

STATE OF MICHIGAN
IN THE SUPREME COURT

EMPLOYERS MUTUAL CASUALTY COMPANY

Plaintiff/Counter-Defendant-Appellee,

v.

HELICON ASSOCIATES, INC., a Michigan corporation, ESTATE OF MICHAEL J. WITUCKI, in its capacity a successor in interest to Michael J. Witucki, a deceased individual,

Defendants/Counter-Plaintiffs,

and

DR. CHARLES DREW ACADEMY, a Michigan public school academy, JEREMY GILLIAM,

Defendants, and

WELLS FARGO ADVANTAGE NATIONAL TAX FREE FUND, a series of the Delaware business trust known as the Wells Fargo Funds Trust, Delaware Business Trust, WELLS FARGO ADVANTAGE MUNICIPAL BOND FUND (in part as successor to the Wells Fargo Advantage National Tax-Free Fund), a series of the Delaware business trust known as the Wells Fargo Funds Trust, a Delaware business trust, LORD, ABBETT MUNICIPAL INCOME FUND, INC., on behalf of its series Lord Abbett High Yield Municipal Bond Fund, a Maryland corporation, PIONEER MUNICIPAL HIGH INCOME ADVANTAGE, a Massachusetts business trust, by Pioneer Investment Management, Inc., its investment advisor,

Defendants-Appellants.

_____ /

Supreme Court
No. _____

Court of Appeals
No. 322215

Wayne County Circuit Court
Case No. 12-002767-CK

APPLICATION FOR LEAVE TO APPEAL BY DEFENDANT-APPELLANT

NOTICE OF FILING SUPREME COURT APPLICATION

EXHIBITS

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I. **STATEMENT IDENTIFYING THE JUDGMENT APPEALED FROM AND RELIEF SOUGHT.**

Defendant-Appellant Funds¹ (the “Funds”), seek leave to appeal from, or peremptory reversal of, the Court of Appeals’ December 1, 2015 Opinion wherein the Court of Appeals affirmed the grant of summary disposition entered in a declaratory judgment action filed by Plaintiff-Appellee Employers’ Mutual Casualty Company (“EMC”). *Employers Mutual Casualty Company v. Wells Fargo*, --- Mich. App. ---; --- N.W.2d ---; published opinion per curiam of the Court of Appeals, issued December 1, 2015 (Docket No 322215) (attached hereto as Ex. A, and referred to herein as the “Opinion”).

The Funds seek reversal of the Opinion and remand directing the Court of Appeals to address those policy exclusions before it on appeal that were not addressed in the Opinion.

This Court has jurisdiction to consider this application pursuant to MCR 7.303(B)(1) and MCR 7.305.

¹ Wells Fargo Advantage National Tax Free Fund (a series of the Wells Fargo Funds Trust, a Delaware business trust), Wells Fargo Advantage Municipal Bond Fund (a series of the Wells Fargo Funds Trust, a Delaware business trust), Lord Abbett Municipal Income Fund, Inc. (on behalf of its series, Lord Abbett High Yield Municipal Bond Fund), and Pioneer Municipal High Income Advantage Trust are referred to herein as the “Funds.”

etc. Courts across the nation have harmonized the coverage grants and fraud exclusions in D&O and E&O policies by recognizing that these policies are intended to cover **negligent** misrepresentation, misstatement and omission claims, while excluding **intentional** misrepresentation and omission claims.

The Opinion eviscerates negligent misrepresentation and omission coverage under Michigan D&O and E&O policies by failing to acknowledge the distinction between negligent and intentional misrepresentation/omission claims. The Funds sought coverage under the EMC Policies for a consent judgment (the “Consent Judgment”) entered under the Connecticut Uniform Securities Act (the “CUSA”) against two of EMC’s insureds.³ The Funds’ CUSA claims were negligence-based—they required no showing of scienter or dishonest intent.⁴ The Funds’ negligence-based Consent Judgment should not have implicated the Fraud Exclusion in the EMC Policies. Neither EMC, nor the Funds, nor the Court of Appeals cited a single case or authority that would support a different conclusion.

Notwithstanding the unanimity of the authority before it, the Court of Appeals held that the Fraud Exclusion in the EMC Policies precludes coverage for the Funds’ negligence-based Consent Judgment. It reasoned that all omissions and untrue statements of material fact are, by definition, “dishonest.” In other words, the Opinion—a published decision that, unless reversed

³ EMC’s insureds were Helicon Associates, Inc. (a Michigan-based charter school management company, referred to herein as “Helicon”) and Michael Witucki (Helicon’s President, referred to herein as “Witucki”).

⁴ *Conn Nat Bank v Giacomi*, 242 Conn 17, 47; 699 A2d 101, 118-19 (1997) (standard of liability under the CUSA is reasonable care); *see also Lehn v Dailey*, 77 Conn App 621, 630; 825 A2d 140, 147-48 (2003) (**rejecting** the argument that Section 36b-29(a)(2) “requires scienter and cannot be predicated on **mere negligence.**”) (emphasis added).

by this Court, will be binding on every trial court to examine the issue—eviscerated the express coverage for misstatements, misleading statements, and omissions in the EMC Policies.⁵

The result reached by the Court of Appeals is not just a contradiction of the weight of authority and controlling Michigan insurance policy construction precedent. Nor is the Opinion a wrong that affects only the Funds. E&O insurance—also known as malpractice, or professional liability insurance—is what doctors, dentists, chiropractors, lawyers, accountants, architects and engineers all rely upon for coverage. All of these professionals are subject to negligent misrepresentation or omission claims based on the advice they give (or fail to give) in the course of their business. If the Opinion is allowed to stand, it jeopardizes the negligent misrepresentation/omission coverage these professionals rely upon to protect both themselves and their clients. The same is true of the negligent misrepresentation/omission coverage in the D&O policies purchased by the officers, directors and board members of schools, charities, clubs and corporations. Even towns, counties, public schools, water and sewer districts and the employees, teachers and elected or appointed officials that work for them—the **target market** for the specific EMC policy form at issue here—will be in jeopardy of losing the negligent misrepresentation/omission coverage they purchased.

Put simply, the Opinion, if not reversed, will expose thousands of Michigan insureds to the very liability they bought insurance to protect against. And the loss suffered by Michigan insureds will result in an improper windfall to insurers, who advertise and underwrite their E&O/D&O (and similar) policies to cover misstatements, misleading statements, and omissions.

⁵ Not even EMC argued for this result. EMC sought to affirm the Trial Court’s decision by urging the Court of Appeals to look beyond the Consent Judgment—as the Trial Court did—to find evidence of intentionally dishonest conduct in the pleadings from the underlying case. But EMC’s argument was directly contrary to the express language of the Fraud Exclusion which required a determination, by “judgment or adjudication,” that EMC’s insureds engaged in dishonest or fraudulent conduct.

The harms that will result from the Opinion if it is allowed to stand need not come to pass. There is only one construction of the EMC Policies that is consistent with controlling Michigan insurance policy construction law. That single interpretation brings Michigan in line with the rule that fraud/dishonesty exclusions in D&O and E&O policies are applicable only to claims requiring a showing of scienter or intent. It also allows this Court to reverse the Opinion and avoid depriving thousands of Michigan insureds of the negligent misrepresentation/omission coverage they rely upon to protect themselves and their clients.

B. MCR 7.305(B)(5) (CLEAR ERROR AND FAILURE TO FOLLOW PRECEDENT).

Leave to Appeal or peremptory reversal of the Opinion is also justified under MCR 7.305(B)(5). This Court has recognized clear rules for interpreting insurance policies. Courts must give effect to all words and phrases in a policy. Courts must not adopt policy interpretations that render coverage illusory. If a policy is susceptible to more than one reasonable interpretation, it is ambiguous and must be construed in favor of coverage. The Opinion violated each of these construction principles. Its conclusion that even negligence-based claims are barred by the Fraud Exclusion renders the EMC Policies' express coverage grant for misstatements, misleading statements and omissions meaningless. It ignored the many cases dictating that the Fraud Exclusion applied only to intentional conduct—cases which, if not dispositive, should have at least indicated that the Fraud Exclusion was susceptible to another reasonable interpretation, requiring it to be construed in favor of coverage. And the Opinion failed to give meaning to the language in the EMC Policies conditioning the application of the Fraud Exclusion on a **determination** (by judgment or adjudication) that EMC's insureds committed acts of fraud or dishonesty. **There was no such determination.** Michigan law has repeatedly recognized that when parties enter into a consent judgment—as they did here—factual issues are neither tried nor conceded.

While the Opinion's conflicts with Michigan law are, by themselves, sufficient to merit this Court's review, the defects in the Opinion don't end there. The Opinion is also internally inconsistent. At one point, the Opinion states that a negligence claim would not trigger the Fraud Exclusion in the EMC Policies. Opinion at p. 4 ("Mere negligence will not trigger the exclusion."). But the Opinion then reaches the exact opposite conclusion—holding that the Funds' negligence-based⁶ CUSA claims are barred by the Fraud Exclusion. *See* Opinion at p. 3-4. Both statements cannot be true.

Any one of the issues identified above is sufficient to justify granting the Funds' Application for Leave to Appeal ("Application"). In sum, granting leave to appeal is now the only way to: 1) preserve the negligent misrepresentation and omission coverage thousands of Michigan insureds count on to protect themselves and their clients; 2) eliminate the unwarranted windfall that will result when insurers rely on the Opinion as a basis for refusing to honor the negligent misrepresentation and omission coverage they sold and issued to Michigan insureds; and, 3) correct the Opinion's clear deviation from controlling Michigan law.

