No. ___________

IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

GRANT THORNTON LLP, Plaintiff Below/Petitioner,

v.

KUTAK ROCK LLP, Defendant Below/Respondent.

PETITION FOR APPEAL

Honorable Rudolph J. Murensky, II
Circuit Court of McDowell County
Civil Action No. 04-C-33-M

John H. Tinney (WV Bar #3766)
John K. Cecil (WV Bar #9155)
The Tinney Law Firm, PLLC
222 Capitol Street, Ste. 500
Charleston, WV 25337-3752
(304) 720-3310

Stanley J. Parzen
Mayer Brown LLP
71 South Wacker Drive
Chicago, IL 60606
(312) 782-0600

Counsel for Grant Thornton LLP

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INTRODUCTION

This case is one of several arising from the insolvency and eventual closure in September of 1999 of the First National Bank of Keystone ("Keystone" or the "Bank"). For a number of years, Keystone's management fraudulently concealed the Bank's financial condition from federal regulators and others. Plaintiff Grant Thornton LLP ("Grant Thornton") is an accounting firm that performed a single audit of Keystone's 1998 financial statements. Defendant Kutak Rock LLP ("Kutak" or the "Firm") served as Keystone's principal outside counsel for several years preceding the Bank's collapse. In the case before the Circuit Court, Grant Thornton sued Kutak for defrauding Grant Thornton and committing other torts against it before and during Grant Thornton's audit of Keystone. Simply put, Grant Thornton contends that the Kutak attorneys intentionally and negligently misrepresented, and failed to disclose, facts that would have alerted Grant Thornton to Keystone's dire financial condition and the efforts at concealment by the Bank's management. These tortious acts caused Grant Thornton to issue an audit report that incorrectly assessed the accuracy of Keystone's 1998 financial statements.

Grant Thornton seeks as damages the costs it has incurred as a result of Kutak's misconduct directed against it, including the costs of defending litigation brought against Grant Thornton after the collapse of Keystone, and the amount of any judgment against it in that litigation. In particular, after the Bank closed, both Grant Thornton and Kutak faced claims of professional malpractice brought by the Federal Deposit Insurance Corporation ("FDIC"), which was appointed Keystone's receiver. Kutak settled with the FDIC for $22 million, while Grant Thornton defended the case against it in the U.S. District Court for the Southern District of West Virginia, and was held liable to the FDIC for $25 million for having conducted a negligent audit. *See Grant Thornton, LLP v. FDIC*, 535 F. Supp. 2d 676, 729 (S.D. W. Va. 2007) ("*Grant*

Thornton I"), *rev'd in part on other grounds sub nom. Ellis v. Grant Thornton LLP*, 530 F.3d 280 (4th Cir. 2008). Subsequently, the district court awarded Grant Thornton a credit of only $1.3 million for the Kutak-FDIC settlement—an amount calculated without considering Grant Thornton's direct claims against Kutak—and entered a reduced final judgment against Grant Thornton of $23.7 million. *See Grant Thornton, LLP v. FDIC*, 694 F. Supp. 2d 506, 532 (S.D. W. Va. 2010) ("*Grant Thornton II*"). Among the damages that Grant Thornton now seeks from Kutak is the amount of this final judgment.

Strong evidence on the record before the Circuit Court supports Grant Thornton's claims against Kutak. Both the FDIC in bringing claims against Kutak, and the district court in determining the amount of the settlement credit in *Grant Thornton II*, detailed the serious misconduct committed by Kutak attorneys—particularly the partner in charge of the Keystone engagement, Michael Lambert—in connection with the Bank's failure. Indeed, both expressed the view that Mr. Lambert was "probably the one person" who could have "stopped" the Keystone fraud. And, based on his conduct while representing Keystone, the FDIC and the Office of the Comptroller of the Currency ("OCC") no longer permit Mr. Lambert to represent insured depository institutions.

Kutak's wrongful conduct harmed Grant Thornton directly. In particular, Grant Thornton has shown in this litigation that Kutak attorneys (i) failed to disclose to Grant Thornton critically important information regarding the Bank and its management, (ii) failed to speak up when Keystone's management misrepresented the Bank's financial condition to Grant Thornton, and (iii) made affirmative misrepresentations to Grant Thornton regarding the Bank and its management. Based on this evidence and the opinions of two well-qualified experts, Grant

Thornton demonstrated that Kutak's silence and its affirmative misrepresentations contravened the West Virginia Rules of Professional Conduct and violated duties that the Firm owed to Grant Thornton under West Virginia law.

The Circuit Court granted summary judgment to Kutak, but not based on any argument that the evidence failed to support the elements of the claims that Grant Thornton pled and sought to prove. Instead, the court held that Grant Thornton's claims—although stated as direct claims for fraud, negligent misrepresentation, and tortious interference with contract—were in reality claims for contribution, or perhaps indemnity. The court then held that these claims, so characterized, were barred under West Virginia law by (i) Kutak's settlement with the FDIC and (ii) a combination of the district court's finding that Grant Thornton acted negligently in connection with the Keystone audit and the district court's award of a settlement credit in *Grant Thornton II.* The Circuit Court also ruled that, as a matter of law, Grant Thornton's negligence and its "voluntary" decision to defend against the FDIC's claims precluded its recovery of the expenses incurred in the Keystone-related litigation.

The Circuit Court's ruling is flawed in a number of respects. As the district court itself recognized, under West Virginia law the Kutak-FDIC settlement extinguished only claims for contribution—that is, claims premised on the theory that Kutak and Grant Thornton shared a common obligation ***to Keystone*** and that Kutak therefore should pay its share of the jointly caused damages. The direct claims Grant Thornton has asserted in this case, by contrast, are premised on the theory that Kutak breached duties it owed ***to Grant Thornton.*** As a result of this fundamental fact, Grant Thornton's right to be compensated for a fraud directed against it cannot by affected by Kutak's settlement with another party—as other courts have recognized in permitting similar claims to go forward. Likewise, while the district court's finding of negligence against Grant Thornton precluded it from suing Kutak for indemnity, that finding has no bearing on the direct claims Grant Thornton has asserted here. Like claims for contribution, claims for indemnity are premised on joint liability to a third party; by contrast, Grant Thornton's claims in this case are predicated on Kutak's violation of rights belonging to Grant Thornton.

Unlike the Circuit Court in this case, the district court recognized the distinction between claims for contribution (or indemnity) and direct claims: it held that Grant Thornton's contribution claims were barred by the Kutak-FDIC settlement, but stated that any direct claims that Grant Thornton had against Kutak "may be addressed" in a separate lawsuit. In taking a different approach, the Circuit Court misread this Court's precedents, and effected a radical and unwarranted expansion of the contribution bar recognized by those decisions to preclude even properly pled direct claims. That ruling is at odds with not only the jurisprudence of this Court, but also with that of other jurisdictions. The Circuit Court committed further error in ruling that Grant Thornton could not recover its collateral litigation expenses, improperly deciding an issue that Kutak raised for the first time in its reply memorandum in support of its summary judgment motion and, on the merits, misstating and misapplying West Virginia precedent addressing when such expenses are recoverable.

The legal issues presented in this case merit review by this Court. Cases often settle, and parties in West Virginia understand that a settlement between a plaintiff and a tortfeasor extinguishes contribution claims by and against any joint tortfeasors. This Court has never previously indicated, however, that settlement also extinguishes claims between joint tortfeasors based on breaches of independent duties. If adopted, the Circuit Court's view that such direct claims should be recharacterized as claims for contribution (or perhaps indemnity), and therefore precluded by a settlement between one joint tortfeasor and the plaintiff (or by the claimant's own negligence), would have far-reaching and undesirable implications that this Court should consider.

As this petition will show, precedent in West Virginia and elsewhere recognizes the fundamental right of parties, even parties adjudged negligent, to pursue direct claims such as those alleged here if they can prove the necessary elements. There is nothing in law, logic or West Virginia's policy promoting settlements that supports the contrary approach adopted by the Circuit Court—which entails essentially rewriting the complaint to contain claims for contribution and indemnity that were never pled. Indeed, that approach works a severe injustice and encourages opportunistic behavior by permitting a defendant, even one that has defrauded a co-defendant claimant, to extinguish its direct liability to that claimant by settling a separate claim with the plaintiff. But where, as here, the defendant-claimant was not involved in the settlement negotiations and is not a party to the settlement agreement, the settling party's wrongful conduct toward the claimant would not have factored into the settlement at all. As a result, the defendant-claimant's rights would be severed without compensation, and the settling defendant would be immunized against accountability for its wrongful conduct.

Indeed, the Circuit Court's ruling undermines West Virginia's public policy interests by discouraging parties from collaborating to settle all direct claims at an early stage, and instead encouraging them to litigate over whether the claims should be reframed as barred contribution claims. It also perniciously incentivizes unethical attorneys and others to engage in misconduct against third parties involved in an engagement for a common client. The wrongdoer can commit malfeasance safe in the knowledge that if the engagement goes wrong, it can divest those third parties of their right to assert direct claims by settling quickly with the client. For these reasons, as elaborated more fully below, this Court should grant review.

KIND OF PROCEEDING AND NATURE OF THE RULINGS

On February 10, 2004, Grant Thornton filed this civil action in the Circuit Court of McDowell County, alleging claims for fraud, negligent misrepresentation, and tortious interference with contract against Kutak based on its actions in connection with Grant Thornton's audit of Keystone. On March 11, 2010, the Circuit Court granted Kutak's motion for summary judgment. *See* Order Granting Def.'s Mot. for Summ. J. (entered Mar. 11, 2010) ("Cir. Ct. Op."). On March 24, 2010, Grant Thornton filed a motion to alter or amend the judgment, which the court denied on August 31, 2010. *See* Order Den. Grant Thornton's Mot. to Alter or Amend J. (entered Aug. 31, 2010) ("Alter/Amend J. Order"). This petition follows that ruling.

STATEMENT OF FACTS

A. The Keystone fraud and collapse

The facts relevant to this appeal, which must be viewed in the light most favorable to Grant Thornton, *see* Syl. Pt. 1, *Painter v. Peavy*, 451 S.E.2d 755 (W. Va. 1994), are as follows.

Keystone was a small community bank, servicing primarily McDowell County and the surrounding area, until 1992, when it began securitizing high-risk loans. Keystone would acquire and pool the loans, sell interests in the pool to investors, and retain for itself a residual interest. *See Grant Thornton I*, 535 F. Supp. 2d at 679-80.[1] Although Keystone appeared to be

[1] The Circuit Court made "[t]he findings of fact as set forth in [*Grant Thornton I*] . . . a part of [its order granting Kutak's motion for summary judgment] the same as though set forth [t]herein *in extenso*." Cir. Ct. Op. at 4 ¶ 12.

exceptionally profitable, in reality the securitization program led to massive financial losses. *See id.* at 681. Despite intensive oversight by federal regulators, Keystone's management successfully concealed the losses, and their own embezzlement of Bank funds, for a number of years by engaging in a massive fraud that involved falsification of the Bank's books and records. *See id.*; *see also* Answer and Aff. Defs. of Kutak Rock LLP, ¶¶ 18-21 (entered Oct. 27, 2008) ("Kutak Answer").

