

No. A-05-1293

STATE OF MINNESOTA
IN SUPREME COURT

HOYT PROPERTIES, INC. AND HOYT/WINNETKA, LLC,

Respondents,

v.

PRODUCTION RESOURCE GROUP, LLC,
HAAS MULTIPLES ENVIRONMENTAL MARKETING AND DESIGN, INC.
D/B/A ENTOLO-MINNEAPOLIS AND ENTOLO, INC.,

Appellants.

APPELLANTS' REPLY BRIEF

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SUMMARY OF THE ARGUMENT

Respondents Hoyt Properties, Inc. and Hoyt/Winnetka, LLC (collectively, “Respondents”) spend much of their brief trying to prove that Production Resource Group, LLC (“PRG”) is actually the alter ego of Haas Multiples Environmental Marketing and Design, Inc., d/b/a Entolo-Minneapolis (“Haas”), and Entolo, Inc. (“Entolo”). Their apparent goal is to color this Court’s view of this case, so that this Court will rule for them because they allegedly were “wronged.”

There are two problems with Respondents’ argument. First, it is irrelevant. The issue here is whether Karl Robinson made a factual statement on which Respondents reasonably and actually relied. Second, Respondents’ assertion that PRG is indisputably an alter ego, so that they will prevail if allowed to proceed, is based on mischaracterizations of the record and demonstrably erroneous allegations.

Under existing Minnesota precedent, Robinson’s alleged representations regarding the viability of a piercing claim are not actionable because they did not communicate any specific factual information. Apparently recognizing this fact, Respondents and amicus ask this Court to abolish its long-held distinction between nonactionable statements of law and actionable statements of fact, or, at a minimum, to blur that line beyond recognition. This untenable result would make nearly every statement uttered by an attorney during settlement negotiations actionable, and would seriously undermine the finality of most settlements.

Respondents also fail to confront Appellants’ argument that the *totality* of the circumstances – the negotiation setting, Hoyt’s business and legal sophistication, the

settlement agreement's integration clause and express carveouts for other creditors' remedies, and Respondents' failure to observe their own customary business practice of documenting representations – preclude Hoyt from establishing reasonable and actual reliance. This alone defeats their case.

With respect to the partial rescission and dismissal with prejudice issues, Respondents offer no reason why they should be permitted to benefit from the inconsistent and confusing pleadings they filed below.

This Court should therefore affirm the District Court's entry of judgment in favor of Appellants.

ARGUMENT

I. BECAUSE THE DECISION TO PIERCE THE CORPORATE VEIL INVOLVES A MULTI-FACTOR BALANCING INQUIRY AND EQUITABLE CONSIDERATIONS, THE ALLEGED EXCHANGE BETWEEN HOYT AND ROBINSON COULD NOT – AND DID NOT – IMPLY ANY SPECIFIC FACTS.

A. Under Existing Precedent, Robinson's Alleged Representations Constituted a Nonactionable Legal Opinion That Did Not Directly or Indirectly Communicate the Existence of Any Specific Facts.

Respondents seek to brush aside this Court's longstanding distinction between actionable misrepresentations of fact and nonactionable statements of legal opinion as a mere "technicality." Respondents' Br. at 20. This Court should not adopt such an unwise and unworkable rule.

The non-Minnesota cases Respondents cite in support of this radical proposition do not support their notion of a modern trend toward abolishing this distinction. Respondents' Br. at 22. In Lawyers Title Insurance Corp. v. Pokraka, 595 N.E.2d 244

(Ind. 1992), the Indiana Supreme Court did not even rule on the law/fact distinction. Id. at 249. To the extent that the Texas Court of Appeals' decision in Bourland v. Huffhines, 244 S.W. 847 (Tex. Civ. App. 1922), can be considered "modern,"¹ its holding is not good law in light of the Texas Supreme Court's more recent reaffirmation of "the general rule that misrepresentations involving a point of law . . . will not support an action for fraud." Fina Supply, Inc. v. Abilene Nat'l Bank, 726 S.W.2d 537, 540 (Tex. 1987) (holding no exception to general rule where the parties are "two equally sophisticated business entities . . . with equal access to legal advice").

The other cases cited by Respondents illustrate the wisdom of retaining the workable rule articulated by this Court in Miller v. Osterlund, 154 Minn. 495, 191 N.W. 919 (1923), that "[a] misrepresentation though involving [a] matter of law will be held actionable if it amounts to an implied assertion that facts exist that justify the conclusion of law which is expressed." Id. at 496, 191 N.W. at 919. For instance, in Peterson v. Auvel, 552 P.2d 538 (Or. 1976), the Oregon Supreme Court held that the defendants' statement that an earnest money agreement was unenforceable was an actionable misrepresentation of fact because defendants knew for a fact that the agreement was enforceable. Id. at 539, 542. Similarly, in Nelson v. Taff, 499 N.W.2d 685 (Wis. Ct. App. 1993), the Wisconsin Court of Appeals carved out an exception to Wisconsin's general rule that "misrepresentations of law are . . . not actionable as fraud" where defendant had informed plaintiff that he would be purchasing a limited partnership

¹ Respondents indicated that Bourland was decided in 1992. Respondents' Br. at 22. In fact, it was decided in 1922. 244 S.W. at 847.

interest when in fact defendant knew that the entity in question was a general, rather than limited, partnership. Id. at 686-87.

