OA 12-8-88

IN THE SUPREME COURT OF FLORIDA

NOV [illegible] 1988
CLERK, SUPREME COURT
By _____ Deputy Clerk

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 REPLY BRIEF ON MERITS

ROBERT E. MORRIS, ESQUIRE
Morris & Rosen, P.A.
4016 Henderson Boulevard
Tampa, Florida 33629
(813) 289-4009
Attorneys for Petitioner

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.

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.

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The significant and primary issue before this Court is the doctrine of "equitable subrogation" as it relates to sureties and the remaining and unpaid contract funds still in the hands of the owner and specifically named bond obligee. It is interesting to note that neither the Respondent nor the amicus of the Respondent is able to cite one (1) single case in support of their position or in support of the matter on appeal from the Florida Fifth District Court of Appeal (except for the Florida Fifth District Court of Appeal case which is under review by this Court, which case likewise cites no judicial decisions in support of its majority decision). On the other hand, the position of the Petitioner is supported by a plethora of case law, pre-Code and post-Code, from the Florida Supreme Court, numerous courts geographically situated in the State of Florida (applying Florida law), decisions from numerous state Supreme Courts, numerous appellate courts and federal courts (applying both "state law" and "federal law").

The apparent fundamental misunderstanding of the Respondent and the amicus curaie brief supporting the position of the Respondent is in not recognizing the position in which a performing surety stands upon the default of its principal and contractor. The surety's right to remaining contract funds to complete the construction project and pay subcontractors and materialmen is

the fundamental cornerstone of the surety relationship; and, recognizing the overwhelming and essentially unanimous judicial authority in support of the same (both pre-Code and post-Code), the sureties have established their premiums accordingly.

Upon default of the contractor and principal, a performing surety stands in the shoes of three (3) parties and wears three (3) separate hats. 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. (Emphasis Added). (At Page 845).

Related to the foregoing is the fact that the contractor is only entitled to receive and keep its profits. The contractor is a "trustee" for the contract funds which are to be used to pay its subcontractors and materialmen. Indeed, it is even a crime for a contractor to divert funds that are for subcontractors and materialmen. State v. Ferrari, 398 So.2d 804 (Fla. 1981). When construction monies are paid to a contractor wherein subcontractors, sub-subcontractors, materialmen, laborers and suppliers remain unpaid, the contractor is responsible for the payment of the same; and the sole "asset" of the contractor is its profits. The recognition and understanding of the same is fundamental in order to fully recognize and understand the reasons for the established law that a performing surety has prior right to earned but unpaid contract funds remaining in the hands of the owner. The Florida Fifth District Court of Appeal apparently did not either recognize or understand the underlying premise in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., 524 So.2d 439 (Fla. 5th DCA 1988). Virtually every other

court in the nation which has considered the matter has recognized and understood the same. For example, see: Jacobs v. Northeastern Corp., 206 A.2d 49 (Pa. 1965); Canter v. Schlager, 267 N.E.2d 492 (Mass. 1971); Travelers Indemnity Co. v. Clark, 254 So.2d 741 (Miss. 1971); United States Fidelity & Guaranty Co. v. First State Bank, 494 P.2d 1149 (Kan. 1972); Alaska State Bank v. General Insurance Co. of America, 579 P.2d 372 (Alaska 1978); Third National Bank v. Highlands Insurance Co., 603 S.W.2d 730 (Tenn. 1980); and Fidelity and Casualty Company of New York v. Central Bank of Birmingham, 409 So.2d 788 (Ala. 1982).

The well-reasoned and authoritative decision of In Re: J. V. Gleason Co., 452 F.2d 1219 (8th Cir. 1971), 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 lienholders to the extent of the surety's performance. (Emphasis Added). (At Pages 1223 and 1224).

The "federal cases" (although the courts are within the State of Florida and are apparently applying Florida law) cited in Petitioner's Initial Brief also recognize the underlying and fundamental principle. The 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); McAtee v. United States Fidelity and Guaranty Company, 401 F.Supp 11 (N.D. Fla. 1975); In Re: Ward Land Clearing and Drainage, Inc., 73 B.R. 313 (Bkrtcy. N.D. Fla. 1987); and In Re: Bush Painting Company, Inc., Case Number 88-04002, U.S. Bankruptcy Court, N.D. Fla. (1988).

