

UNITED STATES DISTRICT COURT FOR THE
EASTERN DISTRICT OF WISCONSIN, MILWAUKEE DIVISION

FEDERAL INSURANCE COMPANY,

Plaintiff,

vs.

Case No. 05-C-0764

VIRCHOW KRAUSE & COMPANY, LLP

Defendant.

ANSWER

Virchow Krause & Company, LLP (hereinafter "VK"), by its attorneys, pleads, moves and answers the complaint herein as follows:

1. The defendant lacks knowledge or information sufficient to form a belief as to the allegations of Paragraph 1 and leave the plaintiff to its proof with respect to those allegations.

2. The allegations of Paragraph 2 make no assertions as to this defendant and require no answer.

3. Defendant's principal place of business is Madison, Wisconsin. The defendant admits the balance of the allegations of subparagraph 3.

3 (a). (The complaint includes two paragraphs identified as No. 3. This subparagraph of the answer pertains to the second subparagraph numbered 3 in the complaint.) The defendant lacks knowledge or information sufficient to form a belief as

to the allegations that the amount in controversy exceeds \$75,000 exclusive of interest and costs and leaves the plaintiff to its proof with respect to those allegations.

4. In answer to Paragraph 4, VK admits that it has offices in the Eastern District of Wisconsin. VK admits that a substantial part of its services to Cape were performed in the Eastern District. Defendant denies that there were “omissions” on the part of VK which give rise to any of the claims asserted in this suit. VK admits that it performed auditing activities and services at the offices of Cape. VK admits that it issued reports regarding Cape’s financial statements, but denies that it issued the financial statements themselves. The financial statements in question are prepared and issued by Cape. VK lacks knowledge or information sufficient to form a belief that the audited financial statements were delivered to Federal through Regional Insurance Agency, Inc. in Milwaukee and leaves Federal to its proof with respect thereto. VK lacks knowledge or information sufficient to form a belief as to the allegation that Federal issued bonds in Milwaukee or that Federal issued bonds in reliance on financial statements audited by VK and leaves Federal to its proof with respect to those allegations.

5. The allegations of Paragraph 5 of the complaint are admitted.

6. VK lacks knowledge or information sufficient to form a belief as to the meaning that the plaintiff attaches to the term “general accounting services” as used in Paragraph 6 and accordingly leaves Federal to its proof with respect to those allegations.

7. VK denies that it audited Cape's accounting records as alleged in Paragraph 7. VK admits that it audited Cape's financial statements for the years indicated and VK admits that copies of its audit reports with Cape's financial statements are attached to the complaint as exhibits. However, VK's audit reports and the attached financial statements did not include any of the handwritten markings found on the exhibits to the complaint. Defendant denies that any of the handwritten entries or notations found on the exhibits to the complaint represent any part of VK's work or representations.

8. Defendant admits the allegations of Paragraph 8.

9. Defendant admits the allegations of Paragraph 9.

10. Defendant admits the allegations of Paragraph 10.

11. In answer to Paragraph 11, VK admits that Federal constitutes a "third party" as to VK, in that VK had no contractual relationship with Federal relative to Cape. VK lacks knowledge or information sufficient to form a belief as to the meaning that the plaintiff attaches to the allegation that third parties like the plaintiff would "rely" upon the financial statements in their underwriting process, decision making as to issuance of bonds and in their decision making as to extending credit and leave Federal to its proof with respect to those allegations.

12. In answer to Paragraph 12, VK denies that it committed negligent acts or that it caused injury to any third party in the performance of its work for Cape.

13. The defendant lacks knowledge or information sufficient to form a belief as to

the allegations of Paragraph 13 and leaves the plaintiff to its proof with respect to those allegations.

14. In answer to Paragraph 14, defendant lacks knowledge or information sufficient to form a belief as to whether the plaintiff relied upon financial statements audited by VK and leaves the plaintiff to its proof with respect to those allegations. Based on the information provided to VK and reasonably relied upon by VK in the performance of its audits, VK believed that the reports that it issued as a result of its audits were appropriate. VK lacks knowledge or information sufficient to form a belief as to the allegations that the financial statements contained numerous material errors with respect to Cape's true financial condition and with respect to the results of operations at the time the financial statements were audited and leaves the plaintiff to its proof with respect to those allegations.

15. In answer to Paragraph 15, VK admits that it did not report or disclose that the financial statements were not in accordance with GAAP as adopted by the American Institute of Certified Public Accountants, because VK believed (and properly so based on the information presented by its client at the time of the performance of the work) that the financial statements did conform to GAAP.

16. Paragraph 16 of the complaint is denied.

17. VK denies that it failed to adhere to GAAP or GAAS in performing its work. VK lacks knowledge or information sufficient to form a belief as to the plaintiff's

meaning in the allegations set forth in subparagraphs (a) through (e) of Paragraph 17 of the complaint and leaves the plaintiff to its proof with respect to each and every allegation set forth therein. To the extent VK understands the allegations of Paragraph 17 and its subparts, those allegations are denied.