Miller illustrates how this rule is properly applied. There, this Court held that an insurance company could not avoid liability for fraudulently representing that it was authorized to write insurance in Minnesota because that statement conveyed specific factual information: “To say of a foreign insurance company that it has the right to write insurance in Minnesota, conveys the meaning to the average man that the company has complied with the well-known requirements of our laws, and has received the Insurance Commissioner’s license or authority to transact insurance business here.” Id. at 497, 191 N.W. at 919. Likewise, a representation that a property is a six-unit building when it is zoned and registered for only five units amounts to a factual representation about a specific, incontrovertible feature of the property in question. Simonsen v. BTH Properties, 410 N.W.2d 458, 461 (Minn. Ct. App. 1987). Similarly, a representation regarding the existence of a contract – as distinguished from the contract’s validity, a much more complex question – basically asserts a yes-or-no answer to a straightforward factual question, Nodak Oil Co. v. Mobil Oil Corp., 533 F.2d 401, 406 (8th Cir. 1976).²

A legal conclusion concerning the viability of a piercing claim, on the other hand, cannot be characterized as implying specific facts that are true or false. As noted in Appellants’ opening brief, Appellants’ Br. at 21-22, this Court has set forth eight relevant

² Despite Appellants’ observation that Nodak is an Eighth Circuit case interpreting North Dakota law, Appellants’ Br. at 20, Respondents doggedly persist in including Nodak in a list of citations purportedly indicating what “Minnesota courts have long held.” Respondents’ Br. at 24.

factors under the first prong of the piercing-the-veil test: “insufficient capitalization for purposes of corporate undertaking, failure to observe corporate formalities, nonpayment of dividends, insolvency of debtor corporation at time of transaction in question, siphoning of funds by dominant shareholder, nonfunctioning of other officers and directors, absence of corporate records, and existence of corporation as merely façade for individual dealings.” Victoria Elevator Co. of Minneapolis v. Meriden Grain Co., Inc., 283 N.W.2d 509, 512 (Minn. 1979). This multi-factor list is “not exhaustive,” and Minnesota courts are free to weigh other factors in deciding whether to pierce the veil. Hopkins v. Trans Union, L.L.C., 2004 WL 1854191, at *4 (D. Minn. Aug. 19, 2004). Compare Bridas S.A.P.I.C. v. Government of Turkmenistan, 345 F.3d 347, 360 n.11 (5th Cir. 2003) (finding 21 factors relevant under first prong of piercing-the-veil test), *cert. denied on other grounds*, 541 U.S. 937 (2004). Thus, a statement that a piercing-the-veil claim is not viable, as alleged in this case, implies no specific facts under the first prong because the underlying facts are too numerous for any specific facts (e.g., that two companies have separate bank accounts, officers, and directors) to be implied.

The second prong of Minnesota’s piercing-the-veil test, which requires a plaintiff to demonstrate “an element of injustice or fundamental unfairness,” Victoria Elevator, 283 N.W.2d at 512, similarly fails to communicate any specific facts. Because there is little guidance as to what set of facts would satisfy this prong, it is even more vague and subjective than the first prong. See, e.g., *id.* (reciting but not applying test); Snyder Elec. Co. v. Fleming, 305 N.W.2d 863, 868 n.1 (Minn. 1981) (same); Barton v. Moore, 558 N.W.2d 746, 749 (Minn. 1997) (same). Thus, a statement that a piercing claim is not

viable implies nothing about the numerous facts that a court would have to address under this prong, nor did Hoyt inquire about any particular factor. Like the first prong, the “fundamental unfairness” prong is simply too vague and imprecise to imply the existence of any facts on which Hoyt could have relied.

Respondents also make the untenable argument that “courts across the country” have held that statements regarding the viability of a legal claim are actionable. Respondents’ Br. at 26. Respondents’ primary authority for this audacious claim is Rosenbaum Capital LLC v. Boston Communications Group, 445 F. Supp. 2d 179 (D. Mass. 2006). Rosenbaum Capital was a securities fraud action alleging that defendants had repeatedly declared their belief that their defenses to a patent action were meritorious, even though they were simultaneously taking actions that demonstrated that they actually knew they were willful patent infringers. Id. at 172-73. False statements about a party’s knowledge and beliefs are not statements regarding whether a legal claim is viable.³ Indeed, Respondents do not even believe their own argument – that statements

³ The other cases cited by Respondents are similarly inapposite because they (like Rosenbaum Capital) feature significant evidence of the falsity of the speaker’s beliefs or statements whose falsity is not open to reasonable debate. Lowther v. Hopper Truck Lines, 377 P.2d 192 (Ariz. 1962), involved an insurance adjuster informing a plaintiff that the insurance company was not liable, which he knew was false, as evidenced by his alleged use of undue influence over the plaintiff. Id. at 192-93. In Sainsbury v. Pennsylvania Greyhound Lines, Inc., 183 F.2d 548 (4th Cir. 1950), an insurance adjuster based his statement regarding the plaintiff’s inability to recover for his injuries on an indisputably false statement of “well settled” law. Id. at 550. Raymark Industries, Inc. v. Stemple, 714 F. Supp. 460 (D. Kan. 1988), held that plaintiff, an asbestos manufacturer, had stated a claim for fraud by alleging that opposing counsel, who had filed a class-action suit and participated in settlement talks, had falsely represented that their clients in fact suffered from asbestos-related diseases. The court reasoned that this

about the viability of a legal claim are actionable – because they twice claim that an attorney’s statements about the likelihood of success at trial are not actionable. Respondents’ Br. at 32, 42.

