SUPREME COURT OF LOUISIANA

2007 C 2116

JAMES H. "JIM" BROWN,
as Commissioner of Insurance of the State of Louisiana

versus

ANA INSURANCE GROUP,
a Louisiana Partnership

Writ of Review
to the Court of Appeal, First Circuit
Parish of East Baton Rouge

Original Brief on the Merits by the Commissioner of Insurance, Defendant in Reconvention and Applicant

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Statement of the Case

1. Introduction

This dispute concerns actions by the Commissioner of Insurance in his role as liquidator of an insolvent insurance company. Among the assets that the Commissioner liquidated were certain securities (stock and a debenture or bond, convertible into stock) issued by Mobil Telecommunication Technologies Corp. (M-Tel). The Commissioner, through his agents, elected to liquidate these securities by a programmed or staged sale, that is, selling fixed amounts of the securities at regular intervals over a period of time, to obtain a reasonable average price for them.

Barbara McDaniel Presley, individually and as succession representative for her deceased husband, Sam Presley Jr., claims to be the beneficial owner of the liquidated company. She alleges that the Commissioner should have sold the securities all at once, immediately upon gaining control of them, and that, had he done so, he would have realized more money from the sale.

The Commissioner contends that his actions were within his discretion as a public entity; therefore he is shielded from liability by La. R.S. 9:2798.1. The Commissioner further contends that Presley has failed to carry her burden of proving breach of a duty or a causal link between any alleged breach of duty and her claimed damages. Finally, the Commissioner contends that Presley is not a proper plaintiff to enforce any obligation that may arise from the liquidation of the M-Tel securities.

2. Factual background

In August 1990, Sam Presley Jr. purchased American National Agents Group (ANA) for $50,000. Although he ostensibly placed 83% ownership in his then girlfriend, Barbara McDaniel, and 17% in an employee and friend,

Morris Mahana,[1] in later criminal proceedings he admitted that he was the *de facto* owner of 100% of ANA. (Later, Mahana purported to transfer all but 0.5% of his interest to Barbara McDaniel Presley.)

At the same time Sam Presley Jr. purchased ANA, he also purchased in his own name two affiliated companies: United States General Agency (USGA) and American Funding Services, Inc. (AFSI). He operated ANA's business by using USGA as a general agent and AFSI as a premium financer.

In 1992, the Louisiana Department of Insurance investigated ANA, learned of its actual insolvency, and placed it in conservatorship.[2] Shortly afterward, the court placed ANA in rehabilitation.[3] In May 1993, the court placed ANA in liquidation.[4] In October 1993, the court decreed that ANA, USGA, and AFSI were a single business enterprise, and ordered the liquidation of USGA and AFSI along with ANA.[5]

In due course, the Commissioner filed in the liquidation proceeding a petition against the Presleys and Mahana, alleging their indebtedness to the estate on account of their use and abuse of ANA assets.[6] In response, the Presleys filed a reconventional demand against the Commissioner with numerous allegations, including mismanagement of the estate.[7] Eventually all claims by each side against the other were dismissed or settled except for one: the Presleys' claim against the Commissioner over the liquidation of the M-Tel securities previously held by USGA.

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[1] 9 R. 1745–49, 18 R. 3894.

[2] 2 R. 68; Commissioner's Exhibit 21.11.

[3] 2 R. 127–29.

[4] 3 R. 328; 9 R. 1730.

[5] 4 R. 791–92.

[6] 6 R. 1086.

[7] 8 R. 1693.

3. The M-Tel securities

Before their liquidation, USGA held a $1 million M-Tel debenture (a bond convertible into common stock) and 50,000 shares of M-Tel stock. These securities came under the Commissioner's control on October 18, 1993.

Upon gaining control of USGA's M-Tel debenture, the Commissioner was faced with the problem of how to liquidate it. The debenture was classified as a "junk bond," meaning its rating was below investment grade.[8] And the market for a $1 million junk bond is "very thin."[9]

To liquidate this security and others in the estate, the Commissioner contracted with investment professionals. He retained Charles Reichman, C.P.A., as an independent contractor to serve as investment funds manager. Reichman, in turn, negotiated a contract with Richard Bickerstaff of Hattier, Sanford & Reynoir to manage the ANA estate's investment portfolio. Reichman also contracted with Asset Management, Inc. (owned by Bickerstaff) to help oversee the investments held by various liquidated estates, including ANA.

Under Reichman's supervision, the M-Tel securities were liquidated through a programmed or staged sale, that is, selling a fixed number of shared periodically over time to obtain a reasonable average price. The debenture was converted into common stock in order to facilitate its staged sale, because shares of stock are easier to sell separately than are pieces of a debenture bond.[10] As a result of the sale, the estate realized a gain of more than $1 million.

Despite the $1 million gain, the Presleys alleged that the Commissioner should have obtained even more for the sale. With the benefit of hindsight,

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[8] 25 R. 5450 (testimony of defense expert Walter Morales).

[9] *Id.*

[10] *Id.* at 5451.

they contended that the price of the M-Tel securities was at an all-time high in October 1993, and that if the Commissioner had dumped the entire M-Tel load on the market then, the profit would have been greater.

