

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF TENNESSEE
NASHVILLE DIVISION

**NATIONAL UNION FIRE INSURANCE
COMPANY OF PITTSBURGH, PA,**

Plaintiff,

v.

SMALL SMILES HOLDING CO., LLC,

Defendant.

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) **Civil Action No. 3:10-cv-00743**
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**MEMORANDUM OF LAW IN SUPPORT OF
PLAINTIFF/COUNTER-DEFENDANT
NATIONAL UNION FIRE INSURANCE COMPANY
OF PITTSBURGH, PA'S MOTION TO DISMISS
DEFENDANT/COUNTER-PLAINTIFF
SMALL SMILES HOLDING CO., LLC'S
COUNTERCLAIM PURSUANT TO FED. R. CIV. P. 12(B)(6)**

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Plaintiff/Counter-Defendant, National Union Fire Insurance Company of Pittsburgh, Pa. (“National Union”), by and through its attorneys, Bass, Berry & Sims, PLC and Sedgwick, Detert, Moran & Arnold LLP, hereby respectfully submits this memorandum of law in support of National Union’s motion to dismiss in its entirety the Counterclaim asserted by Defendant/Counter-Plaintiff, Small Smiles Holding Company, LLC (“SSHC”), for failure to state a claim upon which relief may be granted pursuant to FED. R. CIV. P. 12(b)(6).

PRELIMINARY STATEMENT

National Union’s motion to dismiss presents a simple question to this Court: can an insured (SSHC) sue its insurer (National Union) for having filed a good faith lawsuit seeking to rescind the insured’s policies even as the insurer is defending the insured in accordance with those policies pending this Court’s determination on whether the policies may be rescinded? The answer to that question is no. SSHC’s disagreement with National Union’s rescission action does not give rise to independent claims against National Union. National Union cannot be punished for seeking a judicial determination as to the validity of SSHC’s policies while dutifully continuing to defend SSHC in a number of actions under those policies. The proper means for SSHC to challenge National Union’s position is for the defendant to defend this rescission action on the merits. Further, allowing SSHC’s Counterclaim to proceed would not only be improper for the reasons set forth below, but would also have implications beyond the instant dispute, as this type of counterclaim would have a devastating chilling effect on insurers’ willingness to honor their policies while awaiting a judicial determination on whether they may rescind their policies. For all these reasons, SSHC’s Counterclaim should be dismissed.

In this Action, National Union seeks a declaration from the Court that it is entitled to rescind certain dental professional liability insurance policies it issued to SSHC (the “Policies”, as defined in greater detail below) based upon National Union’s good faith belief that, prior to the issuance of

each of the Policies, SSHC breached its duty to disclose to National Union (to which it was applying for the insurance) a multitude of known devastating facts about itself that were material to the risks insured and necessarily increased National Union's risk of loss under the Policies. Although not at issue in the instant motion, National Union, much to its surprise, only learned of SSHC's breach of its duty to disclose these crucial facts while investigating coverage as to a number of lawsuits that SSHC tendered under the Policies for a defense and indemnity.

In that regard, SSHC, which manages over 50 dental clinics operating in at least 22 states, is a defendant in several civil lawsuits around the country that are being brought by potentially tens of thousands of former patients of the clinics under SSHC's management who allege, *inter alia*, that medically unnecessary, excessive and painful dental procedures were performed by SSHC dentists and other professionals upon minor children in order to defraud the parents and guardians of the children and third-party payors. These lawsuits erupted after a wholly-owned subsidiary of SSHC (FORBA Holdings, LLC) and the dental clinics managed by SSHC entered into a highly-publicized settlement of over \$24 million with the United States of America, 22 states and relators in 3 *qui tam* actions, thereby resolving a multi-year Medicaid fraud investigation involving a number of federal and state agencies, including the United States Department of Justice.

Nevertheless, and despite the gravest concerns as to the extent of SSHC's breach of its duty to disclose, National Union continues to honor all obligations under the Policies and, subject to a full and complete reservation of rights thereunder, is affording a defense in each of the matters that SSHC tendered to National Union. To that end, National Union did not unilaterally rescind any of the Policies or deny coverage for claims that may otherwise be covered notwithstanding SSHC's failure to disclose. Rather, National Union appropriately reserved all rights under the Policies,

including, but not limited to its right to seek rescission as equitable relief, and later, commenced this Action seeking a judicial determination of its right to rescind the Policies.

In response to the filing of this Action, SSHC has interposed unsubstantiated, and bordering on frivolous, counterclaims alleging, without any factual support, that National Union separately violated both the Tennessee Consumer Protection Act (the “TCPA”) and Tennessee’s bad faith failure to pay statute instead of simply litigating the merits of National Union’s claim for rescission. However, neither claim is sufficiently pled and they plainly cannot survive National Union’s motion to dismiss under FED. R. CIV. P. 12(b)(6), insofar as SSHC’s counterclaims are not supported by any factual allegations, and at bottom, stem from its disagreement with National Union as to the merits of the rescission claim. As discussed below, SSHC’s disagreement as to the merits, however strenuous, simply cannot support its Counterclaim.

As to the TCPA cause of action asserted in Count I of SSHC’s Counterclaim, SSHC purports to cast National Union’s good faith act of applying for the appropriate judicial relief from the Court as an unfair or deceptive act or practice otherwise prohibited under the statute. However, SSHC’s claim must fail because SSHC does not allege each of the necessary elements in support of a TCPA violation, namely: 1) an unfair or deceptive act or practice; and 2) how the unfair or deceptive act or practice caused an ascertainable loss.

As to the statutory bad faith claim asserted in Count II of SSHC’s Counterclaim, SSHC generally alleges that National Union’s good faith act of seeking appropriate judicial relief from the Court violated the statute, but fails to plead each and every necessary element thereunder, namely that: 1) the Policies are due and payable; 2) a formal demand for payment threatening litigation for bad faith failure to pay was made; 3) 60 days elapsed after making the formal demand before filing suit (unless there was a refusal to pay prior to the expiration of the 60 days); and 4) the alleged

refusal to pay was not in good faith. Therefore, SSHC's claim for bad faith refusal to pay must be dismissed.

