

1991

Home Savings and Loan, a Utah Corporation v. The Aetna Casualty and Surety Company : Brief in Opposition to Certiorari

Utah Supreme Court

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IN THE SUPREME COURT, STATE OF UTAH

HOME SAVINGS AND LOAN, a)	Appeal from Utah Court
Utah corporation,)	of Appeals' Decision
)	Dated August 6, 1991
Plaintiff/Appellee,)	(Case No. 890101-CA)
)	
vs.)	
)	
THE AETNA CASUALTY AND)	Case No. 910436
SURETY COMPANY,)	
)	
Defendant/Appellant.)	
)	
)	

**APPELLEE'S BRIEF OPPOSING AETNA'S
PETITION FOR WRIT OF CERTIORARI**

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PARTIES

On Appellee's motion, the Court of Appeals on December 4, 1990 ordered that the Resolution Trust Corporation, as conservator of newly chartered Home Savings Bank, F.S.B., be substituted as Appellee in place of Home Savings & Loan. Utah R. App. P. 38(b). For reasons of consistency, Appellee will be referred to in this Brief as "Home"; as does Aetna in its Petition and as the Court of Appeals did in its Decision.

QUESTIONS PRESENTED FOR REVIEW

The two issues as to which Aetna seeks certiorari may be framed as follows:

1. Does the definition of "discovery," as set forth in a "notice" rider to a now outdated bond form, warrant re-examination by the Supreme Court of the issue of "coverage"; where the Court of Appeals' holding is based on language in the "preamble" of the Aetna Bond, which no longer appears in the standard bond now used by the surety industry for financial institutions?

2. Under the facts of this case, does Aetna establish sufficient basis for the Supreme Court to exercise its supervisory power to re-examine the Court of Appeals' and Trial Court's construction of Section 11 of Aetna's bond?

OPINION OF THE COURT OF APPEALS

The Utah Court of Appeals, on August 6, 1991, affirmed the Judgment entered November 2, 1988 in Home's favor.

JURISDICTION

The Supreme Court has jurisdiction to consider Aetna's petition. Utah Code Ann. § 78-2-2(5) (1953) (as amended 1989, Supp. 1991). Home's Brief opposing Aetna's petition is timely filed, within an extension of time granted by the Supreme Court.

CONTROLLING PROVISIONS

As Aetna concedes, "No provisions of the Utah Constitution, Utah Code Annotated, or other regulations are determinative of the issues in this case."

STATEMENT OF THE CASE

I. Nature of the Case.

Home seeks indemnification for losses caused by the dishonest conduct of one of its employees, Larry Glad, which it sustained and discovered during the period a Savings & Loan Blanket Bond issued by Aetna was in effect. Home's losses arose when the United States District Court, D. Utah, in Armitage v. Home Savings & Loan, Civil No. C82-0670K (Kane, J.) voided the notes and trust deeds of 36 husband and wife borrowers who had borrowed from Home to invest in AFCO, a Utah corporate enterprise headed by Grant Affleck. The Armitage jury returned a verdict adverse to Home on August 14, 1984. Following the jury's verdict, Home wrote off the loans in the latter part of 1984. (Trial Exh. 220). Subsequently, the Armitage Court, on February 24, 1986, entered judgment formally voiding the borrowers' notes and trust deeds. The principal on the 36 notes voided by the Armitage Court totaled approximately \$1.2 million, which resulted in a net loss to Home of approximately \$998,000.

II. Procedural History and Trial Court Disposition.

This action was tried to a jury over a five-week period in October - November 1987. The Trial Court (Hon. Michael R. Murphy) entered judgment in Home's favor on November 2, 1988.

