UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

Robert Verdun, *et al.*,

Plaintiffs,

v.

Twin City Fire Insurance Company,

Defendant.
_____/

***FILED UNDER SEAL***

Case No. 17-11254

Sean F. Cox
United States District Court Judge

**OPINION & ORDER**
**GRANTING DEFENDANT'S MOTION FOR JUDGMENT ON THE PLEADINGS**

This is an insurance coverage dispute. Currently pending before the Court are: 1) a Sealed Motion for Judgment on Pleadings filed by the Defendant Insurer; and 2) a Sealed Motion for Summary Judgment filed by the two insured Plaintiffs. The motions have been fully briefed by the parties and the Court heard oral argument on August 16, 2018. For the reasons below, the Court shall GRANT Defendant's Motion for Judgment on the Pleadings because no material fact relevant to Counterclaim Counts I & II (and Defendant's corresponding Affirmative Defenses 5 & 6) is disputed, and Judgment in favor of Defendant requires no factual development beyond the pleadings and documents attached to them. As explained below: 1) Plaintiff Robert Verdun is not covered under the policy at issue because the claim at issue was made against him only in his uninsured capacity as owner and seller of an insured company, not in his insured capacity as a director or officer; and 2) because the policy excludes coverage for Plaintiff Universal Exports Holdings, Inc., because the claim against it is based on and arises from Universal's liability under a contract, thereby implicating a contractual liability exclusion

in the Policy.

## BACKGROUND

### A. Procedural Background

Plaintiffs Robert Verdun ("Verdun") and Universal Exports Holdings, Inc. ("Universal") (collectively, "Plaintiffs") initiated this action on April 21, 2017. At that time, they filed a motion asking the Court to allow them to file the complaint under seal, because the complaint asserts causes of action arising out of Defendant's denial of insurance coverage for Plaintiffs' defense and settlement of an underlying claim brought against them by a non-party to this case. That settlement involved a confidentiality provision. Thus, the request to seal.

Plaintiffs' "Complaint for Declaratory Judgment and Other Relief and Jury Demand" includes the following counts: 1) "Declaratory Judgment Pursuant to 28 USC § 2201(a) (Covered Loss)" (Count I); 2) "Reformation" (Count II); 3) "Declaratory Judgment Pursuant to 28 USC § 2201(a) (Exclusion V(A)(1))" (Count III); 4) "Breach of Contract" (Count IV); and 5) "Bad Faith Under MCL § 500.2006(4)" (Count V).

Defendant Twin City Fire Insurance Company ("Twin City") filed a "Counterclaim for Declaratory Relief" (D.E. No. 16) seeking declaratory judgments of no coverage: 1) "Declaratory Judgment (No Coverage for Verdun - Insured Capacity" (Count I); 2) "Declaratory Judgment (No Coverage for Universal - Exclusion V(A)(1)" (Count II); 3) "Declaratory Judgment (No Coverage – Uninsurable)" (Count III); 4) "Declaratory Judgment (No Coverage – Exclusion IV(L)" (Count IV); and 5) "Declaratory Judgment (No Coverage – Exclusion IV(M)" (Count V).

The Scheduling Order in this matter provided that discovery closed on November 13,

2017 and that the parties were to file motions by January 31, 2018. (D.E. No. 26). But, perhaps because most facts are undisputed, the parties later stipulated to moving up the deadline for filing motions to December 15, 2017. (D.E. No. 27). That stipulation provided that, if the motions filed do not resolve the case, then the Court would set a new scheduling order that would provide a schedule for witness identification, discovery, and additional dispositive motions.

On December 15, 2017, Twin City filed a Sealed Motion for Judgment on the Pleadings (D.E. No. 32), along with a supporting brief (D.E. No. 33) and Statement of Material Facts Not in Dispute. (D.E. No. 34). Plaintiffs' filed a Sealed Response and brief in opposition to that motion (D.E. No. 39 & 40), along with a Sealed Counter-Statement of Material Facts. (D.E. No. 41).

In addition, on December 15, 2017, Plaintiffs filed a Sealed Motion for Summary Judgment. (D.E. No. 35). That motion includes two of the same issues that are included in Defendant's Motion for Judgment on the Pleadings (i.e., whether Verdun is entitled to indemnification as an Insured Person and whether Universal's right to indemnification is barred by the Policy's contract exclusion), along with other issues. This motion has also been fully briefed.

**B. Factual Background**

This Court's practice guidelines are included in the Scheduling Order and provide, consistent with Fed. R. Civ. P. 56 (c) and (e), that:

> a. The moving party's papers shall include a separate document entitled Statement of Material Facts Not in Dispute. The statement shall list in separately numbered paragraphs concise statements of each undisputed material fact, supported by appropriate citations to the record. . .
>
> b. In response, the opposing party shall file a separate document entitled

> Counter-Statement of Disputed Facts. The counter-statement shall list in separately numbered paragraphs following the order or the movant's statement, whether each of the facts asserted by the moving party is admitted or denied and shall also be supported by appropriate citations to the record. The Counter-Statement shall also include, in a separate section, a list of each issue of material fact as to which it is contended there is a genuine issue for trial.
>
> c. All material facts as set forth in the Statement of Material Facts Not in Dispute shall be deemed admitted unless controverted in the Counter-Statement of Disputed Facts.

