SUPREME COURT OF FLORIDA

CASE NO.: 65,118

DIXIE NATIONAL BANK OF DADE COUNTY, etc.,

Plaintiff,

v.

EMPLOYERS COMMERCIAL UNION INSURANCE COMPANY OF AMERICA, etc.,

Defendant-Third Party Plaintiff-Appellant,

v.

DR. THOMAS F. CARNEY, etc., et al.,

Third Party Defendants-Appellees.

ON CERTIFIED QUESTIONS FROM THE UNITED STATES COURT OF APPEALS, ELEVENTH CIRCUIT, ON APPEAL FROM THE UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF FLORIDA

REPLY BRIEF OF APPELLANT

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INTRODUCTION

In this reply brief, Employers will use the same party designations and abbreviations used in its initial brief and in the appellees' brief. In addition, references to the appellees' brief filed by the Directors and American Home will be referred by the abbreviation "DB".

REPLY TO APPELLEES' STATEMENT OF THE CASE

The appellees devote a substantial portion of their statement of the case and facts (DB 7-13) trying to disparage Employers' position by showing that its initial theory was equitable subrogation and by asserting that its reliance on the assignment and on the conventional subrogation theory was "belated". (DB 10). This is transparently a diversionary device which has no legal significance. Neither the district court nor the appellees attempted to justify the summary judgment on the ground that Employers' amendment alleging the assignment was untimely. (R. 818-823; 921-930; DB 14-42).[1]

Another unjustified diversionary attempt to discredit Employers' position appears from appellees' repeated use of the pejorative verb "extracted"[2] to characterize Employers' obtaining of the assignment. (DB 9, 17, 23, 32). The choice of the verb is entirely the appellees' own. It does not come from the orders under review, nor is it supported by the record. The stipulated

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1 Employers' motion to amend to allege the assignment was granted by the district court in May, 1981 (R. 784), months before the entry of the orders under review. We concede that the amendment was an attempt by Employers "to improve its position" (DB 11), but we do not see how any stigma can attach to a litigant on that account. Every amendment is an attempt to improve the position of the party seeking to amend, else there would be no sense in amending.

2 According to the American Heritage Dictionary of the English Language, Houghton Mifflin Co. (1970) the word means "to draw out forcibly", or "to obtain despite resistance, as by contrivance or extortion. . ."

facts state merely that: "Employers and Dixie National settled their dispute and Dixie National gave an assignment of claims to Employers". (R. 872). There is no basis for the veiled suggestion that the assignment was anything other than a part of the consideration for the settlement, fairly bargained for and freely given.

It is true, as appellees' statement points out (DB 12-13), that Employers does not challenge the conclusion below that the evidence does not establish that the Directors had any actual knowledge of the embezzlement, dishonest purpose, or furtive design. It is equally true, however, that the appellees have not disputed (and have thereby impliedly conceded) that the evidence was sufficient to go to the jury on the issue of the Directors' negligence, and that, had the Bank been suing the Directors, it would, on the basis of the evidence of record, have had a cause of action against them for that negligence. Thus, a central legal issue implicit in the U.S. Court of Appeals' Certified Question I is whether Employers, by virtue of the assignment, stands in the shoes of the Bank.

REPLY ARGUMENT AS TO POINT I

The appellees correctly observe (DB 24) that Employers relies primarily on Dispatch Services, Inc. v. Airport Bank of Miami, 266 So.2d 127 (Fla. 3d DCA 1972) and on First National Bank of Atlanta v. American Surety Co., 71 Ga.App. 112, 30 S.E.2d 402 (1944) as authority for a "no" answer to the first certified

question. Employers' central reliance on these two cases is entirely appropriate for three reasons. First, unless and until this Court overrules a decision of a district court of appeal, the decision represents the law of Florida.[3] Second, the legal linchpin of the summary judgment below was the holding that even though this is a case of conventional subrogation based on an assignment, the "balancing of the equities" test applies; if that holding was wrong under Florida law, then the first certified question must be answered "no", and the summary judgment collapses for lack of legal support. Third, Dispatch Services is the only Florida case that has squarely addressed the question of whether the balancing test applies in cases of conventional subrogation, and it expressly adopted "the reasoning and conclusions reached by the Georgia court in First National Bank of Atlanta. . . "Dispatch Services, 266 So.2d at 129.

Employers has focused attention right where it should be -- on the one Florida case directly addressing the key legal issue. The appellees, on the other hand, have ranged far afield in trying to justify the decision below on the basis of the law and policy of foreign jurisdictions. The Florida cases which they cite do not deal with the central issue, and certainly provide no persuasive reasons why this Court should decide the conventional subrogation question any different than did the Third District Court of Appeal in Dispatch Services.

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3 Stanfill v. State, 384 So.2d 141 (Fla. 1980).