Prior to trial, Aetna moved for summary judgment, contending that judgment should be entered in Aetna's favor because Home, allegedly, had "discovered its loss" before the Aetna Bond went into effect on June 21, 1982 (though the Armitage verdict was not returned until more than two years later, and judgment formally entered eighteen months after that). Simultaneously, Home sought a determination that, consistent with the bond's insuring agreements, Home both "sustained" and thus "discovered" its loss on the AFCO-investor loans during the time the Aetna Bond was in effect. The Trial Court denied Aetna's motion for summary judgment and issued a separate Order construing the Bond, in which it ruled:

that plaintiff sustained a "loss," as the term "loss" is contemplated in the Aetna Bond, on August 14, 1984. Accordingly, plaintiff discovered its "loss sustained" during the period the Aetna bond was in effect.

Sept. 21, 1987 Order (R. 385) (copy attached at Appendix, Tab 1); see Ct. App. Decis., p. 6.

At trial, Aetna asserted: that Home had not proven that Glad was dishonest; that Home's losses were caused by Home's mismanagement, not by Glad; that Home had failed to timely notify Aetna of a covered loss or potential loss; that Section 11 excluded coverage; and that its Bond was void ab initio because of failure to disclose information material to the risk being insured. Because Aetna failed to prove any prejudice, the Trial

Court disposed of Aetna's "timely notice" defense in instructing the jury. Aetna, as the Court of Appeals noted, did not appeal the Trial Court's ruling on "notice." Ct. App. Decis., p. 17. The jury found that Glad's conduct was dishonest; and that Glad's conduct caused Home's losses in connection with 34 of the 36 loans that the jury reviewed. The jury also found that Home did not learn of Glad's dishonest conduct in connection with the AFCO-investor loans until after the effective of the Aetna Bond.

Following trial, Aetna filed a JNOV motion in which it contended, in contrast to the position it now takes in its Petition, that the evidence at trial did not establish that Glad was dishonest; or that Glad's misconduct caused Home's losses. The Court denied Aetna's motion. Judge Murphy also rejected Aetna's "Section 11" defense, in considering the jury's responses to special interrogatories. Additional hearings ensued, which involved matters extraneous to Aetna's present Petition. Judgment was entered November 2, 1988.

Aetna appealed, asserting nine grounds alleged to constitute error. The parties filed extensive briefs and the issues were argued in November, 1990. On August 21, 1991, the Court of Appeals affirmed the judgment. Judge Greenwood wrote for the majority, joined by Judge Billings. Judge Bench dissented.

III. Statement of Facts.

Home highlights the following distinctions to the "Statement of Facts" in Aetna's Petition.¹

¹ A more detailed exposition of pertinent facts may be found in Home's Statement of Facts in its Brief to the Court of Appeals, at pp. 10-26. See Tab 2, hereto.

1. Aetna issued a then standard Form 22 Savings & Loan Blanket Bond to Home, effective June 21, 1982. Prior coverage was through F&D of Maryland. Ct. App. Decis., p.4.

2. Aetna solicited Home's business, not vice versa. Ct. App. Decis., p. 4 & 30 n. 23.

3. Initially, Home applied for the same amount of coverage it had with F&D. Federal examiners, during the course of a routine examination, directed Home to increase its coverage from \$900,000 to \$1,135,000, consistent with regulatory formulas. Appellee's Brief to Ct. Appeals, p. 11.

4. Alcorn v. Affleck was filed in U.S. Bankruptcy Court in April 1982 by several hundred disgruntled AFCO investors against 68 named defendants, including Home and 16 other financial institutions. Aetna's Statement omits that:

a. The Alcorn complaint (Trial Exh. 358) asserted causes of action common to all 17 financial institutions and was not directed exclusively to Home or its employees.

b. The Complaint did not allege that any of Home's employees had engaged in any specific dishonest conduct; though it did assert a fraud claim (as well as 22 other causes of action) common to the 68 defendants.

c. Notwithstanding the Alcorn complaint, Home believed that its trust deeds were enforceable because it had prepared a document for each borrower to sign, acknowledging his/her sole responsibility to repay his/her note. See Ct. App. Decis., p. 3.

d. Aetna did not ask Home to disclose pending lawsuits in the application it instructed Home to complete.

