

CASE NO. A07-1212

State of Minnesota
In Supreme Court

MARK SCHMITT,
Employee/Respondent,

vs.

INNOVATIVE LAWN SYSTEMS AND
TOTAL REPAIR SERVICES,
Employers/Respondents,

and

AMERICAN INTERSTATE INSURANCE CO.,
Insurer/Respondent,

and

WEST BEND MUTUAL INSURANCE CO.,
Insurer/Relator-Appellant,

and

MINNESOTA DEPARTMENT OF LABOR & INDUSTRY
REHAB UNIT, MINNESOTA DEPARTMENT OF HUMAN SERVICES,
ST. PAUL RADIOLOGY AND REGIONS HOSPITAL,

Intervenors,

and

SPECIAL COMPENSATION FUND,
Respondent.

**BRIEF OF RESPONDENT INNOVATIVE
LAWN SYSTEMS**

(Additional Counsel Listed on Following Page)

HANSEN, DORDELL, BRADT,
ODLAUG & BRADT, P.L.L.P.
John H. Guthmann (#123079)
Trisha A. Vicario (#343845)
3900 Northwoods Dr., Ste. 250
St. Paul, MN 55112
(651) 482-8900

Attorneys for Employer/Respondents

MINNESOTA DEPARTMENT
OF HUMAN SERVICES
Zennie Crudup
P.O. Box 64994
St. Paul, MN 55164-0994
(651) 431-3191

Intervenor/Respondent

ST. PAUL RADIOLOGY
Pang Her
166 Fourth Street E.
St. Paul, MN 55101-1421

Intervenor/Respondent

SPECIAL COMPENSATION FUND *Attorneys for Insurer/Respondent*

Thaddeus V. Jude
443 Lafayette Road
St. Paul, MN 55155
(651) 282-5005

Attorney for SCF/Respondent

JARDINE, LOGAN & O'BRIEN,
P.L.L.P.
Matthew P. Bandt (#306940)
8519 Eagle Point Blvd., Ste. 100
Lake Elmo, MN 55042
(651) 290-6579

Attorneys for Insurer/Appellant

BERNARD J. ROBICHAUD
Attorney Reg. No. 174014
211 Washington Ave. No.
Minneapolis, MN 55401
(612) 333-3343

Attorneys for Employee/Respondent

HEACOX, HARTMANN,
KOSHMRL, COSGRIFF
& JOHNSON, P.A.
Jay T. Hartmann (#124291)
550 Hamm Bldg.
408 St. Peter Street
St. Paul, Minnesota 55102
(651) 222-2922

MICHAEL G. GRIER (#132196)
7301 Ohms Lane, Suite 475
Edina, MN 55439
(952) 345-2805

*Attorney for Regions Hospital-
Intervenor/Respondent*

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STATEMENT OF LEGAL ISSUES

- I. If West Bend Mutual Insurance Company has no responsibility for Mark Schmitt's workers' compensation benefits, did the lower courts commit an error of law by ruling that Innovative Lawn Systems was not insured by American Interstate Insurance Company at the time of the employee's injury?**

The Compensation Judge ruled that American Interstate Insurance Company properly cancelled its policy.

The WCCA did not reach this issue because West Bend Mutual Insurance Company was ordered to provide insurance coverage to Innovative Lawn Systems.

Apposite Authority:

Minn. Stat. § 176.185

- II. Does substantial evidence support the compensation judge's ruling that West Bend is estopped from denying that it insured ILS for workers' compensation liability?**

The Compensation Judge Held: In the affirmative.

The WCCA Held: In the affirmative.

Apposite Authorities:

Neuberger v. Hennepin County Workhouse, 340 N.W.2d 330 (Minn. 1983);

Northern Petrochemical Co. v. U.S. Fire Ins. Co., 277 N.W.2d 408 (Minn. 1979);

O'Donnell v. Continental Casualty Co., 116 N.W.2d 680 (1962).

- III. Did the compensation judge have jurisdiction to determine if West Bend Mutual Insurance Company was estopped from denying that it insured ILS for workers' compensation liability?**

The Compensation Judge Held: In the affirmative.

The WCCA Held: In the affirmative.

Apposite Authorities:

Minn. Stat. §§ 176.181;

Minn. Stat. § 175A.01, subd. 5 (2004);

Minn. Stat. § 176.371;

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Kahn v. State, 289 N.W.2d 737 (Minn. 1980);

Pincombe v. Miketin Boarding Home, 1999 WL 984635 (W.C.C.A. Sept. 23, 1999).

IV. Is ILS entitled to an award of attorney's fees and costs against the insurer found responsible for workers' compensation benefits?

The Compensation Judge Held: In the negative.

The WCCA Held: In the negative.

Apposite Authorities:

Garrick v. Northland Insurance Co., 469 N.W.2d 709 (Minn. 1991);

Morrison v. Swenson, 274 Minn. 127, 138, 142 N.W.2d 640 (1966);

American Standard Insurance Co. v. Le, 551 N.W.2d 923 (Minn. 1996).

STATEMENT OF THE CASE

On November 30, 2004, Mark Schmitt (hereinafter “employee”) sustained a work-related injury to his left foot and ankle while employed by Innovative Lawn Systems (hereinafter “ILS”). The claim was tendered by ILS to West Bend Mutual Insurance Co. (hereinafter “West Bend”) but coverage was denied. After American Interstate Insurance Co. (hereinafter “American Interstate”) also denied coverage, the employee filed a Claim Petition against ILS, West Bend and American Interstate. The Special Compensation Fund was also named in case ILS was found to be uninsured. Both insurers refused to provide a defense to ILS. ILS was forced to retain counsel. Shortly before the hearing, American Interstate agreed to pay the employee’s benefits under a Temporary Order.