4. The criminal proceedings against various persons

Unknown to the Commissioner when the M-Tel securities were being liquidated, Reichman and Bickerstaff were engaged in a criminal scheme unrelated to ANA. Their offenses related to a $25 million investment fund run by the Department. Under their scheme, they purchased securities in the name of Asset Management, Inc., marked up the price, and sold the same securities to the receivers at the marked-up price.[11] The scheme netted some $221,000 in fees for Asset Management, of which Bickerstaff kicked back $90,000 to Reichman.[12] The two were caught, and pleaded guilty to both state and federal offenses in connection with their scheme.

Meanwhile, the Presleys too were implicated in criminal proceedings. They, along with others, were charged by federal prosecutors with conspiracy, RICO, mail fraud, and wire fraud, all in connection with ANA.[13] Sam Presley eventually made a plea agreement with the federal prosecutors. As part of the plea agreement, he admitted that, though ANA was purchased ostensibly in Barbara's name, in fact "ownership and control rested with [Sam] Presley,"[14] and he forfeited his interest in ANA and its affiliates.[15] In

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[11] *See* Affidavit in Support of Application for Arrest Warrant (Charles Reichman) ¶ 4 and Affidavit in Support of Application for Arrest Warrant (Richard Bickerstaff) ¶ 4. Both affidavits are included in Commissioner's Exhibit 54.

[12] *See* Admission by Charles Reichman ¶¶ 14–15 and Admission by Richard Bickerstaff ¶¶ 19–20. Both admissions are included in Commissioner's Exhibit 54.

[13] Commissioner's Exhibit 14, deposition of Peter Strasser, depo. exh. 2.

[14] *Id.*, depo. exh. 8.

[15] *Id.*, depo. ex. 7 ¶ 2 ("He is also subject to forfeiture ..."); *id.* ¶ 5 ("The defendant hereby agrees to forfeit ..."); *id.* page 4 (signatures of Sam Presley and his attorney, Provino Mosca).

exchange for Sam Presley's admission and plea, the charges against Barbara Presley were dismissed.[16]

Sam Presley was imprisoned for his crimes. A few months after his release, he died, and Barbara Presley was appointed as his succession representative.

5. Action of the trial court

As stated above, the Commissioner filed a petition against the Presleys alleging wrongful conduct by them detrimental to ANA. In response, the Presleys filed a reconventional demand against the Commissioner alleging numerous things, including mismanagement of ANA's assets. In response to the reconventional demand, the Commissioner pleaded peremptory exceptions of discretionary-function immunity and no right of action.[17] Later, on learning that Sam Presley, not Barbara Presley, was the true owner of ANA, the Commissioner pleaded an exception of no right of action based on this fact.[18] In the alternative, the Commissioner pleaded exceptions of res judicata and collateral estoppel, based on Sam's admission in federal court that he was the true owner of ANA.[19] The trial court overruled these exceptions except for discretionary-function immunity, which was referred to the merits.[20]

Before trial, all claims were settled or dismissed except for one: the claim arising from the programmed sale of USGA's M-Tel securities. The case proceeded to a bench trial on this single remaining claim.

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[16] *Id.*, depo. exh. 9 at 14; *see also id.*, depo. exh. 10.

[17] 17 R. 3631.

[18] 18 R. 3869.

[19] 18 R. 3996.

[20] 19 R. 4131 (overruling exception of no right of action); 23 R. 5085 (referring discretionary-function immunity to the merits).

Ultimately the trial court rendered judgment in Presley's favor.[21] The trial court found that the M-Tel securities were sold "in such a way that [Reichman and Bickerstaff] received unjustified money payments," and "in such a manner merely to profit Bickerstaff and Reichman," but did not specify any particular act or omission by Reichman or Bickerstaff connected with the M-Tel securities.[22] Also absent from the trial court's reasons for judgment is any mention of discretionary-function immunity. As for the measure of damages, although the record reflects that Asset Management received only $12,630 in commissions from the ANA estate,[23] the trial court rendered judgment for nearly 100 times that amount: $1,247,132.[24]

6. Action of the court of appeal

The Commissioner appealed the trial court's judgment, but a divided panel of the court of appeal voted 3:2 to affirm. The majority found that the Commissioner failed to adequately supervise Reichman and Bickerstaff, and that this failure to supervise somehow caused a loss to the ANA estate. The majority wrote that the Commissioner had a duty to make sure that Reichman and Bickerstaff followed the Insurance Code,[25] but did not explain how the programmed sale they conducted would have violated the Insurance Code.

Unlike the trial court, the majority did address the Commissioner's defense of discretionary-function immunity. But like the trial court, the majority rejected it. The majority reasoned that a failure to supervise is "not an omission 'reasonably related to the legitimate governmental objective' of

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[21] 23 R. 4990.

[22] 25 R. 5474.

[23] *E.g.* 17 R. 3747.

[24] 23 R. 4990.

[25] *Brown v. ANA Ins. Group*, 2006-0626 p. 25 (La. App. 1 Cir. 7/18/07), 965 So.2d 902, 920, writ app. at A-36 ("We believe that upon appointment of the agents, the Commissioner's fiduciary duty included oversight of his agents to ensure that they acted in compliance with the dictates and policy of the Insurance Code.").

the liquidation provisions of the Insurance Code."[26] And though the trial court made no finding of recklessness, the majority postulated that, "Indeed, the Commissioner's failure to oversee his appointed agents constitutes reckless misconduct."[27] Thus, the majority held La. R.S. 9:2798.1 inapplicable.