Ct. App. Decis., p. 28 & 30, n. 25.

e. After Home in December, 1982 notified Aetna of a potential loss possibly covered by the bond, Aetna retained Suitter & Axland to monitor the Armitage litigation, to review pleadings, sit in on depositions, etc. (Pre-Trial Order, R. 726). On September 30, 1983, having had the benefit of monitoring the Armitage lawsuit and having reviewed the very same pre-June 21, 1982 pleadings that it now emphasizes in its Petition, Aetna advised Home in writing that the pleadings did not set forth any claims that would be covered under its Bond and opted not to defend Home. See Ct. App. Decis., p. 22 n. 15; Trial Exh. 140.

5. As Aetna states, Home, prior to June 21, 1982, had learned of a dishonest act by employee Larry Glad. Aetna fails to mention, however, that the jury found that the dishonest act about which Home had learned was "not related to the AFCO investor loans," Jury Ans. to Special Interrog. No. 7; and that Home immediately terminated Glad after it learned of that particular dishonest act. See Ct. App. Decis., p. 2-3.

6. The jury concluded that any failure by Home to disclose material information in connection with the application for insurance it completed was not intentional. Jury Ans. to Special Interrogatories Nos. 1-4; Ct. App. Decis., p. 6, 27.²

7. Contrary to the innuendo in Aetna's petition, Home has always maintained that it discovered Larry Glad's dishonest

² Aetna does not seek review of the Court of Appeals' rejection of its misrepresentation defense. See Ct. App. Decis., p. 26-30.

conduct, vis-a-vis the AFCO-investor loans, in the Fall of 1982, in the course of discovery in Armitage and, thus, after Aetna's bond went into effect in June, 1982. See Appellee's Brief to Ct. Appeals, p. 26. The jury agreed, finding that Home did not learn of dishonest conduct by Glad in connection with the AFCO-investor loans prior to June 21, 1982. Jury Ans. to Spec. Interrog. No. 7; Ct. App. Decis., p. 6, 17.

IV. Governing Contract Provisions.

The Bond at issue is now an outdated Standard Form No. 22 "Savings & Loan Blanket Bond" (1970 revised version), as amended by the thirteen "riders" designated in the Bond's cover sheet and appended to the Bond. (Trial Exh. 343). Coverage for fidelity losses is governed by the introductory paragraph of the insuring agreements, which the Court of Appeals labeled "the Preamble," Ct. App. Decis., p. 15, and by Rider 6041. Section 11, paragraph 3, of the Bond terminates coverage as to a particular employee once an employer learns of dishonest conduct by the employee. Section 4 of the Bond defines the Insured's duty to provide notice. Rider 6091 specifically amends Section 4, and clarifies that the Insured is expected to give notice, not only once a covered loss has been sustained, but also "when the Insured becomes aware of facts which would cause a reasonable person to assume that a loss covered by the bond . . . will be incurred even though the exact amount . . . of loss may not be then known." The Court of Appeals held that Rider 6091 governs only the Insured's duty to provide timely notice and concluded that it does not bear on whether a loss that results from dishonest conduct is or is not covered by the Bond. Ct. App. Decis., p.15-

26. According to the Court of Appeals, Rider 6091 does not govern the outcome of any issues on appeal.

Furthermore, the form of bond which Aetna asks the Supreme Court to again interpret is one that is no longer used by sureties or financial institutions, having been displaced in 1986 by the significantly revised Form 24 "Financial Institution Bond."³ In particular, the introductory insuring agreement language (the "Preamble") found in the 1970 Form 22 S&L Aetna Bond, on which the Court of Appeals and Trial Court based their holding, does not appear in the new Financial Institution Bond.

ARGUMENT

I. Aetna fails to establish any "special or important" reason why the Supreme Court should re-examine the Court of Appeals' holding regarding coverage.