Respondents’ unwise call for the adoption of a broad new rule of law should not divert this Court from what Hoyt allegedly said. Hoyt alleged that he responded to PRG’s request for a release by saying to Kuller and Robinson, “Well, that would be piercing the veil I don’t know of any reason why [PRG] could be liable, do you?”⁴ (App. 204-205, Hoyt Dep. at 112:1-115:15.) Hoyt testified that in asking about “pierc[ing] the veil,” he meant, “could you go beyond Entolo and – and pierce the veil of somebody who had an ownership interest in Entolo.” (App. 204, Hoyt Dep. at 110:16-18.) Thus, Hoyt’s alleged question regarding liability under a piercing theory called for a quintessentially legal conclusion, not for a detailed factual rundown of whether Entolo was sufficiently capitalized, observed corporate formalities, paid dividends, was solvent, had functioning officers and directors, kept corporate records, or any other factor relevant to either the separateness or fundamental unfairness prongs of Victoria Elevator.

Similarly, Robinson’s alleged representation that “they” were “totally separate” simply restated his conclusion regarding the viability of a piercing claim. In piercing-the-veil cases under Minnesota law, the “separateness” of legal entities is both an initial legal

cont.

misrepresentation was factual because the attorneys’ filing and settling of the suit implied “certain representations as to the *existence* of an asbestos-related injury.” *Id.* at 467.

⁴ Contrary to Respondents’ unsupported characterization of this exchange, Hoyt did not state that he felt “uncomfortable” about relinquishing a claim for piercing the veil. Respondents’ Br. at 18; App. 205, Hoyt Dep. at 114:1-8.

presumption and a conclusion arrived at only after considering both prongs of the Victoria Elevator test. In Ass'n of Mill & Elevator Mut. Ins. Co. v. Barzen Int'l, Inc., 553 N.W.2d 446 (Minn. Ct. App. 1996) ("Barzen"), the Court of Appeals held, "In conclusion, the facts do not rebut the presumption of corporate separateness in this case. Most of the Victoria Elevator factors reflect this separateness, and none of these factors, alone or jointly, support piercing." Id. at 450; see also Snyder Elec. Co., 305 N.W.2d at 868 (Minn. 1981) ("Whether the corporation is a separate entity or not depends on a number of factors."). Because Victoria Elevator requires a complex weighing of non-dispositive and non-exclusive factors, including "fundamental fairness," a court can conclude that two entities are "separate" even if they do not have separate officers or boards of directors. Indeed, if the "fundamental unfairness" prong has not been satisfied, Victoria Elevator mandates a conclusion of "corporate separateness" no matter what facts have been shown regarding the relationship between the two entities. 283 N.W.2d at 512. Thus, as an opinion given by one attorney at the request of an opposing lawyer, the alleged representation that Entolo and PRG were "totally separate" could not imply any specific facts – it is a legal conclusion.

B. Respondents' Policy Prescriptions Would Deter Settlements and Pave the Way for a Flood of Rescission Suits.

In attempting to fashion a new standard under which Robinson's alleged representation would be actionable, Respondents urge this Court to adopt a rule that, in the settlement negotiation context, would make actionable representations concerning "success in litigation," "tax liability (or lack thereof)," and "the validity of patents."

Respondents' Br. at 29-30. These examples demonstrate that Respondents' proposed rule is unworkable.

First, any rule under which all "representations regarding success in litigation" are actionable would undermine Minnesota's "strong public policy of encouraging settlement." Wall v. Fairview Hosp. & Healthcare Servs., 584 N.W.2d 395, 404 (Minn. 1998). Settlement negotiations would never get off the ground if the parties knew that statements of bargaining position, such as their evaluation of the viability of legal claims and the outcome of contested litigation, could be used against them in subsequent litigation to overturn any settlement. Settlement negotiations are an arena in which chest-thumping regarding a party's liability, or the extent of that liability, is fully expected.

Respondents claim that PRG's position would "interject an unneeded element of uncertainty into the bargaining process" by causing parties "to wonder whether their representation was a 'legal conclusion' to some degree that would make it non-actionable." Respondents' Br. at 30. Any such uncertainty can be easily resolved by putting any representations and warranties a party wants to rely on in the final written agreement, which is Hoyt's invariable practice except in this case. (App. 195, Hoyt Dep. at 25:20-26:14.) By contrast, Respondents' astonishing position is that no matter what the scope of the representations and warranties, and without regard to an integration clause, a party may always undo the settlement by alleging after the fact that it relied on an oral statement by opposing counsel concerning the viability of a complex legal claim.

