19-2263-cv

United States Court of Appeals

for the

Second Circuit

DEVIVO ASSOCIATES, INC, DENNIS J. DEVIVO,

Plaintiffs-Appellants,

– v. –

NATIONWIDE MUTUAL INSURANCE CO.,

Defendant-Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NEW YORK

REPLY BRIEF FOR PLAINTIFFS-APPELLANTS

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I. COUNTS 1 AND 2 STATE A CLAIM

The mutual exchange of consideration in the exclusive agent contract is as follows:

> 2. The exclusive agents have agreed to place clients eligible for Nationwide insurance products exclusively with Nationwide over the course of an entire career. Over the past four decades, individual exclusive agents have produced premium totals for Nationwide typically exceeding tens of millions and up to hundreds of millions of dollars.
>
> 3. In exchange for that long-term exclusive commitment and resulting high premium amounts, exclusive agent contracts include major deferred compensation provisions, called Agency Security Compensation ("ASC") Plans in most cases, which increase over the life of the contract as the agent's business grows and are payable upon retirement or other cancellation of the contract. Nationwide characterizes these plans as "substantial deferred income" and a "unique" incentive for committing to a long-term exclusive relationship. Nationwide has assured the exclusive agents in the past that Nationwide is "committed to continuing these valuable benefits."

(Amended Complaint ¶¶ 2 - 3 (APPX A-9 - A-10).)

Mr. DeVivo's ASC Plan is set forth in Paragraph 11 of his Agency Agreement. Paragraph 11(h), titled "Amendments and Termination," is the paragraph at issue in Counts 1 and 2. It is set forth on p. 35 of the Opening Brief with each of its four sentences numbered and is repeated here for convenience:

> **[#1]** Nationwide hopes and expects to continue the Agency Security Compensation Plan indefinitely, and every effort has been made to meet future conditions. **[#2]** In order to protect the Agency and Nationwide against unforeseen conditions, however, the right to amend or terminate this plan is ***necessarily*** reserved by Nationwide. **[#3]** Nationwide may terminate this plan by notification, at least sixty (60) days prior to such termination, in writing. **[#4]** No change in the Plan or termination, however, can alter or modify rights or benefits received or credited prior to such change or modification. (Emphasis added.)

(Agreement ¶ 11(h) (APPX A-36).)

Nationwide has announced that it will terminate all remaining Exclusive agent contracts, including Mr. DeVivo's, on July 1, 2020 and that it is now phasing out one of the two components of the ASC Plan -- Extended Earnings -- so that Extended Earnings will not be paid when the contracts are terminated. (Amended Complaint ¶ 5 (APPX A-10) and ¶ 7 (APPX A-11).)

Mr. DeVivo's Amended Complaint states that Nationwide's unilateral cancellation of his entire Extended Earnings payment, valued at approximately $692,000 (Amended Complaint ¶ 45 (APPX A-18)), breaches the express provisions of the Agreement (COUNT 2) and, in the alternative, breaches the covenant of good faith and fair dealing in the Agreement (COUNT 1).

A. NATIONWIDE IS BREACHING THE EXPRESS PROVISIONS OF PARAGRAPH 11(h) (COUNT 2)

1. Sentences #1 - #3 of Paragraph 11(h)

Nationwide argues that "Appellants cannot say, in good faith, that they reasonably expected deferred compensation to continue indefinitely ...." (Brief of Defendant-Appellee Nationwide Mutual Insurance Company (Answering Brief, Document 51, Page 37.) But that is exactly what Nationwide itself intended and expected when it drafted and executed the governing contract in 1994:

> **[1]** Nationwide hopes and expects to continue the Agency Security Compensation Plan indefinitely, and every effort has been made to meet future conditions.

(Corporate Agency Agreement ¶ 11(h), first sentence (Sentence #1), Exhibit A to the Amended Complaint (hereafter, the "Agreement") (APPX A-36). Immediately following that statement of intent and expectation, the parties carved out a narrow exception to apply in case, despite Nationwide's best efforts, an amendment or termination might become "necessary" in order to protect both Mr. DeVivo and Nationwide against "unforeseen conditions":

> **[2]** In order to protect the Agency and Nationwide against unforeseen conditions, however, the right to amend or terminate this plan is necessarily reserved by Nationwide.

(*Id*., second sentence (Sentence #2)).

The meeting of the minds on these two provisions of ¶ 11(h) is clear. In order

to preserve the mutual *quid pro quo* which underlies the entire arrangement (exclusive commitment in exchange for ASC Plan), both Mr. DeVivo and Nationwide intended and expected that the ASC Plan would continue "indefinitely" (*i.e.*, to the end of the Agreement) with a specific proviso allowing a change in the Plan, but only if *necessary* to protect *both* parties against "unforeseen conditions."