The first question presented by Aetna's Petition concerns the scope of coverage provided by Aetna's promise to indemnify Home for "loss sustained by the Insured at any time but

³ In 1986, the surety industry approved for use the Form 24 Financial Institution Bond (Revised January, 1986). The Financial Institution Bond displaces former versions of the Form 24 Bankers Blanket Bond and the Form 22 S&L Blanket Bond. Harvey C. Koch, "Overview of Major Developments and Changes During the Last Decade in Financial Institution Bonds," Financial Institution Bonds (ABA, Tort & Insurance Practice Section; Eds. Koch & Rouse; 1989) (Symposium, Washington, D.C., April 17-18, 1989) (attached at Tab 3). A specimen of the standard Form 24 Financial Institution Bond (revised to January, 1986) is attached hereto at Tab 4. The Financial Institution Bond replaces the Form 22 S & L Blanket Bond (as revised Dec. 1982), a specimen of which is attached at Tab 5, which differs significantly from the 1970 version it replaced. Also attached for comparison purposes, at Tab 6, is a specimen of the Form 24 Bankers Blanket Bond (revised to July, 1980). At Tab 7 is a specimen of the Form 24 Bankers Blanket Bond (revised to April, 1969) (which is similar to the Form 22 S&L Bond at issue). Home asks that the Court take judicial notice of the different, standard versions attached hereto.

discovered during the Bond Period." Aetna Bond, "Preamble" to Insuring Agreements.⁴ Section 4 of the Aetna Bond provides that written notice must be provided to Aetna "at the earliest practicable moment after discovery of any loss hereunder . . ."

Rider 6091 specifically amends Section 4, and provides that:

Discovery occurs when the Insured becomes aware of facts which would cause a reasonable person to assume that a loss covered by the bond has been or will be incurred even though the exact amount or details of loss may not be then known. Notice to the insured of an actual or potential claim by a third party which alleges that the Insured is liable under circumstances, which, if true, would create a loss under this bond constitutes such discovery.

The Court of Appeals concluded that this definition of discovery in Rider 6091 applied only to the term "discovery" as used in the Notice Provision and not to the term "discovery" as used in the Preamble to the Insuring Agreements. The Court of Appeals relied on several factors in this regard: (i) the phrase "discovered during the Bond Period," as it appears in the Preamble, expressly refers to "loss sustained," not dishonest employee conduct; (ii) the above definition of discovery was added by an endorsement, the stated purpose of which was to "amend" only the Notice Provision (namely, Section 4 of the Bond); (iii) the Bond includes a "Definitions" section that includes numerous definitions that "apply throughout the bond" and Aetna did not include the definition of "discovery" in the general Definitions section; and (iv) different definitions of "discovery" for notice

⁴ In the entire breadth of its Petition, Aetna only once mentions "the preamble" to its Bond (which governs coverage generally) and never mentions Rider 6041 (the fidelity insuring agreement). It is these express provisions on which the Court of Appeals and the Trial Court based their holdings. See Ct. App. Decis., p. 15-16.

purposes and coverage purposes "does not cause disharmony of the bond language [given] the different purposes those provisions are intended to serve." See Ct. App. Decis., p. 24-26.

This Court should decline to review the coverage issue for several reasons. First, the coverage question is extremely unlikely to recur in subsequent litigation, and is thus not a "special and important" question worthy of discretionary review. Second, the dire consequences predicted by Aetna are not likely to occur. Third, the Court of Appeals correctly construed the coverage provisions of the Bond. Finally, the Alcorn complaint did not warrant entry of summary judgment in Aetna's favor.

