

Nos. A04-1442 and A04-1612

State of Minnesota
In Supreme Court

Wooddale Builders, Inc.,

Appellant,

vs.

Maryland Casualty Company d/b/a Zurich North America,

Appellant,

vs.

American Family Insurance Group, and
Western National Insurance Group,

Appellants,

West Bend Mutual Insurance Company,

Respondent,

American Economy Insurance Co. (SafeCo),

Respondent.

**REPLY BRIEF OF APPELLANT
AMERICAN FAMILY INSURANCE**

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ARGUMENT AND AUTHORITIES

I. The argument of Amicus Curiae Defective Construction Homeowners of Minnesota to “Reject the Application of Pro Rata by Time on the Risk” must be dismissed as not properly under consideration.

This court granted review of the only two issues raised on appeal: the end date for allocation of indemnity pro rata by time on the risk; and the responsibility of successive primary insurers for defense in that setting. None of the parties appealed the trial court’s decision to allocate indemnity pro rata. In fact, the trial court reached the conclusion to do so on uncontroverted evidence that the involved damage was continuous and indivisible, and on the parties’ agreement that indemnity should be allocated pro rata under the circumstances. Order and Memorandum (West Bend App. at 1-5).

The question whether pro rata allocation of indemnity is appropriate is not before the court in this case. It is, however, the subject of an appeal currently pending before the court of appeals. Kootenia Homes, Inc. v. Federated Mut. Ins. Co. (A05-278). Kootenia (where the parties have raised, brief and developed evidence bearing on this issue) is a better forum for addressing the amicus’s concerns about whether to apply pro-rata allocation in this setting.

An amicus's role is limited. The rules do not provide for an amicus to petition for review. ERIC J. MAGNUSON & DAVID F. HERR, MINN.PRAC.APPELLATE RULES ANNOT. (3d ed.) at 420. “[A]n amicus may not raise an issue not addressed by the parties.” Peterson v. BASF Corp., 657 N.W.2d 853, 863 (Minn. Ct. App. 2003), citing Country Joe, Inc. v. City of Eagan, 560 N.W.2d 681, 687 n. 7 (Minn. 1997). When that happens, the appellate courts “do not consider these arguments.” Id. Amicus Homeowners’ argument to reject pro rata allocation altogether, therefore, must be ignored.

II. There is no justification for abandoning *Jostens* in determining the defense duties of primary insurers simultaneously obligated to defend claims of continuous indivisible injury.

This case comes to the Supreme Court from orders issued on cross-motions for partial summary judgment. Wooddale and its five insurers, all with identical primary obligations to defend and indemnify Wooddale, sought an adjudication of the insurers’ duties with respect to claims indisputably arising out of a “continuous and indivisible” sequence of property damage occurring over multiple policy periods. Order and Memorandum (West Bend App. at 1-4). The insurers already were sharing the investigation expenses and defense obligations in the claims and suits

against Wooddale. Id. at 3. The parties agreed that the insurers' right to reallocate these defense costs "had been properly reserved." Id. at 3.¹

This is not a contribution action among insurers, as is the situation in some of the cases West Bend cites. Instead, ours is a context essentially indistinguishable from that in which the Jostens case² was decided: an insured's action for defense and indemnity involving multiple primary insurers. This context calls for a contract analysis along established lines (rather than so-called equity jurisprudence) to determine the insurers' obligations to defend the insured viewed as of the time that the defense was tendered. Jostens, 387 N.W.2d at 166. The rules are settled and clear:

1. "A duty to defend an insured on a claim arises when any part of the claim is 'arguably' within the scope of the policy's coverage [.]"

Jostens, 387 N.W.2d at 166.

2. "The duty to defend is separate from, and broader than, the duty to indemnify." Brown v. State Auto. & Cas. Underwriters, 283 N.W.2d 822, 825 (Minn. 1980).

¹ West Bend is mistaken when it contends that the parties never stipulated to the equivalent of a loan receipt. West Bend Brief at 30 p. 12.

² Jostens, Inc. v. Mission Ins. Co., 387 N.W.2d 161 (Minn. 1986).

3. “[W]here it can be argued ... that either of two insurers has primary coverage for a claim, both insurers have a duty to defend that claim.” Jostens, 387 N.W.2d at 167.

4. “If it is established that both insurers arguably had coverage ... the insurers, as between them, shall be equally liable for the insured’s defense costs[.]” Jostens, 387 N.W.2d at 167.

5. Any rule must “encourage two insurers, when tendered a defense, to resolve promptly the duty to defend issue” and must prevent insurers from” adopt[ing] a ‘wait and see’ attitude while leaving the insured to defend himself.” Jostens, 387 N.W.2d at 167.

