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SUPREME COURT

SUPREME COURT OF WISCONSIN

Kemper Independence
Insurance Company,

Plaintiff-Respondent,

Appeal No. 2019-AP-000488

v.

Ismet Islami,

Defendant-Appellant-Petitioner.

BRIEF OF WISCONSIN ASSOCIATION FOR JUSTICE

On Review of Wisconsin Court of Appeals May 27, 2020 Decision
Affirming Summary Judgment in the Waukesha County Circuit Court
Honorable William J. Domina Presiding
Circuit Court Case No. 13-CV-002875

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INTRODUCTION

Years after entering a legal separation agreement, Ydbi Islami set fire to Ismet Islami's house—a property in which he no longer had any legal or insurable interest—and Ismet's home and property was lost. After committing the arson, Ydbi lied about his crime, including to the property's insurer, Kemper Independence Insurance Company ("Kemper"). Indisputably, Ismet was not involved in the arson, she did not lie about anything related to the matter, and the parties agree that she is innocent of misconduct for all material purposes.

Kemper's position on Ismet's claim for insurance coverage seems to be that, under its policy, Ismet was entitled to full coverage for her loss when Ydbi criminally set her home ablaze, but that she lost the right to any coverage whatsoever when Ydbi lied about his involvement in the deed, months later.

The lower courts accepted the carrier's coverage stance, and the Wisconsin Association for Justice ("WAJ") asks this Court to reconsider the issue and reverse the bizarre interpretation of the policy under the circumstances involved here. In our view, the lower courts misapprehended and misapplied the law as to this innocent insured's claim for insurance coverage.[1] We believe that the policy contains clear terms affording coverage to innocent insureds like Ismet, and consistent with those terms, any reasonable insured would rightly expect to receive coverage here. In accordance with prevailing, and well-established, law, the policy should be construed in favor of coverage.

[1] Ismet offers several reasons why she is entitled to coverage, including that Ydbi cannot be considered her "spouse" for coverage purposes in light of their legal separation and, by virtue of statute, Kemper is prohibited from denying the claim as she is the victim of domestic abuse. WAJ agrees that the case can and should be resolved on those grounds, but offers an analysis of her entitlement to coverage as an innocent insured should the Court reach the issue.

ARGUMENT

I.

In Line with the Modern Trend, Wisconsin Courts Do Not Invalidate Coverage for Innocent Insureds Unless Their Policies Include Clear Terms of Joint Interests and Responsibilities for Misconduct.

The question of whether an innocent insured is entitled to recover the proceeds of a fire insurance policy has historically presented a difficult challenge for courts. *See, e.g.*, *Watts v. Farmers Ins. Exchange*, 98 Cal. App. 4th 1246 (Cal. Ct. App. 2002) (analyzing large number of decisions addressing the issue); *see also* Leane English Cerven, *The Problem of the Innocent Co-insured Spouse: Three Theories on Recovery*, 17 VAL. U. L. REV. 849 (1983). More specifically, the issue inevitably required significant competing interests to be balanced—avoiding a possible benefit to a wrongdoer versus preventing the imposition of fraud on an innocent party. *Id.*

Traditionally, under the "old rule," arson on the part of one insured barred any recovery that could be available to another insured. Steven Plitt, *Analyzing the Innocent Co-Insured Exception to Intentional Acts in Community Property States*, CLAIMS JOURNAL (June 10, 2008), https://www.claimsjournal.com/news/national/2008/06/10/90828.htm. Courts that chose to bar recovery reasoned that co-insureds automatically have joint, indivisible obligations, and that allowing recovery to an innocent co-insured could unjustly benefit the wrongdoing insured. *Id.*; *see also Vance v. Perkin Ins. Co.*, 457 N.W.2d 589, 591 (Iowa 1990). For example, where spouses hold an indivisible interest in the whole of community property, a payment to the innocent insured for the full value of the lost property would indirectly flow to the guilty spouse who would be a participant in the marital community. In other words, courts applying the

absolute bar focused on the interests and obligations arising from the nature of property ownership. *Id.*

Over time, courts began to reject the principles underlying the "old rule." *Hedtcke v. Sentry Ins. Co.*, 109 Wis. 2d 461, 479–89, 326 N.W.2d 727 (1982) (describing trend away from rule absolutely barring recovery). These courts recognized that the imposition of liability for fraud on an innocent person is contrary to the American system of justice, which is premised on individual responsibility for misconduct. *Id.*; *see also American Econ. Ins. Co. v. Liggett*, 426 N.E.2d 136, 140 (Ind. App. 1981). The courts reasoned that reasonable insureds would not expect arson or other intentional acts to be imputed, that punishing innocent victims runs contrary to basic notions of fair play and justice, and that imputing the incendiary actions of a wrongdoing insured to an innocent insured produced inequitable results. *Hedtcke*, 109 Wis. 2d at 483–89. Moreover, by imposing constructive trusts or, where necessary, placing appropriate limitations on remedies, the courts also recognized that relief could be adequately fashioned to prevent a wrongdoer from profiting. *Id.* at 488. As a result, the law trended toward a modern rule that deemed the absolute bar to be inappropriate, and required courts to determine rights based on the particular factual context. *Id.* at 486, 489.