A. This issue is extremely unlikely to be presented in subsequent litigation.

The standard bond form at issue here was revised in 1982 to move the contents of Rider 6091 into the body of the bond form. That 1982 revision made three changes to the discovery definition that are relevant to this Court's determination as to whether this case warrants discretionary review. First, the Surety Association of America, which issues the standard bond form, removed the definition of discovery from the Notice Provision and placed it in an entirely separate and independent section of the bond. See Standard Form No. 22, Revised to December 1982, Section 4 (attached hereto as Tab 5). Second, the Surety Association added the following as the first sentence in the new discovery provision: "This bond applies to loss discovered by the Insured during the bond period." Third, the Surety Association deleted the language in the Preamble to the Insuring Clauses that had granted coverage for "loss sustained by the

Insured at any time but discovered during the Bond Period."

Thus, the 1982 and subsequent changes wholly undermine Aetna's suggestion that this case qualifies for discretionary review. As previously stated, the question presented by the language at issue here is extremely unlikely to recur since that language was revised by the Surety Association, ostensibly to resolve this ambiguity, almost ten years ago. Second, the Court of Appeals indicated that it likely would agree with Aetna's coverage position under the new bond language, even though it rejected Aetna's coverage position under the prior ambiguous language. See Ct. App. Decis. p. 23 ("This [new] language clearly ties coverage to discovery of possible loss, because the definition of discovery is given in the context of the bonds' applicability, rather than in the context of notice requirements").⁵

B. The dire consequences that Aetna predicts as a consequence of the the Court of Appeals' Decision are illusory.

Aetna vigorously complains that the decision of the Court of Appeals will "uniquely prejudice Utah financial institutions and their depositors," and will create "uncertainty and confusion" for financial institutions in Utah. This complaint is totally groundless. As a result of the 1982 and 1986 revisions to the standard bond form, the decision of the Court of Appeals -- even if it is incorrect -- will have no practical precedential impact

⁵ In discerning that two of the cases on which Aetna relied in its Reply Brief contained operative provisions not in and different from those in the Aetna Bond, the Court of Appeals stated that, "Royal Trust and Clay are instructive as to how Aetna might have drafted its bond to obtain the result it now seeks."

on current bond coverage issues in this state.

In addition to its "uncertainty and confusion" argument, Aetna predicts that the Court of Appeals' holding will "encourage financial institutions to postpone reporting losses in the hopes of buying higher limits for known problems." This argument is pure speculation, is contrary to the record, and of dubious validity given the revisions in the standard bonds that have transpired since the Aetna Bond was formulated in 1970. As a practical matter, possibility always exists with a "discovery" bond that an insured may be tempted to manipulate the claim. Affirmative defenses to such errant conduct include fraud or misrepresentation, or that the insured has not timely notified its insurer of actual or potential loss. Neither issue is before the Court. The Court of Appeals' Decision in no way increases incentive to hide knowledge of past employee misconduct, in order to obtain higher coverage. What it may do is encourage insurers to ask about former employees in applications for fidelity bond coverage, see U.S. Fidelity & Guaranty Co. v. Empire State Bank, 448 F.2d 360, 366 (8th Cir. 1971) (which implicitly made this same, unheeded, recommendation 20 years ago); or ask insureds to disclose all pending lawsuits in applications for bond coverage (as Aetna now does), see Ct. App. Decis., p. 30 n. 24.

Aetna belatedly argues that the Court of Appeals' Decision will leave Utah financial institutions without coverage, because fidelity insurers will refuse to renew coverage once they receive notice of potential loss. Aetna Petition, p. 14. As the Court of Appeals noted at page 25 n. 17 of its Decision, Aetna never raised this argument below and both the Court's Sept. 21, 1987

