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IN THE SUPREME COURT OF FLORIDA

TRANSAMERICA INSURANCE COMPANY, Petitioner, vs. BARNETT BANK OF MARION COUNTY, N.A., Respondent.	Case No. 72,531 District Court of Appeal, Fifth District Case No. 86-1328

ON APPEAL FROM THE FIFTH DISTRICT COURT OF APPEAL

PETITIONER'S INITIAL BRIEF ON MERITS

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ISSUES ON APPEAL

ISSUE I

WHETHER A SURETY'S PRIORITY AND CLAIM TO "EARNED BUT UNPAID" REMAINING CONTRACT FUNDS IN THE HANDS OF AN OWNER/BOND OBLIGEE, UNDER THE WELL-ESTABLISHED DOCTRINE OF EQUITABLE SUBROGATION, IS GOVERNED BY THE FILING/PERFECTION REQUIREMENTS OF ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE (CHAPTER 679, FLORIDA STATUTES).

ISSUE II

WHETHER A PERFORMING SURETY'S PRIORITY CLAIM AND RIGHT TO "EARNED BUT UNPAID" REMAINING CONTRACT FUNDS IN THE HANDS OF AN OWNER/BOND OBLIGEE IS A "SECURITY INTEREST" SUBJECT TO THE FILING OR PERFECTION REQUIREMENTS OF ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE (CHAPTER 679, FLORIDA STATUTES).

ISSUE III

WHETHER A TRIAL COURT MAY PROPERLY DENY A PARTY THE RIGHT AND OPPORTUNITY TO CLAIM SET-OFF AND WHETHER A TRIAL COURT MAY PROPERLY ENTER A PARTIAL SUMMARY JUDGMENT ON AN ISSUE WHICH IS NOT BEFORE THE COURT.

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STATEMENT OF THE CASE AND STATEMENT OF THE FACTS

For purposes of clarity and reference, as used in this Initial Brief, the letter "R" refers to the Record on Appeal (page numbers) and the letter "T" refers to the Transcript (page numbers) of transcribed proceedings, as the same were filed with the Fifth District Court of Appeal. Additionally, reference to paragraphs and page numbers to items contained in Record on Appeal (R) is sometimes utilized for ease of reference.

The litigation in the Circuit Court was instituted by the Plaintiff and Respondent, BARNETT BANK OF MARION COUNTY, N.A., due to the nonpayment of its obligors of a number of promissory notes. The Plaintiff and Respondent, BARNETT BANK OF MARION COUNTY, N.A., in part, sought declaratory judgment against TRANSAMERICA INSURANCE COMPANY, a Defendant and the Petitioner, that it had priority to unpaid contract funds based upon its perfected and recorded security agreements and financing statements. The Petitioner, TRANSAMERICA INSURANCE COMPANY, filed its Answer and Affirmative Defenses on or about December 17, 1984, and subsequently filed its Answer and Affirmative Defenses to the First Amended Complaint, with the same located at R 125-150 and R 1251-1279. Due to the fact that the Plaintiff's Complaint, the Corrected Complaint and the First Amended Complaint contain minor deviations, pursuant to agreement and stipulation of counsel for BARNETT BANK OF MARION COUNTY, N.A., Steven H. Gray, Esquire, it was agreed that the initial Answer and Affirmative Defense of TRANSAMERICA INSURANCE COMPANY would serve as appropriate pleadings with regard to the partial summary judgment issue.

On or about October 8, 1985, BARNETT BANK OF MARION COUNTY, N.A. filed its Motion for Partial Summary Judgment on the issue of priority to unpaid contract funds; and the said Motion is contained at R 1559-1726. On or about

February 20, 1986, TRANSAMERICA INSURANCE COMPANY filed its Motion for Partial Summary Judgment with regard to the prior right and claim of TRANSAMERICA INSURANCE COMPANY, as performing surety, to earned but unpaid contract funds, to the extent of performance; and the same is contained in R 1316-1319. Partial Summary Judgment was entered in favor of BARNETT BANK OF MARION COUNTY, N.A. (R 1336-1351); and the Trial Court entered its Order Denying Transamerica's Motion for Partial Summary Judgment (R 1542-1543).

TRANSAMERICA INSURANCE COMPANY timely filed its Notice of Appeal and Amended and Supplemental Notice of Appeal (R 1544-1546 and R 1547-1549). On March 24, 1988, the Florida Fifth District Court of Appeal filed its majority decision with written dissent; and Motion for Rehearing and Motion for Clarification were subsequently filed. The Motion for Rehearing and Motion for Clarification were denied by the Fifth District Court of Appeal on May 6, 1988.

TRANSAMERICA INSURANCE COMPANY timely filed its Notice to Invoke Discretionary Jurisdiction; and by Order entered September 6, 1988, the Florida Supreme Court accepted jurisdiction and discretionary review.

G. P. Turner Construction, Inc. was a contractor engaged in the construction business. In 1979, G. P. Turner Construction, Inc. and others entered into an Agreement of Indemnity instrument with TRANSAMERICA INSURANCE COMPANY. Thereafter, TRANSAMERICA INSURANCE COMPANY provided payment bonds, payment and performance bonds, contract bonds, subcontract bonds, and related bonds on behalf of G. P. Turner Construction, Inc., wherein G. P. Turner Construction, Inc. was the contractor and principal and TRANSAMERICA INSURANCE COMPANY was Surety. (R 1336-1351). BARNETT BANK OF MARION COUNTY, N.A. loaned funds to G. P. Turner Construction, Inc. on numerous occasions (R 1-120; R 217-338; and

R 423-543). BARNETT BANK OF MARION COUNTY, N.A. perfected, under the Uniform Commercial Code, its security interests in inventory, accounts receivable, contract rights, general intangibles, and chattel paper prior to any filing or recording of any Financing Statement by TRANSAMERICA INSURANCE COMPANY. (R 1337).

At issue before the Circuit Court and the Fifth District Court of Appeal was the priority positions of BARNETT BANK OF MARION COUNTY, N.A. (which had filed and perfected its financing statements) vis-a-vis the priority position of TRANSAMERICA INSURANCE COMPANY (as surety) under the doctrine of equitable subrogation, as a performing surety, since it had not earlier filed and recorded its financing statement (Agreement of Indemnity). (R 1559-1726 and R 1336-1351). The Affidavits and Depositions filed clearly reflect that the contractor and principal, G. P. Turner Construction, Inc., was not timely paying its bills as they became due. (R 705-713; R 714-761; R 762-818; R 819-899; R 900-936; R 955-1011; R 1012-1048; and R 1154-1203).

It is undisputed that BARNETT BANK OF MARION COUNTY, N.A. perfected its "security interest" prior to the time that TRANSAMERICA INSURANCE COMPANY filed and recorded its Agreement of Indemnity. (R 1559-1726 and R 1336-1351). The Trial Court and the Fifth District Court of Appeal have effectively ruled that TRANSAMERICA INSURANCE COMPANY's prior claim and right under the well-established doctrine of equitable subrogation is governed by and controlled by the perfection and recording requirements of Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes). [R 1336-1351; R 1357-1358; R 1542-1543; Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., 524 So.2d 439 (Fla. App. 5th DCA 1988)].

The Petitioner, TRANSAMERICA INSURANCE COMPANY, takes issue with the entry

of the Partial Summary Judgment in Favor of Plaintiff, Barnett Bank of Marion County, N.A. (R 1336-1351), the Order Denying Motion for Rehearing/Reconsideration (R 1357-1358), the Order Denying Transamerica's Motion for Partial Summary Judgment (R 1542-1543), and the majority decision (with written dissent) of the Fifth District Court of Appeal.

The issues on appeal to the Supreme Court are as follows:

ISSUE I

WHETHER A SURETY'S PRIORITY AND CLAIM TO "EARNED BUT UNPAID" REMAINING CONTRACT FUNDS IN THE HANDS OF AN OWNER/BOND OBLIGEE, UNDER THE WELL-ESTABLISHED DOCTRINE OF EQUITABLE SUBROGATION, IS GOVERNED BY THE FILING/PERFECTION REQUIREMENTS OF ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE (CHAPTER 679, FLORIDA STATUTES).