Moreover, adopting PRG's position would not unsettle customary bargaining practices because PRG's position is already the law in Minnesota. Rather, it is

Respondents and amicus Minnesota Trial Lawyers Association (“MTLA”), MTLA Br. at 7, who seek to erase the line between statements of law and statements of fact, thereby creating a thriving cottage industry of litigating oral representations allegedly made during settlement negotiations. While such a rule would create a bonanza for disgruntled parties to settlement agreements, it would undermine the stability of such agreements and burden Minnesota’s courts with constant litigation over settlement agreements.

Second, Respondents’ suggestion that this Court should adopt a rule under which “representations of tax liability (or the lack thereof)” and “representations regarding the validity of patents” are actionable highlights the radical nature of their policy proposal. No doubt, in a narrow set of cases such representations should be actionable because they directly convey specific false factual information. For example, an attorney should be liable for fraudulently representing that a client has no tax liability when the attorney knows that the client has failed to file tax returns or pay tax that is owed in a given year. Similarly, a representation that a patent is valid should be actionable when the person making the statement knows that the patent has previously been invalidated. However, representations about tax liability and patent validity generally involve complex legal analysis as to which reasonable minds can and do differ. Except in the simplest cases, they are not remotely analogous to such cut-and-dried questions as whether an insurance license or zoning approval was obtained.

In sum, the Minnesota courts have shown that in creating an exception to the general rule that an action for fraud requires a misrepresentation of past or present fact, they can draw reasonable distinctions between nonactionable statements of law and

statements of law that are actionable because they imply factual information. The alleged representations in this case fall squarely on the nonactionable side of this line, and Respondents have adduced no precedent or policy that should lead this Court to conclude otherwise.

II. RESPONDENTS HAVE FAILED TO DEMONSTRATE THE ACTUAL AND REASONABLE RELIANCE ELEMENTS OF FRAUDULENT MISREPRESENTATION.

A. Respondents Utterly Ignore Minnesota Case Law on Reasonable Reliance, Which Defeats Their Case.

Respondents have failed to refute Appellants' argument that given *all* the circumstances of this case – the settlement context, Hoyt's business and legal sophistication, Hoyt's undisputed standard business practices, and the settlement agreement's integration clause – Hoyt's reliance was unreasonable as a matter of law.

Respondents' new claim that Appellants' "unreasonableness" argument relies upon a negligence standard is a red herring. Respondents' Br. at 43. Contrary to Respondents' assertion, Appellants are not invoking contributory negligence as a defense. Rather, Appellants contend that Respondents have failed to raise a genuine issue of material fact on reliance. It is well settled that one of the elements of fraudulent misrepresentation is detrimental reliance, Davis v. Re-Trac Mfg. Corp., 276 Minn. 116, 149 N.W.2d 37, 38-39 (1967), and that "establishing the reasonableness of the reliance is essential to any cause of action in which detrimental reliance is an element," Nicollet Restoration, Inc v. City of St. Paul, 533 N.W.2d 845, 848 (Minn. 1995).

Although Respondents attempt to evade Minnesota precedent on reasonable reliance by boldly asserting that “Minnesota courts have long recognized that a party can justifiably rely upon a representation unless its falsity is known or is obvious to him or her,” Respondents’ Br. at 38, this is not the law. Rather, the cases cited by Respondents stand for a different proposition: that a party’s failure to investigate does not mean that it unjustifiably relied on a factual representation. Spiess v. Brandt, 230 Minn. 246, 253, 41 N.W.2d 561, 566 (1950) (plaintiffs had not waived their right to rely upon defendants’ misrepresentations of material facts by failing to investigate, especially when defendants had actively thwarted plaintiffs’ attempts to examine the corporate books). Like Appellants, the Court of Appeals misread Spiess as standing for the proposition that “[a] party’s reliance is reasonable unless the party is on notice that the representation is not to be trusted or knows or has reason to know that the representation is false.” Hoyt Properties, Inc. v. Prod. Res. Group, LLC, 716 N.W.2d 366, 375 (Minn. Ct. App. 2006).

Because PRG’s reasonable reliance argument does not turn on Hoyt’s failure to investigate the corporate structures or operations of PRG, Haas, and Entolo before entering into the settlement agreement, the other cases cited by Respondents are similarly inapposite. Respondents’ Br. at 38. Erickson v. Midgarden, 226 Minn. 55, 57, 31 N.W.2d 918, 919 (1948) (“[A] purchaser can rely on representations relating to a prospective purchase, even though by making an actual inspection of the property . . . or by consulting the official survey records . . . the true condition of the premises would have been disclosed.”); Nave v. Dovolos, 395 N.W.2d 393, 398 (Minn. Ct. App. 1986)

("[A]ssertions of fact as to quality intended to induce a business transaction may be justifiably relied upon without further investigation.").