Keystone finally closed its doors on September 1, 1999, when an examination by the OCC revealed that the Bank was reporting on its books $500 million of loans that it did not actually own. *See Grant Thornton I*, 535 F. Supp. 2d at 695, 702; Kutak Answer ¶ 1. These loans were in fact owned by a different financial institution, United National Bank ("United"), which was using Keystone as a conduit for its own purchase of loans from originators. *See* Cir. Ct. Op. at 2 ¶ 4.

B. Kutak's knowledge of the Keystone fraud

For the six years prior to Keystone's closure, Kutak attorneys performed extensive work for the Bank, including services related to its loan securitization program, litigation, and regulatory compliance. *See* Ex. J, Grant Thornton LLP's Resp. to Mot. of Kutak Rock LLP for Summary J. on Grant Thornton's Compl. (entered Dec. 17, 2008) ("Grant Thornton Resp.");[2] *see also Grant Thornton II*, 694 F. Supp. 2d at 511-12; GT Ex. I at 2. Michael Lambert was the partner in charge of the Firm's representation of Keystone, and was closely enmeshed in the Bank's business affairs. *See* Cir. Ct. Op. at 2 ¶ 5; *Grant Thornton II*, 694 F. Supp. 2d at 511; *see also id.*

[2] References to the exhibits to the Grant Thornton Response will appear hereinafter as "GT Ex. __."

at 516-20; GT Ex. J; Ex. 18 at 66:8-13, Mem. of Law in Supp. of Mot. of Kutak Rock LLP for Summ. J. on Grant Thornton's Compl. (entered Nov. 10, 2008) ("Kutak Summ. J. Mem.").[3] Because of Mr. Lambert's conduct in connection with Keystone's failure, the FDIC and the OCC no longer permit him to represent insured depository institutions. *See* GT Ex. E ¶ 40.

The FDIC's lead investigator into Kutak's representation of Keystone concluded that, "at least by 1996, Kutak Rock's knowledge of irregularities at Keystone clearly triggered a duty to report to the Board." Ex. B at 5, Grant Thornton LLP's Resp. to Kutak Rock LLP's Mot. to Exclude Test. of Professor John Taylor (entered Nov. 10, 2009);[4] *see also Grant Thornton II*, 694 F. Supp. 2d at 521. As the FDIC explained in a mediation letter submitted in connection with its settlement discussions with Kutak in 2002 ("FDIC mediation letter"), Mr. Lambert (and thus the Firm) was aware of nine red flags regarding the securitization program that revealed the Bank's troubled financial condition and the corrupt activities of its management and business partners. *See* GT Ex. I at 2-4.

Evaluating much of the same evidence that Grant Thornton relies on in this case, the district court in *Grant Thornton II* explained that these red flags revealed to Kutak as early as 1994 that the Bank's management was "falsif[ying]" its "records" and "violating federal banking regulations." *Grant Thornton II*, 694 F. Supp. 2d at 518; *see also* GT Ex. I at 3.[5] They also

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[3] References to the sequentially numbered exhibits to the Kutak Summary Judgment Memorandum and to Kutak Rock LLP's Reply to Grant Thornton LLP's Response to Kutak Rock's Motion for Summary Judgment (entered Jan. 7, 2009) ("Kutak Reply") will appear hereinafter as "Kutak Ex. __."

[4] This exhibit will be referred to hereinafter as the "Taylor Report."

[5] The district court issued its opinion in *Grant Thornton II* on March 10, 2010, one day before the Circuit Court entered its decision granting Kutak's motion for summary judgment in this case. Although the Circuit Court thus did not have the benefit of the district court's factual findings in rendering its

revealed to Kutak that (i) "the loans going into Keystone's securitizations were of poor quality," and the securitizations were "not performing well," *Grant Thornton II*, 694 F. Supp. 2d at 517-19; (ii) the "loan data underlying the securitization[s]" was of "question[able] . . . integrity," *id.* at 519; and (iii) a number of Keystone's securitization partners were "dishonest," engaging in a "scheme to defraud" it, and otherwise placing "the Bank's interests . . . in jeopardy," *id.* at 517-20. *See* GT Ex. I at 2-3. The red flags also alerted Kutak that the Bank's "residual valuations"—*i.e.*, the valuations of the interests in the securitized loans that Keystone retained—"were overstated," *Grant Thornton II*, 694 F. Supp. 2d at 516-517, 520, and that the Bank's assets were "inflated," *id.* at 519. *See* GT Ex. I at 2-3; *see also Grant Thornton II*, 694 F. Supp. 2d at 519. And the red flags further revealed to the Firm that the OCC had made a referral to the FBI "regarding inappropriate appraisal fees paid to Terry Church [a director and officer of the Bank]," *Grant Thornton II*, 694 F.2d at 519,[6] and that Keystone's CFO, Ron Mitchell, considered himself "a sham CFO" without "qualifications for the job," *id.* at 519. *See* GT Ex. I at 4.

Based on Kutak's knowledge of these red flags, the FDIC concluded—and the district court agreed in *Grant Thornton II*—that Mr. Lambert was "probably the one person who had the knowledge, credibility and persuasiveness sufficient to have stopped" those responsible for

decision, the Circuit Court found in denying Grant Thornton's motion to alter or amend judgment that "[p]laintiff had previously presented all this evidence [from the district court's opinion in *Grant Thornton II*] to this Court and [the findings and conclusions in that opinion are] not new evidence." Alter/Amend J. Order at 3; *see also* Kutak Rock LLP's Resp. in Opp'n to Grant Thornton LLP's Mot. to Alter or Amend the J. 4-5 (entered June 23, 2010) (same). Grant Thornton agrees that the findings in *Grant Thornton II* are fully consistent with the evidence available to the Circuit Court in deciding Kutak's motion for summary judgment, and in any event has provided citations to the record or the Circuit Court's findings in this case (including the findings in *Grant Thornton I*) for all significant factual statements made herein.

[6] Ms. Church was a key architect of the Keystone fraud. *See Grant Thornton I*, 535 F. Supp. 2d at 680.

defrauding the Bank, and that he "could have prevented most of the $800 million in losses suffered by the Bank." GT Ex. I at 2; *see also Grant Thornton II*, 694 F.2d at 521. And in the opinion of John Taylor, Grant Thornton's legal ethics expert, "the extensive involvement of Kutak Rock in Keystone's securitization business gives rise to a plausible inference that Kutak Rock must have known about the criminally fraudulent activities being carried out by Keystone's corrupt management." Taylor Report at 1-2.

C. Kutak's violations of duties to Grant Thornton in connection with Grant Thornton's audit of Keystone

On September 10, 1998, Keystone retained Grant Thornton to audit the Bank's financial statements as of December 31, 1998. *See Grant Thornton I*, 535 F. Supp. 2d at 682-83. On April 19, 1999, Grant Thornton issued its audit report, concluding that Keystone's financial statements were fairly stated in accordance with Generally Accepted Accounting Principles. *See id.* at 695; *see also* Cir. Ct. Op. at 2 ¶ 3. This conclusion later turned out to have been incorrect. *See* Cir. Ct. Op. at 2 ¶ 4.

As described below, during the course of the audit, Kutak attorneys made misstatements to the Grant Thornton auditors—Stanley Quay and Susan Buenger—and failed to correct misstatements that Keystone's management made to the auditors in the attorneys' presence. The Kutak attorneys also did not inform the auditors of highly relevant and important information regarding the Bank's long history of improper—and in some cases clearly illegal—conduct. Assuming, as the evidence indicates, that Kutak knew the relevant facts at the time of the audit, it is Mr. Taylor's opinion that the Firm's misstatements, half-truths, and failures to speak up to correct the lies of others violated a number of provisions of the West Virginia Rules of Professional Conduct. *See* Taylor Report at 5-6. And the evidence also demonstrates that

Kutak's misconduct was a significant factor in Grant Thornton's issuance of an incorrect audit report: Grant Thornton's accounting expert, Kevin Bandoian, opined that if Kutak had been truthful with the Grant Thornton auditors, "the loan fraud would have been discovered prior to the issuance of any audit report." GT Ex. R at 8.

The following discussion summarizes the evidence detailing the major instances in which Kutak's actions violated the West Virginia Rules of Professional Conduct and its duties to Grant Thornton.

1. **Kutak's affirmative misrepresentations to Grant Thornton**

"Regardless of confidentiality considerations, a lawyer may not knowingly make false statements of material fact to third persons such as Grant Thornton." Taylor Report at 5 (citing Rule 4.1(a) of the West Virginia Rules of Professional Conduct). Nonetheless, on a number of occasions, Kutak attorneys made direct and fraudulent misrepresentations to the Grant Thornton auditors regarding matters of unquestionable importance to Grant Thornton's auditing process. *See* supplemental answer 3(a), (b), (d), (g), & (j), Grant Thornton's Supplemental Resp. to Def.'s 1st Set of Interrogs. (entered Nov. 13, 2008) ("Supplemental Resp."); *see also* Taylor Report at 5. Kutak attorneys also uttered misleading half-truths and failed to speak up on important subjects in contexts where those actions were the legal equivalent of affirmative misrepresentations. *See* Supplemental Resp. at supplemental answer 3(f), (i), & (k); *see also* Taylor Report at 5-6.

For example, before Grant Thornton accepted the Keystone engagement, a Kutak attorney told Mr. Quay that Keystone management was "honest," *see* Supplemental Resp. at 7—thus directly contradicting what, according to the FDIC (and the district court in *Grant Thornton*

II), Kutak knew about the fraudulent conduct of the Bank's management. *See, e.g.*, GT Ex. I at 2-4; *Grant Thornton II*, 694 F. Supp. 2d at 517-18; Tr. of Evidentiary Hr'g Held Before the Hon. David A. Faber, Judge, U.S. District Ct. in Charleston, W. Va. at 56 (attached as App. Ex. A) ("Settlement Credit Hr'g Tr."), *Grant Thornton II*, 694 F. Supp. 2d 506. And, on several occasions, Mr. Lambert confirmed for the auditors representations made by Keystone's management regarding the value of Keystone's residuals in connection with various securitizations. *See* Supplemental Resp. at 5. Yet, as the district court and the FDIC concluded, Mr. Lambert had ample reason to know that the value of the residuals was less than Keystone's management was claiming. *See* supra pp. 7-10.[7]

Perhaps Kutak's most significant misstatement was contained in an attorney disclosure response that Mr. Lambert sent Grant Thornton on March 1, 1999.[8] The response stated "[w]e confirm as correct the Bank's representation to you that there are no unasserted possible claims with respect to which we have advised the Bank of a probability of assertion and which must be disclosed in accordance with [Financial Accounting Standard No.] 5 ("FAS No. 5")." GT Ex. H at 4.[9] According to Mr. Taylor, this statement "amount[ed] to a representation that there were no

[7] In particular, Mr. Lambert knew that two originators involved in Keystone's securitizations had engaged in a fraudulent practice called "fronting." *See* GT Ex. I at 2-3; *see also Grant Thornton II*, 694 F.2d at 516, 518. "'Fronting' is a common scam in the consumer lending industry in which loan originators use either loan proceeds or their own funds to make the payments on poor quality loans to create the appearance of performance so that the loans will be purchased by unsuspecting entities such as Keystone." *Grant Thornton II*, 694 F. Supp. 2d at 517.