On June 14, 2006, Compensation Judge Gary Mesna conducted a hearing. In his Findings and Order of August 24, 2006, the compensation judge concluded that West Bend was estopped from denying workers’ compensation insurance coverage to ILS. (Appellant’s Appendix at A-4). The compensation judge also found that American Interstate had properly cancelled its prior workers’ compensation policy. (*Id.*). As a result of the estoppel, West Bend was ordered to reimburse American Interstate for all workers’ compensation benefits paid as a result of the employee’s injury and assume liability for any benefits that might be owed in the future. (*Id.* at A-4). The compensation judge also denied a claim by ILS for attorney’s fees from the insurer found responsible for benefits. (*Id.*).

West Bend appealed, claiming that the compensation judge erred as a matter of law and fact in both finding that West Bend was estopped from providing coverage and in failing to find coverage with American Interstate. ILS filed a cross appeal seeking review of the compensation judge's failure to award attorney's fees.

On May 24, 2007, the Workers' Compensation Court of Appeals (hereinafter "WCCA") affirmed. The WCCA held that it had jurisdiction to consider the estoppel issue. The WCCA further ruled that substantial evidence supported the compensation judge's Findings and Order that West Bend was estopped from denying that it provided workers' compensation coverage to ILS.

The WCCA also affirmed the compensation judge's denial of ILS' claim for attorney's fees. However, the WCCA made it clear that the claim for attorney's fees was rejected because the WCCA was hesitant to issue a ruling that would contradict the Minnesota Court of Appeals holding in *Sazama Excavating, Inc. v. Wausau Insurance Cos.*, 521 N.W.2d 379 (Minn. Ct. App. 1994). Even though the WCCA denied ILS' cross appeal for attorney's fees, the WCCA agreed that *Sazama* may not accurately represent Minnesota law. (Appellant's Appendix at A-16 to A-17.

West Bend appeals from the ruling of the WCCA. In addition, ILS has filed a notice of review, seeking review of the WCCA's denial of the claim for attorney's fees against West Bend.

STATEMENT OF FACTS

In the early 1990's, Jeff Trog and Dave Otterdahl went into business together, operating a business that engaged in activities that included construction, construction repair and maintenance, lawn care, light landscaping, erosion control and snow plowing. (June 14, 2006 Hearing Transcript (hereinafter T.) at 60-62). Jeff Trog and Mr. Otterdahl received legal advice that they should operate their various business activities through several corporations, each of which was devoted to a single type of business activity. (*Id.* at 62-63). As a result, five corporations were formed. They were named Structural Repair Systems, Inc., Valley Landscaping, Inc., Valley Erosion, Inc., Total Repair, Inc. and Valley Waterproofing, Inc. (*Id.* at 61-64).

Jeff Trog and Mr. Otterdahl insured their businesses through Dennis Just of the Ross Nesbit Agency. (*Id.* at 64-65). Mr. Just wrote workers' compensation coverage for the corporations with American Interstate. Structural Repair Systems, Inc. and Valley Landscaping, Inc. were listed on the declarations page of the policy as the named insured. Valley Erosion, Inc., Total Repair, Inc. and Valley Waterproofing, Inc. were added to the policy as additional named insureds through an Additional Insured endorsement. (American Interstate Ex. 2 (American Interstate policy) at p. 9; ILS Hearing Exhibit 3; Dennis Just's May 31, 2006 deposition (hereinafter "Just depo.") at 54-55). Each additional insured was individually entitled to all of the rights of the named insured. (Just depo. at 55).

On December 18, 2000, American Interstate sent Mr. Just a letter indicating that it would not issue a renewal on the policy and it mailed a notice of cancellation to Structural Repair Systems, Inc. (Just depo., Ex. 5). Cancellation of the coverage was to be effective on February 24, 2001. (*Id.*). Although five separate corporations were named insureds under the American Interstate policy, American Interstate only sent notice of cancellation to Structural Repair Systems. (Just depo., Ex. 5; Just depo. at 61-62). There is no evidence that American Interstate attempted to send a notice of cancellation to Valley Landscaping, Inc., Total Repair, Inc., Valley Erosion, Inc., or Valley Waterproofing, Inc. Moreover, it is undisputed that American Interstate never filed a notice that it was canceling the coverage of any of the five businesses with the State of Minnesota, as required by law. Minn. Stat. § 176.185 (2000).

On October 2, 2001 Jeff Trog and Mr. Otterdahl entered into a written agreement to end their business relationship. The agreement divided the existing corporations and accompanying assets. (American Interstate Hearing Ex. 10A). Valley Erosion, Inc. was not included in the settlement agreement. Although it was inactive, Valley Erosion, Inc. continued to exist with Jeff Trog as owner of 100% of the stock. (*Id.* at 68-69, 71).

After the Otterdahl dissolution, Jeff Trog decided to operate solely through Total Repair, Inc., although he continued to engage in basically the same business activities. (*Id.* at 71-72). Jeff Trog relied upon Mr. Just to place workers' compensation for his business. (*Id.* at 67). A policy was written through West

Bend and issued to Total Repair, Inc. (*Id.* at 34). The policy number was WCN 0608545. (American Interstate Hearing Ex. 8 (West Bend policy)).

