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STATE OF WISCONSIN
SUPREME COURT

CONTINENTAL PROPERTIES COMPANY, INC.,
CONTINENTAL 355 FUND LLC,
CONTINENTAL 342 FUND LLC,
CONTINENTAL 332 FUND LLC,
CONTINENTAL 347 FUND LLC,
CONTINENTAL 335 FUND LLC,
CONTINENTAL 326 FUND LLC,
CONTINENTAL 298 FUND LLC, and
CONTINENTAL 235 FUND LLC,

Plaintiffs-Appellants-Petitioners,

v.

HISCOX INSURANCE COMPANY, INC.,

Defendant-Respondent.

Appeal No. 2024AP000197
Waukesha County Circuit Court Case No. 2020CV000248
The Honorable Michael J. Aprahamian, presiding

NON-PARTY BRIEF OF UNITED POLICYHOLDERS

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ARGUMENT

United Policyholders ("UP") submits this brief in support of Plaintiffs-Appellants-Petitioners (collectively, "Continental") to supplement the arguments in a case of general public interest.

Continental's Vice President of Construction, Angelo Eguizabal, stole money from Continental through a kickback scheme with a colluding contractor. (App.129-135; App.254-55; R.247, 3; App.018.) Continental submitted evidence that the scheme caused Continental to lose millions of dollars that Eguizabal approved for payment to the colluding contractor in exchange for Eguizabal's kickback payment. (R.115, ¶35.) Continental sought to recover these losses from Defendant-Respondent Hiscox Insurance Company, Inc. ("Hiscox") under an insurance policy promising to pay for loss "resulting directly from Theft . . . committed by an Employee, whether identified or not, acting alone or in collusion with other persons." (App.191.)

Continental did *not* seek to recover losses innocent third parties suffered because Eguizabal lied to or stole from *them*. Nor did Continental seek to recover losses it suffered in paying contingent liabilities to third parties that sued Continental because of Eguizabal's misconduct. Continental sought to recover only the losses it incurred because Eguizabal stole from *Continental*.

The Circuit Court nevertheless granted summary judgment in favor of Hiscox, applying the "direct means direct" circular logic of *Tri City National Bank v. Federal Insurance Co.*, 2004 WI App

12, 268 Wis. 2d 785, 674 N.W.2d 617, a Court of Appeals decision that addressed a different circumstance entirely—a loss in the form of a contingent third-party liability the insured incurred because of employee misconduct. (App.013-042.) The Court of Appeals affirmed. (App.009.)

Both courts erred. *Tri City* does not apply under the present circumstances. As numerous courts in other states have recognized, losses "resulting directly from" a triggering event such as employee theft include all *first-party* losses proximately caused by the event. The covered losses do not extend to amounts the employee stole from *others*, resulting in contingent third-party liabilities the insured might face, because contingent liabilities typically do not produce *actual* losses absent additional events (*e.g.*, a lawsuit). But Continental did not seek reimbursement for contingent third-party liabilities.

Tri City recognized that the drafting history of the language at issue supports this reading. 2004 WI App 12, ¶ 19. The language was borrowed from standard form fidelity bonds which added "directly" to the phrase "resulting from" to avoid the indemnitor (whether a surety or an insurer) paying contingent liabilities caused by employee dishonesty, *not* to limit coverage for losses the insured itself suffers through the theft of the insured's own money. And the Hiscox language here expressly confirms "directly" is not a restriction on *first-party* losses. It cannot mean the insured's employee must himself pocket the money he steals to trigger coverage because Hiscox promised to pay whether the employee

acts "alone *or* in collusion with others" who receive the money. (App.191 (emphasis added).)

Hiscox argues it relies on court decisions such as *Tri City* to limit the coverage Hiscox's policy provides to only more immediate losses—such as when an employee himself pockets the insured's money. But if Hiscox relies on court decisions, then Hiscox must rely on contrary, *conflicting* decisions, here, including decisions that disagree with *Tri City* issued by courts in other states in which Hiscox also sells policies with identical, standard form language. Hiscox must intend both that "direct means direct" *and* "direct means proximate cause" because that is what courts in various states have held under certain circumstances. And if Hiscox intends *identical* language to mean *different* things in different places, the language must be ambiguous, in which case, it must be construed against Hiscox under Wisconsin law.