The majority also rejected the Commissioner's argument that Barbara Presley has no right of action. The Commissioner argued that the M-Tel securities belonged to USGA, not ANA, that Sam Presley was 100% owner of USGA, and that he had forfeited his interest in USGA as part of his guilty plea in federal court. But the majority reasoned that Barbara Presley, as "owner of record" of ANA, had a right of action anyway, because the assets of the two companies were pooled as a result of the trial court's single-business-enterprise designation, thus giving Barbara an interest in USGA assets. The majority acknowledged but did not refute the Commissioner's evidence that, in fact, Barbara did not own ANA.

Judge McClendon, joined by Judge Parro, dissented from the majority's failure to apply La. R.S. 9:2798.1. Judge McClendon held that the Insurance Code permits a programmed sale and authorizes the Commissioner to retain investment advisers to help liquidate securities and other assets found in a liquidated estate. Thus, "the hiring of investment advisers, and accepting their decisions relating to the method and timing of the liquidation of various assets, were discretionary, within the course and scope of the commissioner's powers and duties, grounded in economic policy, and directly related to the statutory duties of the commissioner and the legislative objective."[28] Judge McClendon further pointed out that Presley had the burden of proving

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[26] *Id.* p. 21, 965 So.2d at 917, writ app. at A-32.

[27] *Id.*

[28] *Id.* p. 5, 965 So.2d at 924, writ app. at A-43 (McClendon, J., dissenting).

negligent supervision and found an absence of evidence enabling her to carry that burden.[29] Judge Parro joined Judge McClendon's dissent, and further found that Barbara Presley has no right of action.[30]

Specification of Errors

1. The court of appeal erred by failing to apply La. R.S. 9:2798.1 to a claim against the Commissioner alleging negligent supervision of an independent contractor.

2. The court of appeal erred in postulating that the Commissioner acted recklessly, without differentiating the Commissioner's actions from ordinary negligence.

3. The court of appeal erred by imposing liability on the Commissioner for negligent supervision even though Presley failed to prove the elements of this claim.

4. The courts below erred in failing to sustain the Commissioner's exception of no right of action.

Argument

1. The Commissioner cannot be held liable for allowing the M-Tel securities to be liquidated through a programmed sale.

A. The Commissioner acted reasonably in retaining investment professionals to assist in liquidating the M-Tel securities and allowing them to liquidate the securities through a programmed sale.

Part and parcel of the negligent-supervision allegation is what Reichman and Bickerstaff did while supposedly not being supervised: the programmed or staged sale of the M-Tel securities. If the programmed sale was proper, then there is no causal connection between alleged failure to supervise and

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[29] *Id.* p. 6, 965 So.2d at 924, writ app. at A-44 (McClendon, J., dissenting).

[30] *Id.*, 965 So.2d at 925–27, writ app. at A-47–A-49 (Parro, J., dissenting).

any claimed damages. The court of appeal failed to address this threshold question.

At trial, Presley argued and tried to prove that the programmed sale was improper. She argued that Reichman and Bickerstaff made this decision so as to churn the ANA account and generate increased commissions. She failed, however, to show any increase in Asset Management's commissions resulting from the programmed sale. (Actual commissions earned from ANA by Asset Management were only $12,630, and only part of this is attributable to the M-Tel securities.[31]) Although the programmed sale yielded a net profit of over $1 million, Presley argued that the profit would have been $2.4 million higher if the M-Tel securities had been sold immediately.

But hindsight is not the measure of conduct; the measure is what a reasonably prudent administrator would have done, knowing what was known at the time. The evidence at trial established that a reasonably prudent administrator would have done exactly what was done here.

Two defense experts testified on the standard of care: W.O. Myrick and Walter A. Morales. Myrick has experience as a regulator examining insurance companies, liquidating them, and supervising them. He has served as Chief Examiner in Louisiana and as Acting Deputy Commissioner over the Louisiana Office of Receivership.[32] He is a certified insurance examiner and certified financial examiner.[33] He testified that the standard of care is that of a fiduciary.[34] In his view, to immediately dump the M-Tel securities on the market without the benefit of analysis and professional advice would have

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[31] *See*, *e.g.*, 17 R. 3747.

[32] 24 R. 5374. *See also* Commissioner's Exh. 13, Myrick's résumé, for details of his expert qualifications.

[33] 24 R. 5375.

[34] 24 R. 5379.

been "inappropriate."[35] Rather, the prudent thing to do was to obtain advice from investment advisors, assess that advice, and usually to follow that advice.[36] In his opinion, the Commissioner met this standard of care by seeking out and following the advice of Bickerstaff and the Hattier firm in liquidating the M-Tel securities.[37]

Morales is a professional asset manager, and was accepted by the Court as an expert financial advisor.[38] He too testified that, in liquidating the M-Tel securities, the standard of care called for the Commissioner to obtain expert financial advice. "It's well established that a fiduciary can employ outside experts to provide advice…. [i]t's well within the role of a fiduciary in order to designate [an] advisor to assist in discharging fiduciary activity. " he testified.[39] Moreover, the programmed sale, or sale in stages, of the M-Tel securities was reasonable advice for the advisors to give. "It's not at all uncommon to see a fiduciary dispose of a concentrated position that way."[40]

Morales elaborated on some of the specific steps a fiduciary should follow when coming into possession of these kinds of securities. "First of all he needs to find out what he has."[41] In this case, the fiduciary received reports from Hattier and others about M-Tel, all of them positive. Next, the fiduciary must assess those assets against anticipated liabilities. As Morales put it, "you have to balance the need to liquidate, generate cash to pay claims and pay expenses of the estate versus the objective of trying to maximize the value" of

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[35] 25 R. 5406-07.

