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IN THE SUPREME COURT OF FLORIDA

CASE NO. 82,365

ALLEN GEE, as Official Liquidator of
UNIVERSAL CASUALTY & SURETY COMPANY, LTD. (in liquidation),
Petitioner,

vs.

SEIDMAN & SEIDMAN, and
BINDER DIJKE OTTE & CO., et al.,
Respondents,

BRIEF OF AMICUS CURIAE THE STATE OF FLORIDA, DEPARTMENT OF INSURANCE

Respectfully submitted,

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INTRODUCTION

By order dated November 30, 1993, this Court granted a motion by the Florida Department of Insurance (hereafter "the Department") to appear as amicus curiae in support of the Petitioner, Allan Gee. Gee is the duly-appointed liquidator of an insolvent Cayman Islands insurance company. On behalf of the insurer, Gee brought an action in Miami against the auditors who had reviewed the company's records, filed audit reports with the Cayman Islands insurance regulators which they knew were necessary for the company's licensure and continuation in business, yet failed to perform any investigation which would have revealed that the company's sole asset, a $10 million certificate of deposit, was entirely nonexistent. The jury reached a verdict in the liquidator's favor in the amount of $15.7 million, the total debts owed by the insolvent insurer after its liquidation.

The accountants filed an appeal, and the Third District Court of Appeal reversed the jury verdict, holding that the liquidator was estopped from bringing an action for negligence because the sole shareholder of the failed insurer was at all times fully aware of the fraud, and knowingly perpretrated same, citing the case of Cenco Inc. v. Seidman & Seidman, 686 F. 2d 447 (7th Cir. 1982). As soon as the appellate opinion was published, the Florida Department of Insurance moved for permission to appear as amicus, as did the National Association of Insurance Commissioners and the American Institute of Certified Public Accountants. These amici

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participated with the original parties in proceedings upon motions for rehearing and rehearing en banc.

Following a second round of oral arguments, the Third District issued an opinion denying rehearing but asserting that most of the arguments asserted by the Florida Department of Insurance and the National Association of Insurance Commissioners had not been raised below, and thus the original opinion did not pass on their validity. Finally, the Third District in a separate opinion certified to this Court the question of whether the liquidator should be estopped, where the fraudulent acts of company management "benefited" the company, an assumption with which the Department takes issue herein.

Gee has sought to invoke both conflict and certified-question jurisdiction, and all three opinions issued by the Third District are brought before this Court for review. The Department will seek to assert its concerns without unnecessarily duplicating the brief filed by the National Association of Insurance Commissioners, which is presently seeking amicus status, or by the Petitioner, Allan Gee.

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ADOPTION OF STATEMENT OF THE CASE AND FACTS

The Department adopts the Statement of the Case and Statement of the Facts as filed by the Petitioner, Allan Gee, and also the corresponding portion of the brief filed by the National Association of Insurance Commissioners.

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SUMMARY OF THE ARGUMENT

The Florida Department of Insurance, as regulator of insurance companies and as the statutory liquidator of insurers which become insolvent, has serious concerns about the Third District's holding that the liquidator of an insurance company is subject to the defense of equitable estoppel based upon the moral derelictions of prior company management, even though every other U.S. jurisdiction which has considered this question under modern insurance statutes has held otherwise. The Third District, without really analyzing the question, incorrectly assumed that there was an identity of interest between the insurance company and its sole shareholder. Most worrisome to insurance regulators, the case can be interpreted as establishing a rule of law to the effect that if an insurance company's management has knowingly concealed financial problems, independent auditors who negligently fail to report such problems to the regulatory authorities have no liability. Since insurance companies are regulated almost entirely by means of independent audit reports transmitted directly to regulatory authorities, and without satisfactory audit reports no company is allowed to remain in business, the Third District's holding is quite troubling. It will not only decrease the assets available to pay the claims of insolvent companies in liquidation, but will also have the effect of lessening the reliability of audit reports, making it both more difficult and more expensive to regulate insurance companies throughout the United States.

