12-15878-EE

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

FEDERAL DEPOSIT INSURANCE CORPORATION, AS RECEIVER OF INTEGRITY BANK OF ALPHARETTA, GEORGIA,

Plaintiff-Appellant,

v.

STEVEN M. SKOW, ALAN K. ARNOLD, DOUGLAS G. BALLARD, CLINTON M. DAY, JOSEPH J. ERNEST, DONALD C. HARTSFIELD, JACK S. MURPHY, AND GERALD O. REYNOLDS,

Defendants-Appellees.

On Interlocutory Appeal From The United States District Court For The Northern District Of Georgia in Case No. 11-cv-0111-SCJ

REPLY BRIEF FOR APPELLANT FDIC

KYLE M. KEEGAN
CHRIS D. KIESEL
Keegan, DeNicola, Kiesel,
Bagwell, Juban & Lowe, LLC
5555 Hilton Ave., Suite 205
Baton Rouge, Louisiana 70808
(225) 364-3600

COLLEEN J. BOLES
Assistant General Counsel
KATHRYN R. NORCROSS
Senior Counsel
MINODORA D. VANCEA
Counsel

FEDERAL DEPOSIT INSURANCE CORPORATION
3501 Fairfax Drive, VS-D7176
Arlington, VA 22226-3500
(703) 562-2049
mvancea@fdic.gov

Counsel for the Federal Deposit Insurance Corporation

Date: May 13, 2013

CERTIFICATE OF INTERESTED PERSONS AND CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1 and Circuit Rule 26.1-1, Appellant, Federal Deposit Insurance Corporation ("FDIC"), as Receiver of Integrity Bank of Alpharetta, Georgia, submits the following Certificate of Interested Persons and Corporate Disclosure Statement.

1. Interested Persons

The name of each person, attorney, association of persons, firm, law firm, partnership, and corporation that has or may have an interest in the outcome of this action including subsidiaries, conglomerates, affiliates, parent corporations, public-traded companies that own 10% or more of a party's stock and any other identifiable entities related to any party in this case are as follows:

Ambler, Robert R. - counsel for Appellee

Arnall Golden Gregory, LLP - counsel for Appellee

Arnold, Alan K. - Appellee

Bagwell, Dustin R. - counsel for FDIC, Appellant

Bailey Cavalieri, LLC - counsel for Cincinnati Insurance Company

Ballard, Douglas G. - Appellee

Balser, David L. - counsel for Appellee

Baxter, Jeffery. R - counsel for Appellee

Boles, Colleen J. - counsel for FDIC, Appellant

Brooks, Richard D. - counsel for Cincinnati Insurance Company

Carnes, Hon. Julie E. - Judge, U.S. District Court, Northern District of Georgia

Cincinnati Insurance Company - Third-party insurer

Cochran & Edwards, LLC - counsel for Appellee

Danzig, Aaron M. - counsel for Appellee

Day, Clinton M. - Appellee

Edwards, Richard R. - counsel for Appellee

Ernest, Joseph J. - Appellee

Federal Deposit Insurance Corporation, as Receiver of Integrity Bank - Appellant

Hartsfield, Donald C. - Appellee

Haskell, Slaughter, Young & Rediker - counsel for Appellee

Jones, Hon. Steve C. - Judge, U.S. District Court, Northern District of Georgia

Kandawalla, Darius - counsel for Cincinnati Insurance Company

Keegan, DeNicola, Kiesel, Bagwell, Juban & Lowe, LLC - counsel for FDIC, Appellant

Keegan, Kyle M. - counsel for FDIC, Appellant

Kiesel, Chris D. - counsel for FDIC, Appellant

King & Spalding LLP - counsel for Appellee

Klingler, Tracy - counsel for Appellee

Manley, James B. - counsel for Appellee

Marshall, Edward A. - counsel for Appellee

McKenna Long & Aldridge, LLP - counsel for Appellee

Mitchell, Richard A. - counsel for Appellee

Murphy, Jack S. – Appellee

Norcross, Kathryn R. – counsel for FDIC, Appellant

Reeves, T. Dylan - counsel for Appellee

Reynolds, Gerald O. - Appellee

Richmond, Lawrence J. - counsel for FDIC, Appellant

Simkins Hollis, Jeanne - counsel for FDIC, Appellant

Simkins Hollis Law Group, P.C. - counsel for FDIC, Appellant

Skow, Steven M. - Appellee

Smith, Kirk D. - counsel for Appellee

Vancea, Minodora D. - counsel for FDIC, Appellant

Watson, J. Scott - counsel for FDIC, Appellant

Young, Frank M. - counsel for Appellee

2. Corporate Disclosure

The Federal Deposit Insurance Corporation is a corporation established under 12 U.S.C. § 1811.

Date: May 13, 2013

Respectfully submitted,

/s/
Minodora D. Vancea
Counsel for the Federal Deposit Insurance Corporation, as Receiver of Integrity Bank

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"BJR" – the business judgment rule

"Br." – FDIC's Opening Appellate Brief

"CERCLA" – Comprehensive Environmental Response, Compensation, and Liability Act

"FDIC" – the Federal Deposit Insurance Corporation

"FIRREA" – the Financial Institutions Reform, Recovery, and Enforcement Act of 1989

"FTCA" – the Federal Tort Claims Act

"RedBr." – Defendants' Appellate Brief

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SUMMARY OF ARGUMENT

Defendants contend that the Georgia statute merely imposes a duty of ordinary diligence, but does not actually impose liability for the breach of that duty. That is nonsense. Under Georgia law, whenever there is a duty, there is liability for its breach. O.C.G.A. § 51-1-6.

The breach of the duty of ordinary care or diligence is defined, by statute, as "ordinary negligence." O.C.G.A. § 51-1-2. Notwithstanding that statutory ordinary negligence standard, Defendants urge that federalism requires this Court to follow two intermediate Georgia decisions that depart from statutory text. But the Georgia Supreme Court would never follow intermediate decisions that repeal the ordinary negligence standard imposed by the Georgia statute. Judicial repeal of a state statute is not federalism.