[36] 25 R. 5407.

[37] 25 R. 5431.

[38] 25 R. 5432-33. *See* Commissioner's Exh. 11, Morales's résumé, for details of his expert qualifications.

[39] 25 R. 5440.

[40] 25 R. 5442.

[41] 25 R. 5444.

the investments.[42] In other words, the fiduciary must figure out what assets are available to manage the liabilities, and within the assets, what is the outlook.[43]

Morales was asked whether it would ever be prudent for a fiduciary to immediately dump all the securities as soon as they were received. "The only way I can envision the requirement to do that," he testified, "would be if you had bills staring you in the face that had to be met and you had to generate cash and that was the way to generate cash. Then the prudent thing to do would have been to sell all the stock on that day. Short of that, selling it over time to take yourself out of the business of trying to predict whether this is the high or low price is the prudent way to go."[44]

Here, the Commissioner met the standard of care established by these two experts. He obtained the advice of experts and followed their advice.[45]

B. The decision to conduct a programmed sale was a discretionary act under La. R.S. 9:2798.1.

In *Fowler v. Rodriguez*,[46] this Court set out a two-step inquiry, derived from the U.S. Supreme Court's decision in *Berkowitz v. United States*,[47] to determine whether the discretionary-acts doctrine of La. R.S. 9:2798.1 applies in a specific fact situation. First, the court must determine whether a statute, regulation, or policy prescribes a course of action for the public entity to follow. If so, there is no discretion on the part of the public entity and therefore no immunity. If a court determines that discretion is involved, then the court must determine whether that discretion is the kind shielded by the

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[42] 25 R. 5444-45.

[43] 25 R. 5445.

[44] 25 R. 5456.

[45] 25 R. 5431 (Myrick's testimony).

[46] 556 So.2d 1 (La. 1989).

[47] 486 U.S. 531 (1988).

exception, that is, one grounded in social, economic, or political policy. If it is, then the doctrine applies and the public entity is insulated from liability.[48]

The status of the *Fowler* test is uncertain in light of this Court's 2003 plurality decision in *Gregor v. Argenot Great Central Insurance Co.*[49] In *Gregor*, the plurality criticized *Fowler*'s distinction between operational acts (for which there is no immunity) and policymaking or ministerial acts (for which there is immunity).[50] The *Gregor* plurality advocated a more literal interpretation of La. R.S. 9:2798.1.

Whichever way the Court resolves the tension between *Fowler* and *Gregor*, the result here should be the same. Under *Gregor*, the programmed sale was "within the course and scope of [the Commissioner's] lawful powers and duties." And under *Fowler*, the decision on how to liquidate the M-Tel securities was grounded in social, economic, and political policy.

i. The programmed sale was within the course and scope of the Commissioner's lawful powers and duties.

When a Louisiana court orders the liquidation of an insurer, the Commissioner has the duty under La. R.S. 22:737(A) to "immediately proceed to liquidate the property, business and affairs of the insurer." Note the statutory command is not to immediately *liquidate*, but to immediately *proceed* to liquidate. The word *proceed* authorizes a programmed or staged liquidation. Webster's Unabridged Dictionary defines *proceed* as "to begin and carry on a series of actions or measures."[51] Similarly, Webster's Ninth New Collegiate Dictionary defines *proceed* as "to go on in an orderly and

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[48] *Fowler*, 556 So.2d at 15 (on reh'g). *See also Simeon v. Doe*, 618 So.2d 848, 852–53 (La. 1993).

[49] 2002-1138 (La. 5/20/03), 851 So.2d 959.

[50] *See Gregor*, 2002-1138 pp. 10–12, 851 So.2d at 966–67.

[51] Webster's New Twentieth Century Dictionary of the English Language 1434 (2d ed. 1983).

regulated way," "to begin and carry on an action, process, or movement," "to be in the process of being accomplished," and "to move along a course."[52]

Here, the Commissioner's agents did exactly what La. R.S. 22:737(A) instructed them to do. Upon gaining control of the M-Tel securities, they immediately proceeded to liquidate them by instituting a programmed sale: "an orderly and regulated way" to liquidate a large block of securities.

ii. The decision to conduct a programmed sale was grounded in social, economic, and political policy.

When a statute vests the Commissioner with some discretion, the Court must presume that the Commissioner is exercising that discretion based on the same policy concerns that animate the statutes themselves.[53] Here, the public policy behind the statutes themselves is evident. Insurance is an industry affected with the public interest, and the purpose of the Insurance Code—including the provisions at issue here—is to regulate that industry in all its phases.[54] The purpose of Part XVI of the Insurance Code (governing rehabilitation, conservation, and liquidation of insolvent insurers) is to "protect the interest of the insurer's policyholders, members, stockholders, creditors, or the public …."[55] The public policy behind these statutes is exactly the kind of social, economic, or political policy protected by the discretionary-acts doctrine.

