E-FILED
11/8/2018 3:02 PM
CLERK & MASTER
DAVIDSON CO. CHANCERY CT.

IN THE CHANCERY COURT FOR THE STATE OF TENNESSEE
TWENTIETH JUDICIAL DISTRICT, DAVIDSON COUNTY

ZANDER GROUP HOLDINGS, INC.; JEFFREY J. ZANDER; BRIAN EAGLE, as Trustee of the Zander Group Holdings, Inc. Employee Stock Ownership Plan; and STEPHEN M. THOMPSON,	)	
Plaintiffs,	)	
vs.	)	**No. 17-1246-BC**
FEDERAL INSURANCE COMPANY,	)	
Defendant.	)	

MEMORANDUM AND ORDER: (1) GRANTING IN PART AND DENYING IN PART PLAINTIFFS' MOTION FOR PARTIAL SUMMARY JUDGMENT AND (2) SETTING 11/16/18 DEADLINE TO RESPOND ON SCHEDULING CONFERENCE

This lawsuit is an insurance coverage dispute. The Plaintiffs/Insureds allege that, with respect to a federal court lawsuit where they have been sued for breach of fiduciary duties, the Defendant//Insuror wrongfully claims that its limit of liability coverage is $1,000,000, and claims that, with respect to Plaintiff Thompson, coverage is prorated between the Defendant and another insuror. The Plaintiffs' position is that the limit of liability applicable to the federal court lawsuit is $3,000,000 and that the Thompson coverage is only excess coverage not subject to proration. These disputes are particularly significant for these parties because the insurance policy in issue provides that defense

costs are deducted from, not paid in addition to, the coverage limits. The Plaintiffs have asserted in the *Second Amended Complaint* filed June 11, 2018 four causes of action:

Count 1 – Failure To Deal Fairly and in Good Faith,

Count 2 – Breach of Contract,

Count 3 – Declaratory Judgment (Liability Limit), and

Count 4 – Declaratory Judgment (Excess Coverage).

The Defendant denies the Plaintiffs' allegations and claims, and has asserted 25 affirmative defenses.

The case is presently before the Court on a motion for partial summary judgment (the "*Motion*") filed by two of the Plaintiffs, Zander Group Holdings, Inc. and Jeffrey J. Zander (the "Plaintiffs")[1]concerning Counts 2, 3 and 4 of the June 11, 2018 *Second Amended Complaint.* The *Motion* asserts there are no genuine issues of material fact and asserts that judgment in favor of the Plaintiffs should be entered declaring, under Count 3, that the policy at issue provides $3 million in coverage; entering a finding pursuant to Tennessee Civil Procedure Rule 56.05 that the Defendant's repudiation of the 3 million coverage constitutes a breach under Count 2; and as to Count 4 declaring that the fiduciary liability policy at issue provides only excess coverage to Plaintiff Thompson because he is covered under a separate policy. The Defendant opposes the *Motion* and asserts it should be denied and fulsome discovery[2] should proceed.

[1] Plaintiffs Brian Eagle and Stephen M. Thompson did not join in the *Motion.*

[2] In a July 10, 2018 Order discovery was limited to see if initially the claims in the lawsuit could be narrowed or the issues focused for discovery.

After considering the law, the record and argument of Counsel, the Court determines that the *Motion* shall be granted in part, and that, as to the portion of the *Motion* that is denied, fulsome discovery shall proceed on those remaining claims.

It is therefore ORDERED that the Plaintiffs' motion for summary judgment is granted with respect to Endorsement No. 3, and the Court declares that Endorsement No. 3 is not ambiguous and that the plain, ordinary meaning of Endorsement No. 3 does not provide the Defendant a defense to $3 million coverage in this case.

It is further ORDERED that with respect to Plaintiffs' summary judgment motion concerning the applicability of the Increased/Excess Limits Warranty to Policy No. 82379126, the *Motion* is denied but not on the merits. More development of the facts and application of the law to the facts is needed for this issue to be decided. The summary judgment filings revealed facts that a mistake was made by the Defendant in referencing the wrong policy number on the Warranty. Accordingly, full discovery shall proceed, and leave is granted to amend the *Answer* if the Defendant determines that an amendment is needed. This ruling, the Court repeats, is not on the merits, and issues concerning the application of the Increased/Excess Limits Warranty remain pending.

With respect to the last part of Plaintiffs' motion for summary judgment, it is denied. The Court determines that the plain text of the insurance policy in issue establishes that it is irreconcilable with Plaintiff Thompson's Great American professional liability policy, and under Tennessee law the costs of defending Plaintiff

Thompson must be prorated. It is therefore ORDERED that the Plaintiffs' motion for summary judgment on Count 4 of the *Second Amended Complaint* is denied. It is additionally ORDERED that based on the determination herein that the two excess coverage clauses are void as a matter of law, Count 4 is dismissed with prejudice because issues relating to the scope of coverage and an insurer's duty to defend present questions of law when there are no disputed material facts.[3]

It is additionally ORDERED that the July 10, 2018 stay on additional discovery between the parties is lifted.