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ARGUMENT:

THE THIRD DISTRICT OPINION ESTABLISHES AN INCORRECT RULE OF LAW BARRING THE LIQUIDATOR OF AN INSURANCE COMPANY FROM RECOVERY AGAINST PROFESSIONALS WHO HAVE BEEN NEGLIGENT IN THEIR DUTIES, CAUSING DIRECT HARM TO THE COMPANY, ITS POLICYHOLDERS, ITS CREDITORS, AND THE PUBLIC GENERALLY

The Third District decision has immense public importance and, concomitantly, has the potential to cause severe harm to insurance-company regulators in particular, as well as countless innocent parties. The Florida Department of Insurance is well aware that the case at bar does not in fact involve an insurance company liquidated under United States law. However, the case was tried in Florida under this state's Rules of Civil Procedure. It was tried on negligence theories and the jury was instructed using Florida Uniform Jury Instructions. Both at the trial level and at the appellate level, the parties have cited and relied only upon cases from United States jurisdictions. Neither party has pointed out a significant difference between the law of the Cayman Islands under which the subject insurance company was liquidated and the laws of the United States. The Third District opinions cited nothing but American cases.

Accordingly, the Third District case is already being cited throughout the country as a decision under United States, and in particular, Florida, law. Since Florida's insurance statutes are similar to those of other states, as will be more fully discussed below, an erroneous ruling will have national impact. Thus, the Department is greatly concerned that the case will be construed to circumscribe the broad statutorily-awarded powers of an insurance

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company's liquidator, and shield from liability certain professionals whose breach of duty may proximately cause the insolvency of an insurance company, to the severe detriment of policyholders, creditors, and the public generally. Shielding such persons from liability not only diminishes the assets available for the liquidator who must pay the insolvent company's claims, but also has the effect of rendering every insurance company's statutory filings less reliable, so that enforcement of the laws for regulation of insurance companies will be both more difficult and more expensive throughout the United States.

There are several aspects of the Third District opinions which are particularly troublesome to the Department. First, the Third District accepts the blanket generalization that a liquidator "stands in the shoes of" or has no better rights than the prior management of the insolvent company, so that if the misdeeds of the company's former management would equitably estop those persons from recovery against other wrongdoers, the liquidator suffers from the same disability. Such a rule is contrary to the letter and spirit of modern insurance laws, which give to the liquidator the rights of the shareholders, policyholders, and creditors as well as the rights of the company itself. The Third District also wrongly assumes that the interests of the company are identical to the interests of its shareholders; for an insurance company, that assumption is certainly incorrect.

Further, if the Third District's view prevails, there will be no incentive for independent auditors of insurance companies to

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use proper care in detecting management fraud, and thus Florida's entire regulatory scheme will become unreliable. An auditor's negligent failure to report financial irregularities to regulatory authorities is a direct and proximate cause of loss to the company, because without the auditor's "clean" opinion, no insurer can continue in business. Unlike other types of business, a regulated insurance company while operating must always have assets in excess of its liabilities, so that if it becomes shaky, it can be liquidated or rehabilitated with no loss to the policyholders. Continuation of an insurer in business once it fails to meet this test of solvency cannot possibly lead to profit, but invariably causes the insurer to fall deeper into debt. As explained further below, the independent audit is the cornerstone of the regulatory process. Auditors and other professionals who deal with insurance companies are by rule and by statute required to report all financial irregularities directly to state authorities. Florida and its sister states require, and rely upon, an annual independent audit for each insurance company licensed in the jurisdiction. As Florida has recently experienced the massive public consequences of several insurance-company failures, this Court certainly understands that the public is not served by any weakening of the regulatory scheme.

I. MODERN INSURANCE COMPANY LIQUIDATION STATUTES GIVE THE LIQUIDATOR BROAD POWERS

The liquidation of an insurance company in American jurisdictions is controlled by a set of fairly uniform state

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statutes dating generally from the mid-1960's and 1970's. Similarly, the regulation of insurance companies in the United States is conducted via basically uniform sets of statutes. Organizations such as the National Association of Insurance Commissioners (NAIC), which has also petitioned for amicus curiae status in this case, and the Tort and Insurance Practice Section of the American Bar Association have contributed significantly to the development of uniform laws regulating insurance. The development of the law in this area has taken place in state courts and state legislatures, since regulation of insurance companies is a matter for state rather than federal regulation, pursuant to the McCarran-Ferguson Act, 15 U.S.C. sections 1011-1015. Accordingly, when seeking guidance in the area of insurance-company liquidations, a court should first examine cases decided under modern state insurance laws. Only if no cases exist on point would there be any need to examine cases decided under other statutory schemes such as bankruptcy, federal banking laws, or general corporate law, in the hope of obtaining some guidance. Such cases would, at any rate, be merely analogous to some degree and not controlling.

