STATE OF MICHIGAN

IN THE SUPREME COURT

RICHARD JAMES,

Plaintiff,

and

SAFECO INSURANCE COMPANY OF AMERICA,

Plaintiff-Appellee,

v

STATE FARM FIRE AND CASUALTY COMPANY,

Defendant-Appellant,

and

AUTO CLUB GROUP INSURANCE COMPANY,

Defendant

and

DAVID GASOWSKI,

Defendant-Appellee.

Supreme Court Docket No. 130460

COA Docket No. 262805

St. Clair County Circuit Court
Case No. 03-2466-NZ
Hon. Peter E. Deegan

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DEFENDANT-APPELLEE DAVID GASOWSKI'S BRIEF IN RESPONSE TO COURT ORDER

- PROOF OF SERVICE -

FILED

AUG 10 2007

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MICHIGAN SUPREME COURT

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IV. STATEMENT OF QUESTIONS INVOLVED

1. WHETHER STATE FARM, BY FAILING TO PLEAD RELEASE AS AN AFFIRMATIVE DEFENSE IN THIS DECLARATORY RELIEF ACTION, WAIVED ITS RIGHT TO OPPOSE PLAINTIFFS' ATTEMPT TO INVOKE OFFENSIVE COLLATERAL ESTOPPEL AS INCONSISTENT WITH THE TERMS OF THE PARTIES' RELEASE AND SETTLEMENT AGREEMENT IN THE UNDERLYING ACTION?

2. WHETHER, FOR PURPOSES OF COLLATERAL ESTOPPEL, THE IDENTITY OF THE JET-SKI DRIVER WAS ACTUALLY LITIGATED AND DETERMINED BY A FINAL JUDGMENT IN THE UNDERLYING ACTION?

3. WHETHER, FOR PURPOSES OF COLLATERAL ESTOPPEL, STATE FARM WAS A PARTY, OR IN PRIVITY WITH A PARTY, TO THE UNDERLYING ACTION?

4. HOW SHOULD AN INSURER PROCEED WHEN IT BELIEVES ITS INSURED IS COMMITTING FRAUD TO INVOKE COVERAGE, AND DOES THAT DEPEND ON WHETHER THE INSURER LEARNS OF THE CONFLICT OF INTEREST DURING THE COURSE OF THE LITIGATION?

5. IF AN ADVERSE JUDGMENT PROCURED BY FRAUD OF THE INSURED IS ENTERED, WHETHER THE INSURER IS ESTOPPED FROM CONTESTING LIABILITY?

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BACKGROUND

The instant case arises out of jet-ski accident which occurred on August 31, 2002. Mr. Gasowski was a passenger on a jet-ski owned by Mario Silvestri ("Mr. Silvestri") which was being driven by Richard James ("Mr. James"). Mr. James negligently lost control of the jet ski, allowing it to crash into a wooden bridge in a channel near Big Muscamoot Bay in St. Clair County. As a direct and proximate result of Mr. James's negligence, Mr. Gasowski suffered a closed head injury, brain hemorrhaging, a torn aorta, back injury, foot drop, bruised lung, broken ribs, a lacerated spleen, vocal cord paralysis, and severe and permanent scarring on his back, side and knees.

After the accident, State Farm took possession of the jet-ski and sent its Claims Specialist from its Special Investigation Unit ("SIU"), Jerry Capps, to record witness statements. However, none of these statements were Examinations Under Oath ("EUOs"). Mr. Capps recorded the statement of Scottie Stevens, who indicated that Mr. Gasowski was the passenger on the jet-ski. **(Exhibit A)**. Paul Varblow, another State Farm representative, took the recorded statement of Mr. James on October 15, 2002. **(Exhibit B)**. Mr. James clearly stated that Mr. Gasowksi was the passenger. **(Id)**. Mr. Varblow also indicated his understanding that Mr. Gasowski was the passenger. **(Id)**. On October 16, 2002, State Farm took the recorded statement of Mr. Gasowski. **(Exhibit C)**. Mr. Gasowski clearly indicated that he was the passenger on the jet-ski. **(Id)**. Other witnesses were also identified and gave statements; State Farm had access to these statements from the outset and took exclusive possession of the jet-ski.

After State Farm's investigation, in November, 2002, criminal charges were brought against Mr. Gasowski at the behest of State Farm. Mr. Gasowski was charged with operating the jet-ski under the influence of alcohol contrary to MCL 324.80176(1).

(Exhibit D). During Mr. Gasowski's criminal trial, Mr. Capps was in attendance and had several meetings with the prosecutor. **(Exhibit E, p 46-50)**. In fact, Mr. Capps was present for every day of the trial, and had at least one closed-door meeting with the prosecutor. During the trial, Mr. James testified under oath that he was driving the jet-ski, and an expert witness testified that Mr. Gasowski could not have been driving the jet-ski. The jury acquitted Mr. Gasowski of this charge, finding that he was not the driver. During his deposition, Mr. Capps testified:

> Q. Now, you disagree with the jury's finding that Mr. Gasowski was not the driver. Correct?
>
> A. Yes.
>
> Q. So the jury was wrong. Correct?
>
> * * *
>
> A. I would guess I would say yes then.

(Exhibit E, p 172).

On January 10, 2003, Mr. Gasowski filed an action in St. Clair County Circuit Court, Case No. 03-0101-NO (the "negligence action") naming as defendants Mr. James and Mr. Silvestri. **(Exhibit F)**. Mr. Silvestri was insured under a boat owner's policy through State Farm with a $500,000 limit of liability. **(Exhibit G)**. Mr. Silvestri was the owner of the jet-ski which Mr. James was driving. Under the terms of the policy, Mr. James qualified as an "insured" for the reason that he was operating the jet-ski with Mr. Silvestri's permission. The policy also provided that "[i]f a loss covered by this policy is also covered by other insurance, we will use this formula to determine our payment:

> a. divide the applicable coverage limit of this policy by the total amount of insurance covering the loss;
>
> b. multiply the result by the amount of the loss;
>
> c. the answer is our amount of payment.

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(Id, p 8). The policy also provides that "[t]he injured person, or, when appropriate, someone acting on behalf of that person, shall:

a. give us written proof of claim, under oath if required, as soon as practicable;

b. execute authorizations to allow us to obtain copies of medical reports and records; and

c. submit to physical examination by a physician selected by us when and as often as we reasonably require.

(Id). This provision allows State Farm to conduct EUOs.

Mr. James was insured under a boat owner's policy through Safeco Insurance Company ("Safeco") covering Mr. James's jet-ski which was disabled and not in use at the time of the jet-ski accident. **(Exhibit H)**. The Safeco policy had a $300,000 limit of liability and provided coverage to Mr. James for any liability for which he became legally responsible that resulted from the use of a non-owned boat (or jet-ski) used with the permission of the owner. The Safeco policy also provided that "[t]his insurance is excess over any other valid and collectible insurance except insurance written specifically to cover as excess over the limits of liability that apply in this policy." **(Id, p 6)**.