[3] Dismissal of Plaintiffs' Count 4 Declaratory Judgment action is the logical result of the Court's denial of the Plaintiffs' motion for summary judgment. The Count 4 declaratory judgment claim related solely to an issue of contract construction as a matter of law to which there are no genuine issues of material fact. Under Tennessee law, it is appropriate for the Court to *sua sponte* dismiss this claim with prejudice based on the denial of the Plaintiffs' motion for summary judgment. *See, e.g., Patton v. Estate of Upchurch*, 242 S.W.3d 781, 791 (Tenn. Ct. App. 2007) ("Trial courts also have the authority to grant summary judgment *sua sponte*, but 'only in rare cases and with meticulous care" when "the party against whom summary judgment is rendered has had a full and fair opportunity to meet the proposition that there is no genuine issue of material fact to be tried, and that the party for whom summary judgment is rendered is entitled thereto as a matter of law.'") (citation omitted); *Policeman's Ben. Ass'n of Nashville v. Nautilus Ins. Co.*, No. M2001-00611-COA-R3CV, 2002 WL 126311, at *6 (Tenn. Ct. App. Feb. 1, 2002) ("Where the relevant facts are not in dispute, issues relating to the scope of coverage and an insurer's duty to defend present questions of law and are properly resolved by summary judgment."); *Victoria Ins. Co. v. Hawkins*, 31 S.W.3d 578, 580 (Tenn. Ct. App. 2000) ("The Trial court denied Victoria's motion for summary judgment and sua sponte granted judgment to defendants."); *Minton v. Long*, 19 S.W.3d 231, 240 (Tenn. Ct. App. 1999) ("Had the trial judge been correct in granting summary judgment to the Mintons on the basis that the foreclosure sale did not terminate the easement and that the intent of the trustee in the deed to Third National Bank was to transfer the property subject to the easement as a matter of law, then it would have logically followed that the dismissal of the counter-claim, whether *sua sponte* or otherwise, was also a correct action."); *Planet Rock, Inc. v. Regis Ins. Co.*, 6 S.W.3d 484, 490 (Tenn. Ct. App. 1999) ("The issues relating to the scope of coverage and an insurer's duty to defend present questions of law which can be resolved by summary judgment when the relevant facts are not in dispute.") (citations omitted).

It is further ORDERED that by November 16, 2018, Counsel shall contact the Docket Clerk, Mrs. Smith (615-862-5719), on their availability to participate in a Rule 16 Conference by telephone on the following dates and times:

December 3, 2018 at noon, and
December 5, 2018 at noon.

During the telephone conference deadlines for discovery to be completed, whether referral to mediation would be productive, amendment of the pleadings, and selection of a trial date shall be discussed.

The undisputed facts and law on which the foregoing rulings are based are provided below.

Plaintiffs' Motion For Partial Summary Judgment

The Plaintiffs seek entry of summary judgment[4] that the Court declare: (1) that the applicable amount of liability coverage is $3 million and (2) that the Defendant's coverage for Plaintiff Thompson is excess only.

With respect to the first issue for summary judgment that the applicable coverage is $3 million, the Plaintiffs' analysis consist of two parts: (a) the Increased/Excess Limits Warranty the Defendant asserts in support of a limit of $1 million in coverage is inapplicable and (b) Endorsement No. 3, the Defendant also asserts in support of coverage limits of $1 million, is inapplicable.

[4] Such a ruling would provide a finding in Plaintiffs' favor on Count 2 (Breach of Contract) and Counts 3 and 4 (declaratory judgment).

The last part of the Plaintiffs' motion analyzes the wording of Plaintiff Thompson's professional liability policy issued by the Defendant compared to the wording of the Great American policy to support Plaintiffs' Count 4 claim that Defendant's coverage as to Plaintiff Thompson is excess coverage.

Below, the Court uses this same format.

$3 Million Versus $1 Million Coverage

Increased/Excess Limits Warranty

The Defendant's responses to the *Plaintiffs' Statement of Undisputed Material Facts* ("PSUMF") paragraphs 1, 2, 4-7, 8 and 12 establish the facts that around August 23, 2017, the United States Secretary of Labor commenced an action against Plaintiffs styled *R. Alexander Acosta, Secretary of Labor v. Zander Group Holdings, Inc. et. al.*, Case No. 3:17-cv-01187 (the "Federal Court Action"). All of the Plaintiffs have been sued in the Federal Court Action which alleges that all of the Plaintiffs breached various duties owed to the Zander Group Holdings, Inc. Employee Stock Ownership Plan (the "ESOP"), an employment pension plan.

The Plaintiffs tendered defenses of the Federal Court Action to the Defendant. The Plaintiffs sought coverage effective October 18, 2016 under Policy No. 82260292, a Fiduciary Liability Policy (the "FLP") issued by the Defendant to Plaintiff Zander Group Holdings, to which all the Plaintiffs are insureds. The FLP provides on its face coverage

of $3 million, and the Plaintiffs assert this is the coverage amount. The Defendant asserts, however, the coverage limit of the FLP for the Federal Court Action is $1 million.

The liability limit dispute between the parties for the Federal Court Action stems from an "Increased/Excess Limits Warranty" (the "Warranty") Zander Group Holdings Inc. submitted to the Defendant around October 18, 2016. The Warranty references another Policy: No 82379126, an Employment Liability Policy (the "ELP") issued by the Defendant to Zander Group Holdings Inc. Citing to the reference in the Warranty to the ELP number, the Plaintiffs assert the Warranty applies to the ELP and does not limit the liability coverage for the FLP in connection with the Federal Court Action. The Defendant admits that the Warranty references "Policy #82379126" (i.e., the ELP Policy), but asserts that the reference to the ELP Policy is a mere scrivener's error and mutual mistake of fact, and therefore is applicable to the FLP to limit coverage to $1 million. Thus, the Defendant asserts in opposition to summary judgment mixed issues of law and fact, of which some implicate Tennessee law on mistake. In reply, the Plaintiffs dispute that the existence of a mistake provides the Defendant relief.