Under the modern rule, rather than focusing on the interests and obligations arising from the nature of property ownership, courts have focused on the contract of insurance, and the language of the policy, to determine whether the rights of the insureds are joint or separate. Cerven, 17 VAL. U. L. REV. 849, 865–69; *Hedtcke*, 109 Wis. 2d at 483–89. Where policy terms are clearly set forth, courts have found obligations and rights to be joint. *Id.* But where policy language is fairly susceptible to more than one meaning, courts have interpreted the policy language against the insurer that drafted the policy, in accordance with the reasonable

expectations of a buyer, and deemed the rights and obligations separate, or several. *Id.*

Since 1982, the Wisconsin Supreme Court has sanctioned the use of the modern rule in this State, and Wisconsin courts have therefore applied principles of insurance policy construction to determine the rights of the innocent insured. *Hedtcke*, 109 Wis. 2d at 479–89.

II.

The Kemper Policy at Issue Covers Property Subject to Legally Separate Rights, Contains Terms That Create Separate Responsibilities, and Specifically Offers Protection to Innocent Insureds Against Joint Responsibility.

In our view, consistent with the modern approach adopted by Wisconsin courts, the Kemper policy at issue was clearly designed to offer protections to an innocent insured from the misconduct of another insured. As we now demonstrate, under the particular factual circumstances at issue here, we believe that the policy was issued to parties who clearly had separate rights and obligations under terms that would treat the insureds separately, and that—as a result—any reasonable innocent insured would rightly expect to be covered here.

First, the policy was issued to insureds who clearly had separate interests—the policyholders had been legally separated and the property covered by the policy was owned severally. A-App. 201–24. In other words, Ismet's home and vehicle, to which she held sole title, were covered under the policy, as was Ydbi's vehicle for which he held title. *Id.* Ydbi had no insurable interest in Ismet's home, and in light of his legal separation from Ismet, Ydbi had no legal interest in any proceeds relative to the loss of Ismet's home. *Id.* Because the

policy was issued to cover separately owned property to insureds who had separate legal rights, the policyholders clearly did not have joint interests at the time the policy was issued.

Second, the policy includes clear terms indicating that misconduct and the consequences for misconduct would be treated separately against the policyholders. A-App. 268. Indeed, the policy terms specifically exclude coverage to an insured who intentionally does wrong while at the same time preserve coverage for the innocent insured who commits no misconduct relative to the same loss:

> 1.h **Intentional Loss.**
> Intentional Loss means any loss arising out of any act an "insured" commits or conspires to commit with the intent to cause a loss.
>
> This exclusion only applies to an "insured" who commits or conspires to commit an act with the intent to cause a loss.

Id. By virtue of the application of the policy's terms with respect to intentional acts, any insured would reasonably expect responsibility for misconduct to be separate, and clearly not joint.

Third, and similarly, the policy includes terms which treat statements and representations as well as the potential consequences for statements and representations singularly and separately:

> No oral or written statement or representation made by you or on your behalf and no breach of an affirmative warranty affects our obligations under this policy:
>
> 1. Unless we rely on it and it is either material or is made with intent to deceive; or
> 2. Unless the fact misrepresented or falsely warranted contributes to the loss.

A-App. 270. In other words, by limiting consequences for statements and representations to those made by "you" rather than "any" or "all" insureds, the policy again suggests that the policyholders would be treated separately rather than jointly with respect to responsibility for statements and representations.

In summary, the Kemper policy was issued to cover property that was separately owned, and contained clear terms indicating that the conduct of insureds would be treated separately with respect to acts, statements, or representations. Under circumstances like those at issue here, any innocent insured would rightly and reasonably expect to receive coverage from the policy.

III.

Kemper's Policy Interpretation Should Be Rejected Because It Is Inconsistent with Policy Terms, Is Out-of-Line with Reasonable Expectations, and Would Lead to an Absurd Result.

Kemper relied on a concealment or fraud condition to deny Ismet's claim for coverage, but in our view, construing the provision as Kemper asks would be inconsistent with this Court's long-established principles of insurance policy interpretation and construction.

