IN THE SUPREME COURT OF FLORIDA

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CASE NO. 83,108

JANE DOE, for and on behalf of CHARLENE DOE,

Appellant.

-vs.-

ALLSTATE INSURANCE COMPANY,

Appellee,

ON CERTIFIED QUESTION FROM THE UNITED STATES CIRCUIT COURT OF APPEALS, ELEVENTH CIRCUIT

APPELLANT'S REPLY BRIEF

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TABLE OF CONTENTS

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TABLE OF AUTHORITIES

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ARGUMENT

I.

ALLSTATE EXPRESSLY WAIVED THE ABSENCE OF COVERAGE BY CORRESPONDENCE ACKNOWLEDGING THE EXISTENCE OF COVERAGE WRITTEN AFTER ALLSTATE LEARNED ALL THE FACTS UPON WHICH THE ABSENCE OF COVERAGE WAS BASED

Buried in a footnote on page 5 of the Answer Brief, Allstate makes a weak effort to sweep under the rug a whole and important issue by cavalierly asserting that Jane Doe did not plead the express waiver which occurred when Allstate acknowledged its intent to provide coverage in its letter to the Lucases dated November 9, 1988. By way of reminder, that letter not only made no mention of any lack of coverage for the subject incident, but instead stated facts which reflected that there was coverage.

First, the November 9th letter expressly recognized that there was insurance protection up to the limits of the liability policy, where it stated that the "the amount of damages claimed in the suit may be in excess of the protection afforded under your policy [because t]he suit papers do not indicate the extent of damages that the plaintiff(s) hope(s) to recover." R1-30-Ex. D (emphasis added). Similarly, the letter went on to reinforce the recognition that coverage was to be provided, where it stated: "Under your policy . . ., the limit of liability could be less than the amount which may be recovered under the suit." Id. (emphasis added). Driving the point home that Allstate viewed the loss as covered up to those limits was the next sentence, which stated: "If the

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verdict is in excess of the policy limit, you will be personally liable for such excess." Id. (emphasis added).

Allstate in its Answer Brief tacitly accepts Doe's position on the merits of the express waiver issue that the language of that letter is inconsistent with Allstate's belatedly-asserted position that there was no coverage for the subject incident. Allstate makes no argument that the letter could have any meaning other than as a statement that there was coverage for the subject incident up to the limits of the policy. Therefore, Allstate in essence agrees that it expressly waived its position that there was no coverage, and unconvincingly submits that this Court should ignore the merits of that matter because of a perceived pleading deficiency and the absence of a separately certified question on that issue.

There was no need for the Does to plead express waiver as a separate affirmative defense from implied waiver because waiver is but a single legal theory. "Waiver is commonly defined as the intentional or voluntary relinquishment of a known right." American Somax Ventures v. Touma, 547 So. 2d 1266, 1268 (Fla. 4th DCA 1989). Accord., e.g., Matter of Garfinkle, 672 F.2d 1340, 1347 (11th Cir. 1982). That definition holds true regardless of whether the party asserting waiver establishes the fact of the waiver by introducing direct evidence that another party expressly stated the relinquishment of that known right, or by circumstantial evidence which would establish the waiver by implication.

In other words, the question whether waiver is express or implied is simply one of what method of proof will be employed to

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establish that defense. There is never any need to plead what evidence one expects to introduce in support of a legal defense, so there is no need to characterize waiver as express or implied in the Answer to a Complaint to preserve the issue for appeal.

The defenses pleaded by Doe included the defense that Allstate waived--or should be estopped from asserting--the absence of coverage by virtue of the fact that "Allstate has assumed the defense of the [state court] action with knowledge of all the facts to establish the defense of lack of coverage." R1-18-1, 2. The November 9th letter was part and parcel of Allstate's assumption of the defense, so its effect as an express waiver was properly pled.

Furthermore, the circumstances which establish Allstate's waivers--express and implied--were fully litigated and adjudicated below, without objection from Allstate that the express waiver issue had not been pleaded. Therefore, even if the express waiver issue would properly have been pleaded as a separate legal defense, the issue has been tried by implied consent.

Allstate expressly waived the absence of coverage and the issue is properly before this Court. Allstate does not suggest that the enactment of the Claims Administration Statute nor the decision in AIU Ins. Co. v. Block Marina Investment, Inc., 544 So. 2d 998 (Fla. 1989) have any effect on the doctrine of express waiver. Therefore, the certified questions should be rephrased as suggested and answered in the affirmative.

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II.

