

NO. 36764-5-II

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COURT OF APPEALS, DIVISION II

STATE OF WASHINGTON

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FIDELITY AND DEPOSIT COMPANY OF MARYLAND,

Appellant,

v.

ALLIANCEONE RECEIVABLES MANAGEMENT, INC., a  
Delaware corporation, d/b/a ALLIED CREDIT and/or  
ALLIANCEONE, INC.,

Respondent,

DEBORAH JO DALLY, and NAVY FEDERAL CREDIT  
UNION,

Defendants

FILED  
COURT OF APPEALS  
DIVISION II  
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STATE OF WASHINGTON  
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BRIEF OF RESPONDENT

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## **I. ISSUES PRESENTED**

1. Whether an indemnity provision for loss arising out of an act or omission can be triggered when there otherwise is no viable cause of action for the alleged act or omission?
2. Whether an indemnity provision that applies to loss arising out of an act or omission of the indemnitor requires that the alleged act or omission be actionable under a cognizable legal theory?
3. Does a clause that provides for indemnification for loss arising out of an act or omission of the indemnitor require proof of some type of causal connection with the alleged loss?
4. Does an indemnification provision for loss arising out of the act or omission of the indemnitor extend to loss resulting from the criminal acts of an employee of the indemnitee?
5. Whether Appellant presented evidence that raised genuine issues of material fact on any of the causes of action alleged?

## **II. COUNTER STATEMENT OF THE CASE**

### ***A. INTRODUCTION***

This lawsuit arises out of the theft of funds from the City of Poulso (‘‘the city’’) by a former employee, Deborah Dally. From June, 1996 up to December, 2002, when her theft was discovered, Dally was employed by the city as a municipal court administrator. Over that extended period of time, she stole cash and checks that had been made payable to the city by Respondent AllianceOne. AllianceOne provided, and continues to provide, contract collection services, pursuing overdue fines, penalties and other sums owed to the city.

Appellant Fidelity & Deposit Company of Maryland (‘‘Fidelity’’) insured the city against employee dishonesty, and paid the city for Dally’s theft. It now seeks to recover from AllianceOne and the Navy Federal Credit Union (NFCU). The trial court properly granted summary judgment. Fidelity has no viable cause of action against AllianceOne.

**B. BACKGROUND**

On April 11, 1994, the city entered into a Professional Services Contract with AllianceOne, the purpose of which was to collect unpaid fines, penalties and costs owing to the city. (CP 26-27.) The contract contains the following pertinent provision:

**VII. Remittances:** Funds collected by the Agency shall be paid to the Client on or before the fifteenth (15) day of each month for collections made the proceeding month. Payments to the Client shall be for the total amount collected, less the appropriate fees. The Agency shall supply sufficient documentation with monthly payment to allow independent verification of total amounts collected and calculations of appropriate fees withheld. In the event additional reports are deemed necessary by the Client for further breakdown purposes, the Agency will cooperate with the Client in providing necessary reports. The Client may audit the Agency's records pertaining to accounts assigned for collection upon reasonable advance notice.

The contract identifies the "Client" as the City of Pouslbo Municipal Court in the first paragraph, but also as just the City of Pouslbo above the signature line on the second page. (*Id.*)

Typically, AllianceOne submitted four checks per month to the city: two on or about the 15<sup>th</sup> day of each month, and two

checks at the end of each month. (CP 22-24, and 578-1007.) One of the checks paid the interest that had been collected and the other was for principal. In some months there were additional remittances. (CP 22-24.) A total of 252 checks were identified as having been stolen. (CP 23 and 578-1007.)<sup>1</sup>

Along with the checks, AllianceOne provided the city with statements, which broke out how much had been received, from whom, and the allocation to principal and interest. (CP 22-24 and 28-578.) The statements allowed the city to verify funds and credit the appropriate accounts and files.

Throughout the subject period of time, AllianceOne made checks payable to the city in several slightly different ways: to “Poulsbo Municipal Court,” to “Poulsbo Municipal Infractions,” to “Poulsbo Municipal,” and to “Poulsbo Municipal Criminal.” (CP 23-24 and 578-1007.) The vast majority of the checks were made payable to “Poulsbo Municipal Court,” or “Poulsbo Municipal.” (*Id.*) Only a handful were made payable in the other two ways. The city negotiated and deposited checks made payable in the varied ways that Dally did not manage to steal. (CP 23-24.)

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<sup>1</sup> CP 1011-1017 is a list of the AllianceOne checks that Dally stole. CP 1019-1023 is a list of the checks that Dally did not steal.

In December, 2002, Dally's theft was finally detected by another Poulsbo Municipal Court employee.