Mr. James was also insured under a homeowner's policy through Auto Club Insurance Association ("ACIA") with a $300,000 limit of liability. **(Exhibit I)**. The ACIA policy also provided:

> If at the time of loss there is other insurance in the name of an Association or Corporation of Property Owners or Tenants covering the same property covered by this Policy, the insurance afforded by this Policy shall be excess over the amount recoverable under such other insurance. Otherwise, if both this and other insurance apply to a loss, we will pay our share. Our share will be the proportionate amount that this insurance bears to the total amount of all applicable insurance. However, if the other insurance is specifically written as excess insurance over this Policy, the Limits of this Policy apply first.

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(Id, p 14).

The negligence action specifically alleged that "Gasowski was a passenger on a jet ski . . . which was being operated by James and owned by Silvestri." **(Exhibit F, ¶ 7)**. State Farm assumed the defense of Mr. James and Mr. Silvestri in the negligence action by hiring attorney Timothy Egerer of the law firm Romain, Kuck & Egerer ("State Farm's retained counsel").

State Farm's retained counsel continued to represent Mr. James. State Farm's retained counsel was representing Mr. James at the time Mr. James's "Responses to Request for Admissions" were filed. **(Exhibit J)**. Mr. James admitted that Mr. Gasowski was the passenger and that he was the driver of the jet-ski. **(Id)**. State Farm's retained counsel was representing Mr. James when State Farm's retained counsel moved for a protective order to prevent Mr. Gasowski from taking the depositions of State Farm employees. **(Exhibit K)**. State Farm's retained counsel was representing Mr. Silvestri when Mr. Silvestri admitted, through his response to request for admissions, that Mr. James was driving the jet-ski. **(Exhibit L)**.

On June 23, 2003, the trial court entered an Order for Substitution of Attorneys for Mr. James because State Farm wrongfully refused to continue to defend Mr. James. **(Exhibit M)**. Though the allegations of the negligence action had not changed in any way, and State Farm had all relevant information since before the negligence action was filed, State Farm withdrew its defense of Mr. James, claiming that Mr. James was not the driver of the jet-ski. State Farm reached this conclusion unilaterally. In fact, there has never been a finding by any court or jury that Mr. Gasowski was driving the jet-ski. State Farm never instituted a declaratory action to determine whether Mr. James was driving the jet-ski. Instead, Mr. Capps testified that "[t]he majority of the evidence that

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[State Farm had] indicates that [Mr. James] was not the driver, therefore, was not an insured under the policy." **(Exhibit E, p 33)**. Therefore, State Farm, based upon nothing more than its own opinion, withdrew its defense of Mr. James. Interestingly, evidencing the fallacy of State Farm's position, Mr. Capps testified:

Q. And is there still a question as to who the driver of the watercraft was?

A. No.

Q. You're aware that Mr. James has testified that he was the driver of the watercraft at the time of the accident?

A. Yes.

Q. You witnessed him so testify under oath, did you not?

A. Yes, I did.

Q. Are you aware that under our legal system when there's contradictory testimony that that is what we call a fact question?

A. Yes.

Q. Is there a fact question as to who the driver was?

A. I suppose there is.

Q. Isn't it true, sir, that your company is obligated to defend if there's an allegation that falls within the coverage when there's a fact question as to what the facts are?

A. I would say yes.

Q. And isn't it true that your company breached the contract when it withdrew Mr. James' defense?

A. I don't believe so, no.

(Exhibit E, p 29-30).

Based upon the fact that State Farm had wrongfully withdrawn its defense of Mr. James, Mr. James instituted Case Number 03-2466-NZ against State Farm, Mr. Silvestri

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and Mr. Gasowski, seeking a declaration that State Farm breached its duty to defend ("the declaratory judgment action" or "DJA"). Specifically, the DJA alleged that "Defendant State Farm's conduct constitutes a beach of contract and a violation of the implied duty of good faith and fair dealing."

State Farm's retained counsel continued to represent Mr. Silvestri in the negligence action. Safeco, who insured Mr. James under a boat owner's policy, provided a defense to Mr. James.[1] The case proceeded to case evaluation, and the evaluators unanimously evaluated the case at $700,000. Mr. Gasowski filed a motion for summary disposition in the negligence action as to liability. Unsurprisingly, Mr. Gasowski's motion was vigorously opposed; in fact, Mr. James and Mr. Silvestri each filed their own counter-motions for summary disposition.

The trial court heard oral arguments on the dueling motions for summary disposition on June 14, 2004. (**Exhibit N**). The trial court granted Mr. Gasowski's motion for summary disposition, and denied Mr. James and Mr. Silvestri's cross-motions, after finding that Mr. James was the driver of the jet ski at the time of the accident (**Exhibit O**).

In his pre-trial statement, Mr. James stated that "plaintiff, David Gasowski, was a rear seat passenger at the time that this accident occurred" (**Exhibit P**). For his part, Mr. Silvestri, still being represented by State Farm's retained counsel, stated that "Richard James, with the Plaintiff, David Gasowski, as a rear-seat passenger, was operating the second jet ski." (**Exhibit Q**). These documents, coupled with the trial court's decision to grant summary disposition to Mr. Gasowski, make it clear that the fact

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[1] Safeco later intervened as a party plaintiff in the DJA.

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that Mr. James was driving the jet-ski had been conclusively established. Trial in the negligence action was set to begin on November 30, 2004.

Before trial began, however, the negligence action was settled, and, on November 17, 2004, the negligence action was dismissed with prejudice and without costs. (**Exhibit R**). In connection with dismissal, the parties executed a "Release and Settlement Agreement" (the "Agreement"). (**Exhibit S**). The Agreement was drafted by State Farm's retained counsel on behalf of State Farm, and was executed by all the parties. (**Exhibit S**). The Agreement stated, in pertinent part:

> [T]he Plaintiff, the Defendants, and the Insurers agree as follows:
>
> 1. Within ten (10) days of the full execution of this Release and Settlement Agreement and Stipulation and Order for Dismissal of the primary action by all authorized signatories, the Plaintiff will receive the sum of Six Hundred Thousand and 00/100 ($600,000.00) Dollars to be paid equally by each of the three aforementioned insurers, to wit: $200,000.00 each.
>
> 2. If it is **determined** in the Declaratory Action that Richard W. James was the driver of the jet ski at the time of the August 31, 2002 occurrence, following the entry of a final order, then Plaintiff shall receive an additional One Hundred Thousand and 00/100 ($100,000.00) Dollars to be paid equally by each of the three Insurers, to wit: Thirty Three Thousand Three Hundred thirty Three and 00/100 ($33,333.00) Dollars within ten (10) days of the issuance of the final Order.
>
> 3. However, if it is **determined** in the Declaratory Action that Richard W. James was not the driver of the jet ski at the time of the August 31, 2002 occurrence, then Plaintiff shall not receive any further monies from the Defendants or their Insurers.
>
> The undersigned further declare that the terms of this Release and Settlement Agreement have been completely read and are fully understood and voluntarily accepted for the purpose of making a full and final compromise, adjustment and settlement of any and all tort claims, disputed or otherwise, on account of the damages above mentioned and for the express purpose of precluding forever any additional tort claims arising out of the aforesaid personal watercraft/jet ski accident which forms the basis of the primary lawsuit.