ALLSTATE IMPLIEDLY WAIVED ITS RIGHT TO DENY COVERAGE BY PROVIDING THE LUCASES A DEFENSE WITHOUT RESERVATION OF RIGHTS, WITH KNOWLEDGE OF ALL THE FACTS UPON WHICH ALLSTATE'S BELATED DENIAL OF COVERAGE WOULD BE BASED

A. The Claims Administration Statute did not Abrogate the Common Law of Waiver or Estoppel-by-Defense:

There is no merit to Allstate's argument that § 627.426, Fla. Stat. (1982), the Florida Claims Administration Statute, has abrogated Florida's common law of waiver and estoppel by defense, as those doctrines pertain to the present case, for the simple reason that the Claims Administration Statute does not deal with waiver or estoppel of the absence of coverage, only waiver or estoppel to assert defenses to coverage which otherwise exists. Subsection (2) of the statute, upon which Allstate expressly relies on page 6 of its Answer Brief, recognizes its limited applicability to situations other than that present here, where it states: "A liability insurer shall not be permitted to deny coverage based on a particular coverage defense unless . . . ." (emphasis added). It is not Doe's position that Allstate has waived a coverage defense under the policy, rather that it waived the absence of coverage.

Although Allstate does not come right out and say so, its position on this issue seems to be that the Claims Administration Statute provides the exclusive remedy and mechanism for addressing any and all cases involving waivers or estoppel by insurers, and that the failure of the statute to provide a remedy for the waiver of the nonexistence of coverage precludes the courts from

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continuing to recognize such a common law remedy. In other words, Allstate asserts that the statute preempts the field on waiver or estoppel.

Section 627.426 of the Florida Statutes makes no mention of the common law remedy which the Does sought below, much less does the statute express an intent to abrogate the common law doctrine in question. Therefore, the remedy provided under the statute for noncompliance therewith is not exclusive, but is merely cumulative to that available under the common law where an insurer has waived the defense of the absence of coverage. The law on the point is as follows:

> Whether a statutory remedy is exclusive or merely cumulative depends upon the legislative intent as manifested in the language of the statute. The presumption is that no change in the common law is intended unless the statute is explicit and clear in that regard. . . . Unless a statute unequivocally states that it changes the common law, or is so repugnant to the common law that the two cannot coexist, the statute will not be held to have changed the common law.

Thornber v. City of Fort Walton Beach, 568 So. 2d 914, 918 (Fla. 1990)(emphasis added).

There is no reason that the remedy provided by the Claims Administration Statute and the common law doctrine of waiver-by-defense cannot "coexist," because the two legal theories have different purposes and different elements. The two legal theories operate in two very different situations to begin with. As noted by this Court in AIU Ins. Co. v. Block Marina Investment, Inc., 544 So. 2d 998, 999 (Fla. 1989), the statute applies only where there

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would otherwise be coverage, but for "a particular coverage defense[1]." On the other hand, the doctrine of waiver-by-defense operates where there would have been no coverage under the policy in the first place,

There is nothing implicitly inconsistent between the statutory remedy and the common law doctrine because the elements of a claim under the two theories are dissimilar. To prevail against an insurer under the Claims Administration Statute the insured need not establish that the insurer provided him or her with a defense to a non-covered claim. To the contrary, the statute provides a remedy for the insurer's failure to provide a defense or a written denial of a defense. The AIU Insurance case did not involve the type of situation which exists here, where an insurer unqualifiedly defended its insured. To the contrary, during the time that a defense was being provided to the insured in that case, it was being provided by AIU "subject to a reservation of its right to assert a coverage defense." 544 So. 2d at 999. The conduct said to be actionable there was not defending the insured, but in withdrawing the defense without the notice required by the statute.

Thus, the Claims Administration Statute neither expressly nor impliedly abrogates the common law doctrine of waiver-by-defense. The existence of that statute is not relevant to any issue in this appeal, and this Court should reject Appellee's effort to interject the limitations of that statute into this case.

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[1]See § 627.426(2).

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III.

ALLSTATE IS ESTOPPED TO CONTEST THE ABSENCE OF COVERAGE BY VOLUNTARILY DEFENDING ITS INSUREDS THE LUCASES WITHOUT ANY RESERVATION OF RIGHTS

A. This Court Should Follow the Universal Rule Concerning an Unreserved Assumption of the Defense:

The estoppel-by-defense doctrine was recognized by the Fourth District Court of Appeal in Cigarette Racing Team v. Parliament Ins. Co., 395 So. 2d 1238 (Fla. 4th DCA 1981). In the Cigarette Racing case, "Parliament Insurance Company assumed the defense of its insured, Cigarette, without a reservation of rights or a notice to Cigarette of possible non-coverage." 395 So. 2d at 1240. The Fourth District noted the general rule "that waiver and estoppel will not operate to create coverage in an insurance policy where none originally existed," but then recognized the applicability of the doctrine of estoppel-by-defense as follows:

> There is an exception to the rule, however, which provides that "when an insurance company assumes the defense of an action, with knowledge, actual or presumed, of facts which would have permitted it to deny coverage, it may be estopped from subsequently raising the defense of non-coverage."