⁶ *See* n. 4 *supra*.

III. STATEMENT OF QUESTIONS PRESENTED FOR REVIEW.

- A. WHETHER THE FRAUD EXCLUSION PRECLUDES COVERAGE FOR NEGLIGENTLY MADE UNTRUE STATEMENTS OR OMISSIONS OF MATERIAL FACT.**

- B. WHETHER A CONSENT JUDGMENT WITH NO FINDINGS OF FACT OR OTHER ADJUDICATIVE TRAITS IS SUFFICIENT TO TRIGGER THE FRAUD EXCLUSION, WHICH EXPRESSLY REQUIRES A “DETERMINATION” OF FRAUDULENT OR DISHONEST CONDUCT BY JUDGMENT OR ADJUDICATION.**

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VII. STATEMENT OF MATERIAL PROCEEDINGS AND FACTS.

A. RELEVANT STIPULATED FACTS.

1. On or about December 15, 2008, the Funds filed suit against Helicon, Witucki and others in the United States District Court for the Eastern District of Michigan, case number 08-CV-15162 (the “Liability Action”). *See* Appellants’ Opening Brief at p. 4. As pertinent here, the Liability Action alleged that Helicon, Witucki and others made material misstatements and/or omissions in connection with the offering and sale of bonds (the “Bonds”) issued to finance the acquisition of Crescent Academy’s (a Michigan charter school) building. *See* Appellants’ Opening Brief at p. 4 (attached hereto as Ex. B); *see also* Stipulation Letter (attached hereto as Ex. C).⁷

2. On April 25, 2012, the United States District Court for the Eastern District of Michigan entered a consent judgment in the Liability Action in favor of the Funds and against Helicon and Witucki, jointly and severally, in the aggregate amount of \$3,387,526 (the “Liability Judgment”). *See* Appellants’ Opening Brief at p. 6; *see also* Consent Judgment at pp. 1-2 (attached hereto as Ex. D).⁸

3. On November 20, 2012, the Court entered a consent judgment in the Liability Action in favor of the Funds and against Helicon and Witucki, jointly and severally, in the aggregate amount of \$873,810.70 for the Funds’ costs and fees. Order, dated November 20, 2012, at pp. 1-2 (the “Fee Judgment”). *See* Appellants’ Opening Brief at p. 6; *see also* Ex. D (Consent Judgment) at pp. 1-2; *see also* Ex. C (Stipulation Letter) at ¶6.

⁷ Attached below as Ex. C to Appellants’ Opening Brief and Ex. A to Funds’ Response to EMC’s Motion for Summary Disposition, dated June 20, 2013.

⁸ Attached below as Ex. E to Appellants’ Opening Brief; and Ex. 4 and 5 to EMC’s Motion for Summary Disposition, dated March 27, 2013; *see also* Funds’ Response to EMC’s Motion for Summary Disposition, dated June 20, 2013, at pp. 5-6.

4. The Liability Judgment and the Fee Judgment (collectively, the “Consent Judgment”) total \$4,261,336.70.⁹ *See* Appellants’ Opening Brief at p. 6; *see also* Ex. C (Stipulation Letter) at ¶6.

5. The Consent Judgment is premised solely on Helicon and Witucki’s liability under the **negligence-based** Connecticut Uniform Securities Act. *See* Appellants’ Opening Brief at pp. 3-5; *see also* Ex. D (Consent Judgment) at pp. 1-2; *see also* Ex. C (Stipulation Letter) at ¶¶6-7.

6. EMC is an insurance company that issued the following insurance policies to Helicon:

- a. Policy No. 1K3-93-27 covering Policy Period from 12/16/07 to 12/16/08 (the “Linebacker Policy”); and,
- b. Policy No. 1M3-93-27 covering Policy Period from 12/16/07 to 12/16/08 (the “Umbrella Policy”).

Collectively, the Linebacker Policy and the Umbrella Policy shall be referred to as the “EMC Policies.” *See* Appellant’s Opening Brief at p. 6; *see also* Ex. C (Stipulation Letter) at ¶1.

7. Helicon and Witucki were both “Insured(s)” under the EMC Policies. *See* Appellant’s Opening Brief at p. 6; *see also* Ex. C (Stipulation Letter) at ¶¶6-7.

8. The Umbrella Policy is what is known as a “following-form” policy. That means that if the Consent Judgment is covered by the Linebacker Policy, but exceeds the limits of the same, then the Consent Judgment is also covered under the Umbrella Policy: 1) to the extent the loss exceeds the available limits of the Linebacker Policy; and, 2) up to the available limits of the Umbrella Policy. Conversely, if the Consent Judgment is excluded from coverage under the

⁹ This amount does not include post-judgment interest.

Linebacker Policy, it is also excluded from coverage under the Umbrella Policy.¹⁰ *See* Appellant's Opening Brief at pp. 6-7; *see also* Ex. C (Stipulation Letter) at ¶ 9.

9. EMC agrees the Consent Judgment is covered, and payable under, the EMC Policies unless one or more of the exclusions identified in EMC's Complaint in the underlying declaratory judgment action (case number 12-002767-CK, Circuit Court, County of Wayne, State of Michigan, the "Underlying Suit") operates to remove the Consent Judgment from coverage. *See* Appellant's Opening Brief at p. 7; *see also* Ex. C (Stipulation Letter) at ¶10.

10. The only exclusion considered by the Court of Appeals, and therefore the only exclusion relevant to this Application is the Fraud Exclusion. *See* Opinion at p.4

B. THE UNDERLYING SUIT.

EMC filed its Complaint in the Underlying Suit on February 28, 2012, alleging that certain exclusions in the EMC Policies removed the Consent Judgment from coverage. *See* Appellant's Opening Brief at pp. 7-8. The applicability of these exclusions was placed before the Trial Court on a series of cross motions for summary disposition, followed by two oral argument sessions. *See* Appellant's Opening Brief at p. 8. On May 27, 2014 the Trial Court granted summary disposition in EMC's favor. *Id.* As pertinent here, the Trial Court found that the Fraud Exclusion barred coverage for the Funds' Consent Judgment. *Id.*

C. THE COURT OF APPEALS PROCEEDING.

The Funds timely filed their Notice of Appeal on June 12, 2014 and their Opening Brief on November 12, 2014. EMC filed its Response Brief on February 9, 2015. The Funds filed their Reply Brief on March 16, 2015. The Court of Appeals granted oral argument, which was

¹⁰ This stipulated fact makes reference to the text of the Umbrella Policy unnecessary. Therefore, all policy citations appearing herein shall be to the Linebacker Policy.

held on October 14, 2015. The Court of Appeals issued the Appellate Opinion on December 1, 2015.

The only exclusion addressed by the Court of Appeals in the Opinion is the Fraud Exclusion which states the EMC Policies do not provide coverage for “any action brought against an ‘insured’ if by judgment or adjudication such action was based on a determination that acts of fraud or dishonesty were committed by the ‘insured.’” *See* Opinion.¹¹ The Court of Appeals held that the Consent Judgment constituted a determination by judgment or adjudication that Helicon and Witucki were liable to the Funds for acts of fraud or dishonesty, and therefore coverage was excluded pursuant to the Fraud Exclusion. *See* Opinion at pp. 3-4. The Court of Appeals stated:

Witucki and Helicon assisted in the offering and sale of bonds to the Funds without the proper authority, resulting in a substantial loss in the value of the investment when the bonds were required to be reissued. Pursuant to the plain language of the above statute, **the consent judgment, by finding a violation of that statute, necessarily found that Witucki and Helicon made “untrue statement[s] of material fact” or “omission[s] to state a material fact.”** The word “dishonest” is defined in *Black's Law Dictionary* (10th ed) as “Deceitfulness as a character trait; behavior that deceives or cheats people; *untruthfulness*; *untrustworthiness*” (emphasis added). **Because statements and representations made by Helicon and Witucki were “untrue,” and those statements and representations comprised the statutory violation, they committed acts of fraud or dishonesty within the meaning of the policy exclusion.**

See Opinion at p. 4. The Court of Appeals held its interpretation did not render coverage under the EMC Policies illusory because “[m]ere negligence will not trigger the exclusion.” *See* Opinion at p. 4. The Court of Appeals did not discuss the EMC Policies’ express grant of coverage for “misstatements,” “misleading statements,” and “omissions.” It did not explain the conflict between its holding that “mere negligence will not trigger the exclusion” and its holding that the Fraud Exclusion barred coverage for the Funds’ **negligence-based** CUSA claim. Nor

¹¹ The Court of Appeals declined to address the other exclusions before it on appeal based on its holding relative to the Fraud Exclusion. *See* Opinion at p. 4.

did it explain how a negligent omission (which, by definition, is the failure to make a statement) involves an “untrue” statement of fact.¹²

D. PERTINENT STATUTORY AND POLICY LANGUAGE.

1. Section 36b-29(a)(2) of the CUSA.

The Consent Judgment is premised upon Section 36b-29(a)(2) of the CUSA which states, in pertinent part:

(a) Any person who: . . . (2) offers or sells or materially assists any person who offers or sells a security by means of any **untrue statement of a material fact or any omission to state a material fact** necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, who knew **or in the exercise of reasonable care should have known of the untruth or omission**, the buyer not knowing of the untruth or omission, and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission, **is liable to the person buying the security**, who may sue either at law or in equity to recover the consideration paid for the security, together with interest at eight per cent per year from the date of payment, costs and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he no longer owns the security.