(Exhibit S)(emphasis added). Thus, the Agreement provided for additional sums to be paid to Mr. Gasowski if it was **"determined"** in the DJA that Mr. James was the driver of the jet-ski.

In November, 2004, Mr. Gasowski commenced an action against State Farm, alleging breach of contract, breach of the duty of good faith and fair dealing, libel & slander, malicious criminal prosecution, malicious civil prosecution, intentional infliction of emotional distress, breach of confidentiality, and collateral estoppel ("the Gasowski action"). **(Exhibit T)**.

State Farm did not file a declaratory action to seek a determination of whether Mr. James was the driver of the jet-ski. The DJA was filed by Mr. James against State Farm for breach of the duty to defend. The DJA was litigated with the interests of State Farm, Safeco, and ACIA being represented. Mr. Gasowski's interests were also represented. The DJA was pending for approximately seventeen months, during which time the parties engaged in discovery and numerous motions were filed and decided. The issue of collateral estoppel was raised between counsel on several occasions, and by the court during pre-trial conferences on August 25, 2004 and November 23, 2004. Counsel for State Farm never raised the Agreement as any kind of bar to application of collateral estoppel, or took any steps to preclude the parties from raising collateral estoppel.

In February 2005, Mr. Gasowski filed his "Motion for Summary Disposition Based on Collateral Estoppel" in the DJA. (**Exhibit U**).The motion sought judicial recognition of the fact that the issue of who was driving the jet-ski at the time of the accident had already been resolved in the negligence action, and that collateral estoppel should determine that issue in the DJA. Safeco concurred in the motion. (**Exhibit V**).

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State Farm filed a response to the motion. Its arguments in opposition to the motion mirror the arguments twice made to the Court of Appeals and now to this Court. (**Exhibit W**). State Farm's response to Mr. Gasowski's motion for summary disposition did **not** argue that the Agreement barred collateral estoppel, or that the parties in any way agreed to waive collateral estoppel. (**Id**).

Oral argument on Mr. Gasowski's motion for summary disposition was heard on April 11, 2005. (**Exhibit X**). Attorneys for State Farm, Safeco, Auto Club, and Mr. Gasowski were present. State Farm argued, for the first time, that the Agreement barred collateral estoppel, and then, only as an afterthought. (**Exhibit X**). After allowing each party an opportunity for oral argument, the trial court ruled, in pertinent part, that:

> This Court recognizes at the time of the jet ski, jet ski accident, just two people were involved and both were injured. One was the driver and one was the passenger. In Case Number 03-0101 [the negligence action], Gasowski versus James, this Court ruled that Gasowski was not the driver. This Court finds that the Doctrine of Collateral Estoppel applies in this case, in the case of James versus State Farm.

(**Exhibit X** at 19).

Following the trial court's grant of summary disposition to Mr. Gasowski, the "Order Granting David Gasowski's Motion for Summary Disposition Based on Collateral Estoppel" was entered on April 26, 2005 (**Exhibit Y**), and the "Order Granting Plaintiff Safeco Insurance Company of America's Motion for Summary Disposition Based Upon Collateral Estoppel" was entered on April 29, 2005 (**Exhibit Z**).

On May 17, 2005, approximately two weeks after the trial court's decision on Mr. Gasowski's motion, State Farm filed a Claim of Appeal from the orders granting summary disposition to Mr. Gasowski and State Farm. State Farm untimely submitted its brief, and thus forfeited its right to oral argument.

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After the Claim of Appeal was filed, State Farm paid $100,000 to Mr. Gasowski to settle the Gasowski action, which was still pending. **(See Exhibit 1**, Settlement Agreement). State Farm, by way of this $100,000 payment, acknowledged that the issue of whether Mr. James was driving the jet-ski had been "determined." Indeed, the settlement agreement specifically noted that the $100,000 payment was made with reference to the insurers obligations under the prior Agreement. **(Id)**.

On appeal to the Court of Appeals, State Farm raised three arguments: 1) that the parties waived collateral estoppel in the Agreement, 2) that application of collateral estoppel was erroneous because State Farm was neither a party nor a privy in the negligence action, and 3) that application of collateral estoppel was somehow prejudicial. The trial court rejected these arguments, and the Court of Appeals did the same. **(Exhibit 2)**.

On February 2, 2006, the last day on which an application for leave to appeal could be filed, State Farm filed an "Application for Leave to Appeal." Its application failed to identify the grounds for the application as required by MCR 7.302(B), and, again, did no more than reiterate the same arguments it made to the trial court, on appeal, and in its motion for reconsideration. Nevertheless, on June 15, 2007, this Court ordered the parties to submit Briefs addressing the following issues: (1) whether State Farm, by failing to plead release as an affirmative defense in this declaratory relief action, waived its right to oppose plaintiffs' attempt to invoke offensive collateral estoppel as inconsistent with the terms of the parties' release and settlement agreement in the negligence action;(2) whether, for purposes of collateral estoppel, the identity of the jet-ski driver was actually litigated and determined by a final judgment in the negligence action; (3) whether, for purposes of collateral estoppel, State Farm was a party, or in

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privity with a party, to the negligence action; (4) how should an insurer proceed when it believes its insured is committing fraud to invoke coverage, and does that depend on whether the insurer learns of the conflict of interest during the course of the litigation; and (5) if an adverse judgment procured by fraud of the insured is entered, whether the insurer is estopped from contesting liability.

For this Court's convenience, below is a time line of the relevant events which occurred in this case.

Date(s)	Action(s)
8/31/02	Jet-ski accident occurs
8/31/02-11/02	State Farm takes possession of jet-ski, takes witness statements and conducts investigation
11/02	Mr. Gasowski charged with operating under the influence and is later acquitted
1/10/03	Negligence action filed, State Farm's retained counsel representing Mr. James and Mr. Silvestri
1/10/03-6/23/03	State Farm's retained counsel defends case, oversees admissions by Mr. James and Mr. Silvestri that Mr. James was the driver
5/5/03	Mr. Gasowski acquitted of criminal charges
6/23/03	State Farm withdraws defense of Mr. James
9/03	Mr. James files DJA
6/04	Trial court grants Mr. Gasowski's MSD against Mr. James and Mr. Silvestri
11/17/04	Negligence action settled, Agreement signed
11/04	Mr. Gasowski files suit against State Farm
2/05	Mr. Gasowski files MSD based on collateral estoppel - State Farm responds but doesn't raise Agreement

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4/11/05	Trial court hears oral argument and grants MSD on collateral estoppel
5/17/05	Claim of Appeal
5/05	State Farm pays Gasowski $100,000 and settles Gasowski action
11/8/05	COA Opinion

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ARGUMENT

1. Introduction

This action, at its core, is really a dispute between Safeco and State Farm with respect to each insurer's proportionate share of the $700,000 paid to Mr. Gasowski. ACIA made a payment of at least $200,000[2] and did not participate in the Court of Appeals and has not participated in this Court. After State Farm wrongfully withdrew its defense of Mr. James, Safeco assumed Mr. James's defense costs and then paid at least $200,000 towards the settlement. The ACIA and Safeco policies each had a $300,000 limit of liability. The State Farm policy had a $500,000 limit of liability. This action is more about Safeco's attempt to recover the amounts it paid for which State Farm, due the its policy language and the fact that it breached its duty to defend, was liable, than it is about State Farm's imagined theory of "collusion."