Defendants' appeal to the deference owed to the intermediate decisions' supposed "interpretation" of the statute similarly fails because if a statute is plain, as here, there is no place for judicial interpretation. When "the language of a statute is plain and unambiguous, judicial construction is not only unnecessary but forbidden." *Abdulkadir v. State*, 279 Ga. 122, 123, 610 S.E.2d 50, 52 (2005).

Defendants' arguments on the second issue presented fare no better. Defendants concede that the no-duty rule was well-established before FIRREA, and that it is the type of federal common law that continues to apply post-FIRREA.

Defendants argue only that the courts applying the no-duty rule to bar mitigation defenses somehow applied another doctrine. As shown below, that argument fails. The no-duty rule invalidates the failure-to-mitigate defense as the natural, necessary, and unavoidable result of the logic and policy behind the rule. The mitigation defense would also embroil courts in second-guessing FDIC's discretionary functions—an outcome forbidden by the statutory scheme, sovereign immunity (and the discretionary function exception), and constitutional separation-of-powers principles.

ARGUMENT

I. Bank Directors And Officers Are Liable For Ordinary Negligence Under Georgia Law

A. The Georgia Statutes Impose Liability For Ordinary Negligence On Bank Directors And Officers, And Neither Judicial Opinion Nor Legal Commentary Can Displace That Statutory Standard

As Defendants concede (RedBr.27), Georgia by statute requires bank directors and officers to act with ordinary care or diligence (O.C.G.A. § 7-1-490). By statute as well, the "absence of such diligence is termed ordinary negligence." O.C.G.A. § 51-1-2.

To avoid the plain and unambiguous language of O.C.G.A. § 7-1-490, Defendants propose that the statute merely imposes an ordinary diligence duty of care, but does not establish liability for the breach of that duty. RedBr.28. Defendants claim that this permits courts to set the standard for liability, such as by applying the business judgment rule ("BJR"). *Id*. Defendants are incorrect.

As a threshold matter, it is not true that O.C.G.A. § 7-1-490 itself fails to impose a standard of liability. It provides that defendants shall have "no liability" if they act (1) in good faith and (2) with ordinary diligence, the absence of which is statutorily defined as ordinary negligence. O.C.G.A. § 7-1-490(a). Georgia appellate courts have indicated that such statutory language imposes a standard of liability, not just a standard of care. *E.g.*, *Boddy v. Theiling*, 129 Ga. App. 273, 199 S.E.2d 379 (1973); *see* Br.24, 16-17.[1]

Even if O.C.G.A. § 7-1-490 did not itself impose liability for breaching the duty of care that O.C.G.A. § 7-1-490 establishes, another statutory provision does impose that liability. Specifically, O.C.G.A. § 51-1-6 imposes liability whenever there is a breach of *any* duty imposed by statute or other Georgia law: "When the law requires a person … to refrain from doing an act which may injure another, although no cause of action is given in express terms, *the injured party may recover for the breach of such legal duty* if he suffers damage thereby." O.C.G.A. § 51-1-6 (emphasis added). O.C.G.A. § 51-1-6 thus demonstrates that the standard for liability is no different than the standard of care—there always is attendant liability "for the breach" of any duty of care (if damage results). *Id*.

[1] "Br." denotes references to FDIC's opening brief, *see* Table of Abbreviations.

Defendants' theory also contravenes the "traditional" rule that if there is a duty, there is tort liability when that duty is breached. *Sutter v. Hutchings*, 254 Ga. 194, 196-197, 327 S.E.2d 716, 718 (1985) (abrogated on other grounds) (citing leading treatise). Indeed, it would make no sense for the legislature to provide a standard of care that could never be enforced because it did not match the standard for liability. The standard of care is meaningless if it has no teeth. Legislatures are not in the business of imposing meaningless, hortatory duties.

Defendants' constricted reading of O.C.G.A. § 7-1-490 is apparently informed by commentary by the Georgia State Bar. RedBr.28-29. Defendants point to cases where courts look to such commentary in interpreting statutes. RedBr.29. FDIC does not take issue with the unremarkable proposition that courts may look to commentary by practitioners and scholars. What courts cannot do, however, is rely on such commentary to hold that a statute does not mean what it plainly says. Legal commentary cannot modify the liability imposed by statute, as the legislature "alone is entrusted with the authority to amend existing laws." *Abdulkadir*, 279 Ga. at 124.

Defendants nevertheless contend that bank directors and officers are not liable for ordinary negligence (as the statute says they are), because two intermediate Georgia decisions, *Brock Built, LLC v. Blake*, 300 Ga. App. 816, 686 S.E. 2d 425 (2009), and *Flexible Products Co. v. Ervast*, 284 Ga. App. 178, 643 S.E.2d 560

(2007), have attempted to super-impose a court-created business judgment rule, which bars liability for ordinary negligence, on top of the statute. RedBr.20. But if *Brock Built* and *Flexible Products* stand for the proposition that Defendants advance, they would effectively repeal the ordinary negligence standard expressly set forth in O.C.G.A. § 7-1-490 and replace it with a bad faith or gross negligence standard of liability. That cannot be the law. The Georgia Supreme Court has clearly forbidden the courts from amending statutes through the creation of judicial rules. *Abdulkadir*, 279 Ga. at 124. The Georgia Supreme Court's own prohibition against judicial modification of statutory standards is persuasive evidence that it would not follow *Brock Built* and *Flexible Products*'s de facto repeal of the applicable statutory standard. *See* Part I.B., *infra*.

In any event, when read in context, *Brock Built* and *Flexible Products* do not stand for the proposition that bank directors can never be liable for ordinary negligence. *See* Br.34-37. As another Georgia intermediate decision explained in rejecting the theory that a director is only liable for bad faith, "[c]iting *Flexible Products Co. v. Ervast*, the wife argues that the standard of care is not ordinary diligence and that an officer need only act in good faith to avoid liability…. This is inaccurate." *Rosenfeld v. Rosenfeld*, 286 Ga. App. 61, 68-69; 648 S.E.2d 399, 406 (2007) (physical precedent only). "OCGA § 14-2-842(a), which governs, requires that to avoid liability, an officer must act in good faith … and with …. ordinary diligence …. *Flexible Products*, *supra*, is distinguishable on its facts and is inapplicable." *Id*. Defendants complain that FDIC has not explained why *Flexible Products* "is distinguishable on its facts" (RedBr.24), but FDIC was merely citing what the appellate panel in *Rosenfeld* held—a panel that included the judge who wrote *Brock Built*, who concurred in full with *Rosenfeld*'s reasoning.