In General Electric Supply Company v. Epco Constructors, Inc., 332

F.Supp. 112 (S.D. Texas 1971), 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 security agreement of the Bank is inferior to any allowed claim of a laborer or materialman." (At Page 115). Thus, it is clear that both an owner and a laborer or materialman have priority over a lending bank; and a performing surety is subrogated to such positions and interests.

Since the Respondent has absolutely no case law whatsoever to support its position or the majority decision of the Florida Fifth District Court of Appeal, the Respondent attempts to "bootstrap" its way into an argument and position by stating that the plethora of prior case law "bears little relevance to the modern day dispute between sureties and banks" and that the case law is "unconvincing in light of an analysis of the policies and the provisions of the Uniform Commercial Code." (Respondent's Brief, Page 5). The Petitioner is unable to ascertain what "modern day dispute between sureties and banks" and what "policies" have changed since the plethora of case law which does not support the position of the Respondent. A mere cursory review of <u>all</u> case law reflects that there are owners and/or materialmen and/or sureties on one side with a lender/contract assignee on the other side. The interested parties and their respective interests have consistently remained the same. If understood correctly, it appears that the Florida Fifth District Court of Appeal, the Respondent and the Respondent's positions are supported solely by "policy" and scholarly commentary. A mere viewing of the dates of such "scholarly commentaries" and the subsequent numerous cases which have continued to rule contrary to the Respondent's positions is indicative of the fallacy in its arguments and positions. The same have been available for consideration, and were presumably considered, by numerous courts and jurists;

and, even considering the same, the well-established law has continued to be in favor of the performing surety.

As surprising as the contention of the Respondent that prior case law has "little relevance to the modern day dispute between sureties and banks" and the "policy" argument is the most unusual statement of the majority in the Florida Fifth District Court of Appeal case in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, which refers to the "Federal View" and states that it is "in the best interest of the law of the state of Florida to not follow federal precedent and to decide the issues in this case based on our understanding of controlling state law", while totally ignoring at least four (4) prior Florida Supreme Court cases (as pointed out in the written dissent of the Florida Fifth District Court of Appeal). Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra. Most surprising is the majority statement in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, that the "federal cases" have various factors and viewpoints "which are not especially relevant to doing justice between civil litigants in a state judicial system." (At Page 443). The "federal view" distinction is difficult to comprehend. Equitable subrogation is a "common law" matter. There is no general "federal" common law. Erie Railroad Co. v. Tompkins, 58 S.Ct. 817, 304 U.S. 64, 82 L.Ed. 1188 (1938).

In state court or federal court, the civil litigants and issues have been and are the same. On one side you have the owners, subcontractors, materialmen and surety; and on the other side you have a lender/contract assignee. In federal court, you have the United States government as the "owner"; and in state court we have a "public authority" (Florida Statute 255.05) such as the State of Florida, Department of Transportation, as the owner. In resolving a performing surety's right to unpaid contract funds, the respective positions,

legal theories and interests of the owner, subcontractor, materialman, surety and lender/contract assignee are identical, whether in state court or federal court. A mere perusal of "The Miller Act" (40 USC 270, et seq.) and Florida Statute 255.05 will quickly reveal to the most casual observer why Florida Statute 255.05 is referred to by Florida courts as "The Little Miller Act" since the Statute is patterned after "The Miller Act" and Florida courts have indicated that courts should look to "The Miller Act" in order to resolve ambiguities under Florida Statute 255.05.