The parties to this proceeding will discuss at length the conflicting results and policy statements reached by various jurisdictions in accountant-liability actions in other, non-insurance contexts. The Department merely wishes to point out that the law derived from modern insurance codes, which will be discussed below, is quite uniform, and that it demonstrates the incorrectness of the Third District opinion. Since the case at bar

arises in the context of insurance, these are the cases that are truly on point.

Florida's version of the Uniform Insurers Rehabilitation and Liquidation Act, chapter 631 of the Florida Statutes, dates in its earliest form from 1959, but has been frequently amended and updated in accordance with similar state laws in other jurisdictions. The law is to be "liberally construed" to effect its purpose, which is "the protection of the interests of insureds, creditors, and the public generally," sections 631.001(3) and (4), Fla. Stat. (1993). This Supreme Court held that the purpose of Chapter 631 was "to secure equal treatment for all creditors wherever situated," Springer v. Colburn, 162 So. 2d 513,516 (Fla. 1964). Under Chapter 631, the Florida Department of Insurance is given the obligation to commence liquidation proceedings against an insolvent insurance company, and the Department must then "change hats" and accept appointment as the liquidator.

The statutory scheme for liquidating insolvent insurance companies is obviously designed to effect its stated purpose. An executive department of state government becomes the liquidator.[1] The statutory powers given to the liquidator are very broad. The liquidator may avoid preferences and fraudulent conveyances which were undoubtedly binding upon the corporation, but which "any creditor, stockholder, subscriber, or member of such insurer or affiliate might have avoided," section 631.261, Fla. Stat. (1993);

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[1] In most other U.S. jurisdictions, the state's Insurance Commissioner becomes, ex officio, the liquidator.

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see also, sections 631.262 (fraudulent conveyances) and 440.386, Fla. Stat. (1993) (conferring similar powers upon the liquidator of a self-insurance association). Once the liquidator is appointed, the insurer is no longer subject to suit; all proceedings against it are stayed, and can only be pursued as claims within the Receivership proceeding, see sections 631.041 and 631.153, Fla. Stat. (1993). All contract rights against the insurer are cut off at the date of liquidation, see section 631.192, Fla. Stat.(1993). Setoff rights which claimants may have against the insurer's assets are limited, see section 631.281, Fla. Stat. (1993). Some jurisdictions which have adopted the Uniform Insurers Rehabilitation and Liquidation Act have even held that Receiver of an insolvent insurance company cannot be bound by the arbitration provisions within the insurer's contracts, e.g., Corcoran v. Ardra Insurance Co., 156 A.D. 70, 553 N.Y.S. 2d 695 (App. Div. 1988); 77 N.Y. 2d 225, 566 N.Y.S. 2d 575, 567 N.E. 2d 969 (Ct. App. N.Y. 1990), cert. den., 111 S. Ct. 2260 (1991).

In furtherance of the purposes of the Uniform Insurers Rehabilitation and Liquidation Act, all funds which the liquidator is able to marshall are distributed according to statutory priorities which are set out in section 631.271, Fla. Stat. (1993). Under the current statutory scheme, the distribution of assets in a liquidated insurer's estate goes (after payment of administration expenses and any guaranty association's claims-administration expenses) to claims of the Federal government; next, to the wages of non-director, non-officer employees up to $2000; then to all

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claims under the policies, including third-party claims and claims of guaranty associations; then to general creditors; then to claims for unearned premium or premium refunds, or general creditors; then to claims of the state or local government, late-filing claimants, payments due on assessable policies, and only last of all to shareholders or other owners. Clearly, these statutes are weighted so that the company's ownership does not receive whatever assets are recovered.[2] Indeed, if the insurer's officers, directors, and shareholders have either intentionally or negligently contributed to the company's insolvency, it is the practice of the Florida Department of Insurance to bring actions against those parties. In the Department's experience, the Receiver, pursuing any and all actions available to it, is almost never able to recover enough assets to pay all of the estate's claims plus its administrative expenses. However, if there were ever to be sufficient funds to make any distribution to shareholders, wrongdoing shareholders could be barred from recovery in the exercise of the Receivership court's equitable jurisdiction. The Receivership proceeding is conducted entirely in equity.

