

NO. A10-714

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State of Minnesota  
**In Supreme Court**

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David and Melynda Quade,

*Respondents,*

vs.

Secura Insurance,

*Appellant.*

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**APPELLANT'S REPLY BRIEF**

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**TABLE OF CONTENTS**

	<u>Page</u>
TABLE OF AUTHORITIES .....	iii
ARGUMENT .....	1
I.    Resolution of the Disputed Issue Does Not Require the Appraisers to Interpret the Policy or Make Determinations Regarding Coverage. ....	3
II.   This Case Does Not Present a Liability or Coverage Dispute, But Instead Presents a Purely Factual Question Regarding the Amount of the Storm-Related Damage. ....	4
III.  The District Court Properly Followed a Century of Precedent In Ordering That the Enforcement of the Appraisal Award Was Governed By Minnesota Statutes Applicable to Arbitration Proceedings. ....	11
CONCLUSION .....	13

**TABLE OF AUTHORITIES**

	<b><u>Page</u></b>
<b><u>Cases</u></b>	
<i>American Central Ins. Co. v. Ramsey County</i> , 125 Minn. 274, 147 N.W. 242 (1914).....	2, 3, 4, 6, 12
<i>Beebout v. St. Paul Fire &amp; Marine Ins. Co.</i> , 365 N.W.2d 271 (Minn. App. 1985).....	12
<i>David A. Brooks Enterprises, Inc. v. First Systems Agencies</i> , 370 N.W.2d 434 (Minn. App. 1985).....	12
<i>Itasca Paper Co. v. Niagara Fire Ins. Co.</i> , 175 Minn. 73, 220 N.W. 425 (1928).....	2, 3,6
<i>Kavli v. Eagle Star Ins. Co.</i> , 206 Minn. 360, 288 N.W. 723 (1939).....	7, 11
<i>Mork v. Eureka-Security Fire &amp; Marine Ins. Co.</i> , 230 Minn. 382, 42 N.W.2d 33 (1950).....	5
<i>QBE Ins. Corp. v. Twin Homes of French Ridge Homeowners Ass’n</i> , 778 N.W.2d 383 (Minn. App. 2010).....	2, 6, 11
<i>Sampson v. Horace Mann Ins. Co.</i> , No. A03-158, 2003 Minn. App. LEXIS 1215 (Sept. 30, 2003).....	2, 6
<b><u>Minnesota Federal Cases</u></b>	
<i>Orient Ins. Co. v. Skellet Co.</i> , 28 F.2d 968 (8th Cir. 1928) .....	2
<b><u>Statutes</u></b>	
Minn. Stat. § 572.08-572.30.....	11

**Extrajurisdictional**

*Cigna Ins. Co. v. Didimoi Property Holdings, N.V.*, 110 F. Supp.2d 259  
(D. Del. 2000)..... 7

*Fox v. The Employers’ Fire Ins. Co.*, 113 N.E.2d 63 (Mass. 1953) ..... 11

*Johnson v. Nationwide Mut. Ins. Co.*, 828 So.2d 1021 (Fla. 2002) ..... 7, 8, 9, 10

*Kendall Lakes Townhomes Developers, Inc. v. Agricultural Access  
& Surplus Lines Ins. Co.*, 916 So.2d 12 (Fla. App. 2005) ..... 8, 9, 10

*State Farm Fire & Cas. Co. v. Gonzalez*, 805 So.2d 814 (Fla. App. 2002) ..... 8

*State Farm Lloyds v. Johnson*, 290 S.W.3d 886 (Tex. 2009) ..... 7

## ARGUMENT

There is very little in this case, factually or legally, that is actually disputed. Legally, Secura does not dispute the long-standing principle upon which the court of appeals' decision partially was based, and which is argued at length in Respondents' Brief. The proposition that liability and coverage determinations are the exclusive province of the courts is well settled, and Secura as admitted as much. See Opening Brief, p. 12. Factually, it is not disputed that a wind storm caused damage to Respondents' property, that storm-related damages are a "loss" under Secura's policy, that Secura is obligated to pay for storm damage losses, within the terms of its policy, that Secura in fact has paid for what it believes were the storm-related damages sustained by Respondents, and that Secura's policy does not provide coverage for losses occasioned by wear and tear or lack of adequate maintenance. What is disputed in this case is a factual question regarding the amount or extent of the storm-related damage to Respondents' property.