Additionally, both Count I, alleging a TCPA violation, and Count II, alleging bad faith failure to pay, of SSHC's Counterclaim must be dismissed based upon SSHC's failure to plead fraud, to the extent alleged therein, with sufficient particularity pursuant to the enhanced pleading standards under FED. R. CIV. P. 9(b). Alternatively, Count I of the Counterclaim must be dismissed upon SSHC's failure to plead a deceptive act or practice with sufficient particularity pursuant to the enhanced pleading standards under FED. R. CIV. P. 9(b).

For all of the reasons discussed herein, National Union seeks dismissal of both counts of the Counterclaim in its entirety pursuant to FED. R. CIV. P. 12(b)(6), because the allegations in support of each of SSHC's purported causes of action are insufficiently pled.

STATEMENT OF FACTS

A. The Policies

In 2008 and 2009, National Union issued through the Dentist's Advantage Program ("Dentist's Advantage") the following policies of dental professional liability insurance applicable to either entities or individual dentists (collectively, the "Policies") to SSHC:

- Dentists Liability Policy No. DNU3375848 for the policy period September 26, 2008 through September 26, 2009 (the "08/09 Entities Policy");
- Dentists Liability Policy No. DNU3375848 for the policy period September 26, 2009 through September 26, 2010 (the "09/10 Entities Policy");
- Dentists Liability Policy No. DNU6360128 for the policy period December 1, 2008 through December 1, 2009 (the "08/09 Individual Dentists Policy"); and
- Dentists Liability Policy No. DNU6360128 for the policy period December 1, 2009 through December 1, 2010 (the "09/10 Individual Dentists Policy").

(Complaint ¶¶ 10, 19-21)

SSHC owns a dental practice management business and manages a chain of 50 or more affiliated dental practices and dentists in at least 22 states, which specialize in providing dental services to children eligible for dental care under Medicaid or similar programs (“the Small Smiles Centers”) (Complaint ¶¶ 5, 12). SSHC solicited and obtained the Policies on behalf of the insureds described in each of the Policies, including SSHC, its subsidiaries, including but not limited to FORBA Holdings, LLC (“FORBA”), the Small Smiles Centers and the dentists and employees working at the Small Smiles Centers (Complaint ¶¶ 5, 11-13).

B. National Union’s Declaratory Judgment Action

National Union commenced this Action pursuant to 28 U.S.C. §§ 2201 and 2202, seeking a declaration of the parties’ rights and obligations under the Policies, upon filing the Complaint, and attached exhibits, before this Court on August 5, 2010. A copy of the Complaint, together with certified copies of each of the Policies attached thereto, is annexed to the Declaration of Scott D. Greenspan (the “Greenspan Decl.”) as Exhibit A. The Complaint, which was served upon SSHC in Nashville, Tennessee on August 6, 2010 and in Wilmington, Delaware on August 9, 2010, seeks rescission of the Policies due to SSHC’s failure to disclose to National Union known material information pertaining to risks insured by National Union that increased the risk of loss under those Policies (Complaint ¶ 2).

In the Complaint, National Union alleges that prior to the issuance of the Policies, SSHC knew – but failed to disclose – material information relevant to the risks SSHC sought to insure under the Policies, thereby increasing the risk of loss under the Policies and breaching SSHC’s duty to disclose such material information to National Union (Complaint ¶¶ 2, 75, 76). In that regard, National Union alleges that:

- (i) SSHC knew of numerous systemic problems concerning the quality and propriety of dental care provided by the Small Smiles Centers, but failed to disclose the same to National Union (Complaint ¶¶ 22-25).
- (ii) SSHC failed to disclose to National Union that SSHC, its subsidiaries, the Small Smiles Centers and the dentists and employees working at the Small Smiles Centers were the targets of multiple state and federal investigations concerning SSHC's business practices including, *inter alia*, Medicaid fraud and a pattern and practice of subjecting pediatric dental patients to medically unnecessary dental procedures (Complaint ¶¶ 27-30).
- (iii) SSHC knew, but failed to disclose to National Union, the fact that SSHC had made multiple insurance claims arising from the numerous state and federal investigations regarding SSHC's business practices to its prior professional liability insurance carrier under policies immediately preceding the Policies (Complaint ¶¶ 32-36).
- (iv) SSHC failed to disclose that SSHC's previous professional liability insurance carrier had nonrenewed its policies due to claims experience prior to the inception of any of the Policies (Complaint ¶¶ 38-41).
- (v) SSHC did not disclose its indemnification demands to the previous owners of SSHC's dental practice management entities for the Small Smiles Centers for losses caused by the multiple state and federal investigations regarding SSHC's business practices (Complaint ¶¶ 43-52).
- (vi) SSHC knew of multiple *qui tam* actions commenced against SSHC's subsidiaries, certain of the Small Smiles Centers and the dentists and employees working at the Small Smiles Centers alleging Medicaid fraud and a pattern and practice of

subjecting pediatric dental patients to medically unnecessary dental procedures, but did not disclose the same to National Union (Complaint ¶¶ 54-63).

National Union maintains that, although SSHC had a duty to disclose to National Union all information known to SSHC that was material to the risks SSHC sought to insure under the Policies, SSHC breached its duty by failing to disclose known material information to National Union that increased the risk of loss under the Policies (Complaint ¶¶ 26, 31, 37, 42, 53, 64, 75, 76, 77). To that end, National Union alleges that it would not have issued the Policies to SSHC had SSHC disclosed the material facts known to SSHC at the time it sought to obtain, in 2008, or renew, in 2009, its dental professional liability insurance coverage from National Union (Complaint ¶ 78).

Accordingly, National Union now seeks a declaration that SSHC's failure to disclose material information entitles National Union to rescind each of the Policies *ab initio* (Complaint ¶¶ 75-79). Alternatively, and only if National Union does not prevail on its claim for rescission, National Union seeks reformation of the Policies in accordance with the true and actual intent of the parties at the time each of the Policies was issued (Complaint ¶¶ 81-88, 90-91).

