O/a 12-8-88.

IN THE
SUPREME COURT OF FLORIDA

TRANSAMERICA INSURANCE COMPANY,

Petitioner,

CASE NUMBER: 72531

V.

BARNETT BANK OF MARION COUNTY, N.A.,

Respondent.

ON REVIEW FROM THE 5TH DISTRICT COURT OF APPEAL

BRIEF OF AMICUS CURIAE FLORIDA BANKERS ASSOCIATION

Original

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STATEMENT OF THE CASE

This is an Amicus Curiae Brief in support of the decision of the Fifth District Court of Appeal that funds earned but unpaid to a contractor are subject Florida's Uniform Commercial Code filing, perfection and priority provisions. This brief supports the ruling of the Fifth District Court of Appeal that the doctrine of equitable subrogation should not be applied to grant sureties super priority outside the Uniform Commercial Code because that would create uncertainty in commercial transactions and work inequity against the Banking Industry.

Respondent, Barnett Bank filed a complaint in the Circuit Court of Marion County to determine the question of priority between itself, as a bank which financed a contractor, and Transamerica Insurance Company, which guaranteed the contractor's payment or performance, as to earned but unpaid sums due from the owner to the contractor upon the contractor's default on the construction contract. The trial court granted partial Summary Judgment in favor of Barnett Bank and the surety appealed to the Fifth District Court of Appeals which affirmed the Circuit Court's ruling. This court granted the Petitioner, Transamerica Insurance Company's, request for Discretionary Review on September 6, 1988.

STATEMENT OF THE FACTS

For the purpose of this brief, Amicus accepts the facts as stated by the Respondent.

ISSUES PRESENTED FOR REVIEW

ISSUE I

Whether a surety on a construction bond is entitled to Special Treatment inconsistent with the Uniform Commercial Code

ISSUE II

Whether the doctrine of equitable subrogation should be applied to deprive a lender which has complied with the Uniform Commercial Code of its perfected security interest in amounts due a contractor from an owner.

SUMMARY OF ARGUMENT

The banking industry is a cornerstone of the construction industry. Banks provide construction contractors with working capital so that there are construction contracts for the insurance industry to bond. The banking industry only seeks equal treatment. The UCC should be applicable to commercial transactions involving sureties just as it is to other business entities. Application of the UCC to sureties will provide even

handed treatment to all and not give one group preference over another.

The position of the Petitioner and the industry which supports it is to apply a rule of law created long before the UCC in such a manner as to give them preferred status over others. The insurance industry (1) wishes to create an exception to the certainty of the UCC and (2) seeks special treatment by requesting that it be granted a special exception to the rule by which all other parties to a commercial transaction are bound pursuant to the Uniform Commercial Code.

There is no justification for the exception to the Uniform Commercial Code which the insurance industry seeks to provide for itself. Sureties have the same ability as any other commercial entity to protect their interests under the Code by filing.

The "equitable subrogation" that the insurance industry argues for grants them super priority over all other commercial entities. The position sureties argue for is more accurately described as "inequitable subrogation" because they seek an unjustified preferred status over all other participants in the same commercial transaction. The banking industry does not request special treatment; it simply does not want to be treated worse than other commercial entities which assist or finance contractors.

The Fifth District Court of Appeal's opinion is the proper interpretation and is consistent with the purpose of the UCC. It

should be affirmed because it will foster knowledge, certainty, and clarity in the law governing commercial transactions by making sureties, along with all other commercial entities, comply with the Uniform Commercial Code's filing and perfection requirements in order to protect their security interest. The Fifth District's decision is not prejudicial to the insurance industry, it merely requires that industry abide by the same rules as other commercial business.

ARGUMENT

I.

PETITIONER SEEKS SPECIAL TREATMENT INCONSISTENT WITH THE PURPOSE OF THE UNIFORM COMMERCIAL CODE

A. The purpose of the Uniform Commercial Code is to create certainty in commercial transactions.

The purpose of the Uniform Commercial Code ("UCC") is to eliminate confusion and provide certainty in commercial transactions by clarifying and simplifying the law governing commercial transactions. (UCC §1-102). To achieve that goal the UCC drafters provided a framework for filing and perfecting security interests so that parties to a commercial transaction can easily determine the exact nature of any interest other commercial entities may have in a given commercial transaction. In addition, the drafters promulgated a bright-line priority rule which gives the first party to file priority over subsequent parties. This efficient system of filing and the bright-line rule regarding priorities add clarity and certainty to the law governing commercial transactions in furtherance of the purpose behind the UCC.

The Uniform Commercial Code filing requirements assist all parties to commercial transactions because all security interests are made known to them. The public interest is also served by this system because it creates certainty in relationships between businesses and therefore, decreases the need for litigation in

order to determine the rights of parties to a commercial transaction.

B. The Doctrine Of Equitable Subrogation Is Inconsistent With The Purposes Of The Uniform Commercial Code Because It Creates A Preferred Position.