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WHETHER A PERFORMING SURETY'S PRIORITY CLAIM AND RIGHT TO "EARNED BUT UNPAID" REMAINING CONTRACT FUNDS IN THE HANDS OF AN OWNER/BOND OBLIGEE IS A "SECURITY INTEREST" SUBJECT TO THE FILING OR PERFECTION REQUIREMENTS OF ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE (CHAPTER 679, FLORIDA STATUTES).

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WHETHER A TRIAL COURT MAY PROPERLY DENY A PARTY THE RIGHT AND OPPORTUNITY TO CLAIM SET-OFF AND WHETHER A TRIAL COURT MAY PROPERLY ENTER A PARTIAL SUMMARY JUDGMENT ON AN ISSUE WHICH IS NOT BEFORE THE COURT.

ISSUE IV

WHETHER A TRIAL COURT MAY MAKE FINDINGS OF FACT IN A PARTIAL SUMMARY JUDGMENT WHICH ARE NOT SUPPORTED BY THE EVIDENCE AND RECORD.

SUMMARY OF ARGUMENT

ISSUE I

Upon default by the contractor/principal, a performing surety's priority and right to "earned but unpaid" remaining contract funds (including "retainage") in the hands of an owner/bond obligee, under the well-established doctrine of equitable subrogation, is not governed by or subject to the filing or perfection requirements of Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes). The enactment of Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes) did not abrogate or displace the doctrine of equitable subrogation, which principle has been in effect and understood since the 1800's. Principles of law and equity supplement the provisions of the Uniform Commercial Code; and one of such principles is the doctrine of equitable subrogation.

Due to the fact that a surety "stands in the shoes" of the owner/bond obligee and laborers and materialmen who provide improvements to real property, to the extent of performance, such surety is entitled to a priority right and claim to remaining contract funds (including retainage) which have not been paid by the owner/bond obligee to the defaulting contractor/principal.

Numerous authorities and jurisdictions have specifically held that a surety has prior right to such "earned but unpaid" contract funds. Decisions on this specific issue have been rendered by the United States Supreme Court, the Florida Supreme Court, numerous courts within the State of Florida and numerous other courts and jurisdictions. Additionally, established case law likewise holds that a surety's prior right and claim to earned but unpaid contract funds under the doctrine of equitable subrogation has not been displaced or abrogated by the enactment of Article 9 of the Uniform Commercial

Code (Chapter 679, Florida Statutes). Almost every court in the nation which has considered such issue has so held.

Upon default of the contractor/principal, a surety has first and prior right and lien on remaining unpaid contract funds, to the extent of the performance of its bond obligations and to the extent needed to complete the contract, under the doctrine of equitable subrogation. Such rights of a surety need not be "perfected" under Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes) because Article 9 of the Uniform Commercial Code is not applicable to such suretyship matters; and the performing surety stands in the place of the owner/bond obligee and proper bond claimants (subcontractors, materialmen, suppliers, etc.).

ISSUE II

The priority claim and right of a performing surety to "earned but unpaid" remaining contract funds (including "retainage") in the hands of an owner/bond obligee does not fall within the definition of a "security interest" subject to the filing or perfection requirements of Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes). Security interests under Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes) are consensual in nature. A performing surety's prior right and claim to earned but unpaid contract funds, under the doctrine of equitable subrogation, arises by operation of law and not by contract or agreement between the parties. The Uniform Commercial Code protects only "contract rights" and not those that arise by operation of law.

A suretyship undertaking is not a true financing arrangement or security interest as those conceptual phrases are commonly understood. Upon default of the contractor/principal, a performing surety occupies three (3) positions.

The surety stands in the shoes of the contractor insofar as there are receivables due to it; the surety stands in the shoes of laborers and materialmen who are paid; and the surety stands in the shoes of the owner/bond obligee, for whom the project was completed. When a performing surety assumes the position of the property owner (bond obligee) or the laborers and materialmen who have performed improvements to the real property, the position of such surety is not transposed into a "security interest".

The established and previously understood doctrine of equitable subrogation which provides a performing surety with a prior right and claim to unpaid contract funds should not be effectively abolished by mislabeling the rights of such performing surety as being a "security interest". The Florida Supreme Court should specifically rule and hold that a performing surety's rights under equitable subrogation do not constitute a "security interest" or a "contract right" under the Uniform Commercial Code, as the same arise by operation of law.

ISSUE III

A Trial Court may not properly deny a party the right and opportunity to claim set-off and may not properly enter partial summary judgment on an issue which is not before the Trial Court. A party's right to "set-off" is well established under Florida law. Specific provision for the same is set forth in Florida Rule of Civil Procedure 1.170.

The Trial Court in this litigation entered a Partial Summary Judgment which goes beyond the Motion for Partial Summary Judgment and purports to apply its holdings relating to accounts receivable and contract rights on a job-by-job basis. The Fifth District Court of Appeal did not effectively rule on this issue. Such decision effectively prohibits TRANSAMERICA INSURANCE

COMPANY and the owners/bond obligees from presenting to the Court the applicable law and facts concerning the right of set-off and the amounts relating to the same.

The Trial Court's expansive language in the Partial Summary Judgment in Favor of Plaintiff, Barnett Bank of Marion County, N.A. goes beyond the legal issues raised in the Motion for Partial Summary Judgment of Barnett Bank of Marion County, N.A.; and a summary judgment based on matters entirely outside the issues should not stand. Therefore, such ruling and finding of the Trial Court should be reversed and remanded.

ISSUE IV

A Trial Court may not make findings of fact in a partial summary judgment which are not supported by the evidence and the record. In rendering a summary judgment, no factual determinations should be made by the Trial Judge. Additionally, it is improper for a Trial Judge to make factual determinations in a summary judgment proceeding when there is no basis for such findings or when the facts are disputed.

Due to the foregoing, the "finding" in the statement of the Trial Court that "actual cash" was utilized by G. P. Turner Construction, Inc. "in the normal course of its business operations" should be stricken and set aside; and the failure of the intermediate appellate court to substantially address this issue should be addressed, with specific definitive opinion.

ISSUE I

WHETHER A SURETY'S PRIORITY AND CLAIM TO "EARNED BUT UNPAID" REMAINING CONTRACT FUNDS IN THE HANDS OF AN OWNER/BOND OBLIGEE, UNDER THE WELL-ESTABLISHED DOCTRINE OF EQUITABLE SUBROGATION, IS GOVERNED BY THE FILING/PERFECTION REQUIREMENTS OF ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE (CHAPTER 679, FLORIDA STATUTES).

The Trial Court and the majority opinion of the Florida Fifth District Court of Appeal effectively ruled and held that a Surety's priority and claim to "earned but unpaid" remaining contract funds in the hands of an owner/bond obligee, under the well-established doctrine of equitable subrogation, is governed by the filing/perfection requirements of Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes). In Paragraph 3 (Page 8) of the said Partial Summary Judgment, the Trial Court stated that "Based upon its prior compliance with the Florida Uniform Commercial Code, BARNETT has a superior claim to all accounts receivable and contract rights of TURNER which were earned or vested, but unpaid, as of the moment of the default by TURNER under any job or contract. The right of BARNETT to such accounts receivable or contract rights, up to the point in time set forth previously, is superior to any claim or interest held by TRANSAMERICA under a claim of equitable subrogation." (R 1343).

On appeal, the Fifth District Court of Appeal stated: "We hold that the surety's assignment from a contractor, although conditional or contingent upon the surety's liability following the contractor's default, constitutes a security interest subject to the filing and perfection requirements of U.C.C." Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, at Page 444. The majority opinion in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, initially recognizes the principle, concept and remedy known as "equitable subrogation". However, the majority

opinion, in a radical departure from virtually every judicial decision in the nation, states that a performing surety's priority right under equitable subrogation "just does not seem to describe the situation of the modern day payment or performance bond surety . . ." Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, at Page 445.