Order and the facts stipulated to in the Pre-trial Order establish that Home's loss was sustained following the jury's verdict in 1984, within the bond period, when it then became evident that Home would not be able to rely on the notes and trust deeds that it had presumed to be enforceable. This particular argument, because it was never raised in the approximately 5 year history of this case, has not been briefed and should not be considered for the first time on appeal. If, however, the express language in a bond is capable of being interpreted in a manner inconsistent with the actual language (Aetna's position); then the Insured is entitled to have the ambiguity construed in favor of coverage. See Continental Ins. Co. v. Morgan, Olmstead, Kennedy & Gardner, 148 Cal. Rptr. 57, 66 (Cal. App. 1978). Furthermore, the Court of Appeals' construction was predicated on express language which appears in the 1970 edition Form 22 Aetna S&L Blanket Bond, which is not replicated in the new 1986 Financial Institution Bond or in the immediately prior 1982 version of the Form 22 S&L Blanket Bond. Hence, it is extremely unlikely that this case will produce the adverse result that Aetna foretells. Finally, for an insurer to require notice of potential loss, then suggest it would use that notice as a basis to arbitrarily refuse renewal of a bond, raises serious question concerning the insurer's implied covenant to deal in good faith.

C. The Court of Appeals' holding on coverage is properly based on the bond's insuring agreements.

The Court of Appeals properly began its analysis by examining the express language of the bond. As noted above, the

preamble to the insuring agreements in Aetna's bond states that Aetna will "indemnify" "loss sustained by the Insured at any time but discovered during the Bond period . . ." Historically, because a fidelity bond is an "indemnity insurance contract," courts have held that "the insurer's liability does not arise until the insured has suffered a proven loss." American Empire Ins. Co. of So. Dakota v. Fidelity & Deposit Co. of Md., 408 F.2d 72, 77 (5th Cir. 1969); 13 Couch on Insurance § 46:219 at 163 (1982). To successfully claim under a fidelity bond, an insured must first prove it has sustained an actual loss; i.e., one involving some sort of financial detriment. Continental Cas. Co. v. First National Bank of Temple, 116 F.2d 885, 887 (5th Cir.), cert. denied 85 L.Ed. 1533 (1941).

The Preamble, as the Court of Appeals held, requires Aetna to indemnify loss sustained at any time, but discovered during the bond period. Ct. App. Decis., p. 23-26. As the Trial Court noted, in the usual fidelity loss context, the insured first sustains a loss (e.g., through embezzlement), then later ascertains that the loss was caused by employee dishonesty. In that situation, fidelity insurers freely agree to indemnify actual loss incurred even during an earlier bond period, provided the insured doesn't learn that the earlier loss was the product of employee dishonesty until such time as the second bond is in place.

This case addresses the more infrequent situation where the insurer alleges that the insured discovered dishonest conduct during a prior bond period, but the loss is not actually sustained or discovered until later. Based on the express

language of the Preamble in the Aetna Bond, the Court of Appeals and Trial Court both rejected Aetna's assertion that Home's loss (which had not yet been incurred) was somehow "discovered" during and covered by an earlier bond.

As Aetna explained its position to the Court of Appeals, "Loss refers to the awareness of conditions out of which a claim may arise, not to the insured's adjudicated liability for that loss." It is this metaphysical definition of "loss" and accompanying definition of "discovery of loss," that the Court of Appeals rejected. The Court of Appeals exercised great care to distinguish the cases collected by Aetna, virtually all of which focused on the issue of whether an insured had timely given notice to the insurer of a pre-existing loss or future loss, believed to be covered by the bond. Ct. App. Decis., p. 17-24.⁶

The expectation that an insured should give notice as early as possible, even before loss is actually sustained, has long been recognized.⁷ Prior to 1980, the duty to give notice, however, was not clearly specified in the Form 22 Bond. In the case of the standard Form 22 S&L Blanket Bond, for example, the

⁶ Aetna especially criticizes the Court's distinction of Royal Trust Bank v. National Union Fire Ins. Co. of Pittsburgh, 788 F.2d 719 (11th Cir. 1986). Petition, p. 13 n. 6. As the Court of Appeals correctly noted, the operative language of the bond interpreted in Royal Trust (which appears to have been a Form 24 Banker's Blanket Bond, 1980 revised ed.), differs markedly from that in the Form 22 S&L Bond (1970 revised ed.) with attached riders, which it construed. Ct. App. Dec., p. 23 & n. 16; compare Aetna Bond to bond construed in Royal Trust, supra at 720.