In this regard, each of the three insurance policies at issue contains an "other insurance clause." In Federal Kemper Ins Co, Inc v Health Ins Administration Co, Inc, 424 Mich 537; 383 NW2d 590 (1986), this Court recognized that "other insurance" clauses fall into three general categories:

1. A pro-rata clause, which purports to limit the insurer's liability to a proportionate percentage of all insurance covering the event;

2. An escape or no-liability clause, which provides that there shall be no liability if the risk is covered by other insurance; and

3. An excess clause, which limits the insurer's liability to the amount of loss in excess of the coverage provided by the other insurance.

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[2] It is unknown whether ACIA and Safeco paid 1/3 of the $100,000 State Farm paid to Mr. Gasowksi after it was determined that Mr. James was the driver.

Id at 542. In this case, the State Farm and ACIA policies contain "pro-rata" clauses, **(Exhibit G, I)**, while the Safeco policy contains an "excess clause." **(Exhibit H)**.

In St Paul Fire & Marine Ins Co v American Home Assurance Co, 444 Mich 560; 514 NW2d 113 (1994), this Court considered whether to adopt the minority rule that views all "other insurance" clauses as irreconcilable and prorates liability among all insurers, or to adopt the majority rule that endeavors to reconcile the competing clauses if possible. This Court adopted the majority rule, stating: "We do not view 'other insurance' clauses as being automatically irreconcilable and choose not to adopt a rule that requires this Court to automatically override the contractual language and, perhaps, the negotiated intent of the parties." Id at 578. However, this Court noted that, when faced with competing "other insurance" clauses which cannot be reconciled, liability should be apportioned between the insurers. Id. Therefore, under the rule of law as stated in St. Paul, the competing "other insurance" clauses must be reconciled.

The issue of priority among the insurers, even though it is the central issue of the DJA, has not been presented to the Court in this Application. However, despite State Farm's allegations and rhetoric, the priority of the insurers is the underlying, central issue presented in this case. Nevertheless, Mr. Gasowski now turns to the questions presented by this Court.

2. *State Farm, by failing to plead release as an affirmative defense in this declaratory relief action, waived its right to oppose plaintiffs' attempt to invoke collateral estoppel*

This Honorable Court has asked the parties to brief several issues, some of which were not presented to either the trial court or the Court of Appeals. The first of these

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issues is whether State Farm, by failing to plead release as an affirmative defense, waived its right to oppose collateral estoppel. MCR 2.111(F)(3) provides:

> Affirmative defenses must be stated in a party's responsive pleading, either as originally filed or as amended in accordance with MCR 2.118. Under a separate and distinct heading, a party must state the facts constituting
>
> (a) an affirmative defense, such as contributory negligence; the existence of an agreement to arbitrate; assumption of risk; payment; **release**; satisfaction; discharge; license; fraud; duress; estoppel; statute of frauds; statute of limitations; immunity granted by law; want or failure of consideration; or that an instrument or transaction is void, voidable, or cannot be recovered on by reason of statute or nondelivery;
>
> (b) a defense that by reason of other affirmative matter seeks to avoid the legal effect of or defeat the claim of the opposing party, in whole or in part;
>
> (c) a ground of defense that, if not raised in the pleading, would be likely to take the adverse party by surprise.

(Emphasis added). Moreover, MCR 2.116(D) states, in pertinent part:

> The grounds listed in subrule (c) must be raised as follows:
>
> * * *
>
> (2) The grounds listed in subrule (C)(5), (6), and (7) must be raised in a party's responsive pleading, unless the grounds are stated in a motion filed under this rule prior to the party's first responsive pleading.

MCR 2.116(C)(7), which, pursuant to MCR 2.116(D)(2) must be raised in a party's responsive pleading, states the following defense:

> The claim is barred because of **release**, payment, prior judgment, immunity granted by law, statute of limitations, statute of frauds, an agreement to arbitrate, infancy, or other disability of the moving party, or assignment or other disposition of the claim before commencement of the action.

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(Emphasis added). Michigan law is clear that a failure to raise release as an affirmative defense in a party's first responsive pleading results in a waiver of said defense. Farmers Ins Group v Clear, 94 Mich App 655; 290 NW2d 51 (1980).

With regard to this argument, the Court of Appeals stated:

> Under MCR 2.111(F), an affirmative defense must be raised in a responsive pleading or by motion as provided by the court rules or it is deemed waived. . . State Farm filed affirmative defenses in response to the complaint but failed to raise the affirmative defense of prior release. . .
> And while failure to properly plead an affirmative defense may be excused on the basis that support for the defense was only later discovered, the defense must nevertheless be asserted within a reasonable time after discovering it and the delay in assertion of the defense must not unfairly prejudice the opposing party. [Citation omitted]. Here, the defense was not asserted within a reasonable time after discovering it. A representative of State Farm signed the Release on September 30, 2004, but State Farm failed to bring it to the attention of the court until the April 11, 2005 hearing on summary disposition. Notably, State Farm filed a written motion in opposition to summary disposition on March 14, 2005, but failed to raise the issue of the release. Therefore, we decline to address this issue.

(Exhibit 2, p 3).

State Farm's conduct in this litigation cannot be ignored as it plays a large part in the disposition of this legal issue. Prior to the negligence action being filed, State Farm took possession of the jet-ski and conducted a full investigation. State Farm did not institute a declaratory action or conduct EUOs. State Farm acknowledged its obligation to defend Mr. James. State Farm controlled the defense of Mr. James and Mr. Silvestri in the negligence action until it wrongfully withdrew its defense of Mr. James. The defense was withdrawn based solely upon State Farm's claim that Mr. James was not the driver of the jet-ski. However, the allegations of the negligence action did not change, and State Farm had known all relevant information because of its investigation prior to the filing of the negligence action. After breaching its duty to

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defend, State Farm then entered into the Agreement, which was drafted by State Farm's retained counsel. The Agreement provided that additional payments would be made to Mr. Gasowski if it was "determined" that Mr. James was driving the jet-ski. If State Farm was so sure that Mr. Gasowski was driving the jet-ski, then why enter into such an Agreement? Moreover, if State Farm was so certain that Mr. Gasowski was driving the jet-ski, then why pay Mr. Gasowski the additional $100,000?

In any event, even after the Agreement was signed, State Farm did not raise the Agreement as a defense in the DJA. In fact, after Mr. Gasowski filed a motion for summary disposition based on collateral estoppel, State Farm still **did not raise the Agreement**! State Farm did not even attach the Agreement to its response to Mr. Gasowski's motion for summary disposition. **(Exhibit U)**.