TRANSAMERICA INSURANCE COMPANY also had filed its Motion for Partial Summary Judgment that a performing surety is entitled to priority to and claim to "earned but unpaid" remaining contract funds in the hands of an owner/bond obligee, under the well-established doctrine of equitable subrogation, to the extent of payment and performance by such surety. (R 1316-1319). The Trial Court entered an Order denying TRANSAMERICA'S Motion for Partial Summary Judgment (R 1542-1543); and the Fifth District court of Appeal affirmed the Trial Court's ruling in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra. The rulings and findings of the Trial Court and the majority decision of the Florida Fifth District Court of Appeal concerning this issue are erroneous and contrary to virtually every case in the nation.

At the outset, it is important to understand the basis and apparent rationale of the Trial Court's decision and determination and the apparent bases for the majority decision of the Fifth District Court of Appeal which is now on appeal to this Court. The Trial Court apparently relied upon the Fifth District Court of Appeal case of Waterhouse v. McDevitt and Street Co., 387 So.2d 470 (Fla. 5th DCA 1980). In Waterhouse v. McDevitt and Street Co., supra, the Court held that the lending bank (Barnett Bank) had priority over the Surety (Fidelity and Deposit Company of Maryland) to contract funds. Both the Trial Court and the Respondent, BARNETT BANK OF MARION COUNTY, N.A., rely upon the language contained in Waterhouse v. McDevitt and Street Co., supra,

which states that a surety's "right to subrogation is a contract right controlled by the U.C.C." Waterhouse v. McDevitt and Street Co., supra, at Page 472. (R 1336-1351 and R 1559-1563). In Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, the majority opinion states that its holding "is consistent with, and parallel to, Waterhouse v. McDevitt and Street Co." At Page 446.

Two (2) factors must be noted with regard to the statement by the Fifth District Court of Appeal that a surety's "right to subrogation is a contract right controlled by the U.C.C." First, such statement by the Fifth District Court of Appeal was not supported by any citations of any authority which so holds; and the Appellate Court cited one (1) case for the exact opposite of the ruling and holding of the cited authority. Second, the statement by the Appellate Court was "dicta".

In support of its statement that a surety's "right to subrogation is a contract right controlled by the U.C.C.", the Appellate Court cited First Alabama Bank of Birmingham v. Hartford Accident & Indemnity Company, Inc., 430 F.Supp. 907 (N.D. Ala. 1977). The case cited by the Fifth District Court of Appeal specifically holds the exact opposite of the legal principle for which it is cited. In First Alabama Bank of Birmingham v. Hartford Accident & Indemnity Company, Inc., supra, the Federal Court specifically stated:

> The Uniform Commercial Code protects only "contract rights", not those that arise by operation of law, and every court which has considered the matter has held that a surety's equitable subrogation rights, upon default of its principal-contractor, arise by operation of law, not contract, and that therefore a surety is not required to file financing statements under the Uniform Commercial Code to preserve its rights to equitable subrogation in the event of its principal's default . . . (Citations Omitted) . . . Therefore, the Court rejects the Bank's first contention and holds that the Surety's failure to record its indemnity agreement does not defeat its equitable right to subrogation with respect to contract funds earned prior to its principal's default. (At Page 910). (Emphasis Added).

An additional factor which must be kept in mind when evaluating the statement of the Fifth District Court of Appeal in Waterhouse v. McDevitt and Street Co., supra, is that the referenced statement is pure dicta. In Waterhouse v. McDevitt and Street Co., supra, the Appellate Court even recognized the existence of the well-established doctrine of equitable subrogation. In its opinion, the Court stated:

> We question whether the doctrine of equitable subrogation ever came into play. This case does not involve the surety's obligation to perform upon default of its principal and its concomitant right to subrogation. Rather, the right to reimbursement was based solely on Fidelity's contract agreement with Martin . . . No equitable subrogation was involved because the principal was not in default. The only claim which Fidelity had was its right by contract to reimbursement for payment made in a good faith belief that they were necessary or expedient. 387 So.2d at 472.

In Waterhouse v. McDevitt and Street Co., supra, the Court had already determined that the principal was not in default and therefore the doctrine of equitable subrogation never came into play. Waterhouse v. McDevitt and Street Co., supra, at 472. "NO EQUITABLE SUBROGATION WAS INVOLVED . . ." (Emphasis Added). Waterhouse v. McDevitt and Street Co., supra, at 472. Based upon such judicial determination, any further decision or comment by the Appellate Court concerning priorities relating to equitable subrogation would be dicta. In the case before this court, the principal/contractor, for which TRANSAMERICA INSURANCE COMPANY was surety, was in default and it was not and had not been paying its bills as they became due on a timely basis for literally months prior to the institution of litigation. (R 705-713; R 714-761; R 762-818; R 819-899; R 900-936; R 955-1011; R 1012-1048; and R 1154-1203).

Of course, the law concerning what constitutes a "default" by a principal/contractor is likewise clear. No formal declaration of default is necessary or required. All that is required for default is that the contractor be

in default as a matter of fact. Default includes not timely paying bills as they become due. Travelers Indemnity Company v. West Georgia National Bank, 387 F.Supp. 1090 (N.D. Ga. 1974); Royal Indemnity Co. v. United States, 371 F.2d 462, 1978 Ct. Cl. 46 (1967). When there is default as a matter of fact, the completing surety is "entitled to the earned but yet unpaid progress payment." Royal Indemnity Co. v. United States, supra, at 1094.

In Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, the majority states that its holding is consistent with, and parallel to, Waterhouse v. McDevitt and Street Co." (at Page 446). Waterhouse v. McDevitt and Street Co., supra, specifically recognizes and understands the doctrine of equitable subrogation. Notwithstanding that fact, the majority decision in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, states that the principle, doctrine and remedy known as equitable subrogation "just does not seem to describe the situation of the modern day payment or performance bond surety . . ." (at Page 445). The two (2) decisions certainly do not appear to be either consistent or parallel.

In Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, the majority opinion refers to "The Federal View", points out that "the surety in this case relies on federal decisions" (at Page 443) and states that it finds "it to be in the best interest of the law of the state of Florida to not follow federal precedent . . ." (at Page 444).

"The Federal View" position of the majority is somewhat surprising. Florida Statute 255.05 is patterned after the Federal Statute known as the Miller Act. Miller v. Knob Construction Company, 368 So.2d 891 (Fla. App. 2d DCA 1979); Winchester v. State, 134 So.2d 826 (Fla. App. 2d DCA 1961); Delduca v. U.S. Fidelity & Guaranty Co., 357 F.2d 204 (5th Cir. 1966). Addi-

tionally, Florida courts have indicated that in order to resolve ambiguities under Florida Statute 255.05 that courts have looked to the Miller Act. Blosam Contractors, Inc. v. Joyce, 451 So.2d 545 (Fla. App. 2d DCA 1984). Moreover, Florida Statute 255.05 has even been referred to as "the Little Miller Act". W. G. Mills, Inc. v. M & MA Corporation, 465 So.2d 1388 (Fla. App. 2d DCA 1985).

A mere reading of the Federal Miller Act, 40 USC 270, et seq., and Florida Statute 255.05 (The Little Miller Act) indicates that the intents and purposes of the two (2) Statutes were and are identical. The objective to both Statutes is to require bonds for certain construction work on "public works" projects. It is difficult to understand how the majority, in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, believes that "federal cases stressed various factors and viewpoints which are not especially relevant to doing justice between civil litigants in a state judicial system." (At Page 443). Mere review of the cases, both State and Federal, reveals that the issues and positions of the litigants are identical. The bonds required and provided are to prevent liens on public properties and to provide some recourse for the owner/bond obligee in the event a contractor does not perform its obligations.

The doctrine of equitable subrogation relating to surety bonds has been in effect since the 1800's. Legal history traces the doctrine back to at least 1896 in the United States Supreme Court case of Prairie State National Bank v. U.S., 164 U.S. 227, 17 S.Ct. 124, 41 L.Ed. 412 (1896). The doctrine of equitable subrogation and a surety's prior right to earned but unpaid contract funds is clearly set forth in the United States Supreme Court case of Pearlman v. Reliance Insurance Co., 371 U.S. 132, 83 S.Ct. 232, 9 L.Ed. 2d 190

(1962).