After studying argument of Counsel, the record and the law, the Court concludes that to determine the implications as a matter of law of the admitted mistake a more developed record is needed. That is because with respect to mistake Tennessee law requires the mistake to be a mutual one for it to be forgiven and corrected. Based on the present record and that the Defendant has not had an opportunity to engage in discovery the Court can not decide this issue at this time. Because the record needs to be developed

further as to the foregoing, Plaintiffs' summary judgment motion with respect to the Warranty is denied and, therefore, on that basis Counts 2 and 3 of the *Second Amended Complaint* remain pending.

For upcoming discovery and determination of this issue on the merits, the Court notifies Counsel that the Court will apply the following principles including those stated in *Sikora v. Vanderploeg*, 212 S.W.3d 277, 286–88 (Tenn. Ct. App. 2006) cited by the parties.

> Nevertheless, the law's strong policy favoring the enforcement of contracts as written must occasionally give way. Thus, it is well settled that the courts have the power to alter the terms of a written contract where, at the time it was executed, both parties were operating under a mutual mistake of fact or law regarding a basic assumption underlying the bargain. *Alexander v. Shapard,* 146 Tenn. 90, 105–15, 240 S.W. 287, 291–94 (1922); *Cromwell v. Winchester,* 39 Tenn. (2 Head) 389, 390–91 (1859). The courts are also empowered to modify the provisions of a written contract where only one of the parties was operating under a mistake of fact or law if the mistake was influenced by the other party's fraud. *Dickens v. St. Paul Fire & Marine Ins. Co.*, 170 Tenn. 403, 414–17, 95 S.W.2d 910, 914–15 (1936); *Jones v. Jones,* 150 Tenn. 554, 596, 266 S.W. 110, 121 (1924); *Pittsburg Lumber Co. v. Shell*, 136 Tenn. 466, 472, 189 S.W. 879, 880 (1916); *287 *Pierce v. Flynn*, 656 S.W.2d 42, 46 (Tenn.Ct.App.1983); Restatement (Second) of Contracts §§ 152 & cmt. *a*, at 385–86, 153 & cmt. *a*, at 394 (1981).
>
> The judicial alteration of the provisions of a written agreement is an equitable remedy known as "reformation." *Greer v. J.T. Fargason Grocer Co.,* 168 Tenn. 242, 244–45, 77 S.W.2d 443, 443–44 (1935); *Tenn. Valley Iron & R.R. Co. v. Patterson,* 158 Tenn. 429, 433, 14 S.W.2d 726, 727 (1929). The basic purpose of reformation is to make the contract "conform to the real intention of the parties." *Lebo v. Green,* 221 Tenn. 301, 314, 426 S.W.2d 489, 494 (1968). It is "driven by a respect for the parties' intent and gives effect to the terms mutually agreed upon by the parties." 27 Williston on Contracts § 70:2, at 210. Because the law strongly favors the validity of written instruments, a person seeking to reform a written contract must do more than prove a mistake by a preponderance of the evidence. Instead, the

> evidence of mistake must be clear and convincing. *Hazlett v. Bryant*, 192 Tenn. 251, 263, 241 S.W.2d 121, 125–26 (1951); *Tenn. Hoop Co. v. Templeton*, 151 Tenn. 375, 379–80, 270 S.W. 73, 75 (1925); *Sawyer v. Sawyer*, 106 Tenn. 597, 603, 61 S.W. 1022, 1023 (1901); *Bailey v. Bailey*, 27 Tenn. (8 Hum.) 230, 233 (1847); Restatement (Second) of ContractsS § 155 cmt. *c*, at 410.
>
> An important subcategory of mistake is mistake in the expression, or integration, of the agreement. *Jones v. Jones*, 150 Tenn. at 595, 266 S.W. at 121; *Alexander v. Shapard*, 146 Tenn. at 106–07, 240 S.W. at 291; Restatement (Second) of Contracts ch. 6 introductory note, at 379, 381, § 155 & cmt. *a*, at 406–07. A mistake in expression occurs where one or both parties to a written contract erroneously believe that the contract embodies the agreement that both parties intended it to express. In such cases, the courts may adjust the provisions of the written contract to make it express the true agreement reached by the parties. *Alexander v. Shapard*, 146 Tenn. at 107, 240 S.W. at 291; 27 Williston on Contracts § 70:20, at 257.
>
> In order to obtain reformation on the basis of mistake in expression, a party must present clear and convincing evidence that: (1) the parties reached a prior agreement regarding some aspect of the bargain; (2) they intended the prior agreement to be included in the written *288 contract; (3) the written contract materially differs from the prior agreement; and (4) the variation between the prior agreement and the written contract is not the result of gross negligence on the part of the party seeking reformation. 7 Corbin on Contracts § 28.45, at 283; 27 Williston on Contracts §§ 70:19, at 256, 70:23, at 264–65. Reformation is not automatically barred simply because one of the parties denies that there was an antecedent agreement or claims that the mistake was not mutual. 27 Williston on Contracts §§ 70:13, at 231, 70:21, at 258–59.

Id. at 286–88. (footnotes omitted).

Additional authorities on the doctrine of mistake provide as follows and will be used by the Court as the case proceeds.

- A mutual mistake will provide a basis for equitable relief if the proof is clear and convincing. *Pierce v. Flynn*, 656 S.W.2d 42 (Tenn.Ct.App.1983). A contract, which by reason of a mutual mistake in its execution does not conform to the real agreement of the parties, may be reformed when the mistake is established by

clear and convincing proof. *Commercial Standard Ins. Co. v. Paul*, 35 Tenn.App. 394, 245 S.W.2d 775, 778 (Tenn.Ct.App.1951)(citing *Pittsburg Lumber Co. v. Shell,* 136 Tenn. 466, 189 S.W. 879; *Tennessee Valley Iron & R. Co. v. Patterson,* 158 Tenn. 429, 14 S.W.2d 726; Gibson's Suits in Chancery, 4th Ed., Sec. 945, pp. 770, 771). The Chancellor's finding of no mutual mistake comes to this court with a presumption of correctness unless the preponderance of the evidence is otherwise. Tenn. R.App. P. 13(d).