In May 2002, John Trog approached his brother, Jeff Trog, because he wanted to go into the lawn care, snow plowing and light landscaping business. (T. at 72-73; 120). Jeff Trog agreed to help with financing. Jeff Trog's lawyer noted that Valley Erosion, Inc. was already incorporated for the same business purposes and advised that they continue to conduct business as Valley Erosion, Inc. (*Id.* at 72-73). John and Jeff Trog agreed but decided to change the name of the corporation from Valley Erosion, Inc. to Innovative Lawn Systems, Inc. (*Id.* at 121). They amended the articles of incorporation to reflect the new name and to include John Trog as a 50% owner of the corporation. (*Id.* 73-75; 121; American Interstate Hearing Ex. 10E-10F). John Trog was the company president, 50% shareholder and operated the business. (T. at 74-75). Jeff Trog was a 50% shareholder but was not involved in ILS' day-to-day business activities. Jeff Trog continued to operate Total Repair, Inc. (*Id.* at 74-75; 135).

John Trog had no prior experience operating a business. (*Id.* at 125). He therefore asked Jeff Trog what type of insurance he needed to obtain. (*Id.*). Jeff Trog suggested that John Trog contact Dennis Just for the insurance needs of the business. (*Id.* at 75-76; 94-95). Jeff Trog then called Dennis Just and informed him that his brother would be calling to obtain business insurance for ILS. (*Id.* at 75). Jeff Trog believed that Mr. Just would assist John Trog in purchasing "liability, auto, inland marine, and workers' compensation" insurance. (*Id.* at 76).

Jeff Trog testified that he relied up Mr. Just “a hundred percent [to provide all the insurance Innovative Lawn Care would need]. He’s taken care of us for 20 years.” (*Id.* at 75). Even Mr. Just conceded that Jeff Trog was relying on him to put the right insurance coverage for the business in place. (Just depo. at 90). Mr. Just also conceded that John Trog had no business insurance knowledge and that John Trog relied upon the Ross Nesbit Agency to provide the insurance ILS needed. (Just depo. at 90.).

Mr. Just has been a licensed insurance agent since approximately 1982-1983. (Just depo. at 21). He has written policies as an agent of American Interstate since approximately 1995-96 and West Bend since before joining the Ross Nesbit Agency in 1993. (*Id.* at 26-27). Mr. Just had a written contract with West Bend, which authorized Mr. Just to bind West Bend to coverage. (*Id.*, Ex. 1). Mr. Just testified that he had authority to bind insurance policies on behalf of West Bend. (*Id.* at 29, Ex. 1). West Bend does not dispute Dennis Just’s express authority to bind West Bend to coverage.

John Trog telephoned Mr. Just and spoke to him about obtaining insurance for ILS. (T. at 124). John Trog testified that he asked Mr. Just to provide him with “all the insurance needed to operate the business properly” and stated that he did not know what type of insurance he needed. (*Id.* at 125). He was relying on Mr. Just to obtain all necessary insurance. (*Id.*). As a part of the application process, Mr. Just requested and received ILS’ employer identification number. (Just depo. Ex. 7, at p. 2). After John Trog began bidding projects he learned that

most town home or condominium associations required that he have a million-dollar liability policy and a workers' compensation insurance policy. (T. at 128). Several customers required that he furnish a certificate of insurance demonstrating that he had the necessary insurance in force and effect. (*Id.* at 127-128).

When customers asked John Trog to furnish proof that he had workers' compensation and liability insurance, told Mr. Just what he needed to do business. (*Id.* at 129; Just depo. at 107). As a result, Mr. Just complied with the request and provided Certificates of Liability Insurance to ILS and its customers. (T. at 130; Just depo., Exs. 11-15; American Interstate Hearing Ex. 7). Mr. Just recalls being asked by both John and Jeff Trog to issue Certificates of Insurance on behalf of ILS and testified that there were "multitudes of them." (Just depo. at 106). The Certificates of Insurance described coverage and, in most cases, listed policy numbers for general liability, automobile liability, workers' compensation and employers' liability insurance. (Just depo. at 111; Just depo., Exs. 11-15; American Interstate Hearing Ex. 7). The workers' compensation policy listed on the certificates of insurance was West Bend policy number WCN 0608545, the workers' compensation policy under which Total Repair, Inc. was the named insured. (Just depo., Exs. 11-15; American Interstate Hearing Exs. 7-8).

John Trog testified that his customers accepted the certificates of insurance and, without the certificates, no association would hire ILS. (T. at 131-132). Mr. Just conceded knowing that his insureds request certificates of insurance in order to enable them to conduct business with their customers. (Just depo. at 34).

Additionally, Mr. Just expected that his insureds would rely on the accuracy of a certificate of insurance. (*Id.* at 36, 137) Finally, Mr. Just conceded that the insurance certificates were a representation that the West Bend policy insuring Total Repair, Inc. for workers' compensation also covered ILS. (*Id.*)

On November 30, 2004, employee sustained a work-related injury to his left foot and ankle while employed by ILS. Almost immediately after the injury, John Trog contacted Mr. Just about filing the employee's workers' compensation claim. (T. at 137). Mr. Just told John Trog to locate his insurance file, fill out a claim form and fax it to him as soon as possible. (*Id.*). However, when John Trog looked in his insurance file, he discovered that it contained no accident report forms. (*Id.*). As such, John Trog immediately called Mr. Just and explained the situation. (*Id.*). Mr. Just told John Trog to get an accident report form out of the Total Repair, Inc. file, fill it out and fax it to him. (*Id.*). With Mr. Just's assistance, John Trog completed both a "Supervisor's Report of Accident" and "First Report or Injury." (*Id.*, T. at 138-140). Mr. Just instructed John Trog to list ILS as a division of Total Repair on the "Supervisor's Report of Accident" form. (*Id.* at 140). Mr. Just then filed the claim with West Bend. (*Id.* at 141-142). Mr. Just later told John Trog that West Bend denied coverage because ILS was not insured by the West Bend workers' compensation policy. (T. at 142).¹

¹ As part of the WCCA appeal, ILS offered two pieces of post hearing evidence demonstrating that West Bend considered the Schmidt claim to have been covered by the policy it issued to Total Repair, Inc. The WCCA opinion did not comment on the evidence in its opinion. *See* ILS Cross Appeal Brief at 8-9.

