

NO. A06-2133

State of Minnesota
In Supreme Court

Auto-Owners Insurance Company,

Appellant,

v.

Jason George,
Progressive Insurance Company,
Daniel Evenson and Melissa DesMarais,

Respondents.

APPELLANT AUTO-OWNERS INSURANCE COMPANY'S
REPLY BRIEF TO RESPONDENT AND AMICUS CURIAE

Warren V. Bigelow, Jr. (#8229)
Merrick B. Williams (#300664)
1000 Superior Boulevard, Suite 304
Wayzata, MN 55391
(952) 475-4000

Attorneys for Respondent
Jason George

Theodore J. Smetak (#102155)
ARTHUR, CHAPMAN, KETTERING,
SMETAK & PIKALA, P.A.
500 Young Quinlan Building
81 South Ninth Street
Minneapolis, MN 55402
(612) 339-3500

Attorneys for Respondent
Progressive Insurance Company

James A. Reding, Jr. (#195352)
Amanda J. G. Karls (#0346469)
REDING & PILNEY
8661 Eagle Point Boulevard
Lake Elmo, MN 55042
(651) 702-1414

Attorneys for Appellant
Auto-Owners Insurance Company

Paul D. Peterson (#203919)
Lori L. Barton (#332070)
HARPER & PETERSON, P.L.L.C.
3040 Woodbury Drive
Woodbury, MN 55129-9617
(651) 738-8539

Attorneys for Amicus Curiae
Minnesota Association for Justice

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REPLY ARGUMENT

Introduction

Throughout the litigation and appeal of this matter, Respondent Jason George (“Respondent”) has employed a range of shifting legal theories in a thinly-veiled attempt to distract bench and bar from the central concern of this appeal:

Whether Respondent forfeited his underinsured motorist (“UIM”) claim when he abrogated his UIM carrier’s subrogation rights by arbitrating with and releasing the tortfeasors, while a) representing to his UIM carrier that the arbitration was a binding conclusion to a tort action, and b) failing to provide proper notice of either a binding arbitration as required by Malmin v. Minnesota Mutual Fire and Casualty Company or meaningful notice of a settlement as required by Schmidt v. Clothier and American Family Mutual Insurance Company v. Baumann?

Rather than squarely address the issues on their merits, in his Brief to this esteemed Court, Respondent misstates the facts and presents another new legal theory. Simply stated, none of the averments or arguments presented in Respondent’s brief can alter the fact that his actions have prejudiced Auto-Owners Insurance Company (“Auto-Owners”) by releasing the tortfeasors without adequate notice to the insurer.

Likewise the arguments presented by Amicus Curiae (“Amicus”) are not instructive with regard to this particular matter. Their general framing of the law does not account for the type of situation presented here. Moreover, if Respondent were to be

granted the relief Amicus urges, such a precedent would promote the use of intentionally vague and misleading arbitration notices and perpetuate misuse of the claims process.

As set forth more fully *infra* and in Auto-Owners' initial Brief to this Court, Auto-Owners respectfully requests that this Court reverse the holding of the Minnesota Court of Appeals and hold in accordance with the trial court by dismissing Respondent's claims and affirming summary judgment in favor of Auto-Owners.

I. Given that Respondent Did Not Inform Auto-Owners He Had Reached a Proposed Settlement, Respondent Has Failed to Provide Proper Notice Pursuant to Schmidt v. Clothier.

In his Brief, Respondent presents five main arguments. See Respondent George's Minnesota Supreme Court Brief. Although not so clearly-framed, the first is Respondent's argument in support of the Court of Appeals' finding that he reached and provided Auto-Owners with adequate notice of a settlement. See Id. at 8-12. Respondent cites to language from the Binding Arbitration Agreement he entered into with Melissa DesMarais, Daniel Evenson and Farm Bureau Insurance Company ("Binding Arbitration Agreement") in support of that position. Id. While, Auto-Owners maintains that the language of the arbitration agreement itself is dubious with respect to its intended effect,¹ even assuming it was Respondent's intent to obtain a settlement offer

¹ The intent to treat the agreement as binding is evidenced by the heading of the Binding Arbitration Agreement which contains the words "binding," "release of insurer," and "elimination of personal liability of Respondents." See App. A 90. Furthermore, the body of the Binding Arbitration Agreement provides, in part, for release of DesMarais and Evenson from personal liability and invokes the settlement principles of Loy, Tiegen, and Drake. See App. A 82-83; and A 91, 93 (citing Loy v. Bunderson, 320 N.W.2d 175

and such intent was clearly reflected in the arbitration agreement, that intent was not conveyed to Auto-Owners. See App. A. 97, 100.