[8] Outside counsel is expected to use such a letter to confirm for an auditor that management has properly identified and evaluated all legal claims, and if necessary to reveal to the auditor any previously undisclosed claims. *See* Taylor Report at 12-14.

[9] According to Mr. Taylor, "disclosure of unasserted claims is required" under this standard "where the assertion of the claim is 'probable,' there is at least a 'reasonable possibility' of an unfavorable outcome if the claim is asserted, and the resulting liability would materially affect the financial condition of the client." Taylor Report at 14-15.

unasserted claims that Keystone was required to disclose under FAS No. 5." Taylor Report at 14. The evidence adduced in this case, however, indicates that when Mr. Lambert sent the letter, he was aware of a number of such claims stemming from the activities described in the FDIC's mediation letter. *See* supra pp. 7-10. Moreover, there is evidence indicating that Mr. Lambert was aware at that time that Keystone was in breach of its agreements with United (the bank that actually owned many of the loans claimed by Keystone) governing Keystone's purchases of loans on behalf of United. *See* GT Ex. R at 8; *see also* Supplemental Resp. at 7; Taylor Report at 15; Kutak Ex. 18 at 67:18-68:9; Kutak Ex. 34 at 82:13-21; Settlement Credit Hr'g Tr. at 67-71, 118-120.

Mr. Bandoian has opined that the response should have disclosed—but did not—the information in the FDIC mediation letter, the existence of the agreements between United and Keystone, and the fact that Keystone had breached those agreements. *See* GT Ex. R at 6; *see also* Supplemental Resp. at 7; Settlement Credit Hr'g Tr. at 122:6-8. And according to Mr. Taylor, assuming—as the evidence indicates—that Mr. Lambert knew (or should have known) that this information should have been disclosed, "the audit inquiry letter would be a fraudulent [or negligent] misrepresentation." Taylor Report at 15. Further, these misrepresentations affected the outcome of the audit: as Mr. Quay testified in *Grant Thornton II*, Keystone's "entire house of cards" would have unraveled had the auditors known the truth. Kutak Ex. 18 at 68:9; *see also id.* at 76:10-19; Settlement Credit Hr'g Tr. at 71, 76, 118.

2. Kutak's acquiescence in a false statement by Keystone's management to Grant Thornton

The Circuit Court found that Kutak owed Grant Thornton a duty to disclose information concerning Keystone, rejecting Kutak's argument to the contrary as "without merit." Cir. Ct.

Op. at 13-14. Moreover, under West Virginia's Rules of Professional Conduct, "a lawyer may not simply stand by and do nothing while a client lies to third parties." Taylor Report at 6. On at least one occasion, however, Mr. Lambert was present and said (and did) nothing when Keystone management made false statements to the Grant Thornton auditors that, a jury could permissibly infer, the attorneys knew to be false.

Most notably, in January of 1999, Mr. Lambert participated in a conversation in which a member of Keystone's management confirmed for Mr. Quay that over $200 million of Keystone loans had been transferred to a servicer called Advanta, and that these loans were recorded properly on Keystone's books. *See* GT Ex. R at 6; Taylor Report at 9; Supplemental Resp. at 5-6; Kutak Ex. 32 at 53:4-23; Kutak Ex. 33 at 154:9-160:17; Kutak Ex. 34 at 52:16-56:20. This was "a lie and a fraud" intended to deceive the auditors; in fact, only $6.5 million of the loans transferred to Advanta actually belonged to Keystone, and the rest belonged to United. Taylor Report at 9. The evidence suggests that Mr. Lambert was well aware of the truth: in particular, he sent an e-mail on January 29, 1999 in which he stated that Advanta "has about $6.5 million in [Keystone] loans." GT Ex. N; *see also* Kutak Ex. 18 at 66:20-67:4; Settlement Credit Hr'g Tr. at 66-67. According to Mr. Bandoian, "[a]n auditor in [Mr. Quay's] position would fully expect to have been informed that the amount transferred was significantly less," and "[t]he absence of the transfer to Advanta would have called into question the information reflected on the Bank's books relating to its loans." GT Ex. R at 6, 8. Yet Mr. Lambert said and did nothing. *See id.* at 6; *see also* Settlement Credit Hr'g Tr. at 63-64, 119. "Grant Thornton would not have issued the same audit report, if any at all," had it learned the truth about this transfer. GT Ex. R at 7; *see also* Kutak Ex. 18 at 76:5-9; Settlement Credit Hr'g Tr. at 63, 76.

3. **Kutak's numerous failures to disclose relevant, material information to Grant Thornton**

Finally, Kutak failed to disclose to the auditors other important information that could have revealed the fraud at Keystone. For example, Mr. Lambert failed to inform the auditors that Keystone was in negotiations during the audit to acquire a servicer called Compulink. *See* Supplemental Resp. at 8. This fact "would have called into question the bona fides" of a false confirmation that Compulink provided Grant Thornton in connection with the audit, and should have been disclosed to the auditors. GT Ex. R at 6, 8; Kutak Ex. 18 at 67:8-18; Kutak Ex. 34 at 82:23-83:11, 84:3-15, 104:15-19.

Kutak also failed to tell the auditors about any of the red flags identified by the FDIC and the district court. *See* Supplemental Resp. at 8; GT Ex. R at 6-8. Had Kutak disclosed this critical information to Grant Thornton, "it would not have issued the same audit report, if any." GT Ex. R at 8; *see also id.* at 6; Kutak Ex. 18 at 76:1-4; Settlement Credit Hr'g Tr. at 57, 59-62, 76, 81, 84, 149.

D. The FDIC litigation in federal district court

After Keystone failed, the FDIC, which had been appointed the Bank's receiver, intervened in Keystone-related litigation then pending in the Southern District of West Virginia, and counterclaimed against Grant Thornton for malpractice. *See* Cir. Ct. Op. at 2 ¶ 6. The FDIC alleged that Grant Thornton had been negligent and reckless in issuing a clean audit opinion regarding Keystone's 1998 financial statements. *See id.*; GT Ex. A ¶¶ 144-155. At about the same time, the FDIC investigated Kutak's activities in connection with the Keystone failure, and developed sufficient evidence to present claims of malpractice to the Firm. *See Grant Thornton II*, 694 F. Supp. 2d at 512.

Kutak settled these claims with the FDIC for $22 million and Kutak's agreement to adhere to certain procedures in representing insured depository institutions. *See* GT Ex. E ¶¶ 29-30; *see also Grant Thornton II*, 694 F. Supp. 2d at 513. Grant Thornton went to trial on the FDIC's claims, and the district court ruled in March 2007 that Grant Thornton had been negligent in connection with the Keystone audit, and was liable to the FDIC for $25,080,777 million. *See Grant Thornton I*, 535 F. Supp. 2d at 729. The damages represented Keystone's operating losses—mostly interest that Keystone paid to its depositors—that would have been avoided had the Bank closed immediately following the audit.[10]

Grant Thornton argued that the full amount of the Kutak-FDIC settlement should be subtracted from the judgment because Kutak was responsible for the same losses that the FDIC was seeking from Grant Thornton. The district court ultimately agreed that Kutak and Grant Thornton were responsible for causing the same indivisible loss to Keystone and that Grant Thornton was therefore entitled to a settlement credit, but it awarded Grant Thornton a credit of only $1,343,751 plus 8.563% of any future payments from Kutak on the settlement. *See Grant Thornton II*, 694 F. Supp. 2d at 532; *see also* GT Ex. S. In the district court's view, only that percentage of the settlement was allocable to the operating losses jointly caused by Kutak and Keystone; the lion's share of the settlement, the court concluded, was allocable to the greater losses caused by Kutak alone.[11]

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[10] Grant Thornton has appealed this ruling to the U.S. Court of Appeals for the Fourth Circuit. *See Grant Thornton LLP v. FDIC*, No. 10-1306 (4th Cir.).

[11] Grant Thornton is challenging this ruling as well in its Fourth Circuit appeal, claiming entitlement to a larger settlement credit.

E. Grant Thornton's direct claims against Kutak

On April 3, 2003, as part of the FDIC litigation, Grant Thornton sought leave to file a third-party complaint against Kutak, asserting direct claims for fraud, negligent misrepresentation, and tortious interference with contract, as well as claims for contribution. *See* Cir. Ct. Op. at 3 ¶ 9; *see also* GT Ex. B ¶¶ 108-134. On May 23, 2003, however, Kutak reached its settlement with the FDIC. *See* Cir. Ct. Op. at 2-3 ¶ 7; GT Ex. E at 8. On December 11, 2003, the District Court entered an order ("December 11 Order") denying Grant Thornton's request to implead Kutak. *See* Cir. Ct. Op. at 3 ¶ 10; GT Ex. F. The court explained that West Virginia law barred the contribution claims, *see* GT Ex. F at 2 (citing *Smith v. Monongahela Power Co.*, 429 S.E.2d 643, 648 (W. Va. 1993); *Bd. of Educ. of McDowell Cnty. v. Zando, Martin & Milstead, Inc.*, 390 S.E.2d 796, 805 (W. Va. 1990)), and that there was therefore "no reason to allow Grant Thornton to file a third-party complaint for contribution against Kutak Rock." *Id.* at 3.

The district court also declined to allow Grant Thornton to file a third-party complaint raising its *direct* claims against Kutak, but it made clear that it did not view them as precluded by the contribution bar. Given that the case was "scheduled for trial in less than two months," it explained, "allowing Grant Thornton to add Kutak Rock as a third-party defendant at this late date would only serve to delay the trial." *Id.* at 5. It therefore stated that "[a]ny direct claims Grant Thornton has against Kutak may be addressed in another lawsuit." *Id.*; *see also Grant Thornton II*, 694 F. Supp. 2d at 514.

Grant Thornton accepted the district court's invitation to assert its direct claims against Kutak in a separate litigation, filing the complaint in this action. *See* Complaint of Grant

Thornton LLP (entered Feb. 10, 2004) ("Complaint"). The complaint does not assert contribution claims, but alleges three direct claims: fraud, negligent misrepresentation, and tortious interference with contract. *See id.* ¶¶ 109-125. The complaint seeks monetary damages "to compensate Grant Thornton for the expenses and costs ... resulting from Grant Thornton's being required to defend against claims in Keystone-related litigation," including the attorney's fees expended in defending such claims and the amount of any final judgment. *See id.* at Prayer for Relief ¶ A.[12]

After extensive fact and expert discovery, Kutak moved for summary judgment. In its motion, Kutak argued that Grant Thornton's direct claims were "really . . . claims for contribution," Kutak Summ. J. Mem. at 6, and that, as such, they were barred by Kutak's good faith settlement with the FDIC, *see id.* at 6-9. Kutak also argued that Grant Thornton's claims were barred by the statute of limitations, *see id.* at 10-15, and by principles of collateral estoppels, *see id.* at 15-20. Finally, Kutak argued that it had no duty to disclose confidential client information to Grant Thornton under either the West Virginia Rules of Professional Conduct or common law. *See id.* at 20-28. In Kutak's reply to Grant Thornton's response to its summary judgment motion, Kutak for the first time raised the additional argument that proximate cause principles and the "tort of another" doctrine barred Grant Thornton from recovering its collateral litigation expenses.