It was not until the end of oral argument on Mr. Gasowski's motion for summary disposition that State Farm even mentioned the Agreement to the trial court. **(Exhibit X)**. This is completely different from the situation presented to the Michigan Court of Appeals in Meridian Mut Ins Co v Mason-Dixon Lines, Inc (On Remand), 242 Mich App 645; 620 NW2d 310 (2000). In Meridian, the Court of Appeals observed, and held that

> the available record indicates that defendant discovered the existence of the release during the course of discovery and thereafter moved for summary disposition based on the release. Plaintiffs never disputed defendant's assertion that it moved for summary disposition based on the release shortly after discovering the existence of the release, and plaintiffs did not before the district court challenge the timeliness of defendant's claim of release. Plaintiffs neither now nor before the district court set forth any allegation that defendant's delayed assertion of the release defense unfairly surprised them or otherwise prejudiced them. Because (1) it appears that defendant moved for summary disposition based on the release within a reasonable time of discovering the release and (2) no indication exists that plaintiffs suffered any unfair prejudice, [citation omitted], we conclude that defendant's failure to assert the release in its first responsive pleading did not prevent it from subsequently raising the issue.

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Id at 648.

In this case, however, State Farm, even though it clearly knew of the existence of the Agreement (State Farm's retained counsel drafted and State Farm signed the Agreement), did not even raise the Agreement in response to Mr. Gasowski's motion for summary disposition. Therefore, the Court of Appeals reached the correct conclusion. Pursuant to Michigan law, State Farm waived any right to rely on the Agreement by failing to raise it until the conclusion of oral argument on the motion for summary disposition. Meridian, supra.

Additionally, even if State Farm had not waived its ability to assert the Agreement (although it clearly did), the Agreement doesn't help State Farm. The Agreement is a contract and, as this Court has so often indicated, a contract must be enforced pursuant to its plain and unambiguous language. Rory v Continental Ins Co, 473 Mich 457; 703 NW2d 23 (2005). In this case, the Agreement clearly provides the following language:

> [T]he Plaintiff, the Defendants, and the Insurers agree as follows:
>
> 1. Within ten (10) days of the full execution of this Release and Settlement Agreement and Stipulation and Order for Dismissal of the primary action by all authorized signatories, the Plaintiff will receive the sum of Six Hundred Thousand and 00/100 ($600,000.00) Dollars to be paid equally by each of the three aforementioned insurers, to wit: $200,000.00 each.
>
> 2. If it is **determined** in the Declaratory Action that Richard W. James was the driver of the jet ski at the time of the August 31, 2002 occurrence, following the entry of a final order, then Plaintiff shall receive an additional One Hundred Thousand and 00/100 ($100,000.00) Dollars to be paid equally by each of the three Insurers, to wit: Thirty Three Thousand Three Hundred thirty Three and 00/100 ($33,333.00) Dollars within ten (10) days of the issuance of the final Order.
>
> 3. However, if it is **determined** in the Declaratory Action that Richard W. James was not the driver of the jet ski at the time of the August 31, 2002 occurrence, then Plaintiff shall not receive any further monies from the Defendants or their Insurers.

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(Exhibit S)(emphasis added).

Thus, the Agreement provided for additional sums to be paid to Mr. Gasowski if it was **"determined"** in the DJA that Mr. James was the driver of the jet-ski. The word "determined" is not defined in the Agreement. Therefore, it is appropriate to consult a dictionary. Popma v Auto Club Ins Ass'n, 446 Mich 460, 469-70; 521 NW2d 831 (1994). Merriam-Webster Dictionary defines "determine" as, *inter alia*, "to find out or come to a decision about by investigation, reasoning, or calculation." http://www.m-w.com (accessed August 1, 2007).

Applying this definition, it is clear that it was "determined" in the DJA that Mr. James was the driver of the jet-ski at the time of the accident. The trial court clearly came to a decision about the identity of the driver by "investigation, reasoning, or calculation." The trial court, after thorough briefing by all parties and thorough analysis, reached the decision that Mr. James was the driver. While the underpinning of the trial court's decision was the application of collateral estoppel, this does not alter the fact that, pursuant to the clear language of the Agreement, the trial court "determined" that Mr. James was the driver.

Additionally, State Farm has admitted that the issue of whether Mr. James was driving has been "determined." State Farm paid the additional $100,000 to Mr. Gasowski **(Exhibit 1)**, which was precisely the amount Mr. Gasowski would receive if it was "determined" that Mr. James was the driver. This makes it clear that even State Farm agrees that it has been "determined" that Mr. James was the driver.

This Court has stated, on multiple occasions, that it will not read language into a contract which is not contained therein. Rory, supra; Klapp v United Ins Group

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Agency, 468 Mich 459, 467; 663 NW2d 447 (2003). If State Farm had intended that collateral estoppel would not apply to the question of who was the driver of the jet-ski, its counsel who drafted the Agreement could have requested the insertion of such a provision which he didn't. Indeed, the Agreement was drafted by and experienced State Farm attorney who was no doubt familiar with the doctrine of collateral estoppel. Indeed, Safeco and ACIA both agree that collateral estoppel applies. The parties chose not to include this language in the Agreement, and is not within this Court's province to insert such language. Accordingly, even if State Farm had not waived reliance on the Agreement (even though it clearly did) it would make no difference to this Court's conclusion. Application of collateral estoppel to the determination of whether Mr. James was driving the jet-ski is not inconsistent with the terms of the Agreement. Accordingly, the Application should be denied.

2. *The identity of the jet-ski driver was actually litigated and determined by a final judgment in the negligence action*

The second issue presented by this Court is whether the identity of the jet-ski driver was actually litigated and determined by a final judgment. It must be kept in mind that the Agreement refers to "determined" and not "litigated." The answer to this question is clearly, yes. While both a jury (in Mr. Gasowski's criminal trial) and a judge (in the negligence action) reached the decision that Mr. James was the driver of the jet-ski, State Farm, again in dereliction of its contractual duties, simply would not accept these conclusions. Instead, State Farm has invented a conspiracy theory and accused Mr. Gasowski, Mr. James, and Mr. Silvestri of collusion with no factual basis. Yet, at his deposition, State Farm's employee, Jerry Capps, admitted that State Farm held the

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belief that no insurance fraud occurred. Mr. Capps clearly testified that no insurance fraud was committed:

Q. Well, did you conclude that there was insurance fraud here?

A. No.

* * *

Q. Was your conclusion Mr. James committed insurance fraud?

A. No.

(Exhibit E, p 51, 117).

Nevertheless, the question of whether the identity of the jet-ski driver was determined in the negligence action is relatively straightforward. It is axiomatic that a motion for summary disposition is the procedural equivalent of a trial on the merits. The Mable Cleary Trust v The Edward-Marlah Muzyl Trust, 262 Mich App 485; 686 NW2d 770 (2004); Capital Mortgage Corporation v Coopers & Lybrand, 142 Mich App 531, 536; 369 NW2d 922 (1985); City of Detroit v Nortown Theatre, Inc, 116 Mich App 386, 392; 323 NW2d 411 (1982). In the negligence action, the court heard oral arguments on motions for summary disposition. In fact, Mr. Gasowski filed a motion for summary disposition as to liability, and Mr. James and Mr. Silvestri each filed a counter-motion for summary disposition. The fact that the negligence action was hotly contested with cross-motions for summary disposition further belies State Farm's unsupported argument of collusion.