18. Based on the information presented by its client and based on the work properly and well performed by VK in the course of its audits, VK concluded that there were no material errors or misrepresentations in the financial statements or its audit reports. VK lacks knowledge or information sufficient to form a belief as to the allegations of Paragraph 18 and leaves the plaintiff to its proof with respect to all allegations set forth therein.

19. The defendant lacks knowledge or information sufficient to form a belief as to the allegations of Paragraph 19 and leaves the plaintiff to its proof with respect to those allegations.

20. Defendant lacks knowledge or information sufficient to form a belief as to the allegations of Paragraph 20 and leaves the plaintiff to its proof with respect to those allegations.

21. In answer to Paragraph 21, the defendant incorporates by reference as if set forth in full its answers to Paragraphs 1 through 20.

22. Paragraph 22 of the complaint alleges law and requires no responsive pleading.

23. Defendant denies the allegations of Paragraph 23.

24. Paragraph 24 of the complaint alleges law and requires no responsive pleading.

25. Paragraph 25 is denied.

26. In answer to Paragraph 26, defendant denies that it breached any duty.

Defendant lacks knowledge or information sufficient to form a belief as to whether Federal has suffered damages in any amount and leaves Federal to its proof with respect to all such allegations, whether it be allegations of past or future damages. Defendant lacks knowledge or information sufficient to form a belief as to the allegation that Federal reasonably relied upon the financial statements and leaves Federal to its proof with respect to those claims

27. In answer to Paragraph 27, the defendant incorporates by reference its answers to Paragraphs 1 through 26.

28. Paragraph 28 alleges law and requires no responsive pleading. To the extent Paragraph 28 alleges fact, the allegations are denied.

29. In answer to Paragraph 29, the defendant alleges that an auditor cannot have complete and perfect knowledge of the validity of information set forth by a client in the client's financial statements. Based on the information presented by the client at the time of performance of the audits, VK believed the financial statements were as reflected in VK's audit reports. VK lacks knowledge or information sufficient to form a belief as to

the allegations that the financial statements audited by VK contained numerous misrepresentations of material fact and leaves the plaintiff to its proof with respect to those allegations. If the financial statements contained numerous misrepresentations of material fact, these were misrepresentations by Cape, not VK.

30. Paragraph 30 is denied.

31. Defendant lacks knowledge or information sufficient to form a belief as to the allegations in Paragraph 31 and leaves the plaintiff to its proof with respect to those allegations.

32. The defendant denies the allegations of Paragraph 32.

33. In answer to Paragraph 33, the defendant incorporates by reference as if set forth in full its answers to Paragraphs 1 through 32.

34. In answer to subparagraph 34, the defendant incorporates by reference its answer to subparagraph 29.

35. Paragraph 35 is denied.

36. Paragraph 36 is denied.

37. Defendant lacks knowledge or information sufficient to form a belief as to the allegations of Paragraph 37 and leaves the plaintiff to its proof with respect to those allegations.

38. In answer to Paragraph 38, the defendant denies that it made any material misrepresentations. Defendant denies that Federal has suffered any damages as a result

of any act or omission to act on the part of the defendant. Defendant lacks knowledge or information sufficient to form a belief as to allegations regarding past and future damages and leaves the plaintiff to its proof with respect to those allegations.

AFFIRMATIVE DEFENSES

39. The plaintiff's claim may be barred by virtue of the plaintiff's failure to exercise reasonable care in the performance of its own duties, which contributory negligence was a cause of any loss claimed by the plaintiff herein.

40. The plaintiff may have failed to mitigate its damages.

41. On information and belief, officers and owners of Cape intentionally misrepresented the true financial condition and circumstances of Cape to VK at the time of performance of these audits. VK reasonably relied upon the honesty and accuracy of Cape's officers, owners and representatives with respect to the presentation of Cape's then-current financial condition and the company's pending work and circumstances. If there were inaccuracies in Cape's financial statements, it was the result of this dishonest and deceitful conduct, not the result of any failure of care on the part of VK.

42. The conduct of Cape's officers, owners and representatives as described hereinabove was the proximate cause of any loss sustained by the plaintiff as claimed herein.

43. The conduct of Cape's officers, owners and representatives as described hereinabove constitutes a superseding cause of any loss the plaintiff may have suffered as

claimed in this litigation.

44. By virtue of the conduct of Cape's officers, owners and representatives as described hereinabove, considerations of public policy bar this claim.

45. The plaintiff has failed to join parties necessary to the adjudication of its claims, as a result of which this suit must be dismissed.

46. On information and belief, the plaintiff solicited Cape's business and received premiums as consideration for the plaintiff's assumption of the risk that Cape would fail in the performance of its contracts thereby obligating the plaintiff to conclude those contracts as set forth in its bonds. Accordingly, the plaintiff has waived the right to assert the claims set forth herein and is estopped from doing so.

47. These claims are barred by the economic loss doctrine.

WHEREFORE, the defendant demands judgment dismissing the complaint and all claims for relief alleged by the plaintiff and demands an award of taxable costs and disbursements.

Dated this 16th day of August, 2005.

BELL, GIERHART & MOORE, S.C.

By: /s/ Ward I. Richter
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