On March 11, 2010, the Circuit Court granted Kutak's motion for summary judgment. The court rejected Kutak's collateral estoppel and statute-of-limitations arguments, holding that

[12] Although Grant Thornton's complaint initially also sought damages for injury to its reputation, loss of goodwill, and disruption of its business, Grant Thornton no longer seeks to recover those damages. *See* Kutak Ex. 2.

the former argument was meritless and that the latter presented a jury issue. *See* Cir. Ct. Op. at 13. It also found "without merit" Kutak's argument that it owed no duty to disclose information concerning Keystone to Grant Thornton, noting that "the Bank is a common client of both Kutak and Grant Thornton, on common issues." *Id.* at 13-14. The Circuit Court nevertheless held that Grant Thornton's claims could not proceed because, although "characterize[d]" as direct claims, they were in reality contribution claims barred by Kutak's good faith settlement with the FDIC. *See id.* at 6-10. The court also held, in the alternative, that "[t]o the extent Grant Thornton seeks to recover its alleged damages through a claim of implied indemnity against Kutak, such claim is unsupported by West Virginia law and barred by the District Court's finding of wrongdoing and its judgment against Grant Thornton in [*Grant Thornton I*]." *Id.* at 10. Finally, the court concluded that, "[t]o the extent Grant Thornton seeks to recover the litigation expenses it has incurred in the Federal Litigation, no West Virginia authority permits recovery of such collateral litigation expenses, voluntarily incurred, by an adjudicated wrongdoer." *Id.* at 11.

ASSIGNMENTS OF ERROR

The Circuit Court committed error by:

I. Construing Grant Thornton's claims for fraud, negligent misrepresentation, and tortious interference with contract as claims for contribution (or perhaps indemnity), and dismissing those claims as barred by Kutak's settlement with the FDIC and the district court's finding in *Grant Thornton I* that Grant Thornton was negligent in performing the Keystone audit; and

II. Ruling that Grant Thornton cannot recover its collateral litigation expenses as a matter of law because Grant Thornton was not without fault in incurring those expenses, and had incurred the expenses "voluntarily."

REASONS FOR GRANTING THE PETITION

"A circuit court's entry of summary judgment is reviewed" by this Court "de novo." *Painter*, 451 S.E.2d at 758. In conducting that review, this Court "appl[ies] the same standard for granting summary judgment that is applied by the circuit court." *Merrill v. W. Va. Dep't of Health & Human Res.*, 632 S.E.2d 307, 311 (W. Va. 2006) (per curiam). "Under that standard, '[a] motion for summary judgment should be granted only when it is clear that there is no genuine issue of fact to be tried and inquiry concerning the facts is not desirable to clarify the application of the law.'" *Id.* (quoting *Painter*, 451 S.E.2d at 758 (internal quotation marks omitted)). "In other words, '[s]ummary judgment is appropriate where the record taken as a whole could not lead a rational trier of fact to find for the nonmoving party, such as where the nonmoving party has failed to make a sufficient showing on an essential element of the case that it has the burden to prove.'" *Id.* (quoting *Painter*, 451 S.E.2d at 759). "[T]his Court will reverse summary judgment if [it] find[s], after reviewing the entire record, a genuine issue of material fact exists or if the moving party is not entitled to judgment as a matter of law. In cases of substantial doubt, the safer course of action is to deny the motion and to proceed to trial." *Williams v. Precision Coil, Inc.*, 459 S.E.2d 329, 336 (W. Va. 1995).

I. THE CIRCUIT COURT ERRED IN CONCLUDING THAT GRANT THORNTON'S DIRECT CLAIMS ARE EQUIVALENT TO CLAIMS FOR CONTRIBUTION OR PERHAPS INDEMNITY, AND ARE BARRED UNDER WEST VIRGINIA LAW

The Circuit Court acknowledged that Grant Thornton was "attempt[ing] to characterize its claim[s] in this suit as . . . 'direct claim[s],'" Cir. Ct. Op. at 8-9, but nonetheless recast them as claims for contribution or indemnity. This was error. Grant Thornton's claims have different elements than contribution or indemnity claims, and in particular, are premised on the contention that Kutak breached duties that it owed to Grant Thornton, not to the FDIC. Indeed, the claims do not depend on any showing that Kutak breached duties owed to the FDIC. This Court's intervention is necessary to make clear (i) the crucial distinction between such direct claims and claims for contribution or indemnity, and (ii) that a settlement by one joint tortfeasor with a common plaintiff does not preclude the assertion of such direct claims by (or against) another joint tortfeasor. Accordingly, this Court should grant this petition, and reverse the Circuit Court's order granting Kutak's motion for summary judgment.

A. *Grant Thornton's claims are direct claims, not claims for contribution or indemnity*

Claims for contribution and indemnity allow for the distribution of loss among parties jointly held liable for injury to a third party. Although both legal concepts are rooted in equitable principles, they are "separate and distinct": indemnity must be brought by a person without fault, while contribution is a remedy for joint tortfeasors who share fault. *Dunn v. Kanawha Cnty. Bd. of Educ.*, 459 S.E.2d 151, 155-57 (W. Va. 1995); *see also Sydenstricker v. Unipunch Prods., Inc.*, 288 S.E.2d 511 (W. Va. 1982).

West Virginia law recognizes a clear—and legally significant—difference between contribution and indemnity claims, and direct claims based on breaches of independent legal obligations. The crux of a claim for either contribution or indemnity is the breach of a duty to a third party. *See Dunn*, 459 S.E.2d at 155 ("The idea of indemnity implies a primary or basic liability in one person, though a second person is also for some reason liable with the first, or even without the first, to a third person.") (internal quotation marks omitted); *see also Charleston Area Med. Ctr., Inc. v. Parke-Davis*, 614 S.E.2d 15, 22 (W. Va. 2005) ("Integral to any recovery in contribution is a common obligation owed to an injured party by multiple tortfeasors."); *Sydenstricker*, 288 S.E.2d at 518 (contribution is a "derivative" right, "in the sense that it may be brought by a joint tortfeasor on any theory of liability that could have been asserted by the injured plaintiff"). By contrast, to paraphrase the U.S. District Court for the Northern District of Illinois, the "gist" of Grant Thornton's direct claims "is not that it is more equitable that [Kutak] pay" for the FDIC's damages, "but that [Kutak] has committed a tort on [Grant Thornton], and must pay damages for this." *In re Cenco Inc. Sec. Litig.*, 642 F. Supp. 539, 542 (N.D. Ill. 1986).

The elements of Grant Thornton's claims demonstrate the point. "To prevail on a claim for [fraud or] misrepresentation, a plaintiff must establish [1] that 'the act claimed to be [wrongful] was the act of the defendant . . .[;] (2) that it was material and false; [3] that plaintiff relied on it and was justified under the circumstances in relying upon it; and [4] that he was damaged because he relied on it.'" *Jennings v. Farmers Mut. Ins. Co.*, 687 S.E.2d 574, 579 (W. Va. 2009) (per curiam) (quoting Syl. Pt. 1, *Lengyel v. Lint*, 280 S.E.2d 66 (W. Va. 1981); emphasis omitted); *see also Kidd v. Mull*, 595 S.E.2d 308, 313 (W. Va. 2004). "To establish prima facie proof of tortious interference, a plaintiff must show: (1) existence of a contractual . . . relationship . . .; (2) an intentional act of interference by a party outside that relationship . . .; (3) proof that the interference caused the harm sustained; and (4) damages." Syl. Pt. 2, *Torbett v. Wheeling Dollar Sav. & Trust Co.*, 314 S.E.2d 166 (W. Va. 1983). None of these claims can be established merely by showing that Kutak injured the FDIC (or any other third party); all require some showing that Kutak wrongfully injured Grant Thornton directly.

Courts in a number of jurisdictions have recognized the importance of the fundamental difference between direct claims, and derivative claims for contribution or indemnity, in contexts such as this one. *See, e.g., Cenco Inc. v. Seidman & Seidman*, 686 F.2d 449, 457-58 (7th Cir. 1982) (Posner, J.) (party's claim not one for indemnity because "indemnity is a remedy of one wrongdoer against another," while "[party's] claim is that it was a victim rather than a wrongdoer"); *In re Cendant Corp. Sec. Litig.*, 166 F. Supp. 2d 1, 9 (D.N.J. 2001) ("The right to contribution does not depend upon proof that one tortfeasor has directly harmed another; [but rather] it merely requires proof that both are liable to a plaintiff and one paid more than his or her fair share of the damages."); *In re Sunrise Sec. Litig.*, 793 F. Supp. 1306, 1321 (E.D. Pa. 1992) (state law claims were not claims for indemnity where "based upon duties" owed between defendants, not to plaintiff, and where based on allegation of "direct[] wrong[]" from one defendant to another); *In re Cenco Inc.*, 642 F. Supp. at 542 ("Recovery by indemnity between two defendants who have allegedly committed a tort on a third person is not the same thing as recovering because one defendant also committed a tort on the other[.]") (emphasis omitted).

The difference is more than semantic, moreover, because direct claims and derivative claims carry different implications. *See* Restatement (Second) of Torts § 886B, cmt. c (1979) (observing that "[t]here are different implications" to an indemnity action and "an action of tort [by an indemnitee] against the indemnitor, irrespective of a right of indemnity"). Grant Thornton's "claims are each grounded in separate theories which require proof of different elements than does a simple claim for contribution" or indemnity. *In re Cendant Corp. Sec. Litig.*, 166 F. Supp. 2d at 10. Although Kutak plainly breached its duties to Keystone in connection with the Bank's failure, *see* supra pp. 7-10, that breach is not an element of Grant

Thornton's claims. Rather, Grant Thornton must prove something entirely different: the breach of independent duties that Kutak owed to Grant Thornton.[13]

In seeking summary judgment, a defendant must demonstrate the absence of any genuine issues of fact regarding the elements of the claims pled by the plaintiff. *See Merrill*, 632 S.E.2d at 311. But Kutak never could have succeeded in an overt attack on the merits of Grant Thornton's fraud and other direct claims. To the contrary, the evidence shows that Kutak knowingly misrepresented to Grant Thornton the honesty of Keystone's management, the accuracy of information provided by Keystone's management regarding the value of the Bank's residuals, and the existence of "unasserted possible claims" that Kutak was required to disclose. *See* supra pp. 11-13. The evidence also shows that a Kutak attorney, Mr. Lambert, acquiesced in a critical material misstatement made by Keystone's management to the auditors, in his presence, regarding the value of Keystone loans transferred among servicers, even though contemporaneous evidence shows that he knew that the stated value was grossly overinflated. *See* supra pp. 13-14. And the evidence further shows that Kutak failed to disclose to the Grant Thornton auditors relevant, material information on a host of subjects that would have revealed

[13] An analogy can be found in the way courts have treated claims for breach of contract and tort that are based on identical operative facts and involve overlapping damages. If conduct breaches both an independent legal duty and an enforceable agreement, then a plaintiff may recover in tort as well as in contract, and may recover in tort even if the breach of contract claim is barred for some reason. *See Hargrave v. Oki Nursery, Inc.*, 636 F.2d 897, 899 (2d Cir. 1980); *In re Cendant*, 166 F. Supp. 2d at 12 (observing that if the statute of limitations precluded a breach of contract claim, recovery of the same damages "under . . . independent tort theories" would "not automatically [be] bar[red]"). And if the plaintiff has alleged and can prove all of the independent elements of a tort claim, it is not for the court to determine that the tort claim is in reality a breach of contract claim. *See Lehman v. Dow Jones & Co.*, 783 F.2d 285, 295 (2d Cir. 1986) ("We must therefore inquire whether the complaint pleaded the essential elements of an action for fraud distinct from an action for breach of contract and, if so, whether any triable issues of fact survived the papers on [defendant's] motion for summary judgment."); *cf. Hargrave*, 636 F.2d at 899 (noting that because "complaint sets forth all the elements of an action in tort for fraudulent representations," it states a claim for fraud regardless whether there is also an enforceable agreement).

the Keystone fraud. *See* supra p. 15. Information known to Kutak, but not disclosed to Grant Thornton, included: (i) the existence of significant conflicts of interest between the Bank and its servicers, (ii) the poor performance of the Bank's securitizations, (iii) the perilous state of the Bank's balance sheet (indeed, the Bank's insolvency), (iv) repeated violations of banking regulations and criminal prohibitions by the Bank's management, and (v) the Bank CFO's statement that he was unqualified for the job. *See* supra pp. 8-9.