**C. THE THEFT INVESTIGATION**

On February 4, 2003, Officer T. J. Keeler of the Kitsap County Sheriff's Office formally interviewed Deborah Dally in the presence of her attorney. (CP 1025-29.) Regarding her theft of AllianceOne checks, Dally admitted as follows:

I next asked DEBORAH about the AllianceOne checks. She told me she would get four a month from them, two were for the principal amount collected and two were for interest. She said she would then deposit the checks she wanted into her Navy Federal Credit Union (NFCU) account. I asked her how she would be able to do that without the bank questioning her and she told me she would write up a letter on Poulsbo letterhead stating the money was owed to her for back child support. She also told me the only thing she used the NFCU account for was to have her ex-husband's child support payment direct deposited and to deposit the AllianceOne checks into. She said she would then sign SUE O'BRIEN's name and deposit the check. I asked her why she was signing SUE's name and she told me it was because SUE worked for the city before she did. She told me she would sign SUE's name on the bottom of the letter she used to deposit the checks. DEBORAH told me NFCU never checked any further and

deposited the checks into her account without question.

(CP 1025)

Dally presented checks for deposit at NFCU along with letters that she forged on the city's letterhead. In those letters, she represented that the city had endorsed the check to her, and that it was for past due child support collected from Dally's ex-husband.

(CP 1031)

Dally pled guilty to numerous charges. On April 18, 2003, she was sentenced to the maximum of the sentencing range, 57 months. On June 17, 2003, an order of restitution was entered against her for \$307,261.16. (See, Kitsap County Superior Court Cause No. 03-1-00231-1.)

The Washington State Auditor's Office investigated the city's municipal court accounting records for the period of June 25, 1996 through December 12, 2002, and issued a *Special Audit Report*. (CP 1033-39) That report summarized the audit of the cash and collection agency receipts for that period, and contains the following conclusions:

Our audit has determined that accountability for revenue from the City's collection agency was not properly established in the Court's accounting system for approximately seven and one-half years. When the collection agency remitted funds to the City the former Court Administrator wrote off the amount of the balance of the citizen's account and then deposited the checks for these transactions into her personal banking account. The former Court Administrator subsequently admitted to the Kitsap County Sheriff's Office that she misappropriated public funds from the Court and pleaded guilty to all charges in Kitsap County Superior Court on March 12, 2003. Sentencing is scheduled for April 18, 2003.

(CP 1037.)

The report continues:

(2) Collection Agency Cash Receipts. The former Court Administrator also took funds that the City's collection agency remitted to the Court. To complete processing of these transactions the information must be entered into the DISCIS accounting system and funds deposited in the bank. However, the former Court Administrator again circumvented the Court's internal controls over cash receipts by entering false information in the DISCIS accounting system to eliminate accountability for these funds. Collection agency checks for these transactions were then deposited into the former Court Administrator's personal bank account. We found 254 collection agency checks that were not receipted at

the Court. Those transactions totaled losses of \$285,100.45 between June 25, 1996 and December 11, 2002.

\* \* \* \*

We noted the following internal control weaknesses in the Court:

- No one monitored the manual cash receipting process to ensure that all funds collected were properly entered into the DISCIS accounting system and deposited in the bank each day.
- Transaction information for manual cash receipt forms were not entered sequentially into the DISCIS accounting system.
- Deposits were not made intact daily. Delays in depositing funds ranged from two to 32 days.
- Generic cash receipt forms were used rather than official cash receipt forms with the City's name preprinted on them. These generic forms do not provide an appropriate level of control over cash receipts since they can be purchased by anyone from any office supply store and used for unauthorized purposes.
- No one monitored the various non-cash credit reports to insure that all transactions were

authorized, approved and properly supported. These included reports for restitution out-of-balance, restitution adjustments, accounts receivable adjustments, accounts payable adjustments, adjustment, receipts, overpayments, and deleted accounts.

- No one monitored the account's receivable system to ensure that all funds were properly collected and deposited in the bank. In addition, the Court's accounts receivable were not recorded in the City's accounting system or monitored by the Finance Department.

(CP 1038.)

The state auditor's office recommended that a claim submitted to the city's insurer. The city subsequently made a claim against Fidelity, under Public Employee Dishonesty Policy No. CCP 0045720. Fidelity claims to have paid the city \$306,261.16 for Dally's theft.