On this point, the federal decisions in *Franklin Savings Corp. v. United States* [56] are instructive. *Franklin* involved a claim against the RTC as conservator or receiver for negligent management and operation of a failing S&L. The RTC filed a motion to dismiss based on the federal equivalent to

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[52] Webster's Ninth New Collegiate Dictionary 937 (1984).

[53] *See U.S. v. Gaubert*, 499 U.S. 315, 324 (1991); *La. v. Public Investors, Inc.*, 35 F.3d 216, 221 (5th Cir. 1994).

[54] *See* La. R.S. 22:2(A)(1).

[55] La. R.S. 22:733(B).

[56] 970 F. Supp. 855 (D. Kan. 1997), *aff'd*, 180 F.3d 1124 (10th Cir. 1999).

our discretionary-acts doctrine. The district court granted the motion, and the Tenth Circuit affirmed. In granting the motion, the district court found that the discretion afforded the RTC to manage the troubled S&L was grounded in public policy:

> The RTC's actions while serving as conservator and receiver of [the S&L] were related directly to the public policy considerations regarding federal oversight of the thrift industry. *See Gaubert*, 499 U.S. at 332-33, 111 S. Ct. at 1278-79. Indeed, the nature of and inherent discretion underlying the agency's decisions are what drove Congress to enact the discretionary function exception in the first place.[57]

The Presleys may argue that in selling the M-Tel securities, Bickerstaff and Reichman were not motivated by public-policy concerns, but rather by ulterior motives born of an illegal scheme. But even if Bickerstaff and Reichman had ulterior motives related to M-Tel, their motives would have no bearing on the discretionary-acts analysis. As explained by the U.S. Fifth Circuit in a case applying Louisiana law, "The focus of the inquiry is not on the agent's subjective intent in exercising the discretion conferred by statute or regulation, but on the nature of the actions taken and whether they are susceptible to policy analysis."[58] Thus, as recognized by the Tenth Circuit in *Franklin*, "it is unnecessary for government employees to make an actual 'conscious decision' regarding policy factors," and in fact "courts should not inquire into the actual state of mind or decisionmaking process of [government] officials charged with performing discretionary functions."[59]

In sum: Louisiana law vested the Commissioner with discretion in deciding when and how to liquidate the M-Tel securities. That discretion is grounded in the public policy of protecting the interests of policyholders, creditors, owners, and the general public. Therefore, the discretionary-acts

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[57] 970 F. Supp. at 867.

[58] *La. v. Pub. Investors, Inc.*, 35 F.3d 216, 221 (5th Cir. 1994) (applying Louisiana law); *see also Gaubert*, 499 U.S. at 325, 111 S. Ct. at 1275.

[59] 180 F.3d at 1135.

doctrine of R.S. 9:2798.1 applies, and the programmed sale cannot serve as a basis for imposing liability on the Commissioner.

2. The Commissioner cannot be held liable for negligent supervision of Reichman or Asset Management.

Neither the trial court nor the First Circuit articulated any reason why the programmed sale was supposedly wrong. Instead, they faulted the Commissioner for failing to supervise Reichman and Bickerstaff. Neither lower court explained what this additional supervision should have consisted of, or what difference any additional supervision would have made in how the M-Tel securities were liquidated.

The imposition of liability for negligent supervision is wrong for two big reasons. First, Presley failed to prove the basic elements of a negligent-supervision claim. Second, a public entity's supervision of an independent contractor is a discretionary function under La. R.S. 9:2798.1.

A. Presley failed to prove the elements of a negligent-supervision claim under *Wallmuth v. Rapides Parish School Board*.

In *Wallmuth v. Rapides Parish School Board*,[60] this Court articulated the standard of liability for a school board's failure to supervise students. Before liability can be imposed, "there must be proof of negligence in providing supervision and also proof of a causal connection between the lack of supervision and the accident."[61] Proof of negligence requires proof that "the risk of unreasonable injury [was] foreseeable, constructively or actually known …."[62] Proof of a causal connection requires proof that the risk of harm was "preventable if a requisite degree of supervision had been exercised."[63]

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[60] 2001-1779 p. 8 (La. 4/3/02), 813 So.2d 341, 346.

[61] *Id.*

[62] *Id.*

[63] *Id.*

Surely the duty to supervise an independent contractor cannot be greater than the duty in *Wallmuth* to supervise school children. Yet assuming that these two duties are equal, Presley's negligent-supervision claim fails *Wallmuth*'s test. Before Reichman's and Bickerstaff's crimes came to light, no one had any reason to suspect their wrongdoing. Even more fundamentally, the record contains no evidence that any amount of "supervision" would have uncovered their wrongdoing sooner. A hypothetical supervisor could have been sitting in Reichman's office eight hours a day, reading every piece of paper passing his desk, listening to every conversation, without knowing that, *outside the office*, he was getting kickbacks from Bickerstaff.

If our hypothetical supervisor knew that Reichman and Bickerstaff were conducting a programmed sale of the M-Tel securities, he or she would have approved. As shown above, expert testimony at trial established that a programmed sale was the most reasonable way to liquidate a large block of securities. Nothing in either the trial court's reasons for judgment or the court of appeal's opinion says otherwise.

