limitations period for bringing an action for fraud. The Whites have appealed only the award of summary judgment upon their fraud and negligent supervision claims.

STANDARD OF REVIEW

The standard of review on appeal when a trial court grants a motion for 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." *Scifres v. Kraft*, 916 S.W.2d 779, 781 (Ky.App. 1996); Kentucky Rules of Civil Procedure (CR) 56.03. "The trial court must view the evidence in the light most favorable to the nonmoving party, and summary judgment should be granted only if it appears impossible that the nonmoving party will be able to produce evidence at trial warranting a judgment in his favor." *Lewis v. B & R Corp.*, 56 S.W.3d 432, 436 (Ky.App. 2001), citing *Steelvest v. Scansteel Serv. Ctr., Inc.*, 807 S.W.2d 476, 480-82 (Ky. 1991).

"The moving party bears the initial burden of showing that no genuine issue of material fact exists, and then the burden shifts to the party opposing summary judgment to present 'at least some affirmative evidence showing that there is a genuine issue of material fact for trial.'" *Lewis*, 56 S.W.3d at 436, citing *Steelvest*, 807 S.W.2d at 482. The trial court "must examine the evidence, not to

decide any issue of fact, but to discover if a real issue exists." *Steelvest*, 807 S.W.2d at 480. The Kentucky Supreme Court has held that the word "impossible," as set forth in the standard for summary judgment, is meant to be "used in a practical sense, not in an absolute sense." *Lewis*, 56 S.W.3d at 436. "Because summary judgment involves only legal questions and the existence of any disputed material issues of fact, an appellate court need not defer to the trial court's decision and will review the issue de novo." *Lewis* at 436.

FRAUD

The Whites contend that the trial court erroneously awarded the Bank summary judgment upon their fraud claim. As previously noted, this claim is predicated upon the Bank's failure to provide the Skidmore inspection reports prepared in February through April 1998 when Randy Rose was the contractor on the conference center project and performing substandard work. The Whites suggest that Tipton failed to provide the reports because they reflected badly on her brother's work and she wanted to protect him from the potential consequences of Skidmore's negative evaluations.

The Whites contend that as a result of the failure of Tipton and the Bank to provide them with the inspection reports and timely address the problems identified therein, the construction of the inn and conference center was substantially and significantly delayed, resulting in significant increases in the cost of constructing the project. They suggest that this was what ultimately led to the failure of the project.

KRS 413.120(12) requires that a claim for fraud be brought within five years after the cause of action accrues. The present fraud claim was not brought until the White's filed their Second Amended Complaint on January 26, 2007, almost nine years following the alleged fraudulent conduct. Clearly, then, unless the limitations period contained in KRS 413.120(12) was tolled, the claim was brought outside of the five-year limitations period.

While the trial court awarded summary judgment upon this basis, in their brief, the Whites do not specifically address the statute of limitations issue. They do allege, however, that they did not learn of the Skidmore reports until the time of Tipton's deposition testimony in May 2006. Thus they imply that the limitations period was tolled pursuant to the discovery rule contained in KRS 413.130(3). This provision provides as follows:

> In an action for relief or damages for fraud or mistake, referred to in subsection (12) of KRS 413.120, the cause of action shall not be deemed to have accrued until the discovery of the fraud or mistake. However, the action shall be commenced within ten (10) years after the time of making the contract or the perpetration of the fraud.

However, the discovery rule contained in KRS 413.130 has been interpreted to provide that the limitations period begins to run when, through reasonable diligence, the defrauded party could have discovered the fraud.

> In order to enlarge the five-year statute of limitations to ten years, on a charge of fraud, appellant must allege and prove the fraud was not discovered within the five-year period and also allege and prove the fraud could not have been discovered within that period by the exercise of reasonable diligence. If there were no earlier actual

> knowledge, the limitation commences to run when by the exercise of ordinary care the fraud ought to have been discovered.

Madison County v. Arnett, 360 S.W.2d 208, 210 (Ky. 1962) (citations omitted). "If the five year period of KRS 413.120(12) has elapsed, the plaintiff must allege and prove that the fraud or mistake was not only not discovered within the five year period, but that it could not have been discovered sooner by the exercise of reasonable diligence." *Skaggs v. Vaughn*, 550 S.W.2d 574, 577 (Ky.App. 1977).

In the case at bar, the Whites have failed to demonstrate that with the exercise of reasonable diligence they could not have discovered the alleged fraud – i.e., the alleged cover-up of the Skidmore reports.

The Loan Agreement for the Cliffview Loan states that the Bank would not make advances under the loan unless it obtained a report by an independent inspector "reflecting a condition of such Collateral acceptable to the Bank." Moreover, Richard Wright admits that he met and became acquainted with Skidmore and knew he was doing inspections of the inn and conference center project for the Bank (though not at the time that Rose was on the project). Further, the Wrights knew from their own observations of the project that there were substantial problems with Rose's workmanship and the substandard quality of his work. From the foregoing it could have been deduced that reports had been provided to the Bank which reflected that there were defects in Rose's performance on the job.

Based upon the foregoing, the Whites, with the exercise of reasonable diligence and ordinary care, could have requested and obtained copies of the Skidmore reports within the five-year limitations period and discovered the alleged fraudulent conduct associated with the reports. As such, we do not believe that the Whites may avail themselves of the discovery rule contained in KRS 413.130(3). Accordingly, the statute of limitations bars their fraud claim.

NEGLIGENT SUPERVISION

The Whites' negligent supervision claim is derivative of their fraud claim. The allegation supporting this claim is that management personnel at the Bank failed to properly supervise Deborah Tipton so as to prevent her from covering up the Skidmore reports from the Whites and failing to take proper actions based upon the negative content contained in the reports.

Kentucky has adopted the tort of negligent supervision as described in the *Restatement (Second) of Agency* §213 and §§350-358, and in the *Restatement (Second) of Torts,* § 877. *Smith v. Isaacs*, 777 S.W.2d 912, 914 (Ky. 1989); *see Turner v. Pendennis Club*, 19 S.W.3d 117, 121-22 (Ky.App. 2000); *Oakley v. Flor-Shin, Inc.*, 964 S.W.2d 438, 442 (Ky.Ct.App. 1998). However, the tort of negligent supervision is a second tort that derives from a tort committed by the person negligently supervised. We believe the law is correctly stated in *Grego v. Meijer, Inc.*, 187 F.Supp.2d 689 (W.D.Ky. 2001) that the statute of limitations to be applied to a negligent supervision claim is the limitations period applicable to the underlying tort committed by the employee. *Id.* at 694. Thus, the same statute

of limitations applicable to a fraud claim – five years – is the limitations period applicable to the Whites' negligent supervision claim.

For substantially the same reasons as set forth in the previous section, we likewise conclude that Whitaker Bank was entitled to summary judgment upon the Whites' negligent supervision claim. Tipton's alleged conduct and the Bank's alleged negligent supervision occurred in early 1998, and the claim was not brought until early 2007, well outside of the limitations period. Moreover, for the same reasons as discussed above, the discovery rule contained in KRS 413.130(3) is not applicable under the facts at bar.

CONCLUSION

For the foregoing reasons the judgment of the Fayette Circuit Court is affirmed.

ALL CONCUR.

BRIEF FOR APPELLANT:

Michael J. Leibson
Morehead, Kentucky

BRIEF FOR APPELLEE:

Robert W. Kellerman
Frankfort, Kentucky

J. Mel Camenisch, Jr.
Lexington, Kentucky