Respondent contends that Auto-Owners knew that by substituting its draft, it could set aside the arbitration and preserve its subrogation rights, but elected not to substitute and acquiesced to the settlement. See Respondent George's Minnesota Supreme Court Brief at 11. However, at no time has Respondent articulated why—without being provided a copy of the agreement and in light of Respondent's representations that the arbitration was binding—Auto-Owners could have reasonably concluded Respondent was merely attempting to obtain a settlement offer.

Respondent also relies on language, quoted out of context, from Auto-Owners' May 3, 2005 letter referring to the settlement notice requirements necessary pursuant to Schmidt v. Clothier. Id. at 1-2, 11; Schmidt v. Clothier, 338 N.W.2d 256 (Minn. 1983). However, this language only demonstrates that Auto-Owners, for its part, understood the difference between the normal procedures followed in the context of a settlement offer versus a binding arbitration. Compare American Family Mut. Ins. Co. v. Baumann, 459 N.W.2d 923 (Minn. 1990) and Schmidt, with Malmin v. Minn. Mut. Fire & Cas. Co., 552 N.W.2d 723 (Minn. 1996)). Any doubt Auto-Owners may have otherwise had with respect to Respondent's clearly stated intent to bind Auto-Owners to his arbitration award was quelled by Respondent's reply letter sent the same day, in which Respondent advised: "We intend to go forward with tomorrow's arbitration since proper and timely

(Wis. 1982); Tiegen v. Jalco of Wisconsin, Inc., 367 N.W.2d 806 (Wis. 1985); and Drake v. Ryan, 514 N.W.2d 785 (Minn. 1994)).

Malmin notice was served. We will serve a Notice of Arbitration Award is [sic] as soon as we receive it. We intend to bind Auto-Owners with the result.” See App. A 100. This letter, without the inclusion of the Binding Arbitration Agreement for evaluation by the insurer and in light of the context of Respondent’s prior correspondence, clearly conveyed to Auto-Owners that respondent was proceeding with binding arbitration.

Rather than acknowledge his pre-arbitration communications with Auto-Owners as blatant attempts to convey notice of a purportedly binding arbitration, Respondent simply dismisses these communications as “Schmidt notices,” and amusingly postures they were “admittedly meaningless and unnecessary.” See App. A. 97, 100; Respondent George’s Minnesota Supreme Court Brief at 11.

Given Respondent’s conduct and Auto-Owners’ reasonable reliance on that conduct, the trial court properly analyzed Respondent’s notice of the arbitration pursuant to the requirements set forth in Malmin v. Minnesota Mutual Fire & Casualty Insurance Company and concluded Respondent’s notice was inadequate. See App. A. 39, 48, 59-60, 62 (citing e.g., Malmin). As set forth in Kluball v. American Family Mututal Insurance Company, this lack of adequate notice creates a rebuttable presumption that Auto-Owners has been prejudiced by its inability to protect its subrogation rights and that Respondent’s UIM claims have been forfeited. See Auto-Owners Minnesota Supreme Court Brief at 37 (citing Baumann and Kluball v. American Family Mut. Ins. Co., 706 N.W.2d 912 (Minn. Ct. App. 2005)).

Amicus urge that proper Schmidt notice may follow proper Malmin notice without prejudice to the UIM carrier and present hypothetical scenarios in support of that

position. See Amicus Curiae's Minnesota Supreme Court Brief at 11-13. Although the hypothetical issues presented by Amicus are not before this Court, Auto-Owners recognizes that there may be validity to Amicus' position under some circumstances.² However, as explained *infra*, at no time was Auto-Owners provided with meaningful notice of a settlement offer. See *infra* at 13. Rather, Respondent attempted to mislead Auto-Owners in an effort to bind Auto-Owners to the result of the arbitration. Interestingly, Amicus do not present a hypothetical scenario that is analogous to the facts of this case because not even Amicus can endorse Respondent's conduct.