STANDARD OF REVIEW

West Bend argues on appeal that American Interstate should be primarily liable for the employee's benefits because it failed to provide proper notice of cancellation of insurance to Valley Erosion/ILS. West Bend also contends that the compensation judge did not have jurisdiction to find that it was estopped from denying ILS' coverage. Through its notice of review, ILS contends that whichever insurer is liable for benefits, ILS is entitled to its attorney's fees.

The notice of cancellation, jurisdiction and attorney's fees issues require application of the law to essentially undisputed facts. A decision that rests upon an application of the law, a mixed question of fact and law or application of the law to essentially undisputed facts may be reviewed *de novo*. *Meyering v. Wessels*, 383 N.W.2d 670, 672 (Minn. 1986); *Krovchuk v. Koch Oil Refinery*, 48 W.C.D. 607, 608 (W.C.C.A. 1993), *summarily aff'd* (Minn. June 3, 1993)). ILS agrees that the Supreme Court owes no deference to either of the lower court rulings regarding the jurisdiction, notice of cancellation and attorney's fees issues.

West Bend also appeals from the WCCA opinion affirming the compensation judge's factual determination that West Bend was estopped from denying coverage to ILS. Appellate review of a factual determination is controlled by the substantial evidence standard. *Hengemuhle v. Long Prairie Jaycees*, 358 N.W.2d 54, 37 W.C.D. 235 (Minn. 1984). The Supreme Court must affirm factual findings unless they were clearly erroneous and unsupported by substantial evidence in view of the entire record submitted. Minn. Stat. § 176.421, subd. 1 (1992).

Substantial evidence supports a finding if, in the context of the entire record, it is “supported by evidence that a reasonable mind might accept as adequate.” *Hengemuhle*, 358 N.W.2d at 59. Factual findings are clearly erroneous only if, after reviewing the entire record, the court is left with a definite and firm conviction that a mistake has been committed. *Northern States Power Co. v. Lyon Food Prods., Inc.*, 304 Minn. 196, 201, 229 N.W.2d 521, 524 (1975). Findings should not be disturbed, even though the reviewing court might disagree with them, unless they are clearly erroneous in the sense that they are manifestly contrary to the weight of the evidence or not reasonably supported by the evidence as a whole. *Id.*

West Bend’s WCCA brief conceded that review of the estoppel issue was controlled by the substantial evidence standard. West Bend’s WCCA brief at 9. However, West Bend now seeks the benefit of *de novo* review. West Bend was right the first time. Neither the law of estoppel nor its application is in dispute. Rather, West Bend disputes whether there were sufficient facts to warrant an estoppel.² As a uniquely factual issue, the WCCA correctly determined that the substantial evidence standard applies to judicial review of the estoppel question. *See Drake v. Reile’s Transfer & Delivery, Inc.*, 613 N.W.2d 428, 434 (Minn. Ct. App. 2000) (application of equitable estoppel a question of fact).

² West Bend’s Statement of Facts is extremely selective, resulting in a manifestly unfair representation of the record reviewed by the compensation judge. The substantial evidence standard requires consideration of the entire record, not just that portion of the record supporting a party’s legal position.

ARGUMENT

I. WHILE AMERICAN INTERSTATE IMPROPERLY TERMINATED VALLEY EROSION'S INSURANCE COVERAGE, IT IS ONLY SECONDARILY LIABLE TO WEST BEND.

The compensation judge ruled that American Interstate did not have to follow the workers' compensation insurance policy cancellation procedure that is mandated by statute. However, both courts found that West Bend was estopped from denying workers' compensation coverage. ILS agrees with West Bend that American Interstate improperly cancelled coverage. However, ILS disagrees with West Bend's assertion that the issue is relevant. The insurance cancellation issue should be considered only if the Supreme Court reverses the lower courts and holds that West Bend has no liability. The WCCA properly avoided the insurance cancellation issue because West Bend's liability renders the issue moot.

A. American Interstate failed to effectively cancel the Valley Erosion/ILS policy.

Although the insurance cancellation issue is moot, it must be addressed because it was West Bend's lead argument. The Legislature enacted a strict procedure for an insurer to cancel a policy of workers' compensation insurance. If the procedure is not followed, cancellation is ineffective. To effectively cancel a policy of workers' compensation, an insurer shall:

[f]ile notice of coverage with the commissioner under rules and on forms prescribed by the commissioner. No policy shall be canceled by the insurer within the policy period nor terminated upon its expiration date until a notice in writing is delivered or mailed to the insured.