C. SSHC's Answer and Counterclaim

On September 10, 2010, SSHC served its Answer to the Complaint. A copy of SSHC's Answer is annexed to the Greenspan Decl. as Exhibit B.

Thereafter, SSHC interposed its Counterclaim against National Union dated October 28, 2010, prior to the November 10, 2010 deadline set forth in the Joint Case Management Order dated September 16, 2010. A copy of SSHC's Counterclaim is annexed to the Greenspan Decl. as Exhibit C.

SSHC generally alleges in its Counterclaim that, prior to the issuance of any of the Policies, SSHC purchased its dental professional liability insurance through Dentist's Advantage, which issued professional liability insurance through American Insurance Company and its parent,

Fireman's Fund Insurance (collectively, "Fireman's Fund") (Counterclaim ¶¶ 5, 6). SSHC further alleges that, during the pendency of the policies issued by Fireman's Fund, it notified Dentist's Advantage of the governmental investigations into FORBA and certain of the Small Smiles Centers concerning "wrongful acts in connection with claims for dental services submitted to Medicaid" (as defined therein, the "Governmental Investigations") (Counterclaim ¶¶ 7, 8). Along with those notifications, SSHC alleges that it sent a copy of all subpoenas and letters regarding the investigations to Dentist's Advantage (Counterclaim ¶ 8).

SSHC additionally alleges that in 2008, Dentist's Advantage advised it had terminated its contract with Fireman's Fund, and for that reason its dental professional liability insurance policies would not be renewed with Fireman's Fund, but rather with National Union (Counterclaim ¶ 11). To that end, SSHC alleges, in part, that because SSHC previously notified Dentist's Advantage of the Government Investigations prior to the issuance of any of the Policies, National Union's Action, seeking, *inter alia*, rescission of the Policies, is "frivolous" and "unfounded" (Counterclaim ¶ 21). Therefore, SSHC asserts that National Union's conduct constitutes a violation of: 1) the Tennessee Consumer Protection Act (the "TCPA"), TENN. CODE ANN. § 47-18-101, *et seq.* (Counterclaim ¶¶ 24-28); and 2) Tennessee's bad faith failure to pay statute, TENN. CODE ANN. § 56-7-105 (Counterclaim ¶¶ 30-33). In essence, SSHC asks this Court to find that National Union's lawsuit against SSHC seeking relief from this Court is itself actionable.

In support of Count I of the Counterclaim, for purported violation of the TCPA, SSHC alleges that:

The representations, omissions, and other conduct of National Union in handling SSHC's claims under the Policies, including National Union's bad faith attempt to avoid its contractual obligations under the Policies by engaging in post-claim underwriting and by falsely claiming that SSHC did not provide notice of Government Investigations, constitute unfair or deceptive practices in violation of the TCPA, entitling SSHC to actual damages plus attorneys' fees and costs.

(Counterclaim ¶ 25).

SSHC further alleges that:

As a direct result of National Union's unfair or deceptive acts or practices in violation of the TCPA, SSHC has suffered an ascertainable loss of money or property, including but not limited to the costs associated with seeking the insurance coverage to which it is entitled under the Policies from National Union.

(Counterclaim ¶ 27)

In support of Count II of the Counterclaim, for purported violation of Tennessee's bad faith failure to pay statute, SSHC alleges that:

In keeping with the notification requirements of the Policies, SSHC provided formal notice of each of the claims brought against it as soon as it learned of the claims and formally demanded coverage, including defense and indemnity. National Union has in turn sought rescission of its insurance contracts with the SSHC-Insureds, by falsely claiming that SSHC did not provide notification of the potential claims and investigations against it at the time National Union issued its Policies to SSHC.

(Counterclaim ¶ 31).

SSHC further alleges that:

National Union, in a conspicuous effort to shirk its contractual obligations and obtain rescission of the Policies, has falsely claimed that SSHC did not provide notice of the Governmental Investigations and has otherwise acted in bad faith in regard to its obligation under the Policies.

(Counterclaim ¶ 32).

1. Claims Made by SSHC Under the Policies

SSHC further alleges that it provided notice to National Union of the actions entitled *Parnell, et al. v. FORBA Holdings, LLC, et al.*, pending in the United States District Court, Northern District of Ohio, Western Division, Civil Action No. 10-CV-00172 (the "Parnell Action")², and *Hernandez, et al. v. FORBA Holdings, LLC, et al.*, pending in the District Court of Oklahoma County,

² The Parnell Action has since been dismissed by the plaintiffs therein on a without prejudice basis by notice of dismissal dated October 29, 2010 that was so-ordered and entered by the district court on November 5, 2010. *See Greenspan Decl., Ex. H.*

Oklahoma, Case No. CJ-2010-1632 (the “Hernandez Action”), for which SSHC is seeking coverage under the Policies (Counterclaim ¶¶ 15-18). SSHC also alleges that it “learned of other claims or potential claims against SSHC, FORBA, and certain SSHC-Insureds” and that notice under the Policies was made seeking coverage thereunder with respect to those claims (Counterclaim ¶¶ 19, 20). While not expressly identified by SSHC, National Union understands that SSHC is referring to the lawsuits captioned *Havens, et al. v. Dighton, et al.*, Case No. CV-2009-14194, pending in the Second Judicial District Court, County of Bernalillo, State of New Mexico (the “Havens Action”), and *Wingo v. Small Smiles Dentistry, et al.*, Case No. 2009CV2177, which was filed in the District Court, El Paso County, State of Colorado (the “Wingo Action”).