Indeed, this Court's decision in Spiess established the proper rule that reliance is tailored to "a person of the capacity and experience of the particular individual" who received the representations. Id. at 254, 41 N.W.2d at 567. In Spiess, this Court concluded that the plaintiffs' reliance was reasonable in light of their youthful inexperience, the apparent close friendship between plaintiffs and defendants, and the "disparity" in business experience between the parties. Id. Such circumstances are wholly absent here, where Hoyt's extensive business and legal background, experience negotiating hundreds of commercial transactions, practice of always memorializing all representations on which he intended to rely, and the adversarial relationship between Appellants and Respondents in the unlawful detainer action demonstrate any reliance was unreasonable as a matter of law.

Thus, Spiess's true relevance to this case lies in its holding that, in rescission actions based on alleged fraud, "the question is whether the representations were of such a character and were made under such circumstances that they were reasonably calculated to deceive" the plaintiff, given the plaintiff's "capacity and experience." Id. at 254, 41 N.W.2d at 567; Berg v. Xerxes-Southdale Office Bldg. Co., 290 N.W.2d 612, 616 (Minn. 1980) (same); Boubelik v. Liberty State Bank, 553 N.W.2d 393, 400 (Minn. 1996) (same). Therefore, in the context of settlement negotiations, Hoyt's sophistication in both business and legal matters, combined with his undisputed practice of memorializing

material representations in writing, and the other items set forth above make any reliance on Hoyt's part unreasonable as a matter of law.⁵

Instead of grappling with the cumulative effect of these circumstances, all of which support the unreasonableness of Hoyt's reliance, Respondents reprise the Court of Appeals' error by analyzing these factors in isolation or not at all. For instance, Respondents claim that, under Minnesota law, "even an experienced business man or an attorney can be misled by false statements." Respondents' Br. at 44 (citing Placke v. White-Price Co., 228 N.W. 554, 555 (Minn. 1930)). As Appellants observed in their opening brief, however, Placke supports a reasonable reliance inquiry based on the totality of the circumstances. Appellants' Br. at 35. To determine whether reliance was reasonable, the Placke Court looked not only to the capacity of the plaintiff, an individual "of ordinary business ability," but also to "the number and nature of the documents presented for signature, the representations made, and all the circumstances shown." Id. at 555-56. In Placke, the documents in question were voluminous and prepared by the defendant, and the plaintiff did not read them in their entirety. Id. at 149. This case is nothing like Placke. Here, the settlement agreement was two pages long and was drafted

⁵ First National Bank of Shakopee v. Halo Investments, 394 N.W.2d 158 (Minn. Ct. App. 1986), another case cited by Respondents, is not to the contrary. In First National Bank, the Court of Appeals concluded that plaintiffs had relied on defendants' misrepresentation of ownership where defendants had signed a mortgage document containing an express warranty of title. Id. at 160. Here, the fact that the settlement agreement included an integration clause but – in spite of Hoyt's undisputed standard practice of memorializing all material terms – lacked any written documentation of Robinson's alleged representation weighs heavily in the opposite direction, in favor of a conclusion that Hoyt's reliance was unreasonable as a matter of law.

by Hoyt's attorney before being reviewed by Hoyt, who promptly sent his attorney handwritten comments, and was executed by Hoyt the next day. (App. 228, Meyer Dep. at 46:15-47:8; App. 229, Meyer Dep. at 51:8-54:25; App. 210, Hoyt Dep. at 137:17-25.)

Respondents' remaining case law citations on reasonable reliance further highlight the particularized nature of the reasonable reliance inquiry. For instance, in Kempf v. Ranger, 132 Minn. 64, 155 N.W. 1059 (1916), this Court evinced special concern not for the sophisticated businessman or attorney, but for "those who are not capable of exercising the care that a man of average prudence would use." Id. at 68, 155 N.W. at 1061. It was in that context that this Court stated the familiar proposition that "[t]he question is not whether the representations would deceive the average man. It is a question whether they were of such a character and were made under such circumstances that they were reasonably calculated to deceive the plaintiff." Id. Similarly, in Kraus v. National Bank of Commerce of Mankato, 149 Minn. 108, 167 N.W. 353 (1918), this Court held that plaintiff – "a farmer 77 years of age who was not familiar with city property" and who had become so "forgetful" that "the probate court appointed a guardian of his estate a few months later" – could maintain a fraud action even though his reliance was not reasonable under an ordinary prudent person standard. Id. at 111, 167 N.W. at 354.⁶

The Court of Appeals and Respondents failed to recognize that the particularized reasonable reliance inquiry is not a one-way ratchet. Just as the standard of reasonable

⁶ The final case cited by Respondents, Old Colony Life Ins. Co. v. Moeglein, 165 Minn. 117, 118, 205 N.W. 885, 886 (1925), addresses actual reliance, not reasonable reliance.

reliance must be lowered for forgetful farmers unfamiliar with city property, so must it be raised for successful businessmen with decades of experience in multi-million-dollar commercial real estate deals, legal training and experience, a customary practice of recording all representations in writing, an active and informed role in the negotiation and drafting process, when engaged in settlement talks with an opposing lawyer. Hoyt is certainly no forgetful farmer; he is on the opposite end of the spectrum in terms of sophistication, and the reasonableness of his reliance must be viewed accordingly.