395 So. 2d at 1239, 1240 (quoting City of Carter Lake v. Aetna Cas. & Sur. Co., 604 F.2d 1052, 1059 (8th Cir. 1979)).

Allstate urges this Court to disapprove of the Fourth District decision in Cigarette Racing, seemingly suggesting that it is an aberration in the law. It is not. The exception to the general

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rule that coverage cannot be created by waiver or estoppel is so widely accepted that a Texas court in a 1990 case noted as follows: "We have found no case, nor has either party cited a case, in which the general rule was applied where there was an [unreserved] assumption of the insured's defense by the insurer." State Farm Lloyds, Inc. v. Williams, 791 S.W. 542, 551 Tex. App. 1990). The many other authorities on the point cited in the treatises quoted in Doe's Initial Brief make it clear that Florida would be a lonely minority of one if this Court holds as Allstate urges. This Court should instead follow the universal rule on the point and answer the certified questions as rephrased by Doe in the affirmative.

B. The Record Amply Establishes the Existence of Prejudice:

Doe has established such prejudice as will support the doctrine of estoppel by defense in this case. First, prejudice should be presumed from the fact that Allstate controlled the Lucases' defense during the extreme delay of four years from the time that Allstate learned all the facts supporting its eventual denial of coverage. This case must present a more compelling factual basis than even those which have led to the holdings to the effect that: "prejudice in such a case will be conclusively presumed or that prejudice is an inevitable effect of the insured's loss of the right to maintain control of the defense." See Couch on Insurance 2d § 51:166.

There is no Florida Supreme Court case which expressly addresses the question whether prejudice will be presumed and the

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burden will shift to the insurer to rebut that presumption, but this Court should join the majority of jurisdictions on this point and recognize that presumption. There has been no development in the law over the nearly forty years since the majority rule was announced that "a greater number of courts have ruled either that prejudice is an inevitable effect of the insured's loss of the right to maintain complete control of the defense, or (what amounts to the same thing) that in a situation in which it appears that an insurer has assumed the defense of an action against an insured, prejudice to the insured will be presumed." Annot., 38 A.L.R.2d 1148, supra, at 1151 (emphasis added). Allstate having failed in its burden of rebutting that presumption of prejudice, it was Doe, and not Allstate, who was entitled to summary judgment.

Even if this Court should determine that Florida would follow the minority rule and refuse to recognize the presumption of legal harm from the extraordinary delay and other facts, the record does reflect actual prejudice which resulted from a conflict of interest between the Lucases and Allstate during the time Allstate defended the claim against its insureds. It should go without saying that the most fundamental source of a potential conflict between an insurer and its insured is on the question whether the loss will be within the coverage of the policy. It is in the interest of the insured for the facts and the law to coexist in such a state as his conduct was covered; yet it is in the interest of the insurer for the facts and the law to result in the absence of coverage.

The general principle applicable to conflict-of-interest

prejudice is stated as follows:

> At least one of the reasons for the rule [of estoppel-by-defense] appears to be the existence of conflicts of interest, either actual or potential between the insured and the insurer in connection with the conduct of the defense of the insured. . . . For example, a conflict of interest might arise when the insurer represents the insured in a lawsuit and simultaneously formulates its defense of noncoverage against the insured.

State Farm Lloyds, Inc. v. Williams, 791 S.W. 542, 551 (Tex. App. 1990). The case at bar involves much more than that abstract risk of a conflict of interest; it involves a demonstrable harm to the Lucases' defense to the state court action from the direct activities of Allstate Insurance Company while providing the Lucases with their defense.

At the time of William Lucas' molestation of Charlene Doe, and at the time the state court action for damages was filed by Jane Doe against the Lucases, the question of whether a child molester's acts of deviate behavior were covered under a homeowner's policy which excluded intentional injuries (and injuries which were expected by the insured) was controlled in the Second District (where the state court tort action by Doe against the Lucases was pending) by Zordan v. Page, 500 So. 2d 608 (Fla. 2d DCA 1986). The Second District plainly held that there would be coverage under such policies, even for the intentional acts of deviate sexual relations with a child, so long as the insured possessed no subjective intent or expectation that injuries would result. Regardless of our view now, more than six years after Zordan, as to

the wisdom of that rule of law, it was the law in Tampa where the tort case was pending. Under Zordan, so long as the jury believed William Lucas' testimony that, at the time he perpetrated the acts of molestation upon the minor child, William Lucas did not think that those acts would be harmful to her, he would have been covered under the Allstate policy in question.

