



COMMONWEALTH OF KENTUCKY  
SUPREME COURT OF KENTUCKY  
2012-SC-000267-D

MARK D. DEAN, P.S.C.

APPELLANT

v. APPEAL FROM THE KENTCKY COURT OF APPEALS  
NO. 2010-CA-002152  
AFFIRMING THE SHELBY CIRCUIT COURT  
ACTION NO. 09-CI-00050

COMMONWEALTH BANK &  
TRUST COMPANY

APPELLEE

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**REPLY BRIEF OF APPELLANT MARK D. DEAN, P.S.C.**

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**CR 76.12(6) CERTIFICATE**

The undersigned hereby certifies that copies of this brief were served by U.S. Mail, First Class, postage pre-paid, this 25th day of April 2013, upon the following: Hon. John T. McGarvey, Hon. Eric M. Jensen, and Hon. Bradley S. Salyer, Morgan & Pottinger, P.S.C., 601 W. Main St., Louisville, KY 40202; Hon. Debra Stamper, General Counsel, Kentucky Bankers Association, 600 W. Main Street, Suite 400, Louisville, KY 40202; Hon. William Hickman, III, Jones & Hickman, P.S.C., P.O. Box 3850, Pikeville, KY 41502; the Hon. Charles R. Hickman, Chief Circuit Judge, 501 Main Street, Suite 15, Shelbyville, KY 40065.; Lowry S. Miller, Clerk, Shelby Circuit Court, 401 Main Street, Suite 101, Shelbyville, KY 40065; and Samuel P. Givens, Jr., Clerk, Kentucky Court of Appeals, 360 Democrat Drive, Frankfort, KY 40601. Appellant did not withdraw the record on appeal.

  

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## INTRODUCTION

The Court of Appeals decided disputed issues of material fact in affirming the Shelby Circuit Court's summary judgments dismissing Mark D. Dean, P.S.C.'s ("Dean") claims against Commonwealth Bank & Trust Company ("CBT") relating to CBT's unsafe banking practices which allowed for the perpetration of a check-kiting scheme against Dean. The sworn affidavit and deposition testimony in this case supports that Dean would not have been able to determine from bank statements that its bookkeeper was engaged in check-kiting, had exceeded the scope of her authority, and that her signature upon checks was "unauthorized".

## ARGUMENT

### **I. THE COURT OF APPEALS ERRED IN DECIDING THIS APPEAL ON ALTERNATIVE GROUNDS NOT FULLY EXPLORED IN THE TRIAL COURT OR ARGUED BEFORE THE COURT**

In its Opinion Affirming, the Court of Appeals rejected the trial court's analysis of the case, but affirmed the result, deciding instead that (1) KRS 355.4-406 was the applicable rule of law and (2) the statute operated under the facts of this case to bar Dean's claims against CBT. In determining whether an affirmance on alternative grounds is proper, this Court has looked to whether the issue was presented for consideration by the trial court and whether the parties had sufficient opportunity to present evidence and argument on the issue to the appellate court. Otherwise, the appellate court risks deciding a case on grounds not fully developed, and there is substantial risk that the decision could be based on an incomplete or insufficient record.

The cases cited by CBT bear this out. In *Fischer v. Fischer*, 197 S.W.3d 98, 103 (Ky. 2006), the trial court was "presumed to have examined the issue, as it is pivotal in

determining the ultimate question . . .” and “both sides argued the [alternative] issue extensively at the oral argument before this Court.” Likewise, in *American General Home Equity v. Kestel*, 253 S.W.3d 543, 549 (Ky. 2006), the parties “briefed the issue of litigation-conduct waiver in the trial court” and had the opportunity to do so in the appellate court, though American General chose not to address the merits of the issue. In *Emberton v. GMRI, Inc.*, 299 S.W.3d 565, 576 (Ky. 2009), the appellee “joined with Appellant, Emberton, to address the issue in its summary judgment motion to the trial court” and the record showed “GMRI raised the issue before the Court of Appeals.”

In this matter, the Shelby Circuit Court considered whether KRS 355.4-406 was applicable, but rejected the argument and therefore never addressed the issue of whether, as applied to the facts, KRS 355.4-406 would bar Dean’s claims. *See, R. at 226-234, 2/17/10 Opinion and Order*. Additionally, the parties did not have adequate opportunity to address this issue before the Court of Appeals. The Court of Appeals *sua sponte* cancelled oral arguments, depriving the parties of an opportunity to address issues related to the application of KRS 355.4-406 to this matter. *Appellant’s Brief, Appendix 2*.