Respondents' topsy-turvy approach to reasonable reliance underlies its astonishing argument that "Hoyt's status as an attorney made his reliance more, not less justifiable" because "as an attorney, Hoyt knew that attorneys are not permitted to make false statements 'of fact or law'" under Minnesota Rule of Professional Conduct 4.1. Respondents' Br. at 45. Yet the 2005 comments to Rule 4.1 explain that what counts as a statement of fact, as opposed to a statement of legal opinion or position, "can depend on the circumstances. Under generally accepted conventions in negotiation, certain types of statements ordinarily are not taken as statements of material fact." Minn. R. Prof. Conduct § 4.1, cmt. 2. Respondents, like the Court of Appeals, once again disregard the fact that when it comes to determining the reasonableness of reliance, context matters.

The ABA's recent opinion letter on "Lawyer's Obligation of Truthfulness When Representing a Client in Negotiation: Application to Caucused Mediation," ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 439 (2006), is persuasive authority on

Rule 4.1's intended scope.⁷ The ABA opinion takes the position that "overstatements or understatements of the strengths or weaknesses of a client's position in litigation or otherwise, or expressions of opinion as to the value or worth of the subject matter of the negotiation . . . generally are not considered material facts subject to Rule 4.1" and "are statements upon which parties to a negotiation ordinarily would not be expected justifiably to rely." *Id.* Hoyt has shown no reason why the general conventions of negotiation would not apply here, where he asked for and received an assessment by opposing counsel of his potential piercing claim against PRG.

Further, as this Court has observed, the Preamble to the Rules of Professional Conduct establishes that "[t]he Rules are designed to provide guidance to lawyers and to provide a structure for regulating conduct through disciplinary agencies. They are not designed to be a basis for civil liability." *In re Proposed Petition to Recall Hatch*, 628 N.W.2d 125, 128 (Minn. 2001) (citing Minn. R. Prof. Conduct, Scope). When all the circumstances here are considered, Hoyt's alleged reliance on Robinson's alleged representations is unreasonable as a matter of law.

B. Respondents Have Also Failed to Establish Hoyt's Actual Reliance on the Alleged Representations.

Appellants have not waived their actual reliance argument because they fully briefed the actual reliance argument in the Court of Appeals. PRG's Brief to Court of Appeals at 35-38. However, the Court of Appeals inexplicably overlooked Appellants'

⁷ Contrary to Respondents' assertion, Respondents' Br. at 40, PRG has not waived this argument because the ABA Opinion on which PRG relied, Appellants' Br. at 33, published on April 12, 2006, "made these arguments newly-available" on appeal to this Court. *Peterson v. BASF Corp.*, 711 N.W.2d 470, 482 (Minn. 2006).

actual reliance argument. Hoyt, 716 N.W.2d at 374-75 (Minn. Ct. App. 2006) (portion of the Court of Appeals' opinion titled "Reliance" deals only with the reasonable reliance issue); App. 12-15. Thus, Appellants did not petition for review of the Court of Appeals' decision on actual reliance because there was no decision on this issue to review. Minn. R. App. P. 117, subd. 3(a) (petition for review must contain "a statement of the legal issues sought to be reviewed, and the disposition of those issues by the Court of Appeals"). Given the stringent page limits of the petition for review, Appellants heeded this Court's advice by "focusing the argument on the issue which best satisfies the criteria for review," Hapka v. Paquin Farms, 458 N.W.2d 683, 686 (Minn. 1990), rather than rebriefing an issue on which the Court of Appeals did not even rule.

Moreover, Respondents misstate Appellants' argument on actual reliance. Contrary to Respondents' straw man characterization, Appellants did not argue that Hoyt's failure to include a representation in a fully integrated contract, without more, precludes Hoyt from establishing actual reliance. Respondents' Br. at 48-49. What Appellants actually argued was that "the totality of the circumstances under which the release was negotiated, drafted, and executed," in conjunction with Hoyt's inconsistent accounts of the alleged exchange with Robinson, demonstrated Hoyt's failure to establish actual reliance as a matter of law. Appellants' Br. at 37-40. This argument in no way contravenes the line of cases following Ganley Bros. v. Butler Bros. Bldg. Co., 170 Minn. 373, 212 N.W. 602 (1927), which simply held that a plaintiff can state a cause of action for fraud, notwithstanding a clause in the contract expressly disclaiming reliance on representations. Id. at 375-376, 212 N.W. at 602-03.

Hoyt's failure to memorialize the alleged representations and the Settlement Agreement's integration clause are significant, not in isolation, but in light of the additional undisputed evidence of (1) Hoyt's customary practice of getting all representations in writing; and (2) the Settlement Agreement's express "carve-outs" for potential claims against PRG for fraudulent transfers and fraudulent misrepresentations of financial statements. (App. 206, Hoyt Dep. at 119:14-18; App. 246, Settlement Agreement at ¶7.) This Court has held that "the facts and circumstances surrounding the situation," not the plaintiff's testimony, "are the best measure of whether there was reliance or not." Witzig v. Philips, 274 Minn. 406, 412, 144 N.W.2d 266, 270 (1966); see also Watson v. Gardner, 183 Minn. 233, 237, 236 N.W. 213, 215 (1931) ("The testimony of a party that he relied upon representations made to him is, at most, only a statement as to his own mental reaction or state of mind. While he may directly so testify, such facts as intent, belief, and reliance, are perhaps more cogently shown by the facts and circumstances surrounding a transaction and the acts of the parties thereto.").