In excess of a half a dozen cases which have been decided by Courts within the State of Florida have specifically dealt with the issue and have held that a performing surety has priority to earned but unpaid contract funds. Phifer State Bank v. Detroit Fidelity and Surety Co., 121 So. 571 (Fla. 1929); Florida East Coast Railway Co. v. Eno, 128 So. 622 (Fla. 1930); Union Indemnity Co. v. City of New Smyrna, 130 So. 453 (Fla. 1930); Commercial Bank in Panama City v. Board of Public Instruction of Okaloosa County, 55 So.2d 552 (Fla. 1951).

In addition to the cited Florida Supreme Court cases, other courts within the State of Florida have also recognized and understood the doctrine of equitable subrogation and the surety's prior right and claim to earned but unpaid contract funds. Such cases include Broward County, Florida Commission f/u/b/o General Electric Company v. Continental Casualty Company, 243 F.Supp. 118 (S.D. Fla. 1965); Midtown Bank of Miami v. Travelers Indemnity Company, 366 F.Supp. 459 (5th Cir. 1966); Aetna Insurance Company v. Poole and Kent Company, 303 F.Supp. 963 (S.D. Fla. 1969); and McAtee v. United States Fidelity and Guaranty Company, 401 F. Supp. 11 (N.D. Fla. 1975). Also, more recent cases decided within the State of Florida (applying Florida law) include: In Re: Ward Land Clearing & Drainage, Inc., 73 B.R. 313 (Bkrtcy. N.D. Fla. 1987); and In Re: Bush Painting Company, Inc., Case No. 88-04002, U.S. Bankruptcy Court, N.D. Fla. (1988).

A similar factual situation as is before this Court was presented in the case of Midtown Bank of Miami v. Travelers Indemnity Company, supra. In Midtown Bank of Miami v. Travelers Indemnity Company, supra, the Court stated:

> The law is clear that where a surety makes good under its contract of suretyship upon default of its principal, the surety acquires an

> equitable lien against any sums due its principal remaining in the hands of the one for whose protection the bond was written, and such claim of the surety is superior to any subsequent assignment by the principal to a third person even where such assignment was made prior to the default and payment by the sureties. (Citations Omitted). (At Page 462). (Emphasis Added).

Midtown Bank of Miami v. Travelers Indemnity Company, supra, has been cited with approval in Aetna Insurance Company v. Poole and Kent Company, supra. In Aetna Insurance Company v. Poole and Kent Company, supra, the surety bond was issued January 18, 1965; there was an assignment of contract monies by the subcontractor on May 19, 1965; the subcontractor defaulted on November 22, 1965; the surety completed the job on January 24, 1966; and the general contractor paid the subcontractors' assignment on December 16, 1966. The Court stated that the general rule of suretyship law is "that where insurer makes good under its contract of suretyship upon default of principal, the surety acquires an equitable lien against any sum due its principal remaining in the hands of one for whose protection the bond was written." (Citations Omitted). Aetna Insurance Company v. Poole and Kent Company, supra, at 964. The Court pointed out that the court in Midtown Bank of Miami v. Travelers Indemnity Company, supra, "stated unequivocally that had the funds used to pay the assignment been in the hands of the owner when such owner was notified of the default, then the surety company would have priority over the assignee-bank." Aetna Insurance Company v. Poole and Kent Company, supra, at 965.

In Broward County, Florida Commission f/u/b/o General Electric Company v. Continental Casualty Company, supra, the Federal District Court specifically stated that "it is settled Florida law that a surety completing work after abandonment by the contractor is subrogated to the rights of the owner in the retainage funds as against a money lender who took an assignment of those funds as security for the loan, even though the loan proceeds were used

to pay obligations connected with the bonded job which the surety might have been otherwise obligated to pay." (Emphasis Added and Citations Omitted). Broward County, Florida Commission f/u/b/o General Electric Company v. Continental Casualty Company, supra, at 125.

Following the clear weight of authority, and following applicable Florida law, in McAtee v. United States Fidelity and Guaranty Company, supra, the Federal District Court in the Northern District of Florida stated:

> a surety who completes a contract has an equitable right of subrogation to the rights of the owner . . . to withhold payments to the contractor upon default (Citations Omitted) . . . a surety on a payment bond . . . who by reason of the contractor's default has been compelled to pay debts of the contractor for labor and materials and to complete the contract, is entitled by subrogation to reimbursement from funds otherwise due the contractor but withheld by . . . [the owner] as a result of the contractor's default . . .
>
> Subsequent to passage of the Code in many states, there has been considerable discussion by the courts and commentators as to whether the surety's equitable subrogation claim constitutes a "security interest" under the Code and therefore can only be protected by compliance with the provisions of Article 9. However, all the still viable decisions to date hold that the doctrine of equitable subrogation in suretyship cases does not create a security interest under the Code and has not been displaced or controlled by Article 9. (Citation Omitted). (At Page 14). (Emphasis Added).

In McAtee v. United States Fidelity and Guaranty Company, supra, the Federal District Court cites with approval and authority the case of In Re: J. V. Gleason Co., 452 F.2d 1219 (8th Cir. 1971). In In Re: J. V. Gleason Co., supra, the Federal District Court specifically stated that "All of the still viable decisions hold that the doctrine of equitable subrogation in suretyship cases has not been affected by the adoption of the Code." (Emphasis Added.) In Re: J. V. Gleason Co., supra, at 1223. The Court goes on to cite approximately nine (9) separate cases from approximately seven (7) different jurisdictions in support of its ruling. In Re: J. V. Gleason Co., supra, at 1223. Additionally, the Court states that:

> a suretyship undertaking is not a true financing arrangement or security interest as those conceptual phrases are ordinarily and commonly used. There is no financing in the usual sense but rather a type of insurance running to the owner that insures the contractor's performance in case of default . . . surety merely steps in the shoes of the owner and other lien holders to the extent of the surety's performance. (Emphasis Added). (At Pages 1223 and 1224).

In addition to the cases previously set forth herein, there are numerous other cases indicating that a performing surety has priority and a prior right to unpaid contract funds. In National Shawmut Bank of Boston v. New Amsterdam Casualty Co., 411 F.2d 843 (1st Cir. 1969), the Court stated:

> When, on default of the contractor, it [the surety] pays all the bills of the job to date and completes the job, it stands in the shoes of the contractor insofar as there are receivables due it; in the shoes of the laborers and materialmen who have been paid by the surety, who may have had liens; and not the least, in the shoes of the government, for whom the job was completed. (At Page 845).

The Court further explained the position of the surety in such a case as follows:

> Here the payments were earned but unpaid prior to the contractor's default . . . but upon default, the surety which is obligated to complete the work steps into the shoes of the government - not of the contractor which on default has forfeited its rights. It is subrogated not only to the rights of the government to pay laborers and materialmen from funds retained out of progress payments . . . (Citations Omitted) . . . but also to the government's right to apply to the cost of completion the earned but unpaid progress payments in its hands at the time of default. (At Page 848).

Understanding the doctrine of equitable subrogation and the priority of a surety, the Alaska Supreme Court in Alaska State Bank v. General Insurance Co. of America, 579 P.2d 372 (Alaska 1978) cites with approval National Shawmut Bank of Boston v. New Amsterdam Casualty Co., supra. In Alaska State Bank v. General Insurance Co. of America, supra, the Court points out and states:

> . . . a surety's right to earned progress payments does not qualify as an interest in personal property subject to the filing provisions of the Alaska Uniform Commercial Code since the surety has the right

to complete the job it has bonded and apply any earned funds against its costs. (At Page 1368).