(D.E. No. 16 at 2-3). The Guidelines further provide that while the above is required for summary judgment motions, counsel are strongly encouraged to follow them, to the extent possible, for other motions, such as motions for entry of judgment. (*Id.* at 3). And they did so here.

The parties complied with the Court's practice guidelines such that Plaintiffs' Motion for Summary Judgment includes a "Statement of Material Facts Not In Dispute" ("Pls.' Stmt. A") and Defendant's response brief includes a "Counter-Statement of Disputed Facts" ("Def.'s Stmt. A").[1] In addition, Defendant's Motion for Judgment on the Pleadings included a "Statement of Material Facts Not In Dispute ("Def.'s Stmt. B") and Plaintiffs' response included a Counter-Statement in response to it. ("Pls.' Stmt. B").

The following material facts are undisputed.

**Verdun's Role in CFI**

Computerized Facility Integration, LLC ("CFI") is a Michigan limited liability company that Verdun founded in 2001. From 2001 until May 2015, Verdun was CFI's President and

[1]Because Counsel for Twin City mis-numbered some paragraphs in its original Stmt. A, this Court granted an unopposed motion to allow Twin City to file a corrected version of it. (*See* D.E. Nos. 52-54).

managing member. (Stmts. A at ¶¶ 6-7).

Plaintiffs Verdun and Universal were the sole owners of CFI. (Stmts. B at ¶ 1). Verdun owned 55 percent of the membership interest individually and the remaining 45 percent indirectly through Universal.

**The Sale of CFI**

Effective May 1, 2015, Verdun, Universal and CFI entered into a Membership Interest Purchase Agreement with [redacted] (the "Purchase Agreement"). A true and accurate copy of the Purchase Agreement is located at Docket Entry No. 35-1.

Through that Purchase Agreement, Verdun and Universal sold CFI to [redacted] for [redacted]. (Stmts. B at ¶ 2).

The Purchase Agreement identified Verdun and Universal as the "*Sellers*." (*See* preamble and Definitions section of Purchase Agreement) (emphasis added). CFI was defined as the "Company" being sold, and [redacted] was defined as "the Buyer." (*Id.*).

In Article 3 of the Purchase Agreement, titled "Representations and Warranties Of Seller," the "Sellers" represented and warranted "to Buyer" numerous specified representations and warranties.

Article 3, in Section 3.25, with the heading "No Other Representations," disclaims any representations or warranties other than those set forth in the Purchase Agreement. Section 3.25 includes the following: "For the avoidance of doubt, except for the representations and warranties contained in this Article 3, *no warranty or representation is given on the contents of the documents provided during the due diligence investigation* conducted by or on behalf of Buyer, *including any information in the Data Room and any other reports, financial forecasts,*

*projections or information furnished* by or on behalf of the Company or the Sellers *or their officers, managers, employees, agents or representatives* or in any other documents or other information not contained in this Agreement or the Transaction Documents." (emphasis added).

Article 7 of the Purchase Agreement is titled "Indemnification." Section 7.02, has the heading "Indemnification *by Sellers*" and provides in pertinent part that "*each of the Sellers*" "shall indemnify and defend" Buyer and its affiliates "against, and shall hold each of them harmless from and against, and shall pay and reimburse each of them for, any and all Losses incurred or sustained by, or imposed upon, the Buyer Indemnitees based upon, arising out of, with respect to or by reason of" "any inaccuracy in or breach of any of the representations or warranties, as of the date hereof or as of the Closing Date, *made by the Sellers in this Agreement*." (Section 7.02 of Purchase Agreement) (emphasis added).

Section 7.05, with the heading "Indemnification Procedures," specifies how the parties to the Purchase Agreement can make claims. Subsection (c) of that section provides that a "direct claim" can be made by giving written notice of the claim. It provides that "Such notice by the Indemnified Party shall describe the Direct Claim in reasonable detail, shall include copies of all material written evidence thereof and shall indicate the estimated amount, if reasonably practicable, of the Loss that has been or may be sustained by the Indemnified Party."

Under the Purchase Agreement Verdun remained employed by the company in an executive capacity after the sale. (*Id.* at ¶ 19).

Verdun signed the Purchase Agreement individually, on his own behalf as a "Seller," on behalf of Universal, the other "Seller," and as the President of CFI, the Company being sold, in a signature page that was set forth as follows (with signatures appearing):

IN WITNESS WHEREOF, the parties hereto have executed and delivered this Agreement as of the date first written above.

**SELLERS:**

_____
Robert Verdun

UNIVERSAL EXPORTS
HOLDINGS, INC.
By: _____
Name: Robert A. Verdun
Title: President

**COMPANY:**

COMPUTERIZED
FACILITY INTEGRATION LLC

By: _____
Name: Robert A. Verdun
Title: President

**BUYER:**

[redacted]

By: _____
[redacted] Buyer [redacted]

(Signature page of Purchase Agreement) (underlining, bolding, and capitalization in original).