The undisputed facts and circumstances surrounding the drafting of the Settlement Agreement reveal Hoyt's inability to establish that he actually relied on Robinson's alleged representations. The first reason is that Hoyt inexplicably abandoned his standard business practice of reducing all representations and warranties relating to a transaction to writing (App. 194, Hoyt Dep. at 24:5-14), allegedly choosing instead to rely on the word of opposing counsel, whom he had never met before that day (App. 216, Robinson Dep. at 23:15-24:13; App. 200, Hoyt Dep. at 90:10-20). The second reason is that Respondents claim that Hoyt abandoned his standard business practices because he relied

on Robinson's representations yet, in the very same document, took care to expressly preserve possible claims for fraudulent transfers and fraudulent misrepresentation of Entolo's financial condition.

Because Hoyt's various submissions asserting actual reliance cannot overcome the weight of these undisputed facts and circumstances to the contrary, Appellants' Br. at 38-40, no reasonable jury could conclude that Hoyt actually relied on Robinson's alleged representations. This is especially clear when one considers that of the four individuals – Hoyt, Meyer (Hoyt's attorney), Kuller, and Robinson – involved in the alleged conversation about "piercing the veil," only one (Hoyt) has testified that such an exchange actually occurred. (App. 204: Hoyt Dep. at 112:10-11; App. 205, Hoyt Dep. at 114:9-12, 115:3-15; App. 237-238, Kuller Dep. at 66:15-68:6, 70:25-71:17; App. 220-221, Robinson Dep. at 48:4-49:8, 52:2-9; App. 227, Meyer Dep. at 42:6-43:23.)

III. THIS COURT SHOULD ADDRESS APPELLANTS' PARTIAL RESCISSION AND DISMISSAL WITH PREJUDICE ARGUMENTS, AND AFFIRM THE DISTRICT COURT'S RULING ON BOTH ISSUES.

As Appellants noted in their opening brief, this Court can and should resolve the two remaining issues in this case: whether the District Court properly held that Respondents' complaint pleaded only partial rescission of the Settlement Agreement and whether the District Court abused its discretion in dismissing Respondents' claims with prejudice. Appellants' Br. at 41 & n.4 (citing Hapka, 458 N.W.2d at 686).

Briefly, both issues turn on the District Court's disapproval of Respondents' creation of a procedural morass of improperly filed, never-filed, and internally inconsistent complaints, as well as the motions for leave to amend and "courtesy copies"

that accompanied them. Respondents now try to downplay their request for partial rescission as a “stray line in the Complaint,” Respondents’ Br. at 51 n.37, even though the request to rescind only the release of PRG in paragraph 7 of the Settlement Agreement appeared twice in the Complaint, under Count II and in the prayer for relief, (App. 62 ¶26, App. 63 ¶3), and Respondents took the trouble to amend this language in the First Amended Complaint they sent to the District Court on December 22, 2004 but never formally filed. (App. 343 ¶34, App. 347 ¶3.)⁸ If anything, it is Respondents’ offer to return consideration received under the Agreement that is the “stray line,”⁹ and Respondents should not be allowed to use their internally inconsistent pleadings to support either whole or partial rescission as they see fit.

Respondents’ arguments on dismissal with prejudice similarly reflect their wish to have their cake and eat it too – by voluntarily litigating claims which they have received leave to add, yet falling back on the fact that they were never formally filed, and by seeking both a dismissal without prejudice and an immediate appeal. This Court should not countenance such attempts to manipulate the Minnesota Rules of Civil Procedure.

⁸ Respondents’ contention that the partial rescission argument was not raised “on summary judgment or in any other context” is mysterious in light of the Court of Appeals’ holding that “the [state] district court . . . erred by dismissing Hoyt’s rescission claim on the alternative ground that it was a nonviable claim for partial rescission.” Hoyt, 716 N.W.2d at 376.

⁹ As Appellants noted in the opening brief, Respondents’ offer to return the monetary consideration would not restore the status quo ante in any event. Appellants’ Br. at 42.

IV. RESPONDENTS MISSTATE THE FACTS IN THE RECORD, AS WELL AS THE RELEVANCE OF THOSE FACTS TO THE ISSUES BEFORE THE COURT.

Whether PRG is the alter ego of Haas and Entolo is irrelevant to this appeal. Respondents dwell on this issue in a blatant attempt to curry favor with this Court and deflect attention from the real issues here. Respondents' argument should be rejected for those reasons alone.

In any event, Respondents' claim – that they would clearly prevail on the alter ego issue if allowed to go forward – is simply wrong. Respondents' one-sided version of the facts is based on their startling transformation of the federal district court's denial of PRG's motion for summary judgment in the Knight litigation, Knight v. Prod. Res. Group, LLC, 2005 WL 1630523, at *6-*7 (D. Minn. July 11, 2005), into a slam-dunk victory for them on the merits of their veil-piercing claim. In fact, the Knight court detailed the significant evidence in the record indicating that Haas and Entolo, and PRG were not alter egos, id. at *7, and additional evidence refuting the alter ego theory was before the trial court in this case.