The Alabama Supreme Court has also dealt with the priority and superior right of a surety to contract funds. In Fidelity and Casualty Company of New York v. Central Bank of Birmingham, 409 So.2d 788 (Ala. 1982), the Alabama Supreme Court ruled that "The surety's right to equitable subrogation exists whether a surety steps in and physically completes the contract or whether it merely pays the laborers and materialmen under the contract". The Court stated that "Moreover, since the surety's equitable subrogation rights, upon default of its principal and contractor, arise by operation of law rather than by contract", a bank's argument that the application of "first in time, first in line" rule is not well taken. The Court held that the bonding company which was obligated to complete the contract through payment to materialmen was subrogated not only to the obligation of its principal to pay suppliers, but also to the right of the owner to offset any sums which may have been due to the contractor for such payment. The Court concluded "It makes no difference in this situation when the Bank's assignment was perfected because there is nothing owing . . . to pass by virtue of the assignment." Fidelity and Casualty Company of New York v. Central Bank of Birmingham, supra, at 971.

Virtually all courts which have dealt with the issue have held that a surety's right to equitable subrogation is not governed by the perfection/filing requirements under Article 9 of the Uniform Commercial Code (Chapter 679 of the Florida Statutes). The logic and rationale for the same is quite clear when one considers the specific terms of the Uniform Commercial Code and the original bases of the same. The Uniform Commercial Code specifically deals with established principles of law and equity. Florida Statute 671.103 (Article 1-103 of the Uniform Commercial Code) specifically provides that "Unless

displaced by the particular provisions of this Code, the principles of law and equity . . . shall supplement its provisions."

In addition to the foregoing, numerous other courts and jurisdictions have addressed the well-established doctrine of equitable subrogation and a surety's prior right and claim to "earned and unpaid" contract funds in the hands of the owners/obligees, including both "retainage" and "progress payments". Additional courts and jurisdictions recognizing the same include: American Fire & Casualty Co. v. First National City Bank of New York, 411 F.2d 755 (1st Cir. 1969); Canter v. Schlager, 267 N.E.2d 492 (Mass. 1971); Reliance Insurance Co. v. Alaska State Housing Authority, 323 F.Supp. 1370 (D. Alaska 1971); Finance Company of America v. United States Fidelity and Guaranty Company, 353 A.2d 249 (Md. App. 1976); Pembroke State Bank v. Balboa Insurance Company, 241 S.E.2d 483 (Ga. App. 1978); Lambert v. Maryland Casualty Company, 403 So.2d 739 (La. App. 1981); and Insurance Company of North America v. Northampton National Bank, 708 F.2d 13 (1st Cir. 1983).

The majority decision and opinion in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, does apparently recognize that there are two (2) different types of subrogation. One is known as contractual or conventional subrogation; and the other is known as "equitable subrogation". For unknown reasons, and contrary to virtually every judicial decision in the nation, the majority opinion indicates that the principle, doctrine and remedy of equitable subrogation "just does not seem to describe the situation of the modern day payment or performance bond surety . . ." (at Page 445). The actual holding of the majority opinion in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, is that the surety's assignment from a contractor constitutes a security interest subject to the filing and

perfection requirements of the Uniform Commercial Code. The Court stated:

> We hold that the surety's assignment from a contractor, although conditional or contingent upon the surety's liability following the contractor's default, constitutes a security interest subject to the filing and perfection requirements of U.C.C. (at Page 444).

Thus, the Fifth District Court of Appeal holds that the assignment by the contractor (the contractual or conventional subrogation) is a security interest; however, it goes further to effectively state that equitable subrogation does not apply.

In support of its apparent position that equitable subrogation did not apply to a performing surety, the majority appears to attach significance to the fact that the surety is in a business for profit and when it performs under its bond obligations it is merely fulfilling its own undertaking. What the majority overlooks is that such undertaking has been accomplished by the surety with the prior understanding and knowledge that it had and has the well-established remedy of equitable subrogation, which the Fifth District Court of Appeal apparently now wants to take away.

A significant factor is overlooked by the majority opinion in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra. Rhetorically speaking, one must ask whether the Fifth District Court of Appeal would rule and hold that, upon breach and default by a contractor, the owner is entitled to utilize the remaining contract funds in order to complete the construction project and to pay subcontractors and materialmen who have not been paid for work performed or materials delivered. Certainly, upon the breach by a contractor, the owner should be able to utilize the unpaid contract funds to complete the construction which was originally contemplated. It is important to understand and recognize that the equitable subrogation monies (earned but unpaid contract funds, retainage and unearned contract

funds) are not and were not profits for the surety, TRANSAMERICA INSURANCE COMPANY; but rather, all of the same have been used to pay subcontractors, materialmen and suppliers and to complete the construction project which was originally contemplated.

TRANSAMERICA INSURANCE COMPANY did, in fact, have a contractual or consensual right. The same is set forth in the Agreement of Indemnity of TRANSAMERICA INSURANCE COMPANY (R 721-725). The instrument itself clearly indicates that the contract right of the surety is in addition to and is not in lieu of its other rights. The Agreement of Indemnity specifically provides:

> That this Agreement shall constitute a Security Agreement to the Surety and also a Financing Statement, both in accordance with the provisions of the Uniform Commercial Code of every jurisdiction wherein such Code is in effect and may be so used by the Surety without in any way abrogating, restricting or limiting the rights of the Surety under this Agreement or under law, or in equity. (R 723). (Emphasis Added).

TRANSAMERICA INSURANCE COMPANY does, in fact, have a contract right with regard to its principal/contractor. The same are set forth in the Agreement of Indemnity instrument. (R 721-725). Since BARNETT BANK OF MARION COUNTY, N.A. perfected its security interest first, in the event there were any funds left over after completion of the construction and payment of all subcontractors, materialmen and suppliers, then and in such event, BARNETT BANK OF MARION COUNTY, N.A. should have priority to any such extra funds to the extent the same may be due to its debtor, based upon its perfection of the security interest in the same.

Ironically, the majority decision in Transamerica Insurance Company v. Barnett Bank of Marion County N.A., supra, effectively fails to cite any case law in support of its position and determination that TRANSAMERICA INSURANCE COMPANY does not have a prior right to earned but unpaid contract funds under

the doctrine of equitable subrogation. As pointed out in the dissent by Chief Judge Sharp:

> . . . the doctrine of equitable subrogation entitles the surety, to the extent of its performance and loss under its bond pertaining to the contract, to unpaid contract funds held by the owner which had been earned by the contractor prior to its default. (At Pages 447-448).

Chief Judge Sharp correctly points out that:

> . . . the overwhelming and essentially unanimous post-U.C.C. decisions in this country, federal as well as state courts, have held that (1) the surety's equitable right of subrogation is not a consensual security interest, (2) no U.C.C. filing is necessary to perfect the surety's interest, and (3) the surety's interest continues to be, as it was under pre-Code law, superior to the claim of a contract assignee, such as a bank. (At Pages 449-450).

Based upon the foregoing, it should be clear that TRANSAMERICA INSURANCE COMPANY, as performing surety, is entitled to a prior right and claim to earned but unpaid contract funds, to the extent of its performance of its obligations under the doctrine of equitable subrogation. The majority decision and opinion of the Fifth District Court of Appeal is a radical departure from established case law which has been previously understood for decades and effectively changes the law on a retroactive basis. If Florida desires to change the law which has heretofore been understood, any such change should be accomplished by Statute, after due public notice and discussion, and on a prospective basis only. The decision of the Fifth District Court of Appeal in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, should be reversed.

ISSUE II

WHETHER A PERFORMING SURETY'S PRIORITY CLAIM AND RIGHT TO "EARNED BUT UNPAID" REMAINING CONTRACT FUNDS IN THE HANDS OF AN OWNER/BOND OBLIGEE IS A "SECURITY INTEREST" SUBJECT TO THE FILING OR PERFECTION REQUIREMENTS OF ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE (CHAPTER 679, FLORIDA STATUTES).

A corollary issue related to the first issue is whether a performing surety's priority right and claim to "earned but unpaid" contract funds is a "security interest". Although related to the first issue, TRANSAMERICA INSURANCE COMPANY believes this issue is separate and distinct from the first issue.