⁷ Wildau, K. "Evolving Law of Third-Party Claims Under Fidelity Bonds: When is Third-Party Recovery Allowed?" Tort & Insurance Law J. (Fall 1989), at 92, 113.

duty of an insured to give notice, prior to 1980⁸ was defined solely by Section 4, which directed that:

At the earliest practicable moment after discovery of any loss hereunder the Insured shall give the Underwriter notice thereof . . .

Courts disagreed whether Section 4's "discovery of loss" language required notice prior to the time the insured sustained an actual loss covered by the Bond. Compare, Mount Vernon Bank & Trust Co. v. Aetna Cas. & Sur. Co., 224 F.Supp. 666 (E.D. Va. 1963) (requiring notice prior to realization of loss) and First Security Bank of Utah v. Aetna Cas. & Sur. Co., Civil No. NC-74-23W (Memorandum Decis. and Order, July 11, 1984) (Winder, J.) (holding that insured's duty to give notice in a third-party claim context arises only once the third-party claim causes loss to the insured).⁹ Rider 6091, which expressly amended Section 4, was intended simply to clarify that insurers also wished notice when "The Insured becomes aware of facts which would cause a reasonable person to assume that a loss covered by the bond has been or will be incurred . . ." (Emphasis added).

Finally, Utah law is well settled that if coverage provisions in a policy of insurance are ambiguous (as they would seem to be when an insurer insists that an insuring agreement means something other than what it says), then the insured is entitled to have the ambiguity construed in favor of coverage.

⁸ Rider 6091, for attachment to Standard Forms nos. 5, 14, 20, and 22, was adopted effective December, 1980. See Aetna Bond, Rider 6091.

⁹ A copy of Judge Winder's Decision is attached hereto at Tab 8. Contrary to the implicit threat in Aetna's current Petition, Aetna did not refuse to insure financial institutions in Utah following Judge Winder's Opinion.

LDS Hospital v. Capitol Life Ins. Co., 765 P.2d 857, 858-59 (Utah 1988); see also Continental Ins. Co. v. Morgan, Olmstead, supra at 66.

D. The Alcorn complaint did not warrant entry of summary judgment in Aetna's favor.

In its summary judgment motion, Aetna relied on various alleged events, which it argued would prompt any reasonable person, prior to June 21, 1982, to conclude that a loss covered by its Bond would be sustained. Secondly, it relied on notice ostensibly provided by the Alcorn complaint and one or two other similar actions. The jury's finding that Glad's dishonest conduct which Home discovered prior to June 1982 was not related to the AFCO-investor loans, should preclude Aetna from rearguing those facts yet again to this Court. Still, relying on Rider 6091, and interpreting Rider 6091 to define coverage, Aetna rails that the Alcorn lawsuit (apparently apart from the jury's finding) as a matter of law establishes coverage as falling within the time period of the prior F&D Bond. As Aetna characterizes the issue:

The Majority Opinion rejected Aetna's reliance on a bright line test in a Rider to the bond, which defines "discovery" in third-party claim situations as occurring no later than the date on which Home is sued by a third-party alleging any employee dishonesty. (Aetna Petition, p. 3).

Assuming arguendo that Rider 6091 redefines the Bond's insuring provisions, Aetna conveniently forgets that on September 30, 1983, after studying the Alcorn and other complaints, it advised Home that the pleadings did not assert any causes of action that, if established, would be covered under the Bond. The Court of

Appeals noted the inconsistency of Aetna's position, concluding that, "In effect, Aetna asserted that Home had not discovered any employee dishonesty at a time when the Aetna bond had been in force for over one year." Ct. App. Decis., p. 22 n. 15. Having itself concluded that the Alcorn complaint failed to state allegations which, if true, would establish a loss under the bond, Aetna cannot very well ask this Court to exercise its supervisory/correction powers to now avoid the jury verdict and judgment entered by the Trial Court and, instead, direct that summary judgment be entered in Aetna's favor.