**[redacted] Buyer's Claim**

On August 9, 2016 [redacted] Buyer sent Verdun and Universal a written "Notice Of Direct Claims Against Robert Verdun & Universal Exports Holdings, Inc." ([redacted] Buyer's Claim"). A true and accurate copy of the Claim is located at Docket Entry No. 35-2.

The first page of the Claim, addressed to Robert Verdun, begins by stating that [redacted] Buyer is providing "notice of Direct Claims for Losses against you and Universal Exports Holdings, Inc.

(together, *the "Indemnifying Parties"*) pursuant to Section 7.05(c)" of the Purchase Agreement. (Claim at 1) (emphasis added).

That first page of the Claim asserts that, in connection with Buyer's acquisition of CFI, "*the Indemnifying Parties breached (a) the Purchase Agreement, including several of the Representations and Warranties of Seller set forth in Article 3 of the Purchase Agreement*, and (b) *the implied covenant of good faith and fair dealing*. Buyer estimates its Losses to be approximately [redacted]." (Purchase Agreement at 1) (emphasis added). That first page then summarizes the claim as follows:

> The *Indemnifying Parties* willfully *breached the Purchase Agreement by:* (i) providing intentionally inflated revenue and profit figures to Buyer; (ii) failing to disclose improper accounting practices utilized by CFI which masked the company's true performance; (iii) intentionally misleading Buyer regarding the status of CFI's largest contract, [redacted]; (iv) intentionally misrepresenting the value of the [redacted] revenues and receivables; and (v) failing to disclose that CFI's top salesman responsible for a large percentage of CFI's sales was terminally ill and out of medical leave at the time of negotiation and the closing, and that he would either not return to work or would return only in a limited capacity, thus significantly reducing CFI's future revenues. The Indemnifying Parties' wrongful conduct is described in greater detail below and the documentary evidence referenced below is enclosed with this Notice in accordance with Section 7.05(c) of the Purchase Agreement.

Pages 2 through 5 then contain separate sections that detail each of those claimed breaches of the Purchase Agreement. Each of those sections then details the history of the claimed breach of the Purchase Agreement. Some of those sections note that the alleged false or misleading information, that was later incorporated into the Purchase Agreement, was first presented during negotiations and due diligence.

But each of those sections concludes by: 1) stating, "Accordingly, the *Indemnifying*

*Parties* breached the following *representations set forth in the Purchase Agreement*," and then lists specific sections of the Purchase Agreement; and 2) identifying the Purchase Agreement and its attachments/schedules as the documentary and written evidence in support of the claimed breaches. (Claim, Ex. 2 at 1) (Stmts. A at ¶¶ 22-23) (emphasis added).

**Settlement of the Underlying Claim**

Verdun and Universal retained defense counsel to represent them in responding to the Claim. Verdun and Universal denied and continue to deny the allegations of the Claim.

On September 27, 2016, Verdun entered a Confidential Settlement Agreement and Release with [redacted] (the "Settlement Agreement"). The Settlement Agreement referred to Verdun and Universal as the "Sellers" of the underlying Purchase Agreement. (Settlement Agreement at 1).

Verdun executed the Settlement Agreement with [redacted] in a signature page that was set forth as follows (with signatures appearing):

> IN WITNESS WHEREOF, the parties hereto, intending to be legally bound, have executed this Agreement as of the day and year first written above.
>
> **SELLERS:**
>
> _____
> ROBERT VERDUN
>
> UNIVERSAL EXPORT HOLDINGS, INC.
>
> By: _____
> Name: Robert A. Verdun
> Title: President
>
> **BUYER:**
>
> [redacted]
>
> By: _____
> [redacted]

A true and accurate copy of the Settlement Agreement is located at Docket Entry No. 35-3. (Stmts. A at ¶¶ 31-33).

[redacted] There has never been any judgment or final non-appealable adjudication that Verdun or Universal were liable for Buyer's Claim. (Stmts. A at ¶¶ 40-42).

**The Twin City Policy**

Plaintiffs now seek to recover for the settlement payment under an insurance policy issued by Defendant Twin City. (Stmts. B at ¶ 9).

Defendant Twin City issued a "Private Choice Ovation" Policy Number 35-KB 0279792-14 to CFI as named insured (the "Policy"). A true and accurate copy of the Policy is located at Docket Entry No. 35-4. The Policy defines the Policy Period as June 30, 2014 to June 30, 2015. (Stmts. A at ¶¶ 45-46).

The Policy contains a Directors, Officers and Entity Liability Coverage Part (the "D&O Coverage Part"). It contains two Insuring Agreements that are relevant here: 1) an "Insured Person Liability" Insuring Agreement; and 2) an "Entity Liability" Insuring Agreement. The Aggregate Limit of Liability for the D&O Coverage Part is $1 million. (Stmts. A at ¶ 48-49).

