Freedom to Defraud:

Making Michigan Safe for Fraud

By Howard Yale Lederman

Mr. Paul Brondyke was a longtime Midwestern United Life Insurance Company (MULIC) policyholder. In 1988, he applied to change his policy. He understood that MULIC's agent had "represented that his premiums would be approximately $1,600 per quarter and would remain level."[1] After issuing the modified insurance policy, MULIC told him that he needed to pay a higher premium or his policy would lapse. Refusing, he sued MULIC. When MULIC moved for summary disposition based on the policy's integration clauses and the parol evidence rule, the trial court granted the motion.

MORE ▶

Affirming, the Michigan Court of Appeals explained in *Brondyke v Midwestern United Life Ins Co* that the "plain language" of the integration clauses in the policy showed the parties' intent that "the policy and the application…constitute the final and complete expression of their agreement. Contrary to [Mr. Brondyke's] assertions, they explicitly state that only terms included in either the application or the policy constitute part of the contract."[2] Since the agent's promises were not in the policy or application, they were not in the contract. Thus, the integration clauses nullified them, and Mr. Brondyke lost his life insurance policy.

Brondyke exemplifies how Michigan appellate courts, through conclusive construction of integration clauses, rigid application of the parol evidence rule, and severe limitation of the rule's *exception* for fraud in the inducement, have made Michigan safe for fraud. Fraud is exploiting another person's confidence in you as a person, in your product, and in your service. "'[I]t poisons alike the contract of the citizen.'"[3]

Many attorneys learned the well-known maxim that "[f]raud vitiates every transaction."[4] As Professor Williston emphasized, "'Fraud vitiates and avoids all human transactions from the solemn judgment of a court to a private contract.'"[5] Not so.

Under the parol evidence rule, oral and written "'evidence of contract negotiations, or of prior or contemporaneous agreements that contradict or vary the written contract, [are] not admissible to [contradict or] vary the terms of a contract which is clear and unambiguous.'"[6] "'The practical justification for the rule lies in the stability that it gives to written contracts; for otherwise either party might avoid his obligation by testifying that a contemporaneous oral agreement released him from the duties that had simultaneously assumed in writing.'"[7] However, the rule arose not to shield fraud, but to combat it.[8] "Commercial parties should be entitled to rely on the representations their contractual partners make. Indeed, the stability of commercial relationships depends on such trust, and the legal rules governing those relationships should foster it."[9] Nonetheless, Michigan appellate courts have used the rule and the "integrated contract" to bar proof of fraud, thereby facilitating fraud.[10]

Fast Facts:

Under Michigan law, a contract's integration clause triggers the parol evidence rule.

This integration clause/parol evidence rule combination protects most contracts from fraud attack.

By severely restricting the fraud-in-the-inducement exception to this combination, Michigan appellate courts have made Michigan safer for fraud.

Professor Corbin renamed the parol evidence rule the "rule against contradicting integrated writings" because the rule bars oral and written evidence contradicting integrated contracts.[11] Thus, an integration or merger provision is an essential condition for the rule to apply. "The purpose of an integration clause is to invoke the parol evidence rule."[12] More and more contracts contain integration provisions.[13] An integration provision is a provision declaring "in express terms that it contains the entire agreement of the parties" and that unincorporated precontract agreements or understandings do not survive contract execution.[14] Here is an example:

> THIS AGREEMENT CONSTITUTES THE ENTIRE AGREEMENT BETWEEN THE PARTIES....The preambles and exhibit(s) are part of this Agreement, which constitutes the entire understanding and agreement of the parties, and there are no other oral or written understandings or agreements between the Company and You relating to the subject matter of this Agreement. Any representation(s) not specifically contained in this Agreement made prior to entering into this Agreement do not survive subsequent to the execution of this Agreement.[15]

Although Michigan appellate courts have recognized a fraud-in-the-inducement exception to the parol evidence rule, most pre-1998 cases did not involve integration clauses.[16] "'Fraud in the inducement, however, addresses a situation where the claim is that one party was tricked into contracting.'"[17] "Fraud in the inducement presents a special situation where parties to a contract appear to negotiate freely…but where in fact the ability of one party to negotiate fair terms and make an informed decision is undermined by the other party's fraudulent behavior."[18]

Nonetheless, recent Michigan decisions have practically nullified the exception. Leading the way is *UAW-GM Human Resources Ctr v KSL Recreation Corp* (*UAW-GM*).[19] Plaintiff UAW-GM Human Resources Center contracted with Carol Management Corp (CMC) to use CMC's resort property for a convention. Their contract included an integration provision. The contract did not require that CMC's employees be union employees. But UAW-GM asserted that it had signed the contract on the basis of CMC's oral promises "to provide [UAW-GM] with a union-represented hotel."[20] CMC sold the property to KSL Recreation Corp, which replaced the union employees with nonunion employees. Upon learning of this substitution, UAW-GM canceled the agreement and sued KSL for breach of contract, conversion, and fraud.[21] The lower court granted UAW-GM summary disposition.