6. Any rule must hold the insurer that “bargained for the primary coverage” to that bargain. Jostens, 387 N.W.2d at 167-68.

7. “If defense costs ... are so inextricably intertwined they cannot be fairly sorted out, the costs may be equally divided.” Jostens, 387 N.W.2d at 168.

Relying on foreign decisions based on supposed equity principles rather than these settled Minnesota rules based on contract law, West Bend asks this court to follow the court of appeals and abandon Jostens in cases involving multiple primary coverages for continuous, indivisible injury. The

court of appeals decision on the duty to defend in this kind of case must be reversed for any number of reasons.

The question in these cases is not just what is “fair.” As Jostens teaches, cases like this cannot be divorced from the obligations the insurers have contracted for; decisions have to start with what the insurers’ contracts obligate them to provide to their insureds.

West Bend’s contract specifies that the company has “the duty to defend any ‘suit’ seeking [property] damages.” The contract provides that this duty does not end until the policy’s indemnity limit has been used up. West Bend App. at 146. West Bend’s contract explicitly requires it to pay all expenses incurred in defense of a covered claim. West Bend App. at 150. Nowhere does it call for proration of defense costs. In fact, in the only part of the policy addressing “other insurance,” West Bend covenants that it will take on an equal share of liability in every case in which it and another insurer are both “primary.” This policy only addresses a lesser duty to defend in situations where West Bend is “excess,” a situation that does not apply in our case. The insuring intent as respects “other insurance” is clear: When West Bend and all other insurers are “primary” West Bend contracts

to pay an equal share, for exactly the same reason that the insurers in Jostens³ did.

If the duty to defend is separate from and broader than the duty to indemnify why do our court of appeals and all the foreign courts West Bend cites confuse the two?⁴ These policies specifically state that the insurer is obligated to indemnify for “sums” or “all sums” owed as a result of damage “during the policy period.” They could, but don’t, say anything about limiting the duty to defend in the same way. Rather, the broader duty to defend requires the insurer to defend entirely “when any part of the claim is ‘arguably’ within the scope of the policy’s coverage.” Jostens, 387 N.W.2d at 166. When limitations on the duty to defend are found nowhere in the applicable provisions of the policy, the primary insurer must be held to the unlimited defense “bargain” it has made.

³ If the policy is ambiguous as relates to the duty to defend vis a vis “other insurance,” then it must be construed against West Bend. Security Mut. Cas. Co. v. Luthi, 303 Minn. 161, 168, 226 N.W.2d 878, 883 (1975).

⁴ The court of appeals’ decision rests on the allocability of “liability” (read indemnity). See American Family App. Brief at 11. The Forty-Eight Insulations case that started the trend of foreign cases on which the court of appeals decision rests has this rationale: There is “no reason why” proration by time on the risk should not apply to defense costs if it applies to indemnity. Ins. Co. of N. Am. v. Forty-Eight Insulations, Inc., 633 F.2d 1212, 1225 (6th Cir. 1980). The “reason why” is that defense and indemnity are completely different obligations, as we discuss below.

The court of appeals and West Bend would have us pass over the insurance contract to find “fairness” based exclusively on years on the risk. Why is it “fair” for an insurer with \$5,000,000 of coverage for a one-year term to pay a fraction of the defense costs paid by an insurer with \$500,000 in coverage for five years on the risk? When both carriers bargain for an equal share of the primary defense obligation neither time nor money should be substituted for the promises they have made.⁵

The difference between the duty to indemnify and the duty to defend is fundamental, at least in the decisions of this court. This distinction underlies the decision to affirm an award of all of the insured’s defense costs despite many years in which there was actual injury but no coverage.

Domtar, Inc., v. Niagara Fire Ins. Co., 563 N.W.2d 724, 739 (Minn. 1997).

It is the reason why an insurer will be obligated to defend all the way until there is a decision that there is no coverage for any part of the claim.

Economy Fire & Cas. Co. v. Iverson, 445 N.W.2d 824, 827 (Minn. 1989).

Cases requiring the insured to share equally up-front in the cost of the defense for years it can’t identify its coverage and then participate in a

⁵ This jurisdiction specifically has rejected pro rata by limits allocation of indemnity obligations. Northern States Power Co. v. Fid. & Cas. Co. of N.Y., 523 N.W.2d 657, 662, (Minn. 1994).

defense cost reallocation based on time on the risk⁶ reflect a perspective completely different from Minnesota's, as Domtar and Iverson show.