Conn Gen Stat Ann 36b-29(a)(2) (emphasis added); *see also* Opinion at p. 3-4.

2. Relevant EMC Policy Provisions.

i. The coverage grant.

The EMC Policies provide coverage for a “Wrongful Act” of an insured. *See* Appellants’ Opening Brief at p. 4. The term “Wrongful Act” is defined:

K. “Wrongful Act” means any of the following:

1. Actual or alleged errors;
2. **Misstatements or misleading statements;**
3. Act or **omission** or neglect or breach of duty by an “Insured”;

In the discharge of organizational duties.

¹² An omission renders an otherwise true statement misleading under the circumstances. *See, e.g., Hord v Envtl Research Inst of Michigan*, 463 Mich 399, 412; 617 NW2d 543, 550 (2000).

See Appellants' Opening Brief at pp. 4-5 (emphasis added); *see also* EMC Policies at p. 11 Part I(A), p. 14 Part II(K) (attached hereto as Ex. E)¹³. EMC has admitted that the Consent Judgment falls within this coverage grant unless an exclusion applies. See Appellants' Opening Brief at p. 5.

ii. The Fraud Exclusion.

The EMC Policies contain a Fraud Exclusion that precludes coverage for:

Any action brought against an "insured" if **by judgment or adjudication** such action was **based on a determination** that acts of fraud or dishonesty were committed by the "insured."

Opinion at p. 3 (emphasis added); *see also* Ex. E (EMC Policies) at p. 14 Part III(C).

¹³ Attached below as Ex. D to Appellants' Opening Brief, and Ex. 6 to EMC's Motion for Summary Disposition, dated March 27, 2013; *see also* Funds' Response to EMC's Motion for Summary Disposition, dated June 20, 2013, at pp. 5-6.

VIII. STANDARD OF REVIEW

This Court reviews de novo the Appellate Order affirming the grant of summary disposition in EMC's favor. *Corley v Detroit Bd of Educ*, 470 Mich 274, 277; 681 NW2d 342, 344 (2004).

IX. ARGUMENT

Virtually every D&O and E&O policy issued (in Michigan and elsewhere) contains a coverage grant for misstatements, misleading statements and omissions, and a fraud/dishonesty exclusion like those in the EMC Policies.¹⁴ Thousands of Michigan insureds—ranging from lawyers, to public entities and their employees—rely upon D&O and E&O policies to cover negligent misrepresentation/omission claims. Because of the Opinion, that coverage is now in jeopardy. This result, while harsh, could be countenanced if it was consistent with controlling Michigan law. But it is not. The Opinion violates nearly every significant insurance policy construction principle recognized by Michigan law. It transforms a consent judgment into a factual determination in direct conflict with a decision of this Court (and several Court of Appeals decisions). In addition, the analysis in the Opinion contradicts its ultimate holding. The Opinion as it stands will create unwarranted exposure for thousands of Michigan insureds (as well as numerous and expensive legal battles over insurance coverage) for years to come. The Funds respectfully request that the Court grant the Funds' Application pursuant to MCR 7.305(B)(3), (B)(5)(a) and (B)(5)(b).

¹⁴ The Funds realize this is a strong statement. Support for it may be found at footnotes 15-19 and 21-22, *infra*.

A. THE OPINION DEPRIVES THOUSANDS OF MICHIGAN INSURED OF COVERAGE FOR NEGLIGENT MISREPRESENTATIONS AND OMISSIONS.

MCR 7.305(B)(3) provides that an appeal is proper when an issue of major significance to Michigan jurisprudence is involved. Every insured in Michigan with a D&O or E&O policy has a direct stake in the outcome of the Funds' Application.

Errors and Omissions, or E&O insurance, is the name given to the broad category of policies issued to protect professionals from liability they may encounter in the conduct of their businesses.¹⁵ It includes malpractice policies insuring doctors, nurses and hospitals.¹⁶ It includes professional liability policies ensuring lawyers (and judges), accountants and engineers.¹⁷ It even includes policies—like the EMC “Linebacker” Policy at issue here—insuring municipalities, schools, water and sewer districts and the officials, teachers and employees working for them.¹⁸ Directors & Officers, or D&O insurance, is similar, except it typically covers the officers and directors of businesses, schools, charities and other organizations.¹⁹

¹⁵ *Massamont Ins Agency, Inc v Utica Mut Ins Co*, 489 F3d 71, 74 (CA 1, 2007) (“An errors and omissions policy is intended to insure a member of a designated calling against liability arising out of the mistakes inherent in the practice of that particular profession or business.”); *see also, generally, Stine v Cont'l Cas Co*, 419 Mich 89, 96; 349 NW2d 127, 130 (1984).

¹⁶ *Id.*

¹⁷ *Lawyers' Professional Liability Insurance*, 92 ALR 5th 273 at § 2[a] (2001) (“Professional liability policies provide insurance coverage for wrongful acts, errors, and omissions that a professional may make in the course of carrying out a profession. These policies are also called errors and omission policies or malpractice policies”); *see also Massamont*, 489 F3d at 74 (E&O policies insure against professional liability).

¹⁸ EMC specifically markets the policies issued here to “Towns, Townships, counties, public schools and related governmental entities such as water districts, sewage districts, sanitary districts, park and recreation boards, and planning and zoning commissions.” *See* EMC Brochure (attached hereto as Ex. F); *see also Educators' Liability Insurance*, 94 ALR 5th 567 (2001) (“Educators frequently seek to transfer these exposures by purchasing errors and omissions insurance policies, also called educator's liability policies, which insure against acts, errors, and omissions of the educator.”).

¹⁹ Ackerman, *A Common Law Approach to D&O Insurance "In Fact" Exclusion Disputes*, 79 U Chi L Rev 1429, 1459 (2012) (“Directors' and Officers' (D&O) liability insurance policies are a staple of the modern corporate world. Held by virtually all major organizations, these policies

The EMC Policies at issue here specifically cover “wrongful acts,” a term which is defined to include “misstatements,” “misleading statements” and “omissions.” *See* Appellant’s Opening Brief at p. 6; *see also supra* at pp. 5-6. In this fashion, the EMC Policies provide coverage for misrepresentation and omission claims.²⁰ But this coverage is not unlimited. The EMC Policies exclude misrepresentation and omission claims if it is determined, by judgment or adjudication, that EMC’s insured engaged in acts of dishonesty or fraud (the “Fraud Exclusion”). *See supra* at p. 6. The EMC Policies are supposed to cover **negligent** misrepresentation and omission claims, while excluding **intentional** misrepresentations and omissions. *Ill Union Ins Co v Shefchuk*, 108 F App’x 294, 301 (CA 6, 2004) (“it is not difficult to discern what the insurance company probably meant to do when it drafted the coverage and exclusion provisions in this policy—to insure against negligent acts but not dishonest, fraudulent, or illegal acts.”); Davisson et al, *Directors and Officers Liability Insurance Deskbook* (3rd Edition 2011) at p. 118 (“The D&O policy is intended to insure against the negligent acts of D&Os. The dishonest/fraudulent acts exclusion is intended to remove from coverage claims arising from intentionally fraudulent or dishonest behavior.”). At least that is the way other jurisdictions have harmonized the similar coverage grant and fraud exclusions appearing in other D&O/E&O policies. *See* authority *infra* at pp. 13-14.

The Opinion, however, did not harmonize the coverage grant for misstatements, misleading statements and omissions with the Fraud Exclusion the way other jurisdictions have. Instead, the Opinion construed the term “dishonesty” within the Fraud Exclusion so broadly that

protect their beneficiaries from losses suffered in connection with directors' and officers' performance of their duties.”).

²⁰ This is why EMC conceded that the Consent Judgment was covered under the EMC Policies unless excluded by one of exclusions set forth therein. *See* Appellants’ Opening Brief at p. 7 ¶ 10.

no misstatement, misrepresentation or omission could possibly be covered under the EMC Policies. *See* Opinion at p. 4 (holding that any untrue statement or omission is inherently dishonest). Put differently, the Opinion rendered the express coverage grant in the EMC Policies for misstatements, misrepresentations and omissions meaningless.