The Respondent rhetorically asks "Why shouldn't the surety file a financing statement like everyone else?" The answer is simple. The well-established case law has stated that the same is totally unnecessary and not required under the doctrine of equitable subrogation because equitable subrogation is not a "security interest", is not a consensual assignment, and is not a contractual right. Owners, subcontractors and materialmen do not need to "file"; and the performing surety stands in their shoes. Article 9 of the Uniform Commercial Code (Chapter 679 of the Florida Statutes) deals with consensual security interest; and the doctrine of equitable subrogation is not "consensual" but arises by operation of law, as every court in the nation which has addressed such issue has so held. A surety may want to file its "security agreement" in order to obtain priority to non-equitable subrogation type funds, just as TRANSAMERICA INSURANCE COMPANY did in the litigation before this Court. Such separate consensual "security agreement" may then afford the surety with priority, based upon time of filing, with regard to accounts receivable and contract rights of its principal wherein there has been no default and wherein the same are not related to a bonded job. Such was the case in Waterhouse v. McDevitt and Street Co., 387 So.2d 470 (Fla. 5th DCA 1980).

It is extremely important to understand that the performing surety is not "making a profit" under the doctrine of equitable subrogation. But rather, it is merely using the remaining contract funds in the hands of the owner to complete the job and to pay subcontractors, materialmen and laborers which the principal and contractor did not pay. A performing surety is subrogated to the rights of the owner. If the contractor defaults and it costs the owner (a "public authority" such as the State of Florida) all of or more than the unpaid contract funds to complete the construction project, is a lending bank entitled to obtain and recover from the owner (a "public authority" like the State of Florida) the "earned but unpaid" contract funds although the same were necessary to pay subcontractors and materialmen and to complete the construction? The Respondent and the Florida Fifth District Court of Appeal apparently believe that the answer to the foregoing question is in the affirmative.

Equitable subrogation is truly for the benefit of the owner and the subcontractors and materialmen. If a surety is not entitled to the remaining contract funds (to the extent it performs) upon the default of the contractor/principal, why should not a surety merely tell the owner and named bond obligee "mitigate the damages and contact us when you run out of contract funds"? What about the unpaid subcontractors and materialmen which improved the public works project and their monies are the "earned but unpaid" contract funds? When the bonded contractor defaults upon its construction contract, including non-payment of subcontractors or materialmen, the contractor has no receivables due to it unless the costs of completion are less than the remaining unpaid contract funds; and the receivables assignee, BARNETT BANK OF MARION COUNTY, N.A. in this case, only has the same "right".

The Respondent apparently wants the Florida Supreme Court to change the

law, retroactively, relating to the surety's prior right under equitable subrogation which has been established in the State of Florida for decades, and desires the new law in the State of Florida with regard to the doctrine of equitable subrogation to be contrary to the law in virtually every other jurisdiction. The Florida Supreme Court should reaffirm the law in the State of Florida, in conformity with every other jurisdiction and court, and specifically hold that a performing surety has prior right to unpaid contract funds to the extent of its performance and specifically hold that equitable subrogation is not a "security interest".

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 Respondent, BARNETT BANK OF MARION COUNTY, N.A., continues to misunderstand the position of TRANSAMERICA INSURANCE COMPANY with regard to the set-off issue. TRANSAMERICA's right of set-off, as a performing surety, is because it stands in the shoes of the owner and named bond obligee. National Shawmut Bank of Boston v. New Amsterdam Casualty Co., supra. In Re: J. V. Gleason Co., supra. McAtee v. United States Fidelity and Guaranty Company, supra.

The requirement of "the same parties and in the same right" as set forth in Everglade Cypress Co. v. Tunnicliffe, 148 So. 192 (Fla. 1933) is, in fact, present. The owner is the Florida Department of Transportation and the "other party" is G. P. Turner Construction, Inc. The parties have several construction contracts between themselves; and G. P. Turner Construction, Inc. defaults. The owner or owner's representative cures the breaches and defaults on contract number 1, with the cost and expenses of the same exceeding all monies remaining in the hands of the owner with regard to contract number 1. Due to the breaches and defaults of the contractor, the owner may set-off remaining contract funds under contract number 2 in order to pay for the extra expenses under contract number 1. The performing surety, TRANSAMERICA INSURANCE COMPANY in this case, is entitled to stand in the place and stead of the owner. This is not a set-off against BARNETT BANK by TRANSAMERICA INSURANCE COMPANY; but rather, it is the common owner setting off against the common contractor due to the breaches and defaults of the common contractor.