While Allstate took its time in conducting its defense of William Lucas in that personal injury case--and while he was ignorant of Allstate's conflict of interest and intent to deny coverage-- Allstate was consciously working against his interest in this Court to change the law in the Second District so as to eliminate any chance that Mr. Lucas' acts would be covered by the policy. In July of 1989, more than two and one-half years after the facts of this case were made known to Allstate, and several months after the state court lawsuit had been filed and could have been settled, Allstate succeeded in its plan to reshape Florida law when the Supreme Court decided Landis v. Allstate Ins. Co., 546 So. 2d 1051 (Fla. 1989).

In Landis, this Court accepted Allstate's argument that specific intent to cause harm was not necessary upon which to base an exclusion of coverage; the intentional acts of the child molester in and of themselves would bar coverage. The fact of the prejudice to William Lucas is self-evident: If Allstate had denied coverage or reserved its rights to do so on the basis of such an argument in the present case, the Lucases would have been able to take action to resolve the Doe claim, or at least had control of

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their own defense, prior to the law on coverage changing against them.

There were other forms of prejudice from the delay in Allstate denying coverage to the Lucases. For example, as argued in Doe's Motion for Summary Judgment, "during the pendency of this litigation, the Lucas children have forgotten the names of witnesses who may prove beneficial to the Lucases' case." On the damages issue, in light of its intent to deny coverage, it would not concern Allstate one iota whether a verdict were large or small, so Allstate necessarily had less interest in pursuing discovery and investigation on the matter of damages sustained by Charlene Doe, to the prejudice of its insured.

In fairness to counsel retained by Allstate to defend the Lucases, Appellant does not suggest any professional negligence, ethical misconduct, or other violation of his role as counsel for the Lucases. However, it is common knowledge that insurers control the purse-strings when it comes to financing discovery, retaining experts, and other expensive matters in defense of serious cases.

While counsel no doubt was doing all he could with the resources that Allstate allotted, the insurer's differing interest from that of the Lucases undoubtedly resulted in some prejudicial differences in the manner the litigation was conducted, however slight were those differences. "Once established, the amount of prejudice, whether large or small, becomes irrelevant when determining the applicability of the doctrine of estoppel." Florida Physicians Ins. Co. v. Stern, 563 So. 2d 156, 160 (Fla. 4th

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DCA 1990). There being actual prejudice shown from Allstate's conflict of interest and delay in denying coverage, the doctrine of estoppel-by-defense is applicable and the certified questions should be answered in the affirmative so that the judgment in Allstate's favor can be reversed.

IV.

DOE HAS STANDING TO ASSERT ALLSTATE'S WAIVER AND ESTOPPEL

Allstate questions Doe's standing to offer the arguments that Allstate has waived or is estopped from asserting the nonexistence of coverage. Doe submits that she has standing, as established by the authority of Johnson v. Dawson, 257 So. 2d 282, 284 (Fla. 3d DCA), cert. denied, 266 So. 2d 673 (Fla. 1972). However, even if this Court were to disapprove of the Johnson court's analysis of a tort claimant's standing, Allstate did not preserve the standing argument because it failed to cross-appeal the district court's order adopting the magistrate judge's finding on that issue.

That finding by the magistrate judge, made in footnote 3 on page 10 of her Report and Recommendation, is that "[i]t appears that defendant Doe has standing under Florida law to raise these issues." (citing Johnson v. Dawson, 257 So. 2d 282, 284 (Fla. 3d DCA), cert. denied, 266 So. 2d 673 (Fla. 1972)). The Does' standing has therefore been established in this case and is not subject to challenge by way of naked argument in Allstate's Brief.

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CONCLUSION

WHEREFORE, for the reasons and upon the authorities set forth above, the certified questions should be answered in the affirmative so the judgment under review can be reversed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that true copies hereof were served by mail, upon James W. Guarnieri, Esq., 608 East Morgan Street, Brandon, FL 33510, co-counsel for Appellant, and to Lori J. Caldwell, Esq. and David B. Shelton, Esq., RUMBERGER, KIRK & CALDWELL, 201 South Orange Avenue, P.O. Box 1873, 11 East Pine Street, Orlando, FL 32802, on this, the 6th day of June, 1994.

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