The legal issue presented by this appeal concerns the scope of a common provision in Secura's policy calling for appraisal when the parties fail to agree on the amount of loss and, in particular, whether the appraisers' authority to set the amount of the loss includes the authority to make determinations regarding the cause of the loss. On this issue, there is an undeniable split in authority, nationally. Nevertheless, this Court's decisions going back nearly a century, together with more recent court of appeals decisions, have clearly recognized that the appraisers' authority necessarily extends to factual questions that go beyond mechanical calculations regarding the cash value of a

loss -- even when coverage may be impacted by the appraisers' decisions. See, e.g., *Itasca Paper Co. v. Niagara Fire Ins. Co.*, 175 Minn. 73, 220 N.W. 425 (1928); *American Central Ins. Co. v. Ramsey County*, 125 Minn. 274, 147 N.W. 242 (1914); *QBE Ins. Corp. v. Twin Homes of French Ridge Homeowners Ass'n*, 778 N.W.2d 383 (Minn. App. 2010); *Sampson v. Horace Mann Ins. Co.*, No. A03-158, 2003 Minn. App. LEXIS 1215 (Sept. 30, 2003). See also, *Orient Ins. Co. v. Skellet Co.*, 28 F.2d 968 (8th Cir. 1928). Secura, in its Opening Brief, fully discusses Minnesota's treatment of this issue, as well as the various public policy and practical considerations articulated by Minnesota courts, and courts elsewhere, which justify the trial court's conclusion that an appraisers' assessment of the "amount of loss" necessarily includes determinations as to the cause of the damage claimed.

In contrast, Respondents do little more than point out the acknowledged split in authority, while making the bare assertion that the issue in this case is one of coverage and liability. Significantly, Respondents provide the Court with no reasoned basis why it should depart from its prior decisions regarding the scope of an appraisal panel's authority, or why it should join what Respondents term the "majority" in holding that appraisers can never decide issues regarding causation.<sup>1</sup>

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<sup>1</sup> Respondents cite a myriad of cases purportedly comprising the "majority view," but, oddly, quite a few of those cases actually support Secura's position. Indeed, two of the cases, *Johnson v. Nationwide Mut. Ins. Co.*, 828 So.2d 1021 (Fla. 2002) and *State Farm Lloyds v. Johnson*, 290 S.W.3d 886 (Tex. 2009), which provides the most recent pronouncement in Texas on the issue, are thoroughly discussed in Secura's brief. A third case, *Kendall Lakes Townhomes Developers, Inc. v. Agricultural Access & Surplus Lines Ins. Co.*, 916 So.2d 12 (Fla. App. 2005) specifically rejected the argument that causation is always a coverage issue reserved for the trial court.

**I. Resolution of the Disputed Issue Does Not Require the Appraisers to Interpret the Policy or Make Determinations Regarding Coverage.**

The court of appeals' decision was based on its conclusion that neither the district court nor Secura "identifie[d] a fact question free of confusion with regard to legal issues such that if an appraisal occurred, the appraiser would not have to engage in assessing the law and interpreting the policy." See Slip. Op. at Add. 8.<sup>2</sup> Expanding upon this, and in an apparent attempt to justify the already admitted point that liability and coverage determinations are for the courts, Respondents embark on a lengthy discussion regarding rules of insurance contract interpretation in an effort to support their argument that appraisers are not qualified to interpret contracts or to apply legal principles to determine the liability of a party to a contract. See Respondents' Brief, pp. 9-14.