Defendants also plead for the application of inapposite Delaware law. But that effort to displace the plain language of the Georgia statute serves only to highlight the weakness of Defendants' position under Georgia law. Attempting to illustrate how differing standards of care and liability can coexist, Defendants argue that like Georgia, Delaware has an ordinary diligence standard of care for directors and officers, yet bars liability for their ordinary negligence. RedBr.28. But Defendants ignore the obvious distinction: *There is no statute in Delaware* setting forth the applicable standard of care for directors and officers. Thus, insofar as a Delaware court might apply the BJR to foreclose liability of corporate directors for ordinary negligence, it does not do so in contravention of a clear legislative directive. Georgia courts do not have that luxury: They are bound by the statute.

Because of that, this Court rejected application of Delaware law in circumstances like those here: Even if Florida courts, like Georgia courts, often look to Delaware law for guidance, substituting the Delaware standard for Florida's statutory standard would be contrary to the plain words of a Florida statute—a statute identical to the one at issue here. *FDIC v. Stahl*, 89 F.3d 1510, 1518 n.14 (11th Cir. 1996). *Stahl* therefore fully refutes Defendants' argument that Georgia's Supreme Court would mimic Delaware courts on this issue. RedBr.5-7. Defendants' reliance on *Cottle v. Storer Commc'ns*[2] and *Int'l Ins. Co. v. Johns*[3] (RedBr.33), two cases in which this Court relied on Delaware law, is misplaced for the same reason. Neither this Court nor Georgia courts can use Delaware law to effect a *de facto* repeal of Georgia statutes.

B. Compelling Evidence Demonstrates That The Georgia Supreme Court Would Not Adopt Defendants' Proposed Reading Of The Business Judgment Rule

Even if *Brock Built* and *Flexible Products* held that directors can *never* be liable for ordinary negligence—and they do not—this Court should decline to follow them. Where the Georgia Supreme Court has not spoken on an issue, this Court must predict how that court would decide the issue. "[F]ederal authority may not be bound even by an intermediate state appellate court ruling" if the federal court "is convinced by other persuasive data that the highest court of the state would decide otherwise." *C.I.R. v. Bosch's Estate*, 387 U.S. 456, 465 (1967). Defendants concede this principle (RedBr.26), arguing only that FDIC "has identified no such 'persuasive evidence.'" *Id.* That is mere wishful thinking. The plain language of the statute, prior Georgia Supreme Court decisions, other intermediate Georgia ap-

[2] 849 F.2d 570, 575 (11th Cir. 1988).

[3] 874 F.2d 1447, 1461 (11th Cir. 1989).

pellate decisions, and the decisions of *every* court to consider a similar statute in other States (including a decision of this Court) are more than persuasive. They are compelling.

1. As discussed above, the plain and unambiguous language of O.C.G.A. § 7-1-490 is persuasive—indeed, decisive—evidence that the Georgia Supreme Court would not adopt Defendant's desired rule. The Georgia Supreme Court itself has repeatedly held that no court can create judicial rules that modify the standards imposed by statute. *See Abdulkadir*, 279 Ga. at 124; *see also* Br.22 (collecting cases). There could hardly be anything more persuasive than the Georgia Supreme Court's *own* decisions prohibiting judicial modification of statutory standards to show that *Brock Built* and *Flexible Products*'s repeal of the statutory ordinary negligence standard is improper and would not be followed by that Court.

2. The analysis could end there, but there is more. For example, the Georgia Supreme Court itself long ago spoke to the proper standard of liability for bank directors. *Woodward v. Stewart*, 149 Ga. 620, 101 S.E. 749 (1919), and *McEwen v. Kelly*, 140 Ga. 720, 79 S.E. 777 (1913), describe the standard of care and of liability as ordinary negligence, and expressly reject decisions holding that directors are "only" liable for gross negligence. Br.26-28.

Defendants claim that these decisions are outdated. As FDIC noted, however, in *Boddy*, 129 Ga. App. at 276, the Georgia Court of Appeals held that these decisions form the basis for the *current* governing standard imposed by the statute—ordinary negligence. Br.17. Defendants have no answer to *Boddy*. Defendants' further attempt to characterize the relevant language in *Woodward* and *McEwan* as *dicta* is beside the point: Whether *dicta* or not, that language—expressing the views of the Georgia Supreme Court and showing disagreement with a gross-negligence standard—is persuasive evidence that the court would not adopt that standard.

In any event, the Georgia Supreme Court's later holding, premised *McEwen*, that "directors are personally liable for the losses" that "ordinary care on their part would have prevented" is certainly not *dicta*. *Shannon v. Mobley*, 166 Ga. 430, 143 S.E. 582, 585 (1928).[4] *Shannon* plainly states an ordinary negligence standard.

3. Two intermediate Georgia decisions provide further persuasive evidence that the Georgia Supreme Court would not adopt Defendants' rule. Both *Boddy*, 129 Ga. App. 273, and *Rosenfeld*, 286 Ga. App. 61, indicate that the proper standard of liability for corporate officers and directors is ordinary negligence. *See* Br.24, 29-30. As discussed previously, *Rosenfeld* rejected the idea that an officer

[4] *Shannon* and *Atherton v. Anderson*, 99 F.2d 883 (6th Cir. 1938), both of which relied on *Briggs v. Spaulding*, 141 U.S. 132 (1891), to impose liability for *ordinary* negligence, further refute Defendants' suggestion that the out-of-context reference in *Briggs* to "gross inattention," which was quoted in *McEwen* and *Woodward*, was meant to suggest a standard other than ordinary negligence.

or director can be liable only for bad faith, not for ordinary negligence. Defendants dismiss *Rosenfeld* as only physical precedent, but that does not mean that the Georgia Supreme Court would not find its reasoning *persuasive*—especially when *Rosenfeld* tracks the plain language of the statute, while *Brock Built* and *Flexible Products* undertake no actual analysis of the statute. *See Augusta Iron & Steel Works, Inc. v. U.S. Fidelity & Guar. Co.*, 790 F.2d 852, 852 (11th Cir. 1986) (finding that physical precedent is "persuasive"). At the very least, *Boddy* and *Rosenfeld* prove that Defendants' proposed rule is neither the unanimous nor even the majority view among Georgia appellate courts that have considered director liability.