This evidence is more than adequate to allow Grant Thornton's direct claims to go to a jury. Indeed, the Circuit Court ***rejected*** Kutak's sole argument going to the merits of those claims—namely, that it owed Grant Thornton no duty to disclose information concerning Keystone. *See* Cir. Ct. Op. at 13-14.

Only by recasting Grant Thornton's claims as ones for contribution—and perhaps indemnity—did the Circuit Court find a basis for dismissing them. But "[i]n the law, 'recovery under principles of contribution or indemnity' is, quite simply, a different animal from 'recovery under principles of direct tort liability.'" *In re Cenco Inc.*, 642 F. Supp. at 541. The Circuit Court should have considered Grant Thornton's claims on their own terms. This Court's intervention is warranted to correct the error.

B. West Virginia's rule relieving a joint tortfeasor that has settled with the plaintiff in good faith from liability for contribution does not bar Grant Thornton's direct claims

Insisting that Grant Thornton's claims were "in fact" contribution claims, the district court found them "barred by Kutak's good faith settlement with the FDIC." Cir. Ct. Op. at 9. The direct claims at issue here, however, are not subject to West Virginia's contribution bar. The Circuit Court's erroneous holding to the contrary warrants review.

1. **This Court's precedents indicate that the Circuit Court erred in applying the contribution bar to Grant Thornton's claims**

In *Zando,* this Court held that "a nonsettling defendant's right of contribution from a joint wrongdoer is extinguished by the plaintiff's [good faith] settlement with and release of such wrongdoer prior to verdict." 390 S.E.2d at 804. It observed that such a bar to recovery (henceforth, the "contribution bar") was complementary to the established West Virginia "practice of allowing the defendant against whom a verdict is rendered to reduce the damages to reflect any partial settlement the plaintiff has obtained from a joint tortfeasor." *Id.* at 803. Grant Thornton is aware of no West Virginia precedent so much as hinting that the contribution bar also applies to claims not pled as contribution claims. Indeed, in at least two cases, this Court has declined to adopt such an approach.

The first case is *Jennings*, in which this Court considered claims arising from the alleged mishandling by Farmers Mutual Insurance Company ("Farmers Mutual") and one of its agents of a gas station owner's insurance application and claim. *See* 687 S.E.2d at 576-77. The policyholder, Jennings, sued Farmers Mutual and the agent for tort and contract damages; Farmers Mutual cross-claimed against the agent for misrepresentation, contribution, and indemnity, and then settled with Jennings for $500,000. *See id.* at 577.

This Court upheld the lower court's dismissal on summary judgment of all of Farmers Mutual's cross-claims, ruling that the contribution claim had been extinguished by the settlement between Farmers Mutual and Jennings, and that the misrepresentation claim failed because Farmers Mutual had not shown detrimental reliance on the agent's statements. *See Jennings*, 687

S.E.2d at 577-80.[14] Significantly, the Court did not suggest that the settlement precluded the assertion of the misrepresentation claim, which—like the contribution and indemnity claims—was predicated on the agent's alleged misconduct in completing and handling Jennings's application. *See* Defendant, Farmers Mutual Insurance Company's Answer to Plaintiff's Complaint, *Jennings v. Farmers Mutual Ins. Co.*, Civ. A. No. 02-C-373, at 18-19 (Cir. Ct. Monongalia Cnty., Div. 1, May 22, 2008) ("Farmers Mutual Answer") (attached as App. Ex. B). Indeed, the agent did not even raise such an argument. Rather, the Court analyzed the merits of the misrepresentation claim, implying that it could have proceeded had Farmers Mutual been able to show reliance. *See Jennings,* 687 S.E.2d at 579 ("Farmers Mutual has offered no evidence suggesting that the representations contained in Ms. Jennings' application contributed to the 'formation of the conclusion' in the underwriter's mind that the insurance policy should be issued.").

The second case is *Dunn*, in which this Court "consider[ed] whether a good faith settlement between a plaintiff and a defendant in a multiparty lawsuit extinguishes the rights of non-settling defendants to seek indemnification from the settling defendant." 459 S.E.2d at 154. The Court concluded that such indemnity claims were not extinguished "when the liability of the non-settling defendant is predicated not on its own independent fault or negligence, but on a theory of strict liability." *Id.* at 158. It reasoned that "[t]o argue that both contribution and implied indemnity claims should be extinguished by a good faith settlement is to ignore the substantive differences between the two [types of claims]." *Id.* at 157. Because of these

[14] The Court did not address the indemnity claim, presumably because Farmers Mutual declined to appeal the circuit court's ruling dismissing it.

substantive differences, the court stated that it was "pointless" to rely upon cases applying the contribution bar to contribution claims as "precedent" for applying the bar to indemnity claims. *Id.*

The fundamental principle invoked in *Dunn*—that effect must be given to the substantive difference between contribution and other types of claims, and to the pleader's choice of which claim to assert—applies fully here. Because Grant Thornton's direct claims are "separate and distinct legal concepts" from contribution claims, *Dunn*, 459 S.E.2d at 155, they are not subject to the contribution bar.

In reaching the contrary conclusion, the Circuit Court did not discuss *Jennings* or *Dunn*. Instead, it misused *Zando* and *Charleston Area Medical Center* for the proposition that West Virginia's contribution bar applies not only to contribution claims, but also to direct claims properly pled as such. *See* Cir. Ct. Op. at 6 ("where the acts of various parties have resulted in a single, indivisible injury, a good faith settlement bars contribution claims against the settling party," "regardless of different theories of liability") (citing *Zando*, 390 S.E.2d at 803); *see also id.* at 9 (the existence of "a common obligation or liability to a third party" gives rise to "a right of contribution . . . that is extinguished by a good faith settlement," "whatever the theory of liability") (citing *Charleston Area Med. Ctr., Inc.*, 614 S.E.2d at 23). The Circuit Court's reliance on these cases was misplaced because they concern claims unquestionably pled as claims for contribution. And while this Court stated in *Zando* that there is "but one loss" "regardless of the different theories [of liability] and parties pursued by the ***plaintiff***," 390 S.E.2d at 808 (emphasis added); *see also id.* at 807, it never suggested that the contribution bar applies regardless of the theory of liability pursued ***by one joint tortfeasor against another***.

Thus, in dismissing Grant Thornton's claims, the Circuit Court misinterpreted and misapplied this Court's precedents regarding the contribution bar. This Court has in the past exercised its review authority to ensure that the lower courts apply that bar properly, and it should do the same here.

2. Precedents from other jurisdictions likewise demonstrate that the Circuit Court should not have applied the contribution bar to Grant Thornton's claims

This Court's practice in *Jennings* and *Dunn* of treating non-contribution claims as unaffected by the contribution bar is consistent with decisions by other jurisdictions. For example, in *Liberty Seafood, Inc. v. Herndon Marine Products, Inc.*, 38 F.3d 755 (5th Cir. 1994), the U.S. Court of Appeals for the Fifth Circuit considered whether that Circuit's "general rule against claims for contribution by non-settling tortfeasors against settling tortfeasors" applied where a non-settling tortfeasor had asserted a "distinct," independent claim against a settling joint tortfeasor. *Id.* at 757-58. Both tortfeasors were shipowners whose vessels had been involved in an accident resulting in injury to the plaintiff seamen. The seamen's employer paid them "maintenance and cure," and then sought reimbursement for those payments from the other shipowner, which had settled with the seamen on their damages claims.[15] Maritime law provides that "[t]he seaman may claim maintenance and cure only from its employer; but . . . the employer may recover all, or a portion of those payments from a third-party tortfeasor." *Id.* at 758.

[15] "Maintenance and cure is a seaman's right under general maritime law to receive a 'per diem living allowance for food and lodging [maintenance] and . . . payment for medical, therapeutic and hospital expenses [cure].'" *Bertram v. Freeport McMoran, Inc.*, 35 F.3d 1008, 1011 (5th Cir. 1994) (quoting Black's Law Dictionary 954 (6th ed. 1991)). "A shipowner must pay maintenance and cure to any seaman who 'becomes ill or suffers an injury while in the service of a vessel,' regardless of whether either party was negligent." *Id.* (quoting 1B Ellen M. Flynn *et al.*, Benedict on Admiralty § 42, at 4-5 (7th ed. 1993)).

Adhering to circuit precedent, the Fifth Circuit held that the settlement did not bar the reimbursement claim. *See Liberty Seafood*, 38 F.3d at 757 (following *Bertram v. Freeport McMoran, Inc.*, 35 F.3d 1008 (5th Cir. 1994)). The court explained that reimbursement for "maintenance and cure" and reimbursement for damages represent two "distinct claims," and that a settlement between a third-party shipowner and an injured seaman will not bar the employer's maintenance and cure claim, even when both claims stem from exactly the same incident. *Id.* at 758. As the court had explained in *Bertram*, "[a claim for] reimbursement of maintenance and cure . . . is not a derivative right through [the seaman], but [i]s a separate and distinct cause of action." 35 F.3d at 1015 (internal quotation marks omitted). The *Bertram* court also noted as a matter of legal principle that a settlement between a seaman and a defendant could not "release one defendant from an independent claim asserted by another." *Id.* at 1016. Applying similar reasoning, the U.S. Court of Appeals for the Ninth Circuit reached the same conclusion in *United States v. Tug Manzanillo*, 310 F.2d 220, 222 (9th Cir. 1962).