Where, as here, the appellate court’s determination of an issue on appeal gives rise to new issues, determination of the issues are “best reserved for the trial court as it is in the best position to consider any additional arguments presented to it on remand and to address these arguments with appropriate findings.” *Brown v. Louisville Jefferson County Redevelopment Auth., Inc.*, 310 S.W.3d 221, 225-26 (Ky. App. 2010); *see also, Wakefield v. Manning Equip., Inc.*, 2008 WL 898079, \*2 (Ky. App. Apr. 4, 2008)(“[W]e

vacate and remand this matter to the trial court for further discovery at which point the court must reevaluate the issue of KRS 342.610(2)(b) . . .”<sup>1</sup>

**II. THE COURT OF APPEALS ERRED IN DECIDING ISSUES OF FACT TO DETERMINE THAT KRS 355.4-406 BARRED DEAN’S UCC CLAIM**

The Court of Appeals’ affirmance turns on whether the “circumstances make it unreasonable to expect that [Dean] should have discovered the unauthorized payment.” *Opinion Affirming, Appendix at 1, p. 9-10* (Emphasis added). “Reasonableness” is a question of fact. *R.T. Vanderbilt Co., Inc. v. Franklin*, 290 S.W.3d 654 (Ky. App. 2009).

In reviewing a summary judgment, the Court of Appeals is merely to decide whether an issue of fact exists, not to determine the issue of fact. *James Graham Brown Found., Inc. v. St. Paul Fire & Marine Ins. Co.*, 814 S.W.2d 273, 276 (Ky. 1991). Though the Court of Appeals claimed to be resolving this case on “uncontroverted facts”, *Opinion Affirming, p. 10*, in truth, there are genuine issues of material fact in dispute and the Court of Appeals weighed evidence in reaching its conclusion. The genuine issues of material fact include, but are not limited to, (1) whether CBT alerted Dean to suspicious activity on its account and (2) whether Dean, even if it had received bank statements, could reasonably determine that signatures on the checks were “unauthorized.”

The Court of Appeals impermissibly resolved the first issue against Dean. In its recitation of facts, it concludes that in “January 2005, Belinda Nichols, Commonwealth’s Market President for Shelbyville, learned of suspicious activity on Dean’s escrow account indicative of check-kiting; she arranged a meeting with Mark on February 1, 2005, to discuss the account activity.” *Opinion Affirming, p. 3*. In direct contrast to this,

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<sup>1</sup> CR 76.28(4)(c) allows for citation to unpublished cases rendered after January 1, 2003.

Mark Dean submitted a sworn affidavit testifying that “CBT never reported to me the suspicious activity by Ms. Wills.” *R. at 191-92, Affidavit of M. Dean.*

The Court of Appeals further impermissibly decided the disputed issue of whether Dean could ascertain from the bank statements that Wills’ signature was “unauthorized”. In order for Dean to have known the signatures were “unauthorized,” Dean would have had to be able to ascertain from the statements that Wills had exceeded the scope of her authority. The Court concluded, “Mark effectively acknowledges that when, finally, he did look at the bank statements, he *was* alerted to Jody’s curious accounting and check-writing practices . . .” *Opinion Affirming, p. 10.* Notably, the Court of Appeals does not cite to where in the record this alleged acknowledgement can be found. In fact, the record evidence is directly contrary to this finding: Mark Dean’s sworn affidavit testimony is that law enforcement officials could not decipher the CBT statements without expert intervention and that “even if I had received any bank statements, like the law enforcement officials, I would not have been able to decipher fraud without expert intervention.” *R. at 191-92, Affidavit of M. Dean.* (emphasis added). CBT’s own employee, Nate Evans, Director of Risk Management and Credit Policy at CBT, also provided deposition testimony that supports that it would have been unreasonable to expect a customer to be able to determine from the statements that fraud was occurring, such that Wills’ signature would be recognized as “unauthorized”. *Evans Depo., p. 35-39.*

This is a distinguishing factor between the present matter and case law cited by CBT. Even CBT must admit that the main case upon which it relies, *Concrete Materials, Corp. v. Bank of Danville*, 938 S.W.2d 354 (Ky. 1997), is distinguishable: “Unlike in this

action, the embezzling employee in *Concrete Materials Corp.* was not authorized to sign checks.” (Emphasis added). The question presented in *Concrete Materials*, was far easier to resolve than the question presented here. Where an unauthorized employee signs a check or where the signature of another is obviously forged, review of bank statements and accompanying items will easily reveal the “unauthorized” nature of a signature. In the present matter, however, Wills’ signature, on its face, would not have appeared to be “unauthorized.” Rather than impermissibly construe the evidence against Dean, the Court of Appeals should have remanded this matter to the trial court for further proceedings based upon its ruling that KRS 355.4-406 was applicable to the case.