This evidence was that, among other things:

- PRG played no role in arranging the lease between Hoyt and Haas (or the subsequent assignment of that lease to Entolo) that was at the heart of the parties' dispute. (App. 197: Hoyt. Dep. 46:21-47:7.) (App. 80, 100-101.)
- Entolo was a solvent, independently functioning corporation when it assumed Haas's duties under the lease. Knight, 2005 WL 1630523 at *7.

- Haas and Entolo had their own officers and directors, followed corporate formalities, and maintained corporate records. Id.
- Haas and Entolo had valid boards of directors that took action by unanimous written consent – which, under Minnesota law, has “the same force and effect as an action taken in a board meeting.” Id. at *6 (citing Minn. Stat. § 302A.239). These boards approved the GMAC financing agreement. Id.
- Pursuant to the GMAC financing agreement, Haas and Entolo deposited their receivables into a “lock-box” account, and those amounts immediately became the property of GMAC, not PRG. Id. at *5. This type of financing arrangement, designed to pay down debt to secured creditors, is not inherently unfair to unsecured creditors, Barzen, 553 N.W.2d at 450, nor is such an arrangement at all uncommon, Am. Commercial Lines v. Ostertag, 582 S.W.2d 51, 53 (Ky. Ct. App. 1979) (“[J]oint credit agreements are an inevitable consequence of a parent-subsidiary relationship.”).
- PRG did not use the GMAC financing agreement to siphon funds from its subsidiaries. Between May 2001 through January 2003, when Entolo ceased operations, Entolo received more funds from GMAC than it repaid to GMAC. (Supp. App. 7 ¶14.)
- Following September 11, Haas and Entolo’s business began collapsing, as evidenced by a 23% drop in sales from 2000 to 2001 and a precipitous 58% drop from 2001 to 2002. (Supp. App. 4 ¶¶9-10.) Thus, Haas’s and Entolo’s financial woes preceded and necessitated PRG’s increasing role in its subsidiaries’

activities. “This increase in control by the parent constitutes a reasonable reaction of a parent to its failing subsidiary” and therefore did not weigh in favor of piercing the parent’s corporate veil. Barzen, 553 N.W.2d at 450.

- Despite Respondents’ strident allegations of wrongdoing by PRG, the district court below and the Knight court rejected their claims that the GMAC financing agreement violated Minnesota’s Fraudulent Transfer Act. (App. 27, 37; Knight, 2005 WL 1630523 at *4-*6). Respondents abandoned this issue in the Court of Appeals.

Respondents also overstate the significance of the federal district court’s denial of PRG’s motion for summary judgment in the Knight litigation. The district court simply held that, “[v]iewing the evidence in the light most favorable to Plaintiffs,” Knight had raised a genuine issue of material fact on both prongs of the piercing-the-veil test: whether Haas and Entolo were mere instrumentalities and whether allowing the corporate veil to remain in place was unjust or unfair. Knight, 2005 WL 1630523 at *6-*8. This is a world apart from finding PRG liable on a piercing theory.

Finally, Respondents claim that Robinson knew PRG was liable on a veil-piercing theory, but they fail to acknowledge that at the time of the settlement negotiations with Hoyt on December 26, 2002, the unverified allegations of the Knight complaint were less than three weeks old. Moreover, PRG remained sufficiently confident in the position expressed by Robinson to move for summary judgment on the piercing issue in Knight.¹⁰

¹⁰ The district court heard argument on PRG’s summary judgment in Knight on May 20, 2005, and issued its decision on July 11, 2005. 2005 WL 1630523 at *1.

Robinson was not required to accept Knight's allegations as true in evaluating the viability of a piercing claim. Spitzmueller v. Burlington Northern Railroad Co., 740 F. Supp. 671, 674, 677 (D. Minn. 1990) (applying Minnesota law) (failure to disclose pending litigation was not a misrepresentation because "a pending legal claim . . . may be susceptible to a number of outcomes, some advantageous and some adverse to a party such as this defendant. But which outcome was likely to occur could not have been more than rank conjecture."). Thus, even if Respondents' factual assertions about alter ego were true – and they were not, as demonstrated above – the Knight complaint did not alert Robinson to any existing "facts" susceptible to misrepresentation. Therefore, Respondents' claim that it is clear that they will prevail on their alter ego allegation is wrong as well as irrelevant.

CONCLUSION

For the foregoing reasons, and the reasons stated in the opening brief, Appellants respectfully request that this Court reverse the decision of the Court of Appeals and affirm the District Court's entry of judgment in favor of Appellants.

Respectfully submitted,

Dated: November 9, 2006

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CERTIFICATE OF COMPLIANCE

Pursuant to Minnesota Rule of Civil Appellate Procedure 132.01 subd. 3, the undersigned hereby certifies, as counsel for Appellants, that this brief complies with the type-volume limitation as there are 6,941 words of proportional space type in this brief. This brief was prepared using Microsoft Word 2002.

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