**Insuring Agreement A**

Insuring Agreement A, which is entitled Insured Person Liability, of the D&O Coverage Part provides:

> The Insurer shall pay Loss on behalf of the Insured Persons resulting from an Insured Person Claim first made against the Insured Persons during the Policy Period or Extended Reporting Period, if applicable, for a Wrongful Act by the Insured Persons, except for Loss that an Insured Entity pays to

or on behalf of the Insured Persons as indemnification.

(Stmts. A at ¶ 50).

"The Policy defines Insured Person to include any natural person who is or was a duly elected or appointed director or officer of Universal or CFI. The definition of Insured Person does not include owners of or persons with membership interests in Universal or CFI." (Stmts. B at ¶ 12).

As to an Insured Person, the Policy defines a "Wrongful Act," in pertinent part, as "any actual or alleged:" 1) "error, misstatement, misleading statement, act, omission, neglect or breach of duty committed by an Insured Person *in their capacity as such*"; or 2) matter claimed against an Insured Person, solely by reason of their serving in such capacity. (Stmts. A at ¶ 56) (emphasis added).

The Policy defines Insured Person Claim, in pertinent part, as any "*written demand* for monetary damages or other civil-non-monetary relief commenced by the receipt of such demand against an Insured Person." An Insured Person Claim constitutes a Claim under the Policy. (Stmts. A at ¶ 53) (emphasis added).

In this action, Verdun claims that he is "an Insured Person under the Policy because he was president of CFI and therefore was a duly elected or appointed officer of CFI." (Compl. at ¶ 48).

**Insuring Agreement C**

Insuring Agreement C of the D&O Coverage Part, entitled Entity Liability (Elective), provides in part that:

> [T]he Insurer shall pay Loss on behalf of an Insured Entity resulting from an Entity Claim first made against such Insured Entity during the Policy Period or Extended Reporting Period, if applicable, for a Wrongful Act by the Insured Entity.

(Stmts. A at ¶ 51).

As to an Insured Entity, the Policy defines a "Wrongful Act," in pertinent part, as "any actual or alleged" "error, misstatement, misleading statement, act, omission, neglect or breach of duty" committed by an Insured Entity.

The Policy defines an Entity Claim, in part, as any "written demand for monetary damages or other civil-non-monetary relief commenced by the receipt of such demand [...] against an Insured Entity." The Policy defines Insured Entity to include a Subsidiary.

**Relevant Policy Provisions That Apply To Both Insuring Agreements**

The Policy defines Loss as Defense Costs and Damages. The Policy defines Damages as "the amounts, other than Defense Costs, that the Insureds are legally liable to pay solely as a result of a claim covered by this [D&O] Liability Coverage Part, including: (1) compensatory damages; (2) settlement amounts; ... ." (Stmts. A at ¶ 57-58).

The Policy provides that "Damages shall not include . . . matters uninsurable pursuant to any applicable law." (Stmts. B at ¶ 14). The parties refer to this as the "uninsurable" provision. (Stmts. A at ¶ 59).

Exclusion IV-L in the D&O Coverage Part states that the insurer shall not pay Loss "of an Insured, based upon, arising from, or in any way related to gaining of any personal profit, remuneration or advantage to which such Insured is not legally entitled *if a judgment or other non-appealable final adjudication establishes that such a gain did occur.*" (Emphasis added). The parties refer to this as Exclusion IV-L as the "ill-gotten gains" exclusion. (Stmts. A at ¶ 60).

Exclusion IV-M in the D&O Coverage Part states that the insurer shall not pay for Loss of an Insured "based upon, arising from, or in any way related to any criminal or deliberately fraudulent act or omission or any willful violation of law by such Insured *if a judgment or other non-*

*appealable final adjudication establishes such an act, omission or violation* [...]." (Emphasis added.) . The parties refer to this as Exclusion IV-M as the "criminal and deliberate fraud" exclusion. (Stmts. A at ¶ 61).

The parties refer to Exclusion V (A)(1) as the "contract" exclusion. Exclusion V(A)(1) in the D&O Coverage Part states:

> The Insurer shall not pay Loss under Insuring Agreement (C) in connection with any Claim based upon, arising from, or in any way related to any actual or alleged ... liability under any contract or agreement, provided that this exclusion shall not apply to the extent that liability would have been incurred in the absence of such contract or agreement.

(Stmts. A at ¶ 62).

**Twin City's Denial of Coverage**

Twin City denied coverage under the Policy and Plaintiffs Verdun and Universal filed this action seeking insurance coverage for the settlement payment.

It is undisputed that Buyer's August 9, 2016 letter is a Claim under the Policy because it is a written demand for monetary relief against an Insured Person (Verdun) and an Insured Entity (Universal). (Stmts. A at ¶ 63). The Claim asserts "Wrongful Acts" by an Insured Entity. (*Id.* at ¶ 82).

Verdun notified Twin City of a Potential Claim on July 14, 2016. (Stmts. A at ¶ 66). Verdun notified Twin City of the Claim on August 22, 2016. (Stmts. A at ¶ 67).