Absent from Respondents' brief, however, is any explanation as to how or why the trial court's referral to appraisal would require the appraisers to interpret the policy. As discussed in Secura's Opening Brief, the appraisers are being asked merely to determine the amount of the loss from the July 10, 2008 wind storm. Thus, while this Court, in *Itasca Paper*, 220 N.W. at 427, acknowledged that the duties of appraisers occasionally do require them to construe contracts, determining the amount of the loss from the storm in this case does not require the appraisers to interpret the policy, or even look at the policy.

Among the matters addressed by the Court in *American Central*, *supra*, was whether an attorney was competent to act as an appraiser in a case involving lost

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<sup>2</sup> All references to "Add." are to the Addendum to Secura's Opening Brief.

inventory when the attorney had never been a dealer in men's clothing, the inventory at issue. Noting that appraisers must determine many matters other than the mere value of specific property produced before them for examination and appraisal, including, among other things, whether the damage resulted from causes covered by the policy or from other causes not covered thereby, the court concluded that the duties imposed upon appraisers do not require the appraisers to be experts, although the appraisers should be familiar with the matters and things which they are called upon to appraise. *American Central*, 125 Minn. at 378-79, 147 N.W.2d at 244. As Respondents note, in the context of a claim for damage to real property, the appraisers selected by the parties typically are building contractors. *See* Respondents' Brief, p.10. Building contractors may not be qualified to interpret contracts and decide complex liability issues, but they unquestionably are qualified to assess the underlying nature and cause of the damage, which is all that the referral to appraisal tasks them to do -- determine the amount of the loss. If, after the appraisal is complete, a coverage dispute actually exists, either party may bring a declaratory judgment action to have that issue resolved by the court. *See* Trial Court Order at Add.11.

**II. This Case Does Not Present a Liability or Coverage Dispute, But Instead Presents a Purely Factual Question Regarding the Amount of the Storm-Related Damage.**

In arguing that questions regarding whether and to what extent damage has been caused by a covered peril are "inherently questions of liability," and are, therefore, never appropriate for appraisal, Respondents advocate for a more restrictive interpretation of the appraisal provision that even the court of appeals would have given it in this case.

The court of appeals acknowledged that whether an appraisal was necessary depended on how it characterized the disputed issue and the phrase “amount of loss” in the appraisal clause:

If the disputed issue is how much of the total claimed damage was caused by the storm, then, as the insurer contends, an appraisal is necessary to determine the factual issue of the amount of storm-related loss. But if the issue is whether the claimed damage is covered by the policy, which also may include a causation question, then the legal issues of coverage and liability must be submitted to the district court.

*See Slip. Op. at Add. 5.*

Taking the latter position, Respondents argue that this Court already has determined that appraisers are not qualified to resolve causation issues, citing *Mork v. Eureka-Security Fire & Marine Ins. Co.*, 230 Minn. 382, 42 N.W.2d 33 (1950). Whether the board of appraisers was qualified to consider issues of causation, however, was not the issue in *Mork*. In that case, the insureds’ home was damaged due to a series of events that began with an explosion inside their furnace and eventually culminated in the freezing of water within plumbing and heating pipes. The matter initially was submitted to an arbitration panel that determined the loss but “also found, apparently, that the loss was not covered by the policy at issue,” prompting this Court to comment merely that “[t]he latter finding was not within their province and mere surplusage. The finding of appraisers on the question of coverage, which would be a decision on a question of law, would not be final.” *Mork*, 230 Minn. at 384, 42 N.W.2d at 35. The claim in *Mork* was that the arbitrators had exceeded their authority in attempting to construe the policy of

insurance where coverage turned on the meaning of the word “direct” used in policy language that extended coverage to include “direct loss or damage by. . .explosion.” *Id.*

