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State of Minnesota  
*In Supreme Court*

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No. A10-1992

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Remodeling Dimensions, Inc.,

Appellant,

vs.

Integrity Mutual Insurance Company,

Respondent,

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**BRIEF OF APPELLANT**

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## **II. STATEMENT OF ISSUES PRESENTED.**

- I. Is an insurer, which exercises its contractual right to direct and control litigation in defense of its insured—under a reservation of rights—in breach of its duty to defend when the attorney it retained fails to obtain a reasoned arbitration award or special verdict, the absence of which renders it impossible for the insured to demonstrate coverage?**

The district court held that the insurance company's failure to obtain a reasoned award was a breach of contract. The court of appeals reversed, holding that it did not need to reach this issue because of existing Minnesota law, specifically *Pine Island Farmers Co-op v. Erstad & Riemer, P.A.*, 649 N.W.2d 444 (Minn. 2002).

This is a question of first impression in Minnesota. Authority: *Stumpf v. Continental Cas. Co.*, 794 P.2d 1228 (Or. Ct. App. 1989); *U.S. Concrete Pipe Co. v. Bould*, 437 So.2d 1061 (Fla. 1983); *Pacific Indem. Co. v. Linn*, 766 F.2d 754 (3d Cir. 1985); *Herrera v. C.A. Seguros Catatumbo*, 844 So.2d 664, 668 (Fla. Ct. App. 1979); *Gay & Taylor, Inc. v. St. Paul Fire & Marine Ins. Co.*, 550 F.Supp. 710, 714–16 (W.D. Okla. 1981); *Duke v. Hoch*, 468 F.2d 973 (5th Cir. 1972); and *Smoot v. State Farm Mut. Auto. Ins. Co.*, 299 F.2d 525 (5th Cir. 1962).

- II. Did the court of appeals err in its application and extension of the *Pine Island Farmers Co-op v. Erstad & Riemer* decision to the tripartite relationship in this case?**

This was a question that was not raised or briefed by either party at the district court or at the court of appeals. The court of appeals extended the holding of *Pine Island Farmers Co-op v. Erstad & Riemer* by requiring a dual representation of the insured and insurer before a conflict of interest arises in the tripartite relationship—even when defense is provided under a reservation of rights. This is a matter of first impression in Minnesota. Authority: *Pine Island Farmers Co-op v. Erstad & Riemer, P.A.*, 649 N.W.2d 444 (Minn. 2002); Minn.R.Prof.R. 1.7.

- III. Did the court of appeals improperly depart from its role as an error correcting court by its determination of facts not contained in the district court record, making a coverage determination as a matter of law, and directing summary judgment in favor of Integrity?**

The court of appeals held that, in insurance coverage disputes, it had the discretion to review the record and make factual and legal determinations, even in the absence of such findings by the district court. Authority: *Day Masonry v. Independent School Dist. 347*, 781 N.W.2d 321 (Minn. 2010); *Eagan Economic Development Authority v. U-Haul Co.*

*of Minnesota*, 787 N.W.2d 523 (Minn. 2010); *Franklin v. Western Nat'l Mut. Ins. Co.*, 574 N.W.2d 405 (Minn. 1998); *Thiele v. Stinch*, 425 N.W.2d 580 (Minn. 1988).

### III. STATEMENT OF THE CASE & FACTS.

#### A. Factual Background.

##### 1. **The Parties & Their Insurance Contract.**

Appellant, Remodeling Dimensions, Inc. (“RDI”) is engaged in the residential design and construction business, and is located in St. Louis Park, Minnesota. (AA 1.) Respondent, Integrity Mutual Insurance Co., Inc. (“Integrity”), is in the business of selling various insurance products. (AA 1.) On or about September 1, 2002, the parties entered into an insurance contract (“the policy”) whereby Integrity agreed to provide general liability coverage to RDI. The policy was in effect for four years, through September 1, 2006. (AA 2, 5–7.)