It can be seen, therefore, that the purposes of the statutes require the liquidator to have substantially "bigger shoes" than the company's former management could have worn. The liquidator acts on behalf of innocent injured parties. It is not always bound even by legitimate contractual acts of the prior management, and is

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[2] Gee asserts, and the accountants do not contest, that the distribution he would make is similar to that in the Uniform Insurers Rehabilitation and Liquidation Act.

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empowered to invalidate most wrongful acts that have caused diminution of the company's assets. As explained above, there is virtually no way that a wrongdoing shareholder would ever receive a share of the assets of the Receivership estate. Thus, there is absolutely no reason to bar the liquidator from pursuing an action merely because prior management's moral derelictions would have equitably estopped those persons from pursuing such claims.

The Third District attempted, in its opinion on rehearing, to sidestep this problem by contending that the rights of anyone other than the insolvent company itself were not argued or presented below. However, since it was undisputed that the liquidator sought recovery only so that he could pay the creditors, this is really a distinction without a difference. The company itself had no continued existence, and the liquidator's duty was to recover assets on behalf of those who had been harmed, not the shareholder.

II. THE INTERESTS OF AN INSURANCE COMPANY'S SHAREHOLDERS ARE NOT IDENTICAL TO THOSE OF THE COMPANY

The question certified to this Court by the Third District is consistent with that Court's view of the case, but it perpetuates the error made by the original panel opinion, confusing the sole shareholder with the insurance company he owned. The question is:

> **WHETHER THE LIQUIDATOR OF A BANKRUPT COMPANY SHOULD BE PERMITTED TO RECOVER FOR LOSSES SUFFERED BY THE COMPANY'S CUSTOMERS AND CREDITORS, AGAINST AN AUDITOR WHICH NEGLIGENTLY FAILED TO DISCOVER THE FRAUD OF THE COMPANY'S MANAGER, WHERE THE MANAGER'S FRAUDULENT ACT WAS INTENDED TO AND DID BENEFIT THE COMPANY?**

Clearly, the question presumes that the interests of the company's

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sole shareholder (the wrongdoer) in continuing his fraud were entirely identical to the interests of the company, so that continuing the company in business past the point of its insolvency benefited the shareholder and thus the company.

Gee's counsel maintains that factually, the evidence below clearly established the shareholder "looted" the company for his own benefit. But even if actual looting had not occurred, a Cenco estoppel would be inapposite because, due to the peculiar nature of an insurance company, it can never be in the company's interest for its existence to continue after the "break-even" point which the regulators identify under statutory accounting principles. Each policy written after that point carries risks that cannot be paid from the company's assets in the ordinary course of business--such is the very definition of insolvency for statutory purposes, see sections 631.061 and 631.011(11), Fla. Stat. (1993).

Furthermore, the Third District's adoption of the "engine of theft" terminology from the Cenco case is also inapplicable to insurance companies. Policyholders are not "outsiders" of an insurance company. Rather, the company has the duty of utmost good faith toward all of its policyholders, and the sole justification for its existence is to maintain its solvency so that it can cover the risks it has assumed on its policies.

The business of insurance has its origins in antiquity. By the Middle Ages, insurance was an aspect of the "law merchant," a well-developed set of international rules separate and apart from the English common law. Thereafter, insurance continued to develop

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primarily by custom and usage, rather than by statute, until modern times. In the last century, all modern jurisdictions have developed extensive insurance codes which attempt to capture, define and occasionally modify the rules governing this industry. The courts very early concluded that the relationship between insured and insurer is one of "mutual confidence" which "pivots on good faith and fair dealing." "The courts have increasingly held the insurer to a standard of conduct commensurate with the public nature of its business, the adhesive character of its contracts, and the anticipated benefits of the coverage provided by such contracts." SHERNOFF, GAGE and LEVINE, INSURANCE BAD FAITH LITIGATION (Matthew Bender 1991), at section 1.02, citing Germania Ins. Co. of New York, 80 Ky. 223 (1882).