Plaintiffs informed Twin City of the terms of a potential settlement with Buyer before entering the Settlement Agreement. Twin City agreed that it would not assert lack of consent to settlement as a coverage issue. (Stmts. A at ¶ 68).

"Verdun is an Insured Person under the Policy because he was president of CFI and therefore

was a duly elected or appointed officer of CFI." (Twin City's Answer at ¶ 48). Twin City agreed to treat Universal as a Subsidiary, qualifying as an Insured Entity under the terms of the Policy, based upon representations made to Twin City by Plaintiffs. (Stmts. A at ¶ 70; Twin City's Answer at ¶ 45).

There is no judgment or other non-appealable final adjudication establishing that Verdun or Universal gained any personal profit, remuneration or advantage to which they are not legally entitled. (Stmts. A at ¶ 71).

After the Complaint was filed, Twin City reimbursed Plaintiffs' defense costs as an "accommodation." (Stmts. A at ¶ 72). The Policy's $1 million limit was eroded by Twin City's reimbursement of Plaintiffs' defense costs after the lawsuit was filed. The remaining limit is $888,393. (Stmts. A at ¶ 73).

## ANALYSIS

This Court has diversity jurisdiction over this insurance-coverage dispute and the parties agree that Michigan law governs. As the Sixth Circuit has explained:

> Under Michigan law, "insurance policies are subject to the same contract construction principles that apply to any other species of contract," and "unless a contract provision violates law or one of the traditional defenses to the enforceability of a contract applies, a court must construe and apply unambiguous contract provisions as written." *Rory v. Cont'l Ins. Co.*, 473 Mich. 457, 703 N.W.2d 23, 26 (2005).

*Northern Ins. Co. of New York v. Target Corp.*, __ F. App'x __, 2017 WL 5899790 at * 3 (6th Cir. 2017).

Defendant Twin City filed a Motion for Judgment on the Pleadings and Plaintiffs filed a

Motion for Summary Judgment. For the most part,[2] however, both motions are based upon the same four things: 1) the Purchase Agreement; 2) the Policy; 3) the Claim; and 4) the Settlement. As such, the Court shall first address Twin City's Motion for Judgment on the Pleadings.[3]

## I. Twin City's Motion For Judgment On The Pleadings

In its Motion for Judgment on the Pleadings, Twin City moves for judgment on pleadings as to Counterclaims I, II, and III, and its corresponding affirmative defenses. [4]

### A. Standard of Decision

Under Fed. R. Civ. P 12(c), "[a]fter the pleadings are closed – but early enough not to delay trial – a party may move for judgment on the pleadings." The Sixth Circuit has explained:

> "For purposes of a motion for judgment on the pleadings, all well-pleaded material allegations of the pleadings of the opposing party must be taken as true, and the motion may be granted only if the moving party is nevertheless clearly entitled to judgment." *S. Ohio Bank v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 479 F.2d 478, 480 (6th Cir. 1973). But we "need not accept as true legal conclusions or unwarranted factual inferences." *Mixon v. Ohio*, 193 F.3d 389, 400 (6th Cir. 1999). A Rule 12(c) motion "is granted when no material issue of fact exists and the party making the motion is entitled to judgment as a matter of law." *Paskvan v. City of Cleveland Civil Serv. Comm'n*, 946 F.2d 1233, 1235 (6th Cir. 1991).

---

[2]Plaintiffs' Motion for Summary Judgment also attached portions of Verdun's deposition and an affidavit from him.

[3]Twin City filed its Motion for Judgment on the Pleadings, pursuant to Fed. R. Civ. 12(c). In response to it, Plaintiffs "request that the Court accept Exhibits 5-8 [that they filed in response to the motion] and convert Defendant's Motion to one for Summary Judgment." (Pls.' Resp. Br. at 2). The Court declines to so, and shall rule on the motion as filed. Otherwise, Twin City asks to take discovery before the Court rules on the issues. (*See* Def.'s Reply Br. at 1-2).

[4]In a footnote Twin City states that it "has asserted other defenses beyond the scope of this motion, which require extensive additional factual development and will be pursued by Twin City if the Court denies this motion." (Def.'s Motion at 2 n.1).

*Jackson v. Professional Radiology, Inc.*, 864 F.3d 463, 466 (6th Cir. 2017).

On a motion for judgment on the pleadings, the court may consider the pleadings themselves and exhibits incorporated by reference into the complaint. *Haeberle v. University of Louisville*, 90 F. App'x 895, 899 (6th Cir. 2004). Thus, in addition to the pleadings, the Court may consider the Purchase Agreement, the Policy, the Claim, and the Settlement Agreement, without converting the motion into a motion for summary judgment.

**B. Issues Presented In Twin City's Motion**

Twin City asserts that the settlement payment at issue here is not payable for three reasons: 1) because the Buyer claim was made against Verdun only in his uninsured capacity as owner and seller of an insured company, not in his insured capacity as a director or officer; 2) because the policy excludes coverage for Universal because Buyer's claim is based on and arises from Universal's liability under a contract (the Purchase Agreement), thereby implicating a contractual liability exclusion in the Policy; and 3) because the settlement payment represented Plaintiffs' return of consideration received in the sale of CFI, which is uninsurable disgorgement and not an insurable loss.