Minn. Stat. § 176.185, subd. 1 (2000). In addition to requiring an insurer to provide notice to the insured, the statute also requires that the notice of cancellation be “filed with the commissioner [of the Department of Labor and Industry]” by the insurer. *Id.*

Thus, the statute contains two prerequisites. Failure by the insurance company to complete *both* prerequisites results in an ineffective cancellation. *Id.*

In this case, ILS is the same corporation that American Interstate insured under the name Valley Erosion, Inc. It is undisputed that Valley Erosion, Inc. followed the requirements of Minnesota law and legally changed its name to ILS. Furthermore, American Interstate admits that it failed to satisfy both statutory prerequisites in the case of Valley Erosion, Inc./ILS. It is undisputed that American Interstate made no attempt to send a notice of cancellation to Valley Erosion, Inc., a named insured. It is also undisputed that American Interstate never filed a notice of cancellation with the Commissioner of the Department of Labor and Industry in the case of any of the five corporations in which Jeff Trog had an ownership interest, including Valley Erosion, Inc.

Based upon an application of the strict and unambiguous requirements contained in the statute, there should be no issue as to American Interstate’s workers’ compensation liability in the event that West Bend has no coverage obligation. However, instead of following the statute, the compensation judge adopted American Interstate’s unprecedented argument that the statute can be ignored under the “right” circumstances. Because the statute is mandatory and has

no exceptions, American Interstate's position can only prevail if this court agrees that a compensation judge can rewrite a statute.

The compensation judge opined that because "Jeff Trog received the notice [of cancellation sent to]" Structural Repair Systems, Inc., "the notice of cancellation was effective to terminate and cancel the policy of insurance that covered Valley Erosion, Inc. as an additional named insured." (Appellant's Appendix at A-3). The compensation judge also agreed with American Interstate's invitation to disregard the statute because Valley Erosion, Inc. was an "inactive" company for a year and that Jeff Trog procured insurance for only his "active" companies. (*Id.*). Finally, the compensation judge concluded that since ILS was a "new and different business with a new name and a new owner, failure to properly cancel the policy that had covered Valley Erosion, Inc. would not extend coverage to a new and different company." (*Id.*).

By allowing a coverage cancellation with neither a notice to each named insured nor a filing with the Commissioner for the Department of Labor and Industry, the compensation judge essentially repealed the requirements of Minn. Stat. § 176.185. Further, the compensation judge created an "inactive" versus "active" company distinction found nowhere in the statute. The statute requires notice to all insured companies, not just "active" companies.

The compensation judge's basis for disregarding the statute places many businesses at risk of losing their insurance. Individuals and corporations routinely purchase closely-held and publicly traded stock. Name and ownership changes are

perfectly legal transactions and have nothing to do with the validity of a corporation's insurance policies. Performing a legal transaction is no basis for voiding an insurance policy.

Here, American Interstate admits that it failed to provide notice of cancellation of workers' compensation insurance to Valley Erosion, Inc. and that it failed to file a notice of cancellation with the Commissioner for the Department of Labor and Industry. Whether Valley Erosion, Inc./ILS amended its articles of incorporation, changed its name or changed the make up of its stockholders, or is inactive as a business is irrelevant to a determination under Minn. Stat. § 176.185. The notice requirements contained within Minn. Stat. § 176.185 are not mere suggestions—they are mandatory for insurers. Accordingly, if this Court finds no coverage with West Bend, the plain and unambiguous language of the workers' compensation statute requires a finding that American Interstate covered ILS for the Mark Schmitt injury.

B. American Interstate's improper cancellation of coverage is moot if West Bend is found to provide coverage.

One need only examine the purpose of Minn. Stat. § 176.185 to reject West Bend's argument that American Interstate should have the first coverage priority. Section 176.185 was enacted to provide for continuous worker's compensation coverage to all eligible employees by affording the employer ample notice and time so that it can procure insurance when its existing policy terminates or is cancelled. *Ives v. Sunfish Sign Co., Inc.*, 275 N.W.2d 41, 43 (Minn. 1979) (citing

Kenny v. AAA Delivery Service, 391 Mich. 454, 457 (1974); *Nehring v. Bast*, 103 N.W.2d 368, 375 (Minn. 1960); *T.H. Mastin & Co. v. Russell*, 214 Miss. 700, 708 (1952); and, *Moore v. Adams Electric Co.*, 264 N.C. 667 (1965)).

Further, in *Donarski v. Lardy*, 251 Minn. 358, 88 N.W.2d 7 (1958), the Minnesota Supreme Court required the insurer to prove that the insured received actual notice. *Id.* The court imposed this requirement based on Minnesota's public policy of providing ample opportunity for insureds to procure other insurance. *Id.* at 364-65, 88 N.W.2d at 12.

In the instant case, West Bend is the proper insurer. The statutory purpose of providing continuous coverage for ILS is served by rejecting West Bend's appeal. West Bend should not be permitted to hand off the liability it is estopped from denying to American Interstate.

II. ILS HAD NO WAY OF KNOWING MINNESOTA'S STATUTORY INSURANCE CANCELLATION REQUIREMENTS.

West Bend argues for the first time on appeal to the Minnesota Supreme Court that ILS could not have relied on West Bend to its detriment if it had American Interstate coverage. An issue cannot be raised for the first time on appeal to the Minnesota Supreme Court. *Thiele v. Stich*, 425 N.W.2d 580, 582 (Minn. 1988).

Even if the court considers the issue, it should discard West Bend's position. There is no evidence in the record that ILS had any notion of what was required to cancel a workers' compensation insurance policy under Minnesota

law. In fact, the only workers' compensation insurance ILS thought it had was with West Bend. To accept West Bend's argument is to accept a fictional view of the facts. There is overwhelming evidence in the record to establish that ILS relied to its detriment on the representations of West Bend, through its agent, alone. West Bend's new attempt to pass off its liability on American Interstate must be rejected.