Nevertheless, the motions for summary disposition were all designed to determine whether Mr. James was liable for negligence. To have collateral estoppel effect, the issue of who was driving the jet-ski must have been essential to the resulting judgment. Eaton County Road Commissioners v Schultz, 205 Mich App 371; 521 NW2d

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847 (1994). It is beyond argument or citation that, for Mr. James to have been negligent, he must have been driving the jet-ski. It is simply impossible for Mr. James to have breached his duty of care to Mr. Gasowski if Mr. James was not the driver of the jet-ski. Accordingly, the question of whether Mr. James was the driver of the jet-ski was a "question of fact essential to the judgment," and therefore was actually litigated and necessarily decided by the trial court. Id. Quite simply, the trial court could not have granted summary disposition without a determination that Mr. James was the driver. No appeal was taken of the trial court's decision in the negligence action that Mr. James was the driver. Accordingly, this element of collateral estoppel is clearly satisfied.

More importantly, this Court must be wary of State Farm's attempt to paint Mr. Gasowski, Mr. James, and Mr. Silvestri as co-conspirators in some elaborate scheme. As noted above, State Farm has already admitted that it believed that no insurance fraud occurred. **(Exhibit E, p 117)**. The question then becomes, why would State Farm allege a systematic scheme on the part of these three individuals to conceal who was the driver? In fact, State Farm can offer this Court - just as it could offer the trial court and the Court of Appeals - nothing more than its rogue Claims Specialist's[3] and counsel's opinion that there was some type of collusion. Fortunately, mere speculation and conjecture cannot carry the day in this or any other Court. Cloverleaf Car Co v Phillips Petroleum Co, 213 Mich App 186, 192-93; 540 NW2d 297 (1995).

Additionally, even if the identity of the driver was not actually litigated (although it clearly was), State Farm would nevertheless be barred from denying liability under the policy. Under Michigan law, when an insurer fails to fulfill its duty to defend an insured,

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[3] Mr. Capps had previously worked for State Farm in Virginia and shortly after coming to Michigan he was charged with carrying a concealed weapon without a permit, but pled guilty to failing to register a firearm. **(Exhibit E, p 125)**. See Oakland County Circuit Court Case Number 2001-180746-FH.

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it becomes liable for the full amount of the insured's liability, even if the liability arises by way of settlement or consent judgment. Alyas v Gillard, 180 Mich App 154, 160; 446 NW2d 610 (1989). Indeed, the Michigan Court of Appeals has stated that when an insurer breaches its duty to defend, it is "bound by any reasonable settlement entered into in good faith between the insured and the third party." Id.

In this case, it is clear that State Farm breached its duty to defend Mr. James. The duty to defend arises when the allegations of the complaint even arguably come within the policy coverage. American Bumper & Mfg Co v Hartford, 452 Mich 440, 450; 550 NW2d 475 (1996). In this case, it is undisputed that State Farm would owe primary coverage to Mr. James if Mr. James was the driver of the jet-ski. **(Exhibit G)**. It is also undisputed that the negligence action alleged that Mr. James was the driver of the jet-ski. **(Exhibit F)**. Thus, there can be no doubt that State Farm owed a duty to defend to Mr. James. State Farm acknowledged this fact by undertaking the defense of Mr. James. It is likewise undisputed that State Farm withdrew its defense of Mr. James even though the allegations of the negligence action had not changed and State Farm had all information available prior to the filing of the negligence action.

Michigan law is clear that an insurer is obligated to defend "until the claims against the policyholder are confined to those theories outside the scope of coverage under the policy." American Bumper, supra. Because State Farm withdrew its defense of Mr. James while the allegation that he was the driver remained, State Farm breached its duty to defend. Therefore, under Michigan law, it became bound by any judgment, consent decree, or reasonable settlement entered into by Mr. James. Alyas, supra.

In this case, there can be no argument that the eventual settlement of the negligence action was reasonable. State Farm, in fact, participated in the settlement

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negotiations. However, it was not the eventual settlement that renders State Farm liable, but the trial court's finding that Mr. James was liable and, necessarily, was the driver of the jet-ski. Thus, even if the issue of whether Mr. James was driving the jet-ski was not actually litigated (even though it clearly was), State Farm cannot contest liability because it breached its duty to defend.

3. State Farm was a party, or in privity with a party, to the negligence action

Under this prong of the test for collateral estoppel, only parties to the former judgment or their privies may take advantage of or be bound by it. Howell v Vito's Trucking and Excavating Co, 386 Mich 37, 43; 191 NW2d 313 (1971). However, for purposes of collateral estoppel, "substantial identity, not precise identity, is all that is required." Dearborn Heights School District No 7 v Wayne County MEA/NEA, 233 Mich App 120; 592 NW2d 408 (1998)(quoting Local 98 of the United Ass'n of Journeymen & Apprentices of the Plumbing & Pipefitting Industry of the United States & Canada, AFL-CIO v Flamegas Detroit Corp, 52 Mich App 297, 302; 217 NW2d 131 (1974)). The purpose of the substantial-identity rule is to ensure that collateral estoppel is applied only where the interests of the litigating party are adequately represented in the first proceeding. Id. Thus, a nonparty to an earlier proceeding will be bound by the result if that party controlled the earlier proceeding or if the party's interests were adequately represented in the original matter. Id.

As a general rule, once a final judgment has been entered on behalf of the party suing the insured, the insurer may not reopen the factual or legal basis of the judgment when the insured makes a coverage claim. *Windt, Insurance Claims and Disputes* § 6:22 (5th Ed 2007). This is true whether or not the insurer defended the insured and,

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if it did not defend, whether or not such refusal was justified. Id (citing State Farm Mut Ins Co v Christensen, 88 Nev 160 (1972)). It has been stated by a leading treatise that:

> One who has undertaken to indemnify another against loss arising out of a certain claim and has notice and opportunity to defend an action brought upon such claim is bound by the judgment entered in such action, and is not entitled, in an action against him for beach of his agreement to indemnify, to secure a retrial of the material facts which have been established by the judgment against the person indemnified.

Couch on Insurance 3d § 239.73 (2000)(multiple citations omitted).

Michigan law is in accord with this principle. As stated long ago by this Court, "[t]he law abhors multiplicity of suits." Krolik & Co v Ossowski, 213 Mich 1, 7; 180 NW 499 (1920). Thus, it has been held that an insurer who has been given notice and an opportunity to defend and who breaches its duty to defend is bound by the judgment entered. Alyas, supra; Capitol Reprod v Hartford Ins Co, 800 F2d 617 (6th Cir 1986)(applying Michigan law)("Under Michigan law, when an insurer fails to fulfill its duty to defend an insured, it becomes liable for the full extent of the judgment against the insured").