The Court of Appeals defined the issue as whether, when a contract includes an integration clause, courts can consider parol evidence in determining whether the contract is integrated and saw the issue as one of first impression in Michigan.[22] The Court held that an integration clause "is conclusive" and that "parol evidence is not admissible to show that the agreement is not integrated," except when fraud "invalidate[s] the integration clause."[23] The Court quoted sections of Williston and Corbin stating that integration provisions are conclusive.[24] In *Van Pembrook v Zero*

Mfg Co, the Court of Appeals had held that an integration clause does not bar evidence of prior or contemporaneous agreements not interfering with the contract terms.[25] The *Van Pembrook* Court had reasoned that such evidence was admissible, because it did not contradict or vary the contract terms, but only showed the circumstances of the contract's formation.[26] However, the *UAW-GM* Court rejected *Van Pembrook* and severely limited the fraud exception. The Court concluded that "a contract with a merger clause nullifies all antecedent claims," including fraud claims arising from unincorporated precontract agreements and statements inducing a party to contract.[27] Parol evidence of these agreements and representations "would vary the terms of the contract."[28] The Court declared that its conclusion honored and implemented the parties' decision to include an integration provision in their contract.[29] As the contract was integrated, and the promises varied from the contract provisions, evidence of the agreement regarding union employees was inadmissible.

Therefore, the Court almost abrogated the fraud exception: Vitiation of a contract with an integration clause could occur only when the integration clause itself arose from fraud or when the entire contract arose from fraud.[30] Moreover, the Court narrowed the second prong necessary to establish fraud: The plaintiff must not only show an incorporated precontract agreement or representation, but must also show that the defendant induced him or her to suppose that the contract incorporated the agreement or representation, or "to execute an incomplete writing, while describing it as complete, the written provision may be voidable on the ground of fraud."[31]

Thus, the Court dismissed the plaintiff's fraud claims because the "'plaintiff made no allegations of fraud…invalidat[ing] the contract or merger clause itself.'"[32] Moreover, the fraud claims "require[d] reliance on a misrepresentation….Here, the merger clause made it unreasonable for plaintiff's agent to rely on any representations not included in the letter of agreement."[33]

In its decision, the *UAW-GM* Court ignored other parts of the same sections of Corbin that it had cited and quoted, such as:

> [O]ral testimony is admissible to prove fraud....This is so, even though the testimony contradicts the terms of a complete integration in writing....
>
> * * *
>
> [F]raud in the inducement of assent...may make the contract voidable without preventing its existence, and without showing that the writing was not agreed on as a complete integration of its terms. In such case the offered testimony may not vary or contradict the terms of the writing, although it would be admissible even if it did so; it merely proves the existence of collateral factors that have a legal operation of their own. One that prevents the written contract from having the full legal operation that it would otherwise have had. This is not varying or contradicting the written terms of agreement, although it does vary or nullify in part their legal effect.[34]

Additionally, the Court misinterpreted the parties' intent in including an integration provision. Their intent was not to nullify precontractual understandings or agreements inducing them to contract or to abridge their rights to sue for fraud. Rather, their intent was to contract in accordance with their understandings and agreements and to preserve their rights to sue for fraud. Their intent was not to surrender unnamed rights, but to define their benefits and responsibilities.

Therefore, the Court of Appeals has almost eliminated the fraud exception to the parol evidence rule. By definition, fraud in the inducement involves precontract fraudulent concealment or representations that are contrary to or different from the contract provisions. Indeed, fraud in the inducement involves enticing prospects with promises when the promissor intends to keep the promises out of the contract. Few fraudulent inducement claims can survive execution of a contract containing an integration provision.

In fact, the Court's decision rewards fraud. The decision promotes deceit. The decision also disrupts the trust essential for nonfraudulent business relationships. The Court ignored that fraudulently induced contracts do not deserve to survive. Instead, they should be reformed or abrogated. Thus, the Court has made Michigan safer for fraud.