> Mutual mistake has been defined as "one common to both parties to a contract, each laboring under the same misconception ... respecting a material fact, the terms of the agreement, or the provisions of the written instrument designed to embody such agreement." 17 C.J.S., Contracts, § 144. A mistake is remediable only if it relates "to a fact which constitutes, or goes to, the very essence, or basis, of the contract...." *Id.* Our cases have recognized that equitable relief on the ground of mutual mistake is available "not only when the mistake is expressly proved, but also when it is implied from the nature of the transaction." *Robinson v. Brooks,* 577 S.W.2d 207, 208 (Tenn.Ct.App.1978), quoting from 12 C.J.S., Cancellation of Instruments, § 27b. (1).

Eatherly Const. Co. v. HTI Mem'l Hosp., No. M2003-02313-COA-R3CV, 2005 WL 2217078, at *13–14 (Tenn. Ct. App. Sept. 12, 2005) (citation omitted).

- Mutual mistake is a defense to contract formation. Mutual mistake results when both parties to a contract share a common assumption about a vital existing fact upon which they based their bargain and that assumption is false, and because of the mistake, a quite different exchange of values occurs from the exchange of the values the parties contemplated. In order for a contract to be voidable due to mutual mistake, the mistake must relate to a basic assumption on which the contract was made and have a material effect on the agreed exchange of performances, and the party seeking relief must not bear the risk of mistake. Under the doctrine of mutual mistake, a contract is reformable or voidable if it can be shown that the parties were both mistaken about a basic fact which is material to the agreement, but only if avoidance is just and reasonable. The doctrine of mutual mistake is limited to cases in which both parties were reasonable in their inconsistent interpretations of the contract and in which neither party is more at fault than the other. Thus, a mistake which results from a party's lack of due care may be insufficient to support a claim of mutual mistake. In addition, the judicial remedy must not unfairly prejudice the rights of an innocent third party. Reformation is the appropriate remedy when the mistake is one as to

> expression, while voidance is the proper remedy where a mistake as to a basic assumption on which the contract was made has a material effect on the agreed exchange of performances.
>
> A mutual mistake of fact cannot lie against a future event. Mutual mistakes must concern past or present facts, not unexpected facts that occur after the document is executed.
>
> If partial performance has occurred on one side, the mutual mistake doctrine does not mechanically cancel all remaining obligations on the other side and thereby allow the nonperforming party simply to retain the benefit conferred by the partial performance. On the contrary, the doctrine permits the court to grant relief only on such terms as justice requires.

17A AM. JUR. 2D *Contracts* § 198 (West 2018) (footnotes omitted).

Endorsement No. 3

PSUMF 29 establishes that Endorsement No. 3 of the Fiduciary Coverage Section mandates a $1 million limit of liability for any loss "on account of any **Claim** based upon, arising from, or in consequence of any written demand, suit or other proceeding pending against, or order, decree or judgment entered for or against any **Insured**, prior to 10/18/2016, or the same or substantially the same fact, circumstance or situation underlying or alleged therein." Thus, pursuant to that Endorsement, coverage is limited to $1 million for any loss due to a claim arising from a proceeding pending against the Insured prior to October 18, 2016, which proceeding is derived from the same facts or circumstances upon which coverage is sought. The operative wording is quoted as follows.

> **Loss** on account of any **Claim** based upon, arising from, or in consequence of any written demand, suit or other proceeding pending against, or order,

> decree or judgment entered for or against any **Insured**, prior to 10/18/2016, or the same or substantially the same fact, circumstance or situation underlying or alleged therein.

The pertinent undisputed facts, taken from the Telfeyan affidavit, are that the Department of Labor (the "DOL") launched an official investigation into the ESOP in July of 2014 pursuant to Section 504 of ERISA. That statute gives the DOL investigative authority to determine whether any person has violated ERISA or any regulations or orders issued thereunder. As part of the DOL investigation and prior to October 18, 2016, the summary judgment record establishes facts that the DOL requested significant documents and information from the Zander Group, made an onsite visit to the Zander Group's facilities, and conducted interviews of the Zander Group's management. Additionally, the summary judgment record establishes that the Federal Court Action arose from and is based upon the same facts, circumstances and situations as the DOL investigation concerning the creation and valuation of the ESOP.

Applying the wording of Endorsement No. 3 to the foregoing undisputed facts, it is the Defendant's position that the above facts of the DOL investigation fit the wording of Endorsement No. 3: that the loss in this case – the matters in the Federal Court Action – are "based upon, aris[e] from, or [are] in consequence of" any "proceeding pending against . . . any Insured." In particular, the Defendant argues that the FLP defines "Claims" to include both a "formal administrative or formal regulatory proceeding commenced by the filing of a notice of charges, formal investigative order or similar

document," and that this definition encompasses the undisputed facts of record of the DOL investigation.

The Court, however, concludes that the Plaintiffs are correct and prevail on this issue based upon the plain, unambiguous wording of Endorsement No. 3. The Court adopts the following reasoning quoted from page 8 of the Plaintiffs' September 7, 2018 *Reply*.