Amicus also suggest that the holding in Kluball v. American Family Mutual Insurance Company should be reversed to the extent it permits forfeiture of a UIM claim where a claimant has provided faulty or nonexistent Malmin notice when the UIM carrier's subrogation rights are not compromised. See Amicus Curiae's Minnesota Supreme Court Brief at 13 (citing Kluball and Malmin). Auto-Owners contends that permitting Respondent to continue to pursue his UIM claim after engaging in manipulative notice conduct would taint the claims system and spawn misuse of the judicial resources of this state.

² Notwithstanding the forgoing, Auto-Owners argues that even to the extent case law implies that UIM claimants and tortfeasors may reach a settlement following a verdict or binding arbitration, such case law also disallows parties from using a Schmidt notice as a mechanism for subsequently compromising the UIM carrier's subrogation rights. See, e.g., Moundson v. Bitzan, 588 N.W.2d 169, 172 (Minn. Ct. App.1999) ("[t]he procedure outlined in Schmidt was not intended to allow a tortfeasor to limit its liability by waiting until a verdict is rendered, offering to settle with the injured insured for the amount of that verdict, and defeating the UIM carrier's subrogation rights when it fails to respond to notice of that settlement under Schmidt").

Specifically, adoption of Amicus' position would encourage UIM claimants to provide vague and/or misleading notice so as to surreptitiously settle with their tortfeasor while leading their UIM carrier to believe their arbitration will be treated as a binding conclusion to a tort action. Such ambiguity and manipulation would, as this case demonstrates, circumvent the purpose of alternative dispute resolution and necessitate protracted litigation to determine the actual intent and effect of otherwise straightforward arbitration proceedings. The resulting tax on party and state judicial resources must not be tolerated. As such, a clear message must be sent to UIM claimants that their claims may be forfeited by virtue of their own misconduct.

However, even setting aside these reasons, it is clear that permitting Respondent to pursue his UIM claim here would result in prejudice to Auto-Owners. Id. As in Kluball, the instant case presents a scenario where the UIM claimant has compromised the UIM carrier's subrogation rights by releasing the tortfeasors without first providing proper notice of a settlement. Kluball at 918 (In Kluball the court found that Schmidt notice was provided to the UIM carrier, but not until after the tortfeasor was released. Here meaningful Schmidt notice was never provided.). Although Auto-Owners is not bound to the arbitration award, as Amicus, the Court of Appeals and the trial court correctly concluded, the fact remains that Respondent's actions caused Auto-Owners to evaluate the arbitration as a binding conclusion to a tort action, and thereby denied Auto-Owners of a meaningful opportunity to evaluate and protect its subrogation rights. Accordingly, Auto-Owners rights have been prejudiced because it can never subrogate against the tortfeasors to recover UIM payments to Respondent. Respondent has not presented

evidence to refute this conclusion. As such, Auto-Owners respectfully requests that this Court reverse the holding of the Minnesota Court of Appeals and hold in accordance with the trial court.

II. Auto-Owners Has Not Modified Its Legal Arguments on Appeal, Except to the Extent Necessary to Address Respondent's Shifting Legal Theories.

Respondent contends that it was Auto-Owners, not Respondent, that changed its legal theory on appeal. In support of this argument, Respondent has presented this esteemed Court with inaccurate statements set forth as fact in his Brief. Specifically, Respondent contends that, in its Answer to Respondent's Complaint, Auto-Owners acknowledged Respondent's decision to arbitrate was an effort to obtain a settlement offer, but changed its position on appeal to contend the arbitration was characterized as a binding conclusion to a tort action. See Respondent George's Minnesota Supreme Court Brief at 6, 12. Respondent also avers that "everybody," including Auto-Owners knew the arbitration was "nothing more and nothing less than an effort to obtain a best settlement offer." See Respondent George's Minnesota Supreme Court Brief at 5, 13.

As set forth *supra*, Respondent represented the arbitration as a binding conclusion to a tort action up until appeal of this matter and Auto-Owners reasonably relied on that characterization. In its Answer, Auto-Owners acknowledged that it was served with a "Schmidt v. Clothier Notice." See App. R. 31 (referring to paragraph IX at App. R. 29). However, such an acknowledgment only confirmed that Auto-Owners had in fact received a document from Respondent which was labeled as such. Acknowledgement of

service in no way amounted to an acknowledgement that the document provided “proper” notice of a settlement, as Respondent contends. See Respondent George’s Minnesota Supreme Court Brief at 3. Likewise, while Auto-Owners sent a facsimile message to Respondent advising that Auto-Owners would not substitute its draft, despite Respondent’s contentions, that correspondence in no way validated Respondent’s purported Schmidt notice. See Respondent George’s Minnesota Supreme Court Brief at 2 (referring to App. R. 25.). There was never a reason for Auto-Owners to substitute its draft—an option that must be offered to a UIM insurer pursuant to Schmidt v. Clothier in the event of a settlement—because Respondent represented he had reached a binding conclusion to his tort claim. Schmidt.