Further, in Aetna Life Ins Co v Maxwell, 89 F2d 988 (4th Cir 1937), the United States Court of Appeals for the Fourth Circuit considered whether an insurer was a "party" or "privy" to the prior suit for purposes of collateral estoppel. The court stated:

> The insurance company, having been notified of the suit against the physician and having participated in the defense of the suit, at least to a limited extent, was indeed bound by the judgment upon the issues at stake therein and estopped to contest the validity thereof. When a person is responsible over to another, either by way of operation of law or by express contract of insurance, and is duly notified of the pendency of a suit and requested to assume the defense, he is no longer regarded as a stranger because he has the right to appear and defend the action, and the judgment, if obtained without fraud or collusion, will be conclusive against him whether he has appeared or not.

Id at 991.

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A similar result should be reached by this Court in this case. As noted by the Court of Appeals:

> Although State Farm was not a named party in the first tort action, mutuality need not be shown and the doctrine of collateral estoppel is applicable when, State Farm, a defendant in the present declaratory action, and James, a defendant in the first tort action, had a relationship such that the liability of State Farm is entirely dependent on the culpability of James in the first action. [Citation omitted]. And while defense counsel's loyalty was to James, and the relationship between State Farm and the defense counsel did not rise to the level of an attorney-client relationship, State farm had the type of relationship with James and the defense counsel that gave it a direct interest in the subject matter such that it is bound by the prior judgment.

(Exhibit 2, p 4).

The Court of Appeals clearly reached the correct result. The allegations of the negligence action gave rise to a duty to defend on the part of State Farm, and thus State Farm controlled the defense of Mr. James. Contrary to State Farm's unsupported representations, it was doing much more than simply "paying the bill." As this Court has stated "[i]t has been appropriately recognized that '[defense counsel] occupies a fiduciary relationship to the insured, **as well as to the insurance company**. . . " Atlanta Int'l Ins Co v Bell, 438 Mich 512, 519; 475 NW2d 294 (1991)(quoting Widiss, *Insurance Law*, p 822, 835-36)(emphasis added). Moreover, as stated by the Michigan Court of Appeals: "[I]nsurers, who in fact do the investigating, in fact choose the counsel, in fact pay the judgment, in fact pay deductible property damage claims and in some instances some medical and hospital expenses, are much more the 'real party in interest' than the named insured." Brown v Spitza, 45 Mich App 97, 105; 206 NW2d 260 (1973). Thus, because State Farm conducted its own investigation even pre-suit and was in a position to control the defense of Mr. James, it therefore follows that it should be bound by an adverse judgment.

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The Restatement (Second) of Judgments supports the rule that collateral estoppel applies under these circumstances. Section 58 of the Restatement (Second) of Judgments states:

> (1) When an indemnitor has an obligation to indemnify an indemnitee (such as an insured) against liability to third persons and also to provide the indemnitee with a defense of actions involving claims that might be within the scope of the indemnity obligation, and an action is brought against the indemnitee involving such a claim and the indemnitor is given reasonable notice of the action and an opportunity to assume its defense, a judgment for the injured person has the following effects on the Indemnitor in a subsequent action by the indemnitee for indemnification:
>
> (a) The indemnitor is estopped from disputing the existence and extent of the indemnitee's liability to the injured person; and
>
> (b) The indemnitor is precluded from relitigating those issues determined in the action against the indemnitee . . .

Moreover, common sense and logic also compel the same result. If an insurer was not bound by the judgment under collateral estoppel, what would stop an insurer from attempting to subsequently relitigate issues determined in negligence actions? Under State Farm's flawed analysis, a liability insurer could allow a judgment to be entered finding its insured liable, and then, instead of indemnifying its insured, could file an action to relitigate the issue of whether the insured was liable! Thus, the doctrine of collateral estoppel is designed specifically to prevent this type of conduct. Multiplicity of lawsuits would be rampant.

Moreover, were this Court to hold that State Farm, because it withdrew its defense, is therefore not bound by the underlying judgment, it would encourage liability insurers to refuse to provide a defense to their insureds and, when an adverse judgment is rendered, attempt to relitigate the underlying issue of liability. This type of reasoning would lead to an absurd result and allow insurers free reign to force their insureds (who

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normally have limited resources) to expend significant resources for which the insurer is contractually liable. As noted by Windt, "allowing the insurer to avoid the collateral estoppel rule unjustly penalizes the insured. It would require the insured to incur the cost of having to relitigate issues that should have already been conclusively established at the insurer's expense." *Windt, supra* at § 6:22 n 6. For these reasons, this Court should find that the Court of Appeals did not err in concluding that State Farm was a "party" to the negligence action for purposes of collateral estoppel.

4. How an insurer should proceed when it believes its insured is committing fraud to invoke coverage

It must again be noted that State Farm had admitted that it does not believe insurance fraud was committed. **(Exhibit E, p 117)**. State Farm conducted an extensive pre-suit investigation and took exclusive possession of the jet-ski. This is a hypothetical question - no such circumstances exist in this case. Thus, this is not a proper case to consider such an issue. In fact, there is simply no evidence, and State Farm has presented none, that any type of collusion was involved. Indeed, Safeco and ACIA also are involved in this action because Mr. James was driving the jet-ski, yet neither of these insurers believe that any collusion took place. In fact, Mr. Capps and State Farm's counsel appear to be the only people who claim that some type of collusion occurred. However, State Farm has admitted that it does not believe that fraud occurred. **(Id)**. The Court of Appeals stated:

> State Farm has failed to provide any authority in support of its claims of collusion and prejudice. It is insufficient for an appellant to merely announce its position and then leave it to this Court to discover and rationalize the basis for its argument or search for authority to support or reject its position. [Citation omitted]. Moreover, State Farm offers nothing more than conjecture and speculation of collusion, which is insufficient to create a question of fact for the jury.

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(Exhibit 2, p 4). The Court of Appeals clearly reached the correct result. As noted, State Farm has never presented any court with any evidence to support its contrived theories of collusion.

State Farm had the opportunity to present some type of evidence to support its imagined theory of collusion on countless occasions. State Farm simply has not presented anything. Nothing was presented to the trial court, even when the trial court specifically asked for it. Nothing was presented to the Court of Appeals. Nothing has been presented to this Court. State Farm had all the information available prior to the negligence action being filed, as a result of its extensive investigation and taking possession of the jet-ski.

Nevertheless, this Court has presented the question of how an insurer should proceed when it believes its insured is committing fraud to invoke coverage. Because of State Farm's wrongful conduct, this is not the correct case to consider this issue. In any event, State Farm should have proceeded consistent with its contractual and common law duties. These duties gave State Farm a multitude of options. State Farm could have taken EUOs pre or post-suit which it didn't. In fact, this Court, in an Opinion authored by Justice Taylor, lauded EUOs as effective tools for insurers to "gather facts so as to discover and eliminate fraudulent insurance claims." Cruz v State Farm Mut Auto Ins Co, 466 Mich 588, 597; 648 NW2d 591 (2002). State Farm was the defendant in Cruz and therefore was aware of this Court's endorsement of EUOs as an effective and "favorable" tool for discovering facts. Id. Indeed, in Cruz, this Court noted that, without EUOs, "insurance carriers would lack important tools with which to root out fraud, as well as the means to responsibly investigate claims." Id at 598 n 14. State

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Farm, even though it conducted an extensive investigation and took exclusive possession of the jet-ski, did not use this "important" tool.