Nationwide's April 2018 "unilateral amendment" designed to transfer Mr. DeVivo's Extended Earnings into Nationwide's pocket cannot be reconciled with these provisions of ¶ 11(h). The rationale that Nationwide has offered to explain its decision to keep Mr. DeVivo's Extended Earnings -- which it describes as a "separate business decision" unrelated to its ACE Program -- is simply that deferred compensation plans "are not part of contracts in the *independent* agent channel." (Amended Complaint ¶ 33 (APPX A-15) (emphasis added).) That explanation does not even connect or relate to Mr. DeVivo's *exclusive* contract -- the only contract which pays Extended Earnings, which will remain in force until July 1, 2020 -- much less comport with the meeting of the minds Mr. DeVivo and Nationwide reached when the exclusive contract was formed in 1994.

a. Sentence #2 Is An Operative Proviso

Nationwide's argument as to why it need not honor the meeting of the minds that took place at the formation of the contract is that the first half of Sentence #2 -- "**[i]n order to protect [Mr. DeVivo] and Nationwide against unforeseen**

conditions, however" -- is a separate prefatory statement which cannot limit what Nationwide says is a freestanding absolute right to amend or terminate. *But these two halves of Sentence #2 are not compartmentalized*. The first half of Sentence #2 does not simply state the purpose of the proviso, it also provides the basis for the parties' specific direction that the right to amend or terminate must be "***necessarily*** reserved." The reservation is "necessary" because it protects *both* parties, Mr. DeVivo as well as Nationwide, from "unforeseen conditions." Without that antecedent, the word "necessarily" has no purpose or meaning.

The entire sentence defines the scope of the "necessarily reserved" right to amend or terminate. If the parties had intended to simply state that Nationwide would have an absolute right to amend or terminate, untethered from the "unforeseen conditions" language, the word "necessarily" would not be there. Sharing the goal of preserving their mutual exchange of consideration indefinitely, the parties would not have deemed it "necessary" to give Nationwide a unilateral right to withdraw its part of the consideration at will.

Sentence #2 in its entirety is a narrow proviso to the statement of intention and expectation in Sentence #1 -- a proviso which was "necessarily" included by the parties when the contract was formed, in order to protect ***both*** Mr. DeVivo and Nationwide from "unforeseen conditions." If the parties had had any intention of giving Nationwide an absolute right to amend or terminate the ASC Plan at will, none

of the following would have been included in ¶ 11(h):

- Sentence #1 (stating an intention to continue ASC indefinitely with best efforts);

- the first half of Sentence #2 (the "unforeseen conditions" clause, defining the term "necessarily reserved" in the second half of Sentence #2); and

- the word "necessarily" in the second half of Sentence #2 (the word "necessarily" would not have been included if Nationwide were simply declaring an absolute right).

b. If The "Unforeseen Conditions" Clause Is Viewed As Prefatory Only, The Operative Clause Must Still Be Interpreted In A Manner Which Comports With The Stated Purpose.

Assuming, *arguendo*, that the first half of Sentence #2 can be deemed to be a prefatory clause only, it still has to be analyzed in conjunction with the reservation of the right to amend or terminate which follows, in order to ensure that the "reading of the operative clause is consistent with the announced purpose." *District of Columbia v. Heller*, 554 U.S. 570, 578 (2008) (D.C.'s ban on individual handguns held unconstitutional under the Second Amendment). In the Answering Brief, Nationwide cites the *Heller* decision for the proposition that a prefatory clause does not "limit or expand the scope of the operative clause" (Answering Brief, Document 51, Page 29), *i.e.*, that the prefatory clause does not "limit the [operative clause] grammatically" when it "announces a purpose" (*Heller* at 577), but Nationwide overlooks the cardinal principle that the interpretation of the operative clause (as

written) must be "consistent with the announced purpose." (*Id*. at 578.)

In *Heller*, for example the Supreme Court was construing the Second Amendment in connection with the District of Columbia's ban on individual handguns and applying the above-described principles. At issue in *Heller* was the meaning of the Second Amendment's prefatory clause: "A well regulated Militia, being necessary to the security of a free State ...." Justice Stevens, writing for the 4-person dissent, argued that "well regulated militia" referred to organized state militias, not individual citizens. (*Id*. at 637.) In response, Justice Scalia, writing for the 5-person majority, noted that:

> The two sides in this case have set out very different interpretations of the Amendment. Petitioners and today's dissenting Justices believe that it protects only the right to possess and carry a firearm in connection with militia service. See Brief for Petitioners 11-12; *post*, at 2822 (STEVENS, J., dissenting). Respondent argues that it protects an individual right to possess a firearm unconnected with service in a militia, and to use that arm for traditionally lawful purposes, such as self-defense within the home. See Brief for Respondent 2-4.

(*Heller* at 577.) Stating that "we must determine whether the prefatory clause of the Second Amendment comports with our [the majority's] interpretation of the operative clause" (*Heller* at 595), Justice Scalia relied on "originalist" theory to conclude that in 1789 "It was understood across the political spectrum that the right [to keep guns] helped to secure the ideal of a *citizen* militia, which might be necessary to oppose an oppressive military force if the constitutional order broke down." (*Id*. at 599

(emphasis added).) This then led to Justice Scalia's conclusion with respect to the relationship between the prefatory clause and operative clause: "**We reach the question, then: Does the preface fit with [the] operative clause ...?** It fits perfectly, once one knows the history that the founding generation knew ...." (*Id*. at 598.)