### **III. CBT CANNOT CLAIM ERROR BY THE COURT OF APPEALS BECAUSE IT FAILED TO FILE A CROSS-APPEAL**

CBT charges that the Court of Appeals erred in its opinion. *See, Appellee’s Brief, p. 18-21.* If CBT believed the Court of Appeals’ decision to be erroneous, it was required to file a cross-appeal to have the issue reviewed. *Lainhart v. Rural Doxol Gas Co.*, 376 S.W.2d 681, 682 (Ky. 1964)(“Appellee did not avail itself of cross-appeal as provided by CR 74; thus, the judgment may not be modified . . .”); *Smith v. Wal-Mart Stores, Inc.*, 6 S.W.3d 829 (Ky. 1999)(party must file “protective cross-appeal” to allege trial court error); *Wright v. Thomas*, 209 S.W.2d 315, 317 (Ky. 1948)(where no cross-appeal, Court of Appeals cannot consider alleged error); *Miller v. Richards*, 205 S.W.2d 308, 309 (Ky. 1947)(appellee must take cross appeal to have Court of Appeals consider error); *Oliver v. Crewdson’s Adm’r*, 77 S.W.2d 20 (Ky. 1934)(part of judgment unfavorable to appellee cannot be considered on appeal unless cross-appeal is taken). Just last week, the Court of Appeals re-affirmed that an appellee cannot complain of an error from which it failed to

take a cross-appeal. *S. Tax Serv., LLC v. Tax Ease Lien Inv. 1, LLC*, 2013 WL 1688311 (Ky. App., Apr. 19, 2013).

In any event, the argument fails on the merits. CBT and *Amicus* would have this Court give a free pass to any bank that provided statements to a customer regardless of any error or culpability on the part of the bank. For example, if discovery reveals that CBT's own employee provided counterchecks in exchange for a share of the stolen money or if CBT's employee knew that Wills' actions were unauthorized or illegal, but covered them up instead of reporting them, CBT and *Amicus* allege that KRS 355.4-406 completely indemnifies the bank. KRS 355.4-406, however, is not a blanket indemnification statute.

CBT and *Amicus* rely on *Concrete Materials* to their peril. *Concrete Materials* does not hold that all claims are limited by the one-year time limit in KRS 355.4-406(6). In *Concrete Materials*, this Court discussed claims not barred by the one-year statute, including claims containing questions of fact about the agency of the employee, just like in this case. *Concrete Materials*, at 259-260. In *Concrete Materials*, a bank customer claimed "that the conduct of the bank allowed the embezzlement of corporate funds by a corporate employee." *Id.* at 256. The bank teller stamped two deposit slips, one blank, and the corporate employee created false bank records from the blank slip. *Id.* Unlike in the case at bar, even a brief examination of the bank statements would have revealed the unauthorized withdrawals. *Id.* at 258. This Court found that fact to be a determinative factor in that case.

In this case, forensic accounting was required for discovery, and the bank statements could not provide notice to Dean, of any unauthorized activity. This Court

distinguished *Concrete Materials* from *Bullitt County Bank v. Publishers Printing Co.*, 684 S.W.2d 289 (Ky. App. 1984), where the Court of Appeals found that banks have a duty to exercise good faith and use ordinary care in handling customer accounts. In *Concrete Materials*, this Court held that that banks could be subject to negligence claims under a situation such as arose in *Bullitt County Bank*, regardless of the time limit under KRS 355.4-406(6). *Concrete Materials* at 258.

#### **IV. DEAN'S UCC CLAIM IS NOT BARRED BY THE STATUTE OF LIMITATIONS**

This was the original issue appealed to, but not addressed by, the Court of Appeals. Dean hereby incorporates the arguments in his appellant's brief to the Court of Appeals as if such argument were set forth in full. *Dean's Court of Appeals Appellant Brief*.

The trial court dismissed Dean's UCC claim pursuant to K.R.S. § 355.4-111, which provides "[a]n action to enforce an obligation, duty, or right arising under this article must be commenced within three (3) years after the claim for relief accrues." Currently, there are no cases directly addressing this statute and its application.

In *McLain v. Dana Corp.*, 16 S.W.3d 320 (Ky. App. 1999), the Court made clear that "the discovery rule provides that a cause of action accrues when the injury is, or should have been discovered." "A cause of action will not accrue...until the plaintiff discovers or in the exercise of reasonable diligence should have discovered not only that he has been injured but also that his injury may have been caused by the defendant's conduct." *R.T. Vanderbilt Co., Inc. v. Franklin*, 290 S.W.3d 654, 659 (Ky.App. 2009).