The Court need not reach the third issue if it agrees with Twin City on the first two issues. As such, the Court will address those issues first.

**1. Is Verdun Covered Under The Policy?**

The first issue presented in the motion is whether Verdun is entitled to indemnification under the Policy.

As the Sixth Circuit has recognized, "[u]nder Michigan law, the insured has the burden of proving coverage. *American Tooling Center, Inc. v. Travelers Cas. & Surety Co.*, __ F.3d __,

2018 WL 3404708 at *2 (6th Cir. 2018) (citations omitted).

The Policy contains a Directors, Officers and Entity Liability Coverage Part (the "D&O Coverage Part"). Verdun claims that he is "an Insured Person" under the Policy because he was president of CFI and therefore was a duly elected or appointed officer of CFI. (Compl. at ¶ 48).

The Policy defines Insured Person Claim, in pertinent part, as any "written demand for monetary damages or other civil-non-monetary relief commenced by the receipt of such demand against an Insured Person." An Insured Person Claim constitutes a Claim under the Policy. (Stmts. A at ¶ 53). The Policy defines a Wrongful Act, in pertinent part, as:

> (1) any actual or alleged . . . error, misstatement, misleading statement, act, omission, neglect or breach of duty committed by an Insured Person *in their capacity as such* [...], or, with regard to Insuring Agreement (C) an Insured Entity; or
>
> (2) matter claimed against an Insured Person, solely by reason of their serving in such capacity [...]."

(Stmts. A at ¶ 56) (emphasis added).

Accordingly, the parties agree that: 1) claims brought against Verdun in his capacity as the owner or seller of CFI *are not* covered under the Policy; and 2) claims brought against Verdun in his capacity as the President of CFI *are* covered under the Policy.[5]

Plaintiffs argue that Verdun is entitled to coverage for alleged Wrongful Acts undertaken in his insured capacity as an officer of CFI. Verdun argues that he acted in that capacity when the alleged wrongful acts occurred, i.e., during negotiations and due diligence before the sale to Buyer. Verdun argues that his right to indemnification as an insured officer of CFI is not eviscerated by his

[5]In this action, Verdun asserts that he is "an Insured Person under the Policy because he was president of CFI and therefore was a duly elected or appointed officer of CFI." (Compl. at ¶ 48).

status as CFI's owner/seller (an uninsured capacity). Plaintiffs argue that, under the terms of the Policy, as long as Verdun committed the alleged wrongful acts as an officer of CFI it is irrelevant that he was also CFI's owner.

Plaintiffs first argue that Verdun's ownership of CFI does not negate his right to coverage as an insured officer of CFI. That is, they argue that his dual capacity does not defeat coverage for an insured officer. They direct the Court to *McAininch v. Wintermute*, 491 F.3d 759 (8th Cir. 2007) and *Ratcliffe v. International Surplus Lines Ins. Co.*, 550 N.E.2d 1052 (1990).

Plaintiffs note that in *McAninch*, the Eighth Circuit found that the policy did not require that an officer who was also an owner act "solely" in her insured capacity. But in that case, the indictment at issue expressly alleged that the officer at issue acted in *both* her capacity as an owner and as a director. *McAinich,* 491 F.3d at 763. Because the indictment clearly alleged wrongful conduct against the insured taken in her capacity as a director, the court found that the fact that it also alleged that she acted in her capacity as owner did not defeat coverage.

Similarly, in *Ratcliffe,* the Illinois state court found that the policy at issue did not limit coverage to acts that were committed "solely" by the insured in their capacities as officers or directors. *Ratcliffe, supra*, at 1059.

Here, however, Twin City does not argue that the Policy requires that Verdun was acting "solely" in his capacity as an officer of CFI in order to be covered; it acknowledges the Policy has no such requirement. Rather, Twin City argues that the Claim at issue was asserted against Verdun only in his capacity as the owner/seller of CFI and therefore there is no coverage. That is, unlike the insurer in *McAinich*, Twin City does not assert that a "dual capacity" defeats coverage for an insured person who is accused of acting in both his uninsured and insured capacities. What Twin

City argues is, that based on the record before the Court, the Claim at issue here was only asserted claims against Verdun in his capacity as a seller/owner of CFI and therefore there is no coverage.

As an additional argument, Plaintiffs assert that the Purchase Agreement "is clear" that the phrase "Seller" means Verdun as both a CFI Officer and as its owner. (*See* Pls.' Br. at 9). Plaintiffs argue that because Verdun signed the Purchase Agreement as both CFI's owner and as its President, the term "Seller" should be construed as referring to Verdun "in all capacities." *(Id.)*.

Twin City responds that the above argument is preposterous, explaining as follows in its Reply Brief:

> Seeking to avoid the inescapable conclusion that "Seller" means "seller," Plaintiffs advance a preposterous definition of "Seller" that includes Verdun "in all capacities," inferring from Purchase Agreement's preamble a nonsense equation: "'Seller'" = Verdun = As CFI Officer and Owner." *Id.* at 9. Verdun was a Seller because he sold the company (which he could do only in his owner capacity" not because he managed the company that was sold.