The worst thing that our hypothetical supervisor might have figured out is that Asset Management, Inc.'s services were unnecessary because they duplicated the services being performed by others. Indeed, that was the conclusion reached by defense expert W.O. Myrick.[64] But if the Commissioner is to be faulted for failing to detect the duplication sooner, then the measure of damages should be the commissions earned by Asset Management from the ANA estate: $12,630, or roughly 1% of the damages awarded by the trial court.[65] (The amount of Asset Management's commissions would not have

[64] 25 R. 5410.

[65] 17 R. 3747.

alarmed our hypothetical supervisor, as they were substantially less than the $17,532 earned by Hancock Bank, which is not accused of any wrongdoing.[66])

In sum: the record contains no evidence that the Commissioner knew or should have known about Reichman's and Bickerstaff's misdeeds before they came to light. Nor is there any evidence that the Commissioner would have learned of their misdeeds sooner had he supervised them more closely. Nor is there any evidence that any level of supervision would have made a difference in the way the M-Tel securities were liquidated.

B. Presley likewise failed to establish any standard of care for supervising the independent contractors or breach of any standard of care.

Both the trial court and the court of appeal faulted the Commissioner for failing to supervise Reichman and Bickerstaff. But neither the trial court nor the court of appeal has articulated exactly what the Commissioner should have done but failed to do. This gap in the lower courts' reasoning reflects a gap in Presley's case. Presley offered no evidence concerning the standard of care to be exercised by the Commissioner in supervising Reichman and Bickerstaff; nor did she offer any evidence that the Commissioner's conduct fell below any articulated standard of care. In fact, this record contains no evidence on what the Commissioner did or did not do in supervising Reichman and Bickerstaff.

The evidence cited by the court of appeal does not come close to satisfying Presley's burden of proof. The court cited the testimony of L.D. Barranger, who testified that the Commissioner, rather than develop his own guidelines for supervising independent contractors, followed guidelines published by the National Association of Insurance Commissioners:

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[66] *Id.*

> Q. Do you know, sir, if Commissioner Brown had in place any particular method or work product or — what is the word I am —
>
> A. Policies or procedures?
>
> Q. Yes, that would identify supervision over people such as Mr. Reichman?
>
> A. No, he did not have. We had the NAIC's publication that we used as a method —
>
> [Objection made and overruled.]
>
> Q. You can answer.
>
> A. I was just saying to you that there is a manual that the NAIC has with relationship to liquidations, receiverships really, and that was at the time pretty much the bible that everybody used. It was a very narrow written document that did go into a lot of detail regarding takedown and things like that.[67]

From this testimony about the Commissioner's adherence to NAIC guidelines, the court of appeal assumed that (a) "the NAIC manual did not provide guidelines for oversight of agents retained by the Commissioner,"[68] and (b) this absence of published guidelines established the Commissioner's failure to supervise Reichman and Bickerstaff.

In dissent, Judge McClendon pointed out that the flaw in the majority's reasoning: the conclusion does not necessarily follow from the premise. "From my review, I cannot say that the absence of formal or written procedures, without more, automatically equates to proof of negligent supervision or an intentional failure to supervise."[69]

Judge McClendon was right on this point and another: Presley, not the Commissioner, bore the burden of proof.[70] The absence of any mandatory statute or regulation dictating how the Commissioner must oversee an independent contractor is a gap in Presley's case, not the Commissioner's.[71]

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[67] 24 R. 5343–44.

[68] *Brown*, 2006-0626 p. 20 n. 22, 965 So.2d at 917 n. 22, writ app. at A-31 n. 22.

[69] *Brown*, 2006-0626 p. 6, 965 So.2d at 924, writ app. at A-44 (McClendon, J., dissenting).

Without such a statute or regulation, Presley had the burden of offering some other evidence on the standard of care. She failed to carry this burden.

C. Any decision on the level of supervision exercised by the Commissioner over his independent contractors—including whether to supervise them at all—was a discretionary act under La. R.S. 9:2798.1.

The absence of a mandatory statute or regulation governing supervision of Reichman and Bickerstaff carries another implication: it means the level of oversight was left to the Commissioner's discretion. The court of appeal failed to realize this. The crux of its imposition of liability is its holding that the Commissioner had no discretion concerning the supervision of an independent contractor. Acknowledging that the Commissioner had discretion to retain an independent contractor, the court of appeal reasoned that the Commissioner's delegation of duties to an independent contractor "included oversight and supervision [of the contractor] to ensure compliance with the law on liquidation."[72] The court of appeal then reasoned that any failure to supervise an independent contractor "was not an omission 'reasonably related to the legitimate governmental objective' of the liquidation provisions of the Insurance Code."[73]

The problem with this reasoning is that it conflicts with prevailing law. The level of supervision exercised by a public entity over an independent contractor is itself a discretionary function. If, as here, no statute or

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[70] *Id.* ("Further, on the specific claim of negligent supervision, Mrs. Presley bore the burden of proof.").