These cases demonstrate clearly how the Circuit Court's application of West Virginia's contribution bar to the "separate and distinct cause[s] of action," *Bertram*, 35 F.3d at 1015, asserted by Grant Thornton in this case violates fundamental legal principles. In *Tug Manzanillo*, the Ninth Circuit explained the error as follows: "To hold that by paying certain sums to [a plaintiff] . . . [a tortfeasor] had thereby discharged its then existing liability to [a third-party], is a wholly impermissible conclusion. If A is indebted to B he cannot discharge that indebtedness by payment to C." 310 F.2d at 222. Similarly, Kutak should not be able to discharge its independent liability on Grant Thornton's direct claims by settling with the FDIC.

In re Cendant, 166 F. Supp. 2d 1, also contradicts the Circuit Court's approach. There, the U.S. District Court for the District of New Jersey considered whether the bar on contribution imposed by the Private Securities Litigation Reform Act of 1995 ("PSLRA"), Pub. L. No. 104-67, 109 Stat. 737 (1995), precluded a defendant company from bringing independent state law tort claims against its co-defendant auditor, where both the company and the auditor had settled with the plaintiff class. *See* 15 U.S.C. § 78u-4(f)(7)(A) (providing that "a covered person who settles any private action at any time before final verdict or judgment shall be discharged from all claims for contribution brought by other persons"). The court ruled that the bar did not apply to such independent claims, declining to "read such a requirement" into the PSLRA "[i]n the absence of any statutory language or legislative history which would indicate an intent to codify a requirement that independent state law claims be barred in addition to contribution claims." *In re Cendant*, 166 F. Supp. 2d at 6. As the court explained, "'[r]ecovery by contribution between two defendants who have allegedly committed a tort on a third person is not the same thing as recovering because one defendant also committed a tort on the other.'" *Id.* at 10-11 (quoting *In Cenco Inc.,* 642 F. Supp. at 542) (alterations omitted); *see also In re Cenco Inc.*, 642 F. Supp. at 541 ("Waiver of [a contribution or indemnity claim] is not necessarily waiver of [a direct claim].").

3. The overlap between the damages that Grant Thornton seeks in this case and the judgment in *Grant Thornton I* does not transform Grant Thornton's claims into barred contribution claims

In holding that Grant Thornton's direct claims were in reality contribution claims, the Circuit Court reasoned that Grant Thornton "seeks to recover the same, indivisible damages from Kutak for which it was awarded a set-off"—namely, the amount of the district court's judgment in *Grant Thornton I.* Cir. Ct. Op. at 8. The reduction of Grant Thornton's liability to the FDIC to reflect the amount of the Kutak-FDIC settlement does not justify the preclusion of Grant Thornton's direct claims against Kutak.

West Virginia allows "the defendant against whom a verdict is rendered to reduce the damages to reflect any partial settlement the plaintiff has obtained from a joint tortfeasor." *Zando*, 390 S.E.2d at 803. The settlement-credit rule "is premised on the principle that a plaintiff is entitled to one, but only one, complete satisfaction for his injury," and also "counterbalances the loss of the right of contribution." *Id.* at 803-04. Verdict reduction thus is a (partial) substitute for contribution: "The settling defendant is, in effect, paying a share of liability on the verdict," reducing what the non-settling defendant must pay to make the plaintiff whole. *Id.* at 804.

Here, the relatively small amount of the settlement credit reflected the district court's conclusion that Kutak's settlement with the FDIC covered not only the damages that Kutak and Grant Thornton jointly caused Keystone, but also the much greater damages for which Kutak alone was potentially responsible. The credit substituted (imperfectly) for Grant Thornton's right to seek contribution from Kutak for the damages that they jointly inflicted on the Bank. But the credit could not substitute for Grant Thornton's direct claims, which seek compensation for harms that Kutak caused Grant Thornton. *See In re Masters Mates & Pilot Pension Plan*, 957 F.2d 1020, 1033 (2d Cir. 1992) ("[A]lthough judgment reduction compensates a nonsettling defendant for his lost rights of indemnity and contribution, it does not necessarily compensate him for other lost claims."). Put another way, the fact that "Grant Thornton and Kutak Rock caused a single, indivisible loss to the bank," GT Ex. F at 3, does not preclude a subsequent finding that Kutak caused a distinct injury to Grant Thornton for which it may recover.

To be sure, Grant Thornton seeks in this suit to recover damages that include the amount of any final judgment paid to the FDIC, and part of that amount also might have been recoverable through an action for contribution, were such an action available. But while "[i]t is not uncommon for two different causes of action"—such as causes of action in contract and tort—"to provide the same recovery," *In re Cendant*, 166 F. Supp. 2d at 12, that overlap has never been understood to prevent a party from pursuing both claims. *See Hargrave v. Oko Nursery, Inc.*, 646 F.2d 897, 900 (2d Cir. 1980) (in case involving overlapping tort and contract claims, noting that "[o]ne immediate and direct 'injury' [defendant's] alleged tortious misrepresentations caused to plaintiffs was the loss of the money paid by them [pursuant to their contract]"). Because Grant Thornton's claims are distinct from claims for contribution (or indemnity), the nature of the damages sought does not affect the viability of those claims. *See Cendant*, 166 F. Supp. 2d at 12 ("[T]his Court does not believe that because Cendant might have plead [sic] a contribution claim—which it did, and which was dismissed—the damages sought automatically convert the state law claims into impermissible contribution claims.").

Nor will Grant Thornton, even if it ultimately proves Kutak's liability in this case, necessarily recover the entire amount of its own liability to the FDIC. Grant Thornton's actual recovery will depend on its ability to demonstrate to a jury that particular losses were a "natural" and "proximate" consequence of Kutak's breach of its duties to Grant Thornton. *Thomason v. Mosrie,* 60 S.E.2d 699, 706-07 (W. Va. 1950). That is a very different standard than the one the district court applied in determining the amount of the settlement credit. There, it analyzed the scope of Kutak's liability to the FDIC and decided what portion of the settlement should be allocated to the damages for which Kutak and Grant Thornton were jointly responsible.

Consistent with this analysis, a number of jurisdictions have rejected the notion that direct claims may be recharacterized as contribution claims if they seek compensation for damages paid to a third party. In *Cenco Inc.*, 686 F.2d 449, for example, the U.S. Court of Appeals for the Seventh Circuit ruled that a defendant auditor that had settled with the plaintiffs in a securities class action could pursue direct state law claims against its co-defendant—its former client—for damages that consisted solely of the settlement amount, despite the unavailability of a claim for contribution or indemnity. *See id.* at 457-58. The court stated that "if [the auditor] can prove that [the client] defrauded it into issuing false audit reports which in turn exposed it to liability to the class plaintiffs, the amount it paid to settle with the class would be a permissible item of damages." *Id.* at 458.[16] And in *Bertram*, the Fifth Circuit did not express concern over the employer shipowner's recovery of the entire amount of the maintenance and cure payment as reimbursement, even though that recovery apparently overlapped with the settling shipowner's payment to the plaintiff pursuant to their settlement. *See Bertram*, 35 F.3d at 1017 n.5. The overlap simply did not affect the status of the reimbursement claim as "separate and distinct" from a damages claim for contribution or indemnity. *Id.* at 1015. *See also In re Cendant*, 166 F. Supp. 2d at 11 (holding that fact that

[16] *See also In re Cenco Inc.*, 642 F. Supp. at 542 (holding that fact that portion of damages sought by co-defendant on independent claims—namely, the settlement amount paid to the plaintiffs—"overlaps what [co-defendant] maybe could have recovered through indemnity does not make it indemnity") (emphasis and internal quotation marks omitted); *In re Cenco Inc. Sec. Litig.*, 601 F. Supp. 336, 341-42 (N.D.Ill. 1985) ("The real proximate cause issue is not whether [the auditor] voluntarily settled, but whether [the client's] fraud was a cause of [the auditor's] potential liability to the class. If so, [the auditor's] settlement payment follows from that exposure and can be recoverable . . . .").

defendant "might have asserted a contribution claim to recover the same damages [from a co-defendant] does not convert its state law claims into contribution claims, so long as there is an independent basis for direct liability and the damages are a reasonably foreseeable consequence of the breach(es) of duty alleged"); *In re Sunrise Sec. Litig.*, 793 F. Supp. at 1321 (although "[t]he damages that the non-settling defendants seek for their tort and contract claims are similar, although not identical to the damages that they seek for their indemnification claims[, s]uch an overlap does not necessarily transform the claims into claims for implied indemnity").

Moreover, in *Jennings*, 687 S.E.2d 574, Farmers Mutual's misrepresentation claim sought recovery of all damages "suffered" "[a]s a direct and proximate result of [the agent's] negligence, carelessness, fault and wrongful conduct." Farmers Mutual Answer at 19 ¶ 16. This measure of damages might well have encompassed the amount of Farmers Mutual's settlement with Jennings, and this Court did not suggest that such an overlap would be relevant to the viability of the claim.

Finally, it should be noted that the damages sought by Grant Thornton in this case, although encompassing its liability to the FDIC, are not identical to that liability. In addition to the amount of the judgment in *Grant Thornton I* (as reduced by the settlement credit), Grant Thornton also seeks recovery of the expenses it has incurred over the last decade of litigation stemming from the collapse of Keystone. Grant Thornton's claim of additional damages further demonstrates the error in the Circuit Court's reasoning and the need for this Court's intervention. *See In re Cendant*, 166 F. Supp. 2d at 11 (noting that cross-claimant "also seeks damages" against its co-defendant "beyond recovery of a portion of the [settlement amount]").

4. **The district court's finding in *Grant Thornton I* that Grant Thornton was negligently responsible for some of Keystone's losses does not justify treating Grant Thornton's claims as subject to the contribution bar**

According to the Circuit Court, Grant Thornton's status as an "adjudicated wrongdoer" justified treating its claims as contribution claims barred by the Kutak settlement. Cir. Ct. Op. at 9; *see also id.* ("Regardless of Grant Thornton's characterizations, this action by a party with fault is, in fact, an action for contribution, and thus is barred by Kutak's good faith settlement with the FDIC."). But the district court's finding in *Grant Thornton I* that Grant Thornton was negligent in connection with the Keystone audit does not affect the nature or viability of its direct claims.

It is well-established in West Virginia (as elsewhere) that "[i]n the case of an intentional tort"—including fraud—"contributory negligence is not a defense." *Bradley v. Appalachian Power Co.*, 256 S.E.2d 879, 887 (W. Va. 1979); *see also Cenco*, 686 F.2d at 454 ("Negligence is not a defense to an intentional tort such as fraud."); Restatement (Second) of Torts § 481 (1965); Restatement (Second) of Torts § 545A (1977) (same). Indeed, it would be perverse if a fraudster could escape liability entirely because its victim acted negligently in connection with the fraud.

Grant Thornton I also does not affect the viability of Grant Thornton's claim for negligent misrepresentation. The rule in West Virginia is that "a party is not barred from recovering damages in a tort action so long as his negligence or fault does not equal or exceed the combined negligence or fault of the other parties involved in the accident." *Bradley*, 256 S.E.2d at 885. And "the issue of apportionment of negligence or causation is one for the jury or other trier of the facts, and only in the clearest of cases where the facts are undisputed and reasonable minds can draw but one inference from them should such issue be determined as a matter of law." *Reager v. Anderson*, 371 S.E.2d 619, 625 (W. Va. 1988). This is not such a case, and a jury should decide whether Grant Thornton's own negligence in connection with the Keystone audit should reduce its recovery on its claim for negligent misrepresentation.