(Def.'s Reply at 3).

The Court agrees with Twin City that this argument is simply not supported by the terms of the Purchase Agreement.

It is undisputed that at the time of the sale, Verdun and Universal were the sole owners of CFI, the company that was sold under the Purchase Agreement. Thus, the Purchase Agreement identified Verdun and Universal to each be a "Seller" under the Purchase Agreement. (*See* preamble and definition sections of Purchase Agreement). Verdun signed the Purchase Agreement individually on his own behalf as a Seller, and on behalf of the other Seller, Universal. Verdun also signed the Purchase Agreement as the President of CFI, which was the company being sold, not a seller. There is simply no way to construe the term "Seller" as having referred to Verdun in his capacity as CFI's president.

Twin City asserts that Verdun is not entitled to coverage because the Buyer Claim was simply not made against him in his asserted insured capacity as President of CFI. It contends that, when you examine the relevant terms of the Purchase Agreement, the Policy provisions, and the Claim at issue, it is clear that the Buyer Claim was made against Verdun solely in an uninsured capacity, as the seller of CFI.

Twin City asserts that "it is mere happenstance that Mr. Verdun, a Seller in his personal capacity, was also the officer that executed the Purchase Agreement on behalf of CFI," the company that was sold. (Def.'s Br. at 9).

The parties have not directed the Court to any Michigan cases that deal with this issue. Moreover, they only direct the Court to a few cases on this issue and none of them are very analogous to the facts that we have here because, in those cases, there was either a criminal indictment or a complaint that specified the capacity or capacities under which the person was sued. We do not have such express allegations as to capacity here, as the claim was settled before a complaint was filed in court.

Accordingly, the Court must look to the Purchase Agreement, the Policy, and the Claim in order to determine if the Claim against Verdun was one made against him in his capacity as President of CFI. This Court concludes that when you do that, Verdun lacks coverage.

Answering two questions regarding the Claim shows that it was not made against Verdun in his capacity as President of CFI.

First, the Court considers the nature of the claim at issue; *what was alleged to have been breached in the Claim*? In its Claim, Buyer asserted that *specific representations and warranties in the Purchase Agreement* were breached. While the Claim noted, during the narrative portion of

the Claim letter, that the alleged false or misleading information, that was later incorporated into the Purchase Agreement, was first presented during negotiations and due diligence, the Claim itself was based upon the representations and warranties in the Purchase Agreement. Moreover, the Purchase Agreement itself expressly disclaimed, in Article 3, Section 3.25, any representations or warranties other than those in the purchase agreement – including any representations or information provided by the Company (CFI) or its officers during due diligence.

Second, the Court should consider *who* is alleged to have breached the representations and warranties in the Purchase Agreement? Buyer's Claim was directed to Robert Verdun and Universal, who were the only two "Sellers" identified in the Purchase Agreement. Moreover, the first page of the Claim, addressed to Robert Verdun, begins by stating that Buyer is providing "notice of Direct Claims for Losses against you and Universal Exports Holdings, Inc. (together, *the "Indemnifying Parties"*) pursuant to Section 7.05(c)" of the Purchase Agreement. (Claim at 1) (emphasis added).

Thus, the Claim expressly stated that is was a "Direct Claim" pursuant to Section 7.05(c) of the Purchase Agreement. Article 7 provides that the *"Sellers"* will indemnify Buyer for losses arising out of "any inaccuracy in or breach of any of the representations or warranties, as of the date hereof or as on the Closing Date, *made by Sellers* in this Agreement . . . " (Purchase Agreement at Section 7.02(a)) (emphasis added). Article 7 does not provide for Direct Claims against officers of the contracting parties, nor does it contain any reference to such officers. As such, Verdun in his capacity as President of CFI cannot be an indemnifying party under the Purchase Agreement.

The Court agrees with Twin City that the "inescapable conclusion" is the Buyer was not

asserting a Claim under Article 7 against Verdun in his capacity as President of CFI. As such, he lacks coverage under the Policy.

**2. Does The Contract Exclusion Bar Coverage Of The Claim Against Universal?**

The second issue is whether Universal is covered under the policy, in light of the Contract Exclusion.

"If the insured demonstrates that the policy provides coverage, then the insurer has the burden of showing that an exclusion precludes coverage." *American Tooling Center, Inc. v. Travelers Cas. & Surety Co.*, __ F.3d __, 2018 WL 3404708 at *2 (6th Cir. 2018) (citations omitted).

"Exclusionary clauses in insurance policies are strictly construed in favor of the insured." *Northern Ins. Co. of New York v. Target Corp.*, supra, at *3. "However, 'it is impossible to hold an insurance company liable for a risk it did not assume,' and, thus, 'clear and specific exclusions must be enforced.' " *Id.* at 566 (internal alterations and citations omitted).