Government's interest in the law of insurance is intense because insurance is the primary method for risk-sharing in modern society. "Perhaps no other business affects the public so intimately as does the insurance business. It is entirely clear that the business of insurance is 'affected with a public interest' and therefore is subject to stringent regulation." VANCE ON INSURANCE, 3d ed. (West, 1951), at 36. Insurance companies have unique duties toward their policyholders that other businesses do not assume toward their clients or investors. For example, an insurer which fails to promptly pay or settle a claim is liable for damages beyond its contractual liability, see section 624.155, Fla. Stat. (1993). If the insurer unsuccessfully attempts to deny coverage, it is statutorily liable for the insured party's attorney

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fees in the coverage litigation, see section 627.428, Fla. Stat. (1993). The policyholder must likewise deal with the insurer in the utmost of good faith, and a policy may be void where there has been a misrepresentation by the applicant, see section 627.409, Fla. Stat. (1993). Unlike other businesses whose solvency is of no official concern, "One of the prime obligations of the insurer is to remain solvent so that its contractual obligations may be fulfilled," VANCE ON INSURANCE, supra, at 43. The failure of an insurance company is so detrimental to the public that guaranty associations have been created by the various states to provide a minimal "safety net" for stranded policyholders. States also extensively regulate the types of investments in which insurers may engage, requiring detailed financial reporting by all insurers licensed to do business in the state.

By its very nature, therefore, an insurance company cannot be an "engine of theft" against "outsiders," because what it sells is the willingness to assume the risk of its policyholders. The policyholders are not simply "customers" as the word is used by the Third District. There is in fact more identity of interest between the company and its policyholders and creditors than between the company and its own shareholders. The shareholders are entitled only to the excess profits which may be generated after all of the risk obligations are met. Where the company is unable to meet the risks it has assumed [i.e., it is insolvent], every modern jurisdiction will promptly liquidate the company, in which event the shareholders will have no legally recognizable rights to the

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company's assets. The shareholders are simply claimants in the insolvency estate, having the lowest possible priority and, even if there are any remaining assets, shareholders are subject to any equitable defenses which the liquidator may raise against their recovery. Thus, the law should not prevent a recovery by the company on behalf of its policyholders and creditors, where the wrongdoing is only that of the shareholders.

The Third District should have phrased its certified question as follows:

> **WHETHER THE LIQUIDATOR OF AN INSOLVENT INSURANCE COMPANY MAY RECOVER FOR THE LOSSES SUFFERED BY THE COMPANY, ITS POLICYHOLDERS, AND ITS CREDITORS, AGAINST AN AUDITOR WHO WAS RETAINED TO PREPARE AUDIT REPORTS TO REGULATORY AUTHORITIES BUT NEGLIGENTLY FAILED TO DISCOVER FINANCIAL WRONGDOING BY THE INSURANCE COMPANY'S MANAGEMENT?**

The correct answer is "yes," provided that negligence and proximate cause are established by a preponderance of the evidence, as they were in the case at bar.

III. MODERN INSURANCE REGULATORY SCHEMES RELY HEAVILY UPON THE FIDELITY OF INDEPENDENT PROFESSIONALS

Insurance companies domiciled in Florida and nearly every other state are required to file annual and quarterly financial statements with the state's Department of Insurance. In Florida, approximately sixteen hundred companies file annual audited reports, representing about $22 billion in annual written premium. Approximately 3500 carriers file annual audit reports with the NAIC. Throughout the United States, there are approximate 5000 to 6000 admitted carriers. The audited reports are the basic tools

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used in virtually every state for supervision and regulation of insurance companies. In Florida and in other states, every annual statement must be verified by a separate, independent audit prepared at the company's expense. Failure to comply with these regulations is a basis for revocation of an insurer's authority to transact business.[3] Section 624.424, Fla. Stat. (1993), which sets out Florida's version of these reporting requirements, also prohibits an insurer from using the same set of auditors for more than five consecutive years, obviously in order to preserve the independence of the auditors.

Even though the Department of Insurance is authorized to examine each insurer whenever necessary and is required to conduct an examination every three years (section 624.316, Fla. Stat. [1993]), the Department is generally unable to do more than the minimum number of required examinations. Even one of the three-year examinations may be omitted because in Florida, our legislature has specifically authorized the Department to rely upon the reports of independent certified public accountants, see section 624.316, Fla. Stat. (1991). This recent amendment to section 624.316 (and to similar statutes in other states) was supported by the NAIC, on the basis that under-funded state regulators simply have no choice other than relying on independent audits. Prior to this amendment, the Department already relied in practice, and by rule, upon independent audits.

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[3] Gee asserts, and the accountants do not contest, that the Cayman Islands have an identical requirement for an annual independent audit.