This determination as to whose reading of the Second Amendment established consistency between the prefatory clause and the operative clause was the fulcrum of the *Heller* decision. If Justice Stevens' interpretation of "well regulated militia" had prevailed, the D.C. ban on individual handguns would have been constitutional.

Here, the phrase "protect the Agency and Nationwide against unforeseen conditions" is not susceptible to multiple interpretations. The statement of purpose is clear and unambiguous, and it is equally clear that Nationwide's interpretation of the "necessarily reserved" right to amend or terminate, as an absolute power which may be exercised at will, is not "consistent with the announced purpose." (*Heller* at 578.) The interpretation which is consistent is that Nationwide's authority to amend or terminate the ASC Plan does not extend to purposes inconsistent with protecting Mr. DeVivo and Nationwide from "unforeseen conditions." (APPX A-24).)[1]

[1]This analysis of the *Heller* decision was presented to the district court, both in writing (Mr. DeVivo's July 3, 2019 letter memo (APPX A-58)) and again at the July 17 hearing (Transcript of Proceedings 13:18 - 17:5 (APPX A-109 - A-113).)

c. Sentence #3 of Paragraph 11(h) Does Not Confirm Nationwide's Position on Sentence #2.

Nationwide additionally argues that the third sentence (Sentence #3) of ¶ 11(h), stating that Nationwide may terminate the entire Plan with sixty days written notice, confirms Nationwide's position that Sentence #2 gives Nationwide absolute power to take Mr. DeVivo's Extended Earnings. (Answering Brief, Document 51, Page 29.) Mr. DeVivo addressed this argument in the Opening Brief, repeated here for convenience:

> But Sentence #3 does not convey a separate new power unhinged from the rest of the paragraph. Nationwide's power to "terminate this plan" is conveyed by Sentence #2 and is qualified by the "unforeseen conditions" language in that sentence. Sentence #3 merely adds a 60-day written notice requirement if Nationwide opts to terminate. In any event, Nationwide has not terminated the ASC plan under that provision -- it is simply denying Mr. DeVivo his Extended Earnings because he did not accept Option 1 of the ACE Program.

(Brief for Plaintiffs-Appellants, Document 41, Page 44.)

2. Sentence #4 Of Paragraph 11(h)

Regardless of one's view of Sentences #1 - #3, Nationwide is also breaching Sentence #4 by eliminating "rights ... credited prior to" the phase-out of Mr. DeVivo's Extended Earnings. This issue turns on the definition of the word "credited" as applied to Extended Earnings. At the hearing, the district court asked Nationwide's counsel to explain it:

THE COURT: Well, let me ask you one question about that. I am glad you raised it. That was my second question.

It does say, though, at the end of that sentence, However, the termination -- or rather no change in the plan or termination, however, can alter or modify rights or benefits received or credited prior to such change or modification. So my question relates to the meaning of credited in this context.

I mean, I imagine what you are going to say to me is that a termination can affect the amount of credits that have been accrued, but I think the plaintiff might argue that the termination itself affects the ability of the agency to claim those credits. And isn't that a violation or contrary to 11H?

* * *

MR. LINDSMITH: [ ] But as to extended earnings, that is a totally different formula [from DCIC] and it can only be calculated at the time the agent cancels because it's a 12-month lookback.

THE COURT: Right.

MR. LINDSMITH: So there is no credit. There is no accrual.

THE COURT: Okay.

MR. LINDSMITH: There is no -- nothing has happened with extended earnings.

THE COURT: Right. So there is not accounting until the date of the agency termination is determined?

MR. LINDSMITH: No one even knows what it is, Your Honor.

THE COURT: Right.

And here the only issue being presented by the plaintiff is the extended earnings and not DCIC?

> MR. LINDSMITH: That is the only issue in Counts 1 and 2.
>
> THE COURT: Right. Okay. All right. That explains that, then.

(Transcript of Proceedings 10:16 - 12:12 (A-106 - A-108.) Later, Mr. DeVivo's counsel presented a different view:

> MR. TEDARDS: But the word "credited," which you asked Mr. Lindsmith about, the word "credited" operates here as applying to extended earnings for this reason: Nationwide itself characterizes the extended earnings as deferred compensation. Deferred compensation is their term for extended earnings. And 409A, the IRS provision that Nationwide wants to use to keep from paying this out for some time, even if you take one of the options, 409A's purpose is to regulate NQDC, nonqualified deferred compensation. So it doesn't regulate ERISA, but it regulates these informal plans.
>
> THE COURT: Okay.
>
> MR. TEDARDS: So the definition long established a deferred compensation is compensation that you are entitled to, that you actually have control over, but you choose to defer the receipt of that until later.
>
> Now, if 409A is regulating extended earnings, as Mr. Lindsmith says it does, that means those extended earnings have to be ***deferred compensation***, which Nationwide says it is, and deferred compensation is something that you are ***entitled*** to. You are, in a sense, ***credited*** with it. What should have happened here instead of what Nationwide did, is if it decided that it wanted to terminate Mr. DeVivo, but have the effective date delayed until July 1st, 2020 to follow and be consistent with its approach under 409A and with the definition of deferred compensation, his entitlement should have been frozen at that point like is done with all other deferred compensation plans. So we

> believe that both Sentence Number 2 and Sentence Number 4 have been breached expressly before we get to the covenant part.