4. Lastly—but by no means least—decisions of numerous federal circuit courts and state supreme courts, including this Court in *Stahl*, holding that similar statutes impose an ordinary negligence standard of liability are further persuasive evidence that Defendants' reading of *Brock Built* and *Flexible Products* is contrary to the plain words of the Georgia statute, and thus would not be adopted by the Georgia Supreme Court. Br.31 (citing cases). As this Court explained, courts cannot create judicial rules that modify statutory standards—in particular, courts cannot adopt a BJR that "elevates the simple negligence standard [imposed by a similar statute] to one of gross negligence." *Stahl*, 89 F.3d at 1517-18.

Defendants dismiss *Stahl* and other cases to the same effect, arguing that the Georgia Supreme Court would follow *Brock Built* and *Flexible Products*' "interpretation" of the statute, not the holdings of "foreign" courts. RedBr.17, 25, 29. But *Brock Built* and *Flexible Products* did not actually provide an "interpretation" of the statute—they *de facto* repealed it. Neither case interpreted or provided any analysis of the statute; they instead proceeded under the misguided assumption that the BJR controls (*see* RedBr.27), ignoring the fundamental principle, recognized in Georgia and elsewhere, that such court-created rules cannot modify statutory standards. *Abdulkadir*, 279 Ga. at 124. Moreover, if a statute is plain, as here, judicial interpretation is "unnecessary" and "forbidden." *Abdulkadir*, 279 Ga. at 123; *see also Frazier v. Southern R. Co.*, 200 Ga. 590, 593, 37 S.E.2d 774 (1946) ("courts may not substitute by judicial interpretation language of their own for the clear, unambiguous language of the statute."). Thus, there is no "interpretation" to which this Court could defer. Finally, calling the business judgment rule a "standard of review" (RedBr. at 27) does not erase the fact that it is a judicial rule, and thus cannot convert a statutory ordinary negligence standard into gross negligence.

C. As This Court Explained, Applying The Statutory Ordinary Negligence Standard Will Not Render The BJR Meaningless

Defendants and their *amici* argue that holding directors liable for ordinary negligence would render the BJR "meaningless," harming corporate governance.

RedBr.34-36. But those policy arguments are for the Georgia legislature—not this Court—and the legislature has already imposed an ordinary negligence standard.

In any event, this Court and others have already rejected Defendants' argument, holding that an ordinary negligence standard does not deprive directors of the protections of the BJR. As this Court explained, there is "no conflict" between ordinary negligence and the BJR because, "[w]hen courts say that they will not interfere in matters of business judgment, it is presupposed that judgment—reasonable diligence—has in fact been exercised." *Stahl*, 89 F.3d at 1517.

A director "cannot close his eyes to what is going on about him … and have it said that he is exercising business judgment." *Id.* Similarly, as FDIC explained, there is no judgment in making objective errors such as saying that two plus two equals three, or choosing a course of action that reasonable bank directors would not take—*e.g.*, actions that, as here, violate underwriting standards, the bank's loan policies, or banking regulations.[5] Defendants fail to explain how such non-discretionary actions involve the use of "judgment." Thus, "[d]espite the defendant directors' arguments that they were shielded by the business judgment rule," there is no violation of the BJR when a court "determine[s] that, at the time the

[5] Defendants' suggestion that FDIC's interpretation of ordinary negligence is akin to gross negligence is mistaken. RedBr.35. Negligent actions are actions which attentive, reasonably prudent directors would not take, whereas, as Defendants concede, grossly negligent actions are those which even "inattentive" directors would not take.

loans were made, a reasonably prudent director would not have approved such transactions." *FDIC v. Bierman*, 2 F.3d 1424, 1434 (7th Cir. 1993) (affirming damages award against directors for ordinary negligence).

Moreover, it bears reemphasizing that there is no Georgia case applying the BJR to bank directors. *Brock Built* and *Flexible Products* do not involve bank directors. *McEwen*, *Woodward*, and *Shannon* do, and they apply an ordinary negligence standard to bank directors.

There are good reasons why the law treats a bank and its directors differently than private corporations. For example, under the Georgia banking code, the directors take a sworn oath that they will diligently and honestly administer the affairs of the bank. O.C.G.A. § 7-1-484. Directors of private corporations do not. And many bank directors do not merely supervise officers as in private corporations, but actively manage the bank by participating in the lending decisions made by the lending committee.

Differences between bank directors and directors of ordinary corporations also show why none of policy justifications Defendants proffer in support of eliminating ordinary negligence liability (via the BJR) apply to bank directors. The first justification, that courts lack "competence" to second-guess issues which involve business judgment or discretion (RedBr.9), does not apply where, as here, there is no use of judgment or discretion in the first place. Bank directors and officers have less discretion in their actions than their counterparts at ordinary corporations, because their actions are constrained and guided by many statutes, rules, regulations, internal bank policies and industry-wide underwriting standards, etc. Following these objective standards often involves no use of judgment as they allow only one course of action, namely, following these standards. Thus, allowing ordinary negligence claims based on the directors' failure to comply with such policies and standards does not amount to second guessing the directors' business judgment, as there is no exercise of judgment involved in the first place.

The second justification, that "shareholders … don't want … directors to be risk averse" (RedBr.9-10) does not apply to banks, because the rules applicable to bank governance do not take into account solely the interests of shareholders, but also—and primarily so—the interests of depositors. *Atherton*, 99 F.2d at 888 (a "bank is not a private corporation in which stockholders *alone* are interested," but a "quasi governmental agency" whose "principal purpose[] … is to hold and safekeep the money of its depositors"). *Id*. Depositors certainly want bank directors to be as risk-averse as reasonable prudence requires, so as to safeguard their deposits.