> When the Court interprets "proceeding" in context and in accordance with its usual, natural and ordinary meaning, that term clearly does not embrace an investigation. No one speaks of an investigation "pending against" a party. One speaks of a lawsuit or other proceeding, such as an arbitration, as "pending against" a party. There was no "suit or other proceeding pending against" the Zander parties prior to October 18, 2016 [only] …an investigation . . . .
>
> Likewise, Federal's argument that the Policy defines "Claim" to include a factfinding investigation (Response at 28) goes nowhere. Plaintiffs have not asserted any Claim arising out of the DOL investigation. Rather, as Federal's own Reservation of Rights letter (Second Amended Complaint Ex. 2, n1) recognizes, the Claim at issue here arises out of the "DOL Correspondence and the DOL Complaint" and was "first made on June 28, 2017." Because Plaintiffs have not asserted a Claim that arises out of a written demand made, or a suit or other proceeding pending against Plaintiffs, prior to October 18, 2016, Endorsement No. 3 provides no defense to Federal in this case.

Thus, the Court concludes as a matter of law from the plain, unambiguous text of Endorsement No. 3 that the DOL investigation in this case does not come within the terms of Endorsement No. 3. Accordingly, the Plaintiffs' motion for summary judgment is granted, and the Defendant is barred from asserting Endorsement No. 3 as a defense to

the Plaintiffs' claim of $3 million in coverage in Counts 1, 2 and 3 of the *Second Amended Complaint*.

Plaintiff Thompson's Professional Liability Coverage

Lastly, the Plaintiffs seek summary judgment on Count 4 – Declaratory Judgment for the Court to declare as a matter of law that "the [Zander Group Holdings] Policy provides only excess coverage to Thompson for defense and indemnity of the Federal Court Action" and to "declare that no funds Federal has paid or will pay to defend or indemnify Thompson under the [Zander Group Holdings] Policy reduce in any manner the coverage available to Zander Group Holdings, Inc., Jeffrey J. Zander, or any other insured, under the [Zander Group Holdings] Policy." *Second Amended Complaint*, p. 10, ¶¶ 43; 44 (April 12, 2018).

As to this part of the summary judgment the issue is that Plaintiff Thompson maintains, in addition to the coverage with the Defendant, another professional liability policy. It is with Great American Insurance Company. The Plaintiffs assert that the Great American policy is the primary coverage for Plaintiff Thompson and the Defendant's policy is only excess. The effect of this position is that funds paid by the Defendant to indemnify or defend Plaintiff Thompson would not reduce the coverage available to the Plaintiffs.

The Defendant's position on this issue is that its policy and the Great American policy are mutually exclusive and repugnant requiring proration under Tennessee law.

The Defendant's Responses to *Plaintiffs' Statements of Undisputed Material Fact* establish that the Defendant has agreed to prorate Mr. Thompson's primary defense because the "other-insurance provisions in the Fiduciary Policy and Great American Policy…are mutually repugnant and cannot be reconciled," and the Defendant agrees with the Plaintiffs that the Great American other insurance clause is "irreconcilably in conflict with that of the Fiduciary-Liability Policy."

> 15. Federal is providing a primary, not excess, defense to Mr. Thompson under the Fiduciary –Liability Policy in the Federal Court Action. (2d Am. Compl. ¶ 39; Answer ¶39.)
>
> RESPONSE: Undisputed for the purpose of ruling on the Zander MSJ only. By way of further explanation, Federal and Great American agreed to prorate the primary defense of Thompson in the DOL Action given other-insurance provisions in the Fiduciary Policy and Great American Policy that are mutually repugnant and cannot be reconciled. (Brown Aff. ¶¶ 19-20).
>
> 16. Policy number MPL1668711 contains an other-insurance clause irreconcilably in conflict with that of the Fiduciary-Liability Policy. (Zander Dec. Ex. 3; Am. Compl. Ex. 3.)
>
> RESPONSE: Undisputed for the purpose of ruling on the Zander MSJ only.

Federal Insurance Company's Response To Plaintiffs Zander Group Holdings, Inc. And Jeffrey J. Zander's Statement Of Undisputed Facts In Support Of Motion For Partial Summary Judgment, p. 9, ¶¶ 15-16 (Aug. 17, 2018).

In support of their positions, both parties cite to the 1967 Tennessee Supreme Court case of *United Servs. Auto. Ass'n v. Hartford Acc. & Indem. Co.* 414 S.W.2d 836 (1967). It addressed the issue of "other insurance" clauses within the context of dual

automobile liability insurance policies. In that case, the Court was "convinced that the 'other insurance' provision of the policies here before us are in substantial measure repugnant to the general insurance provisions of the policies; and therefore void." *Id.* at 839–40. Because both policies were mutually repugnant and as a result void, the Tennessee Supreme Court, applying the Ninth Circuit Court of Appeals case law[5], determined "that the only reasonable result to be reached is a proration between the two insurance companies in proportion to the amount of insurance provided by their respective policies." *Id.* at 841.

Thirty years later, the Court of Appeals in *Shelter Mut. Ins. Co. v. State Farm Fire & Cas. Co.* 930 S.W.2d 570 (Tenn. Ct. App. 1996), discussed the development of case law in Tennessee on the issue of "other insurance" clauses. The Court of Appeals noted the Tennessee Supreme Court's decision in *United Servs. Auto. Ass'n v. Hartford Acc. & Indem. Co.*, and also analyzed the "other insurance" clauses based, in part, on recently passed legislation.[6] *Id.* In *Shelter Mut. Ins. Co. v. State Farm Fire & Cas. Co.*, the Court

[5] The Tennessee Supreme Court relied on the Ninth Circuit Court of Appeals case of *Oregon Auto. Ins. Co. v. U.S. Fid. & Guar. Co.*, 195 F.2d 958 (9th Cir. 1952).