(Transcript of Proceedings 17:14 - 18:19 (A-113 - A-114) (emphasis added).)

As Nationwide recites in its Answering Brief, the district court adopted Nationwide's facial explanation, adding that the complexity of the alternative analysis "reinforce[s]" that conclusion:

> [The district court] explained that "credited" is a "fairly clear word" that is "not applicable to the extended earnings, because nothing can be credited until it is actually earned, and nothing can be earned until a date for termination is decided . . . .And I think the lengths to which you have to go to try to explain it that way, to me, reinforce the notion that that is not a plain or fair reading of that actual provision." (Transcript of Proceedings 28:1 - 28:13 (APPX A-124).)

(Answering Brief, Document 51, Pages 31 - 32.)

Nationwide and the district court are mistaken. If Extended Earnings are "non qualified deferred compensation" (NQDC) regulated by 26 U.S. § 409A (Internal Revenue Code ("IRC") § 409A), as Nationwide insists,[2] then Mr. DeVivo is

[2]This conveniently allows Nationwide to delay paying the agents Extended Earnings for years if they accept an ACE option:

> 45. The amount of Mr. DeVivo's Extended Earnings at risk because of Nationwide's "unilateral amendment" is approximately $692,000. Even if Mr. DeVivo were to agree to an early purchase next month to save his Extended Earnings, he would not get the benefit of his Extended Earnings for years. That is because of the restrictions Nationwide has attached to the ACE Options, which range from a minimum of 5 years under Option 1 to virtually

(continued...)

"entitled" to those Extended Earnings, *i.e*. he has "earned" them (to use the court's term) for the work be has performed. *See*, 26 CFR § 1.409A - 1(a)(1) and 1(b):

> **Subsection1(a)(1)**: *nonqualified deferred compensation plan* means any plan ... that provides for the deferral of compensation (within the meaning of paragraph (b) of this section). (emphasis in the original)
>
> **Subsection 1(b):** a plan provides for the deferral of compensation *if*, under the terms of the plan and the relevant facts and circumstances, the service provider [Mr. DeVivo] has a ***legally binding right*** during a taxable year to compensation that, pursuant to the terms of the plan, is or may be payable to ... the service provider [Mr. DeVivo] in a later taxable year. Such compensation is deferred compensation for purposes of Section 409A. (emphasis added)

Nationwide cannot have it both ways. If Extended Earnings are deferred compensation subject to IRC § 409A, Mr. DeVivo has a ***legally binding right*** to those earnings now. If he does not have a legally binding right, then the Extended Earnings are ***not*** deferred compensation and, therefore, are not subject to IRC § 409A.

---

[2](...continued)

> indefinite periods at the other end of the Options. (*Id*.) Nationwide takes the position that IRC § 409A (controlling the payment of non-qualified deferred compensation (NQDC)) applies to Extended Earnings and, because § 409A prohibits payments of NQDC until a complete "separation from service" has occurred, Nationwide states that it will keep Mr. DeVivo's Extended Earnings until he finally escapes from the restrictions years into the future.

(Amended Complaint ¶ 45 (APPX A-18).)

B. IN THE ALTERNATIVE, NATIONWIDE IS BREACHING THE COVENANT OF GOOD FAITH AND FAIR DEALING IN THE AGREEMENT (COUNT 1)

Nationwide argues that its confiscation of Mr. DeVivo's Extended Earnings has not been shown to be "arbitrary" or "irrational," citing two decisions which dismissed implied covenant claims because the "plaintiff did not allege any facts which tended to show that defendants' actions were arbitrary or irrational." (Answering Brief, Document 51, Page 33.) For this purpose, "arbitrary" is defined as "without sound basis in reason and generally taken without regard to the facts," and "irrational" is defined as, among other things, "unreasonable" or "illogical." (*Id*.)

Paragraph 33 of the Amended Complaint, summarizing Nationwide's explanation for taking Mr. DeVivo's Extended Earnings, satisfies both criteria. Nationwide says this was a "separate business decision from our transition from exclusive to independent agent contracts," which Nationwide took because deferred compensation plans "are not part of contracts in the *independent* agent channel." (Amended Complaint ¶ 33 (APPX A-15) (emphasis added).) As noted above at p. 4, that explanation does not even connect or relate to Mr. DeVivo's *exclusive* contract -- the only contract which pays Extended Earnings -- which will remain in force until July 1, 2020. The explanation is obviously "without sound basis in reason" and "illogical."

Nationwide next advances its "reasonable expectations" argument, stating that

Mr. DeVivo could not say, in good faith, that he "reasonably expected deferred compensation to continue indefinitely." (Answering Brief, Document 51, Page 37.) But as explained above at p. 3, Nationwide had the exact same expectation as Mr. DeVivo when the parties entered the contract:

> **[1]** Nationwide hopes and expects to continue the Agency Security Compensation Plan indefinitely, and every effort has been made to meet future conditions.