Beside the interests of depositors, the rules applicable to bank governance also take into account the public's need to prevent systemic risk, as well as the interests of regulators and deposit insurance. The Georgia Supreme Court recognized as much almost a century ago in imposing liability for ordinary negligence.

Shannon, 143 S.E.at 585 ("[i]f the qualities of integrity, diligence, and loyalty are required in any institution more than in others, it would seem to be in banking institutions" because of the special need to protect depositors and prevent systemic risk, since "[t]he commerce of the world rests largely upon confidence in banking corporations"). Thus, the BJR's premise that "shareholders can diversify the risks of their corporate investments" (RedBr.9-10) does not apply to banks given that the diversification of the *risk to shareholders* does nothing to prevent the *risk to the financial system* deriving from bank failure.

The courts' solicitude for the interests of depositors helps explain why the law imposes enhanced liability on bank directors and officers, and why, regardless of the standard that applies to ordinary directors, courts have awarded damages against bank directors for ordinary negligence. *See, e.g.*, *Bierman*, 2 F.3d at 1434; *Atherton*, 99 F.2d 883; *Hoye v. Meek*, 795 F.2d 893 (10th Cir. 1986); *Rankin v. Cooper*, 149 F. 1010 (C.C.W.D. Ark. 1907).

II. Defendants' Mitigation Defense Is Barred By Federal Law

Defendants' mitigation defense is barred. The no-duty rule clearly forecloses affirmative defenses, like those asserted here, that would enrich bank directors at the expense of the public. The defense would also invite impermissible judicial second-guessing of FDIC's undisputed discretion over how best to liquidate the assets of a failed depository institution.

A. The No-Duty Rule Bars Defendants' Mitigation Defense

Defendants first argue that under *O'Melveny & Myers v. FDIC*, 512 U.S. 79 (1994), "state law, not federal common law applies where no provision of FIRREA governs." RedBr.39-42. This argument is easily disposed of, given that this en banc court has twice held the opposite after considering *O'Melveny*. *See* Br.37-38, *Motorcity of Jacksonville, Ltd. v. Southeast Bank, N.A.* (*Motorcity I*), 83 F.3d 1317, 1330 (11th Cir. 1996) (en banc); *Motorcity II*, 120 F.3d 1140, 1144 (11th Cir. 1997) (en banc).

Under *Motorcity*, federal common law, not state law, applies, even if no specific provision of FIRREA governs, as long as that federal common law predated FIRREA. The only question that remains here is whether the federal common-law no-duty rule predated FIRREA. *See* R.E. 139 at 33. As shown below, it did.

1. The Reasoning And Operation Of The No-Duty Rule Require Its Application To The Defense Of Mitigation

Defendants concede—as they must—that the no-duty rule is a longstanding and well-established rule of federal common law that survived *O'Melveny*. *See* RedBr.44 (admitting that the rule has "been the law for almost a century" and that this makes the no-duty rule the type of preexisting federal common-law doctrine that *Motorcity* "contemplates"). Defendants' sole argument on appeal is that a bank director's mitigation defense against FDIC somehow does not fall within the scope of the no-duty rule. RedBr.44,50.

Nothing could be further from the truth. Each of the federal courts of appeals striking mitigation (and similar) defenses against FDIC explicitly relied on the language of the no-duty rule. *See Bierman*, 2 F.3d at 1438 ("failure to mitigate [defenses] may not be maintained against the FDIC in its receivership capacity because *no duty is owed* to the directors and officers") (emphasis added); *FDIC v. Oldenburg*, 38 F.3d 1119, 1121 (10th Cir. 1995) (agreeing that "FDIC [as receiver] *owes no duty* to the failed [bank] or to the wrongdoers who contributed to its failure, but rather to the public at large") (emphases added); *FDIC v. Mijalis*, 15 F.3d 1314, 1324 (5th Cir. 1994) (mitigation defense should be invalidated "because *the FDIC owes no duty* to failed financial institutions or their former directors and officers") (emphasis added).

In striking such mitigation defenses, moreover, the pre-FIRREA courts explained that they were applying the no-duty rule at issue in *First State Bank of Hudson Cnty. v. United States*, 599 F.2d 558 (3d Cir. 1979) and *Harmsen v. Smith*, 586 F.2d 156 (9th Cir. 1978)—two longstanding cases that Defendants admit are at the core of the no-duty doctrine. *See FDIC v. Carlson*, 698 F. Supp. 178, 179 (D. Minn. 1988) (citing *Harmsen* and *First State Bank*); *FDIC v. Greenwood*, 719 F.Supp. 749, 751 (C.D. Ill. 1989) (same); *FSLIC v. Roy*, 1998 WL 96570, at *1 n.2 (D. Md. 1998) (same). *Bierman*, *Mijalis*, and *Oldenburg*, in turn, adopt the reasoning of *Roy*, *Carlson*, and *Greenwood*.

The cases barring mitigation defenses against FDIC thus demonstrate that FDIC is not asking for a new "proposed rule" (RedBr.42), but the straightforward application of the *existing* no-duty rule to mitigation defenses. Indeed, judicial decisions have repeatedly demonstrated that the logic and policy of the no-duty rule *require* its application to affirmative defenses such as mitigation and contributory negligence. As explained in *First State Bank* and *Harmsen*, the logic behind the no-duty rule is that "the FDIC's purpose is to stabilize the banking industry and promote public confidence in banks and that, therefore, its duty is to the general public not individual banks, directors or officers." *Carlson*, 698 F.Supp at 179. This logic applies with equal force to mitigation defenses asserted against FDIC-receiver, because FDIC as receiver also is a banking agency that serves to promote "the goal of a stable banking system," and its duty is to the general public and not individual banks, directors or officers. *Id*.

Because "it is the public which is the intended beneficiary of [FDIC as receiver], …. nothing could be more paradoxical or contrary to sound policy than to hold that it is the public which must bear the risk of errors of judgment made by its officials in attempting to save a failing institution—a risk which would never have been created but for the defendants' wrongdoing in the first instance." *Bierman*, 2 F.3d at 1438 (quoting *Roy*, 1998 WL 96570). The no-duty rule requires that directors of failed banks, and not the public, bear the risk of any decisions that FDIC might make in salvaging and liquidating the assets of the failed institution. *Id*.