The city negotiated many AllianceOne checks throughout the entire period of time the theft occurred. (CP 23-24; *Compare*, CP 1011-17, the list of CHECKS THAT DALLY STOLE, with CP 1019-23, the list of CHECKS THAT DALLY DID NOT STEAL.) The city did not refuse any checks tendered by AllianceOne, and

no representative of the city ever contacted AllianceOne to direct how checks were to be made payable. (CP 24.) Dally stole checks made payable in different ways, and the city cashed checks made payable in those different ways. The course of dealings between the parties is uncontroverted, and there was no exclusive manner checks were to be made payable. (*Id.*)

After the theft was discovered, the city and AllianceOne continued to do business in exactly the same way, under the 1994 contract. A new agreement was executed in March, 2007, and the parties continue to do business. (CP 24.) Even after Dally's theft was discovered, the city did not direct that remittance checks be made payable in any specific way or in any different manner. AllianceOne continues to this day to make checks payable to "Poulsbo Municipal Court." (*Id.*) The city continues to cash them, just like it did during the period of time Dally was employed. The city has never contacted AllianceOne to discuss whether AllianceOne would review endorsements on returned checks on behalf of the city. AllianceOne does not provide such a service for any client. (*Id.*)

***D. FIDELITY'S CLAIMS***

In November, 2004, Fidelity filed this lawsuit against AllianceOne, Dally and NFCU. Against AllianceOne, Fidelity asserted three claims: breach of contract, negligence and indemnification. AllianceOne moved for summary judgment, which was heard on June 22, 2007, by the Honorable Russell Hartman of the Kitsap County Superior Court. (June 22, 2007, *Verbatim Report of Proceedings*.) At that hearing, Judge Hartman reserved ruling. He issued his decision granting summary judgment on July 20, 2007. The order granting the motion was entered that day. (CP 1172-74) Fidelity filed a motion for reconsideration, which was denied on July 30, 2007. (CP 1177-78)

Because the dismissal of AllianceOne did not dispose of all claims against all parties, AllianceOne moved the court for certification under CR 54 (b), and for entry of final judgment. On August 24, 2007, that motion was granted, (CP 1294-1301), and final judgment was entered that day. (CP 1302-10)

### III. ARGUMENT

#### A. **REVIEW STANDARD**

This court reviews an order granting summary judgment *de novo*. *Osborn v. Mason County*, 157 Wn.2d 18, 134 P.3d 197 (2006); *Ross v. Ticor Title Ins. Co.*, 135 Wn.App 182, 143 P.3d 885 (2006).

CR 56 provides that summary judgment

shall be rendered forthwith when the pleadings, depositions, answers to interrogatories and admissions on file, together with affidavits, if any, show that there is no genuine issue of material fact as a matter of law.

The purpose of summary judgment is to avoid an unnecessary trial. *Zobrist v. Culp*, 18 Wn.App. 622, 637, 570 P.2d 147 (1977). The moving party bears the initial burden of showing the absence of an issue of fact. *Young v. Key Pharmaceutical, Inc.*, 112 Wn.2d 216, 225, 770 P.2d 180 (1989). If that showing is made, the inquiry then shifts to the party with the burden of proof at trial, Fidelity, to establish the existence of each essential element of the claims. *Howell v. Spokane & Inland Empire Blood Bank*, 117 Wn.2d 619, 818 P.2d (1991). The non-moving party may not oppose summary judgment by nakedly asserting that there are

unresolved issues of fact. *Bates v. Grace United Methodist Church*, 12 Wn.App. 111, 529 P.2d 466 (1991). Conclusory allegations, speculative statements or mere arguments are legally insufficient. *McMann v. Benton County*, 88 Wn.App. 737, 946 P.2d 1183 (1997).

Here, AllianceOne satisfied the initial burden of showing the absence of an issue of fact. Fidelity failed to meet the burden that was on it to respond to the motion. There are no genuine issues of material fact, and AllianceOne was entitled to judgment as a matter of law.

***B. ALL OF APPELLANT'S LIABILITY THEORIES REST ON THE SAME TWO ISSUES: THE "PAYEE" ISSUE, AND THE "ENDORSEMENT VERIFICATION" ISSUE***

Each of Fidelity's three causes of action is based upon the same two sets of factual contentions. First, that AllianceOne is liable for the manner in which checks were made payable to the city (the "payee" issue). Second, Fidelity asserts that AllianceOne is liable for not reviewing and verifying endorsements on returned checks to make sure that they were properly endorsed and deposited into the city's account (the "endorsement verification" issue). No other factual grounds have ever been raised to support the breach of contract, negligence or indemnity causes of action.

As a matter of law, the factual grounds were, and they continue to be, insufficient to sustain any cause of action.

***1. THE PAYEE ISSUE***

Fidelity asserts that AllianceOne is liable for not making checks payable in the way it contends. Such arguments are without merit. Fidelity admits that the Professional Services Contract did not specify how payments were to be made. (Appellant's Brief, pg 4; CP 26-27.) That agreement did not contain any instruction as to how checks should be made payable. It did not contain an exclusive definition of "Client."