The precedential impact of the Opinion on Michigan jurisprudence is chilling. Nearly every E&O and D&O policy contains the same coverage grant appearing in the EMC Policies, extending coverage to “misstatements,” “misleading statements” and “omissions.”²¹ Fraud

²¹ The Funds realize this is a very broad statement. But it is important that the Court understand the sweeping impact the Opinion will have. What follows is a string cite of cases with the same (or substantively identical) coverage grant as the EMC Policies. This is by no means an exhaustive list. But it should be sufficient to demonstrate to the Court that the Funds are not engaging in hyperbole when they say the unintended consequences of the Opinion will be far reaching. **Michigan authorities include:** *Auto-Owners Ins Co v Lloyds London England/Certain Interested Underwriters*, 2009 WL 2974877, at *3; unpublished opinion per curiam of the Michigan Court of Appeals, issued September 17, 2009 (Docket No 287396) at *3 (“Wrongful Act means any actual or alleged act, error, **omission, misstatement, misleading statement**, neglect or breach of duty by any Assured.”) (emphasis added) (E&O); *Pinckney Cmty Sch v Cont'l Cas Co*, 213 Mich App 521, 526, 540 NW2d 748, 750-51 (1995) (same) (D&O); *Krueger Seed Farms, Inc v Szlarczyk*, 1999 WL 33453867, at *2 n 4; unpublished opinion per curiam of the Michigan Court of Appeals, issued March 9, 1999 (Docket No 200249) at *2 n 4 (same) (D&O); *Yale Pub Sch v MASB-SEG Prop Cas Pool*, 2004 WL 2881889, at *1; unpublished opinion per curiam of the Michigan Court of Appeals, issued December 14, 2004 (Docket No 250053) at *1 (same) (E&O); *Unionville-Sebewaing Area Sch v MASB-SEG Prop Cas Pool, Inc*, 2004 WL 177142, at *2; unpublished opinion per curiam of the Michigan Court of Appeals, issued January 29, 2004 (Docket No 242084) at *2 (same) (E&O); *Manistee Cty Intermediate Sch Bd v MASB-SEG Prop Cas Pool, Inc*, 2005 WL 1048747; at *3, unpublished opinion per curiam of the Michigan Court of Appeals, issued May 5, 2005 (Docket No 252603) at *3 (same) (E&O). **Federal and out-of-state cases include:** *Andy Warhol Found for Visual Arts, Inc v Fed Ins Co*, 189 F3d 208, 212 (CA 2, 1999) (defining “Wrongful Act” as “any error, **misstatement or misleading statement, act or omission**, or neglect or breach of duty”...) (emphasis added) (D&O); *Culbreath Isles Prop Owners Ass'n, Inc v Travelers Cas & Sur Co of Am*, 601 F App'x 876, 877 (CA 11, 2015) (same) (non-profit management and organization liability policy); *TranSched Sys Ltd v Fed Ins Co*, 67 F Supp 3d 523, 527 (DRI, 2014) (same) (D&O); *D'Amelio v Fed Ins Co*, 2004 WL 937328, at *2; unpublished opinion of

the US District Court for Massachusetts, issued April 28, 2004 (Docket No CIVA 02CV12174PBS) at *2 (same) (D&O and representations and warranties policies); *Sigma Chi Corp v Westchester Fire Ins Co*, 587 F Supp 2d 891, 893 (ND Ill, 2008) (same) (D&O); *MDL Capital Mgmt, Inc v Fed Ins Co*, 274 F App'x 169, 172 (CA 3, 2008) (same) (E&O); *Hartford Cas Ins Co v Chase Title, Inc*, 247 F Supp 2d 779, 781 (D Md, 2003) (same) (E&O); *Screen Actors Guild Inc v Fed Ins Co*, 957 F Supp 2d 1157, 1160 (CD Cal, 2013) (same) (D&O); *Lumbermens Mut Cas Co v Dadeland Cove Section One Homeowners' Ass'n, Inc*, 2007 WL 2979828, at *1; unpublished opinion of the US District Court for the Southern District of Florida, issued October 11, 2007 (Docket No 06-22222-CIV), at *1 (same) (D&O); *HCC Employer Servs, Inc v Westchester Cty Surplus Lines Ins Co*, 2006 WL 1663343, at *2; unpublished opinion of the US District Court for the Southern District of Texas, issued June 5, 2006 (Docket No CIV A H-05-1275), at *2 (E&O); *Upsher-Smith Labs, Inc v Fed Ins*, 264 F Supp 2d 843, 847 (D Minn, 2002) *aff'd sub nom Upsher-Smith Labs, Inc v Fed Ins Co*, 67 F App'x 382 (CA 8, 2003) (same) (E&O); *Axis Surplus Ins Co v Johnson*, 2008 WL 4525409, at *2, unpublished opinion of the US District Court for the Northern District of Oklahoma, issued October, 3, 2008 (Docket No 06-CV-500-GKF-PJC), at *2 (same) (D&O); *Krueger Int'l, Inc v Royal Indem Co*, 481 F3d 993, 994 (CA 7, 2007) (same) (employment practices liability policy); *Stauth v Nat'l Union Fire Ins Co of Pittsburgh*, 185 F3d 875 at *4; unpublished per curiam opinion of the US Tenth Circuit Court of Appeals, issued June 24, 1999 (Docket Nos 7-6437, 97-6438) at *4, (same) (D&O); *Seneca Ins Co v Kemper Ins Co*, 2004 WL 1145830, at *5; unpublished opinion of the US District Court for the Southern District of New York, issued May 21, 2004 (Docket No 02 CIV. 10088 PKL) at *5, *aff'd*, 133 F App'x 770 (CA 2, 2005) (same) (D&O); *Nat'l Stock Exch v Fed Ins Co*, 2007 WL 1030293, at *1; unpublished opinion of the US District Court for the Northern District of Illinois, issued March 30, 2007 (Docket No 06 C 1603) at *1 (same) (executive liability policy); *Mt Hood, LLC v Travelers Cas & Sur Co of Am*, 2009 WL 536848, at *1; unpublished decision of the US District Court for Oregon, issued March 3, 2009 (Docket No CIV 08-1068-AA) at *1 (same) (non-profit D&O); *Huntingdon Ridge Townhouse Homeowners Ass'n, Inc v QBE Ins Corp*, 2009 WL 4060458, at *3; unpublished opinion of the US District Court for the Middle District of Tennessee, issued November 20, 2009 (Docket No 3:09-CV-00071) at *3 (same) (D&O and E&O); *Fed Sav & Loan Ins Corp v Oldenburg*, 671 F Supp 720, 725 at n 2 (D Utah, 1987) (same) (D&O) *Comerica Inc v Zurich Am Ins Co*, 498 F Supp 2d 1019, 1021 (ED Mich, 2007) (same) (D&O); *see also, e.g., Rogers v Tudor Ins Co*, 325 Ark 226, 234, 925 SW2d 395, 399 (1996) (“Wrongful Act” defined to include “any actual or alleged breach of duty, neglect, error, misstatement, misleading statement or omission by the Insureds...”) (non-profit D&O); *Noxubee Cty Sch Dist v United Nat Ins Co*, 883 So 2d 1159, 1164 (Miss, 2004) (same) (school board liability policy); *United Westlabs, Inc v Greenwich Ins Co*, 2011 WL 2623932, at *4; unpublished opinion of the Delaware Superior Court issued June 13, 2011 (Docket No CIVA 09C-12048 MMJ), at *4 (same) (private company reimbursement policy); *Ferguson v Travelers Indem Co*, , 2014 WL 3798524, at *2; unpublished per curiam opinion of the New Jersey Court of Appeals, issued August 4, 2014 (Docket No A-

exclusions like the one in the EMC Policies are equally prevalent.²² If the Opinion were applied to every policy with a coverage grant and fraud exclusion like those in the EMC Policies,

3530-12T3) at *2 (same) (E&O); *Nat'l Union Fire Ins Co of Pittsburgh v Miller*, 228 W Va 739, 743;724 SE2d 343, 347 (2012) (same) (governmental liability policy); *Mut Assur Adm'rs, Inc v US Risk Underwriters, Inc*, 1999 OK CIV APP 129, ¶ 6; 993 P.2d 795, 797 (1999) (same) (E&O); *Wauwatosha Sch Dist v Nat'l Union Fire Ins Co of Pittsburgh, PA*, 1998 WL 893239 at *2; unpublished per curiam opinion of the Wisconsin Court of Appeals, issued December 22, 1998 (Docket No 97-2538) at *2 (same) (E&O); *Cigna Corp v Executive Risk Indem, Inc*, 2015 PA Super 43, 111 A3d 204, 212 (2015) (same) (E&O); *TIG Specialty Ins Co v Koken*, 855 A2d 900, 907 at n 8 (Pa Commw Ct, 2004) *aff'd*, 586 Pa 84, 890 A2d 1045 (Pa Ct App, 2005) (same) (D&O). *Syracuse Univ v Nat'l Union Fire Ins Co of Pittsburgh, PA*, 975 NYS2d 370 at *2 (NY Sup Ct, 2013) *aff'd*, 976 NYS2d 921; 112 AD3d 1379 (NY Ct App, 2013) (same) (not-for-profit D&O policy); *Stevens v Cincinnati Ins Co*, 2002 WL 984631, at *4; unpublished per curiam opinion of the Iowa Court of Appeals, issued May 15, 2002 (Docket No 01-101) at *4 (same) (non-profit organization policy); *Bank of Am Corp v SR Int'l Bus Ins Co*, SE, 2007 WL 4480057, at *4; unpublished opinion of the North Carolina Superior Court, issued December 19, 2007 (Docket No 05 CVS 5564) at *4 (same) (professional liability policy); *WellPoint, Inc v Nat'l Union Fire Ins Co of Pittsburgh, PA*, 29 NE3d 716, 723 (Ind, 2015) *opinion modified on other grounds after reh'g*, 38 NE3d 981 (Ind, 2015) (same) (E&O); *Aug Entm't, Inc v Philadelphia Indem Ins Co*, 146 Cal App 4th 565, 571; 52 Cal Rptr 3d 908, 911 (2007) (same) (D&O); *Amos ex rel Amos v Campbell*, 593 NW2d 263, 265 (Minn Ct App, 1999) (same) (E&O); *AT & T Corp v Faraday Capital Ltd*, 918 A2d 1104, 1107 (Del, 2007) (D&O).