The parties’ insurance contract contains the following salient, operative provisions. With respect to business liability coverage and the defense of any such claims, the contract contains the following broad indemnity provision:

- a. We [Integrity] will pay those sums that the insured [RDI] becomes legally obligated to pay as damages because of “bodily injury”, “property damage”<sup>[1]</sup> or “personal and advertising injury” to which this insurance applies. *We will have the right and duty to defend the insured against any “suit”<sup>[2]</sup> seeking those damages. However, we will have no*

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<sup>1</sup> The policy defines “property damage” as: “(a) Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or (b) Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the ‘occurrence’ that caused it.” (Policy Section II (F)(17) at AA 52).

<sup>2</sup> The policy provides that “‘suit’ means a civil proceeding in which damages because of ‘bodily injury’, ‘property damage’, ‘personal and advertising injury’ to which this insurance applies are alleged. ‘Suit’ includes: (a) An arbitration

*duty to defend the insured against any "suit" seeking damages for "bodily injury", "property damage" or "personal and advertising injury", to which this insurance does not apply. We may at our discretion, investigate any "occurrence" and may settle any claim or "suit" that may result.*

(AA 38 (emphasis added).)

b. This insurance applies:

(1) To "bodily injury" and "property damage" only if:

- (a) The "bodily injury" or "property damage" is caused by an "occurrence"<sup>3</sup> that takes place in the "coverage territory";
- (b) The "bodily injury" or "property damage" occurs during the policy period.

(Policy Section II (A)(1) at AA 39.)

The policy provides a coverage exclusion for damage to or arising out of "your work," stating:

This insurance does not apply to:

....

k. Damage To Property.

"Property damage" to:

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proceeding in which such damages are claimed and to which the insured must submit or does submit with our consent." (Policy Section II(F)(18) at AA 52.)

<sup>3</sup> According to the policy: "Occurrence" means an accident, *including continuous or repeated exposure to substantially the same general harmful conditions.*" (Policy Section II(F)(13) at AA 51 (emphasis added).)

....

- (5) That particular part of any real property on which you or any contractor or subcontractor working directly or independently on your behalf is performing operations, if the “property damage” arises out of those operations; or
- (6) That particular part of any property that must be restored, repaired or replaced because “your work”<sup>4</sup> was incorrectly performed on it.

(Policy Section II B(k)(5) & (6) at AA 41, 43–44.)

However, the policy then provides a partial exemption or a limitation to this “your work” exclusion, stating:

Paragraph (6) of this exclusion does not apply to “property damage” included in the “products completed operations hazard.”

(Policy Section II(B)(k) at AA 44.)

The policy further defines the “products completed operations hazard,” in relevant part, as:

- a. [A]ll “bodily injury” and “property damage” occurring away from premises you own or rent and arising out of “your product” or “your work, except:
  - (1) Products that are still in your physical possession; or
  - (2) Work that has not yet been completed or abandoned. However, “your work” will be deemed completed at the earliest of the following times:

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<sup>4</sup> The term “your work” is defined as: “(1) Work or operations performed by you or on your behalf; and (2) Materials, parts or equipment furnished in connection with such work or operations,” and includes: “(1) Warranties or representations made at any time with respect to the fitness, quality, durability, performance or use of ‘your work,’ and (2) The providing of or failure to provide warnings or instructions.” (Policy Section II(F)(22) at AA 52–53.)

- (a) When all the work called for in your contract has been completed.
- (b) When all of the work to be done at the job site has been completed if your contract calls for work at more than one job site.
- (c) When that part of the work done at the job site has been put to its intended use by any person or organization other than another contractor or subcontractor working on the same project.

(Policy Section II (F)(16) at AA 51–52.)

By operation of these policy sections, the actual work performed by RDI on any project may be excluded from coverage, by operation of the “your work” exclusion. However, any other damage to *other* property, occurring away from RDI’s office, which resulted from its completed work, is covered, under the “products completed operations hazard” portion of the policy.