More specifically, insurance policy language is construed plainly and from the perspective of a reasonable insured. *State Farm Mut. Auto. Ins. Co. v. Langridge*, 2004 WI 113, ¶ 14, 275 Wis. 2d 35, 683 N.W.2d 75. Language must be viewed in context, as "it is necessary to look beyond a single clause or sentence to capture the essence of an insurance agreement." *Folkman v. Quamme*, 2003 WI 116, ¶ 21, 264 Wis. 2d 617, 655 N.W.2d 857. If the language is

plain, it is applied as written. *Id.* ¶ 13. If, however, policy language is susceptible to more than one reasonable interpretation, the ambiguity is resolved in the insured's favor. *Marnholtz v. Church Mut. Ins. Co.*, 2012 WI App 53, ¶ 10, 341 Wis. 2d 478, 815 N.W.2d 708. This Court has recognized that "insurers have the advantage over insureds because they draft the contracts." *Folkman*, 264 Wis. 2d 617, ¶ 16. Further, "[o]ccasionally a clear and unambiguous provision may be found ambiguous in the context of the entire policy." *Id.* ¶ 19. It is thus "necessary to look beyond a single clause or sentence to capture the essence of an insurance agreement . . . ." *Id.* ¶ 21. "Insurers dislike this principle. Yet, the opposite principle—that courts must mechanically apply a clear provision regardless of the ambiguity created by the organization, labeling, explanation, inconsistency, omission, and text of the other provisions in the policy—is not acceptable." *Id.* A policy that builds up false expectations, contains inconsistent provisions, or is so "deceptive that it befuddles the understanding and expectations of a reasonable insured" are considered ambiguous. *Id.* ¶¶ 20, 31. And ultimately, insurance policies must be given a reasonable interpretations, not ones which lead to absurd results. *McPhee v. American Motorists Ins. Co.*, 57 Wis. 2d 669, 679–80, 205 N.W.2d 152 (1973).

Applying the straightforward principles of insurance policy construction to determine the rights of the innocent insured in this case, this Court should interpret and construe the policy in favor of coverage for the following reasons:

- Though the concealment or fraud condition can be read to void coverage on a joint basis, other policy terms create the reasonable expectation that the rights of the insureds are several under the specific circumstances at issue in this case. The inconsistency creates ambiguity, and the ambiguity must be construed in favor of coverage. *See Spence v. Allstate Ins. Co.*, 883 S.W.2d 586, 591–93 (Tenn. 1994)

(finding provisions similar to those at issue to be ambiguous in context).

- By virtue of the terms of the intentional-act exclusion, Ydbi was not a covered "insured" under the terms of the policy when he made the misrepresentations at issue. More specifically, the terms of the intentional-act exclusion operate to exclude wrongdoers from coverage for a loss once the wrongdoer commits an intentional act resulting in loss, but the exclusion does not preclude coverage for all individuals or any claim relative to the loss. After he committed arson on Ismet's home, Ydbi was excluded from coverage for the loss as an insured under the plain terms of the intentional-act exclusion, and he did not qualify as an insured when he later misrepresented his involvement in the arson. This plain reading of the policy means that Ydbi's misrepresentations cannot be applied to void coverage as to Ismet under the concealment and fraud condition.

- Construing the policy in favor of coverage will avoid an absurd result. Why would Ismet be entitled to full coverage for her loss when Ydbi criminally set her home ablaze but lose the right to any coverage whatsoever when Ydbi lied about his involvement months later?

Ultimately, the policyholders involved here kept their property interests separate, and purchased a policy that provided for separate rights, responsibilities, obligations, and interests in material respects. No wrongdoer can receive any benefit under the circumstances in issue, and prohibiting coverage to Ismet in this context would be inconsistent with both the policy terms, prevailing law, and basic notions of fair place and justice. Kemper's position should therefore be rejected.

CONCLUSION

We believe that the approach Wisconsin courts apply to address the issue of the innocent insured is well-settled and in line with the most well-reasoned authority.

This Court need not reconsider the approach at this time, but should recognize that the lower courts misapprehended and misapplied the law to the specific factual circumstances and context at issue in this case.

For those reasons, the Court of Appeals' decision should be reversed.

Dated this 2nd day of December, 2020.

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FORM AND LENGTH CERTIFICATION

I certify that this brief conforms to the rules contained in § 809.19(8)(b) and (c) for a brief produced using the following font: proportional serif font: minimum printing resolution of 200 dots per inch, 13 point body text, 11 point for quote and footnotes, leading of minimum 2 points, maximum of 60 characters per full line of body text. The length of this brief is 2,338 words.

Dated this 2nd day of December, 2020.

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I hereby certify that I have submitted an electronic copy of this brief which complies with the requirements of Wis. Stat. § 809.19(12). I further certify that this electronic brief is identical in content and format to the printed form of the brief filed as of this date. A copy of this certificate has been served with the paper copies of this brief filed with the court and served on all opposing parties.

Dated this 2nd day of December, 2020.

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