[6] The legislation is Tennessee Code Annotated section 56-7-1101. It codified which automobile liability insurance was primarily responsible when the driver of an automobile was covered by two policies. This legislation was passed to bypass the Court's rulings on cancelling out mutually repugnant automobile policies to then apply a prorated coverage between the two policies.

> The act was codified as Tenn.Code Ann. § 56-7-1101(a). It was passed to resolve the problem of which insurance company was primarily responsible when the driver of an automible was covered by two policies. In *Continental Ins. Co. v. Insurance Co. of North America*, 224 Tenn. 306, 315, 454 S.W.2d 709, 713 (1970), the Tennessee Supreme Court had held that when two policies had mutually repugnant excess coverage clauses the clauses canceled each other out and the loss would be prorated between the two policies. Because the decision penalized insurers who wrote high limits coverage, the

declined to apply a blanket rule that "other insurance" provisions are null and void in all circumstances and, instead, adopted the majority approach to attempt to reconcile and interpret the clauses to give effect to the intentions of the parties, if possible.

> Over the years, courts have grappled with the determination of how to allocate damages when two separate policies cover an insured involved in an accident. This determination is not an easy one to make because insurance policies often contain "other insurance" clauses. Insurance companies use these clauses to define the sum they will pay in the event that multiple insurance policies cover the same injury. The "other insurance" clauses traditionally break down into the following three types: 1) pro rata clauses, such as the one found in Shelter's policy, provide that, in the event other insurance is available, the loss will be prorated between the insurance policies; 2) excess clauses, such as the one found in State Farm's policy, provide that, in the event other insurance is available, the subject policy will cover liability only to the extent its coverage is in excess of the other policy limits; and 3) escape clauses provide that, in the event other insurance is available, the subject policy will not cover any liability.
>
> The guiding principle when analyzing such policies is the determination of which policy provides primary coverage. When strict construction of "other insurance" clauses results in the conclusion that no primary coverage exists, courts are quick to strike down both "other insurance" clauses as repugnant to each other. This is true, for example, when two policies each have excess clauses as to the same event so that each attempts to pass primary responsibility for coverage on to the other company. On the other hand, when it is clear from a reading of the two competing policies which policy is primary, there is no need for courts to intrude because the general rules of contract come into play.
>
> There are two lines of reasoning used by the courts when analyzing this issue. The majority rule is "that where there are two applicable insurance policies, one containing a pro rata clause and the other an excess clause, the provisions of each will be interpreted to give effect to the intent of the

---

legislature stepped in to provide that primary coverage would follow the car. *See* House Debates, Tape No. H-258, 88th Gen.Assy., 1973.

Lanius v. State Farm Mut. Auto. Ins. Co., No. 88-57-II, 1988 WL 72406, at *2 (Tenn. Ct. App. July 13, 1988).

contracting parties." *Jones v. Medox, Inc.,* 430 A.2d 488, 493 (D.C.App.1981). The second line of reasoning is that whenever two "other insurance" clauses conflict they are repugnant, and thus, the court must void the clauses and prorate the damages. *Lamb–Weston, Inc. v. Oregon Auto. Ins. Co.,* 219 Or. 110, 341 P.2d 110, 119 (1959).

In *Lamb–Weston,* a lessee's employee drove a leased vehicle and crashed it into a warehouse. The owner/lessor of the vehicle had a pro rata "other insurance" clause in his insurance policy, and the employer/lessee's policy had an excess "other insurance" clause. The *Lamb–Weston* court held as follows: "In our opinion, whether one policy uses one clause or another, when any come in conflict with the 'other insurance' clause of another insurer, regardless of the nature of the clause, they are in fact repugnant and each should be rejected in toto." *Id.* As such, Oregon courts will hold that both policies provide primary coverage on a pro rata basis. *Id.* 341 P.2d at 118.

A key case relied upon by the Oregon Supreme Court in *Lamb–Weston* was *Oregon Auto Insurance Co. v. United States Fidelity & Guaranty Co.,* 195 F.2d 958 (9th Cir.1952). In *Oregon Auto* the driver's policy had an excess "other insurance" clause and the owner's policy had an exclusionary or exculpatory "other insurance" clause. In that situation, a repugnancy did exist because both insurers could have avoided primary liability to their insured leaving their insured with no coverage even though two companies had each issued a policy. As stated by the court in *Oregon Auto:* "It is plain that if the provisions of both policies were given full effect, neither insurer would be liable. The parties admit that such a result would produce an unintended absurdity...." *Oregon Auto Ins. Co.,* 195 F.2d at 959. The court went on to state "where both polices carry like 'other insurance' provisions, [they] must be held mutually repugnant and hence be disregarded." *Id.* at 960. Neither the facts in *Lamb–Weston* nor the facts in the instant case involve like "other insurance" clauses.

While *Oregon Auto* was correct in its logic, interpretation, and ruling based upon the express language of the two policies and the competing types of "other insurance" clauses, the *Lamb–Weston* court went one step further, ignored the clear, consistent, and unambiguous language of the policies, and rendered a blanket rule that "other insurance" provisions were null and void in all circumstances.

The *Jones* case, which explains the majority view, involved a pro rata clause and an excess clause. The issue in the case was whether the court

should attempt to reconcile and to interpret the clauses to give effect to the intentions of the parties or whether it should simply apply the *Lamb–Weston* rule. *See Jones*, 430 A.2d at 489. The court decided the majority rule was the better approach. *Id.* at 493. It then analyzed the facts of the case using the majority rule and concluded that the pro rata clause and the excess clause were not repugnant. Next, the court held the insurance company using the pro rata clause liable for the amount covered by the company's policy limit and held the insurance company using the excess clause liable for any damages which exceeded the policy limit. *Id.* at 494–95.

