

NO. A12-1017

State of Minnesota
In Court of Appeals

Minnesota Laborers Health and Welfare Fund,
 Minnesota Laborers Pension Fund, Minnesota Laborers Vacation Fund,
 Construction Laborers' Education, Training, and Apprenticeship Fund
 of Minnesota and North Dakota, Minnesota Laborers Employers
 Cooperation and Education Trust,

Appellants,

vs.

Granite Re, Inc.,

Respondent,

vs.

EnviroTech Remediation Services, Inc., David P. Sobaski,
 Karla P. Sobaski, Daniel Krause, Margaret Krause, Brent Krause,
 Jane Krause, William Sievers, Jill Sievers, Brent Anderson,
 and JoAnne M. Anderson,

Third-Party Respondents.

REPLY BRIEF OF APPELLANTS

ANDERSON, HELGEN, DAVIS
 & NISSEN, P.A.

Pamela H. Nissen (#259810)
 Rebecca A. Peterson (#392663)
 150 South Fifth Street, Suite 3100
 Minneapolis, MN 55402
 (612) 435-6363

FELHABER, LARSON, FENLON
 & VOGT, P.A.

Ruth S. Marcott, Esq. (#0176825)
 444 Cedar Street, Suite 2100
 St. Paul, MN 55101
 (651) 312-6034

Attorneys for Appellants

(Additional Counsel for the Respondents appear on inside cover)

GREGERSON, ROSOW, JOHNSON
& NILAN, LTD.

Daniel R. Gregerson (#0336518)
650 Third Avenue South, Suite 1600
Minneapolis, MN 55402
(612) 338-0755

Attorneys for Respondent Granite Re, Inc.

FORSBERG LAW OFFICE, P.A.
Eric W. Forsberg (#30995)
222 South Ninth Street, Suite 2960
Minneapolis, MN 55402
(612) 215-3302

*Attorneys for Third-Party Respondents
Daniel Krause, Margaret Krause, Brent Krause,
Jane Krause, William Sievers and Jill Sievers*

EnviroTech Remediation Services, Inc.
c/o William J. Sievers
2451 Forest Street
St. Paul, MN 55109

Unrepresented

David P. Sobaski
9006 Carter Path
Inver Grove Heights, MN 55076

Unrepresented

Karla P. Sobaski
9006 Carter Path
Inver Grove Heights, MN 55076

Unrepresented

Brent Anderson
6236 Knoll Drive
Edina, MN 55436

Unrepresented

JoAnne M. Anderson
6236 Knoll Drive
Edina, MN 55436

Unrepresented

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INTRODUCTION

Respondent Granite Re, Inc. presents itself as a naïve or perhaps simply uninformed party against whom enforcement of its contractual obligation would result in decimation of the entire construction industry. Respondent would have this Court find, that without any information or knowledge as to its principal's operations or contractual obligations, it issued a \$2,010,740 payment bond. Appellants' Appendix ("Appendix" or "App.") 91. Its principal, EnviroTech Remediation Services, Inc. was a contractor with an obligation to pay its employees compensation per the terms of a collective bargaining agreement. When Respondent issued a payment bond, in excess of \$2,000,000, guaranteeing that all laborers would be paid in full, it knew and intended that payment in full included EnviroTech's full obligations to its laborers per that collective bargaining agreement. Whether the words "payment in full" are used in a statute or used in a private contract; the words have the same legal effect.

The contract between Granite Re and EnviroTech included ten individuals who had an interest in EnviroTech. At least some of those individuals owned EnviroTech. Granite Re contracted with the very individuals who owned the company that perpetrated the fraud upon the Funds and should not be allowed to avoid its responsibility. The doctrine of fraudulent concealment should be applied in these circumstances and the Appellant Funds' claim deemed timely.

ARGUMENT

Appellant Funds submit this Reply Brief in accordance with Minnesota Appellate Rule 128.01, subd. 4 and will therefore limit the argument herein to responding to new matters raised in Respondent's Brief. See Minn. R. App. P. 128.01, subd. 4.

I. THE APPELLANT FUNDS ARE INTENDED THIRD-PARTY BENEFICIARIES UNDER MINNESOTA LAW.

A. Under a traditional analysis, the Appellant Funds are a third-party beneficiary of the contract between Granite Re and EnviroTech.