The doctrine of equitable subrogation is not applied in every dispute involving a surety over funds held by a government entity. As such, a court must determine on a case-by-case basis whether the surety or the bank is entitled to priority, and neither party to the transaction knows, at the time of its agreement with the contractor, what its rights will be upon default. Thus, applying the doctrine of equitable subrogation to priority disputes between banks and sureties only adds uncertainty to the law and hence, the doctrine defeats the certainty which the Uniform Commercial Code attempts to provide. Note, National Shawmutt Bank: Another Step Toward Confusion In Surety Law, 64 N.W.U.L. Rev. 582, 594 (1969); Comment, Equitable Subrogation -- Too Hardy a Plant to be Uprooted By Article 9 of the UCC? 32 U. Pitt. L. Rev. 580, 591 (1971); Suretyship: Subrogation Under the Uniform Commercial Code, 65 Colum. L. Rev. 927, 933 (1965).

In short, the insurance industry is defending an exception to the certainty of the Uniform Commercial Code. That is, an exception to the rule by which all other commercial enterprises are bound. Insurance companies are not foreigners to the realm

of commercial transactions. Indeed the insurance industry boldly argues that the bonding of construction contracts is so common everyone should assume that the surety has a priority security interest. However, the flaw in this line of reasoning is obvious; if anything, the development of the insurance industry's pervasive interest in these commercial transactions cuts in favor of requiring that sureties file UCC statements because the Code is designed to encompass the expansion of commercial practices. See, e.g., Division of Triple T Service, Inc. v. Mobil Oil Corp., 60 Misc 2d 720, 304 N.Y.S.2d 191 (N.Y. Sup. Ct. 1969), affirmed without opinion, 311 N.Y.S.2d 961 (App. Div., 1970)(The court noted that franchising was not alien to everyday commercial transactions and, therefore, falls within the purview of the Code.).

There is no authority for the surety's position that it should be granted super priority. There is no policy justification for the special treatment of a sureties when the well recognized Uniform Commercial Code filing system is available and they can protect their interests by filing. Comment, Equitable Subrogation -- Too Hardy a Plant to be Uprooted By Article 9 of the UCC? 32 U. Pitt. L. Rev. 580, 592 (1971)(noting that sureties are customarily first to enter into the transaction and thus, can easily protect their interest by being the first to file). Indeed, this is the same way any other party to the transaction would have to protect its interest. No

public interest is served by giving sureties a preferred position over any other commercial business. In fact, public interest is best served by requiring that sureties file a Uniform Commercial Code statements to protect their interest because the Code creates certainty in relationships between business entities. See, Comment, Equitable Subrogation -- Too Hardy a Plant to be Uprooted By Article 9 of the UCC? 32 U. Pitt. L. Rev. 580, 590-91 (1971). Thus, because of valuable policy considerations a surety's security interest in a contractor's accounts receivable should be filed pursuant to the Uniform Commercial Code.

There is no way to harmonize the insurance industry's position with the purpose of the Uniform Commercial Code. Clearly, the insurance industry is defending an exception which is inconsistent with the express purpose of the Uniform Commercial Code. Florida courts have recognized that because the Code's filing requirements add certainty to business transactions such exceptions are disfavored. See, Sun Bank, N.A. v. Parkland Design and Development Corp., 466 So. 2d 1089, 1092 (Fla. 5th DCA 1985). In this case the insurance industry merely seeks to perpetuate the problem of uncertainty the Uniform Commercial Code was specifically designed to eliminate. Thus, the insurance industry's argument for the application of the doctrine of equitable subrogation is at odds with the express purpose of the Uniform Commercial Code adopted by the Florida legislature and as such, its argument should be rejected.

It is important to note that the Fifth District Court of Appeal opinion results in no prejudice or injury to sureties. For a nominal filing fee, a mere $5.25,[1] a surety can protect its priority against subsequently obtained security interests. Transamerica Ins. Co. v. Barnett Bank of Marion County, N.A., 524 So. 2d 439, 446 (Fla. 5th DCA 1988).

By requiring sureties to file UCC financing statements the District Court's decision only made business dealings more certain, not less certain. Thus, the District Court implicity recognized that the doctrine of equitable subrogation is contrary to the purpose of Florida's Uniform Commercial Code.

II.

EQUITABLE SUBROGATION SHOULD NOT APPLY TO A SURETY'S INTEREST IN A CONTRACTOR'S ACCOUNTS RECEIVABLE OBTAINED PURSUANT TO A PAYMENT AND OR PERFORMANCE BOND

Generally, equitable remedies are denied to a party who could have protected himself but negligently failed to do so. Lanigan v. Lanigan, 78 So. 2d 92, 96 (Fla. 1955)(stating "equity aids the vigilant and not the indolent"); see also, Folsom v. Farmers' Bank of Vero Beach, 136 So. 524, 527 (Fla. 1931) (stating the doctrine of equitable subrogation applies only in situations where the law fails to provide relief). The Fifth

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1 Fla. Stat. § 15.091 (1987).

District Court clearly recognized this equitable principle and thus, decided not to apply equitable subrogation to assist the surety because it could have protected its interest by filing a UCC statement. Transamerica, 524 So.2d at 446.