*Mork* stands for nothing more than the basic proposition, again admitted by Secura, that liability and coverage determinations are the exclusive province of the courts. Beyond citing *Mork*, which simply does not address the issue presented in this case, Respondents attempt to downplay the significance of this Court’s decisions in *American Central* and *Itasca Paper*, *supra*, arguing that these cases are of no value because the Court’s comments regarding the scope of an appraiser’s authority were *dicta*. The Court’s comments in *American Central*, however, are an express recognition that a proper appraisal requires the appraiser to consider more than just what it would cost to fix specific property and that the authority may extend to determinations regarding whether the damage resulted from causes covered by the policy. *American Central Ins. Co.*, 125 Minn. at 378, 147 N.W. at 244. Likewise, the *Itasca Paper* court also recognized the authority of an appraisal panel to decide issues beyond mere valuation. The dispute in that case did not concern just the cost to fix the property at issue, but rather, the appraisal panel’s authority in determining the amount of loss to evaluate whether the damaged property was covered pulpwood, or some other type of wood that was not covered. *Itasca Paper*, 220 N.W. at 426. Relying on *American Central*, the Court concluded that the appraisal panel’s findings regarding the nature of the property involved was final and conclusive even though those findings had a direct impact on whether the loss was covered. *Id.*, 220 N.W. at 427. *American Central* and *Itasca Paper*, along with cases like *QBE Ins. Corp.*, *supra* and *Sampson v. Horace Mann Ins. Co.*, *supra*, demonstrate a

willingness on the part of Minnesota's appellate courts to vest appraisers with broad authority to decide questions of fact "which are involved as mere incidents to determination of the amount of the loss or damage." *See Itasca Paper*, 220 N.W. at 427.

To further support their claim that disputed causation issues are always liability questions that must be resolved by the courts, Respondents offer a string cite of cases, relegated to a footnote, that oddly includes cases discussed by Secura in support of its position. Respondents, however, offer no argument as to why these cases present a better or more reasoned view of the role of appraisal than the body of case law discussed in Secura's Opening Brief. Public policy in Minnesota, and elsewhere, favors appraisals as providing a plain, speedy, inexpensive and just determination of the loss. *See, e.g., Kavli v. Eagle Star Ins. Co.*, 206 Minn. 360, 288 N.W. 723, 725 (1939); *Cigna Ins. Co. v. Didimoi Property Holdings, N.V.*, 110 F. Supp.2d 259, 269 (D. Del. 2000). Yet, as the Texas Supreme Court noted in *State Farm Lloyds v. Johnson*, 290 S.W.3d 886, 892 (Tex. 2009), one of the cases cited in footnote 10 of Respondents' Brief, if appraisers can never allocate damages between covered and excluded perils, then the appraisal process can never be used to assess damage except in cases in which the property at issue is brand new, a result that would render appraisal clauses largely inoperative. *Johnson*, 290 S.W.3d at 292-93. As the *Johnson* court further concluded, "[a]ny appraisal necessarily includes some causation element, because setting the 'amount of loss' requires appraisers to decide between damages for which coverage is claimed from damages caused by everything else." *Id.* at 893.

Respondents also suggest that before causation questions can become an issue for appraisal, Secura must first concede causation. *See* Respondents' Brief, p. 19. While a curious assertion, it is an attempt to place this case factually outside that body of case law which holds that when an insurer admits there is a covered loss, but there is a disagreement on the amount of the loss, the appraisers, in arriving at the amount to be paid, are permitted to sort out how much is to be paid on account of a covered peril, excluding payment for "a cause not covered such as normal wear and tear, dry-rot, or various other designated, excluded causes." *See Johnson v. Nationwide Mut. Ins. Co.*, 828 So.2d 1021, 1025 (Fla. 2002) (quoting *State Farm Fire & Cas. Co. v. Gonzalez*, 805 So.2d 814, 816-17 (Fla. App. 2002)). Respondents' argument, however, continues to be based on a mischaracterization of the present dispute as one in which Secura has denied all liability for coverage of any damage. This argument simply ignores the fact that Secura admitted liability, and paid Respondents, for the damages to their property that Secura determined to be caused by the storm, an admittedly covered peril. Indeed, the same footnote that accuses Secura of being the party who is parsing the claim concedes as much: "Secura did not claim that its liability for damage to other structures was negated by a policy exclusion. It admitted liability and paid for damage elsewhere, but denied liability for damage to the roofs." *See* Respondents' Brief, pp. 19-20 n. 12.