Grant Thornton is not aware of any other court that has held that a claimant's own negligence transforms claims pled as direct claims into barred contribution claims. Indeed, several courts in other jurisdictions have rejected such an argument. In *Liberty Seafood*, for example, the Fifth Circuit allowed the employer shipowner to recover on its reimbursement claims even though it had been adjudged partially at fault for the accident. 38 F.3d at 758 ("[T]he partial fault of the shipowner does not preclude recovery for maintenance and cure from a joint tortfeasor for its portion of the fault."). And in *In re Cendant*, the district court squarely rejected the proposition that fault matters in holding that Cendant—a "tortfeasor," 166 F. Supp. 2d at 8 n.3—could bring its direct state law claims against its former auditor. *See id.* at 8-9.

The district court's ruling also runs counter to this Court's approach in *Jennings*. It is true that this Court did not indicate in its opinion whether the insurer admitted fault as part of the settlement with Jennings. But Farmers Mutual certainly was not exonerated, and indeed the lower court pointedly noted that Farmers Mutual did not press its claim for implied indemnity—a claim that would have been available had it been without fault. *See* Order, *Jennings,* Civ. A. No. 02-C-373, at 4 (emphasizing that "[o]ne of the requisite elements of implied indemnity is that the actions of the proposed indemnitee did not contribute to the injury," and that "[t]he real issue is whether Farmers is entitled to contribution from [the agent]") (attached as App. Ex. C).[17]

[17] The Circuit Court also held that, "[t]o the extent Grant Thornton seeks to recover its alleged damages through a claim of implied indemnity against Kutak, such claim is unsupported by West Virginia law and barred by the District Court's finding of wrongdoing and its judgment against Grant

C. Permitting Grant Thornton's claims to go forward furthers the public policy interests of West Virginia

The Circuit Court expressed concern that permitting Grant Thornton to assert its claims notwithstanding the Kutak settlement "would place a chilling effect on settlements, and settlements would cease to exist." Cir. Ct. Op. at 14. As the Fifth Circuit explained in *Liberty Seafood*, however, "once it is recognized that [the joint tortfeasor that settled] in fact had two separate grounds of liability to the [nonsettling tortfeasor], it becomes clear that settlement policy is not implicated." 38 F.3d at 759. The settled party "cannot extinguish its . . . liability [on a] . . . a separate and independent claim . . . by settling a separate and unrelated claim with the [plaintiff]." *Id.*

Moreover, the Circuit Court's approach raises multiple questions that may hamper settlements in future cases. Was the dispositive factor in the decision (i) the similarity of the conduct underlying the direct claims and hypothetical claims for contribution or indemnity, (ii) Grant Thornton's status as an "adjudicated wrongdoer," or (iii) the overlapping nature of the damages? The court does not say, and its opinion provides little guidance. By contrast, the

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Thornton in [*Grant Thornton I*]." Cir. Ct. Op. at 10. As explained above, *see* supra pp. 21-25, Grant Thornton has not asserted an indemnity claim in this suit; and for reasons similar to those discussed with respect to the contribution bar, the unavailability of indemnity is irrelevant to the viability of Grant Thornton's direct claims. As already noted, both the Fifth Circuit in *Liberty Seafood* and the District of New Jersey in *In re Cendant* held squarely that a tortfeasor need not be innocent of wrongdoing in order to bring independent claims against a joint tortfeasor, *see Liberty Seafood*, 38 F.3d at 758; *In re Cendant*, 166 F. Supp. 2d at 8-9, even though in neither case would the claimant have been able to pursue a claim for indemnity, *see Bertram*, 35 F.3d at 1015 (noting Fifth Circuit precedent holding that "the advent of proportional fault theories had limited the ability of a defendant who settled with the plaintiff after trial to recover, either through indemnity or contribution, from a defendant who had settled before trial"); *In re Cendant Corp. Sec. Litig.*, 139 F. Supp. 2d 585, 594 (D.N.J. 2001) (noting Cendant's acknowledgment that federal securities laws would bar claims for indemnity). As the court explained in *In re Cendant*, there is a dispositive "distinction between indemnity and the ability of a tortfeasor to recover independently against co-defendants under separate grounds." 166 F. Supp. 2d at 8 n.3.

straightforward approach of treating direct claims on their own terms not only better comports with precedent and logic, but also would provide certainty and guidance in future cases.

Indeed, contrary to the Circuit Court's fears, West Virginia's "strong public policy favoring out-of-court resolution of disputes," *Zando*, 390 S.E.2d at 804, "should be advanced" by this Court's application of a clear rule distinguishing between direct claims and claims for contribution or indemnity. *Liberty Seafood*, 38 F.3d at 759. In particular, such a rule would encourage tortfeasors to negotiate global settlements that resolve potential liability to co-defendants as well as the plaintiff.[18] Moreover, because West Virginia law also bars tortfeasors that have settled with a plaintiff from *bringing* contribution claims, *see Jennings*, 687 S.E.2d at 578, the Circuit Court's approach would discourage prompt settlement by tortfeasors who believe they may have viable direct claims against a joint tortfeasor. By contrast, if direct third-party claims are allowed to proceed notwithstanding settlement, early consideration of such claims should prompt all the parties involved "to work together to reach settlement of all claims, and thus avoid any further litigation." *Bertram*, 35 F.3d at 1017; *see also In re Cendant*, 166 F. Supp. 2d at 18 (had defendant "truly wanted to buy complete peace, it could have insisted that [co-defendant] agree to release [it] from any and all claims arising out of the action, including state law claims, however styled").

[18] In the vast majority if not all cases, such consideration of possible independent claims should not be unduly burdensome. Generally, as here, the universe of third parties that may have viable independent claims will be small; most tortfeasors who jointly cause an injury to a plaintiff do not owe each other any independent legal duties. For example, when party A injures party B in a car accident, and party C—a doctor—exacerbates the injury by his negligent treatment, the existence of an independent duty from A and C—and thus the assertion of direct claims by C against A—is extremely unlikely absent unusual circumstances. *See, e.g., Pennington v. Bluefield Orthopedics, P.C.*, 419 S.E.2d 8, 10-11 (W. Va. 1992) (presenting such facts).

Moreover, the public policy in favor of settlement is not the only policy consideration implicated here. The "underlying objectives of tort liability . . . are to compensate the victims of wrongdoing and to deter future wrongdoing." *Cenco*, 686 F.2d at 455. The ruling below fails to advance either objective. Extinguishing Grant Thornton's direct claims against Kutak based on Kutak's settlement with the FDIC is unfair to Grant Thornton, which was not involved in those negotiations and received no credit for the extinguishment of its direct claims, yet is entitled to legal compensation to the extent Kutak has harmed it directly.

The Circuit Court's approach, if allowed to stand, also would undermine deterrence by over-incentivizing tortfeasors to settle on the cheap with plaintiffs in order to divest joint tortfeasors of any direct claims. To be sure, West Virginia courts review settlements for good faith, and this Court has emphasized that "the good faith test carries inherent safeguards in view of the low probability that a plaintiff will enter into a nominal settlement with a solvent defendant whose liability is significant." *Smith*, 429 S.E.2d at 243. But West Virginia courts have not hitherto taken into account the value of direct third-party claims in determining whether a settlement is in "good faith." *See id.* at 651-52. Indeed, in this case, the district court (applying West Virginia law) expressly presumed that Grant Thornton's direct claims against Kutak survived the "good faith settlement," GT Ex. F at 3, 5. And a plaintiff has no reason to factor in the value of direct claims in calculating the settlement amount and terms. Accordingly, neither the plaintiff's vigilance in negotiating the settlement nor judicial review for "good faith" is likely to be effective in weeding out opportunistic behavior by defendants.

The Circuit Court's approach also would encourage unethical parties to engage in wrongful conduct in the first place. For example, taking the facts of this case, it would allow attorneys to dissemble with impunity to auditors involved in an engagement for a common client—so long as the attorneys settle with the client before the auditors' direct claims against them can be fully adjudicated. Thus, attorneys aware of a client's wrongdoing will have an additional incentive to continue hiding the facts from the auditor, including through direct misrepresentations—exactly as Kutak did in this case.

These important policy considerations, which the Circuit Court did not consider, further counsel in favor of this Court granting this petition.

II. THE CIRCUIT COURT ERRED IN RULING THAT GRANT THORNTON CANNOT RECOVER ITS COLLATERAL LITIGATION EXPENSES FROM KUTAK

The Circuit Court acknowledged that, "[u]nder the law of West Virginia and elsewhere, the costs and expenses incurred in collateral litigation may be recovered when they are the proximate result of another defendant's conduct." Cir. Ct. Op. at 11 (citing *Thomason*, 60 S.E.2d at 706). Nonetheless, the court concluded that Grant Thornton could not recover its expenses incurred in Keystone-related litigation because "Grant Thornton's own acts of wrongdoing, not Kutak, caused Grant Thornton to have to defend itself in the Federal Litigation brought against it," and "Grant Thornton voluntarily incurred the costs and attorneys' fees [it] now seeks to recover from Kutak." *Id.* at 11-12. This Court should correct this ruling for at least two reasons. First, the Circuit Court should not have even addressed this issue because it was not properly raised in Kutak's motion for summary judgment. And second, on the merits, the ruling misstated and misapplied West Virginia law and usurped the role of the jury.

To begin with, the recoverability of Grant Thornton's collateral litigation expenses was not properly before the Circuit Court because Kutak—the moving party—raised it for the first time in its ***reply*** memorandum in support of its motion for summary judgment. "Of course, a party seeking summary judgment always bears the initial responsibility of informing the district court of the basis for its motion." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986) (interpreting federal rules); *Williams*, 459 S.E.2d at 337 ("the initial burden of production and persuasion is upon the party moving for a summary judgment").[19] And as this Court has stated, "[w]hen a motion for summary judgment is mature for consideration and ***properly is documented with such clarity as to leave no room for controversy***, the nonmoving party must take the initiative and by affirmative evidence demonstrate that a genuine issue of fact exists." *Williams*, 459 S.E.2d at 335 (emphasis added). Kutak's reply memorandum argued that Kutak's fraud could not have proximately caused Grant Thornton's collateral litigation expenses, *see* Kutak Reply at 12-14, and in particular that "[t]he 'tort of another' doctrine does not allow recovery of prior litigation expenses by joint or successive tortfeasors or by one whose own wrongdoing caused or contributed to the harm." *Id.* at 13. Kutak's initial memorandum in support of its motion for summary judgment, however, did not in any way indicate that these arguments were a basis for that motion—even though Grant Thornton's complaint was clear that the damages it sought included "an award of reasonable attorneys' fees, costs and other expenses incurred by Grant Thornton in defending against claims in . . . litigation relating to the closure of Keystone." Complaint at Prayer for Relief ¶ A.[20]

[19] This Court has stated that "there should be no doubt that our interpretation of Rule 56 is consistent with that of the United States Supreme Court." *Williams*, 459 S.E.2d at 335 n.6.