Although never stated in the Counterclaim, and notwithstanding SSHC’s suggestions to the contrary, National Union acknowledged coverage under the applicable Policies, pursuant to the terms and conditions contained therein, and agreed, subject to a complete reservation of rights, to undertake SSHC’s defense (and/or the defense of SSHC-related insureds) in all four of these actions. Indeed, National Union successfully defended SSHC-related insureds at trial in the Wingo Action, and prevailed. Copies of the applicable reservation of rights letter corresponding to the Parnell Action, the Hernandez Action, the Havens Action and the Wingo Action are annexed to the Greenspan Decl. as Exhibit D, E, F and G, respectively. A copy of the Order and Judgment entering the jury verdict in the Wingo Action is annexed to the Greenspan Decl. as Exhibit I.

ARGUMENT

STANDARD OF REVIEW FOR A MOTION TO DISMISS

Pursuant to FED. R. CIV. P. 12(b)(6), a district court should dismiss a claim for relief in any pleading, including a counterclaim, that fails to “state a claim upon which relief can be granted.” *See generally May v. Nat’l Bank of Commerce*, 390 F. Supp. 2d 674, 675 (W.D. Tenn. 2004); *Birmingham-Jefferson County Transit Auth. v. Boatright*, 2009 WL 2601926, at *1 (M.D. Tenn.

Aug. 20, 2009). The purpose of a motion brought under Rule 12(b)(6) is to test the sufficiency of the pleading as a matter of law and whether the pleader (*e.g.*, a counter-plaintiff) is entitled to the relief sought, assuming that all well-pleaded factual allegations contained therein are true. *Doe v. Univ. of the South*, 687 F. Supp. 2d 744, 750 (E.D. Tenn. 2009). *See also League of United Latin Am. Citizens v. Bredesen*, 500 F.3d 523, 527 (6th Cir. 2007). A court, however, “need not accept as true legal conclusions or unwarranted factual inferences.” *Mixon v. State of Ohio*, 193 F.3d 389, 400 (6th Cir. 1999). To that end, and upon a motion to dismiss, the court considers the allegations contained in the pleading, any exhibits attached thereto and any document annexed to the motion to dismiss to the extent referenced in the pleadings and central to the pleader’s claim. *See generally Amini v. Oberlin Coll.*, 259 F.3d 493, 502 (6th Cir. 2001).

Although, for the purposes of a Rule 12(b)(6) motion, the claims alleged by the pleader are typically construed in the most favorable light, and all well-pleaded factual allegations in connection therewith are generally accepted as true, those legal principles are inapplicable to bare assertions of legal conclusions. *See Doe*, 687 F. Supp. 2d at 750, *Bredesen*, 500 F.3d at 527. *See also Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949-1950 (U.S. 2009). “While legal conclusions can provide the framework for a [pleading], all claims must be supported by factual allegations.” *Id.* at 1950. Consequently, “[t]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements, do not suffice.” *Id.* at 1949 (citing *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 555 (U.S. 2007)). The pleader must actually show, through well-pleaded factual support, that the allegations in the complaint (or pleading) are entitled to the assumption of truth. *Iqbal*, at 1949-50.

Furthermore, the complaint (or pleading) must also “state a claim to relief that is plausible on its face.” *Id.* at 1949 (citation omitted). A claim has requisite “facial plausibility” when the plaintiff (or counter-plaintiff) “pleads factual content that allows the court to draw the reasonable inference

that the defendant [or counter-defendant] is liable for the misconduct alleged.” *Id.* (citation omitted). Although the plausibility standard differs from a “probability requirement,” it still requires more than a “sheer possibility that a defendant [or counter-defendant] has acted unlawfully.” *Id.* (citation omitted). “Where a complaint pleads facts that are ‘merely consistent with’ a defendant’s [or counter-defendant’s] liability, it ‘stops short of the line between possibility and plausibility of entitlement to relief.’” *Id.* (citation omitted).

Therefore, “[w]here the well-pleaded facts do not permit the court to infer more than the mere possibility of misconduct, the complaint has alleged—but it has not ‘show[n]’—‘that the pleader is entitled to relief.’” *Id.* at 1950 (quoting FED. R. CIV. P. 8(a)(2)). Accordingly, a pleading that raises only the mere “possibility of misconduct” is insufficient and so the court should grant the motion to dismiss for failure to state a cause of action under FED. R. CIV. P. 12(b)(6). *See, e.g., Hutchison v. Metro. Gov’t of Nashville and Davidson County*, 685 F. Supp. 2d 747, 751 (M.D. Tenn. 2010) (granting motion to dismiss because plaintiff’s conclusory claims were not supported by any facts and, therefore, “stopped short of the line between possibility and plausibility” regarding defendant’s liability (internal citation omitted)).

POINT I

THE FIRST CLAIM FOR VIOLATION OF THE TENNESSEE CONSUMER PROTECTION ACT (THE “TCPA”) IS INSUFFICIENTLY PLED AND SHOULD BE DISMISSED

In Count I of its Counterclaim against National Union, SSHC makes the conclusory and factually bare allegation that the “representations, omissions, and other conduct of National Union in handling SSHC’s claims under the Policies, including National Union’s bad faith attempt to avoid its contractual obligations under the Policies by engaging in post-claim underwriting and by falsely claiming that SSHC did not provide notice of Government Investigations, constitute unfair or deceptive acts or practices in violation of the TCPA....” (Counterclaim ¶ 25).

In pleading its Counterclaim, however, SSHC improperly seeks to make actionable under the TCPA, as an unfair or deceptive act or practice, National Union's good faith act of applying for the appropriate judicial relief from the Court. In that regard, and despite National Union's grave concerns as to SSHC's failure to disclose material information, National Union did not unilaterally rescind the Policies and reject covered claims thereunder; but, rather has expressly committed to defending covered claims, subject to a complete reservation of rights, pending a determination from the Court that National Union may rescind the Policies based upon SSHC's breach of its duty to disclose, which is contested and denied in its entirety by SSHC.

For the reasons discussed below, SSHC fails to allege sufficient facts in support of its cause of action under the TCPA. As such, Count I of the Counterclaim should be dismissed.