III. ILS RELIED TO ITS DETRIMENT ON THE REPRESENTATIONS OF COVERAGE BY WEST BEND, THROUGH ITS AGENT.

On appeal to the Minnesota Supreme Court, West Bend jettisons all of its previous arguments against estoppel in favor of a single assertion. West Bend argues that it was unreasonable for ILS to rely on the representations of coverage by West Bend's agent when "ILS conceded it never informed the agent that it had Employees." (Appellant's Brief at 17). For an issue that West Bend claims should be decided as a matter of law, it is interesting that West Bend fails to discuss the legal standard for estoppel, instead focusing on its narrow view of the factual record.³

As the WCCA correctly noted, whether equitable estoppel is applicable depends on the facts of each case and is a question for the trier of fact. *O'Donnell v. Continental Casualty Co.*, 263 Minn. 331, 116 N.W.2d 680, 684 (1962); see *Drake v. Reile's Transfer & Delivery, Inc.*, 613 N.W.2d 428, 434 (Minn. Ct. App.

³ In addition, West Bend has never disputed the fact that Mr. Just and the Ross Nesbit Agency had actual and apparent authority to bind West Bend to a workers' compensation policy. (Appellant's Appendix at A-14).

2000) (application of equitable estoppel a question of fact). The one isolated fact cited by West Bend does not overcome the overwhelming record in favor of the compensation judge's application of the estoppel doctrine.

The doctrine of equitable estoppel may be invoked "to prevent a party from taking unconscionable advantage of [its] own wrong by asserting [its] strict legal rights." *Northern Petrochemical Co. v. U.S. Fire Ins. Co.*, 277 N.W.2d 408, 410 (Minn. 1979); see *Neuberger v. Hennepin County Workhouse*, 340 N.W.2d 330 (Minn. 1983). Three elements must be satisfied to establish an equitable estoppel: (1) promises or inducements were made by one party; (2) the other party reasonably relied upon the promises or inducements; and, (3) the relying party was or will be harmed if estoppel is not applied. *Eide v. State Farm Mutual Automobile Ins. Co.*, 492 N.W.2d 549, 556 (Minn. Ct. App. 1992).

What West Bend fails to explain is how the failure to inform Mr. Just that ILS had employees has anything to do with reliance on the affirmative representations of coverage contained in the certificates of insurance. In fact, the record demonstrates that John Trog had no understanding of whether information about his employees was relevant to his need for workers' compensation insurance. To the contrary, the record is replete with references to John Trog's lack of business and insurance sophistication and his total reliance upon Mr. Just. Notably, West Bend omits any discussion of the key facts that produced the outcome in this case: John Trog specifically advised Mr. Just that his customers required him to carry workers' compensation insurance; John Trog requested

written proof that he carried workers' compensation insurance; West Bend, through its agent, provided the written proof to both John Trog and his customers; and, John Trog believed that the commercial insurance package he paid for included workers' compensation coverage.

Mr. Just understood something that West Bend fails to understand. Even Mr. Just expected ILS to rely on the accuracy of certificates of insurance to prove that ILS carried the insurance listed on the certificate. (Just depo. at 36, 137).

West Bend's citation of one fact, taken out of context, does not permit a holding that the compensation judge made clearly erroneous findings of fact. The evidence supporting application of the estoppel doctrine is overwhelming in this case. A reversal of the lower court rulings would render ILS liable for both the employee's compensation benefits, the amount for actual and necessary disbursements expended by the Special Compensation Fund, and a penalty in the amount of 65% of all compensation benefits ordered to be paid. Minn. Stat. § 176.183, subd. 2 (2006). Relieving West Bend of liability for events completely within its control would not only result in great injustice to ILS but would essentially condone West Bend and its agent's affirmative misrepresentations to ILS. The lower court rulings must be affirmed.

IV. THE COMPENSATION JUDGE HAD JURISDICTION TO ESTOP WEST BEND FROM DENYING WORKERS' COMPENSATION COVERAGE.

The workers' compensation courts have jurisdiction to hear and determine "all questions of fact and law arising under the workers' compensation laws."

Minn. Stat. § 175A.01, subd. 5 (2004); Minn. Stat. § 176.371. The workers' compensation law contains the statutes that control all aspects of workers' compensation insurance. Minn. Stat. §§ 176.181, .185. Despite the fact that the statutes governing insurance coverage are part of the workers' compensation act, West Bend argues that this case does not involve an issue pertaining to "the laws relating to workers' compensation." West Bend's Brief at 19.

West Bend's position flies in the face a long case history. Insurance coverage issues necessarily require compensation judges to apply the law of insurance contract formation and agency principles. Indeed, West Bend concedes that the workers' compensation courts routinely decide these issues. West Bend's Brief at 18-19 (citing; *Nehring v. Bast*, 103 N.W.2d 368 (Minn. 1960); *Oster v. Riley*, 150 N.W.2d 43 (Minn. 1967); and, *Runnoe v. Bobs Business of Dorset, Inc.*, slip. op., No. 474-62-7391, 1994 WL 738334 (W.C.C.A. Dec. 27, 1994)); *see also Steidel v. Metcalf*, 297 N.W. 324 (Minn. 1941); *Krebs v. Krebs*, 36 W.C.D. 288 (W.C.C.A. 1983).