²² See, e.g., *Steadfast Ins Co v Prime Title Servs, LLC*, 2008 WL 5216020, at *5; unpublished opinion of the US District Court for the Western District of Michigan, issued December 11, 2008 (Docket No 1:07-CV-366) at *5 (E&O policies “generally contain exclusions for dishonest, intentional, fraudulent, or criminal acts.”); 4 *Law & Practice of Insurance Coverage Litigation* § 47:32 p. 47 (2005) (“D&O policies typically exclude claims arising from, brought about or contributed to by the dishonest, fraudulent, or criminal acts of the insureds”); 4 *New Appleman on Insurance* (Law Library Ed) §25 p. 2 (1999) (“Almost all [E&O] policies exclude coverage for “any dishonest, fraudulent, criminal or malicious act.”); Davisson et al, *Directors and Officers Liability Insurance Deskbook* (3rd Edition 2011) at p. 118 (“The D&O policy is intended to insure against the negligent acts of D&Os. The dishonest/fraudulent acts exclusion is intended to remove from coverage claims arising from intentionally fraudulent or dishonest behavior.”); 4 *New Appleman on Insurance* (Law Library Ed.) §25.06[2] p. 64 (1999) (“almost all claims-made D&O policies provide that the dishonesty exclusion applies when determined by a judgment or other final adjudication. The courts have held that this language cannot exclude settlements.”); 26A *Securities Litigation: Damages* § 20.30(1) p. 106 (2015) (“Most D&O policies contain an exclusion that states that the insurer will not be liable for losses in connection the dishonest or

coverage for negligent misrepresentation and omission claims—at least in Michigan—would cease to exist. This result would not only be devastating to the thousands of insureds relying upon D&O and E&O insurance for such coverage, it is also directly contrary to the weight of authority.

Nationally, the coverage grant for misstatements and omissions exists in harmony with the Fraud Exclusion because courts have made the logical conclusion that a negligent misrepresentation or omission is not fraudulent or dishonest. *Wojtunik v Kealy*, CV-03-2161-PHX-PGR, 2011 WL 1211529, at *9, n16; unpublished opinion of the US District Court for Arizona, issued March 31, 2011 (Docket No CV-03-2161-PHX-PGR) at *9, n 16 (attached hereto as Ex. G) (noting that the same fraudulent acts exclusion is inapplicable to claims under the Arizona Securities Act because the “three non- § 10(b) securities fraud claims did not require any proof of scienter amounting to deliberate fraud.”); *Cent Power Sys & Servs, Inc v Universal Underwriters Ins Co*, 49 Kan App 2d 958, 969; 319 P3d 562, 570 (2014) (“The insurers argue that even negligent misrepresentation should be considered a dishonest or fraudulent act covered by the exclusion...Given the mandate that we consider policy exclusions in favor of providing coverage, we conclude that this exclusion does not prevent coverage for merely negligent acts.”); *Jensen v Snellings*, 841 F2d 600, 615 (CA 5, 1988) (fraud or dishonesty exclusion did not apply to the extent plaintiff’s misrepresentation claims regarding tax consequences and oil and gas programs could be premised on theory of negligence rather than fraud); *Clarendon Nat Ins Co v Vickers*, 265 F App’x 890, 891 (CA 11, 2008) (“Because a viable claim was alleged without regard to Vickers’ mens rea, exclusion A (dishonest and fraudulent actions) does not apply”);

fraudulent conduct of the insured. This ‘fraud’ exclusion has traditionally been subject to a ‘final adjudication’ condition”).

Brooks, Tarlton, Gilbert, Douglas & Kressler v US Fire Ins Co, 832 F2d 1358, 1369-70 (CA 5, 1987) (fraud or dishonesty exclusion does not preclude coverage for constructive fraud because fraudulent intent is not an element); *Faulkner v Am Cas Co of Reading, Pa*, 85 Md App 595, 630, 584 A2d 734, 751 (Md Ct App, 1991) (“Had the allegation been merely that he knowingly participated, coverage might be deniable because of the exclusion from coverage of claims brought about or contributed to by the dishonesty of directors or officers. . . negligent error, misstatement, misleading statement, act, or omission is within the definition of a “wrongful act,” for which the policy provides coverage.”).

The insurance industry itself knows fraud or dishonesty exclusions are not intended to extend to negligent misrepresentation/omission claims because it places them in policies that expressly provide coverage for “negligent” misstatements or omissions.²³ The Sixth Circuit referred to this practice as “meaningless or illogical” because a policy that only provides coverage for “*negligent* breach of duty, error, misstatement, omission, ‘publication injury’ or other *negligent* act” would never cover “dishonest” conduct in the first place. *Ill Union*, 108 F App’x at 301 (emphasis in original). *Ill Union* went on to state that “it is not difficult to discern what the insurance company probably meant to do when it drafted the coverage and exclusion provisions in this policy—to insure against negligent acts but not dishonest, fraudulent, or illegal acts.” *Id.*; see also *Alstrin v St Paul Mercury Ins Co* 179 F Supp 2d 376, 397 (D Del, 2002) (in which the **insurer argued** that a policy’s fraud or dishonesty exclusion did not render coverage

²³ *Faulkner v Am Cas Co of Reading, Pa*, 85 Md App 595, 630; 584 A2d 734, 751 (Md Ct App, 1991) (dishonesty exclusion contained in policy with coverage grant for “negligent error, misstatement, misleading statement, act, or omission”); *MSO Washington, Inc v RSUI Grp, Inc*, 2013 WL 1914482, at *9; unpublished decision of the US District Court for the Western District of Washington, issued May 8, 2013 (Docket No C12-6090 RJB) at *9 (dishonesty exclusion contained in policy with coverage grant for any “negligent act, error or omission ... in the rendering of or failure to render professional services”).

for misstatements, misleading statements, or omissions illusory because “certain securities fraud claims can be sustained based on recklessness or negligence”).

Not only do policies that contain fraud or dishonesty exclusions contain grants of coverage for misrepresentations and omissions, they are specifically advertised as such. EMC’s own website advertises E&O—or, in EMC’s vernacular, “Linebacker” Policies just like EMC Policies at issue here—to governmental entities:

Government entities are typically responsible for the decisions and acts of their employees, board members and volunteers when carrying out their duties for the organization. Occasionally, those decisions and acts create difficult situations that may lead to a lawsuit for damages and a costly defense.

EMC’s lineback policy provides protection for liability and defense costs for the wrongful acts of insureds that may occur through the process of conducting business: **actual or alleged errors, misstatements or misleading statements, acts or omissions**, and neglect or breach of duty by an insured. The policy also provides employment-related practices liability coverage for harassment, discrimination, wrongful termination and other employment wrongful acts.

Linebacker coverage is available for public schools, political subdivisions and related entities such as water, sewage and sanitation districts, fire departments, and parks and recreation boards.

See Employers Mutual Casualty Company, *Errors and Omissions*, <http://www.emcins.com/BusinessIns/General/Errors_Omissions.aspx> (accessed January 6, 2016) (attached hereto as Ex. H) (emphasis added). EMC produces a similar advertising piece targeted at public officials which specifically touts, under the header “What does it cover?”, the fact that its “Linebacker” policy covers “misstatements,” “misleading statements,” and “omissions.” *See* EMC Brochure (attached hereto as Ex. F). This is probably why EMC never argued that **negligent** misrepresentations and omissions fall within the Fraud Exclusion. Instead EMC urged the Court of Appeals to look past the Consent Judgment (in direct contradiction of the Exclusion’s “determination” by “judgment or adjudication” language) and infer dishonesty or fraud from mere allegations in the Liability Action; *Compare* Appellee’s Brief at pp. 21-23

(attached hereto as Ex. I) with *Pendergest-Holt v Certain Underwriters at Lloyd's of London*, 600 F3d 562, 572 (CA 5, 2010) (“When a D&O policy requires a ‘final adjudication’ to trigger an exclusion, courts have consistently held that the adjudication must occur in the underlying D&O proceeding, rather than in a parallel coverage action or other lawsuit.”).

As a result of the Opinion, the clear distinction between intentional and negligent misrepresentations and omissions no longer exists in Michigan—they are all “dishonest” for purposes of fraud/dishonesty exclusions. That means Michigan public schools, political subdivisions, water, sewage and sanitation districts, fire departments, parks and recreation boards, doctors, dentists, chiropractors, lawyers (and judges), accountants, architects, engineers, and all manner of other businesses are now in jeopardy of losing their coverage for “misstatements,” “misleading statements,” and “omissions.” The consequences for Michigan insureds will be severe. Unless the Opinion is reversed, a single negligent misrepresentation or omission that was thought to be covered could result in financial ruin when the insured is forced to pay the judgment itself.

Given the Opinion’s broad impact on Michigan insurance law and its severe departure from the overwhelming weight of authority, the Funds respectfully request the Court accept jurisdiction and grant the Funds’ Application, peremptorily reverse the Opinion, pursuant to MCR 7.305(B)(3).

B. THE OPINION CONFLICTS WITH MICHIGAN LAW REGARDING THE NATURE AND EFFECT OF A CONSENT JUDGMENT AND THE PROPER INTERPRETATION OF AN INSURANCE POLICY.

1. The Opinion conflicts with Michigan law on the nature and effect of a consent judgment.

The Fraud Exclusion requires a two part analysis: 1) was there a judgment or adjudication; and 2) did that judgment or adjudication actually “**determine**” that the insured

committed acts of fraud or dishonesty? The Court of Appeals erred in its analysis of the second question. Although the Consent Judgment makes no express factual findings, the Court of Appeals held that “the consent judgment, by finding a violation of [Conn Gen Stat Ann 36b-29(a)(2)], necessarily found that Witucki and Helicon ‘made untrue statements of material fact’ or ‘omissions to state a material fact.’” Opinion at p. 4. This conclusion is in direct conflict with *Acorn Inv Co v Mich Basic Prop Ins Ass’n*, 495 Mich 338; 852 NW2d 22 (2014) and several Michigan Court of Appeals decisions.