## **2. The Provenzano Addition Project.**

On or about January 23, 2003, RDI entered into a construction agreement with Mike and Peggy Provenzano (the “Provenzanos”) whereby it agreed to perform the following work on their home:

- build a lower level, flat roof addition onto the east side of the home;  
**and**
- replace the trim around the windows of the existing portion of the home.

(Provenzano Addition Contract at AA 120–121.)

The Provenzanos’ home was originally built by LeGran Homes in 1993. (AA 127.) The contract provided that any dispute arising out of the parties’ relationship

would be submitted to binding arbitration with the American Arbitration Association (“AAA”). (AA 125.)

During the project, the Provenzanos requested that RDI perform additional work—removal of a master bedroom window in the original portion of the house so they could move a large armoire into the bedroom. (AA 133–34.) RDI agreed to do this additional work to accommodate the Provenzanos. (*Id.*) RDI completed the construction of the addition and the replacement of window trim in approximately June 2003. (AA 127–28.)

### **3. The Provenzano’s Arbitration Claim.**

Three years later, in June 2006, the Provenzanos hired Northwest Diversified Services (“NDS”) to investigate moisture issues with the house. Following an inspection and testing, NDS found that moisture was invading the structural parts of both the original construction and the addition, and opined that this moisture intrusion was causing substantial damage to the house, including structural rot and mold infestation. (AA 144–45.) NDS attributed this water intrusion to several sources, including the improper installation and flashing of windows in both the addition and the existing home. (*Id.*)

On July 14, 2006, the Provenzanos commenced arbitration against RDI with the AAA, claiming it was liable for all of the damage to their home—in both the addition and the existing home. (AA 128–32.) The Provenzanos based this claim on two alternative theories:

1. They claimed there were a number of defects in the work performed by RDI on both the addition and on the windows in the existing home that allowed water intrusion causing structural damage to the walls of the house.<sup>5</sup>
2. Alternatively, they contended that RDI was negligent, that it should have recognized that the original construction (performed by LeGran Homes) was defective and causing water intrusion and damage, and that RDI failed to report this to the Provenzanos so they could take action against LeGran Homes.

(Provenzanos' Summary of Claims at AA 129–30.)

Other than the flat roof repair (which was undisputedly part of RDI addition project), the Provenzanos did not apportion their claims based on the area of the house they believed was damaged, which builder's work caused the damage, or under which theory they believed RDI was liable. (AA129–32, 184.)

In the Arbitration, the Provenzanos sought damages from RDI totaling \$264,100.00, broken down into the following general categories:

1. Total low bid from the bid request \$188,500.00;
2. Flat roof repair \$6,000.00;
3. Replacement of various windows and doors \$32,000.00 (location unspecified);

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<sup>5</sup> According to the Provenzanos' Prehearing Brief, the defective work performed by RDI that resulted in water intrusion and structural damage to the house included the following: improperly installed window trim, improperly re-installed master bedroom window, improperly installed patio door, improper installation of addition flat roof, improperly installed fenestrations, improperly flashed dormer roof, and improperly applied window trim. Moreover, the Provenzanos alleged that RDI's negligent work exacerbated the existing defects in the original LeGran work. Last, the Provenzanos contended that RDI was negligent for its failure to recognize and report the defects in the original LeGran construction. (AA 177–84.)

4. Final cleaning and air clearance \$11,100.00;
5. Construction management fees \$17,500.00;
6. Inspection costs \$3,000.00;
7. Design costs \$6,000.00.

(AA 184.)

Again, none of the bids presented by the Provenzanos apportion these repair costs between the addition and the existing home, nor do they apportion these costs to faulty work performed by RDI or to that of the original builder, LeGran Homes. (*Id.*) Simply put, the Provenzanos sought to have RDI held responsible for all alleged damage, regardless of which builder's faulty work might have originally caused the damage, and this included damage to the existing home that extended beyond RDI's "work." (AA 180–84.)