(Agreement ¶ 11(h), first sentence (APPX A-36).) With that clear statement of intention and expectation from Nationwide, including a "best efforts" type of commitment to address future conditions, with only a narrow proviso to protect *both* parties from "unforeseen conditions," the last thing Mr. DeVivo would expect would be a total confiscation of his Extended Earnings for no purpose other than to enrich Nationwide at his expense.

Nationwide's other "reasonable expectations" argument, that Mr. DeVivo could not have expected the ASC Plan to continue because he had the right to terminate the contract (Answering Brief , Document 51, Page 38), is nonsensical. The fact that a party to an agreement has a right to terminate it does not mean that that party cannot reasonably expect the other party to live up to its obligations while the agreement is in force.[3]

[3]And if the other party does breach, the injured party is entitled to a choice. He can terminate the contract for breach and sue for damages, or he can remain in the contract and seek specific performance. Mr. DeVivo's declaratory and injunctive relief action represents the second choice.

Finally, Nationwide argues that the implied covenant cannot negate its explicit contract right to terminate Mr. DeVivo's Extended Earnings at will. (*Id*. at 38 - 39.) This begs the question whether Nationwide has the right to terminate the Extended Earnings at will. (See the discussion on pp. 4 - 8, *supra*, demonstrating that Nationwide may not unilaterally amend or terminate Mr. DeVivo's Extended Earnings for a purpose inconsistent with protecting Mr. DeVivo and Nationwide from "unforeseen conditions.") But more fundamentally, this argument raises an issue as to exactly what Nationwide's expected "fruits" from this contract are. As this Court explained in *Spinelli v. Nat'l Football League*, 903 F.3d 185, 206 (2d Cir. 2018), the relevant inquiry when a defendant argues that an implied covenant claim would negate another contract right is "whether the implied term that might preserve the fruits of the contract for one party spoils the fruits for another."

Here, Nationwide's hope and expectation at the formation of the contract was to preserve the *quid pro quo* and mutual exchange of consideration at the heart of the contract by continuing the ASC Plan indefinitely, making every effort toward that end. (Agreement ¶ 11(h), first sentence (APPX A-36).) This is what constituted the "fruits" of the contract for both Nationwide and Mr. DeVivo when the contract was formed.

Nationwide's new objective 25 years later, to withdraw its consideration and destroy the *quid pro quo*, is inconsistent with the intention and expectation of the

parties when the contract was formed. Mr. DeVivo's implied covenant claim, aimed at protecting the *quid pro quo* and mutual exchange of consideration, is an attempt to preserve the fruits of the contract that both Nationwide and Mr. DeVivo expected when the contract was formed.

II. COUNT 3 STATES A CLAIM

Count 3 arises from Nationwide's announcement that it will "take the business" of any exclusive agent, including Mr. DeVivo, who does not accept an ACE option, using non-compete and non-solicitation clauses following an at-will termination on July 1, 2020. (Amended Complaint ¶¶ 37 - 42 (APPX A-17).) The essential claim in Count 3 is that the forfeiture provision in Mr. DeVivo's Agreement (¶ 11(f)) would not be enforceable following an at-will termination for refusal to select an ACE option.

The ACE Program is not part of, or contemplated by, the existing exclusive contracts or the independent contracts that Nationwide says it wants the exclusive agents to adopt. (Amended Complaint ¶¶ 61 - 62 (APPX A-21).) It is a separate program invented by Nationwide to: (a) keep former exclusive agents like Mr. DeVivo under Nationwide's control for many years (even though they would be nominally classified as "independent"); (b) delay payment of all components of the ASC Plan for years, until the agent can achieve a final "separation" from Nationwide; and (c) extract funds from the agents. (*Id*., ¶ 6 (APPX A-10), ¶ 45 (APPX A-18), and

Exhibit B thereto (APPX A-39 - A-41) (chart showing restrictions ranging from 5-10 years).)

With respect to the enforceability of the forfeiture provision in Mr. DeVivo's contract following the announced termination on July 1, 2020, Nationwide recognizes the general rule in New York that an otherwise enforceable restrictive covenant is unenforceable where the company terminates without cause and that enforcement of this particular forfeiture for competition provision has been deemed to be "unreasonable as a matter of law" if Nationwide terminates the current Agreement at will. Nationwide has not located any New York decisions that conflict with the essential reasoning of *Cray, op, cit*. Opening Brief at 24 - 25.

Nationwide presents an affirmative defense, however, that an exception to the rule applies because Mr. DeVivo has the opportunity to continue with Nationwide under an independent contract. (Answering Brief, Document 51, Pages 32 - 33.) But Nationwide is not willing to continue with an independent contract unless Mr. DeVivo additionally enters the separate ACE Program, *i.e.*, ***purchases*** the right to function as an independent agent, agrees to ***long-term restrictions*** tying him to Nationwide for many years, and ***foregoes his entire ASC package*** for the duration of those restrictions. That is not a "continuation" of his employment. That is a completely new, predatory business arrangement, which is unrelated to a potential independent agency agreement.