In reaching its decision, the *Jones* court discussed the criticisms of the *Lamb–Weston* rule. It properly labeled the *Lamb–Weston* line of cases as situations where courts "abandon all attempts to discern the intent of the contracting parties where there are dissimilar 'other insurance' clauses and take the position that all 'other insurance' clauses, regardless of their nature, are mutually repugnant, requiring proration of liability." *Id.* at 492. A second flaw in the application of the *Lamb–Weston* rule noted by the court was as follows: "Courts applying the *Lamb–Weston* rule ignore a basic rule of contracts requiring consideration of all the language in a policy provision to determine its meaning and intent." *Id.* In addition, the court pointed out that application of the *Lamb–Weston* rule may substantially impact the insurance industry and the policy rates charged to consumers. The *Lamb–Weston* rule introduces a new item of uncertainty into the equation. This uncertainty likely results in duplications of claim investigation, claim supervision, and settlement and defense costs. Such duplication may increase the cost of each claim as well as the ultimate increase in premiums paid by all policy holders. *Id.* at 493.

The Kentucky Court of Appeals in *Hartford Insurance Co. v. Kentucky Farm Bureau Insurance Co.*, 766 S.W.2d 75 (Ky.App.1989), adopted the majority view and designated the pro rata policy in that case as the primary insurance policy. In adopting the majority view, the court, relying on the *Jones* decision, pointed out that a criticism of *Lamb–Weston* was that it "ignores a basic rule of contracts by failing to consider all of the language in a policy to determine its meaning and intent." *Hartford Ins. Co.*, 766 S.W.2d at 77. Further, the Kentucky court noted that when courts apply the minority repugnancy rule, they are effectively "legislating pro rata apportionment whenever a policy has a 'other insurance' clause and legislation is not a proper judicial function." *Id.*

The Tennessee Supreme Court has addressed this issue in several cases all of which involved automobile liability policies which contained "other insurance" clauses. *State Farm Ins. Co. v. Taylor,* 511 S.W.2d 464 (Tenn.1974) (involving a pro rata and an excess clause); *Continental Ins. Co. v. Insurance Co. of N. Am.,* 224 Tenn. 306, 454 S.W.2d 709 (1970) (involving two excess clauses); *Commercial Union Ins. Co. v. Universal Underwriters, Inc.,* 223 Tenn. 80, 442 S.W.2d 614 (1969) (involving an excess and a pro rata clause); *United Servs. Auto. Ass'n v. Hartford Accident and Indem. Co.,* 220 Tenn. 120, 414 S.W.2d 836 (1967) (involving an excess clause and an escape clause). *But see Tennessee Farmers Mut. Ins. Co. v. Canal Ins. Co.,* 58 Tenn.App. 1, 425 S.W.2d 762 (1967) (finding that it could give both of the "other insurance" clauses effect and distinguishing *United Servs. Auto Ass'n*). In 1967, the supreme court adopted the view expressed in *Oregon Auto. United Servs. Auto Ass'n.,* 414 S.W.2d at 840. Later, in 1969, the court expressly adopted the reasoning of *Lamb–Weston. Commercial Union Ins. Co.,* 442 S.W.2d at 618. Thus, in the cases cited above, the court applied the blanket rule of *Lamb–Weston,* determined that the "other insurance" clauses were repugnant, and prorated the damages.

In response to the court's decision in *Continental Ins. Co.,* the Tennessee General Assembly enacted legislation which superseded the court's decisions. 1973 Tenn.Pub.Acts ch. 209 (currently codified at Tenn.Code Ann. § 56–7–1101 (1994)). This statute designated which insurance policy provides primary insurance coverage in all cases arising out of the use of motor vehicles. The legislative history of this act demonstrates the General Assembly's desire that the courts attempt to apply the provisions of insurance policies as they are written. In a 1 May 1973 discussion of the act, Representative McWilliams stated as follows:

> This is a bill the necessity of which was brought about by a court decision in the case of [*Continental Insurance Co. v. Insurance Company of North America*]....
>
> The confusion has been brought about because of a court decision between two insurance companies in which they said that irrespective of the provisions of the policy, [liability] should be pro rated between the two insurance companies....
>
> [This act] would require the Supreme Court of this state to follow the provisions of that policy, those policies.

> Given the fact that the General Assembly's actions superseded the court's decisions, at present, this court is left without binding authority. In other words, this is essentially a case of first impression.
>
> It is the opinion of this court that the better approach is that explained in the *Jones* opinion. Not only is this the approached followed by a majority of the courts, but it also allows the courts to consider the fact of individual cases as opposed to applying a blanket rule. Moreover, there is evidence that the supreme court no longer agrees wholeheartedly with the *Lamb–Weston* rule. *See Continental Ins. Co. v. Excel Ins. Co.*, 541 S.W.2d 952 (Tenn.1976). In *Continental*, the supreme court decided a case involving two insurance policies. The 1973 Public Act did not apply, however, because the policies were issued prior to May 1973. *Id.* at 953. In deciding the case, the supreme court noted the decisions adopting the *Lamb–Weston* rule, but made the following conclusion:
>
> > We have examined with care the provisions of the two insurance policies exhibited to the stipulation in the present case, however, and we do not find that they are repugnant or in conflict. For that reason, we are of the opinion that the pre–1973 cases are not applicable, and that the appellant is not entitled to the proration which it claims.
>
> *Id.* at 954. Finally, although the legislative history of Tennessee Code Annotated section 56–7–1101 is not binding on this court, it is our opinion that it is persuasive authority in favor of adopting the majority view.