The question has arisen whether remedial statutes, like the Michigan Consumer Protection Act (MCPA),[35] the Michigan Franchise Investment Law (MFIL),[36] and the Michigan Uniform Securities Act (MUSA),[37] override or restrict *UAW-GM*. "The MCPA is a remedial statutory scheme designed 'to prohibit unfair practices in trade or commerce and must be liberally construed to achieve its intended goals.'"[38] However, the MCPA has several large exceptions, and the Michigan Supreme Court has interpreted the exception for specifically authorized transactions or conduct[39] broadly, thereby severely limiting the MCPA's reach.[40] Further, the Michigan Court of Appeals has applied *UAW-GM* in the only known MCPA appellate case involving a parol evidence issue.[41] The MFIL's purpose is "to remedy perceived abuses by large franchisors engaged in manipulating, coercing or lying to unsophisticated investor franchisees."[42] Nevertheless, the Michigan Court of Appeals has applied *UAW-GM* to a recent MFIL appellate case involving a parol evidence issue.[43] The MUSA's purpose is to bar the "sale of [unregistered] securities to protect the public against fraud and deception in issuance, sale, exchange, or disposition of

Fraud in the inducement involves enticing prospects with promises when the promissor intends to keep the promises out of the contract. Few fraudulent inducement claims can survive execution of a contract containing an integration provision.

securities."[44] I am not aware, however, of any Michigan appellate case involving MUSA and parol evidence issues. As for federal statutes, the Employee Retirement Income Security Act (ERISA) is a remedial statute: "Congress enacted ERISA to 'protect…the interests of participants in employee benefit plans and their beneficiaries.'"[45] Nonetheless, the Sixth Circuit Court of Appeals has extended the parol evidence rule-integration provision combination to ERISA release agreements.[46] Accordingly, remedial statutes do not limit the destructive effect of *UAW-GM*. ■

Howard Yale Lederman is an officer and Publications Committee co-chairperson of the State Bar of Michigan Antitrust, Franchising, and Trade Regulation Section. He is also a charter member of the State Bar Appellate Practice Section. He practices mainly appellate, commercial, and employment litigation with Norman Yatooma & Associates, PC, in Birmingham, Michigan. Several Michigan publications have published his appellate, commercial, and employment law articles and updates.