In order to buttress its affirmative defense, Nationwide injected a new argument in its July 11, 2019 Reply letter (six days before the oral argument) that the ACE Program can nevertheless be deemed a continuation of Mr. DeVivo's current employment because, under the current contract, Nationwide is the exclusive owner of Mr. DeVivo's records concerning his clients, also called "policyholder information." From that, Nationwide has deduced that it has the right to exact a price for continued use of the information after the July 1, 2020 termination. (Nationwide Reply letter (APPX A-63).) This claim that Nationwide is the exclusive owner of Mr. DeVivo's policyholder information is insupportable. The fully-integrated Agreement which governs the entire relationship between Mr. DeVivo and Nationwide does not allocate, assign, or even mention ownership of any form of policyholder information, much less allocate ***exclusive*** ownership to Nationwide, which has been confirmed by multiple judicial decisions.

Mr. DeVivo responded to Nationwide's July 11 Reply letter at the July 17 oral argument, pointing out the lack of contractual support for Nationwide's position. The discussion, which resulted in the district court's conclusion that Nationwide owns the policyholder information because it's just in "the nature" of the Agreement, is excerpted in the Opening Brief (Document 41, Pages 31 - 33). At this Rule 12 stage, with no contract provision or extrinsic evidence available for support, the district court had no basis for such a conclusion. *See*, *e.g.*, the excerpts from the *Potter* and

Bland decisions on pp. 21 - 22, *infra.*

A. Mr. Devivo Has Not "Forfeited" Arguments Related To Ownership Of Policyholder Information

Two things are wrong with Nationwide's disingenuous assertion that Mr. DeVivo has forfeited his right to argue the policyholder information ownership issue. (Answering Brief, Document 51, Pages 40 - 46.) First, it is ***Nationwide***, not Mr. DeVivo, who injected this issue into the case in its July 11, 2020 Reply letter, attempting to salvage its affirmative defense to Count 3. Mr. DeVivo is rebutting that affirmative defense, not launching a new claim. Second, Nationwide emphasizes that its claim that it owns policyholder information is irrelevant to Mr. DeVivo's case-in-chief directed to the enforceability of the forfeiture provision after an at-will termination. (*Id*. at 41.) This is technically correct. The forfeiture provision does not protect policyholder information at all. Quite the opposite: the forfeiture provision *presumes* that a departing agent has policyholder information. See, *e.g.*, *Nationwide Mut. Ins. Co. v. Bland*, No. 99-2005, 2004 U.S. Dist. LEXIS 5551, *17-18 (D.Conn. Mar. 30. 2004), *aff'd*, *Nationwide Mut. Ins. Co. v. Mortensen, et al*., 606 F.3d 22 (2d Cir. 2010) (denying Nationwide's motion for summary judgment against exclusive agents who resigned and then used policyholder information to compete, construing this same contract form):

> [T]he forfeiture for competition clause clearly permits departing agents to retain a list of the names of the

> customers they serviced for Nationwide. With customers' names in their rightful possession, agents can obtain policyholder file information directly from the customers and other sources. *Fleming*, No. 99-1417 at 29.

(citing *Nationwide Mut. Ins. Co. v. Fleming*, No. 99-1417, 2001 U.S. Dist. LEXIS 26739, *40 (W.D. Pa. Oct. 2, 2001), also discussed in Mr. DeVivo's Opening Brief, Document 41, Pages 27 - 30.)

Interestingly, Nationwide points out that "Appellants could have brought a claim about ownership if they had wanted to" and notes that "such claims are not foreign to Appellant's counsel who explicitly made a claim about ownership in *Potter*." (Answering Brief, Document 51, Pages 52 - 54.) Nationwide is fortunate that such a claim has thus far been unnecessary in this case,[4] given the decision in *Potter* on Nationwide's motion to dismiss:

> I am left, then, with an Agency Agreement that nowhere employs the term "Book of Business" and does not expressly state that Nationwide owns policyholder data or what that data may include; an Addendum that may or may not have amended the Agency Agreement and may or may not have been supported by consideration; and a series of nonbinding decisions from various state and federal courts interpreting similar but often not identical contractual provisions in circumstances that are not directly in line with the dispute in this case. In their arguments, the parties have also referenced industry practices and how the phrase "Book of Business" is understood in the industry. I find that the Agency Agreement is ambiguous as to what kind

[4]*Potter* was decided on 2018 facts before Nationwide issued its threat to "take their business," so the forfeiture clause was not before the *Potter* court.

> of customer information Nationwide owns and whether its ownership of such information is exclusive. Resolving this ambiguity would require consideration of evidence outside of the Agency Agreement itself. This question therefore cannot be resolved on a Motion to Dismiss. I hold that the plaintiffs have stated a viable claim in Count 3 and will deny the Motion to Dismiss as to that count.

(*Potter Ins. Agency, Inc. v. Nationwide Mut. Ins. Co.*, 374 F. Supp. 3d 572, 582 (W.D. Va. 2019).) The *Bland* decision, construing the same contract, also highlighted the necessity of persuasive extrinsic evidence to back any Nationwide ownership claim based on this contract:

> Nationwide contends that its interpretation of the Agent's Agreement is supported by custom and usage, and it presents an affidavit from an expert witness, Richard Steward, asserting that the exclusive-independent-agency relationship would not be economically feasible if the insurance company was not the exclusive owner of the policyholder information. But a jury would not have to believe this evidence and defendants offer conflicting evidence. Accordingly, Nationwide's motion for summary judgment on these counts must be denied.