A consent judgment, though enforceable as a judgment, is nothing more than a settlement approved by the court. *Acorn*, 495 Mich at 354; *Am Mut Liab Ins Co v Michigan Mut Liab Co*, 64 Mich App 315, 327; 235 NW2d 769, 776 (1975) (a court’s approval of a consent judgment is “ministerial”). It does not constitute an adjudication, or even a concession, of any of the facts or allegations at issue in the case. *Acorn*, 495 Mich at 354 (“The court does not determine ... the rights and obligations of the parties in a consent judgment.”) (internal quotations omitted); *Smit v State Farm Mut Auto Ins Co*, 207 Mich App 674, 682; 525 NW2d 528, 532 (1994) (When parties enter into a consent judgment “factual issues are neither tried **nor conceded**.”) (emphasis added); *accord Bristol W Ins Co v Whitt*, 406 F Supp 2d 771, 783 (WD Mich, 2005) (“The problem with this argument is that the underlying case was resolved by consent judgment, where factual issues are neither tried **nor conceded**.”) (emphasis added); *Badgley v Varelas*, 729 F2d 894, 899 (CA 2, 1984) (“Like most consent judgments, the agreement between the plaintiffs and the County defendants contains **no admission of liability**.”) (emphasis added); *In re Kennedy*, 243 BR 1, 12 (Bankr WD Ky, 1997) *subsequently aff’d*, 249 F3d 576 (CA 6, 2001) (“This Court has carefully reviewed the Michigan Consent Judgment and finds that **it is simply a blanket entry of**

judgment on the fraud counts of the Plaintiffs' Complaint. **It includes no** language or discussion of culpability, fault, or **concessions as to liability.**") (emphasis added).

The absence of a concession or determination of liability is why a consent judgment does not support issue preclusion. *Am Mut Liab Ins Co*, 64 Mich App at 327 (“A consent judgment reflects primarily the agreement of the parties. The action of the trial judge in signing a judgment based thereon is **ministerial only**. The parties have not litigated the matters put in issue, they have settled. The trial judge has not determined the matters put in issue, he has merely put his stamp of approval on the parties' agreement disposing of those matters”); *Rzepka v Michael*, 171 Mich App 748, 756; 431 NW2d 441, 444 (1988); *Goldman v Wexler*, 122 Mich App 744; 748, 333 NW2d 121, 123 (1983); *accord Arizona v California*, 530 US 392, 414; 120 S Ct 2304, 2319; 147 L Ed 2d 374 (2000).

In short, under controlling Michigan law, the Consent Judgment didn't “determine” anything. It was insufficient on its face to support application of the Fraud Exclusion (which could apply only if there was a **determination**, by judgment or adjudication, that EMC's insureds committed acts of fraud or dishonesty). Opinion at p. 3 (quoting Fraud Exclusion); *see also* Ex. E (Insurance Policy) at Part III(C).

This exact issue was litigated in *Wojtunik v Kealy*, CV-03-2161-PHX-PGR, 2011 WL 1211529; unpublished opinion of the US District Court for Arizona, issued March 31, 2011 (Docket No CV-03-2161-PHX-PGR) (attached as Ex. G hereto).²⁴ *Wojtunik* noted, like the Michigan authority above, that a consent judgment is not a determination or concession of any of

²⁴ *Wojtunik* considered a consent judgment for liability under the negligence-based Arizona Securities Act. *See State v Gunnison*, 127 Ariz. 110, 618 P2d 604 (1980) (intent is not an element of an Arizona Securities Act claim); *accord Tech Corp v Valentine*, 925 F2d 910, 922 n7 (6th Cir, 1991) (“Like most states, Michigan's Blue Sky [securities] laws do not require a specific intent to defraud.”) (*citing Gunnison*).

the allegations in the lawsuit. *Id.* at *9. As a result, *Wojtunik* concluded that “the mere existence of the [consent judgment] cannot be deemed to have established as a matter of law that the Insureds committed deliberate securities fraud so as to invoke the fraud exclusion.” *Id.* The Arizona (and United States Supreme Court) cases cited in *Wojtunik* on the effect of a consent judgment are indistinguishable from *Acorn* and the other Michigan cases discussed above. Compare *Chaney Bldg Co v City of Tucson*, 148 Ariz 571, 573; 716 P2d 28, 30 (1986); and, *Arizona*, 530 US at 414; with, *Acorn*, 495 Mich at 354. Thus, the result here should be the same as in *Wojtunik*. The Fraud Exclusion cannot be triggered by the Consent Judgment.

The fact that the Consent Judgment did not **determine** anything—and therefore cannot support application of the Fraud Exclusion—is also evident from the way the trial court and the Court of Appeals struggled to identify what, exactly, Helicon and Witucki did to give rise to the Consent Judgment. Rather than referring strictly to the Consent Judgment (as required by the plain language of the Fraud Exclusion), the Trial Court was forced to cherry pick mere allegations from the pleadings in an effort to support its conclusion that Helicon and Witucki engaged in “dishonest” conduct. See Appellants’ Reply Brief at p. 8 (attached hereto as Ex. J). While the Court of Appeals correctly confined itself to the Consent Judgment and the CUSA section it was based on, it still was unable to determine whether Helicon or Witucki made an untrue statement of fact, an omission, or both. Opinion at p. 4 (“Pursuant to the plain language of the above statute, the consent judgment, by finding a violation of that statute, necessarily found that Witucki and Helicon made untrue statements of material fact or omissions to state a material fact”) (emphasis added). These struggles exist only because the Consent Judgment is not a determination or adjudication of Helicon and Witucki’s conduct. Helicon and Witucki **settled** the Funds’ claim against them. That this contractual settlement became a judgment as a

result of the “ministerial” actions of a court does not somehow transform the settlement into a determination or admission of the facts alleged in the Liability Action. *Am Mut Liab Ins Co*, 64 Mich App at 327.²⁵

The Fraud Exclusion requires a “**determination**” that acts of fraud or dishonesty were committed by the insured before coverage can legitimately be denied. Opinion at p. 3 (emphasis added). The Consent Judgment, while technically a “judgment,” contains no such determination. Nevertheless, the Opinion treats the Consent Judgment as a factual determination sufficient to trigger the Fraud Exclusion. By doing so, the Opinion conflicts with the pronouncements in *Acorn*, *American Mutual*, *Smit*, *Rzepka*, *Goldman* and other decisions concerning the effect of a consent judgment. *Supra* at pp. 16-17. The Funds respectfully request this Court peremptorily reverse the Opinion or accept jurisdiction to resolve this conflict. MCR 7.305(B)(3)(b).

2. The Opinion conflicts with Michigan law on the proper interpretation of an insurance policy.

- i. The Opinion failed to construe the EMC Policies as a whole and give effect to language of their coverage grant.

The language of insurance contracts must be read as a whole and must be construed to give effect to every word, clause, and phrase. *Klapp v United Ins Grp Agency, Inc*, 468 Mich

²⁵Numerous courts have recognized that an insurer’s use of language requiring a determination by judgment or adjudication as a condition to enforcing an exclusion is significant given how few cases proceed to final judgment. *See, e.g., Nat’l Union Fire Ins Co of Pittsburgh, Pa v Cont’l Illinois Corp*, 666 F Supp 1180, 1191 (ND Ill, 1987) (noting the “significance of the fact that the prohibition against *adjudicated* determinations of willful misconduct is the only one Insurers chose to specify in the Policies. After all, few lawsuits reach the stage of a full-blown trial—something in the range of 3% of civil filings. And the obverse side of that coin is that the vast majority of civil lawsuits end in settlement.”); *Pendergest-Holt*, 600 F3d at 573 (“a final adjudication exclusion limits the insurer’s recourse if the parties settle—the most likely outcome...”). Here, EMC was defending Helicon and Witucki in the Liability Action. That means EMC agreed to the entry of the Consent Judgment (if they had not they would have denied coverage on the basis of an unauthorized settlement). EMC should not be permitted to stipulate to the entry of a judgment it knew (based on controlling Michigan law) did not trigger the Fraud Exclusion it selected for inclusion in its Policies, then attempt to avoid paying that judgment based on that same inapplicable exclusion.

459, 467; 663 NW2d 447, 453 (2003); *McGrath v Allstate Ins Co*, 290 Mich App 434, 439; 802 NW2d 619, 621 (2010). “If, after reading the entire contract, the language can reasonably be understood in different ways—one providing and the other excluding coverage—the ambiguity is to be liberally construed against the insurer.” *Farm Bureau Mut Ins Co of Mich v Moore*, 190 Mich App 115, 118; 475 NW2d 375, 377 (1991); *Klapp*, 468 Mich at 467 (“**courts cannot simply ignore portions of a contract in order to avoid a finding of ambiguity...contracts must be construed so as to give effect to every word or phrase as far as practicable**”) (emphasis added). The Opinion conflicts with *Klapp* and its progeny because it fails to address the EMC Policies’ coverage grant, much less give effect to it.