II. Aetna does not establish sufficient reason for the Supreme Court to re-examine the Court of Appeals' construction of Section 11.

Section 11 of the Aetna Bond provides that when an insured discovers that one of its employees has engaged in dishonest conduct, the bond "shall be deemed terminated or canceled as to [that] Employee." Its purpose is to shift the risk of loss arising from future misconduct to the insured, once the insured learns of dishonesty but nevertheless elects to retain the employee. Ct. App. Decis., p. 9. In the context of the facts of this case, the Court of Appeals, Decis., p. 14, held:

that coverage for losses caused by Glad's dishonest conduct, where that conduct occurred before Home learned that he was dishonest, and where the coverage for such losses would have continued under renewal of the F&D bond, is not barred by section eleven of the Aetna bond.

In asking this Court to exercise its supervisory function, Aetna asserts that the Court of Appeals ignored "universal" and "clear precedent" contrary to its decision. That "clear

precedent" consists of a single case,¹⁰ decided over a dissenting opinion. In a detailed analysis, the Court of Appeals declined to embrace the majority's holding in Wilson. The Court distinguished most of the other cases Aetna again cites in its Petition,¹¹ noting that each involved the situation where an employer hires an employee, knowing of past dishonest conduct; and concluding that it is proper in such instance to deny coverage for loss arising out of similar subsequent conduct. The jury's finding that Home did not know of any dishonest conduct by Glad prior to hiring him, however, renders these cases inapposite. Jury Ans. to Spec. Interrog. No. 6.

Aetna argues in its Petition that Section 11 "properly leaves" coverage with the insurer in whose bond period the dishonesty was first discovered and that Home would have perfected whatever coverage it had with F&D through timely notice. First, this argument and explanation differs from the interpretation Aetna initially requested below (which was that on discovery of dishonest conduct all coverage for future losses is terminated (even if F&D was still the insurer)). See Aetna's Brief to Ct. Appeals, p. 31, 33. Second, it fails because the dishonest conduct about which Home had learned prior to June 21, 1982 was, as the jury found, not related to the AFCO-investor

¹⁰ C. Douglas Wilson & Co. v. Insurance Co. of No. America, 590 F.2d 1275 (4th Cir.), cert. denied, 444 U.S. 831, 100 S. Ct. 59.

¹¹ Ritchie Grocer Co. v. Aetna Cas. & Sur. Co., 426 F.2d 499 (8th Cir. 1970); Verneco, Inc. v. Fidelity & Cas. Co., 219 So.2d 508, (La. 1969); St. Joe Paper Co. v. Hartford Accident and Indem. Co., 359 F.2d 579, (5th Cir. 1966); cases discussed at Ct. App. Decis., p. 9.

loans; thus notice to F&D of conduct that did not result in the loss that Home later sustained would have perfected nothing. Third, as the Court of Appeals held, Section 11 is ambiguous in the situation where successive insurers are involved, and, for the reasons explained by the Court, is "susceptible to the interpretation that it does not bar the continuation of the same fidelity loss coverage under the Aetna bond that existed under the F&D bond." Ct. App. Decis., p. 14. The holding by the Court of Appeals, which affirmed the Trial Court's ruling below, is based on a textual reading of Section 11 as well as consideration of its purpose and objective, and relies on accepted rules of construction where ambiguity exists. As such, this is not a situation where supervisory correction, pursuant to Rule 46(c), is warranted.

CONCLUSION

Based on the above argument and authorities, Home requests that the Supreme Court deny Aetna's petition for writ of certiorari.

DATED this ____ day of November, 1991.

CALLISTER, DUNCAN & NEBEKER

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CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the foregoing APPELLEE'S BRIEF OPPOSING AETNA'S PETITION FOR WRIT OF CERTIORARI was mailed, postage prepaid, on this ____ day of November, 1991 to the following:

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