As these cases demonstrate, there is nothing new or different in applying the no-duty rule, which, as Defendants concede, precludes judicial interference with decisions of banking agencies tasked with protecting "the integrity of the banking system and the public good" (RedBr.44) to yet another set of banking agency decisions taken in pursuit of the same goal.

Relying on out-of-state authorities, Defendants attempt to confuse the issue by arguing that the mitigation defense does not technically involve any "duty" at all. RedBr.43-46. Defendants cite *FDIC v. Ashley*, 749 F. Supp. 1065, 1068-69 (D. Kan. 1990), for the proposition that "the legal requirement to mitigate damages is not actually a 'duty,' but a limitation on the amount of damages recoverable by the plaintiff." RedBr.45. However, "*Ashley* is based on Kansas law, which does not include duty as an element of failure to mitigate. [Georgia] law, on the contrary, does include the element of duty." *RTC v. Greenwood*, 798 F. Supp. 1391, 1397-98 (D. Minn. 1992). By statute, Georgia expressly imposes a "duty to mitigate." O.C.G.A. § 51-12-11 ("When a person is injured by the negligence of another, he *must mitigate* his damages as far as is practicable by the use of ordinary care and diligence. However, *this duty to mitigate* does not apply in cases of positive and continuous torts.") (emphases added). In fact, Defendants themselves cite a Georgia case discussing this very "duty to lessen damages." RedBr.45-46 (citing *Butler v. Anderson*, 163 Ga. App. 547 (1982)). Defendants have cited no Georgia authority to the contrary.

Defendants' citation of *Butler* for the proposition that the duty to mitigate is not a duty "owed to another party at all" (RedBr.45) is misplaced, as *Butler* nowhere says that. *Butler*'s mere reference to the "general duty" to mitigate nowhere implies that such duty is not owed to other persons. Moreover, Defendants' idea that the duty is not owed to other persons defies general principles of tort law. Whether the precise identity of those persons might not be known ex ante, duties are owed to persons, not to ether: "a person owes *to others a duty* not to subject them to an unreasonable risk of harm." *Sutter*, 254 Ga. at 197 (emphasis added; abrogated on other grounds).

Ultimately, the salient point is not whether the Defendants' failure-to-mitigate defense implicates a duty owed by FDIC to bank directors or some inchoate "general duty" not "owed to another party." RedBr.45. The mitigation defense, if successful, would obviously confer a financial benefit on the directors at the expense of depositors and the public—the ultimate beneficiaries of FDIC's action. As *Bierman* explains, the no-duty rule requires that directors of failed banks, and not the public, bear the risk of any decisions that FDIC might make in salvaging and liquidating the assets of the failed institution. 2 F.3d at 1438. Yet mitigation would disrupt that prudent allocation of risk. The no-duty rule is necessarily incompatible with the defense of mitigation under Georgia law.

2. The No-Duty Rule Applies Whether FDIC Acts As Plaintiff Or Defendant

Defendants next argue that since most pre-FIRREA no-duty cases involved FDIC as defendant, applying the no-duty rule to protect FDIC as plaintiff somehow creates a different rule. RedBr.50-52. Not so.

As an initial matter, the procedural posture in which a doctrine is asserted does not change the name and nature of the doctrine. For example, both plaintiffs and defendants can rely on estoppel, laches, unjust enrichment, breach of contract, etc. Courts do not speak of a different *D'Oench* doctrine when it is asserted by FDIC as a plaintiff rather than defendant. The doctrine applies with equal force in either case. *See Motorcity II*, 120 F.3d at 1142-45 (applying *D'Oench* to FDIC as defendant); *D'Oench, Duhme & Co. v. FDIC*, 315 U.S. 447 (1942) (applying doctrine to FDIC as plaintiff).

The fact that the *D'Oench* doctrine bars state law defenses even when FDIC is a plaintiff refutes Defendants' contention that FDIC becomes subject to all possible state law defenses whenever it elects to sue under state law. *D'Oench* thus demonstrates that contrary to Defendants' assertions, the law does not require FDIC to play by the "same rules" as all other tort plaintiffs when it elects to sue under state law. RedBr.52. As the Supreme Court explained in rejecting similar arguments for treating government agencies the same as private tort parties, such "equal treatment" arguments largely miss the crucial point that "sovereign immunity places the Federal Government on an entirely different footing than private parties." *Lane v. Pena*, 518 U.S. 187, 196-97 (1996).

The four cases cited by Defendants that allowed litigants to assert affirmative defenses in recoupment when sued by the United States (RedBr.51) do not require a different result. This is so for several reasons:

First, the premise on which Defendants' recoupment cases rely—that the government impliedly waives sovereign immunity by filing suit—is no longer good law. The Supreme Court has since held that a waiver of sovereign immunity "must be unequivocally *expressed in statutory text* … and will not be implied." *Lane*, 518 U.S. at 192 (emphasis added).

Second, the text and structure of the FTCA also defy an implied waiver theory. While the FTCA expressly exempts counterclaims from specific procedural prerequisites applicable to the waiver of sovereign immunity (*e.g.*, exhaustion of administrative remedies, 28 U.S.C. § 2675(a)), there is nothing in the FTCA to support the conclusion that its substantive provisions, including the discretionary function exception, 28 U.S.C. § 2680(a), do not apply to counterclaims and affirmative defenses. There would have been no need for the express exemptions from procedural prerequisites for counterclaims if it were possible to imply waiver simply because a governmental entity filed suit.

Third, the Supreme Court has emphasized that the recoupment doctrine on which Defendants rely is narrow, and its application now appears limited to tax cases. *United States v. Dalm*, 494 U.S. 596, 602, 608 (1990); *see also United States v. Nordic Village, Inc.*, 503 U.S. 30, 38-40 (1992) (recognizing that *Dalm* "substantially narrowed" recoupment doctrine). *See generally United States v. Iron Mountain Mines, Inc.*, 881 F.Supp. 1432, 1452-57 (E.D. Cal. 1995) (providing a detailed analysis of this issue). These authorities call into question the recoupment cases Defendants cite and, unsurprisingly, courts have refused to continue to apply that outdated precedent. *See, e.g.*, *Iron Mountain*, 881 F.Supp. at 1452-57 (recoupment defenses do not apply in CERCLA context); *United States v. Green*, 33 F.Supp. 2d 203, 224 n.8 (W.D.N.Y. 1998) (explaining that, following *Dalm*, the implied waiver for recoupment is limited to tax enforcement cases).