The EMC Policies expressly extend coverage to “misstatements,” “misleading statements,” and “omissions.” See Appellant’s Opening Brief at p. 6; see also Ex. E (EMC Policies) at p. 11 Part I(A), p. 14 Part II(K). This Court’s decision in *Klapp* obligates the Court of Appeals to consider and give effect to this language. *Klapp*, 468 Mich at 467. The Opinion does the opposite. The Court of Appeals never mentions this language in the Opinion, and its construction of the Fraud Exclusion effectively deleted the words “misstatement,” “misleading statement,” and “omission” from the EMC Policies.

The Opinion holds that any untrue statement of fact or omission²⁶ is inherently dishonest, regardless of the intent (or lack thereof) with which it is made. Opinion at p. 4 (“Because

²⁶ The Court of Appeals did not address why an omission fits within its definition of “dishonest.” The Court of Appeals’ reliance on the Black’s Law Dictionary’s inclusion of “untruthfulness” within the definition of “dishonest” appears a poor fit for omission liability which involves a true but misleading statement of fact. See, e.g., *Hord v Envntl Research Inst of Mich*, 463 Mich 399, 412; 617 NW2d 543, 550 (2000) (An omission renders an otherwise true statement misleading under the circumstances.). Nevertheless, because the Court of Appeals recognized the Consent Judgment could have been premised on omission liability, it held all negligent omissions are inherently dishonest as well. Opinion at p. 4 (“Pursuant to the plain language of the above statute, the consent judgment, by finding a violation of that statute, **necessarily found that**

statements and representations made by Helicon and Witucki were untrue they committed acts of fraud or dishonesty”). No misstatement, misleading statement or omission would ever be covered under this standard. Even an “innocent” misrepresentation involves an untrue statement of fact. *Roberts v Saffell*, 483 Mich 1089, 1090; 766 NW2d 288, 289 (2009). The Court of Appeals construction of “dishonest” in a fashion which gives no meaning whatsoever to the EMC Policies’ express coverage grant applying to misstatements, misleading statements and omissions is **exactly** what *Klapp* forbids. *Klapp*, 468 Mich at 467. The Funds respectfully request the Court peremptorily reverse the Opinion or accept jurisdiction to resolve this conflict. MCR 7.305(B)(3)(b).

- ii. The Opinion conflicts with the doctrine of illusory coverage as set forth by the Michigan Court of Appeals in *Ile v. Foremost Ins. Co.*

Because the EMC Policies contain an express coverage grant for misstatements, misleading statements, and omissions, some form of this conduct must fall outside of the Fraud Exclusion or this specific coverage grant is illusory. *Ile v Foremost Ins Co*, 293 Mich App 309, 315–316; 809 NW2d 617 (2011), *reversed on other grounds Ile ex rel Estate of Ile v Foremost Ins Co*, 493 Mich 915; 823 NW2d 426 (2012).²⁷ The Court of Appeals recognized as much in the Opinion. Opinion at p. 4 (the “doctrine of illusory coverage is applicable where part of the insurance premium is specifically allocated to a particular type or period of coverage and that coverage turns out to be functionally nonexistent.” (quoting *Ile*, 293 Mich App at 315–316). The Opinion correctly quotes *Ile*, but its conclusion cannot be reconciled with that decision. As

Witucki and Helicon made untrue statements of material fact or omissions to state a material fact”) (emphasis added). This incongruity merely reinforces the fact the Consent Judgment does not provide the “determination” necessary to invoke the Fraud Exclusion at all. *See* argument *supra* at pp. 19-20.

²⁷ While this Court overturned the Court of Appeals in *Ile*, the Opinion’s quotation of the Court of Appeals’ decision in *Ile* indicates the Michigan Court of Appeals still considers that decision’s statement of the doctrine to be good law.

addressed above, under the construction of the Fraud Exclusion adopted by the Opinion, there is simply no way an insured could receive coverage for a misstatement, misleading statement or omission.

The Opinion conflicts with the doctrine of illusory coverage set forth by the Court of Appeals in *Ile*. The Funds respectfully request the Court peremptorily reverse the Opinion or accept jurisdiction to resolve this conflict. MCR 7.305(B)(3)(b).

- iii. The Opinion conflicts with this Court's mandate that ambiguities must be construed in favor of the insured and coverage.

Any ambiguity in an insurance policy must be construed in favor of coverage. *Moore*, 190 Mich App at 118.. This doctrine is particularly applicable to policy exclusion, because the insurer seeks to remove conduct from the insurance policy's general grant of coverage. *Fire Ins Exch v Diehl*, 450 Mich 678, 687; 545 NW2d 602, 606 (1996) ("this Court strictly construes against the insurer exemptions that preclude coverage for the general risk."); *Cas & Sur Grp v Coloma Twp*, 140 Mich App 516, 522; 364 NW2d 367, 370 (1985) ("Since the purpose of insurance is to insure, the courts should not construe a policy to defeat coverage unless the language requires it."); *accord Aetna Cas & Sur Co v Dow Chem Co*, 28 F Supp 2d 440, 445 (ED Mich, 1998) ("[I]t is the insurer's responsibility to clearly express limits on coverage. Thus, insurance exclusion clauses are construed strictly and narrowly.") (internal citation omitted). An exclusion is ambiguous if it is susceptible to more than one reasonable interpretation. *Klapp*, 468 Mich at 467; *Moore*, 190 Mich App at 118. The Court of Appeals disregarded this well-established law when it repeatedly construed the terms of the Fraud Exclusion broadly and in a manner that defeated coverage.

The Opinion errantly equates being "incorrect" with being "dishonest" (e.g. the fact that a statement was untrue makes it dishonest. A defendant's honesty or dishonesty is not at issue in

a claim for negligent misrepresentation. *Kramer v Petisi*, 285 Conn 674, 685; 940 A2d 800, 807 (2008) (“The reason a narrower scope of liability is fixed for negligent misrepresentation than for deceit is to be found in the difference between the obligations of honesty and of care.”) (emphasis added); *see also* authority cited *infa* at pp. 26-27. The fact that virtually every court to consider the issue has concluded that fraud/dishonesty exclusions **do not** extend to negligence-based claims suggests that the construction adopted by the Court of Appeals is patently unreasonable. *Wojtunik*, 2011 WL at *9, n16; *Cent Power Sys & Servs, Inc*, 319 P3d at 570; *Jensen*, 841 F2d at 615; *Clarendon Nat Ins Co v Vickers*, 265 F App'x at 891; *Brooks*, 832 F2d at 1369-70; *Faulkner*, 584 A2d at 751.²⁸

But even if the Court of Appeals believed that construing the Fraud Exclusion so that it swallowed the EMC Policies’ coverage grant for misstatements, misleading statements and omissions was reasonable, the fact that so many other courts had adopted a different construction should have been dispositive. At a minimum, these other authorities demonstrate that the Fraud Exclusion was reasonably susceptible to at least two different constructions—one (adopted by the Court of Appeals) which barred coverage for all misstatements, misleading statements and omissions, regardless of intent; and another (adopted by the overwhelming weight of authority) which barred coverage only for intentional misrepresentations and omissions. The existence of multiple “reasonable” interpretations established an ambiguity and required the Court of Appeals

²⁸ Courts have reached a similar result in the context of fidelity bonds, which **grant** coverage for employees’ “dishonest or fraudulent” acts. There, because the issue is reversed, the courts have concluded intent is necessary to trigger coverage. *See, e.g., Eglin Nat Bank v Home Indem Co*, 583 F2d 1281, 1287 (5th Cir, 1978) (“We thus believe that Florida, in line with the view expressed by Couch on Insurance and the other authorities cited earlier in this opinion, would require willfulness and intent to deceive as essential elements of ‘dishonest or fraudulent acts.’”); *Great Am Ins Co v Langdeau*, 379 SW2d 62, 65 (Tex, 1964) (“To constitute fraudulent and dishonest conduct, the employee must have some degree of intent to perform the wrongful action...mere negligence, carelessness or incompetence is insufficient.”).

to adopt the interpretation that favored coverage.²⁹ *Klapp*, 468 Mich at 467; *Moore*, 190 Mich App at 118. The Court of Appeals did the opposite.

The same issue exists with respect to the question of whether the Consent Judgment constitutes a “**determination**, by judgment or adjudication” sufficient to trigger the Fraud Exclusion in the first place. If not dispositive, the numerous Michigan Supreme Court and Court of Appeals cases stating that consent judgments don’t determine anything—along with the directly-on-point *Wojtunik* decision from Arizona—should have demonstrated that the “determination” requirement in the Fraud Exclusion was, at best, ambiguous as to its application to consent judgments.³⁰ This should have led to a similar result—construction of the Fraud Exclusion in favor of coverage. *Diehl*, 450 Mich at 687; *Moore*, 190 Mich App at 118. Again, the Court of Appeals did the opposite.

The Court of Appeals failed to construe the Fraud Exclusion consistent with the policy construction mandates set forth in *Diehl*, *Klapp*, and *Moore*. The Funds respectfully request the Court peremptorily reverse the Opinion or accept jurisdiction to resolve this conflict. MCR 7.305(B)(3)(b).

C. THE OPINION IS CLEARLY ERRONEOUS AND WILL RESULT IN MATERIAL INJUSTICE.

Aside from its conflicts with Michigan law, the Opinion is internally inconsistent. The Court of Appeals stated that “mere negligence will not trigger the exclusion.” Opinion at p. 4.