No reasonable policyholder would share Hiscox's intent. None would understand identical language to cover less loss in Wisconsin than the same language covers in New Jersey, for example. Wisconsin policyholders would understand that they have purchased and will receive the same breadth of coverage under the same language as insurance consumers in other states where courts have held "resulting directly from" means "proximately caused by."

I. "Resulting directly from" means "proximately caused by."

For decades, courts repeatedly have construed the phrases "resulting directly from" and "direct loss" to impose a proximate cause standard. *See Jefferson Bank v. Progressive Casualty Insurance Co.*, 965 F.2d 1274, 1281-82 (3d Cir. 1992) (Pennsylvania law) (holding that "resulting directly from" means "proximately caused by" and rejecting an "immediacy" requirement); *Omnisource Corp. v. CNA/Transcon. Ins. Co.*, 949 F. Supp. 681, 691 (N.D. Ind. 1996) (Indiana law); *Auto Lenders Acceptance Corp. v. Gentilini Ford, Inc.*, 854 A.2d 378, 386-87 (N.J. 2004) ("In view of the prevailing approach . . . to defining direct loss, in whatever type of policy that term arose, we adopt the conventional proximate cause test as the correct standard to apply when determining whether a loss resulted from the dishonest acts of an employee."); *Frontline Processing Corp. v. Am. Econ. Ins. Co.*, 149 P.3d 906, 911 (Mont. 2006); *Retail Ventures, Inc. v. Nat'l Union Fire Ins. Co.*, 691 F.3d 821, 831–32 (6th Cir. 2012) (Ohio law); *Medidata Sols. Inc. v. Fed. Ins. Co.*, 729 F. App'x 117, 119 (2d Cir. 2018) (New York law); *Principle Solutions Group, LLC v. Ironshore Indem., Inc.*, 944 F.3d 886, 892 (11th Cir. 2019) (Georgia law); *City of Unalaska v. National Union*, 591 F. Supp. 3d 440, 451 (D. Ak. 2022) (Alaska law); *Int'l Paper Co. v. Beazley Ins. Co.*, 731 F. Supp. 3d 1013, 1041 (W.D. Tenn. 2024) (Tennessee law).

This Court has agreed and likewise construed "direct loss" in first-party property insurance to require proximate or efficient

causation. *Kudella v. Newark Ins. Co.*, 3 Wis. 2d 599, 601, 89 N.W.2d 219, 220 (1958). In *Kudella*, this Court construed a policy extending coverage to "direct loss by Windstorm." *Id.* at 600. The Court explained the designated cause "must have been the proximate, and not a remote, cause of the loss, particularly where the policy requires it to be the 'direct' cause of the loss." *Id.* at 601 (quoting 45 C.J.S., Insurance, § 888). The covered peril "need not be the sole cause." *Id.* It is "generally sufficient . . . that the cause designated therein was the efficient cause of the loss, although other causes contributed thereto, unless the contributing cause is expressly excluded." *Id.*[1]

Notwithstanding this lengthy history, insurers and sureties sometimes have advocated for a more restrictive test requiring that loss *immediately* follow in time and space the triggering event for coverage to apply. *See, e.g., Aetna Cas. & Sur. Co. v. Kidder, Peabody & Co. Inc.* 676 N.Y.S.2d 559, 564 (1998). They generally have asserted these arguments only when the insured seeks coverage for contingent, third-party liabilities such as the liabilities at issue in *Tri City*. *Id.*; *see also Tri City*, 2004 WI App 12, ¶¶ 3-5.