[71] *See Alinsky v. U.S.*, 415 F.3d 639, 647 (7th Cir. 2005) ("The plaintiffs fail to identify any mandatory statute or regulation dictating how the FAA must oversee private contractors or assure the contractor complies with federal regulations …. Where the plaintiffs' claim is premised on negligent oversight, such a showing is imperative.").

[72] *Brown*, 2006-0626 p. 20, 965 So.2d at 917, writ app. at A-31 *infra*. *See also* 2006-0626 p. 25, 965 So.2d at 920, writ app. at A-36 ("We believe that upon appointment of the agents, the Commissioner's fiduciary duty included the oversight of his agents to ensure that they acted in compliance with the dictates and policy of the Insurance Code.").

[73] *Brown*, 2006-0626 p. 21, 965 So.2d at 917, writ app. at A-32.

regulation controls the government's monitoring of an independent contractor's work, then the extent of monitoring required or actually accomplished is necessarily a question of judgment or discretion. *Kirchmann v. U.S.*, 8 F.3d 1273, 1276 (8th Cir. 1993); *see also Domme v. U.S.*, 61 F.3d 787, 791 (10th Cir. 1995) (where no governmental orders specified how reviews and inspections were to be conducted, "the regulations allowed the government's employees to exercise choice and discretion."). In fact, when a governmental actor decides the extent to which it will supervise an independent contractor, "it is exercising discretion at one of the highest planning levels." *Blaber v. U.S.*, 332 F.2d 629, 631 (2d Cir. 1964); *see also Kandarge v. U.S. Dept. of Navy*, 849 F. Supp. 304, 309 (D.N.J. 1994) ("[W]hen an agency determines the extent to which it will supervise the safety procedures of private individuals, it 'is exercising discretionary regulatory authority of the most basic kind.'").

If supervising an independent contractor is a discretionary function, then so is the decision not to supervise at all. Under La. R.S. 9:2978.1(B), failure to carry out a discretionary function is protected by discretionary-function immunity: "Liability shall not be imposed on public entities … based upon … the failure to exercise or perform their … discretionary acts …." Thus, if arguably based on policy considerations, both negligence in supervising an independent contractor and failure to supervise a contractor at all are included in the decisions protected by discretionary-function immunity. *Kirchmann*, 8 F.3d at 1277.

Here, the Commissioner undoubtedly acted within his discretion in contracting investment-management responsibilities to an independent contract. The court of appeal conceded this point:

> We believe the Commissioner acted appropriately in retaining financial advisers to assist in the liquidation of the

> ANA estate. Clearly, the appointment of assistants is authorized under the Insurance Code. La. R.S. 22:743.[74]

If the governmental actor acts within its discretion in contracting responsibility to an independent contractor, any claim for lack of oversight is subject to the discretionary-function immunity. *Alinsky v. U.S.*, 415 F.3d 639, 648 (7th Cir. 2005) ("Thus, the discretionary function exemption protects the government from liability for claims premised on the lack of … oversight … since the government acted within its discretion to contract those responsibilities out to" an independent contractor.).

When one realizes that supervision costs money, then the discretionary nature of the decision becomes clear. Simply put, the Commissioner does not have an unlimited supply of "supervision" to dole out. Any decision concerning supervision of an independent contractor is a decision on allocation of limited resources. Any time the Commissioner or a department employee spends supervising is time taken away from other tasks. And whoever the supervisor may be, time spent on supervising translates into dollars spent on supervising; supervisors do not work for free. Therefore, a decision on how much supervision to exercise over an independent contractor is a decision on allocation of public resources — a quintessential discretionary function.

D. The court of appeal's *de novo* finding of recklessness is unsupported by any evidence.

Under R.S. 9:2798.1(C)(2), discretionary-function immunity does not apply "[t]o acts or omissions which constitute … reckless[ ] or flagrant misconduct." The trial court made no finding that the Commissioner's actions were reckless. But the court of appeal postulated *de novo* that, "[i]ndeed, the Commissioner's failure to oversee his appointed agents constitutes reckless misconduct."

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[74] *Brown*, 2006-0626 p. 24, 965 So.2d at 919, writ app. at A-35.

The court of appeal erred here by failing to analyze the Commissioner's conduct according to the criteria of this Court's decision in *Ambrose v. New Orleans Police Department Ambulance Service*.[75] In *Ambrose*, this Court explained that gross negligence (synonymous with recklessness) is much, much worse than ordinary negligence or an error in judgment:

> Gross negligence has been defined as the "want of even slight care and diligence" and the "want of that diligence which even careless men are accustomed to exercise." … Gross negligence has also been termed the "entire absence of care" and the "utter disregard of the dictates of prudence, amounting to complete neglect of the rights of others." … Additionally, gross negligence has been described as an "extreme departure from ordinary care or the want of even scant care." … Gross negligence, therefore, has a well-defined legal meaning distinctly separate, and different, from ordinary negligence.[76]

Under *Ambrose*, gross negligence is synonymous with reckless misconduct; *Ambrose* recognizes "no clear distinction" between these two terms; rather "[t]he two have tended to merge and take on the same meaning."[77]

Whatever Reichman and Bickerstaff may have done, this record contains no evidence to suggest that *the Commissioner* did anything "criminal, fraudulent, malicious, intentional, willful, outrageous, reckless, or flagrant" in connection with the M-Tel securities. Reichman, a C.P.A., was apparently competent to manage liquidation of securities. And before Reichman's and Bickerstaff's arrests, the Commissioner had no reason to suspect that they were dishonest. To accuse the Commissioner of reckless misconduct is to unfairly charge him with knowledge of Reichman's and Bickerstaff's proclivities long before their criminal conduct came to light.