The cases of Dantzler Lumber & Export Co. v. Columbia Casualty Co., 115 Fla. 541, 156 So. 116 (1934); American Home Assurance Co. v. City of Opa Locka, 368 So.2d 416 (Fla. 3d DCA 1979) and Ruwitch v. First National Bank of Miami, 291 So.2d 650 (Fla. 3d DCA 1974), cert. denied 305 So.2d 196, cited by the appellees, (DB 15-16, 28, 38-40) discussed the equitable nature of subrogation generally without dealing with the question of conventional subrogation. No assignment was involved in any of those cases, or in Atlantic Coast Line R. Co. v. Campbell, 104 Fla. 398, 139 So. 886 (1932), also cited by the appellees. (DB 29-30). The Campbell case discussed assignments in conjunction with the subrogation of insurance companies, but merely held that an assignment by an insured to the insurer was not necessary for the insurer to maintain an action in subrogation against a tort-feasor. Neither that case nor any other Florida case cited by the appellees[4] provides any authority for their contention that a subrogation action based on an assignment requires a balancing of the equities.

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4 The Fifth Circuit cases cited by appellees on the subject of subrogation, American Fidelity & Casualty Co. v. United States Fidelity & Guaranty Co., 305 F.2d 633 (5th Cir. 1962), Compania Anonima Venezolana de Navegacion v. A. J. Perez Export Co., 303 F.2d 692 (5th Cir. 1962), and United States Fidelity & Guaranty Co. v. First National Bank in Dallas, 172 F.2d 258 (5th Cir. 1949) (DB 15, 16, 22-23) did not arise in Florida and did not apply Florida law. Moreover, only one of those decisions, the First National Bank in Dallas case, dealt with the issue here, and its holding is plainly contrary to the controlling decision in Dispatch Services, which recognized both the validity and efficacy of an assignment under virtually the same controlling facts as those in the Bank in Dallas case.

The appellees' argument that a fidelity insurer cannot avoid liability on the grounds that the insured's Directors negligently contributed to the loss (DB 35) is an attack on a strawman. Employers has paid its obligation to the Bank under the bond. It is not asserting the negligence of the Directors as a defense to the fidelity bond; rather it is asserting the claim of negligence which the Bank had against its Directors, by virtue of the Bank's assignment of that claim to Employers.

Appellees' argument that the bank's Directors should be considered inseparable from the bank in fidelity bond subrogation cases (DB 37) has no support in Florida law. The holding of the Wisconsin court to the contrary in First National Bank of Columbus v. Hansen, 84 Wis.2d 422, 267 N.W.2d 367 (1978) was based on that court's perception of the balancing of the equities. As already demonstrated, that holding has no validity in Florida, because Florida does not apply a balancing of the equities test in conventional subrogation cases. Dispatch Services, supra.

The appellees' attempt to discredit the plain holding of Dispatch Services is ineffectual. Their discussion of the case (DB 30-31) fails to demonstrate any valid reason why that decision should not control here. The main support cited for appellees' argument is the very order here under attack, in which Judge Davis attempted to discount Dispatch Services, by stating that it was not based on a "rule precluding equitable considera-

tions from conventional subrogation claims", but on "strong policy considerations which shifted the balance of the equities". (DB 24-25; R. 821). That holding patently misconstrued Dispatch Services, which rested squarely on the distinction between the two types of subrogation, which adopted the "reasoning and conclusions" of First National Bank of Atlanta, and which culminated in a holding that a complaint by a fidelity insurer against a bank, alleging conventional subrogation, could not properly be dismissed "for failure to state a cause of action on equitable grounds." Dispatch Services, supra, 266 So.2d at 129.

The appellees also attempt to distinguish Dispatch Services on the ground that the fidelity insurer in that case was the insurer of a bank customer and was suing the bank, while the fidelity insurer here insured the Bank and is suing the Bank's Directors. They characterize that distinction as "fundamental" (DB 25), yet do not show that it has any legal significance under Florida law. Apparently they mean to suggest that Florida would use the balancing of the equities approach in all conventional subrogations in which corporate directors are defendants, while rejecting it in all other conventional subrogation actions. The appellees have not cited -- and cannot cite -- any Florida authority from which it could be inferred that Florida would be inclined to bestow a sacrosanctity on corporate directors that would entitle them to such special treatment before the law. On page 25 of their brief, the Directors cite a number of cases

would entitle them to such special treatment before the law. On page 25 of their brief, the Directors cite a number of cases dealing with the legal efficacy of determinations by specially appointed litigation committees of disinterested corporate directors that it is not in the best interest of the corporation to pursue a derivative action against other directors. The appellees cite these cases for the proposition that corporate directors cannot be "completely divested" of the power to control litigation on behalf of the corporation, and they conclude from them that "claims by a corporation against its directors are not freely fungible . . . because such claims are an inherent matter of corporate governance." (CB 25-26).