The vast majority of the checks were made payable to "Poulsbo Municipal Court," or "Poulsbo Municipal." Only a handful were made payable in the other two ways. The city negotiated and deposited the AllianceOne checks that Dally did not manage to steal. In its Complaint, Fidelity claimed that AllianceOne was liable for failing to name only the "City of Poulsbo Municipal Court" as payee. (CP 1062-63.) The original argument was that failing to have the words "City of" in front of "Poulsbo Municipal Court" somehow caused the theft to occur. On appeal, Fidelity's argument changes, and it now asserts that

AllianceOne had a duty to make checks payable only to the “City of Poulsbo.” (Appellant’s brief, pg. 13-15.)

No evidence has ever been presented, because none exists, that making checks payable in either manner would have prevented Dally’s theft. It did not matter how the checks were made payable, as she stole them regardless of the named payee. She could do so because, as the auditor’s office found, the city exercised no oversight whatsoever.

Fidelity admits that the city’s bank “apparently has been willing to deposit the checks from AllianceOne to the City’s account despite the errors in the payee designation on those checks.” (CP 1067, Ins. 18-20.) The city’s bank has “apparently” done so for over 14 years now, and for over five years since Dally’s theft was uncovered. Fidelity further admits that, “[t]o the extent these checks were accepted by the City’s bank and the funds were actually deposited in the City’s account, AllianceOne’s obligation under the contract was met.” (CP 1073, Ins 17-22.) Fidelity acknowledges that the way AllianceOne made the checks payable was not the problem. It argues that the payee designation breached the contract only when checks were stolen by Dally. As there was no difference in the payee

designations between the checks Dally stole and those that the city deposited, the only difference was Dally's criminal acts.

***a. EVEN IF THE PAYEE ISSUE EXISTED, IT WAS WAIVED***

The course of dealings of the parties has continued for over 14 years. Even if there was a contract requirement that checks only be made payable in the manner Fidelity asserts, **which is not the case**, the city waived such a requirement by negotiating, and by continuing to negotiate, AllianceOne checks.

Waiver is the voluntary relinquishment of a known right, and it may be inferred from uncontroverted facts presented here.

A waiver is the intentional and voluntary relinquishment of a known right, **or such conduct as warrants an inference of the relinquishment of such right**. It may result from an express agreement **or be inferred from circumstances indicating an intent to waive**. It is a voluntary act which implies a choice, by the party, to dispense with something of value or to forego some advantage. The right, advantage, or benefit must exist at the time of the alleged waiver. The one against whom waiver is claimed must have actual or constructive knowledge of the existence of the right. He must intend to relinquish such right, advantage, or benefit; and his actions must be inconsistent with any other intention than to waive them.

(Emphasis Supplied.)

*Singer Credit Corp. v. Mercer Island Masonry, Inc.*, 13 Wn.App. 877, 885, 538 P.2d 544 (1975).

It is difficult to conceive of a factual situation more convincing than the one here where waiver has occurred. The city and AllianceOne have had the same relationship since 1994. It is uncontroverted that, over the six and one-half year period that Dally stole from the city, the city negotiated many checks made payable in exactly the same way as those Dally stole. It is also uncontroverted that the city has never refused any check tendered by AllianceOne, for any reason. The city's bank did not reject any of these checks, or "tighten" its deposit requirements. It is further uncontroverted that, after Dally's scheme was discovered in December, 2002, the city still did not direct that remittance checks be made payable in any different manner. AllianceOne continues to make checks payable to "Poulsbo Municipal Court," and the city has never contacted AllianceOne with any specific payee instructions. Fidelity failed to dispute these facts. The city's conduct unequivocally shows that the payee designations were acceptable, and continue to be acceptable, to the city.

Fidelity conjured-up the convoluted payee issue. There is no such requirement in the contract. Even if there was, there is no doubt but that it was waived by over 14 years of undisputed conduct. If there was such an issue, the city certainly would have raised it by now, but it has continued to this day to accept checks made payable in the same way.

No evidence was submitted of any causal connection between the way the checks were made payable and the loss. In his oral decision, Judge Hartman specifically noted this evidentiary void:

[I]t is my belief that there is no fact in evidence or introduced into the record in connection with the summary judgment motion that shows that the varied payee designations that were used on the checks tendered to the city had any impact or anything to do with which of the checks were stolen. And I do not believe that a reasonable trier of fact could-I believe that a reasonable trier of fact could reach but one conclusion, that the payee designations did not in any sense contribute to the losses which were sustained. Just didn't seem to be any correlation at all between the checks that were picked off and how the payee was designated other than choices that were made by the wrongdoer, Ms. Dally.

*Verbatim Report of Proceedings*, July 20, 2007, pg 3, lines 10-23.<sup>2</sup>

The record before this court is devoid of any evidence of a connection between the payee issue and which checks were stolen, i.e. the loss. The payee issue is simply fiction.