In this regard, the facts of this case are not much different from those in *Kendall Lakes Townhomes Developers, Inc. v. Agricultural Excess & Surplus Lines Ins. Co.*, 916 So.2d 12 (Fla. App. 2005), one of the cases cited in footnotes 6 and 10 as somehow supportive of Respondents' position. Agricultural Excess issued a policy insuring

Kendall Lakes' buildings against physical loss caused by wind storm. The insured filed a claim asserting that, as a result of Hurricane Irene, several units had sustained interior damage due to water seepage, and also claimed that wind from the hurricane had damaged some of the roofs. Responding to the claim, the insurer hired an adjuster to inspect the property and to issue a report regarding the damage claimed. The report stated that none of the units had breaks in either the roof or the skylight area, and that the damage to the interior walls was caused by "wind-blown water seepage," which was not covered by the policy because there was no break in the covered structure. *Kendall Lakes*, 916 So.2d at 14. Two of the buildings, however, had "a few tiles blown off the roof," but the cost to fix this covered item of property damage was less than the policy's deductible and the insurer, therefore, denied the claim. *Id.* Significantly, as in this case, the parties agreed that the insurance policy provided coverage for wind storm damage and did not dispute the meaning of the policy, but instead disagreed as to whether the wind storm caused all of the claimed damages or just a part of it. *Id.* The matter was then submitted to appraisal upon demand of the insured, with the insured's appraiser estimating the covered loss at approximately \$716,000, and the insurance carrier's appraiser estimating the covered damage to all nine buildings at less than \$1,000. *Id.* Based on these conflicts, the court appointed an umpire who, after reviewing the two appraisal reports and conducting a hearing, issued an award in favor of the insurance carrier in which he specifically made a determination regarding coverage, and which was confirmed by the trial court. *Id.*

Upon further review, the Florida Court of Appeals addressed two issues. First, the insured argued, as Respondents argue in this case, that causation of the damages is a coverage issue reserved for the trial court, not the appraisal panel. The *Kendall Lakes* court, however, disagreed. *Id.*, 916 So.2d at 15. The court noted that the insurance carrier had agreed that there was a covered loss, but disagreed as to the amount of the loss. Based on *Johnson v. Nationwide, supra*, the court concluded that although there was a large discrepancy between the insured's and the insurance carrier's estimate of the loss, because the insurer had not wholly denied that there was a covered loss, causation was "an amount-of-loss question for the appraisal panel" not a coverage question that could only be decided by the trial court. *Id.* 916 So.2d at 16.<sup>3</sup>

The fact that the insurance carrier in *Kendall Lakes* denied liability for any interior damage to the condominium units did not equate to a complete denial that there had been a covered loss. Likewise, in this case, Respondents made one claim for all of the property damage resulting from the July 10, 2008 wind storm. Secura agreed it was liable for storm-related damage, paid Respondents for storm-related damage, but simply did not agree that all of the damage claimed was storm-related. Its disagreement regarding the cause of the damage to some roofs<sup>4</sup> does not equate to a denial of all liability such that causation could not be an amount of loss question.

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<sup>3</sup> Ultimately, however, the court did reverse based on the second issue, which was whether the umpire had exceeded his authority in making actual coverage determinations.

<sup>4</sup> Secura did pay for damage to the roof on Respondents' dwelling, which was shingled, not metal.

Finally, Respondents' comment that what they term the "majority rule," is justified by the fact that the contract does not say that "liability, coverage, or causation issues are to be resolved by appraisers -- just the 'amount' of the loss." *See* Respondents' Brief, p. 13. In making this argument, Respondents suggest that the appraisal clause can only be interpreted as limiting appraisal to mechanical calculations of the actual cash value of a loss. This argument, however, loses sight of the fact that the language of appraisal clauses are statutorily mandated and, consistent with the favor in which they are held, should be given a reasonable interpretation to carry out the legislative purpose of discouraging costly litigation and providing a plain, speedy, inexpensive and just determination of the extent of the loss. *See Kavli, supra*, 288 N.W. 723 at 725. *See also Fox v. The Employers' Fire Ins. Co.*, 113 N.E.2d 63, 65-66 (Mass. 1953). This Court already has recognized that a proper appraisal requires the appraiser to consider and decide issues beyond mere valuation, and there is no reason to hold otherwise when the legislature could just as easily have limited appraisal to the determination of "actual cash value" as opposed to the broader "amount of loss."