In addition, West Bend does not question the fact that the workers' compensation courts have applied estoppel principles on numerous occasions. *See, e.g., Lofgren v. Pieper Farms*, 540 N.W.2d 834 (Minn. 1995); *Neuberger v. Hennepin County Workhouse*, 340 N.W.2d 330 (Minn. 1983) (employer estopped from asserting statute of limitations); *Kahn v. State*, 289 N.W.2d 737 (Minn. 1980) (employer estopped from raising delay in filing of formal notice to bar employee's claim when delay was induced by employer's agent); *Pincombe v. Miktin*

Boarding Home, slip. op., No. 502-64-6788, 1999 WL 984635 (W.C.C.A. Sept. 23, 1999) (upholding compensation judge's imposition of insurance coverage by estoppel). Yet, West Bend argues that the workers' compensation courts do not have jurisdiction to estop West Bend from denying ILS' workers' compensation coverage because jurisdiction has never been challenged before. In essence, West Bend argues that all of the decisions cited above are null and void.

The WCCA correctly explained the basis for its jurisdiction in detail. Appellant's Appendix at A-12 to A-13. Strangely, West Bend does not challenge the logic or accuracy of the WCCA's recitation of applicable law. West Bend claims that the instant case does not involve "the laws relating to workers' compensation" but never provides a basis for its bald assertion. The only "support" offered by West Bend for its position is a citation to *Taft v. Advance United Expressway*, 464 N.W.2d 725 (Minn. 1991). However, as noted by the WCCA, *Taft* is completely distinguishable. In *Taft*, the workers' compensation courts were found to lack jurisdiction to apply the Minnesota Insurance Guaranty Act [MIGA], which governs insolvent insurance companies. The holding in *Taft* was premised upon the fact that MIGA's obligations were governed solely by Minn. Stat. § 60C, et. seq. Obviously, the workers' compensation courts could not interpret or apply a statute located entirely outside the workers' compensation law.

Taft provides no analogy to the instant case. The statutes creating the workers' compensation coverage obligation that West Bend is estopped from denying are found entirely within the Workers' Compensation Act. As stated by

the WCCA, “the issue of insurance coverage was clearly ancillary to the employee’s claim for benefits and therefore fell within the purview of the compensation judge’s adjudication of issues arising under the Workers’ Compensation Act.” Appellant’s Appendix at A-13.

Jurisdiction may be raised either by a party or *sua sponte* by the court. As such, West Bend’s proposition that no one ever thought to raise a jurisdictional defense before is incredible.⁴ West Bend’s jurisdictional argument must be rejected.

V. REGARDLESS OF WHICH INSURER IS FOUND LIABLE FOR THE EMPLOYEE’S BENEFITS, INNOVATIVE LAWN SYSTEMS IS ENTITLED TO AN AWARD OF ATTORNEY’S FEES.

In the instant case, both insurers denied coverage to ILS and refused to provide a defense. However, the lower courts each denied ILS’ request for an award of attorney’s fees. Thus, when West Bend filed its Petition for Writ of Certiorari, ILS filed a Notice of Review in connection with the attorney’s fee issue. For the reasons set forth below, ILS is entitled to an award of attorney’s fees against whichever insurer is ordered to provide insurance coverage.

After both West Bend and American Interstate denied coverage, the employee was forced to file a Claim Petition and ILS was required to retain counsel at its own expense. Eventually, within days of the first scheduled hearing,

⁴ West Bend argues that this case really involves a tort or contract claim against the Mr. Just. West Bend seeks to divert attention from the real issue. This case involves a claim against West Bend, not a claim against West Bend’s agent, Dennis Just. The fact that West Bend, ILS, or both, may have also have tort or contract claims against Mr. Just does not change or affect the issues presented in this case.

American Interstate picked up benefits under a temporary order and a new hearing date was selected. Neither insurer has ever accepted its duty to defend ILS.

The compensation judge denied ILS' claim for attorney's fees on the basis that West Bend's liability is predicated upon an estoppel, not a contract, theory. (Appellant's Appendix at A-4). ILS asserts that it is entitled to an award of attorney's fees regardless of the theory of liability.

The WCCA saw the issue of attorney's fees differently. The WCCA accepted each of ILS' arguments for an award of fees. However, the WCCA affirmed the compensation judge's order because it was hesitant to issue a decision inconsistent with the Minnesota Court of Appeals' opinion in *Sazama Excavating, Inc. v. Wausau Insurance Cos.*, 521 N.W.2d 379 (Minn. Ct. App. 1994), *pet. for rev. denied* (Minn. Oct. 27, 1994). (WCCA Opinion, Appellant's Appendix at A-17). ILS asserts that the time has come to overrule *Sazama Excavating, Inc.*

When an insurer breaches its contract by failing to provide a defense to an arguably covered claim, and litigation is required for the insured to enforce its right to a defense and indemnification, the insured is generally awarded fees and costs. *Garrick v. Northland Insurance Co.*, 469 N.W.2d 709, 714 (Minn. 1991); *Morrison v. Swenson*, 274 Minn. 127, 138, 142 N.W.2d 640, 647 (Minn. 1966). The obligation to pay attorney's fees can only be avoided if the insurer provides an attorney to the insured at its own expense under a reservation of rights. *American Standard Insurance Co. v. Le*, 551 N.W.2d 923, 927 (Minn. 1996).

Here, both insurers denied coverage, refused to furnish a defense and left ILS to hire counsel at its own expense. The compensation judge denied ILS' claim for attorney's fees because insurance coverage was imposed by estoppel. The compensation judge made a distinction without a difference. Regardless of how coverage came to exist, West Bend was found liable to provide workers' compensation coverage for the employee's claim. West Bend admitted at oral argument before the WCCA that its workers' compensation policies include coverage for litigation defense costs. In other words, the cost of defending ILS is as much a part of the obligation West Bend was estopped from denying as the workers' compensation benefits it owes the employee. Thus, the theory of liability is irrelevant to West Bend's liability for attorney's fees and costs.