A. SSHC Fails to State a Claim for Relief Under the TCPA

The stated purpose of the TCPA is to "protect consumers and legitimate business enterprises from those who engage in unfair or deceptive acts or practices in the conduct of any trade or commerce in part or wholly within this state". TENN. CODE ANN. § 47-18-102(2). In pertinent part, the TCPA provides that:

[a]ny person who suffers an ascertainable loss of money or property, real, personal, or mixed, or any other article, commodity, or thing of value wherever situated, as a result of the use or employment by another person of an unfair or deceptive act or practice declared to be unlawful by this part, may bring an action individually to recover actual damages.

TENN. CODE ANN. § 47-18-109(a)(1). Thus, the TCPA affords a private right of action for a number of unfair or deceptive acts or practices, including a non-exhaustive list of specifically enumerated conduct deemed impermissible under the TCPA and a catch-all provision otherwise proscribing "any other act or practice that is deceptive to the consumer or any other person...." TENN. CODE ANN. § 47-18-104(a) & (b). Further, Tennessee authorities recognize that the TCPA is applicable to insurance companies. *See generally Myint v. Allstate Ins. Co.*, 970 S.W.2d 920, 925 (Tenn. 1998)

(acknowledging that the “acts and practices of insurance companies” may fall within the purview of the TCPA); *Williamson v. Aetna Life Ins. Co.*, 481 F.3d 369, 378 (6th Cir. 2007) (affirming district court’s dismissal of TCPA claim at summary judgment in the absence of a deceptive or unfair act in denying the insured’s claim).

In pleading and proving a TCPA violation, Tennessee courts have held that there are two “distinct proof obligations” necessary to establish a cause of action: 1) an unfair or deceptive act or practice declared unlawful under the TCPA and 2) that such conduct caused an “ascertainable loss of money or property, real, person or mixed, or any other article, commodity or thing of value wherever situated”. *Waggin’ Train, LLC v. Normerica, Inc.*, 2010 WL 145776, at *3 (W.D. Tenn. Jan. 8, 2010) (citing *Tucker v. Sierra Builders*, 180 S.W.3d 109, 115 (Tenn. Ct. App. 2005)). The TCPA itself does not define the terms “deceptive” or “unfair”. *Cloud Nine, LLC v. Whaley*, 650 F. Supp. 2d 789, 796 (E.D. Tenn. 2009). However, the Tennessee Supreme Court has generally acknowledged that a “deceptive act or practice is a material representation, practice or omission *likely to mislead* a reasonable consumer.” *Ganzevoort v. Russell*, 949 S.W.2d 293, 299 (Tenn. 1997) (citation omitted) (emphasis added).

As further applied in the insurance claims context, however, and for the TCPA to apply, the insured must allege (and prove) that the insurer’s conduct with respect to the claim was unfair and deceptive such that the insurer violated the policy terms, deceived the insured about the policy terms or acted unfairly in some other fashion. *See generally Myint*, 970 S.W.2d at 926; *Sw. Life Ins. Co., v. Mercer*, 100 F. App’x. 372, 378 (6th Cir. 2004) (finding no TCPA violation absent evidence that the insurer, in offering to reinstate a canceled policy, violated the terms under which the policy was

offered, misled the insured as to the necessary prerequisites under which the policy would be reinstated or otherwise acted unfairly).³

Consistent with the foregoing authorities, SSHC does not plead the requisite elements necessary to state a TCPA claim. Notably absent from SSHC's Counterclaim is any factually specific and non-conclusory allegation: 1) identifying any unfair or deceptive act or practice by National Union; 2) that SSHC was misled or deceived by such allegedly unfair or deceptive act or practice; and 3) of an ascertainable loss of money or property that SSHC suffered as a result of the unfair or deceptive act or practice.

1. SSHC Fails to Allege an Unfair or Deceptive Act or Practice for the Purposes of the TCPA

As a threshold matter, and without more, SSHC's conclusory statement that National Union's "representations, omissions, and other conduct in handling SSHC's claims under the Policies" constitute "unfair or deceptive acts or practices in violation of the TCPA" fails to plead a factually sufficient unfair or deceptive act or practice in violation of the TCPA (Counterclaim ¶ 25).

a. SSHC Fails to Allege that National Union's Commencement of This Action is an Unfair or Deceptive Act or Practice for the Purposes of the TCPA

SSHC alleges that the commencement of this Action is by itself an unfair or deceptive act or practice in connection with National Union's "handling" of SSHC's claims under the TCPA (*i.e.*, National Union's "bad faith attempt to avoid its contractual obligations under the Policies...")

³ See also *Fulton Bellows, LLC v. Fed. Ins. Co.*, 662 F. Supp. 2d 976, 997 (E.D. Tenn. 2009) (insured must allege that the insurer violated the terms of the policy, deceived the insured about the policy terms or acted unfairly for the TCPA to apply to the denial of an insurance claim); *Taylor v. Standard Ins. Co.*, 2009 WL 113457, at *5 (W.D. Tenn. Jan. 13, 2009) (dismissing TCPA claim absent any factual allegation that the insurer had violated the terms of the policy, deceived the insured about the policy or acted unfairly as to her insurance claim); *Williams v. State Farm Fire & Cas. Co.*, 2008 WL 2421702, at *5 (W.D. Tenn. June 12, 2008) (finding no violation of the TCPA without a violation of the policy or deception of the policyholder); *Nautilus v. The In Crowd*, 2005 WL 2671252, at *6 (M.D. Tenn. Oct. 19, 2005) (dismissing TCPA counterclaim upon insured's failure to allege how the insurer acted to deceive or mislead the insured, acted to violate the terms of the policy or otherwise acted unfairly when, after defending under a reservation of rights, the insurer filed a declaratory judgment action seeking a judicial determination of its rights under the policy).

(Counterclaim ¶ 25). However, SSHC does not, nor can it, allege how the mere act of National Union filing this Action in good faith qualifies as “a material representation, practice or omission likely to mislead a reasonable consumer” for the purposes of the statute. *Ganzevoort*, 949 S.W.2d at 299 (describing a deceptive act for the purposes of the TCPA).