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To help assure the reliability of independent audits, Florida (as authorized by section 624.316(1)(c)) has by rule adopted NAIC standards for the conduct of insurance-company audits, Fla. Admin. Code R. 4-137.002. This Rule specifically imposes upon the independent auditor a duty to report to the Department any problems noted during examination, whether or not such problems have been satisfactorily resolved, and even any material fact learned subsequently. Each auditor is actually required to file with the Department a letter stating that he or she is familiar with the rules and statutes (including this rule) governing insurance company audits.

Because the independent auditor is the key to insurance-company regulation, and auditors freely assume, for significant compensation, certain very serious responsibilities, public policy requires that auditors be held to the standards they have agreed to follow. If the reliability of audit reports is in any way weakened, which will surely be the case if the threat of civil liability for negligent audits is removed or lessened, the regulatory duties of the Florida Department of Insurance and its counterparts in other jurisdictions will be rendered significantly more difficult. Indeed, the Third District opinion imposes <u>less</u> responsibility upon the independent auditors as the magnitude of the management's fraud increases. Since the Department does not have the resources to audit each statement filed by a regulated insurer and doubts that other states are in any better position, it is extremely important that independent auditors take

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responsibility for their reports.

IV. ALL U.S JURISDICTIONS WHICH HAVE CONSIDERED THE QUESTION UNDER MODERN INSURANCE LAWS HAVE HELD THAT THE LIQUIDATOR OF AN INSURANCE COMPANY IS NOT ESTOPPED TO CLAIM DAMAGES FROM THE COMPANY'S NEGLIGENT AUDITORS, REGARDLESS OF THE FAULT OF THE COMPANY'S PRIOR MANAGEMENT

Relying upon the principles established in the case of Cenco, Inc. v. Seidman and Seidman, 686 F. 2d 449 (7th Cir. 1982), the Third District opinion holds that the Receiver in this case is equitably estopped from pursuing the company's claims against its auditors inasmuch as the dishonest management of the insolvent company was well aware that the auditors' report was incorrect. Such a ruling is, however, in conflict with other cases interpreting the rights and powers of a liquidator under modern insurance codes.[4] It has been specifically held that under the powers both "express and implied" by the Uniform Insurers Rehabilitation and Liquidation Act as enacted in New Jersey, the liquidator of an insolvent insurer can pursue an action for wrongful continuation of corporate existence on behalf of the company, its creditors, policyholders, claimants and other beneficiaries of the estate, even though the parties controlling 80% of the insurer's parent were alleged to have joined the accountants in concealing the insolvency. "The weight of authority

[4] It should be noted that the Uniform Insurers Rehabilitation and Liquidation Act itself provides that the Act should be interpreted and construed so as to make uniform the law of the various jurisdictions which have enacted it, e.g., section 631.001(5), Fla Stat. (1993).

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makes it clear that a statutory receiver, such as the Liquidator here, may prosecute claims on behalf of creditors and policyholders of the insolvent company in order to preserve its estate assets," Matter of Integrity Insurance Co., 573 A. 2d 928, 933 (Superior Ct. of N.J., App. Div., 1990). Relying on Integrity, a Pennsylvania court ruled that the receiver of an insolvent insurer was not limited to the claims belonging to the "corporate body," but had standing to assert the claims "common to shareholders and general creditors" against the company's negligent auditors, Foster v. Peat Marwick Main & Co., 587 A. 2d 382 (Commonwealth Ct. of Pa., 1990).

In Schact v. Brown, 711 F. 2d 1343 (7th Cir. 1982), the Illinois Director of Insurance sought judgment against the insolvent insurer's officers, directors, parent corporation and auditors, based upon the wrongful continuation of the company in business past the point of its insolvency. As one would expect, the "Cenco defense" was immediately raised, Cenco having been decided by the same Seventh Circuit in the same year. The defendants argued that "the Director, standing in the shoes of [the insolvent company], is estopped from proceeding against the extra-corporate...defendants," Schact, supra, at 1346. Rejecting the defendants' argument, the Seventh Circuit explained that Cenco's estoppel should apply only if the situation met a "two-pronged test." A reviewing court would have to determine first whether the judgment sought would compensate the victims of wrongdoing, and second whether it would deter future wrongdoing. The Court found that the Director's action would not "send unqualified signals to

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shareholders that they need not be alert to managerial fraud," which had been a problem for the Cenco court. Recovery would benefit only the injured policyholders and creditors who had priority claims in the estate [just as they have under Florida and Cayman laws], meaning that there is no possibility of the type of "'perverse' compensation" [Id., at 1348] that had so greatly concerned the court in Cenco, and appears largely responsible for the holding in that case. Schact represents the clearest possible statement that the Cenco rationale was never intended to be applied in the insurance-insolvency context.