The parties refer to Exclusion V (A)(1) in the Policy as the Contract Exclusion and it states as follows:

> The Insurer shall not pay Loss under Insuring Agreement (C) in connection with any Claim *based upon, arising from, or in any way related to any actual or alleged ... liability under any contract or agreement*, provided that this exclusion shall not apply to the extent that liability would have been incurred in the absence of such contract or agreement.

(Stmts. A at ¶ 62) (emphasis added).

Plaintiffs contend that the Policy's Contract Exclusion does not apply here because the alleged misrepresentations and omissions were made before the contract at issue was executed, to induce the aggrieved party ([redacted]) to enter the contract (the Purchase Agreement). They

direct the Court to a single, non-binding decision from Pennsylvania, *McPeek v. Travelers Cas. and Surety Co. of America*, 2006 WL 1308087 (W.D. Pa. 2006) in support of their position.

Defendants contend that the Contract Exclusion applies "because the Buyer Claim is based upon, arises from, and is related to the alleged contractual liability." (Def.'s Resp. Br. at 5). Defendant argues that "Plaintiffs' only argument to the contrary, that the misrepresentations were pre-contractual, was rejected in *Certified Restoration Drycleaning Network, LLC v. Fed. Ins. Co.*, 2013 WL 1629291 (E.D. Mich. Apr. 16, 2013) and that *McPeek* is easily distinguishable because the alleged pre-contractual representations were not incorporated into the contract in that case.

The Court concludes that Plaintiffs' reliance on *McPeek* is misplaced and that Universal's right to indemnification is barred by plain language of the Contract Exclusion.

In *McPeek*, the lawsuit was brought against multiple defendants and included both breach of contract and misrepresentation counts. The policy at issue had a contract exclusion similar to the one we have here. The court found that the misrepresentation claims against two specific defendants (McPeek and Herget) were not barred by the contract exclusion because the claims against them were based upon pre-contract fraud, not contractual liability. The court concluded that it is more appropriate to characterize the claims against those defendants as arising out of pre-contract misdeeds, rather than arising out of the contracts. Although it was not determinative, the court found it relevant that no breach of contract claims had been asserted against either McPeek or Herget. *McPeek, supra*, at *4.

A later, published, decision from a Pennsylvania district court also involved a contract exclusion nearly identical to the one in this case. *Federal Ins. Co. v. KDW Restructuring and*

*Liquidation*, 889 F.Supp.2d 694 (M.D. Pa. 2012). The parties there agreed that any breach of contract claims were barred by the contract exclusion but disagreed as to whether misrepresentation claims based on pre-contractual representations and omissions were barred. The insured in that case relied on *McPeek* to support its position. The district court noted that *McPeek* could be distinguished in that the two insureds at issue there did not have breach of contract claims asserted against them. It also noted a "critical distinction" between *McPeek* and the case before it – "the alleged negligent misrepresentations and fraud were expressly made part of the contracts and that in the absence of the contracts, [the insureds] would not have been liable." *Id.* at 707. The court found that because the financial information relied on by the plaintiffs had been incorporated into the purchase agreements, the fraud and misrepresentation claims "are based upon, raise from, or are in consequence of" the insured's liability under the contract and were barred by the exclusion.

The same is true here – Buyer asserted breach of contract claims against Plaintiff and the alleged pre-contractual misrepresentations were incorporated into the Purchase Agreement. And, like the situation in *Federal Ins. Co.*, but unlike *McPeek*, had Buyer not entered into the Purchase Agreement, there would be no independent misrepresentation claims against Plaintiffs. *See also Certified Restoration Drycleaning Network, LLC v. Federal Ins. Co.*, 2013 WL 1629291 (E.D. Mich. 2013) (rejecting argument that contract exclusion did not apply because pre-contractual misrepresentations had been made and noting that the "basis of the injuries alleged" in the complaint against the insured arose from the insured's breach of the agreement.).

Again, the Contract Exclusion here excludes any claim "based upon, arising from, or in any way related to" liability under a contract. Giving plain meaning to the unambiguous

language of that exclusion, the claims asserted against Universal in Buyer's Claim are excluded because they are "based upon, arising from, or in any way related to" liability under the Purchase Agreement. Thus, Universal lacks coverage.[6]

## CONCLUSION & ORDER

For the reasons set forth above, the Court GRANTS Defendant's Motion for Judgment on the Pleadings is GRANTED and this action is DISMISSED WITH PREJUDICE.

IT IS SO ORDERED.

s/Sean F. Cox
Sean F. Cox
United States District Judge

Dated: August 27, 2018

I hereby certify that a copy of the foregoing document was served upon counsel of record on August 27, 2018, by electronic and/or ordinary mail.

s/Jennifer McCoy
Case Manager

I hereby certify that the foregoing is a true copy of the original on file in this Office.
CLERK, U.S. DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
BY: _____ Deputy

[6]Given the Court's rulings on these first two issues, the Court need not reach Twin City's additional argument that because the settlement payment represented Plaintiffs' return of consideration received in the sale of CFI, it is uninsurable disgorgement and not an insurable loss.