Research of the applicable law in Florida has revealed no Florida appellate case which holds that a performing surety's equitable subrogation rights and prior lien and claim to earned but unpaid contract funds is a "security interest" subject to Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes). Even the majority decision and opinion in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, does not hold that a surety's rights under equitable subrogation is a "security interest". The Court held "that the surety's assignment from a contractor . . . constitutes a security interest . . ." (At Page 444, Emphasis Added). Notwithstanding the fact that there do not appear to be any Florida appellate cases ruling on this issue, there are numerous courts and jurisdictions which have specifically dealt with this issue and have ruled that a performing surety's priority right and claim to earned but unpaid contract funds under the doctrine of equitable subrogation is not a contract right, is not a financing arrangement, is not a "security interest" and is not subject to or governed by the filing or perfection requirements of Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes).

The Alaska Supreme Court has specifically dealt with this latter issue. In Alaska State Bank v. General Insurance Co. of America, supra, the Alaska Supreme Court stated:

> . . . a surety's right to earned progress payments does not qualify as an interest in personal property subject to the filing provisions of the Alaska Uniform Commercial Code since the surety has the right to complete the job it has bonded and apply any earned funds against its costs. (At Page 1368).

The same understanding and legal principle is set forth in the one (1) case which was cited by Waterhouse v. McDevitt and Street Co., supra. In First Alabama Bank of Birmingham v. Hartford Accident & Indemnity Company, Inc., supra, the United States District Court stated:

> The Uniform Commercial Code protects only "contract rights", not those that arise by operation of law, and every court which has considered the matter has held that a surety's equitable subrogation rights, upon default of its principal, arise by operation of law, not contract, and that therefore a surety is not required to file financing statements under the Uniform Commercial Code to preserve its rights to equitable subrogation in the event of its principal's default . . . (Citations Omitted) . . . Therefore, the Court rejects the Bank's first contention and holds that the Surety's failure to record its indemnity agreement does not defeat its equitable right to subrogation with respect to contract funds earned prior to its principal's default. (At Page 910).

In McAtee v. United States Fidelity and Guaranty Company, supra, the United States District Court for the Northern District of Florida, apparently applying Florida law, points out that the doctrine of equitable subrogation in surety cases does not create a "security interest" under the Uniform Commercial Code and has not been displaced or controlled by Article 9. The Court stated:

> . . . all the still viable decisions to-date hold that the doctrine of equitable subrogation in suretyship cases does not create a security interest under the Code and has not been displaced or controlled by Article 9. (Citations Omitted). (At Page 14). (Emphasis Added).

In a well reasoned decision, the United States Court of Appeals for the

Eighth Circuit extensively analyzes the relationship between Article 9 of the Uniform Commercial Code and the doctrine of equitable subrogation wherein sureties have priority right and claim to unpaid contract funds in In Re: J. V. Gleason Co., supra. The Court pointed out:

> The scope of the application of Article 9 is contained in § 9-102. It provides: "(1) . . . [T]his article applies . . . (a) to any transaction (regardless of its form) which is intended to create a security interest in personal property . . . including . . . accounts or contract rights; . . ." The official comment which accompanies this section indicates that this section was intended to apply to all consensual security arrangements under the Code. Obviously, the equitable lien, having been created by courts of equity, does not arise from the consent of the parties or by their intent, but by operation of law. Section 9-102(2) provides that the Article applies to "security interests created by contract." In the case of an equitable lien which arises because of the subrogation, the interest is not created by the contract but by law to avoid injustice. . . In the instant case, where the lien arose by operation of law, independent of any consensual agreement, it would seem clear that Article 9 dealing with consensual security interests would not be applicable. . . There is no reason to assume that the provisions of Article 9, are applicable to the suretyship situation. The surety's position is quite different than that of the commercial lender, who is obviously the primary target of Article 9. (At Page 1222).

In pointing out that the doctrine of equitable subrogation and a performing surety's priority right and claim to unpaid contract funds is not a "security interest", in In Re: J. V. Gleason Co., supra, the Court stated:

> . . . a suretyship undertaking is not a true financing arrangement or security interest as those conceptual phrases are ordinarily and commonly used. There is no financing in the usual sense but rather a type of insurance running to the owner that insures the contractor's performance in case of default. No funds are advanced at the time of the suretyship contract. Regardless of the terms of the suretyship agreement, the equitable lien does not attach until the surety pays out funds in performance of the suretyship obligation and either completes the construction contract or satisfies existing liens. In this type of situation the general creditors . . . are not discriminated against. There is no secret lien. The surety merely steps in the shoes of the owner and other lien holders to the extent of the surety's performance.
>
> Suretyship and general financing arrangements are different conceptually and there is no valid reason to paint them with the same broad brush nor is filing for the sake of filing a cogent reason for

> favoring the trustee and general creditors over a surety who has suffered the direct loss on performance. To introduce further complications of filing so-called financing arrangements, which are not in fact true financing arrangements, where no legitimate purpose is served is a waste of time and energy. (At Pages 1223 and 1224). (Emphasis Added).

The Pennsylvania Supreme Court has also held that equitable subrogation rights are not "security interests" within the meaning of Article 9 of the Uniform Commercial Code. In Jacobs v. Northeastern Corp., 206 A.2d 49 (Pa. 1965), the Pennsylvania Supreme Court said:

> Rights of subrogation, although growing out of a contractual setting and ofttimes articulated by the contract, do not depend for their existence on a grant in the contract, but are created by law to avoid injustice. Therefore, subrogation rights are not "security interests" within the meaning of Article 9. (At Page 55). (Emphasis Added).

When one fully understands the position of a performing surety, it is easy to realize that the surety's equitable subrogation rights and prior right and claim to unpaid contract funds is not a "security interest" or a "contract right". As is indicated in National Shawmut Bank of Boston v. New Amsterdam Casualty Co., supra, upon default of the contractor-principal, a performing surety occupies three (3) positions. First, it stands in the place of the contractor insofar as there are receivables due to it. Second, it stands in the place of laborers and materialmen who are paid and who may have otherwise had liens on the subject real property. Finally, it stands in the place of the owner/bond obligee, for whom the job was completed. Upon default by a contractor, the property owner who is holding remaining contract funds certainly has the right to utilize such funds to complete the construction under the contract and to pay subcontractors, materialmen and suppliers which were not paid by the defaulting contractor. Due to the breach and default of the contractor, unpaid contract funds are not owed or due to the contractor unless

and until there are remaining contract funds or a surplus left over, after the construction is completed and unpaid subcontractors, materialmen and suppliers who may have had a lien on the property are paid and satisfied. National Shawmut Bank of Boston v. New Amsterdam Casualty Co., supra.

The owner and bond obligee's right to utilize earned but unpaid contract funds is certainly not a "security interest". A performing surety which stands in the place of such owner/bond obligee, is in no different position than the owner/bond obligee; and such position of the performing surety is not transposed into it holding a "security interest". National Shawmut Bank of Boston v. New Amsterdam Casualty Co., supra.

Unpaid materialmen and suppliers have a prior right to earned but unpaid contract funds. In General Electric Supply Company v. Epco Constructors, Inc., 332 F.Supp. 112 (S.D. Texas 1971), the lending bank in that case urged that its claim, perfected in accordance with the provisions of the Uniform Commercial Code, takes priority over the claims of materialmen. It was undisputed that the bank had complied with the provisions of the Uniform Commercial Code and had, by security agreement, protected its assignment of accounts receivable and contract rights. The supplier, General Electric Supply Company, had not perfected any security interest through a filing of a financing statement. The United States District Court found:

> That the Uniform Commercial Code did not change the rights of materialmen to retainage and funds remaining on hand in connection with public works . . . Thus, the security agreement of the Bank is inferior to any allowed claim of a laborer or materialman. (At Page 115).

As indicated, a performing surety which makes payments to subcontractors, laborers, materialmen and suppliers, also wears the hat or stands in the place of such subcontractors, laborers, materialmen or suppliers. National Shawmut

Bank of Boston v. New Amsterdam Casualty Co., supra.