Fourth, none of the four cases that Defendants cite involved the discretionary function exception. As explained in Section II.B, *infra*, Defendants challenge FDIC's exercise of discretionary functions, which are not open to second-guessing by the courts. Whether or not there is an implied waiver of sovereign immunity for recoupment defenses, there is no waiver of sovereign immunity for discretionary conduct, even if the government initiates suit. Numerous cases so hold, and Defendants have been unable to find any cases to the contrary. In particular, several cases have barred mitigation and other recoupment defenses because they would interfere with the government's discretionary functions. *U.S. v. Sierra Pacific Indus.*, 879 F.Supp.2d 1128, 1136-37 (E.D. Cal. 2012) (barring mitigation defense); *Grijalva v. Superior Court*, 159 Cal. App. 4th 1072 (2008) (barring mitigation defense and rejecting argument that "there is a difference between suing the government and defending against it"); *see also FDIC v. Carter*, 701 F.Supp. 730, 734-35 (C.D. Cal. 1987) (discretionary function exception "appl[ies] both to affirmative suits brought against the government and to counterclaims and affirmative defenses in suits brought originally by the government"); *United States v. Amtreco, Inc.*, 790 F.Supp. 1576, 1583 (M.D. Ga. 1992) ("even though defendants' counterclaims are recoupment claims, they are outside the court's subject matter jurisdiction" because judicial review of discretionary agency conduct violates "the doctrine of separation of powers").

B. Sovereign Immunity And Constitutional Separation-of-Powers Principles Bar Mitigation Defenses Challenging FDIC's Performance Of Discretionary Functions

As FDIC explained, Defendants' proposed mitigation defense is barred because "[t]he discretionary exception to the FTCA … would prevent the assertion of affirmative defenses against the FDIC." *Bierman*, 2 F.3d at 1441; Br.48, 51-52. The FTCA insulates government actors from tort liability for acts or omissions "based upon the exercise or performance or the failure to exercise or perform a discretionary function or duty." 28 U.S.C. § 2680(a). As numerous courts have recognized, it is beyond debate that FDIC's decisions regarding how best to liquidate the assets of a failed banking institution involve such discretionary functions protected from judicial second-guessing. *See Bierman*, 2 F.3d at 1441 ("we think it clear that the FDIC was performing a discretionary function" because of "[t]he responsibilities that devolve onto the FDIC when a bank has failed require quick and complex decision-making"); *Mijalis*, 15 F.3d at 1324; *Oldenburg*, 38 F.3d at 1121; 12 U.S.C. § 1821(d) (granting discretion); Br.51. Indeed, Defendants' brief does not dispute that the actions taken by FDIC as receiver constitute discretionary decisionmaking.

Defendants nonetheless argue that "FDIC's concern about judicial second-guessing of its discretionary decisions is vastly overblown." RedBr.53. But it is Defendants who underestimate the effect of judicial interference with the agency's performance of discretionary functions. According to Defendants, all that a court would assess in applying the defense of mitigation here is whether FDIC's conduct in disposing of the assets of a failed institution was "reasonable." RedBr.53. If certain mitigation measures are unreasonable or impracticable, no court would fault FDIC for not taking them. *Id*. That argument "misunderstands both the purpose of sovereign immunity and the nature of the affirmative defenses at issue."

Grijalva, 159 Cal.App.15 4th at 1078. Requiring courts to determine whether the government's discretionary conduct was reasonable or unreasonable is "precisely" what governmental immunity was meant to prevent. *Id*.; *see also United States v. Gaubert*, 499 U.S. 315, 323 (1991) (discretionary actions are protected from judicial review "even if those particular actions were negligent"); *Wegoland Ltd. v. NYNEX Corp.*, 27 F.3d 17, 21 (2d Cir. 1994) ("[I]t is this judicial determination of a *reasonable* rate that the … doctrine forbids.") (emphasis added).

Congress's command that FDIC's discretionary decisions not be second-guessed in the context of tort suits applies with equal vigor whether the attack is by way of a claim or affirmative defense. First, in either case, the litigant seeks a financial benefit by attacking the agency's discretionary conduct. Whether the compensation owed to the agency is reduced by way of an affirmative defense or by the agency's payment on a claim makes no ultimate difference; the agency's coffers suffer in either case.

Second, whether the attack is asserted by claim or defense, courts remain equally ill-suited to review (and, as shown below, are in fact are constitutionally prohibited from reviewing) such discretionary conduct. Courts are no better equipped or constitutionally permitted to review discretionary functions whether the attack on discretionary conduct is by an affirmative defense than by a claim. There is nothing talismanic about affirmative defenses that would suddenly let courts develop an expertise that they lack. Whether an agency is a plaintiff or defendant, "[a]s compared with the [agency's] expertise, courts do not approach the same level of institutional competence" in a field within the agency's domain. *Wegoland*, 27 F.3d at 21.

Third, Defendants ignore the fact that the discretionary-function exception is rooted in constitutional principles. Virtually all circuit courts, including this Court, have held that because the Constitution's separation-of-powers requirement precludes judicial review for claims or defenses challenging an agency's discretionary conduct, there is no need for a statutory codification of the discretionary function exception, and thus the discretionary function exception applies even to statutes such as the Suits in Admiralty Act that do not codify such exception. *See Wiggins v. United States*, 799 F.2d 962, 966 (5th Cir. 1986) (collecting cases).

As the leading case of *Canadian Transport Co. v. United States* explained, the "history of the FTCA suggests that the exemption for discretionary functions in that Act was derived from the doctrine of separation of powers, a doctrine to which the courts must adhere even in the absence of an explicit statutory command." 663 F.2d 1081, 1085-86 (D.C.Cir.1980). This Court endorsed this reasoning in *Williams v. United States*, 747 F.2d 700 (11th Cir. 1984), where it affirmed and adopted in full the district court's decision applying *Canadian Transport*. 581 F.Supp. 847, 852 (S.D. Ga. 1993).