(*Bland* at *20 - 21.)

B. Nationwide Cannot Resurrect Its Position By Citing Later Decisions Based On Altered Contracts

As explained in the Opening Brief (at 27), during the 2000s Nationwide began to insert new language into the Agency Agreements. These new insertions into various contract forms were not retroactive, so they have no effect on the DeVivo contract, and the decisions issued in the context of these later-altered contracts are not

relevant and easily distinguishable.

Some discussion of these later decisions is necessary, however, because Nationwide is now citing *Forbes* (again) and six more in its Answering Brief (Document 51, Pages 46 - 48). These decisions simply acknowledge the obvious -- that the newer Agency Agreements now say Nationwide owns the policyholder information. Here is a concise summary:

Fox v. Nationwide (*op. cit.* Answering Brief at 48). This is a fraudulent inducement case. Nationwide had induced Ms. Fox to purchase the right to "service" a set of policies and was refusing to make a refund after it devalued the servicing rights with heavy rate increases. Nationwide attempts to distinguish the right to service policies from its claim that it owns the policies and, in addressing Ms. Fox's demand for a refund, the court stated, incidentally, that "[t]here is no dispute the written RAE Agreement [the title of Ms. Fox's Agency Agreement] expressly provides that Nationwide retains ownership of the policies . . . ." *Fox* at **52.

Garbinski v. Nationwide (*op. cit.* Answering Brief at 47). This is a wrongful termination action arising out of a domestic dispute. In the aftermath of the termination, Mr. Garbinski, another victim of an overpriced purchase of "servicing rights" followed by damaging rate increases, demanded various forms of financial relief. In the factual recitation, the court noted that, under Mr. Garbinski's agency agreement, "Nationwide retained ownership of the policies, with Garbinski having

servicing rights as to those policies." *Garbinski* at *9.

Theiss v. Nationwide (*op cit.* Answering Brief at 48). Mr. Theiss was another victim of an overpriced purchase of servicing rights, who brought claims, *inter alia*, for fraudulent inducement and unjust enrichment. Mr. Theiss had both an RAE Agreement and a regular Agent's Agreement and, in disposing of those claims, the court took note of a paragraph in each. The RAE agreement contributed the following:

> ***Agent Has No Ownership Interest in Policies, Renewals, or Expirations*** - Agent agrees and understands that neither the assignment of these policies' servicing rights nor Agent's obligation to reimburse Nationwide for the value of the assignment of these policies grants Agent, either directly or indirectly, explicitly or implicitly, any ownership interest in the policies, renewals, or expirations of the policies assigned, nor to any of the other policies written with Nationwide during Agent's tenure. (emphasis added)

The regular Agent's Agreement contributed this one:

> Service to Customer Upon Cancellation. ***Consistent with the companies' exclusive use and control of all expirations***, it is understood that upon cancellation of this Agreement, the Companies shall retain the ***exclusive*** right to continue to provide insurance services to any and all customers and to continue to solicit such customers for additional business. (emphasis added)

This is one of the alterations Nationwide made in the 2000s, to help Nationwide in its attempts to put the agents out of business and eliminate competition after termination. Without the word "exclusive," the same paragraph in Mr. DeVivo's

contract simply allows Nationwide to keep its policies in force and compete with Mr. DeVivo after termination. [The *Theiss* alterations are identical to the *Forbes* alterations discussed on pp. 27 - 28 of the Opening Brief.]

Bye v. Nationwide (*op. cit*. Answering Brief at 47 - 48). *Bye* is a wrongful termination case, arising from Mr. Bye's apparent breach of the exclusivity clause in his contracts. Mr. Bye, himself, claimed that Nationwide owned his book of business and used that ownership claim as the basis of his complaint that Nationwide made a profit by "churning" agents, taking a failed agent's business and selling it to a new agent for a higher fee, leaving the "churned" agent in the dust. (*Bye* at *21.) As the court put it, "[p]laintiff conceded, and indeed objected to, the fact that Nationwide 'owned his book of business.'" (*Id.* at *20.)

Kohler v. Nationwide (*op. cit.* Answering Brief at 47) is a termination case in which the terminated agents claimed, *inter alia*, that Nationwide had converted their "books of business" by unilaterally terminating their Agent Agreements. On appeal the Ninth Circuit affirmed summary judgment in favor of Nationwide on the theory that the agents had not satisfied the initial element of a conversion claim -- *exclusive* ownership of the converted asset (at p. *5).