## **2. THE “ENDORSEMENT VERIFICATION” ISSUE**

The second factual contention raised is that AllianceOne is liable for failing to verify endorsements on the checks once they were returned by AllianceOne’s bank. Fidelity admits that the Professional Services Contract did not impose such an obligation on AllianceOne. There is no statute, common law or other authority that imposed such a duty.

Fidelity is required to produce evidence of the existence of a duty to verify endorsements, and that the failure to do so caused some type of loss. It did not do so. It could not do so, as it admitted that the contract contains no such obligation and the law does not impose one.

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<sup>2</sup> The cover page of the *VRP* of the oral decision is erroneously dated June 22, 2007, the date of the summary judgment hearing. However, pages 2 through 5 of the oral decision show the correct date in the upper right corner.

Fidelity argues that this state's legislature has placed the duty on a check drawer to verify endorsements, citing RCW 62.A3-406(f). That provision has no application whatsoever to the issues presented here. It deals with the relationship between a check maker and maker's bank. It applies to AllianceOne and AllianceOne's bank. It imposes no obligations on AllianceOne to check endorsement verifications for the benefit of the payee, or the payee's insurance company.

The UCC contains no provision directly applicable to the facts presented in this case. RCW 62.A3-405(b), entitled *Employers Responsibility for Fraudulent Endorsement by Employee*, comes the closest. That provision states, in general, that if an employee (Dally) is entrusted by an employer with handling checks, and the employee fraudulently endorses an instrument, the endorsement is effective as the employer's endorsement. Comment 1 to that section explains:

Section 3-405 is based on the belief that the employer is in a far better position to avoid the loss by care in choosing employees, in supervising them and in adopting other measures to prevent forged endorsements on instruments payable to the employer ....

The UCC does not provide Fidelity with an avenue of relief. Rather, the code puts the burden on the city to choose honest employees, supervise them and establish measures to control and check on how funds are handled and accounted for. As noted in the auditor's scathing report, the city's complete lack of financial controls, or other measures to prevent forged endorsements on instruments payable to the city, resulted in this loss.

**C. THE BREACH OF CONTRACT CLAIM WAS PROPERLY DISMISSED**

Judge Hartman correctly ruled that there was no statutory or common law theory of liability that supports recovery. *Verbatim Report of Proceedings*, July 20, 2007, pg 2, lines 7-9.

The only arguments presented regarding the contract claim concern the payee issue. See, Appellant's Brief, pgs. 13-15 § II B.) Fidelity concedes that the agreement did not require AllianceOne to verify endorsements. The contract also did not identify how checks were to be made payable.

A plaintiff in a contract action must prove a valid agreement, breach and resulting damage. *Lehrer v. State Dept.*

*of Social and Health Services*, 101 Wn.App. 509, 516, 5 P.3d 722, 727 (2000). Breach of contract is actionable only if the contract imposes a duty, the duty is breached, and the breach proximately causes damage to the plaintiff. *Northwest Independent Forest Mfgs. V. Department of Labor and Industries*, 78 Wn.App. 707, 899 P.2d 6 (1995).

The contract did not specify how checks were to be made payable. The uncontroverted evidence is that the city waived such a requirement even if it did exist, which it did not. Fidelity admits that the contract did not require AllianceOne to verify and/or confirm endorsements. The undisputed fact is that the contract did not impose the duties Fidelity claims were breached. Nevertheless, Fidelity boldly goes where no legal theory will take it and continues to assert that the trier of fact could somehow find a breach of contract.

Fidelity failed to raise issues of material fact regarding the breach of contract claim. Having submitted no evidence to the contrary, the breach of contract claim was properly dismissed.

**D. THE NEGLIGENCE CLAIM WAS ALSO PROPERLY DISMISSED**

Fidelity, like any plaintiff, must prove all four elements of a negligence cause of action: (1) duty, (2) breach of duty, (3) damage or injury and (4) proximate cause. *Hansen v. Washington Natural Gas*, 95 Wn.2d 773, 632 P.2d 504 (1981); *Shepard v. Mielke*, 75 Wn.App. 201, 877 P.2d 220 (1994). The existence of a duty is a question of law. *Shepard, supra* at 205.

Fidelity's negligence claim is based upon the same factual allegations as the breach of contract claim; that AllianceOne had some type of duty to review endorsements on returned checks, and a duty to issue checks payable only to the "City of Poulsbo Municipal Court," or the "City of Poulsbo." As a matter of law, no such duty exists.

No duty was imposed on AllianceOne by the terms of the contract, by common law or by statute. Fidelity repeatedly argues that it was foreseeable that checks would be stolen, and that, simply by making payments by check, Fidelity is liable for Dally's theft. Fidelity ignores long-standing law to the contrary. There was no duty to foresee the criminal acts of the city's employee.