State Farm could also have filed a declaratory action to determine whether its claim was valid. As this Court has noted, the declaratory judgment action is a valuable tool, designed "to enable the parties to obtain an adjudication of their rights before actual injuries or losses have occurred." Detroit Base Coalition for the Human Rights of the Handicapped v Michigan Department of Social Services, 431 Mich 172, 191; 428 NW2d 335 (1988). Yet, State Farm never instituted a declaratory action. Instead, it breached its duty to defend Mr. James, and Mr. James filed the DJA.

Again, it cannot be repeated enough that State Farm has admitted that it did not believe that fraud occurred in this case. **(Exhibit E, p 117)**. Mr. Capps made this abundantly clear in his deposition. What Mr. Capps also made clear is State Farm's belief that it can flaunt its contractual duties, act as a sole fact finder, and generally behave as though it is above the law. Perhaps $5 Billion in net assets last year gives it such a belief. Mr. Capps' testimony is critically important to properly addressing this Court's new hypothetical questions.

Mr. Capps testified that "[t]he duty to defend is based on first party coverage, that if an insured has a suit filed against them the company has a duty to provide them with a defense." **(Id, p 21)**. Mr. Capps' statement is consistent with this state's law that an insurer has a duty to defend if the allegations of the complaint even arguably fall within the coverages provided. American Bumper, supra. However, Mr. Capps' testimony also reveals that State Farm unilaterally decided to breach its duty to defend. Mr. Capps testified:

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Q. How do you justify not defending if there is a fact question as to who was driving and if the Complaint that triggers the defense alleges that Mr. James was driving?

A. Because **our** investigation **to us** reveals that there is not a question as to who was driving. The question comes from Mr. James claiming that he was driving. **We do not believe that he was driving.**

(Exhibit C, p 30)(emphasis added). However, in the very next question posed to Mr. Capps, he admitted that there was additional evidence that Mr. James was the driver - the statement of witness Scottie Stevens, and the testimony of an expert witness at Mr. Gasowski's criminal trial. **(Id)**. Yet, this was not enough for State Farm. State Farm, in complete dereliction of its duties, unilaterally determined that Mr. James was not the driver and breached its duty to defend. The allegations of the underlying complaint had not changed. The facts had not changed. State Farm had possession of the jet-ski and had conducted a thorough investigation of the claim prior to the filing of the negligence action. Mr. Capps even admitted that he had come across numerous cases where State Farm thought the facts were one way and turned out to be wrong. **(Id, p 33)**. Yet State Farm, based upon no actual evidence, terminated the defense of Mr. James. Mr. Capps justified State Farm's breach of its duty by stating: "**[w]e decided** based on the information that Mr. James was not the driver." **(Id, p 34)**(emphasis added).

Apparently, the supposed "information" upon which State Farm based its unilateral decision to breach its duty to defend was a report prepared by a paid expert, Packer Engineering. However, Mr. Capps testified that the report from Packer Engineering states that it was "most likely" that Mr. James was not the driver. **(Id, p 174)**. Mr. Capps admitted that "most likely" was not definitive, **(id)**, and that he never asked anyone from Packer how certain they were about this conclusion, even though such information would be important to him. **(Id, p 175)**.

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Therefore, the facts reveal that State Farm, ignoring all the evidence to the contrary, based its unilateral decision to breach its duty to defend upon a single report from an engineering firm which only states the opinion that it was "most likely" that Mr. James was not driving. Yet, the evidence that Mr. James was driving included another expert's opinion that Mr. James was driving, and several witness statements that Mr. James was driving the jet-ski. State Farm had all of this information prior to the filing of the negligence action. State Farm was given countless opportunities to offer any type of evidence that Mr. James was not the driver, at both the trial court and Court of Appeals, and State Farm offered nothing. State Farm did not present the trial court with any expert report indicating that Mr. James was not the driver. Instead, State Farm, apparently believing that it alone can make factual determinations, merely offered its counsel's unsupported opinions and innuendos that some type of mysterious "collusion" took place. Simply put, State Farm's actions in this case are so egregious and contrary to Michigan law that its Application should be peremptorily denied.

Nevertheless, this Honorable Court has asked the parties to provide guidance on how an insurer should proceed. Given the recitation of State Farm's conduct in this case, it is clear that this is a question which need not be answered in this appeal, because State Farm admitted that it did not believe that fraud occurred. **(Exhibit E, p 117)**. However, if an insurer believes that its insured is committing fraud to invoke coverage, the insurer should act in accordance with its contractual duties and Michigan law. The insurer could conduct an investigation by using EUOs or could file a declaratory judgment action. However, under no circumstances should an insurer act the way State Farm chose to act in this case.

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5. State Farm is estopped from contesting liability under these circumstances

The Court has asked whether an insurer is estopped from contesting liability if a judgment is procured through fraud of the insured. It once again bears repeating that State Farm has admitted that no fraud occurred. **(Exhibit E, p 117)**. This Court has thus asked the parties to address a hypothetical situation. Under the circumstances presented in this case, State Farm is clearly estopped from contesting liability, as described above. State Farm admitted that no fraud occurred, breached its duty to defend without any justification, and, despite being given countless opportunities, could never offer any evidence to support its half-baked "collusion" theory.

Regarding this Court's hypothetical (whether an insurer is estopped from contesting liability if a judgment is procured by fraud), the question cannot be answered without additional information. Because State Farm knew all relevant information before the filing of the suit, requested the prosecutor to bring charges, had its representative attend the criminal trial and meet with the prosecutor behind closed doors, failed to take EUOs, failed to a file a DJA, breached its duty to defend after previously acknowledging such a duty, instructed its chosen counsel to withdraw from representing the insured, and failed to present any evidence to support its theory, the answer clearly would be yes, State Farm is estopped from contesting liability under these circumstances. There is simply nothing to indicate that the judgment was procured by fraud. In fact, State Farm participated in the drafting of the Agreement which settled the negligence action, and then, admitted that the issue of whether Mr. James was the driver had been determined by paying Mr. Gasowski the additional $100,000 he was due under the Agreement! Thus, State Farm is estopped from contesting liability and this Application should be denied.

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VIII. CONCLUSION & REQUEST FOR RELIEF

It should be clear that State Farm has not presented any issues that have not been presented - and definitely and correctly resolved - before. Further, State Farm has not even attempted to demonstrate how any of its issues would have any significant impact on the jurisprudence of the State. For these reasons, Mr. Gasowski respectfully requests that this Honorable Court deny State Farm's "Application for Leave to Appeal," and enter an order reflecting such, together with costs, interest, and attorney fees.

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