Shelter Mut. Ins. Co. v. State Farm Fire & Cas. Co., 930 S.W.2d 570, 572–74 (Tenn. Ct. App. 1996).

Applying the foregoing law, this Court begins with the wording of the two policies in issue, quoting the Defendant's wording first, followed by the wording of the Great American policy.

> **XI. OTHER INSURANCE OR INDEMNITY**
>
> If any **Loss** under this Coverage Part is insured under any other valid and collectible insurance policy (other than a policy that is issued specifically as excess of the insurance afforded by this Coverage part), this Coverage part

> shall be excess of and shall not contribute with such other insurance, regardless of whether such other insurance is stated to be primary, contributory, excess, contingent, or otherwise.

Federal ForeFront Portfolio Policy No. 82260292, Section XI. Other Insurance Or Indemnity (emphasis in original).

> **M. Other Insurance Provision**
>
> This Policy shall apply only as excess over, and shall not contribute with, any other valid and collectible insurance available to any **Insured** (including but not limited to any fiduciary liability policy issued to any ESOP or the sponsor of any ESOP to which the Insured provides Professional Services) and will not be subject to the terms of any other insurance.

Great American Insurance Policy, Endorsement: 6 – Amendment To Section X. General Obligations (emphasis in original).

Both of the above quoted provisions attempt to limit liability through the "excess" clause provision. Accordingly, under Tennessee law quoted above, it is necessary to determine whether one policy shows, on its face, that it provides primary coverage and that there is neither a conflict nor repugnancy with the other policy.

> The guiding principle when analyzing such policies is the determination of which policy provides primary coverage. When strict construction of "other insurance" clauses results in the conclusion that no primary coverage exists, courts are quick to strike down both "other insurance" clauses as repugnant to each other. This is true, for example, when two policies each have excess clauses as to the same event so that each attempts to pass primary responsibility for coverage on to the other company. On the other hand, when it is clear from a reading of the two competing policies which policy is primary, there is no need for courts to intrude because the general rules of contract come into play.

Shelter Mut. Ins. Co. v. State Farm Fire & Cas. Co., 930 S.W.2d 570, 572 (Tenn. Ct. App. 1996).

Neither policy identifies itself as "primary insurance." Rather, the plain wording of the two "other insurance" provisions indicates that the intent of each policy was to provide "excess" coverage in the event another policy provides coverage. Both "excess" clauses attempt to limit liability and "shall not contribute" if the loss is insured under "any other valid and collectible insurance." In sum, the two "excess" coverage clauses read within the context of the entire policies are irreconcilable as to which policy would actually provide primary coverage to Mr. Thompson. Without any indication as to which policy is primary, the Court would act arbitrarily by labeling one policy "primary" and the other "secondary", given the plain text of the two policies. Such a ruling would be inconsistent with Tennessee law.

> [W]e have concluded that, in situations where liability insurance policies are thus by their terms brought into contention, to attempt to resolve the problem by labeling one policy 'primary' and the other 'secondary', in some inconsistent or arbitrary manner, is apt to produce even more dubiety of obligation than now exists.
>
> ****
>
> As has been noted, both policies attempt to provide 'excess only' coverage as to non-owned vehicles. Neither policy, however, by its specific terms, offers full and unconditional primary coverage to the insured for loss arising from the operation of owned vehicles. On the contrary, liability is attempted to be restricted where 'other insurance' is available. We are not at liberty to dictate that one policy provides primary coverage to the exclusion of the other, for to do so would be to add non-existent terms to the policies to the detriment of the insured.
>
> ****

> An effort to test the reality of contractual intent, including the reasonable expectations of the assured in these cases, inexorably leads to that same detestable circuity of reasoning and dubiety of obligation upon which we have written before, and to which these underwriting practices so much contribute.
>
> It seems to us that the most reasonable result to be reached, consistent with established rules of construction, is proration between the two insurance companies in proportion to the amount of insurance provided by their respective policies.

Cont'l Ins. Co. v. Ins. Co. of N. Am., 224 Tenn. 306, 314–15, 454 S.W.2d 709, 712–13 (1970).

With respect to the Plaintiffs' argument that because the Great American Policy is an "other valid and collectible insurance policy" that its coverage must necessarily be excess, the Court does not adopt this. The Defendant could make the same legal argument based on its construction of the "excess" clause in the Great American policy. Under these circumstances, the Tennessee Supreme Court has held that this sort of repugnancy results in both provisions being determined to be void and each insurance policy contributing its pro rata share to the defense. "Where provisions of insurance contracts are 'mutually repugnant,' both policies will provide coverage, and coverage will be prorated between the two insurance companies in proportion to the amount of insurance provided by their respective policies." *United Servs. Auto. Ass'n v. Cont'l Ins. Co.*, 1985 WL 4692, at *6 (Tenn. Ct. App. Dec. 24, 1985) (quoting *United Servs. Auto. Ass'n v. Hartford Acc. & Indem. Co.*, 220 Tenn. 120, 131, 414 S.W.2d 836, 841 (1967)).

The Court therefore concludes that the Plaintiffs' motion for summary judgment on Count 4 is denied because the two "excess" other insurance clauses are irreconcilable and mutually repugnant, and Count 4 is dismissed with prejudice as a matter of law.

s/ Ellen Hobbs Lyle
ELLEN HOBBS LYLE
CHANCELLOR
BUSINESS COURT DOCKET
PILOT PROJECT

cc by U.S. Mail, email, or efiling as applicable to:
Eugene Bulso, Jr.
John R. Tarpley
Bradford D. Telfeyan
Stanley J. Lehman
Jennifer P. Richnafsky
Stephen M. Thompson
Brian Eagle