Counsel for Employers must confess that he does not understand what these authorities have to do with the present case, or what valid purpose the Directors have in citing them. None of Employer's contentions is in any way contrary to the holdings of any of these authorities. There is nothing in these cases which casts the slightest doubt on the validity or efficacy of the Bank's assignment which forms the basis for Employer's conventional subrogation claim. The Bank itself executed the assignment in favor of Employers, so this is not a case in which it can be contended that Employers is somehow usurping a right which belongs to the Bank.

In footnote 1 (DB 26), the appellees assert that they have never conceded that the Bank's assignment was intended to

include claims against the Directors. It obviously makes no difference for the purposes of this appeal whether the Directors "concede" this point or not. They obtained their summary judgment without attacking the assignment in any way, other than to urge as a matter of law that Employers could not "improve its position" by relying on the assignment. The orders of the district court and the certification of the court of appeals both presuppose the validity of the assignment. In fact, the opinion on certification specifically states that "the Bank assigned Employers its right to any claims it might have against the third party defendants." (R. 771). Thus, there is no basis, either in law or in fact, for questioning the validity or efficacy of the assignment in the proceedings before this Court.

The appellees argue (on authority of 12 C.F.R. 7.5217 and Section 607.014, Florida Statutes), that if the Directors are held liable to Employers, they "would in turn have a claim for indemnification from the Bank for their losses." (DB 26). That argument is not properly raised in this Court for several reasons: First, the argument was not advanced in the appellees' brief in the Eleventh Circuit Court of Appeals; second, there is no support for the argument in the record below; third, the orders under review did not rest, even in part, on any right of the Directors to be indemnified by the Bank; and fourth, the issue of possible indemnification is not embraced, even impliedly, within the questions certified to this Court by the court of appeals.

Even if it were proper to raise the question of indemnification in this Court -- which it is not -- the argument lacks merit. The only supporting authorities cited provide that banks (12 C.F.R. 7.5217) or corporations generally (§607.014, Fla. Stat.) have the authority or power to indemnify directors for certain type of liability arising out of non-willful torts. Neither the federal regulations nor the state statute confers any right in the directors to be indemnified for damages assessed against them. In fact, §607.014(1) expressly limits a corporation's power to indemnify its directors to proceedings "other than an action by, or in the right of, the corporation. . ." (emphasis added). Here, the right of indemnification for which the Directors contend would come within the prohibition of the statute, because Employers (by virtue of the assignment) is seeking to enforce the right which the Bank had against its own directors for the breach of duties owed to the Bank. Employers thus stands in the shoes of the Bank, and is not presenting a third party claim of the type contemplated by the indemnification statute. Even assuming that a corporation or bank could lawfully undertake to indemnify its directors for wrongs committed against the corporation or bank which they were elected to serve, such a right would have to stem from an express contract clearly and unequivocally indemnifying the directors for liability resulting from their own negligence. See, 12 Fla. Jur.2d, Contribution, Indemnity, and Subrogation, §11. There is no evidence that any

such indemnification agreement exists in this case. Accordingly, the appellees' arguments based on an assumed right of indemnification against the Bank is without merit and should be rejected by this Court.

In Dispatch Services, the Third District Court of Appeal expressly "adopt[ed] the reasoning and the conclusions reached by the Georgia court in First National Bank of Atlanta . . . ." The appellees are closing their eyes to the language just quoted when they contend that the Georgia decision "is simply not reflective of Florida law" (DB 27). While it is true that the Georgia court relied on its state statutes to "break down the exclusiveness of equity" in subrogation matters (30 S.E.2d at p. 406), it is equally true that Florida expressly adopted by court decision the same rule which Georgia followed as a result of its statute.[5]

The argument by appellees that the distinction between conventional and legal subrogation is significant only in determining the source of the right to subrogation (DB 28-29), is squarely refuted by Dispatch Services, which held that a complaint alleging conventional subrogation could not properly be dismissed for failure to state a cause of action on equitable

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5 There is nothing unique or unusual in this. See, e.g., Hoffman v. Jones, 280 So.2d 431 (Fla. 1973), where the Court by judicial fiat abolished the absolute bar of contributory negligence, following the lead of other jurisdictions which had done the same thing by statute.