After filing its Answer, Auto-Owners brought its Notice of Motion for Summary Judgment based on Respondent’s failure to provide proper Malmin notice of the arbitration and the resulting prejudice to Auto-Owners created by Respondent’s destruction of Auto-Owners’ subrogation rights. See App. A 20-38. On appeal, Auto-Owners argued that the District Court properly granted its motion for summary judgment when it held that Auto-Owners was prejudiced by Respondent’s ineffective Malmin notice and found that Respondent had forfeited recovery under his UIM policy. See Auto-Owners’ Brief to the Minnesota Court of Appeals at 19-21. However, in light of Respondent’s new argument on appeal that the arbitration was merely a means to a best settlement, Auto-Owners was required to emphasize that Respondent forfeited his UIM coverage when he released the tortfeasors without first giving meaningful Schmidt notice. Id. at 22-25.

While Auto-Owners has been forced to modify its legal arguments to address Respondent's shifting legal theories, Auto-Owners has consistently maintained that Respondent forfeited his UIM claim when he abrogated Auto-Owner's subrogation rights by arbitrating with and releasing the tortfeasors while conveying the arbitration as a binding conclusion to a tort action and failing to provide proper notice of a binding arbitration or meaningful notice of a settlement. Respondent's accusation that it was Auto-Owners, not Respondent, that changed its legal theory on appeal is wholly unfounded and is not deserving of further consideration by this Court.

III. Respondent's Post-Trial Argument That He May Recover Against Auto-Owners Based on a Default Judgment Obtained Against the Tortfeasors Is Unfounded and Should Not Be Entertained Here on Appeal.

From the time he first provided notice of the arbitration through the time this case was heard and decided by the trial court, Respondent represented that he intended to or had arbitrated his claims to a conclusion that was binding against the tortfeasors and his UIM carrier, Auto-Owners. See e.g., App. A 3-4, 14-16, 97, 100. The Honorable Thomas W. Wexler agreed that Respondent had obtained an arbitration award that was binding against the tortfeasors. See App. A 49, 53, 56. However, because Respondent had failed to demonstrate he provided proper notice to Auto-Owners, Respondent failed to demonstrate Auto-Owners could be bound by it. See App. A 39-40, 56. Moreover, because Respondent had not overcome the presumption that Auto-Owners had been prejudiced by his course of action, Judge Wexler held Respondent had forfeited his UIM claim. See App. A. 39, 48, 59-60, 62 (citing e.g., Kluball and Malmin).

At the Court of Appeals, Respondent continued to argue the arbitration award was somehow binding on Auto-Owners on the basis of the notice principles set forth in Malmin v. Minnesota Mutual Fire and Casualty Company, while raising a new theory that he had merely reached a settlement with the tortfeasors. See Respondent George's Brief to the Minnesota Court of Appeals at 9, 26-29. The Court of Appeals agreed with Respondent's characterization of the award as a settlement—despite Respondent's contrary “conduct during the course of the arbitration and subsequent litigation”—and determined Respondent had not forfeited his UIM claim. See App. A 78, 80, 81-83. The Court of Appeals nonetheless found that the arbitration could have no res judicata or estoppel effect on Auto-Owners. See App. A 83.

Now, in his Brief to the highest court in the State of Minnesota, Respondent argues Auto-Owners can be bound to a default judgment that was entered against the tortfeasors with the express limitation that it not be executed against insurance coverage provided by Auto-Owners. See Respondent George's Minnesota Supreme Court Brief at 15-17. This newest argument is perhaps the most confusing of Respondent's shifting legal theories.

In support of this new theory, Respondent cites a variety of legal authorities for the premise that Auto-Owners should have defended the tortfeasors in this action and that its failure to do so somehow renders the default judgment issued against the tortfeasors binding against Auto-Owners by virtue of its policy. Id. Respondent also overlooks the fact that in its Answer, Auto-Owners clearly asserted provisions and exclusions under the applicable policy as an affirmative defense to Respondent's UIM claim. See App. R. 31.