The bond-by-bond, job-by-job and set-off issue was not even before the Court at the time of the Partial Summary Judgment. Summary judgment should

not go beyond the legal issues raised; and a summary judgment based on matters entirely outside the issues should not stand. Wells v. Thomas, 89 So.2d 259 (Fla. 1956). Hoemke v. Hoemke, 355 So.2d 828 (Fla. 2d DCA 1978).

The action by the Trial Court in deciding an issue not even before it on summary judgment proceedings must 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.

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. 2d DCA 1976). It is not the function of the Court under the summary judgment procedure to decide issues of fact. Trustees of Internal Improvement Trust Fund v. Lord, 189 So.2d 534 (Fla. 2d DCA 1966).

The Trial Court states that the contractor/principal was provided with actual cash by BARNETT BANK and "That actual cash was used . . . in the normal course of its business operations . . ." (R 1340). Such "finding of fact" is improper. First, factual matters are not to be resolved in summary judgment proceedings. Second, it is difficult to comprehend how a finding could be made concerning "that actual cash" being used "in the normal course" of business operations considering the fact that G. P. Turner Construction, Inc. was not paying its subcontractors, suppliers or BARNETT BANK and was holding over half a million dollars of unpaid bills.

The finding by the Trial Court is improper and must be stricken and set aside.

ISSUE V

"WHETHER THE WRIT OF CERTIORARI FOR CONFLICT JURISDICTION WAS IMPROVIDENTLY GRANTED BY THIS COURT."

Although the jurisdictional issue has already been extensively briefed and the Florida Supreme Court has accepted discretionary jurisdiction, BARNETT BANK OF MARION COUNTY, N.A. again raises the topic of jurisdiction and discretionary review.

The Florida Supreme Court has accepted jurisdiction and discretionary review. The majority decision in Transamerica Insurance Company v. Barnett Bank of Marion County, N.A., supra, rendered by the Florida Fifth District Court of Appeal directly and expressly conflicts with four (4) prior decisions from the Supreme Court of Florida. 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 its majority Opinion, the Fifth District Court of Appeal ruled that a financing bank of a contractor has priority over a performing surety to earned but unpaid contract funds when the contractor defaults on bonded construction jobs. The referenced four (4) prior decisions of the Florida Supreme Court, following the doctrine of equitable subrogation, held that the performing surety has a prior right to earned but unpaid contract funds ahead of a lender and contract assignee.

This Court has jurisdiction and has exercised discretionary review pursuant to Florida Rule of Appellate Procedure 9.030(a)(2)(A)(iv) and pursuant to Article V, Section 3(b)(3) of the Constitution of the State of Florida.

CONCLUSION

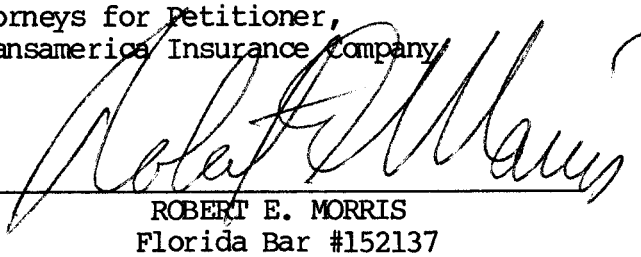
The Petitioner, TRANSAMERICA INSURANCE COMPANY, desires the Florida Supreme Court to reverse the majority decision of the Fifth District Court of Appeal, to reverse and set aside the Partial Summary Judgment in Favor of Plaintiff, Barnett Bank of Marion County, N.A., and to direct the entry of Partial Summary Judgment in favor of TRANSAMERICA INSURANCE COMPANY, 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 and holding that equitable subrogation is not a "security interest" or a "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 for consideration.

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

Respectfully submitted,

MORRIS & ROSEN, P.A.
4016 Henderson Boulevard
Tampa, Florida 33629
(813) 289-4009
Attorneys for Petitioner,
Transamerica Insurance Company

By: 

ROBERT E. MORRIS
Florida Bar #152137

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, 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; 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; and to J. THOMAS CARDWELL, ESQUIRE, of Akerman, Senterfitt & Eidson, 17th Floor, Firstate Building, Post Office Box 231, Orlando, Florida, 32802, this 14th day of November, 1988.

ROBERT E. MORRIS