grounds. The general language in Boley v. Daniel, 72 Fla. 121, 72 So. 644 (1916) (DB 29) does not establish that conventional subrogation is applicable only to a party who pays another's debt, "having no interest in or relation to the matter." If this were the rule, an insurer which paid a claim and received an assignment could never attain the status of a conventional subrogee, because a liability insurer always has "an interest in or relation to the matter." Yet the Florida courts have repeatedly recognized the conventional subrogation rights of insurance companies based on assignments. In addition to Dispatch Services, see Forsyth v. Southern Bell Tel. & Tel. Co., 162 So.2d 916, 921 (Fla. 11st DCA 1964); Rosenthal v. Scott, 150 So.2d 433, 434 (Fla. 1961); and Morgan v. General Insurance Co. of America, 181 So.2d 175, 178 (Fla. 1st DCA 1965) ("[T]here is no doubt that appellee [the subrogated insurance company] could have proceeded independently against the defendant tort-feasors by taking from appellants [the insureds] an assignment and subrogation agreement"). Accordingly, the appellees are wrong in their contention that the distinction between the two types of subrogation has no significance other than in determining the original source of the subrogation. Florida, along with a number of other states, also distinguishes between the two types of subrogation for the purpose of determining whether a "balancing of the equities" is required for recovery. Since the Third District held in Dispatch Services that the "balancing of the

equities" test does not apply in conventional subrogation claims based on an assignment, the first certified question should be answered "No".

REPLY ARGUMENT AS TO POINT II

Most of the authorities relied on by the appellees under Point II have already been discussed in Employers' main brief and under Point I of this brief. The reasoning of the Wisconsin court in Hansen is fallacious because it treats a bank and its directors as indistinguishable entities for the purpose of applying the rule that an insurer may not sue its own insured. The well-reasoned decision of the U.S. District Court in Manufacturers Bank and Trust Co. of St. Louis v. Transamerica Insurance Co., 568 F.Supp. 790 (E.D. Mo. 1983) recognized this basic fallacy and respectfully declined to follow Hansen. This Court should do the same. The bank is an entity separate from its directors. A suit against the directors is not the same as a suit against the bank, and the authorities discussed on page 37 of the appellees' brief do not hold otherwise.

The case of Ruwitch v. First National Bank of Miami, 291 So.2d 650 (Fla. 3d DCA 1974), on which the appellees so heavily rely (DB 39-40) is distinguishable on its facts and is not contrary to Employers' position on this appeal. In Ruwitch, the insurer of a bank which had suffered a loss because of the forgery of certain loan instruments made payment to the bank and, without benefit of an assignment, sued two guarantors of the bad

debt. The district court of appeal, applying the equitable subrogation rule requiring superior equities in a subrogor, disallowed recovery on the ground that the equities of the surety for hire were not superior to those of the guarantors, because both parties were only secondarily liable for the bank's loss. The Ruwitch court simply held, on the particular facts before it, that the equities did not preponderate in favor of the paid surety so as to entitle it to equitable subrogation. The decision clearly does not hold that the equities must invariably preponderate against a paid surety.

The present case, unlike Ruwitch, is not one in which the party from whom subrogation is sought is only secondarily liable, nor is Employers seeking to impose on the Directors the liability of guarantors. The Directors here are being charged with primary liability for violating a duty which they owed directly to the Bank which they served. While the Directors are not guarantors of the honesty of a bank's employees, they are obliged to exercise reasonable care commensurate with their responsibilities as Directors. They are charged in this case with failing to exercise due care in their supervisory responsibilities as Directors. As stated in Joy v. North, 692 F.2d 880 (2d Cir. 1982) on which the appellees rely (DB 25):

> Directors who willingly allow others to make major decisions affecting the future of the corporation wholly without supervision or oversight may not defend on their lack of knowledge, for that ignorance itself is a breach of fiduciary duty. 692 F.2d at 896.

Contrary to the appellees' contentions, no injustice will result from permitting Employers to proceed with its subrogation claim, nor would enforcement of the claim "nullify" Employers' obligation to the Bank. Employers satisfied that obligation when it paid the Bank's claim. The present claim is not against the Bank, but against its Directors. The equities do not preponderate in their favor, since they are charged with a breach of their responsibilities to the Bank by their negligent failure to supervise and audit in a manner which would have prevented the embezzlement.

CONCLUSION

Based on the reasons and authorities advanced in the main brief and in this brief, the first certified question should be answered "No". If the first certified questions is answered "Yes", making it necessary to address the second certified question, that question should be answered "No".

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CERTIFICATE OF SERVICE

WE HEREBY CERTIFY that a true and correct copy of foregoing Reply Brief of Appellant was mailed to Edward G. Rubinoff, Esq., of PREDDY, HADDAD, KUTNER, HARDY & JOSEPHS, P.A., Attorneys for the Directors, 12th Floor, Concord Building, 66 West Flagler Street, Miami, Florida 33130; and to Michael J. Cappricio, Esq., of FOWLER, WHITE, BURNETT, HURLEY & KNIGHT, P.A., Attorneys for American Home Assurance Company, 5th Floor, City National Bank Building, Miami, Florida 33130, this 10th day of July, 1984.

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