The WCCA denied ILS' claim for attorney's fees through its reluctant application of *Sazama Excavating, Inc.* In *Sazama Excavating, Inc.*, the insured commenced a declaratory judgment action against Wausau in district court after it failed to follow the policy cancellation procedure set forth in the applicable policy, refused to pay a claim, and refused to provide a defense to the insured. 521 N.W.2d at 381. The Minnesota Court of Appeals affirmed the trial court's ruling that Wausau improperly cancelled the policy but reversed the trial court's award of attorney's fees to the insured. *Id.* at 383-84. The court of appeals rationalized its refusal to apply *Morrison* and its progeny on the basis that workers' compensation is a creature of statute and that common law principles, such as the *Morrison* rule, should not be applied to a workers' compensation policy. *Id.*

The WCCA found “merit” to ILS’ argument that *Sazama Excavating, Inc.* does not represent the law and should be overruled. (WCCA Opinion, Appellant’s Appendix at A-17). The premise for the holding in *Sazama Excavating, Inc.* was a demonstrably erroneous belief that common law principles, such as those found in *Morrison*, do not apply to workers’ compensation cases absent express legislative authorization because workers’ compensation is statutorily based. *Id.* at 384.

As noted by the WCCA, numerous common law concepts have been applied to resolve workers’ compensation disputes without legislative intervention. (WCCA Opinion at A-17, n.4) (citing *Neuberger v. Hennepin County Workhouse*, 340 N.W.2d 330 (Minn. 1983) (employer estopped from asserting statute of limitations); *Westendorf v. Campbell Soup Co.*, 309 Minn. 550, 243 N.W.2d 157 (Minn. 1976) (res judicata); *Denardo v. Divine Redeemer Memorial Hosp.*, 450 N.W.2d 290 (Minn. 1990) (equitable apportionment); *Kahl v. Minnesota Wood Specialty, Inc.*, 277 N.W.2d 395 (Minn. 1979) (attorney-client privilege)). *See also Nguyen v. Compass Group USA*, slip. op., No. 575-61-8492, 2004 WL 692073 (W.C.C.A. Feb. 12, 2004) (applying common law fraud principles of *Weise v. Red Owl Stores, Inc.*, 286 Minn. 199, 202, 175 N.W.2d 184, 187 (Minn. 1970)).

The *Sazama Excavating, Inc.* court also found that because the rights and liabilities of workers’ compensation insurers are imposed by statute, and not by private contract, an award of attorney’s fees in a coverage dispute is precluded absent legislative action. *Sazama Excavating, Inc.*, 521 N.W.2d at 384. Again,

and with all due respect, the court of appeals' premise is not accurate. For example, under the no-fault act, liability insurance is mandated by statute. Minn. Stat. § 65B.48 (2004). No-fault insurance is but another statutory scheme. Yet, attorney's fees are routinely awarded in coverage cases when insurers have refused to comply with a contractual duty to defend. In fact, an auto policy was at issue when the *Morrison* rule was reaffirmed by the *American Standard* court. 551 N.W.2d at 923-24. As the WCCA recognized, there is no rational basis to distinguish between statutorily mandated automobile insurance and statutorily mandated workers' compensation insurance when applying the *Morrison* rule.

Moreover, the workers' compensation statute does not require insurers to include a duty to defend in workers' compensation policies. Minnesota law only requires insurers to cover statutory workers' compensation benefits. Minn. Stat. § 176.185, subd. 3-4 (2004). Thus, insertion of a duty to defend into workers' compensation policies is *purely* a private function and has nothing to do with the state's police power. As such, the *Sazama Excavating, Inc.* court was mistaken in its belief that the duty to defend in a workers' compensation policy is based solely upon statutory rather than common law principles.

The WCCA was absolutely correct in stating that *Sazama Excavating, Inc.* allows workers' compensation insurers to breach their contractual duty to defend, leaving insured employers with no remedy. (WCCA Opinion, Appellant's Appendix at A-17). The Minnesota Supreme Court should do what the WCCA

felt constrained from doing—overrule *Sazama Excavating, Inc.* and award ILS its attorney's fees and costs.

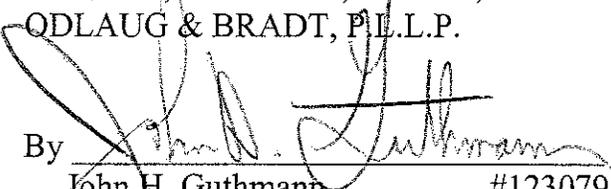
CONCLUSION

The Minnesota Supreme Court should affirm the lower court rulings that estopped West Bend from denying workers' compensation insurance to ILS. If however, the estoppel holding is reversed, ILS is nevertheless entitled to insurance coverage from American Interstate due to its ineffective cancellation of the policy it issued to Valley Erosion/ILS. Finally, and regardless of which insurance company is ordered to cover ILS, the court should overrule the Minnesota Court of Appeals decision in *Sazama Excavating, Inc.* and award ILS its attorney's fees.

Respectfully submitted.

Dated: August 17, 2007

HANSEN, DORDELL, BRADT,
ODLAUG & BRADT, P.L.L.P.

By 

John H. Guthmann #123079

Trisha A. Vicario #343845

Attorneys for Respondents
3900 Northwoods Drive, Suite 250
St. Paul MN 55112
651-482-8900