Respondent cites to *Cretex Cos, Inc. v. Const. Leaders, Inc.*, 342 N.W. 135 (Minn. 1984) for the proposition that this Court may only look at the contract to determine whether the Funds were an intended third-party beneficiary of the contract between Granite Re and EnviroTech. Respondent's Brief, 19. In fact, the *Cretex* court looked to all of the surrounding circumstances to determine whether the suppliers had a claim on the performance bond. "The contract must be read in light of *all* the circumstances..." *Id.* at 140 (emphasis added). Beyond its expansion of its factual analysis, the Court referred to a number of secondary sources including the American Jurisprudence series, Restatement of Contracts and the Restatement of Securities. *Id.* at 138-139. Justice Yetka's dissenting opinion in *Cretex* aptly notes: "Construction jobs are not negotiated in a vacuum." *Id.* at 141.

In determining whether the Appellant Funds are a third-party beneficiary of the contract between Respondent Granite Re and EnviroTech, this Court may properly consider all of the circumstances surrounding the contract. Respondent knew that its principal EnviroTech would use laborers to complete the project. Respondent did not issue the \$2,000,000 payment bond in a vacuum. It intended to provide protection for EnviroTech's laborers to make sure that they received payment in full, not just a pay check. The express language of the contract as well as application of the circumstances surrounding the implementation of the contract direct this Court to find that the Appellant Funds are an intended third-party beneficiary of the contract between Granite Re and EnviroTech under the intent to benefit test.

Respondent's Brief on the issue of the duty-owed test is conclusory and does not raise any new issues. Simply put – EnviroTech owes a duty to pay the laborers the full amount required by the collective bargaining agreement. If Granite Re paid to the Appellant Funds the amounts owing for the fringe benefit contributions, EnviroTech's obligation to the laborers and to the Funds would be fully discharged. The Appellant Funds are intended beneficiaries under the duty owed test.

B. The Appellant Funds seek fulfillment of the payment in full promise Granite Re made to the laborers who performed services on the Xcel High Bridge Project.

Ultimately the question before the Court is simple. Respondent Granite Re promised that every laborer on the project would be paid in full from EnviroTech.

The laborers providing services on the project were not paid in full. Payment from Respondent Granite Re to the Appellant Funds of the amounts claimed would fulfill that promise.

Respondent seeks to dismiss the United States Supreme Court's opinion in the *Sherman* case. *United States ex rel, Sherman v. Carter*, 353 U.S. 210 (1957). Granite Re urges this Court to restrict the reasoning set forth in *Sherman* to only statutory bond claims. This Court has already rejected such restriction. In the *Twin City Pipe Trades Peak Mechanical* case, this Court expanded *Sherman* beyond statutory bonds to provide a remedy for employee benefit plans, such as Appellant Funds. *Twin City Pipe Trades Service Assoc., Inc. v. Peak Mechanical, Inc.*, 698 N.W.2d 549 (Minn.App. 2004).

The *Sherman* opinion provides direct guidance for this Court with respect to application of the opinion to the bond at issue:

[T]he trustees of the fund have an even better right to sue on the bond than does the usual assignee since they are not seeking to recover on their own account. The trustees are claiming recovery for the sole benefit of the beneficiaries of the fund, and those beneficiaries are the very ones who have performed the labor."

Sherman, 353 U.S. at 219.

The *Mountbatten Surety Co. Court* from United States District Court for the Southern District of New York captured this holding best: "Carter gives a strong indication that the Supreme Court believes that denying union fund trustees the standing to sue upon construction bonds on behalf of their beneficiaries undermines the purpose of having union fund trusteeships." *Mountbatten Surety*

Co., Inc., 2000 WL 1752916 (S.D.N.Y 2000), (Respondent's Appendix 25-36, 32). This Court found that employee benefit plans were claimants under a private bond. The New York court, applying *Sherman*, concludes that the contract should be construed against the for-profit sureties who are "sophisticated repeat players who undertake surety obligations for profit." *Id.* at *30 (Respondent's Appendix 34). This reasoning comports with Minnesota Courts who since 1929 have found that the private surety bond contract in the case of any ambiguity, should be construed against the insurer. See *Lamberton Bldg. & Loan Ass'n v. Nat'l Sur. Co.*, 225 N.W. 724, 724 (Minn. 1929).