There are genuine issues of material fact as to when Dean discovered, or should have discovered his injury – the embezzlement of funds by check kiting scheme – and

also that his injury was caused by CBT's conduct. For Dean to have known that the checks bore an "unauthorized" signature, he had to first know that Wills had exceeded her authority as signatory or, in other words, that she was engaged in check-kiting. As set forth above, the facts bearing on this issue are highly disputed.

The Bank's own failure to alert Dean to the suspicious activity it was observing (and participating in) further supports application of the discovery rule in this case. Though there is evidence to suggest that CBT was well aware that fraudulent activity was occurring, *R. at 135-192, Evans Depo, pgs. 9-14, 17*, CBT never alerted Dean to such suspicious activity. *R. at 191-92, Affidavit of M. Dean*. CBT concealed this information from Dean because implicating Wills would have also implicated CBT.

The discovery rule applies to toll Dean's statute of limitations until such time as its injury and the source thereof were known. The trial court erred in finding that the discovery rule was inapplicable to Dean's UCC claim and must be reversed.

**V. DEAN'S COMMON LAW CLAIMS ARE NOT BARRED BY THE UNIFORM COMMERCIAL CODE, EITHER BY A STATUTE OF REPOSE OR A STATUTE OF LIMITATIONS**

The Uniform Commercial Code ("UCC") is not a statute without limits. While it is intended to guide commercial transactions and, in part, the negotiation of checks and other instruments, it does not operate to shelter banks from any and all causes of action which might be brought against it. Certainly, for example, the bank would not argue that the UCC pre-empts claims against a bank for employment discrimination or premises liability. Such matters are clearly beyond the statute's scope.

The question for this Court is whether Dean's particular common law claims arise from the payment of an unauthorized check. If not, then like claims for employment

discrimination or premises liability, Dean's negligence and other common law claims are not governed or pre-empted by the UCC, and any statutes of repose or limitations would not apply to the common law claims. In *City National Bank v. Strickland*, 273 S.W.2d 667 (Tex. App. 1954), for example, the court found that the UCC statute of repose did not bar plaintiff's common law claims where the claims were based on the bank vice-president's misrepresentations of the purpose for which the disputed check had been drawn and the use which had been made of the funds, not on the actual honor and cashing of an improper check.

In *Bullitt County Bank*, the Court of Appeals found that the bank breached its duty of good faith and ordinary care when it allowed an employee authorized to deposit checks to present a check with a request that the bank exchange the check for a cashier check made payable to another bank. *Id.* at 291.

There is little doubt, given the law and the facts involved, but that the Bank violated its duty of ordinary care. No employee of the Bank ever notified [Plaintiff] of [Plaintiff's employee's] strange departure from his regular banking duties following 1975. The tellers' deposition testimony indicates that they simply assumed he was acting on behalf of [Plaintiff].

*Id.* at 292.

Just as in *Bullitt County Bank*, CBT never questioned Wills' practice of seeking counterchecks and moving large sums of money, violating the duty of ordinary care. In the *Bullitt County Bank* case, the bank argued that KRS 355.4-406 bars the action; the Court of Appeals ruled otherwise: it bars actions based on unauthorized signatures only.

Dean's common law claims are not based upon the wrongful payment of unauthorized checks, but from CBT's violation of safe banking practices in the provision of checks and in failing to report to the account holder or authorities that irregular

banking activity was occurring.<sup>2</sup> *R. at 1-9, Complaint.* Neither the provision of checks nor negligence in failing to report suspicious activity falls within the parameters of matters covered by the UCC.

### CONCLUSION

For the foregoing reasons, this Court should overturn the Court of Appeals' affirmance of the Shelby Circuit Court's summary judgments. There are genuine issues of material fact with respect to whether it was "reasonable" for Dean to have discovered from the bank statements that check kiting was occurring, rendering Wills' signature "unauthorized" and how KRS 355.4-406 would be applied to the facts of this case. There are genuine issues of material fact with respect to when Dean knew or should have known of his injuries and that CBT's wrongful acts were the cause thereof. Regardless of the disposition of Dean's UCC claim, he has viable common law claims which should not have been dismissed on summary judgment and which are not controlled by either the statute of repose or the statutes of limitations of the Uniform Commercial Code.

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<sup>2</sup> CBT misstates Dean's claims with respect to CBT's failure to notify Dean of the suspicious activity on its account or report such activity to authorities. Dean does not complain that CBT "failed to notify" him of the making of a Suspicious Activity Report ("SAR"), but that CBT wholly failed to make such report. While the statutory provisions cited by CBT purport to restrict CBT's ability to disclose the actual SAR, it does prohibit CBT from notifying Dean of underlying concerns about account activity.