It is clear that Judge Wexler specifically ordered that the default judgment against the tortfeasors be executed “only against insurance coverages other than coverages provided by Auto Owners Insurance Company and Progressive Insurance Company.” See App. A. 62. However, even setting aside this plain fact and the public policy reasons against requiring UIM carriers to defend tortfeasors in actions brought by their own insureds, Respondent’s new argument that the default judgment he obtained against the tortfeasors is somehow binding against Auto-Owners should not be entertained on appeal. See, e.g., Mattson v. Underwriters at Lloyds of London, 414 N.W.2d 717, 722 (Minn. 1987) (a party’s “chameleon-like” characterization of the issues throughout litigation and appeal is “an impermissible shift in the theory of recovery”); see also, Funchess v. Cecil Newman Corp., 632 N.W.2d 666 (Minn. 2001); Midway Nat. Bank of St. Paul v. Bollmeier, 474 N.W.2d 335, 339 (Minn. 1991); Thiele v. Stich, 425 N.W.2d 580, 582 (Minn. 1988); Security Bank of Pine Island v. Holst, 215 N.W.2d 61, 62 (Minn. 1974); Urban v. Continental Convention & Show Management, 68 N.W.2d 633, 635 (Minn. 1955); Leonard v. Parrish, 420 N.W.2d 629, 632 (Minn. Ct. App. 1988); and LaPanta v. Heidelberg, 392 N.W.2d 254, 257 (Minn. Ct. App. 1986).

Assuming Auto-Owners could somehow be bound to a default judgment entered with the explicit instruction that it not be binding against it, and assuming Auto-Owners had been put on notice of Respondent’s intent to use the default judgment in this way, Auto-Owners would have taken action to intervene and oppose such a judgment. However, Respondent’s motion for default judgment was not brought or granted for the purpose of obtaining recovery against Auto-Owners. Rather it was an effort on the part

of Respondent to maintain the possibility of pursuing his claims from any other available insurance coverage. See App. 35-36 of George's Minnesota Court of Appeals Brief; App. A. 63. Furthermore, had Respondent believed he was entitled to bind Auto-Owners to the default judgment he obtained against the tortfeasors, Respondent should have petitioned for an appeal to this Court in his own right.

IV. Respondent Has Failed to Demonstrate His Actions Caused No Prejudice to Auto-Owners.

In addition to the forgoing, Respondent contends prejudice to Auto-Owners cannot be presumed because Auto-Owners never agreed to arbitrate, making the arbitration non-binding on Auto-Owners. See Respondent George's Minnesota Supreme Court Brief at 5, 17-18, 20. As such, he reasons that adequate notice of the proceedings was provided by virtue of his purported post-arbitration Schmidt notice and by naming Auto-Owners in the subsequent lawsuit. See Respondent George's Minnesota Supreme Court Brief at 17. Respondent further claims that Auto-Owners has failed to provide a single example of resulting prejudice caused by his acts. See George's Minnesota Supreme Court Brief at 5.

Auto-Owners maintains that because the arbitration was represented to Auto-Owners as a binding resolution to Respondent's tort action, notice and prejudice to Auto-Owners should be evaluated pursuant to Kluball and Malmin. Kluball; Malmin. However, even if the arbitration is analyzed as a best settlement scenario, as set forth in its initial brief to this court, Auto-Owners has been prejudiced nonetheless.

Because Respondent did not provide proper notice of a pending settlement pursuant to the requirements set forth in Schmidt and as more fully articulated in Baumann, he deprived Auto-Owners of an opportunity to evaluate and protect its subrogation rights before releasing the tortfeasors. See Auto-Owners Minnesota Supreme Court Brief at 37 (citing Schmidt and Baumann).

Specifically, Respondent failed to provide Auto-Owners with proper Schmidt notice because he did not alert Auto-Owners to a settlement. See Auto-Owners Minnesota Supreme Court Brief at 33. Pursuant to the decision in Baumann, proper Schmidt notice must be conveyed in a form that provides, *inter alia*, “thirty days' written notice to the UIM insured of a *settlement agreement*.” See Auto-Owners Minnesota Supreme Court Brief at 33-34 (citing Baumann (emphasis supplied)). Absent such notification, release of the tortfeasor is deemed prejudicial to the underinsurer and the insured's failure to prove a lack of prejudice to the insurer by preponderance of the evidence results in forfeiture of the insured's UIM claim. Id.