Furthermore, Respondent distorts the *Sherman* opinion as it relates to the Funds as assignees of the EnviroTech employees. *Sherman* did not reject the notion that the funds in that case were assignees. To the contrary, the Court specifically found that "[t]he trustees stand in the shoes of the employees and are entitled to enforce their rights." 353 U.S. at 220. There is no doubt that the EnviroTech employees are claimants under the bond's definition. However, it is the Funds who are entitled to make the claim for the contributions due for the labor they provide; contributions which are contractually required to be paid before the employees are paid in full for their services. The Appellant Funds are properly considered claimants for purposes of enforcing Respondent Granite Re's obligations.

The Appellant Funds meet both the traditional tests for intended beneficiaries of the contract between Granite Re and EnviroTech. This Court

need not go beyond the traditional analysis to reach the proper result; finding that the Funds are proper claimants. If the Court goes beyond that analysis, the Funds urge the consistent application of the *Sherman* principles and find that the Funds stand in the shoes of the laborers who performed services on the Xcel High Bridge Project and are therefore proper claimants.

II. THIS COURT SHOULD APPLY THE DOCTRINE OF FRAUDULENT CONCEALMENT TO THE APPELLANT FUNDS' CLAIM AGAINST GRANITE RE.

A. Relevant Law Supports Tolling the Statute of Limitations Based on the Doctrine of Fraudulent Concealment.

Respondent Granite Re inaccurately contends that this Court must deny application of the Doctrine of Fraudulent Concealment because it did not commit the alleged fraud. Respondent's Brief, 25-32. Granite Re's focus is misplaced since the prominent concern is whether equitable principals and general suretyship principles support application of this doctrine here. It is not as black and white as Granite Re maintains.

The cases recognizing the Doctrine of Fraudulent Concealment in Minnesota have never answered whether it may be applicable to surety or any third-party to a contract. See Respondent's Brief, 26-28. Despite this, Respondent Granite Re requests this Court to blindly apply legal theories from precedent with critical factual distinctions. Following this approach, would result in this Court rejecting the equitable principals underlying the foundation for the Doctrine of Fraudulent Concealment. Instead, consideration of all issues and

persuasive authority results in this Court's application of the Doctrine of Fraudulent Concealment to this dispute, and thereby, tolling the statute of limitations.

Adopting Restatement (First) of Security § 121 (1941) and Restatement (Third) of Suretyship & Guaranty § 66 (1996) would not contradict Minnesota law. This Court has applied specific sections from these Restatements in various situations. *Nelson v. Woodlands Nat. Bank*, A05-1739, 2006 WL 1529489 (Minn. Ct. App. June 6, 2006) (citing to Restatement (Third) of Suretyship and Guaranty § 6& 42); *Estate of Frantz v. Page*, 426 N.W.2d 894, 901 (Minn. Ct. App. 1988) (relying on Restatement of Security § 146) *Loving & Associates, Inc. v. Carothers*, 619 N.W.2d 782, 786 (Minn. Ct. App. 2000) (adopting approach in Restatement (Third) of Suretyship and Guaranty § 37 (1996)); *Stabs v. City of Tower*, 40 N.W.2d 362, 370 (1949) (following Restatement of Security §82). Moreover, unlike the authority cited by Respondent Granite Re, there is no split authority interpreting these sections or heavy criticism. Respondent's Brief; 28-29.

In *Domagala v. Rolland*, 805 N.W.2d 14 (2011), the Court analyzed a Restatement provision that received "heavy criticism from multiple jurisdictions," mainly citing public policy issues. *Id.* at 25-26 In refusing to adopt the relevant provision the Court noted:

Because it is not necessary to adopt section 321 to recognize the duty imposed on Rolland or to resolve the issues before us, and *because of the significant public policy concerns surrounding section*

321, we decline at this time to adopt Restatement (Second) of Torts § 321 as a basis for imposing a duty of care in a negligence claim.

Id. (emphasis added). Likewise, in *Travertine Corp. v. Lexington-Silverwood*, 683 N.W.2d 267 (Minn. 2004), the Court considered a Restatement section that was subject to split authority and varying interpretation. *Id.* at 272. Here, Respondent has not cited to one jurisdiction that is critical of the relevant Restatement provisions or establish any differing opinion in applying either provisions.