In that regard, SSHC’s Counterclaim is devoid of any allegations as to how National Union’s conduct in bringing this Action is unfair and deceptive such that National Union violated the terms of any of the Policies, deceived SSHC about the terms of any of the Policies or acted unfairly in some other fashion. *See generally Myint*, 970 S.W.2d at 926. Indeed, SSHC: 1) denies owing any duty to National Union to disclose information known to SSHC that was material to the risks SSHC sought to insure under the Policies (Answer ¶¶ 26, 31, 37, 42, 53, 64, 75, 76); 2) further denies that National Union is entitled to the equitable relief of rescission sought in the Complaint (Answer ¶¶ 75-79); and 3) is vigorously challenging the Action.

This Court’s prior decision in *Nautilus v. The In Crowd*, 2005 WL 2671252 (M.D. Tenn. Oct. 19, 2005), is directly on point, controlling and requires the dismissal of SSHC’s TCPA claim. In *Nautilus*, the insurer agreed to defend its insureds in an underlying civil lawsuit under a comprehensive general liability policy subject to a full reservation of rights, including the right to commence an action to declare the rights and obligations of the parties under the policy. Prior to settlement of the civil lawsuit, of which a portion was ultimately paid under the policy subject to the reservation of rights, the insurer filed a declaratory judgment action seeking a declaration of no coverage under the policy pursuant to the terms, conditions and limitations therein. *Nautilus*, 2005 WL 2671252, *2-3. The insureds, in answering the declaratory judgment action, interposed counterclaims for, *inter alia*, violation of the TCPA premised upon the insurer’s act of filing the declaratory judgment action. *Id.* at *4.

In dismissing the TCPA counterclaim, this Court acknowledged that it “is not aware, however, of any case finding a TCPA violation...where the insurance company provides a defense for the insured...while expressly reserving its rights to contest coverage, and then files a declaratory judgment action to have a court determine the issue of coverage.” *Id.* at *5. Therefore, this Court concluded that no cause of action for a TCPA violation would lie where the allegations in support of the claim “go to the merits of the underlying declaratory judgment action” but do not set forth how the insurer acted to deceive or mislead the insured when the insurer provided a defense under a reservation of rights and then filed suit seeking a judicial declaration as to its obligations under the policy. *Id.* at *6.

SSHC’s allegations in support of its TCPA claim fail the standard articulated in *Nautilus*, insofar as they only apply, if at all, to the basis of the Action (*i.e.*, SSHC’s disagreement with the merits of National Union’s rescission claim) and not as to how SSHC was misled or deceived by National Union’s conduct. National Union, just like the insurer in *Nautilus*, is affording a defense for SSHC as to each of the claims specifically identified in the Counterclaim subject to a complete reservation of rights, including whether each of the Policies should be rescinded. *See Greenspan Decl., Exs. D and E.*⁴ Therefore, and again just like the insurer in *Nautilus*, National Union reserved all rights under the Policies and subsequently commenced a declaratory judgment action seeking a judicial determination of its rights. SSHC, just like the insured in *Nautilus*, fails to allege how National Union’s defense of SSHC under a full reservation of rights and National Union’s subsequent commencement of this Action, seeking a judicial declaration, is in any way deceptive or unfair in the context of the TCPA.

⁴ Although not expressly identified in SSHC’s Counterclaim, National Union is also affording a defense under a reservation of rights in connection with the Havens Action. *See Greenspan Decl., Ex. F.* Additionally, National Union successfully defended Small Smiles in the Wingo Action, resulting in a defense verdict. *See Greenspan Decl., Exs. G and I.*

b. SSHC Fails to Allege that National Union’s “Claims Handling” is an Unfair or Deceptive Act or Practice

SSHC alleges that National Union’s “handling” of claims constitutes unfair or deceptive acts or practices without articulating any factual basis in support of its conclusory statement or even what SSHC means by “handling SSHC’s claims under the Policies.” Nevertheless, and as alleged by National Union in the Complaint, each of the Policies generally afford coverage to SSHC, subject to the conditions, exclusions and limitations therein (Complaint ¶¶ 11-14). Therefore, and as to each of the matters that SSHC alleges was tendered to National Union for coverage under one or more of the Policies, including but not limited to the Parnell Action (Counterclaim ¶¶ 15, 16) and the Hernandez Action (Counterclaim ¶¶ 16, 17), National Union acknowledged coverage under the applicable Policies, pursuant to the terms and conditions contained therein, and agreed, subject to a complete reservation of rights, to undertake SSHC’s defense. *See Greenspan Decl., Exs. D and E.*

In connection with the foregoing, and even assuming that, as SSHC alleges, the Parnell Action and the Hernandez Action are being “handled” in connection with this Action, SSHC does not allege how National Union’s “handling” of those claims is unfair or deceptive or how it is that National Union violated the policy terms, deceived SSHC about any of the policy terms or acted unfairly in any other fashion.

A TCPA claim does not lie in the absence of any allegations consistent with an unfair and deceptive business practice. *See generally Taylor*, 2009 WL 113457, at *5 (granting motion to dismiss a TCPA claim for failure to allege any specific facts to support conclusory allegation that insurer employed any unfair or deceptive business practice in adjusting the claim); *Nature Conservancy v. Browder*, 2008 WL 336744, at *8 (E.D. Tenn. Feb. 5, 2008) (granting motion to dismiss TCPA claim for failure to allege what act or acts were unfair or deceptive); *Scraggs v. La Petite Acad., Inc.*, 2006 WL 2711689, at *4 (E.D. Tenn. Sep. 21, 2006) (granting motion to dismiss

TCPA claim upon failure to allege “facts indicating how the alleged misrepresentation of defendant was deceptive and/or unfair”). Accordingly, National Union respectfully submits that SSHC fails to plead a TCPA violation with respect to a deceptive or unfair act or practice employed by National Union, and therefore, SSHC’s TCPA cause of action should be dismissed.