In *Stouffer & Knight v. Continental Cas. Co.*, 96 Wn.App. 741, 982 P.2d 105 (1999), the plaintiff, a law partnership, sued its malpractice carrier for coverage for the firm's liability for a legal assistant's theft of client trust funds. One of the allegations was that the insurer was negligent for failing to provide loss control services.<sup>3</sup> The court noted that the only contract between the law firm and its insurer was the insurance policy, and that the contract did not mention loss control prevention. With respect to the negligence claim, the court stated, at 753 -54:

Knight next alleges liability on CNA's part for negligent provision of loss control services. A cause of action for negligence requires the plaintiff to establish four elements: (1) the existence of duty owed; (2) breach of that duty; (3) injury resulting from that breach; and (4) a proximate cause between the breach and the injury. *Tincani v. Inland Empire Zoological Soc.*, 124 Wn.2d 121, 127-28, 875 P.2d 621 (1994). The threshold determination, whether a duty exists, is question of law. *Degel v. Majestic Mobile Manner, Inc.*, 129 Wn.2d 43, 48, 914 P.2d 728 (1996). "The existence of a duty may be predicated upon statutory provisions or on common law principles." *Degel*, 129 Wn.2d at 49, 914 P.2d 728) "When no duty of care exists, the defendant cannot be subject to liability for negligent conduct." *Webstad v. Stortini*, 83 Wn.App. 857, 865,

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<sup>3</sup> The insurance company sponsored loss control seminars and mailed newsletters discussing loss prevention.

924 P.2d 940 (1996). Under the common law, a person does not have a duty to protect others from the criminal acts of third parties absent a “special relationship.” *Webstad*, 83 Wn.App. at 865-67, 924 P.2d 940. Washington courts have recognized “special relationships” only in circumstances that are protective in nature, i.e., whether the relationship involved an element of entrustment. *Webstad*, 83 Wn.App. at 869, 924 P.2d 940. Knight does not allege facts necessary to establish a special relationship between himself and CNA. The only contract between the two parties is the insurance policy, which makes no provision for loss control services.

\* \* \* \*

The evidence is undisputed that CNA never undertook the provision of loss control services for Knight. Thus, CNA owed no duty to provide loss control for Knight, and, as a matter of law, Knight cannot maintain an action against CNA based upon negligent provision of loss control services.

Here, there is no duty under the common law, statute, or otherwise that requires a check maker to verify the endorsements on negotiated checks to ensure that they have not been stolen by an employee of the payee. There was no duty to make checks payable as Fidelity claims. No duty existed to protect the city from the criminal acts of the city’s employee. There is no evidence of a special relationship, or even an attempt to argue that one existed.

Financial oversight of employees handling money was the responsibility of the city alone. The failure to have adequate financial controls in place was the city's fault. As a matter of law, AllianceOne did not owe a duty to the city, and Fidelity has no negligence action.

***E. THERE LIKEWISE IS NO VALID  
INDEMNIFICATION CLAIM***

Fidelity contends that the indemnity provision creates a potential avenue for recovery, even though there is no viable underlying legal theory of liability against AllianceOne. According to Fidelity, any loss whatsoever, even those caused by intentional, criminal acts, fall within the provision.

The indemnity clause requires that the loss arise out of an act or omission of AllianceOne. It does not address loss occurring due to the acts or omissions of employees of the city, or of criminals. The provision specifically excludes loss due to the negligence of the city, which indisputably has been established. Fidelity failed to submit any evidence to controvert the auditor's findings. Continuing to assert that the city was not at fault for what occurred is simply ridiculous.

Appellant's argument is that there need not be any type of causal connection whatsoever between AllianceOne's alleged act or omission and the city's loss by theft. That argument would make the phrase "arising out of an act or omission" meaningless. Even though it may be broader than proximate cause, the term "arising out of" still requires a causal connection between the complained of act or omission and the loss.

It is true, as Fidelity submits, that parties to a contract are free to establish liability instead of negligence as the trigger for indemnification. *McDowell v. Austin Company*, 105 Wn.2d 48, 710 P.2d 192 (1985). But, causation, not negligence, is the touchstone of the trigger. *Id.*, citing *Continental Cas. Co. v. Seattle*, 66 Wn.2d 831, 405 P.2d 581 (1965), *Jones v. Strom Constr. Co.*, 84 Wn.2d 518, 527 P.2d 1115 (1974). Causation must exist from the act or omission.

What are the "acts or omissions" under the indemnity claim that Fidelity contends gave rise to the loss by theft? The same two sets of factual contentions it cites to support the breach of contract and negligence claims: the payee issue and the endorsement verification issue. As shown above, there is no

liability under any cause of action for either set of facts, even when all evidence is stretched and construed as broadly as possible in Fidelity's favor. When there is no possible theory of recovery against AllianceOne for either the payee issue or the endorsement verification issue, as a matter of law, there is no liability to indemnify the city for those same alleged acts or omissions.