Respondent Granite Re's attempt to pigeon hole any application of the Restatement (First) of Security § 121 (1941) to a fidelity bond is unsupported. In *Vill. of Herkimer v. Am. Sur. Co. of New York*, 18 A.D.2d 94 (1963), the court applied this provision based on "settled principals of suretyship," it did not hold that this provision *only* applies when a fiduciary retains a bond. *Id.* at 95. In fact, nothing in Restatement (First) of Security § 121 (1941) limits or even refers to a fidelity bond, including the notes. *Id.*

Finally, Respondent Granite Re has confused the apparent connection of the various suretyship cases cited by the Appellant Funds to the Court's analysis here. Respondent Brief; 30-31. The well-accepted principle that a surety's liability is directly connected to its principal's liability is not irrelevant. This factor should be considered in weighing whether equitable principles are properly applied to a surety, such as Respondent Granite Re. Respondent Granite Re, itself, agrees that the cited authority demonstrate that the extent of a surety's

liability is controlled by the underlying liability of its principal. Respondent's Brief, 31. Granite Re, however, incorrectly tries to sever this critical fact from the Court's analysis here. This factor should be utilized in the Court's initial framework when determining whether Granite Re – whom was aware of the liability it assumed in signing the Bond and the risks associated in its business as a surety – should be subjected to the Doctrine of Fraudulent Concealment.

B. Application of the Doctrine of Fraudulent Concealment Does Not Contravene Public Policy.

Respondent Granite Re incorrectly casts itself as an innocent third party in an attempt to foreclose the tolling of the statute of limitations based on EnviroTech's fraudulent concealment. Respondent's Brief, 32. Respondent Granite Re's "innocent party" argument tries to encourage this Court to consider the increase in bond price if the doctrine of fraudulent concealment is adopted. *Id.* No authority or study reflecting this sweeping conclusion, however, is offered by Respondent Granite Re. *Id.* Contrary to its contentions otherwise, invoking public policy does not serve to protect the Respondent Granite Re's interests. "The rule of construction applicable to the contract of a gratuitous surety, always so much the favorite of courts that every intendment is in his favor, does not apply when the surety is a paid surety. Their undertakings are in the nature of insurance contracts." *Standard Salt & Cement Co. v. National Surety Co.*, 134 Minn. 121, 127-128 (Minn. 1916) *See Lamberton Bldg.*, 225 N.W. at 724 (private surety bond contract should be construed against the insurer.) *See Knecht, Inc.*

v. *United Pacific Ins. Co.*, 860 F.2d 74, 83 (3d Cir. Pa. 1988)(“[A] corporate surety in business for profit is not a 'favorite of the law,'”) (citations omitted).

In this instance, as noted above, Granite Re is contractually tied to ten individuals who guaranteed EnviroTech’s obligations to Granite Re. There is no injustice in compelling EnviroTech’s principals to ultimately be held responsible for their fraudulent actions. This Court should reject Respondent Granite Re’s speculation on the increase in the price of bonds and instead consider the recognized equitable and suretyship principles in applying the Doctrine of Fraudulent Concealment here.

III. CONCLUSION

The lower court’s ruling is erroneous as a matter of law and should be reversed in its entirety. Judgment as a matter of law should be entered in favor of the Appellant Funds. In the alternative, this Court should remand the case for further proceedings concerning the factual inquiry as to whether all elements for fraudulent concealment has been met.

Date: September 10, 2012

ANDERSON, HELGEN, DAVIS & NISSEN, PA

By: 

Pamela H. Nissen (Atty. Reg. No. 259810)

Rebecca A. Peterson (Atty. Reg. No. 392663)

150 South Fifth Street, Suite 3100

Minneapolis, MN 55402

Telephone: (612) 435-6363

Email: phn@andersonhelgen.com

FELHABER, LARSON, FENLON & VOGT, P.A.
Ruth S. Marcott (Atty. Reg. No. 176825)
444 Cedar Street, Suite 2100
St. Paul, MN 55101
Telephone: (651) 312-6034
Email: rmarcott@felhaber.com

Attorneys for Appellant Funds

CERTIFICATE OF LENGTH

This hereby certifies that this brief complies with the word count and length limit requirements of Minn. R. Civ. App. P. 132.01, subd. 3. This brief was typed using Microsoft Word 2007. This brief contains 2,903 words, is less than 11 pages excluding table of contents pursuant to Minn. R. Civ. App. 132.01, subd. 3, and complies with the typeface requirements of Minn. R. Civ. App. P. 132.01, subd. 3(a).

A handwritten signature in black ink, appearing to read 'Rebecca A. Peterson', is written over a horizontal line. The signature is fluid and cursive.

Rebecca A. Peterson, Atty. Reg. No. 392663