²⁹ There is support for the conclusion that the term “dishonest” is ambiguous. In the context of a fidelity bond’s “Prior Fraud, Dishonest or Cancellation” exclusion, another panel of the Michigan Court of Appeals held that the phrase “any fraudulent or dishonest act” could be “construed as ambiguous in terms of what falls within its parameters.” *Alcona Cty v Mich Mun League Liab & Prop Pool*, 2011 WL 833240, at *5 n 14; unpublished opinion per curiam of the Michigan Court of Appeal, issued March 10, 2011 (Docket No 292155) at *5 n 14.

³⁰ To be clear, the Funds believe that the authority cited *supra* at pp. 16-20 is controlling and that the Court of Appeals decision regarding the effect of the Consent Judgment was clearly erroneous on the merits. The concept of ambiguity is discussed only to demonstrate that any doubts should have been resolved in favor of coverage.

The Funds agree. The Funds' Consent Judgment is premised on the **negligence-based** CUSA. *Lehn v Dailey*, 77 Conn App 621, 630; 825 A2d 140, 147-48 (2003) (**rejecting** the argument that Section 36b-29(a)(2) "requires scienter and cannot be predicated on **mere negligence.**") (emphasis added); *see also Conn Nat Bank v Giacomi*, 242 Conn 17, 47; 699 A2d 101, 118-19 (1997) (standard of liability under the CUSA is reasonable care). That is exactly why the Consent Judgment is covered. There is no rational way to reconcile the Court of Appeals' statement that "mere negligence" is covered by the EMC Policies with its contrary conclusion that the Funds' Consent Judgment—premised on a CUSA claim requiring "mere negligence" to establish liability—is barred by the Fraud Exclusion.

Nor is there a basis for reconciling the Court of Appeals holding in American tort law. No negligence-based claim is more dishonest than another, because honesty or lack thereof has nothing to do with the concept of negligence. *Kramer*, 285 Conn at 685 ("The reason a narrower scope of liability is fixed for negligent misrepresentation than for deceit is to be found in the difference between the obligations of honesty and of care.") (emphasis added); *Sound Techniques, Inc v Hoffman*, 50 Mass App Ct 425, 422-23; 737 NE2d 920, 926 (2000) ("An individual who makes negligent misrepresentations has honest intentions but has failed to exercise due care."); *Technomedia Int'l, Inc v Int'l Training Servs Inc*, 2010 WL 3545662, at *5; unpublished opinion of the US District Court for the Southern District of Texas, issued September 9, 2010 (Docket No CIVAH-09-3013) at *5 ("Negligent misrepresentation implicates only the duty of care in supplying commercial information; **honesty or good faith is no defense**, as it is to a claim for fraudulent misrepresentation.") (emphasis added); *EAS Grp, Inc v FiberPop Sols, Inc*, 2015 WL 3654323, at *4; unpublished decision of the US District Court for Minnesota, issued June 11, 2015 (Docket No 14-MC-0020 PJS/TNL) at *4 ("A negligent misrepresentation

is made when the misrepresenter fails to discover or communicate certain information that an ordinary person would have discovered or communicated. Fraudulent or intentional misrepresentation, in contrast, requires dishonesty or bad faith.”); *Complaint of Yacob*, 318 Or 10, 20; 860 P2d 811, 816 (1993) (“There is a distinction...between misrepresentation occurring negligently and an affirmative act of dishonest or intentional misrepresentation.”); *See, e.g., Iowa Supreme Court Attorney Disciplinary Bd. v. McGinness*, 844 NW2d 456, 462 (Iowa, 2014) (“Iowa Rule of Professional Conduct 32:8.4(c) provides that ‘it is professional misconduct for a lawyer to ... engage in conduct involving dishonesty, fraud, deceit, or misrepresentation.’ To violate this rule, a lawyer must act with some level of scienter, which means the misrepresentation must be more than a negligent misrepresentation.”).

The Court of Appeals’ error will result in manifest injustice if left uncorrected. EMC is not the victim here, the Funds are. The Funds and their investors lost millions of dollars because of the misstatements or omissions made by Helicon and Witucki. Like so many other businesses and professionals, Helicon and Witucki purchased insurance specifically to cover this exact type of negligence. EMC collected premiums from Helicon and Witucki for this coverage grant. When it issued the EMC Policies, EMC was well aware it was issuing an insurance policy to a business involved in the issuance of bonds, and yet it chose: 1) to grant coverage for misstatements and omissions; 2) not to include any of the numerous securities exclusions employed by the insurance industry; and 3) to employ an exclusion that requires a determination, by judgment or adjudication, of dishonesty rather than merely allegations that could support an inference of dishonest intent. *See* Appellants’ Reply Brief at p. 4, n 4. EMC made these decisions in order to sell its policies and make money. It should not now be allowed to evade its

contractual obligations at the expense of innocent investors—particularly here, where the Opinion will unfairly harm so many other innocent insureds for years to come.

X. REQUEST FOR RELIEF

Wherefore, Defendant-Appellant Funds respectfully request this Court peremptorily reverse the Opinion or, in the alternative, grant the Funds' Application for Leave to Appeal.

Respectfully submitted,

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Dated: January 11, 2016

STATE OF MICHIGAN
IN THE SUPREME COURT

EMPLOYERS MUTUAL CASUALTY COMPANY

Supreme Court
No. _____

Plaintiff/Counter-Defendant-Appellee,

v.

Court of Appeals
No. 322215

HELICON ASSOCIATES, INC., a Michigan corporation, ESTATE OF MICHAEL J. WITUCKI, in its capacity a successor in interest to Michael J. Witucki, a deceased individual,

Wayne County Circuit Court
Case No. 12-002767-CK

Defendants/Counter-Plaintiffs,

and

DR. CHARLES DREW ACADEMY, a Michigan public school academy, JEREMY GILLIAM,

Defendants, and

WELLS FARGO ADVANTAGE NATIONAL TAX FREE FUND, a series of the Delaware business trust known as the Wells Fargo Funds Trust, Delaware Business Trust, WELLS FARGO ADVANTAGE MUNICIPAL BOND FUND (in part as successor to the Wells Fargo Advantage National Tax-Free Fund), a series of the Delaware business trust known as the Wells Fargo Funds Trust, a Delaware business trust, LORD, ABBETT MUNICIPAL INCOME FUND, INC., on behalf of its series Lord Abbett High Yield Municipal Bond Fund, a Maryland corporation, PIONEER MUNICIPAL HIGH INCOME ADVANTAGE, a Massachusetts business trust, by Pioneer Investment Management, Inc., its investment advisor,

Defendants-Appellants.

_____ /

DECLARATION OF SERVICE

I, Doris Jones, being first duly sworn, deposes and says that she is employed with the firm of KITCH DRUTCHAS WAGNER VALITUTTI & SHERBROOK, and that on the 11th

day of January, 2016, she served: **MOTION FOR LEAVE TO APPEAL BY DEFENDANT-APPELLANT FUNDS, NOTICE OF FILING SUPREME COURT APPLICATION, NOTICE OF HEARING, EXHIBITS, AND DECLARATION OF SERVICE** upon:

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by having same enclosed in an envelope with postage thereon fully prepaid and deposition in a United States postal receptacle, and

NOTICE OF FILING SUPREME COURT APPLICATION, AND DECLARATION OF SERVICE upon:

Clerk of the Court
Michigan Court of Appeals
3020 W. Grand Blvd.
Suite 14-300
Detroit, MI 48202

Clerk of the Court
Wayne County Circuit Court
2 Woodward Avenue
Detroit, MI 48226

by having same electronically filed.

I declare that the statements above are true to the best of my information, knowledge and belief.

s/Doris Jones
Doris Jones

STATE OF MICHIGAN
IN THE SUPREME COURT

EMPLOYERS MUTUAL CASUALTY COMPANY

Plaintiff/Counter-Defendant-Appellee,

v.

HELICON ASSOCIATES, INC., a Michigan corporation, ESTATE OF MICHAEL J. WITUCKI, in its capacity a successor in interest to Michael J. Witucki, a deceased individual,

Defendants/Counter-Plaintiffs,

and

DR. CHARLES DREW ACADEMY, a Michigan public school academy, JEREMY GILLIAM,

Defendants, and

WELLS FARGO ADVANTAGE NATIONAL TAX FREE FUND, a series of the Delaware business trust known as the Wells Fargo Funds Trust, Delaware Business Trust, WELLS FARGO ADVANTAGE MUNICIPAL BOND FUND (in part as successor to the Wells Fargo Advantage National Tax-Free Fund), a series of the Delaware business trust known as the Wells Fargo Funds Trust, a Delaware business trust, LORD, ABBETT MUNICIPAL INCOME FUND, INC., on behalf of its series Lord Abbett High Yield Municipal Bond Fund, a Maryland corporation, PIONEER MUNICIPAL HIGH INCOME ADVANTAGE, a Massachusetts business trust, by Pioneer Investment Management, Inc., its investment advisor,

Defendants-Appellants.

_____ /

Supreme Court
No. _____

Court of Appeals
No. 322215

Wayne County Circuit Court
Case No. 12-002767-CK

NOTICE OF FILING SUPREME COURT APPLICATION

TO: Clerk of the Court
Michigan Court of Appeals
3020 W. Grand Blvd.
Suite 14-300
Detroit, MI 48202

Clerk of the Court
Wayne County Circuit Court
2 Woodward Avenue
Detroit, MI 48226

PLEASE BE ADVISED that an Application for Leave to Appeal by Defendant-Appellant Funds has been filed with the Michigan Supreme Court.

Respectfully submitted,

DAVIS & CERIANI, P.C.

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VALITUTTI & SHERBROOK

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Dated: January 11, 2016