Thus, regardless of whether the federal common-law no-duty rule was well-established before FIRREA, Defendants' mitigation defense would still be barred by federal law—the U.S. Constitution. This is because the principle on which the no-duty rule is based—the discretionary function exception or more precisely the idea "that every separate act of the [] receiver in collecting assets is not open to [judicial] second guessing" (*Bierman*, 2 F.3d at 1438)—is in fact constitutionally required by the separation-of-powers doctrine.

Indeed, this Court's expression of the separation-of-powers doctrine in *Williams* precludes any judicial review of discretionary decisions, even if the government *initiates* suit. *Amtreco*, 790 F.Supp. at 1583 (barring recoupment arguments based on *Williams*). This is because whether or not sovereign immunity could be waived by statute, the separation-of-powers requirement cannot be waived because it pertains to the federal courts' subject-matter jurisdiction under Article III. *See Allen v. Wright*, 468 U.S. 737, 750, 752 (1984) (Article III's "'case or controversy' requirement defines with respect to the Judicial Branch the idea of separation of powers on which the Federal Government is founded"; "the law of Art. III standing is built on a single basic idea—the idea of separation of powers").

Thus, the government's initiation of a suit cannot confer jurisdiction on courts over a subject matter that the separation-of-powers doctrine has taken away from them. It is well-known that parties cannot confer subject matter jurisdiction on courts by agreement, waiver, or by filing suit.

Finally, several aspects of FDIC's decision-making process further highlight the impropriety of judicial review of FDIC's "reasonable" mitigation measures. For example, unlike Georgia's duty to mitigate, FIRREA does not require FDIC to minimize losses on *each individual* asset such as the Loss Loans at issue in this litigation. The statute only requires FDIC to minimize *overall* losses in a particular receivership. 12 U.S.C. § 1821 (d)(13)(E). Mitigating losses on individual assets such as the Loss Loans at issue here could impede FDIC's ability to maximize value for all assets in the aggregate because as FDIC explained, what price is better for the part (here the Loss Loans) is not necessarily better for the whole (here, the entire receivership). Imposing a duty to mitigate losses on *individual* loans would thus interfere with FDIC's ability to do aggregate sales of loans, including through purchase and assumption transactions that have helped safeguard the stability of the banking system for decades. Defendants have no answer to this argument. Moreover, value maximization is only one of the considerations that Congress charged FDIC with balancing. For example, the same statutory provision that requires FDIC to maximize value also requires FDIC to ensure that the sale of the failed bank's assets "maximizes the preservation of the availability and affordability of residential real property for low- and moderate-income individuals." 12 U.S.C. § 1821 (d)(13)(E). FDIC balances these and many other factors in deciding what prices to accept, and when and how to structure the sale of a bank's assets. Those discretionary decisions should be left undisturbed.

* * *

To be sure, application of the discretionary function exception or of the separation-of-powers doctrine, "by its very nature, will leave a person [who might have been] wronged by Government conduct without recourse." *United States v. Bein*, 214 F.3d 408, 413 (3d Cir. 2000). By requiring separation of powers, however, the Framers have deemed the harm that would result from judicial interference with discretionary government decisions the worse evil. *See Wiggins*, 799 F. 2d at 966 (noting the "disrupting and overbearing prospect" of judicial second-guessing of discretionary government conduct).

CONCLUSION

For the foregoing reasons, the district court's rulings on the questions presented should be reversed.

Respectfully submitted,

COLLEEN J. BOLES
Assistant General Counsel
KATHRYN R. NORCROSS
Senior Counsel
J. SCOTT WATSON
Counsel

/s/ Minodora D. Vancea
Minodora D. Vancea
Counsel
Federal Deposit Insurance Corporation
3501 Fairfax Drive, VS-D7176
Arlington, VA 22226-3500
(703) 562-2049

KYLE M. KEEGAN,
CHRIS D. KIESEL
Keegan, DeNicola, Kiesel,
Bagwell, Juban & Lowe, LLC
5555 Hilton Ave., Suite 205
Baton Rouge, Louisiana 70808
(225) 364-3600

Attorneys for FDIC

CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B). This brief contains 6,980 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii) and Fed. Cir. R. 32(b). Microsoft Word 2003 was used to calculate the word count.

This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6). This brief has been prepared in a proportionally spaced typeface using Microsoft Word 2003 in 14-point, Times New Roman font.

/s/ Minodora D. Vancea

Minodora D. Vancea
Counsel
Federal Deposit Insurance Corporation
3501 Fairfax Drive, VS-D7176
Arlington, VA 22226-3500
(703) 562-2049

CERTIFICATE OF SERVICE

I hereby certify that two true and correct copy of the foregoing has been served on the following counsel for Defendants-Appellees via ECF and overnight carrier this 13th day of May, 2013:

Robert R. Ambler, Jr.
Jennifer S. Collins
John G. Perry
Womble Carlyle Sandridge & Rice
271 17th Street, NW, Suite 2400
Atlanta, GA 30363

James B. Manley, Jr.
Tracy Klingler
Jeffrey R. Baxter
Ellen C. Carothers
McKenna Long & Aldridge
303 Peachtree Street, N.E.
One Peachtree Center, Suite 5300
Atlanta, GA 30308

David L. Balser
King & Spalding, LLP
1180 Peachtree Street, NE, Suite 1700
Atlanta, GA 30309

Aaron M. Danzig
Edward A. Marshall
Arnall Golden & Gregory
171 17th Street, NW
Atlanta, GA 30363

Richard R. Edwards, III
Cochran & Edwards
2950 Atlanta Road, SW
Smyrna, GA 30080

Frank M. Young, III
Kirk D. Smith
T. Dylan Reeves
Stanley H. Pollock
Haskell Slaughter Young & Rediker
2001 Park Place North
1400 Park Place Tower
Birmingham, AL 35203

/s/
Minodora D. Vancea
Counsel
Federal Deposit Insurance Corporation