As the surety in *Tri City* did, they argue that the form language at issue was changed in 1980 from "loss resulting

[1] The Court later clarified that "[w]here a policy expressly insures against loss caused by one risk but excludes loss caused by another risk, coverage is extended to a loss caused by the insured risk even though the excluded risk is a contributory cause." *Kraemer Bros. v. U.S. Fire Ins. Co.*, 89 Wis. 2d 555, 570, 278 N.W.2d 857, 863–64 (1979).

through" to "directly resulting from" to narrow coverage by excluding contingent liabilities—losses that arise, for example, because the insured must pay an innocent third party from whom the employee has stolen something. *Tooling, Mfg. & Techs. Ass'n v. Hartford Fire Ins. Co.*, 693 F.3d 665, 674, 677 (6th Cir. 2012) (Michigan law) ("As we noted, the 'result[ed] directly from' language was adopted specifically for employee fidelity policies for a reason—to prevent coverage for third-party losses.") (citation omitted); *Mass. Mut. Life Ins. Co. v. Certain Underwriters at Lloyd's of London*, No. 4791-VCL, 2010 WL 2929552, at *16-17 (Del. Ch. July 23, 2010).

Courts often agree with these arguments *in the context of third-party liabilities* where an insured's loss is not "direct" but instead consists of the employee's theft of *someone else's* money—money the insured then must repay because the insured is vicariously liable for its employee's misconduct. Hiscox cites a number of these decisions, which it claims establish a "majority" that is "intact today." (Resp. at 24.)

But each of these decisions addresses a different circumstance—third party liabilities *not* at issue in Continental's claim. *See Pinnacle Processing Group, Inc. v. Hartford Cas. Ins. Co.*, 2011 U.S. Dist. LEXIS 128203 *5-6 (W.D. Wash) (insured sought coverage for liability to bank resulting from fraudulent credit card transactions); *Wilbanks Sec., Inc. v. Nat'l Union Fire Ins. Co.*, 2018 U.S. Dist. LEXIS 19278, *1-4 (W.D. Okla.) (insured sought coverage for liability to purchasers of securities that

employee sold by forging signatures); *Direct Mortg. Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 625 F. Supp. 2d 1171, 1173 (D. Utah 2008) (insured sought coverage for liability to financial institutions that purchased bad loans employee fraudulently issued); *CP Food & Bev., Inc. v. United States Fire Ins. Co.*, 324 F. Supp. 3d 1172, 1174 (D. Nev. 2018) (insured sought coverage for liability to its customers for fraudulent credit card transactions employees processed); *Ameritas Life Ins. Corp v. Fed. Ins. Co.*, 2017 U.S. Dist. LEXIS 216440 at *2-3 (D. Neb. 2017) (insured sought coverage for liability to customers from whom employee stole money).

None of Hiscox's "majority" addresses losses such as Continental's losses, which result from Eguizabal's theft of Continental's own money through a kickback scheme. And the drafting history suggests no intention to restrict coverage here. *See, e.g., Retail Ventures*, 691 F.3d at 828 ("[L]oss 'resulting directly from' employee misconduct refers only to the insured's own loss from employee misconduct and not the insured's vicarious liability to third parties.").

The true "majority" rule that applies to Continental's first-party claim is the proximate cause standard many states have adopted, including Wisconsin.

II. "Resulting directly from" is, at best for Hiscox, ambiguous.

As the citations above confirm, the phrase "resulting directly from" has produced a lot of litigation. That litigation has resulted

in a split of authority. *See, e.g., Tooling, Mfg. & Techs. Ass'n*, 693 F.3d at 674 (6th Cir. 2012) ("It remains the case that state courts and federal courts interpreting state law are split on how to interpret the provision."). And, while a split alone is not dispositive, it signals ambiguity. *See Marotz v. Hallman*, 2007 WI 89, ¶19, 302 Wis. 2d 428, 734 N.W.2d 411 ("Courts reaching contradictory interpretations of the same statute may be indicative of ambiguity," even if not conclusive.) (citation omitted); *Just v. Land Reclamation, Ltd.*, 155 Wis. 2d 737, 752-57, 456 N.W.2d 570 (1990) (finding that "substantial conflicting authority" interpreting the phrase "sudden and accidental" "strengthens the conclusion that the terms are . . . ambiguous"). That is particularly true where, as here, the split has existed for decades.