Here because Respondent's actions caused Auto-Owners to evaluate the arbitration as a binding conclusion to a tort action, Respondent denied Auto-Owners a meaningful opportunity to evaluate and protect its subrogation rights. Accordingly, even if Auto-Owners is not bound to the award—as the District Court and Court of Appeals correctly concluded—Auto-Owners has been prejudiced because it will have no opportunity to recover its UIM payments in subrogation from the tortfeasors.

Respondent's failure to provide meaningful notice before releasing the tortfeasors creates a rebuttable presumption that Auto-Owners has been prejudiced by its inability to

protect its subrogation rights. See Auto-Owners Minnesota Supreme Court Brief at 37, (citing Baumann; Kluball). Respondent has not presented evidence to rebut this presumption. As such, Auto-Owners respectfully requests that this Court reverse the holding of the Minnesota Court of Appeals and hold in accordance with the trial court.

V. Respondent's Contention that His Purported Post-Arbitration Schmidt Notice Was Valid Is Based Wholly on Misstatements of Fact.

Lastly, Respondent alleges Auto-Owners acquiesced to and had knowledge of a settlement offer. See Respondent George's Minnesota Supreme Court Brief at 21. As such, he contends his purported post-arbitration Schmidt notice was valid. Id. For all the reasons set forth *supra*, any averments to this effect are simply not borne out in fact.

Respondent has not explained how acknowledgment of Respondent's post-settlement invitation to Auto-Owners to substitute its draft could be construed as a validation of Respondent's purported Schmidt notice when Respondent represented he had reached a binding conclusion to his tort claim. Likewise, Respondent has not explained why Auto-Owners should have concluded Respondent was attempting to obtain a settlement offer in light of Respondent's representations. Moreover, Respondent has not explained why Auto-Owners' acknowledgment of service of a "Schmidt v. Clothier Notice" amounted to an acknowledgement that the document provided "proper" notice. Finally, Respondent has not explained at what point Auto-Owners should have understood he had obtained a settlement offer, when at least some of his purported Schmidt notices were "admittedly meaningless and unnecessary." See App. A. 97, 100; Respondent George's Minnesota Supreme Court Brief at 11. Allowing a claimant to

force his UIM carrier to play a guessing game in an attempt to accomplish the incompatible goals of a) recovering from and releasing the tortfeasor while b) extinguishing his UIM carrier's ability to litigate the tort claim does not result in an effective, equitable or orderly process and should not be permitted. For this reason and those set forth previously, Auto-Owners respectfully requests that this Court reverse the holding of the Minnesota Court of Appeals and hold in accordance with the trial court.

CONCLUSION

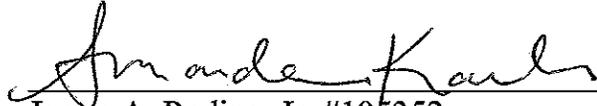
Respondent's course of conduct caused Auto-Owners to evaluate the arbitration as a binding resolution to his tort action. Respondent must not be permitted to leverage his misleading arbitration notices in an attempt to treat the arbitration award as both a best settlement and a binding resolution to his tort action.

The Court of Appeals recognized that Respondent's goals were legally incompatible and correctly concluded Auto-Owners maintains the right to re-litigate the UIM claim. However, even that result is prejudicial to Auto-Owners. Because of Respondent's deceptive arbitration notices, Respondent has managed to destroy Auto-Owner's subrogation rights. Such conduct must not be permitted and must result in forfeiture of Respondent's UIM claim.

For all of the reasons set forth herein and in its initial Brief to this Court, Auto-Owners respectfully requests that this Court reverse the holding of the Minnesota Court of Appeals and hold in accordance with the trial court by dismissing Respondent's claims and affirming summary judgment in favor of Auto-Owners.

REDING & PILNEY, PLLP

Date: 5/14/08



James A. Reding, Jr. #195352

Amanda J. G. Karls #0346469

Attorneys for Appellant Auto-Owners

8661 Eagle Point Boulevard

Lake Elmo, MN 55042

(651)702-1414

CERTIFICATION OF COMPLIANCE

I hereby certify that this brief complies with the word-count requirements of Minn. R. Civ. App. P. 132.01, subs. 1 and 3 for a brief produced with a proportional font. This brief was prepared using Microsoft Office Word 2003, complies with the typeface requirements of the Rules, and contains 3,782 words.

Dated: 5/14/08


Amanda J. G. Karls