2. SSHC Fails to Allege How It was Misled or Deceived by the Allegedly Deceptive Act or Practice

SSHC’s Counterclaim also contains no allegations as to how SSHC was deceived by National Union’s alleged unfair and deceptive act or business practice. In the absence of any such allegations, a TCPA claim does not lie. *Nautilus*, 2005 WL 2671252, at *6 (holding that insured’s TCPA cause of action failed in the absence of any explanation of how the insurer deceived or misled the insured); *Scraggs*, 2006 WL 2711689, at *4 (dismissing TCPA claim absent facts as to how deceptive and/or unfair acts caused loss). *See also Parkway Assocs., LLC v. Harleysville Mut. Ins. Co.*, 129 F. App’x. 955, 960-61 (6th Cir. 2005) (affirming district court’s dismissal of plaintiff’s TCPA cause of action at summary judgment for failure to state a claim, insofar as plaintiff did not explain how it was misled or deceived by the defendant’s allegedly deceptive act or practice). Accordingly, National Union respectfully submits that SSHC fails to plead a TCPA violation in the absence of any allegation as to how SSHC was misled or deceived by National Union’s purportedly deceptive act or practice, if any, and therefore, SSHC’s TCPA cause of action should be dismissed.

3. SSHC Fails to Allege an Ascertainable Loss

In order to prevail on its TCPA cause of action, in addition to alleging an unfair or deceptive act or practice declared unlawful by the TCPA, SSHC must also allege that the complained-of conduct caused an “ascertainable loss of money or property, real, personal or mixed, or any other article, commodity or thing of value wherever situated”. *Tucker*, 180 S.W.3d at 115 (quoting TENN. CODE ANN. 47-18-109(a)(1)). Apart from its factually unsubstantiated claim for actual damages and

attorneys' fees and costs (Counterclaim ¶ 25), SSHC, however, alleges that its ascertainable loss includes, but is not limited to, "costs associated with seeking the insurance coverage to which it is entitled under the Policies from National Union." SSHC's allegation is factually insufficient because SSHC fails to quantify the loss and/or allege how the loss was caused by National Union's unfair or deceptive act or practice. *See Waggin' Train*, 2010 WL 145776, at *4 (granting motion to dismiss TCPA claim, in part, based on the absence of ascertainable loss that is more than conjectural and emanates from the unfair or deceptive conduct); *Browder*, 2008 WL 336744, at *8 (granting motion to dismiss TCPA claim based, in part, on the failure to plead any actual damages). Moreover, it is unclear what "loss", if any, SSHC sustained insofar as it does not (and cannot) allege that any indemnity obligation is due under any of the Policies (*e.g.*, as to the Parnell, Hernandez, Havens and/or Wingo Actions). Accordingly, National Union respectfully submits that SSHC fails to plead a TCPA violation in the absence of any allegation as to an ascertainable loss caused by a deceptive or unfair act or practice, if any, and SSHC's TCPA cause of action should be dismissed.

POINT II

THE SECOND CLAIM FOR BAD FAITH IS INSUFFICIENTLY PLED AND SHOULD BE DISMISSED

In Count II of its Counterclaim, brought under Tennessee's bad faith failure to pay statute, TENN. CODE ANN. § 56-7-105, SSHC makes the conclusory and factually bare allegation that notwithstanding "formal notice of each of the claims brought against [SSHC] as soon as it learned of the claims", National Union nevertheless "sought rescission of [the Policies]...in a conspicuous effort to shirk its contractual obligation" such that "National Union's bad faith refusal to provide coverage constitutes a violation of [the statute]" (Counterclaim ¶¶ 31-33). However, and for the reasons discussed below, SSHC fails to allege sufficient facts in support of its bad faith cause of action under the statute.

A. SSHC Fails to State a Claim for Relief Under TENN. CODE ANN. § 56-7-105

In relevant part, TENN. CODE ANN. § 56-7-105 (the “Bad Faith Statute”) states as follows:

The insurance companies of this state, and foreign insurance companies and other persons or corporations doing an insurance or fidelity bonding business in this state, in all cases when a loss occurs and they refuse to pay the loss within sixty (60) days after a demand has been made by the holder of the policy or fidelity bond on which the loss occurred, shall be liable to pay the holder of the policy or fidelity bond, in addition to the loss and interest on the bond, a sum not exceeding twenty-five percent (25%) on the liability for the loss; provided, that it is made to appear to the court or jury trying the case that the refusal to pay the loss was not in good faith, and that the failure to pay inflicted additional expense, loss, or injury including attorney fees upon the holder of the policy or fidelity bond; and provided, further, that the additional liability, within the limit prescribed, shall, in the discretion of the court or jury trying the case, be measured by the additional expense, loss, and injury including attorney fees thus entailed.

TENN. CODE ANN. § 56-7-105(a).

Therefore, in order to succeed on its claim under the Bad Faith Statute, SSHC must allege (and prove) each of the following necessary elements: 1) that the applicable Policies have, per their terms, become due and payable; 2) that SSHC made a formal demand for payment threatening litigation for National Union’s bad faith failure to pay; 3) that SSHC waited 60 days after making the formal demand before filing suit (unless there was a refusal to pay prior to the expiration of the 60 days); and 4) that National Union’s alleged refusal to pay was not in good faith.

It is well settled that a pleading which fails to adequately state a claim under the Bad Faith Statute should be dismissed. For example, the court in *Life Ins. Co. of N. Am. v. Simpson*, granted the insurer’s Rule 12(b)(6) motion to dismiss its insured’s bad faith counterclaim absent any allegation that the insurer had denied the claim. *Life Ins. Co. of N. Am. v. Simpson*, 2009 WL 2163498, at *3 (W.D. Tenn. July 16, 2009). Similarly, the court in *Taylor* granted the insurer’s Rule 12(b)(6) motion to dismiss the bad faith claim upon the insured’s failure to allege any factual allegations in support of the claim, including the date the insured made a demand for payment and that 60 days had passed since the demand. *Taylor*, 2009 WL 113457, at *6. Further, the court in

Cracker Barrel Old Country Store, Inc. v. Cincinnati Ins. Co., granted the insurer’s Rule 12(b)(6) motion and dismissed the insured’s claim under the Bad Faith Statute for failing to allege that a formal demand was made threatening bad faith litigation prior to interposing the claim under the statute. *Cracker Barrel Old Country Store, Inc. v. Cincinnati Ins. Co.*, 590 F. Supp. 2d 970, 975 (M.D. Tenn. 2008). *See also Williamson*, 481 F.3d at 378 (affirming district court’s summary judgment motion finding that the insured’s unsupported allegation was insufficient to establish that the insurer’s refusal to pay was in bad faith).