Fidelity submitted no evidence showing that AllianceOne's acts or omissions were in any way wrongful, under tort or contract or any other theory, and that the acts or omissions gave rise to the loss. Fidelity failed to submit evidence raising any issue of fact, and summary judgment was proper.

Indemnity agreements are essentially agreements for contractual contributions, whereby one tortfeasor, against whom damages and favor of an injured party have been assessed, may look to another for reimbursement. *Stocker v. Shell Oil Co.*, 105 Wn.2d 546, 549, 716 P.2d 306 (1986). When interpreting an indemnity provision, we apply fundamental rules of contract construction. *Jones v. Storm Constr. Co.*, 84 Wn.2d 518, 520 P.2d 527, 1115 (1974). The words used in a contract should be given their ordinary meaning. *Universal/Land Constr. Co., v. City of Spokane*, 49 Wn. 634, 637, 745 P.2d 53 (1987). Courts may not adopt a contract

interpretation that renders a term absurd or meaningless. *Seattle-First Nat'l. Bank v. Westlake Park Assocs.*, 42 Wn.App. 269, 274, 711 P.2d 361 (1985).

*MacLean Townhomes, LLC. v. America 1<sup>st</sup> Roofing & Builders, Inc.*, 133 Wn.App. 828, 831, 138 P.3d 155 (2006).

However broadly written any indemnity provision may be, this general principal must be kept in mind. The indemnification provision here states that AllianceOne would indemnify the city from any "loss, damage, costs, charges, expense, liability claims, demands, or judgments of whatsoever kind or nature, whether to persons or property arising wholly or partially out of an act or omission on the part of [AllianceOne] its subcontractors and/or employees, except to such injury or damages as shall have been caused by or resulted from negligence of the [city]." The phrase "loss, damage, costs, charges, expense, liability claims, demands or judgments" should be read in the context of the overall intent of indemnification provisions: to provide contractual reimbursement to a party who paid damages due to the other contracting party's acts or omissions. By using the terms "liability claims, demands or judgments," the instant provision was contemplating claims made

against the city by third-parties due to the acts or omissions of AllianceOne in its collections activities.

If the court accepts Fidelity's arguments, it would be impossible to find any boundary to this indemnification provision. Fidelity asserts that there need not be any causal connection whatsoever between the act or omission and the loss, and there need not be any showing that the act or omission was in any manner wrongful. Under Fidelity's theory, an act or omission that is not actionable still gives rise to an indemnification claim. Fidelity's argument really is that this is not an indemnification provision, but an absolute guaranty.

The logic of Fidelity's argument would lead to absurdities. It would make AllianceOne liable if checks were deposited into the city's bank account, and the funds were then illegally electronically accessed and transferred by a thief. Fidelity would assert the indemnification provision applies because the funds in the bank arose out of AllianceOne's act of making payment. This is nothing different than the current allegations, whereby Fidelity claims AllianceOne is liable

because it paid by check, even though there is no liability otherwise for having done so.

Here, there was no claim by a third-party against the city. The claim is for the city's own loss for its own failures and the intentional criminal acts of Dally.

Fidelity was required to come forward with evidence showing that there were issues of fact on its indemnification claim. It was required to show that the loss arose out of the acts or omissions of AllianceOne. It did not, and cannot, make such a showing. The only acts or omissions alleged are the payee issue and the endorsement verification issue. Fidelity failed to show that there is liability under either scenario, or that the loss arose out of either set of factual contentions.

In this court and repeatedly in the trial court, Fidelity makes the argument that the city did nothing wrong. The indemnity provision excepts loss caused by the negligence of the city. As a matter of law, the uncontroverted evidence submitted proves the negligence of the city. The only evidence in this record is that the loss was caused by the city's negligence and the intentional acts of the city's employee, Dally. Dally's acts are

imputed to the city. The exception to the indemnity provision clearly applies.

Judge Hartman carefully, and liberally, construed the indemnity provision. He analyzed both the payee issue and the endorsement verification issue under the indemnification theory. He properly concluded that there was no evidence in the record to show that the loss arose out of the varied payee designations. He also concluded that Fidelity had failed to show there were any material issues of fact regarding the endorsement verification issue. The indemnity provision can only be fairly and properly construed to apply to conduct required under the contract or otherwise imposed by law. The contract did not require any specific payee designation, or endorsement verification, and Fidelity failed to show that the law otherwise imposed any duty on AllianceOne.

There were no reasonable inferences here to construe. As a matter of law, AllianceOne was entitled to dismissal.