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[75] 93-3099 (La. 7/5/94), 639 So.2d 216.

[76] *Id.*, 639 So.2d at 219–20.

[77] *Id.* at 220.

4. Presley has no right of action.

A. Barbara Presley never owned ANA.

In her capacity as Sam Presley's succession representative, Barbara Presley has no claim against the Commissioner. Sam pleaded guilty in federal court to several felonies in connection with his operation of the ANA single-business enterprise, and as part of that plea bargain, he agreed to forfeit his interest in those companies. As Sam's succession representative, Barbara is bound by Sam's admission and forfeiture.

Individually, Barbara Presley has no claim. She did not own USGA, the company whose M-Tel securities are at issue here. Sam owned that company in his own name, but as stated above, he forfeited his interest in it.

Nor does she have any claim as owner of record of ANA. Granted, on paper she was the "owner of record."[78] And for a time, the Commissioner was deceived into believing that she actually owned ANA.[79] But as all would later learn, her ownership was a sham. As part of Sam Presley's plea agreement in federal court, Sam Presley admitted that he, in fact, was 100% owner of ANA.

The court of appeal acknowledged all this, refuted none of it, yet still held that Barbara Presley has a right of action. On page 3 of its opinion, the court of appeal acknowledges that Sam purchased ANA, placing purported ownership in Barbara McDaniel and Morris Mahana, and that Sam operated ANA's business.[80] On page 9 of its opinion, the court of appeal acknowledges the Commissioner's argument that Barbara's purported ownership was a sham.[81] Yet without showing any flaw in the Commissioner's argument, the

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[78] *Brown*, 2006-0626 p. 12, 965 So.2d at 911, writ app. at A-23.

[79] *E.g.,* 6 R. 1086 (Commissioner alleging that "Barbara McDaniel owned 99.5% of ANA ….").

[80] *Brown*, 2006-0626 p. 3, 965 So.2d at 906, writ app. at A-14.

[81] *Id.* p. 9, 965 So.2d at 910, writ app. at A-20.

court of appeal nevertheless held that Barbara, “as an owner of ANA,” had a right of action.[82]

In reaching this holding, the court of appeal reasoned that the single-business-enterprise designation effectively merged USGA and ANA, thus giving Barbara, as supposed owner of ANA, a right of action arising from the liquidation of USGA’s assets.[83] This legal reasoning is faulty; as Judge Parro says in dissent, a single-business-enterprise designation does not erase all legal distinctions for all purposes between the companies forming the enterprise.[84] But an even more fundamental problem with the majority’s reasoning is that it begs the question of Barbara Presley’s ownership of ANA.

B. Even if Barbara Presley were the owner of ANA, the court’s liquidation order would have divested her of her ownership interest.

Even if Barbara Presley were once owner of ANA, she would have no ownership interest today. When the trial court ordered the liquidation of the ANA single business enterprise (including USGA), title to all USGA assets was vested in the Commissioner. La. R.S. 22:735(A). If any assets remain after payment of a liquidated insurer’s debts, then those surplus assets are “distributed in accordance with the direction of the court.” La. R.S. 22:755(G).

And if any debt were owed by the Commissioner to the estate, Barbara Presley would stand at the end of the line to partake of it. The priority for paying the debts of a liquidated insurer is established by La. R.S. 22:746. This statute establishes six ranks for distribution of assets, five of which outrank any claim Barbara Presley would have as former “owner” of ANA. The court of appeal’s judgment violates this statute by giving Barbara Presley a priority she is not entitled to.

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[82] *Id.* p. 11, 965 So.2d at 911, writ app. at A-22.

[83] *Id.* pp. 11–12, 965 So.2d at 911, writ app. at A-22–A-23.

[84] *Id.* p. 3 (Parro, J., dissenting), 965 So.2d at 926–27, writ app. at A-49.

Conclusion

The Commissioner prays that this Court reverse the court of appeal's judgment and hold as follows:

1. That a programmed or staged sale of securities fulfills La. R.S. 22:737(A)'s command to "immediately proceed to liquidate the property ... of the insurer," and is therefore within the course and scope of the Commissioner's lawful duties for purposes of La. R.S. 9:2798.1. Since the result of alleged failure to supervise—the staged sale—was entirely proper, the alleged failure to supervise caused no compensable harm to the ANA estate.

2. That for purposes of La. R.S. 9:2798.1, the level of supervision exercised by the Commissioner over an independent contractor retained under La. R.S. 22:743(A)—including the decision whether to supervise at all—is a discretionary act and is reasonably related to legitimate governmental objectives for which policymaking or discretionary power exists.

3. That even if the Commissioner were negligent in supervising Reichman and Bickerstaff, this ordinary negligence does not rise to the level of "criminal, fraudulent, malicious, intentional, willful, outrageous, reckless, or flagrant misconduct" under La. R.S. 9:2798.1(C)(2).

4. That Barbara Presley is not the owner of ANA or any of its assets, and therefore has no right of action arising from the liquidation of ANA's assets.

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