[20] To the extent that Kutak's memorandum in support of its motion for summary judgment referenced Grant Thornton's claim for attorney's fees, it did so only in the context of Kutak's effort to characterize Grant Thornton's direct claims as claims for contribution. *See* Kutak Summ. J. Mem. at 7.

Although the West Virginia courts do not appear to have specifically addressed whether a moving party can use its reply brief to assert additional grounds for summary judgment, the numerous other jurisdictions to confront this question have held that it cannot.[21] Moreover, several of these courts have specifically held that it is improper—and reversible error—for a court to consider such a belated argument. *See Sartin,* 2009 WL 1076815; *Taggart,* 242 S.W.3d 755; *Truck Ins. Exchange*, 887 P.2d 455; *Canter*, 704 N.Y.S.2d 624; *see also Demmert*, 960 P.2d 606. "The function of a reply memorandum is to respond to the opposition to the primary motion, not to raise new issues or arguments." *Demmert,* 960 P.2d at 611. A contrary rule would be grossly unfair to the nonmoving party—which has no guaranteed right to respond to an argument raised for the first time in a reply brief, *see McDaniel,* 869 F.Supp. at 453; *Buren v. Karrington Health, Inc.*, 2002 WL 58930, at *6 (Ohio Ct. App. Jan. 17, 2002)—and would implicate due process concerns, *see San Diego Watercrafts, Inc. v. Wells Fargo Bank, N.A.*, 125 Cal. Rptr. 2d 499, 506 (Cal. Ct. App. 2002) ("Where a remedy as drastic as summary judgment is involved, due process requires a party be fully advised of the issues to be addressed and be given adequate notice of what facts it must rebut in order to prevail.").

On the merits, as this Court explained in *Thomason*, "[t]hough expenses of litigation and attorney fees incurred in a tort action for fraud generally are not recoverable, costs and expenses incurred in collateral litigation may be recovered when they are a proximate result of the fraud." 60 S.E.2d at 706 (citing 37 C.J.S. Fraud § 141e(2)); *see also* Restatement (Second) of Torts §

[21] *See, e.g., McDaniel v. Miss. Baptist Med. Ctr.*, 869 F.Supp. 445, 453 (S.D. Miss. 1994); *Demmert v. Kootznoowoo, Inc.*, 960 P.2d 606, 611 (Alaska 1998); *Sartin v. Beacon Maritime, Inc.*, 2009 WL 1076815, at *3 (Tex. Ct. App. Apr. 23, 2009); *Taggart v. Md. Cas. Co.*, 242 S.W.3d 755, 760 (Mo. Ct. App. 2008); *Canter v. E. Nassau Med. Group*, 704 N.Y.S.2d 624, 625-26 (N.Y. App. Div. 2000); *Westin Tucson Hotel Co. v. State Dep't of Revenue*, 936 P.2d 183, 187 (Ariz. Ct. App. 1997); *Truck Ins. Exch. of Farmers Ins. Group v. Century Indem. Co.*, 887 P.2d 455, 461 (Wash. Ct. App. 1995).

914(2) (1979). The vast majority of states recognize this principle, and apply the general rule—derived from the general measure of tort damages—that "[l]egal expenses incurred in defending litigation that foreseeably ensued as a result of the defendant's tort may properly be considered as damages proximately caused by the defendant's tortious conduct." 22 Am. Jur.2d *Damages* § 437. The evidence adduced by Grant Thornton in this case is sufficient to create a material issue of fact on whether Kutak's misconduct foreseeably caused the Keystone-related litigation. Instead of examining that evidence, however, the Circuit Court established a *per se* rule that a party may not recover collateral litigation expenses if it is not without fault, and has incurred the expenses "voluntarily." This holding is misguided for several reasons.

First, it is incorrect to characterize Grant Thornton's litigation expenses as "voluntary." Courts have noted that a party may be entitled to recover collateral litigation expenses even if it was a ***plaintiff*** in the prior litigation. *See Elijah v. Fender*, 674 P.2d 946, 951 (Colo. 1984) (en banc); *see also* Restatement (Second) of Torts § 914(2) (1979) ("tort of another" doctrine applies to the "bringing" of suits). That is certainly a far more "voluntary" posture than Grant Thornton's in the FDIC litigation. Grant Thornton did not choose to be sued by the FDIC, and it had a due process right to defend rather than settle the FDIC's claims. *Cf. Elijah*, 674 P.2d at 951 (noting that "[a] party may be placed in a position of having to bring suit as plaintiff to defend his rights"). Furthermore, the FDIC sought much greater damages from Grant Thornton than it ultimately recovered—meaning that Grant Thornton's decision to incur litigation costs almost certainly reduced its total losses. And although the district court ultimately held Grant Thornton liable for negligence, the court did not find that Grant Thornton acted recklessly—as the FDIC alleged. GT Ex. A ¶¶ 150-155.

Second, the Circuit Court repeatedly misstated West Virginia's proximate cause standard, incorrectly asserting that the expenses incurred in collateral litigation must be the "natural ***and*** necessary" consequence of the defendant's act in order to be recoverable. Cir. Ct. Op. at 11-12 (emphasis added). *Thomason* itself is clear, however, that litigation expenses are recoverable even if they are merely the "natural but not the necessary result of the facts alleged" (so long as the expenses are "specifically alleged," as they were here). 60 S.E.2d at 706. Most if not all jurisdictions apply a similar standard, *see, e.g.*, *Collins v. First Fin. Servs., Inc.*, 815 P.2d 411, 413-14 (Ariz. Ct. App. 1991) (expenditure of attorneys' fees must be a "foreseeable ***or*** necessary result of the tortious conduct") (emphasis added), which is consistent with the standard way of calculating tort damages in West Virginia. *See* syl. pt. 4, *McCoy v. Cohen*, 140 S.E.2d 427 (W. Va. 1965) ("One requisite of proximate cause is an act or an omission which a person of ordinary prudence could reasonably foresee might naturally or probably produce an injury, and the other requisite is that such act or omission did produce the injury."); *see also Sheetz, Inc. v. Bowles Rice McDavid Gaff & Love, PLLC*, 547 S.E.2d 256, 270 (W. Va. 2001) ("[I]f a first act of negligence sets off a chain of events or creates a situation ultimately resulting in injury, then such negligence may very well constitute the proximate cause of said injury, even if intervening negligence occurs.").

Third, we are unaware of any West Virginia precedent that has applied—or suggested the existence of—the *per se* rule adopted by the Circuit Court. Indeed, *Thomason* is to the contrary. The defendant in that case had fraudulently induced the plaintiffs to purchase from him a lease on property that had been terminated by the lessor's sale of the property. *See Thomason*, 60 S.E.2d at 701-02. After the plaintiffs bought the lease, the property's purchaser sued them for unlawful detainer and recovered a judgment for possession of the property and damages consisting of the rent during the period of the plaintiffs' unlawful occupancy. *See id.* at 702. The plaintiffs then sued the defendant, seeking damages that included the money they paid "for costs and attorneys fees in defense of the [detainer] action." *Id.* at 703. Although the plaintiffs did not know in purchasing the lease that the property had been sold and the lease terminated, they were at least partially at fault for their liability because, as the Court explained, "the basis of the action of unlawful detainer, in which judgment for possession of the property was rendered, was that [one of the plaintiffs] used the premises for an immoral or illegal purpose." *Id.* at 704. And there is no question that plaintiffs "voluntarily" incurred the fees, in the sense that they could have pursued a settlement with the purchaser, but instead determined to litigate the ownership question. Nonetheless, the Court held that "[t]he allegations in each count relating to damages to the plaintiffs in paying costs and attorney fees . . . constitute sufficient averments of special damages and render the declaration good on demurrer." *Id.* at 706.

Other jurisdictions also have rejected the proposition that a party with some fault cannot recover collateral litigation expenses. In *Collins*, for example, the Arizona Supreme Court rejected the application of just such a rule to claims for conversion brought by First Financial Services, Inc., the holder of a senior lien in a mobile home, against Chrysler First Credit Corporation, which had improperly purported to sell the home to a third party, Collins. *See Collins*, 815 P.2d at 412. The court held that First Financial was entitled to recover from Chrysler the reasonable attorneys' fees First Financial incurred in defending Collins's quiet title action, even though First Financial had lost that action, and also had "committed various errors in properly recording its lien." *Id.* Applying a proximate cause standard, *see id.* at 415, the court explained that "[t]he fact that First Financial did not prevail in the quiet title action does not affect its entitlement to attorneys' fees. *See* [*Elijah*, 674 P.2d at 951]. It was Chrysler's conversion of the mobile home that was the very cause of First Financial's defeat in the quiet title action." *Id.*; *cf. Elijah*, 674 P.2d at 951 ("It is also not mandatory that the party prevail in the earlier litigation.").[22] Here, likewise, Grant Thornton's contention is that Kutak's fraudulent conduct was the "very cause" of Grant Thornton's defeat in the FDIC action.

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[22] As the *Collins* court noted, cases that have indicated the existence of a *per se* rule barring recovery of collateral litigation expenses by parties with some fault have involved "claims for indemnity and contribution among joint tortfeasors," not direct claims. 815 P.2d at 414 (citing *Brochner v. W. Ins. Co.*, 724 P.2d 1293, 1300 (Colo. 1986) (en banc); *Conrad v. Suhr*, 274 N.W. 2d 571 (N.D. 1979)).

CONCLUSION

For the reasons discussed above, this Court should grant this Petition, reverse the Circuit Court's order granting Kutak's motion for summary judgment, and remand to the Circuit Court for further proceedings.

Respectfully submitted,

GRANT THORNTON LLP

Petitioner

BY COUNSEL:

John H. Tinney

John H. Tinney (WV Bar #3766)
John K. Cecil (WV Bar #9155)
The Tinney Law Firm, PLLC
222 Capitol Street, Ste. 500
Charleston, WV 25337-3752
(304) 720-3310

Stanley J. Parzen
Mayer Brown LLP
71 South Wacker Drive
Chicago, IL 60606
(312) 782-0600

Counsel for Grant Thornton LLP

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No. __________

IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

GRANT THORNTON LLP,

Plaintiff,

v. CIVIL ACTION NO. 04-C-33-M
(Judge Murensky)

KUTAK ROCK LLP,

Defendant.

CERTIFICATE OF SERVICE

I, John H. Tinney, counsel for Grant Thornton LLP, hereby certify that on the 29th day of December, 2010, **"Grant Thornton LLP's Petition for Appeal"** was served upon Defendant Kutak Rock LLP by hand delivery to counsel as follows:

David B. Thomas, Esq.
Stephanie D. Thacker, Esq.
Allen Guthrie McHugh & Thomas, PLLC
500 Lee Street, East, Ste. 800
P.O. Box 3394
Charleston, WV 25333-3394

John H. Tinney
John H. Tinney (WV Bar #3766)
John K. Cecil (WV Bar #9155)
The Tinney Law Firm, PLLC
222 Capitol Street, Ste. 500
Charleston, WV 25337-3752
(304) 720-3310

Stanley J. Parzen
Mayer Brown LLP
71 South Wacker Drive
Chicago, IL 60606
(312) 782-0600