Recognizing that "the Agent's Agreement does not specifically indicate who owns the book of business," the *Kohler* court found that "it contains several provisions that undermine Plaintiff's [exclusive] ownership claims" (at pp. *5 - *6),

which it described as follows:

> First, the Agreement states, "Upon cancellation of this Agreement, it is understood that the companies retain the right to continue to provide insurance services to all of the customers and to continue to solicit such customers for additional business." Second, the Agent's Agreement allows Nationwide to deny benefits to plaintiffs who induce a Nationwide customer to cancel its policies or solicits those customers on behalf of another insurance company. Finally, the Agreement contains a one-year noncompetition agreement that would render Plaintiffs' ownership of the book of business essentially useless. As the district court determined, these provisions are fatally inconsistent with Plaintiffs' claimed right to continue selling insurance to Nationwide policyholders.

(*Kohler v. Nationwide Mut. Ins. Co.*, United States Court of Appeals for the Ninth Circuit (June 22, 1998) No. 97-15807, 1998 U.S. App. LEXIS 13619, *7). These three provisions do not operate the same way in Mr. DeVivo's contract.

First, Paragraph 10 of Mr. DeVivo's Agreement is the same as the provision quoted in the *Kohler* decision, but Paragraph 10 *does not preclude post-termination competition by the agent*. As the *Fleming* court put it, looking at the exact same provision, Nationwide's right to "continue to provide insurance services to any and all customers" and to "continue to solicit such customers for additional business" could not

> [B]e read or understood as prohibiting the [agents] from copying and disseminating such information to others in an effort to induce the policyholders to purchase insurance from carriers that compete with plaintiffs.

Nationwide Mut. Ins. Co. v. Fleming, No. 99-1417, 2001 U.S. Dist. LEXIS 26739, *40 (W.D. Pa. Oct. 2, 2001).

Second, because Nationwide is going to unilaterally cancel Mr. DeVivo's contract at will on July 1, 2020, if he refuses to select an ACE option, the "forfeiture for competition" provision in his Agreement will not be enforceable.

Third, there is no "one-year noncompetition agreement" in Mr. DeVivo's Agreement.

Finally, Mr. DeVivo is not bringing a claim for conversion which requires a showing of *exclusive* ownership. Mr. DeVivo's position, as explained in the Opening Brief, is that this is not an "ownership" contest. Policyholder information is commercial data generated in the ordinary course of business, which is possessed and used by both Mr. DeVivo and Nationwide.

Costanzo v. Nationwide (*op. cit*. Answering Brief at 48) was an action brought by Nationwide exclusive agents in reaction to a computer agreement, seeking a declaration that the computer agreement did not convey ownership of the policies from the agents to Nationwide -- another "exclusive ownership" contest. The trial court, citing *Fleming*, found that the agency agreements did not give Nationwide any property interest in the policies, but that the later computer agreement did give Nationwide an ownership interest.

The appellate court did not disturb the trial court's finding with respect to the

agency agreements but split 2-1 on the computer agreement. The majority, relying on statements in the computer agreement such as "the Nationwide System (hardware, software, manuals, policyholder information and related documentation)" is "proprietary to Nationwide," sided with the trial court. (*Costanzo* ¶ 23.) The third member of the panel disagreed, on the basis of this analysis (emphasis is the Court's):

> {¶35} [If] Nationwide had not already owned the information, it did not receive it as a result of the Computer Agreement. This contract did not transfer anything–it was exclusively concerned with the installation and operation of the computer system.
>
> {¶37} Hidden away in Section 9, entitled "Protection and Security" was this: "You also agree that the Nationwide System (hardware, software, manuals, **policyholder information and related documentation**) are [sic–should be is] the property of and proprietary to, Nationwide or Nationwide's third party vendors, and further agree to protect the Nationwide System (hardware, software, manuals, and related documentation) or any part thereof, from unauthorized use or disclosure. * * *" (Emphasis added.) There were no words of conveyance, and construing the language against the drafter, I would hold that the language meant, at most, that the electronic data stored in the system was Nationwide's property. That would have no bearing at all on the ownership of the underlying information–or on the agent's right to use it.

The minority analysis of the Computer Agreement is consistent with the predominant line of decisions construing the DeVivo contract form.

Forbes v. Nationwide *(op. cit*. Answering Brief at 27 - 29). See Mr. DeVivo's Opening Brief, Document 41, Pages 27 - 29.

CONCLUSION AND REQUEST FOR RELIEF

For the reasons stated here and in the Opening Brief, the district court's threshold dismissal of Mr. DeVivo's Amended Complaint should be reversed and remanded for further proceedings consistent with the reversal.

DATED: November 12, 2019

Respectfully submitted,

/s/ William P. Tedards, Jr.

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CERTIFICATE OF COMPLIANCE

The foregoing **REPLY BRIEF OF PLAINTIFFS-APPELLANTS** complies with the type-volume limitation of Rule 32(a)(7)(B) of the Federal Rules of Appellate Procedure, excluding the parts of the brief exempted by Rule 32(a)(7)(B)(iii), and complies with the typeface requirements of Rule 32(a)(5) and the type style requirements of Rule 32(a)(6).

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/s/ William P. Tedards, Jr.

WILLIAM P. TEDARDS, JR.

CERTIFICATE OF SERVICE

I, WILLIAM P. TEDARDS, JR., hereby certify under penalty of perjury that on November 12, 2019, I caused a copy of the

REPLY BRIEF FOR PLAINTIFFS-APPELLANTS

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