In summary, a suretyship undertaking is not a true financing arrangement or security interest as those conceptual phrases are ordinarily understood. A performing surety is entitled to equitable subrogation, and a prior right and claim to earned but unpaid contract funds, and the principle has been in existence for decades. In addition, the vast weight of authority and properly reasoned cases hold that a surety's equitable subrogation rights do not constitute a "security interest" under Article 9 of the Code (Chapter 679, Florida Statutes) and have not been displaced by the enactment of the Uniform Commercial Code. The well-established doctrine of equitable subrogation which provides prior right and claim to a performing surety for earned but unpaid contract funds should not be effectively abolished by labeling, or actually mislabeling, the rights of such performing surety as being a "security interest".

The Court in In Re: J. V. Gleason Co., supra, succinctly states a correct understanding. The Court stated:

> . . . before the Uniform Commercial Code, the doctrine of equitable subrogation in suretyship cases was firmly established and the question of whether this doctrine should be discarded is certainly a legislative one. The doctrine should not be abolished obliquely by labeling or mislabeling certain transactions as "security interests." (At Page 1224).

Of course, the Florida Legislature has dealt with this matter. Florida Statute 671.103 (Article 1-103 of the Uniform Commercial Code) specifically provides that "Unless displaced by the particular provisions of this Code, the principles of law and equity . . . shall supplement its provisions." The doctrine of equitable subrogation is one of "the principles of law and equity" which supplements the Uniform Commercial Code.

A more recent judicial decision also recognizes that the equitable subro-

gation rights of a performing surety do not constitute a "security interest". In 1987, the Court in In Re: Ward Land Clearing & Drainage, Inc., supra, stated that:

> Security interests are, by definition, created by contract, whereas, equitable rights of subrogation are ". . . created by law to avoid injustice. Therefore, subrogation rights are not 'security interests' within the meaning of Article 9." In Re: J. V. Gleason Co., 452 F.2d 1219, 1222 (8th Cir. 1971) quoting Jacobs v. Northeastern Corp., 416 Pa. 417, 206 A.2d 49, 55 (1965).

In the dissent in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, Chief Judge Sharp states that:

> . . . the surety's equitable right of subrogation is not a security interest which requires perfection by filing a financing statement to obtain priority under the U.C.C." (At Page 448).

Although there may be no Florida appellate court decisions on point, virtually every court in the nation which has specifically addressed the issue, including courts within the State of Florida and courts applying what is understood as the law in Florida, has ruled that a surety's equitable subrogation rights are not a "security interest" under Article 9 of the Uniform Commercial Code (Chapter 679, Florida Statutes).

The Florida Supreme Court should specifically hold that a performing surety's equitable subrogation rights are not a "security interest" under Chapter 679 of the Florida Statutes.

ISSUE III

WHETHER A TRIAL COURT MAY PROPERLY DENY A PARTY THE RIGHT AND OPPORTUNITY TO CLAIM SET-OFF AND WHETHER A TRIAL COURT MAY PROPERLY ENTER A PARTIAL SUMMARY JUDGMENT ON AN ISSUE WHICH IS NOT BEFORE THE COURT.

The Motion for Partial Summary Judgment of Barnett Bank of Marion County, N.A. sought a Partial Summary Judgment "as to the issue of priorities of security interests . . . and all accounts receivable, contract rights, inventory and other assets . . ." (R 1559). The Partial Summary Judgment in Favor of Plaintiff, Barnett Bank of Marion County, N.A. (R 1336-1351) goes beyond the Motion filed and purports to apply its holdings relating to accounts receivable and contract rights on a job-by-job basis, thereby effectively prohibiting the owners/bond obligees and the performing surety, TRANSAMERICA INSURANCE COMPANY, from presenting to the Court applicable law and the facts concerning the right of set-off.

The expansive language utilized by the Trial Court in the Partial Summary Judgment in Favor of Plaintiff, Barnett Bank of Marion County, N.A. which creates concern and problems includes the ruling in Paragraph 1 of Page 8 of the Partial Summary Judgment which indicates it pertains to "those accounts receivable of TURNER which were earned but unpaid as of the moment of the default by TURNER under <u>any individual job</u>." (Emphasis Added). (R 1343). Similar concern exists with regard to the Trial Court's holding in Paragraph 3 of Page 8 of the Partial Summary Judgment which indicates that "BARNETT has a superior claim to all accounts receivable and contract rights of TURNER which were earned or vested, but unpaid, as of the moment of the default by TURNER <u>under any job or contract</u>." (Emphasis Added). (R 1343).

Under the Motion for Partial Summary Judgment of Barnett Bank of Marion County, N.A. (R 1559-1726) the issue was not raised as to a bond-by-bond or a

job-by-job determination of priorities. Toward the end of the hearing on November 25, 1985, counsel for BARNETT BANK OF MARION COUNTY, N.A. verbally raised such issue indicating that determination of priority should be on a "bond-by-bond basis". TRANSAMERICA INSURANCE COMPANY took issue with the same. (R 1124-1126; T 58-60).

The rulings of the Trial Court including language of "under any individual job" and "under any job or contract" were not issues before the Court based upon the Motion for Partial Summary Judgment; and such rulings deny the bond obligees and TRANSAMERICA INSURANCE COMPANY the right of set-off.

In Transamerica Insurance Company v. Barnett Bank of Marion County N.A., supra, the majority decision starts to deal with the issue of common law set-off; however, the Fifth District Court of Appeal effective sidesteps the entire issue by stating that the surety would only be entitled to earned but unpaid contract funds "should any remain after the financing bank is paid . . ." (At Page 447). The Fifth District Court of Appeal apparently did not consider the common law set-off rights of the owner (in whose shoes the performing surety stands) and the fact that such issue was not before the Trial Court for determination.

In determining accounts receivable and contract rights on a job-by-job, bond-by-bond or contract-by-contract basis, the Court is effectively precluding the bond obligees and TRANSAMERICA INSURANCE COMPANY, as surety, from utilizing the right of set-off. A clear and simple example places the concern in proper perspective. Assume that there are eleven (11) bonded jobs for the Florida Department of Transportation, the property owner and bond obligee, wherein there is $5,000.00 in earned but unpaid contract funds on one job which are not necessary to be utilized to complete the work or pay subcontrac-

tors, laborers and materialmen on that one job, and the remaining bonded jobs require the expenditure of $400,000.00 over and above the remaining contract funds, including "earned but unpaid" funds, on those remaining jobs. If one considers each job on an individual basis, the Florida Department of Transportation, the owner/bond obligee, and the surety would be denied the right of set-off in applying the $5,000.00 on the one job to the additional loss and costs on the other jobs, although there are common parties and the contractor caused the additional cost of $400,000.00 on the other jobs. Such ruling and decision denies the owner/bond obligee and TRANSAMERICA INSURANCE COMPANY of the rights of set-off.

A party's right to a "set-off" is well established under Florida law. In Lynch v. Florida Mining & Materials Corp., 384 So.2d 325 (Fla. 2d DCA 1980), in an action by a property owner against a construction contractor for the contractor's untimely and unworkmanlike construction, the Appellate Court held that the Trial Court erred in failing to offset the unpaid contract balance against the property owner's award. Likewise, in Russell's Custom Home Repair, Inc. v. O'Donnells Auto Service, 411 So.2d 356 (Fla. 2d DCA 1982), the Court, in applying and utilizing the doctrine of set-off, ruled that the balance due on a contract should ordinarily be deducted from the amount of damages occasioned by defective work under the contract.

The availability of a right and claim of set-off is supported by Insurance Company of the South v. Kennedy & Ely Insurance, Inc., 143 So.2d 199 (Fla. 3d DCA 1962). A history of both recoupment and set-off is set forth in Allie v. Ionata, 466 So.2d 1108 (Fla. 5th DCA 1985); and the Court further points out that provision for the same is set forth in Florida Rule of Civil Procedure 1.170.