### **III. The District Court Properly Followed a Century of Precedent In Ordering That the Enforcement of the Appraisal Award Was Governed By Minnesota Statutes Applicable to Arbitration Proceedings.**

Respondents argue that the district court erred in concluding that an appraisal would be governed by Minnesota's Uniform Arbitration Act. This issue was not the subject of Secura's Petition for Supreme Court Review, and Respondents did not, in responding to Secura's Petition, conditionally seek review by the Court. Assuming,

however, that the matter is properly before the Court, the argument is contrary to longstanding law.

In *QBE, supra*, the court of appeals reaffirmed over 95 years of Minnesota law holding that arbitration laws govern the appraisal process. *QBE Ins. Corp. v. Twin Homes of French Ridge Homeowners Ass'n*, 778 N.W.2d 393, 398 (Minn. Ct. App. 2004). In addressing the respondent's contention that the appraisal panel's decision exceeded their authority, the court of appeals reiterated that appraisal decisions are subject to Minn. Stat. § 572.08-572.30, the arbitration statute. *Id.* The court of appeals held that the arbitration statutes provided the procedures and grounds upon which appraisal awards could be confirmed, modified, corrected or vacated by a court upon application following completion of the appraisal process. Contrary to Respondents' argument, the court's discussion of the applicability of the arbitration act was not dicta, but rather central to its analysis of when an appraisal award could be vacated because the appraisal panel exceeded its power to determine the amount of the loss. *See also, David A. Brooks Enterprises, Inc. v. First Systems Agencies*, 370 N.W.2d 434 (Minn. App. 1985) (affirming trial court's confirmation of the appraisal umpire's award); *American Central Ins. Co.*, 147 N.W. 243 (rules governing arbitrations apply to proceedings for determining the amount of loss under insurance policies); *Beebout v. St. Paul Fire & Marine Ins. Co.*, 365 N.W.2d 271, 273 (Minn. App. 1985) (referring to appraisal provision as an arbitration agreement interpreted with reference to the UAA).

Respondents contend the district court erred in determining that appraisal process was to be an arbitration of all of the disputes between the parties and that the arbitration

act governed the procedure of the appraisal process and enforcement of the appraisal award. However, the district court's Order expressly does not refer all existing or potential disputes to the appraisal process, but rather only the dispute as to "the amount of the loss to Plaintiffs' property caused by the July 10, 2008 storm." Add. 11. Thereafter, in accordance with longstanding Minnesota precedent, the district court's judgment provides that the appraisal determination as to the amount of the storm-related damage could be confirmed or vacated under the statutes governing confirmation or vacation of an arbitration award. Add. 12. Moreover, the judgment reserves the parties' rights to go to court to pursue coverage determinations should such issues arise in the future. Add. 11, 14. Because the district court correctly applied Minnesota precedent and the arbitration act provisions, its judgment should be affirmed.

### CONCLUSION

Despite Respondents' repeated assertions regarding the role of the courts in determining liability and coverage issues, the simple fact remains that the Complaint does not seek policy interpretation or a declaration regarding coverage. The dispute is purely factual -- what is the amount of the damage caused by the July 10, 2008 storm? This type of issue is, and for over 100 years has been, an amount-of-loss question to be determined through appraisal. For all of the reasons stated herein, and in Secura's Opening Brief,

Secura respectfully requests that the decision of the court of appeals be reversed, and the judgment of the trial court reinstated.

Respectfully submitted,

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Dated: June 13, 2011.

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