In support of its cause of action under the Bad Faith Statute, SSHC alleges that it sought a defense and indemnity from National Union with respect to certain claims, including but not limited to the Parnell Action and the Hernandez Action. However, nowhere in the Counterclaim does SSHC allege that: 1) payments are due under the Policies; 2) SSHC made a formal demand for payment threatening litigation as a result of National Union’s bad faith failure to pay; 3) 60 days passed after SSHC made the formal demand for payment before filing suit; and 4) National Union ever refused to pay any such claims in bad faith (Counterclaim ¶¶ 30-33). Accordingly, SSHC fails to allege each of the required elements under the Bad Faith Statute, and therefore its cause of action must be dismissed as a matter of law.

POINT III

SSHC’S COUNTERCLAIM SHOULD BE DISMISSED FOR FAILURE TO SATISFY FED. R. CIV. P. 9(B)

SSHC appears to allege fraudulent conduct on the part of National Union, insofar as SSHC maintains in its Counterclaim that: 1) National Union is “falsely claiming that SSHC did not provide notice of the Government Investigations” in support of SSHC’s claim for a “willful and knowing” violation of the TCPA (Counterclaim ¶¶ 25, 28); and 2) National Union is “falsely claiming that SSHC did not provide notification of...potential claims...at the time National Union issued its

Policies to SSHC” or “the Government Investigations” in support of SSHC’s claim for a violation of Tennessee’s bad faith refusal to pay statute (Counterclaim ¶¶ 31, 32). To the extent that the Counterclaim alleges fraud, SSHC’s allegations fail to comport with the enhanced pleading standards for the purposes of FED. R. CIV. P. 9(b), which states that “[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake.” Accordingly, SSHC has not adequately pled fraud with sufficient particularity to overcome a Rule 12(b)(6) motion to dismiss.

Furthermore, claims brought under the TCPA, whether for fraud or for unfair and deceptive acts, are subject to the specific pleading requirements imposed under Rule 9(b). *See generally Metro. Prop. & Cas. Ins. Co. v. Bell*, 2005 WL 1993446, at *5 (6th Cir. Aug. 17, 2005) (the enhanced pleading standards described in Rule 9(b) are applicable to allegations of unfair and deceptive acts for the purposes of the TCPA); *Rhodes v. Bombardier Capital, Inc.*, 2010 WL 3861074, at *2 (E.D. Tenn. Sep. 24, 2010) (same); *Williamson v. Ocwen Loan Servicing, LLC*, 2009 WL 5205405, at *6 (M.D. Tenn. Dec. 23, 2009) (granting motion to dismiss TCPA claim on the ground that plaintiff did not plead misrepresentation or fraud with the requisite particularity); *McKee Foods Corp. v. Pitney Bowes*, 2007 WL 896153, at *5 (E.D. Tenn. Mar. 22, 2007) (granting motion to dismiss TCPA claim because the complaint failed to specify the time and place of the alleged TCPA violations as required under Rule 9(b)); *Scraggs*, 2006 WL 2711689, at *4 (granting motion to dismiss TCPA claim upon failure to allege with adequate particularity “facts indicating how the alleged misrepresentation of defendant was deceptive and/or unfair, nor that plaintiffs suffered a loss as a result of it”). Accordingly, and regardless of whether SSHC pleads fraud in the Counterclaim, the Rule 9(b) enhanced pleading standards apply to deceptive and unfair acts alleged in connection with SSHC’s TCPA cause of action.

In order to satisfy FED. R. CIV. P.9(b), a complaint of fraud “at a minimum, must ‘allege the time, place, and content of the alleged misrepresentation on which [the plaintiff] relied; the fraudulent scheme; the fraudulent intent of the defendant[]; and the injury resulting from the fraud.’” *Ferrell v. Addington Oil Corp.*, 2010 WL 3283029, at *6 (E.D. Tenn. Aug. 18, 2010) (citations omitted). The reason for the heightened pleading requirement of Rule 9(b) is that claims of fraud “raise a high risk of abusive litigation.” *Id.* Rule 9(b) is intended to provide defendants (or, the counterclaim defendant) with “notice of the specific conduct with which they were charged” so they can prepare responsive pleadings. *Id.* (quoting *United States, ex rel. Bledsoe v. Cmty. Health Sys., Inc.*, 501 F.3d 493, 510 (6th Cir. 2007)).

SSHC does not plead any allegedly false claims or any allegedly unfair and deceptive acts in the Counterclaim in support of either cause of action with sufficient particularity. SSHC fails to allege the time, place, and content of the alleged false claims on which it relies, National Union’s fraudulent scheme (including its fraudulent intent) and the injury resulting from National Union’s purported false claims. The failure to plead these claims proves fatal to the Counterclaim, as SSHC fails to state a claim for relief pursuant to FED. R. CIV. P. 12(b)(6) for an alleged violation of the TCPA by National Union as well as for an alleged violation of the Bad Faith Statute. Therefore, and on this basis alone, the Court should dismiss both of these claims.

CONCLUSION

For the foregoing reasons, Plaintiff/Counter-Defendant National Union respectfully requests that this Court dismiss Defendant/Counter-Plaintiff SSHC’s Counterclaim in its entirety pursuant to FED. R. CIV. P. 12(b)(6).

Dated: Nashville, Tennessee
December 2, 2010

Yours, etc.

/s/ W. Brantley Phillips, Jr.

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