FOOTNOTES

1. *Brondyke v Midwestern United Life Ins Co,* unpublished opinion per curiam of the Michigan Court of Appeals, issued August 4, 2005 (Docket No. 252859), p 1.
2. *Id.* at 2.
3. 12 Williston, Contracts (3d ed), § 1486, pp 321–322.
4. *Id.;* see also Story, *A Treatise on the Law of Contracts* (1972 reprint of 1844 ed, Arno Press, Inc.), § 165, p 105.
5. 12 Williston, § 1486, pp 321–322.
6. *UAW-GM Human Resources Ctr v KSL Recreation Corp,* 228 Mich App 486, 492; 579 NW2d 411 (1998) (*UAW-GM*), lv den 459 Mich 945 (1999), quoting *Schmude Oil Co v Omar Operating Co,* 184 Mich App 574, 580; 458 NW2d 659 (1990); see also *Archambro v Lawyers Title Ins Corp,* 466 Mich 402, 413–414; 646 NW2d 170 (2002); *Hutchinson v Westbrook,* 191 Mich 484, 489; 158 NW 135 (1916); *Lake Erie Land Co v Chilinski,* 197 Mich 214, 218; 163 NW 929 (1917); 6-26 Corbin, Contracts (LexisNexis interim ed, 2002), § 573, p 572.
7. *UAW-GM,* 228 Mich App at 492.
8. See 6 Corbin, supp to § 572C, p 89; 11 Williston, Contracts (West Group, 2004), § 33:1, pp 540–550; *In re Frost Estate,* 130 Mich App 556, 562; 344 NW2d 331 (1983).
9. *Robinson Helicopter Co, Inc v Dana Corp,* 34 Cal 4th 979, 996–997; 22 Cal Rptr 3d 352; 102 P3d 268 (2004) (Wedegar, J., dissenting).
10. See, e.g., *UAW-GM,* 228 Mich App at 502–507; *Fleet Business Credit, LLC v Krapohl Ford Lincoln Mercury Co,* unpublished opinion per curiam of the Michigan Court of Appeals, issued September 28, 2004 (Docket No. 249825); *Brondyke,* p 2.
11. 6 Corbin, supp to § 572C.
12. Davis & Reichman, *Understanding the value of integration clauses,* 18 Franchise L J 135, 136 (Spring 1999); see also 11 Williston, § 33.14, p 614.
13. *UAW-GM,* 228 Mich App at 496.
14. 6 Corbin, § 578, p 111; see also 11 Williston, § 33.14, p 612.
15. Example from franchise agreement between Haircolorexpress International, LLC and Raphael and Teresa Betanzos, May 14, 2003; see also *Hamade v Sunoco, Inc. (R&M),* 271 Mich App 145, 168; 721 NW2d 233 (2006) (quoting integration provision); *Cook v Little Caesar Enterprises, Inc,* 972 F Supp 400, 403–404 (ED Mich, 1997), aff'd 210 F3d 653 (CA 6, 2000) (quoting integration provision).
16. See, e.g., *Chilinski,* 197 Mich App at 218–219; *Schupp v Davey Tree Expert Co,* 235 Mich 268, 271; 209 NW 85 (1926); *Rood v Midwest Matrix Mart, Inc,* 350 Mich 559, 564–567; 87 NW2d 186 (1957); *NAG Enterprises, Inc v All State Industries, Inc,* 407 Mich 407, 411; 285 NW2d 770 (1979). Contra *Van Pembrook v Zero Mfg Co,* 146 Mich App 87, 98; 380 NW2d 60 (1985).
17. *Huron Tool & Engineering Co v Precision Consulting Services, Inc,* 209 Mich App 365, 371; 532 NW2d 541 (1995), quoting *Williams Electric Co, Inc v Honeywell, Inc,* 772 F Supp 1225, 1237–1238 (ND Fla, 1991); see also Story, A Treatise On The Law Of Contracts (5th ed) (Little, Brown & Co. 1874), § 520, p 797.
18. *Huron,* 209 Mich App at 372–373.
19. *UAW-GM,* n 6 *supra.*
20. *UAW-GM,* 228 Mich App at 489.
21. *Id.* at 493.
22. *Id.*
23. *Id.* at 502.
24. *Id.* at 493–494, quoting 4 Williston, Contracts (4th ed, 1990), § 633, p 1014, and 3 Corbin, Contracts (interim ed, 1979), § 578, pp 402–411.
25. *Van Pembrook v Zero Mfg Co,* 146 Mich App 87; 380 NW2d 60 (1985).
26. *Id.* at 98.
27. *UAW-GM,* 228 Mich App at 502.
28. *Id.*
29. *Id.* at 496.
30. *Id.* at 503, citing what is now 6 Corbin, § 578.
31. *UAW-GM,* 228 Mich App at 503.
32. *Id.* at 505.
33. *Id.* at 504–505.
34. 6 Corbin, § 580, pp 136, 142.
35. MCL 445.901 *et seq.*
36. MCL 445.1501 *et seq.*
37. MCL 451.501 *et seq.*
38. *Newton v Bank West,* 262 Mich App 434, 437; 686 NW2d 491 (2004), quoting *Forton v Lazar,* 232 Mich App 711, 715; 609 NW2d 850 (2000).
39. MCL 445.904(1).
40. *Smith v Globe Life Insurance Co,* 460 Mich 446, 465; 597 NW2d 28 (1999); see also *Newton,* 262 Mich App at 438–439.
41. *Mazey v Cubba,* unpublished opinion per curiam of the Michigan Court of Appeals, issued February 15, 2000 (Docket No. 210978).
42. *Jerome-Duncan, Inc v Auto-By-Te, LLC,* 989 F Supp 838, 842 (ED Mich, 1997), citing Michigan House Legislative Analysis, HB 4203, August 2, 1974; see also *Geib v Amoco Oil Co,* 29 F3d 1050, 1056 (CA 6, 1994).
43. *Hamade,* 271 Mich App at 166–172.
44. *Ansorge v Kellogg,* 172 Mich App 63, 67; 431 NW2d 402 (1988); see also *People v Dempster,* 396 Mich 700, 704; 242 NW2d 381 (1976); *Noyd v Claxton, Morgan, Flockhart & Van Liere,* 186 Mich App 333, 338; 463 NW2d 268 (1990).
45. *Aetna Health, Inc v Danila,* 542 US 200, 208; 124 S Ct 2488; 159 L Ed 2d 312 (2004), quoting 29 USC 1001(b).
46. *Astor v Int'l Business Machines Corp,* 7 F3d 533, 539–540 (CA 6, 1993).