Professor Gilmore, one of the leading commentators on the UCC has recognized that the bank's equitable claim is at least equal to the surety's.

> Both the surety and the bank make an essential contribution to the financing of the construction job. It is hard to see that one does more than the other, or disaster having come, has a more meritorious claim for reimbursement than the other. Both have gambled and lost.

2. G. Gilmore, Security Interst and Personal Property, 973, 979 (1965). Thus, because the equities between the bank and the surety are approximately equal the application of the doctrine of equitable subrogation in this situation would merely operate to do inequity, not equity. As such, the insurance industry's argument for the application of the doctrine of equitable subrogation in this case may be more accurately described as an argument for "inequitable subordination."

The doctrine of subrogation developed under the equitable maxim "equality is equity," and it is designed to apply only in those cases where the law fails to treat parties equally. Folsom v. Farmers' Bank of Vero Beach, 136 So. 524, 527 (Fla. 1931). Since the equities with respect to banks and sureties in the case

at bar are equal the application of the doctrine of equitable subrogation would merely function to do inequity to the bank. Thus, upon inspection of the equitable principles which gave birth to the doctrine of subrogation it becomes clear the insurance industry supports a perverted view of equity in its argument for an exception to the Uniform Commercial Code.

The surety in this case had an equal opportunity to file a UCC statement to protect its rights. If "equality is equity" then the insurance industry should not be granted super priority via the doctrine of equitable subrogation. The surety in this case failed to pay the $5.25 it would have taken to protect its rights pursuant to the UCC and seeks to shift the burden of its own neglect to the banks which complied with the law.

The manifest inequity that would result from permitting sureties to rely upon the doctrine of equitable subrogation in priority disputes with banks is patently clear. If the insurance companies can obtain the special treatment for which it argues, banks will be prejudiced because there will be no way for banks to assure themselves that an equitable lien (a species of secret lien) does not exist. Thus, banks would be exposed to a hidden and potentially financially devastating risk if the doctrine of equitable subrogation were applied to priority disputes between banks and sureties.

The insurance industry argues that a proposal to unconditionally subordinate a surety's security interest to that

of subsequent lenders regardless of whether the surety had perfected its interest was rejected. G. Gilmore, supra, at 977. Proposed § 9-312(7) would have granted banks super priority over sureties. Doubtless, the insurance industry opposed this proposed section and eventually persuaded the drafters not to adopt it. See, National Shawmut Bank of Boston v. New Amsterdam Casualty Co., 411 F.2d 843, 846 (1st Cir. 1969) (stating that by defeating proposed § 9-312(7) sureties had "won the battle to defend the preserve of subrogation"); Comment, Surety vs. Lender: Priority of Claims to Contract Funds, 10 Washburn L.J. 356, 364-65 (1971). Rejection of proposed § 9-312(7) did not, however, give sureties a superior lien. It simply left transactions to be goverened by the usual UCC rules. It did no more than create a level playing field. The insurance industry wants to tilt the field by exempting itself from the application of the UCC and thus create by use of equitable subordination the preferred position it claimed banks would not have under proposed 9-312(7).

It cannot be overemphasized that the District Court's decision results in no prejudice or injury to sureties. For a minimal filing fee the surety in this case could have fully protected its interests. The only thing the Fifth District has done is to establish a level playing field between insurance companies and sureties. The sureties argue for permission to assert an undisclosed interest but for lack of minimal effort

they could have protected. Granting sureties such a right is unjust and unnecessary and is not consistent with the Uniform Commercial Code.

CONCLUSION

There are no economic, commercial, equitable or policy justifications for the application of the doctrine of equitable subrogation to priority disputes between sureties and banks with respect to a contractor's accounts receivable. Conversely, all economic, commercial, and equitable policy considerations indicate that equitable subrogation should not apply to this situation.

Since the equities between banks and sureties are equal in this action the banking industry urges that the equitable maxim "equality is equity" should be applied and since the surety had an equal opportunity to protect its interest, like any other commercial entity would have, it should bear the burden of its own neglect. The doctrine of equitable subrogation should not be applied based upon some convoluted rationale in order to place the loss solely upon the bank and thus reward the surety for failing to file a financing statement.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by 1st class mail, postage pre-paid, this 24th day of October, 1988, to Robert E. Morris, Esquire of Morris and Rosen, P.A., at Suite #1100 Freedom Savings Building, 220 East Madison Street, Tampa, Florida 33602; to Tim D. Haines, Esquire of Green and Simmons, P.A., at Post Office Box 3310, Ocala, Florida 32678; to Frederick B. Karl, Esquire, Thomas J. Maida, Esquire and Patricia Hart Malono, Esquire of Karl, McConnaughhay, Roland & Maida, P.A., at Post Office Box 229, Tallahassee, Florida 32302-0229; and to David T. Knight, Esquire, Jeanne T. Tait, Esquire of Shackleford, Farrior, Stallings & Evans, P.A., at Post Office Box 3324, Tampa, Florida 33601.

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