West Bend contends that “nothing could be simpler than applying the same allocation formula to both indemnity and defense costs[.]” West Bend Brief at 36. Nothing could be farther from the truth. The foreign cases West Bend cites show that pro rata allocation of defense costs by time on the risk inevitably leads to the conclusion that the insured must participate for years when it chooses to “go bare” or for which it cannot prove it had coverage. The insured's pro rata participation in defense causes any number of problems. When and how do we determine the insured's share? If we do that up front, the homeowners' litigation stalls until defense shares are allocated. If the insured has to contribute pro rata, what happens when (as is often the case with general contractors and subcontractors) the insured is no longer in business or bankrupt when the claim against it is made? Does the insured's participation in defense costs give it a right to select counsel and control the defense? If so, what effect does that have on the insurer's contractual right to make those decisions? How do we address the conflicts of interest that are inevitable when the insured and the insurer each have a say in whether a case should be settled or tried? As all of these issues are

⁶ Gulf Chemical & Metallurgical Corp. v. Associated Metals & Minerals Corp., 1 F.3d 365, 373 (5th Cir. 1993), cited at p. 32 of West Bend's Brief.

sorted out, we will find ourselves a long way from achieving the public policy goals that Jostens describes.

Following Jostens in this context also avoids the problem of irreconcilable differences between the insurers' policies. West Bend contends that its policy limits West Bend's duties of both defense and indemnity to damage occurring "during the policy period." On the other hand, as West Bend notes, Western National's policy would impose duties of defense and indemnity with respect to both "'property damage' which occurs during the policy period ... [and] any continuation, change or resumption of that ... 'property damage' after the end of the policy period." West Bend App. at 165; West Bend Brief at 17 n. 5. Conceivably, in this setting, two insurers' time on the risk could overlap. Who pays for that period in which both are primary? When is that battle fought? Allocating defense costs equally avoids this problem altogether.

Each primary insurer has a separate and complete duty to defend. Iowa Nat'l. Mut. Ins. Co. v. Universal Underwriters Ins. Co., 150 N.W.2d 233, 236-37 (Minn. 1967). When Wooddale's case came on for summary judgment all parties sought a determination of the duty to defend as between five insurers with identical duties to Wooddale. Any one of them could have been called on, Domtar, 563 N.W.2d at 739, but since all five were being

called on simultaneously, the question was “‘as between them’ are [these] insurers equally liable for such costs”? Id. quoting Jostens, 387 N.W.2d at 167 (emphasis supplied). If the defense duties could be “sorted out,” then each insurer could pay its own share. But if there is no way to divide up the costs of defending these claims arising from “continuous, indivisible injury” then “as between them” these five insurers must share the costs of defense equally. Jostens tells us that. To use Justice Simonett’s words, the insurer ‘has no cause to complain because it is protecting its own interests and is only doing what it agreed and was paid a premium to do.’ Jostens, 387 N.W.2d at 166.

What difference is there between the concurrently liable primary insurers in Jostens and these five primary insurers, consecutively liable for indemnity but concurrently and simultaneously obligated to afford Wooddale a complete defense? With all due respect to the court of appeals, when we focus properly, on the duty to defend rather than the duty to indemnify, there is no difference at all. Viewed from the standpoint of the time Wooddale was confronted with the homeowners’ allegations - as Jostens tells us to do- the duty to defend Wooddale was no different than the duty Jostens’ insurers owed. The same rules ought to apply in both cases. Not because it’s “simpler.” Not because some ill-conceived notions of

“equity” say so. But because that is what the insurance contracts and our law tell us has to happen.

CONCLUSION

Amicus Defective Construction Homeowners have improperly argued to reject pro rata allocation of indemnity altogether. That improper argument must be ignored.

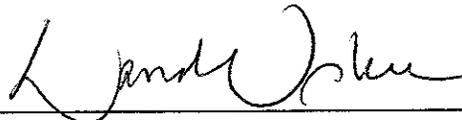
There is no reason to adopt different rules for primary insurers with an immediate and simultaneous duty to defend in case of concurrent and consecutive liability. In fact, pro rata allocation of defense duties invites chaos and undermines the policies Jostens advances.

The court of appeals’ decision to abandon Jostens in the context of continuous, indivisible injury claims must be reversed.

Dated: 11/2/05

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CERTIFICATION OF BRIEF LENGTH

I hereby certify that this brief conforms to the requirements of Minn. R. Civ. App. P. 132.01, subds. 1 and 3, for a brief produced with proportional font. The length of this brief is 2305 words. This brief was prepared using Times New Roman size 14 font.

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