**F. NO CAUSATION EXISTS UNDER ANY OF FIDELITY'S CAUSES OF ACTION**

Recovery under all three theories of liability requires a showing that damages resulted from the breach of contract, from the negligence or from the act or omission of AllianceOne. Fidelity presented no evidence of any causal link under any of these three causes of action.

Conspicuously absent from the Washington State Auditor's report is any mention that AllianceOne was responsible for the loss. Dally's actions, and the internal control weaknesses of the court were the only reason the theft occurred and went undetected for so long. With each pair of checks, AllianceOne provided the city with itemized statements. All someone at the city had to do was to check and see whether the payments referenced in the statements were actually deposited.

A defendant's negligence is a proximate cause of a plaintiff's injury only if such negligence "in a direct sequence, unbroken by any new independent cause, produces the injury complained of." *Hartley v. State*, 103 Wn.2d 768, 698 P.2d 77 (1985). Where the facts are undisputed and do not admit reasonable differences of opinion, causation is a question of law

for the court. *Baughn v. Honda Motor Co.*, 107 Wn.2d 127, 727 P.2d 655 (1986). Here, there is no direct sequence, unbroken by a new independent cause, between the alleged acts and omissions of AllianceOne and the loss. Dally's theft and the city's lack of financial controls were new independent causes of the loss.

Even if there was some fault on the part of AllianceOne, which is not the case, the city's complete failure to have financial controls over employees handling city funds was a superseding cause, preventing the imposition of liability against AllianceOne. *See, Smith v. Acme Paving Co.*, 16 Wn.App. 389, 558 P.2d 811 (1976). As a matter of law, it was not foreseeable to AllianceOne that (1) the city would have absolutely no controls in place to monitor employees handling the city's funds, and (2) that Dally would commit the criminal act of stealing from her employer.

As previously established, there is no duty to protect others from the criminal acts of third-parties absent a special relationship, which clearly did not exist. As a matter of law, causation does not exist.

Fidelity also was required to show that the alleged breach of contract caused its loss. It did not do so. There was no causal

connection between any act of AllianceOne under the contract and Dally's theft.

Finally, the indemnification provision requires a showing of causation. In order for an act or omission to cause a loss, the act or omission must have been, in some manner, wrongful or faulty. Otherwise, there would be a duty to indemnify for acts that are completely compliant with the contract and the law. However it is phrased, there must be a faulty or wrongful act or omission that gives rise to the loss; there must be a connection or the loss does not "arise out of" the act or omission. No evidence of either was submitted in response to the summary judgment motion.

#### **IV. CONCLUSION**

For over six and one-half years, Deborah Dally stole from the city. During that time, Fidelity accepted the city's insurance premium payments on a policy that provided coverage for a loss caused by a dishonest employee. It accepted the risks posed by the city and issued its policy apparently without investigating whether the city even had any controls in place to monitor employees handling funds. Because there were no such controls, Fidelity was

required to pay the city for Dally's theft. Now, it attempts to shift the loss onto AllianceOne by making specious arguments about the way checks were made payable, and that somehow there was a duty to review endorsements on negotiated checks.

Fidelity's response to AllianceOne's motion for summary judgment failed to submit admissible evidence establishing the existence of genuine issues of material fact. Appellant failed to meet its burden.

The trial court properly dismissed all claims against AllianceOne, with prejudice. Based on the foregoing, Respondent AllianceOne respectfully requests that this court affirm the trial court decision granting summary judgment.

**RESPECTFULLY SUBMITTED**, this 24<sup>th</sup> day of March, 2008.

**ALAN B. HUGHES, P.S.**

By:   
Alan B. Hughes, WSBA #14046  
Attorney for Respondent  
AllianceOne Receivables  
Management, Inc.

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COURT OF APPEALS, DIVISION II

STATE OF WASHINGTON

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FIDELITY AND DEPOSIT COMPANY OF MARYLAND,

Appellant,

v.

ALLIANCEONE RECEIVABLES MANAGEMENT, INC., a Delaware  
corporation, d/b/a ALLIED CREDIT and/or ALLIANCEONE, INC.,

Respondents,

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**CERTIFICATE OF SERVICE**

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ORIGINAL

**NANCY SCHWALIER** declares:

NANCY SCHWALIER, under penalty of perjury of the laws of the State of Washington, hereby declares as follows:

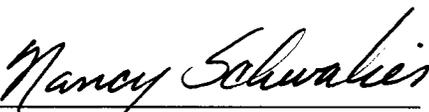
1. On March 24, 2008, I placed a true and correct copy of *Respondent's Court of Appeals Brief* this *Certificate of Service* via U.S. Mail, Postage Prepaid, and First Class for delivery to:

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Signed at Seattle, Washington, on March 24, 2008.

**ALAN B. HUGHES, P.S.**

By:   
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