Yet, Hiscox has made no change to the language. Hiscox admits "insurers like Hiscox rely on the state of the law to adopt policy language." (Resp. Br. 20.) But Hiscox, a Bermuda-based insurer, continues to sell a standard commercial crime policy across state lines in the United States, knowing that courts disagree about the construction of "resulting directly from," at least in certain circumstances.

Knowing about this disagreement, and taking no action to clarify the language, Hiscox must intend the same language to mean different things in different states. That is the very definition of ambiguity, which must be construed against Hiscox. *Preisler v. General Cas. Ins. Co.*, 2014 WI 135, ¶20, 360 Wis. 2d 129, 857 N.W.2d 136 (policy language "is ambiguous when a

reasonable insured would read the policy to provide coverage and the language is susceptible to more than one reasonable interpretation"). Hiscox cannot expect an ordinary policyholder to know that the same words mean one thing in one state and another elsewhere.

III. The Court's decision will reach other crime coverages.

This appeal concerns an employee theft claim, but the Court's answer will not be limited to that specific coverage. "Resulting directly from" and its close variants appear in many forms of commercial crime policies. *See, e.g.*, *City of Unalaska*, 591 F. Supp. 3d at 443 (computer fraud coverage). Hiscox itself relies on a computer fraud decision. (Resp. Br. 24–25 (citing *Pinnacle Processing*)).

All of these coverages will be substantially eroded if the Court adopts a construction that imposes an "immediacy" requirement as fraudulent schemes are increasingly complex and routinely involve multiple steps. *International Paper Company* provides one example.

There, the insured operated a program to support minority-owned businesses by paying above-market prices for products the businesses supplied in exchange for value-added services. 731 F. Supp. 3d at 1019. The minority-owned business received its payments either (a) from the insured directly in "Tier 1" relationship or (b) from a majority-owned business with which the insured contracted in a "Tier 2" relationship, with the expectation

that the majority-owned business would retain the minority-owned business to perform value-added services. *Id.*

An employee of the insured awarded several Tier 1 contracts to businesses owned by his brother and approved the same businesses to receive funds under Tier 2 contracts. *Id.* The businesses never intended to perform and did not perform any of the value-added services but received above-market payments of millions of dollars under the Tier 1 and Tier 2 contracts. *Id.* at 1022, 1033. They then transferred some of the money to the employee in a kickback scheme substantially similar to Eguizabal's scheme. *Id.* at 1022.

The insured discovered the scheme and sought coverage for its losses under its employee theft policy. The insurer denied for all of the same reasons Hiscox denied Continental's claim here, including arguing that "overpayments" to the minority-owned businesses were not "thefts" and that "mark ups" paid through the Tier 2 contracts did not "result directly from" any employee's theft.

The insured filed suit and the insurer moved for summary judgment. The court denied the insurer's motion. As to whether the "overpayments" constituted "theft," the court observed what Tennessee's Model Penal Code acknowledges: "There are a lot of ways of stealing." *Id.* at 1035. One way is to fraudulently collect unauthorized payments for services that the business had no intention of performing, at least where the business then funnels some of the payments back to the employee insider that awarded the contract and made the scheme possible. *See id.* at 1036.

With respect to the "resulting directly from," the court held a proximate cause standard applies. *Id.* at 1042. The court then found disputes of facts precluded summary judgment as to which losses were proximately caused by the scheme. *Id.* at 1043.

Modern theft is multi-step by design. Bad actors use spoofed emails and colluders to make the scheme more convincing and evade detection. But, as *International Paper Company* recognized, complexity does not alter coverage. Only by revising its policy language can Hiscox accomplish that outcome. A proximate cause standard meanwhile keeps the crime, fidelity, and cyber coverage Wisconsin businesses buy meaningful against the schemes that threaten them.

CONCLUSION

UP respectfully requests that this Court reverse the Court of Appeals, which erred in holding that Continental's losses did not result directly from Eguizabal's theft, and hold that "resulting directly from" requires only proximate causation.

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FORM AND LENGTH CERTIFICATION

I hereby certify that this brief conforms to the rules contained in Wis. Stat. §§ 809.19(8)(b), (bm), and (c) for an amicus brief. The length of this brief is 2,598 words.

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