In Emmco Insurance Company v. Marshall Flying Service, Inc., 325 So.2d 453 (Fla. App. 2d DCA 1976), the Court reversed a summary judgment where the same was entered before the appellant had an opportunity under procedural rules to assert a set-off. The Court stated:

> We think this was improper and that appellant should have an opportunity to avail itself of this set-off. (At Page 454).

An order awarding summary judgment should not go beyond the legal issues raised; and any such order should be confined to the relief sought. Wells v. Thomas, 89 So.2d 259 (Fla. 1956). A summary judgment based on matters entirely outside the issues should not stand. Hoemke v. Hoemke, 355 So.2d 828 (Fla. 2d DCA 1978).

Based upon the foregoing, it was error for the Trial Court to effectively deny TRANSAMERICA INSURANCE COMPANY and the owners/bond obligees the right to claim set-off; and it was error for the Trial Court to effectively enter a Partial Summary Judgment on an issue which was not properly before the Court on the Motion for Partial Summary Judgment of Barnett Bank of Marion County, N.A. Therefore, such ruling and finding of the Trial Court and the affirmance by the Fifth District Court of Appeal should be reversed.

ISSUE IV

WHETHER A TRIAL COURT MAY MAKE FINDINGS OF FACT IN A PARTIAL SUMMARY JUDGMENT WHICH ARE NOT SUPPORTED BY THE EVIDENCE AND RECORD.

In the Partial Summary Judgment in Favor of Plaintiff, Barnett Bank of Marion County, N.A., the Trial Court made findings of fact which are not supported by the evidence or the record. Such procedure is incorrect and improper.

In Paragraph 10, Page 5 of the Partial Summary Judgment, the Trial Court states that "BARNETT financed the construction activities of TURNER during the period of active operation by TURNER with actual cash." The Trial Court goes on to state "That actual cash was used by TURNER in the normal course of its business operations . . ." (R 1340).

It is improper for a Trial Court to make such findings based upon the evidence and record before it. First, in rendering a summary final judgment, no factual determination should be made by the Trial Judge. 49 Fla. Jur. 2d, Summary Judgment, Section 42. Second, there is absolutely no basis for the apparent finding of the Trial Court that "actual cash was used by TURNER in the normal course of its business operations . . ." Based upon the Depositions filed of record and the Affidavits with regard to the same, one must wonder what, in fact, G. P. Turner Construction, Inc. was doing with the loans and funds which it may have received from BARNETT BANK OF MARION COUNTY, N.A. since it obviously was not paying all of its business related bills as they became due. The nonpayment of bills and obligations by G. P. Turner Construction, Inc. is clearly indicated by the Affidavit of John S. Clardy, Jr. (R 705-713); the Affidavit of Michael J. Sugar, Jr. (R 714-761); the Deposition of Richard C. Andrews of Barnett Bank (R 762-818); the Deposition of David S. Sutphin of Barnett Bank (R 819-899); the Deposition of Ed Russell (R 900-936);

the Deposition of John R. Brinson (R 955-1011); the Deposition of John S. Clardy, Jr. (R 1012-1048); and the Affidavit in Support of Judgment of Michael J. Sugar, Jr. (R 1154-1203).

Although this issue was raised on appeal before the Fifth District Court of Appeal, in the opinion filed in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, the Appellate Court did not address such issue.

Based upon the Complaint and the First Amended Complaint (R 1-120 and R 423-543), BARNETT BANK OF MARION COUNTY, N.A. apparently loaned substantial sums to G. P. Turner Construction, Inc. Presumably, G. P. Turner Construction, Inc. was obtaining progress payments on the construction projects wherein it was the contractor; and, in addition to monies loaned by BARNETT BANK OF MARION COUNTY, N.A., such progress payments created yet additional funds with which G. P. Turner Construction, Inc. could have paid its expenses "in the normal course of its business operations". The Complaint and First Amended Complaint (R 1-120 and R 423-543) clearly reflect that G. P. Turner Construction, Inc. was not paying BARNETT BANK OF MARION COUNTY, N.A. Additionally, the Depositions and Affidavits referred to in the foregoing paragraphs also indicate that G. P. Turner Construction, Inc. was not timely paying its bills as they became due. Not only was BARNETT BANK OF MARION COUNTY, N.A. not timely paid; but also, Clardy Oil Company was not paid (R 705-713 and R 1012-1048), St. Regis Southern Culvert was not paid (R 900-936), and the Affidavits of Michael J. Sugar, Jr. (R 714-761 and R 1154-1203) reflect over half a million dollars of unpaid bills by G. P. Turner Construction, Inc. Apparently, no one is sure what G. P. Turner Construction, Inc. was doing with all of the borrowed and "earned" monies; however, it is patently obvious that there is no

basis in evidence or the record which supports the Trial Court's statement that the "actual cash was used by TURNER in the normal course of its business operations . . ." (R 1340).

Factual issues are not to be tried or resolved in summary judgment proceedings. Mutual of Omaha Insurance Company v. Eakins, 337 So.2d 418 (Fla. App. 2d DCA 1976). The Trial Judge's unusual position that TRANSAMERICA INSURANCE COMPANY was in some way financing the contractor/principal by providing surety bonds becomes even more unusual when the Trial Court states that the contractor/principal was provided with actual cash by the bank and "That actual cash was used . . . in the normal course of its business operations . . ." (R 1340). Such "finding of fact" is unsupported by the evidence and is actually contrary to all of the evidence. The function of the court under the summary judgment procedure is not to decide issues of fact. Trustees of Internal Improvement Trust Fund v. Lord, 189 So.2d 534 (Fla. App. 2d DCA 1966).

In summary, it is improper for the Trial Court to make findings of fact. This is particularly so in light of the fact that there is no evidence whatsoever in the record that indicates that any such "actual cash" was utilized by G. P. Turner Construction, Inc. "in the normal course of its business operations". The evidence and record indicate to the contrary. Thus, the "finding" and the statement of the Trial Court should be stricken and set aside.

CONCLUSION

The Petitioner, TRANSAMERICA INSURANCE COMPANY, desires the Florida Supreme Court to reverse the majority decision of the Fifth District Court of Appeal, to reverse and set aside the Partial Summary Judgment in Favor of Plaintiff, Barnett Bank of Marion County, N.A., and to direct the entry of Partial Summary Judgment in favor of TRANSAMERICA INSURANCE COMPANY in accordance with its previously filed Motion for Partial Summary Judgment holding that TRANSAMERICA INSURANCE COMPANY has a prior right and claim to earned but unpaid remaining contract funds to the extent of its performance of its bond obligations, holding that equitable subrogation is not a "security interest" or "contract right".

The Petitioner, TRANSAMERICA INSURANCE COMPANY, also seeks opinion of the Florida Supreme Court that a Trial Court may not deny a party its rights to claim set-off and present evidence of the same, and a Trial Court may not enter a Partial Summary Judgment on an issue which is not properly before the Trial Court. Therefore, such ruling and finding of the Trial Court, and to the extent considered by the Fifth District Court of Appeal, the same should be reversed.

Finally, the Petitioner, TRANSAMERICA INSURANCE COMPANY, seeks the order and opinion of the Florida Supreme Court reversing, setting aside and striking the "findings" and the statements of the Trial Court pertaining to matters which are not supported by the evidence and the record.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been provided by U.S. Mail, postage prepaid, to TIM HAINES, ESQUIRE, and YOUNG JOE SIMMONS, ESQUIRE, of Green and Simmons, P.A., Post Office Box 3310, Ocala, Florida, 32678, Attorneys for Respondent; to DAVID T. KNIGHT, ESQUIRE, and JEANNE T. TATE, ESQUIRE, of Shackleford, Farrior, Stallings & Evans, Suite 1400, One Mack Center, 501 East Kennedy Boulevard, Tampa, Florida, 33602; and to THOMAS J. MAIDA, ESQUIRE, and FREDERICK B. KARL, ESQUIRE, of Karl, McConnaughhay, Roland & Maida, P.A., Post Office Drawer 229, Tallahassee, Florida, 32302-0229, this 30th day of September, 1988.

ROBERT E. MORRIS