In Bonhiver v. Graff, 248 N.W. 2d 291 (Minn. 1976), the Supreme Court of Minnesota dealt with the same issue. "Defendants claim that Bonhiver, as Receiver for American Allied, cannot maintain this action, as defendants are charged simply with failing to discover the fraud committed by the company's own officers. Whether or not the company would be precluded from bringing this suit...'the receiver represents the rights of creditors and is not bound by the fraudulent acts of a former officer of the corporation,'" 248 N.W. at 296, citing Magnusson v. American Allied Ins. Co., 290 Minn. 465, 473, 189 N.W. 2d 28 (1971). In addition, the case of Corcoran v. Frank B. Hall & Co., Inc., 149 A.D. 165, 545 N.Y.S.2d 278 (Supreme Ct., App. Div. 1989), while not specifically discussing equitable estoppel, holds that the liquidator has exclusive standing to assert the claims of the company, its policyholders, and its creditors against the auditors who failed to discover the company's insolvency, allowing it to

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continue in existence and incur massive debts.

<u>Corcoran v. Hall, supra,</u> also gives short shrift to any contention that the auditors' misconduct was not the proximate cause of loss to the company. The court recognizes that correct reporting could have led to early regulatory action to rehabilitate the company when it might have been possible to accomplish such rehabilitation. "To posit that there was no injury to Union [the insurer] under these circumstances belies the very reality that Union no longer exists as a consequence of the failure to check the spread of the financial ills when the company might have been saved." <u>Id.,</u> 545 N.Y.S. 2d at 284. Even in a situation where the company may not be a candidate for rehabilitation, the same reasoning applies, since each month that it continues to write policies it incurs significant new liabilities which "come to roost" as debts of the insurer's estate after the insolvency is discovered.

V. PUBLIC POLICY WILL BEST BE SERVED BY AFFIRMANCE OF THE JURY VERDICT IN THIS CASE

The regulation and liquidation of an insurance company is a matter so infused with the public interest that it invokes the police power of the state, <u>Springer v. Colburn, supra.</u> Auditors who, for compensation, freely undertake engagements to participate in such regulation should be answerable for their derelictions. At present, in all other U.S. jurisdictions which have considered the question, they are; but the Third District opinion relieves

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negligent auditors of liability in precisely those circumstances where their vigilance is most needed. There is no necessity or justification for adopting such a rule in Florida.

Of course, the Department recognizes that auditors are not guarantors of the accuracy of everything the insurer files, nor does it attempt to make them so. In actuality, suits against insurance-company auditors are fairly rare. Although the Florida Department of Insurance now has approximately eighty companies in the process of liquidation, each of which has generated multiple claims, it is presently pursuing only five suits against auditors. Thus, the Court need not worry about an explosion of litigation or serious damage to the accounting profession.

Furthermore, in cases where the Department brings such actions, there are many defenses available to the auditors. If the auditors have performed their jobs properly without violating applicable rules and accounting standards, they may not be negligent at all; or, if negligent, they may not always be the proximate cause of the losses sued upon, or they may bear only a portion of the fault in conjunction with others (including company management). The liability of insurance-company auditors is appropriately determined under existing principles of negligence and proximate cause. There is simply no reason to create a new rule of law which automatically shields a negligent auditor from any consequences of his or her torts. No public purpose would be helped, and many important public goals would suffer.

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CONCLUSION

The Florida Department of Insurance, as amicus curiae, respectfully suggests that this Court should modify the certified question and answer it as suggested in section II, above; and that this Court should vacate the Third District opinion and direct that Court to affirm the trial court's judgment entered upon the jury verdict.

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CERTIFICATE OF SERVICE

WE HEREBY CERTIFY that a true and correct copy of this Brief was mailed this 17 day of December, 1993, to all parties on the attached mailing list.

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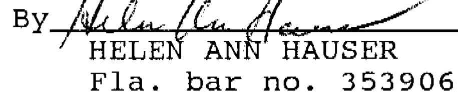
By 
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