In support of their claims, the Provenzanos offered as evidence NDS's final "Mold & Forensic Report."<sup>6</sup> (AA 141–76). The NDS report's section on "Windows and Doors" contains the following comment regarding the flashing and trim on the windows in the original part of the home:

In the original construction surface staining was noted on the Bildrite fiberboard sheathing below and adjacent to the vertical nailing flange. The nail slots in the nailing flange were only partially used. The window was dry fitted into the rough opening omitting: 1) sill pan flashing; 2) rough opening drainage plane back wrap; 3) a sealant bead around the sides of the window unit; and 4) barrier-coated reinforced flashing paper. This method of construction allowed water that penetrated the lap siding to contact the sheathing

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<sup>6</sup> Integrity provided the entire text of this report to both the district court and to the court of appeals, and it is part of the record in both proceedings.

and intrude within the wall assembly. The installation methods omitted are common industry practices and normal manufacturer's specifications. Left unattended, the problem will consume the wall assembly and cause substantial damage to the wall assembly and structure of the home. The windows observed were not installed so as to provide a waterproof barrier for the exterior structural wall systems.

(AA 159).

In the "Opinions" section of its report, NDS made it clear that it considered RDI responsible for damage to the walls of the original construction resulting from its work on the window flashing and trim, when it stated:

The water damaged lap siding, the damaged Bildrite sheathing, the creation of saw kerfs into the sheathing, the rot in the dimensioned lumber of the wall assemblies, the unsecured windows, the dry fitting of the windows into the wall assemblies, etc. were all visible to the licensed contractor and crew that installed the trim boards on the windows. These individuals had an obligation to report these conditions to the homeowner or to correct the condition. These flaws should not have been covered up with the trim boards and ignored. This method of construction allowed water that penetrated the lap siding to continue its contract with the sheathing and intrusion into the wall assembly. The installation methods ignored and allowed to exist are common industry practices and normal manufacturer's specifications. An individual working as a licensed contractor would know that the ignored problems will exponentially consume the wall assembly and cause substantial damage to the wall assembly and the structure of the home; including the trim work that they just completed. The building code requires that all wood with mold or rot be removed and repaired.

(AA 172-73.)

Based on this report, the Provenzano's Pre-Hearing Brief to the AAA charged that RDI was liable for all the damage to their home, including the structural damage to the walls of the original home. (AA 181).

**4. RDI Submits The Claim To Integrity & The Two Reservation Of Rights Letters.**

After receiving notice of the arbitration, RDI submitted the claim to Integrity under the policy. (AA 3, 186.) Integrity agreed to defend RDI in the arbitration, and on about September 7, 2006, Integrity hired Patrick Elliot, Esq. to defend RDI. (AA 186.) With Mr. Elliot's full participation, on September 21, 2006, the AAA issued an order removing Eric Forsberg, Esq. and appointing John G. Patterson, Esq. to be the Arbitrator on the claim. (AA 187–88.) By this same letter, the AAA set a pre-hearing conference for October 2, 2006 and included a Report of Preliminary Hearing and Scheduling Order outlining in detail the items to be covered in the conference. (AA 189–91.) Contained on this Report form was a section for “form of award” which allowed counsel to select from three forms: a standard award, a reasoned award, or findings of fact and conclusions of law. (AA 190.)

The next day, on September 22, 2006, Integrity sent a RDI a reservation of rights letter. (AA 192–93.) According to Integrity:

At this time it is questionable whether or not there is coverage for all or part of Plaintiffs' alleged damages under this policy. . . . Your policy with Integrity does not insure, repair, replace or guarantee its contracted and paid for work, which is a business risk in doing business. *Instead the policy provides indemnity insurance for covered occurrences and resultant damages, separate and apart from the actual contracted work.*

(AA 192 (emphasis added).)

Importantly, this letter nowhere states that RDI was responsible for requesting a reasoned arbitration award so that coverage could be evaluated and determined. (AA 192–93.) There is no evidence in the record indicating whether Mr. Elliot was copied on this reservation of rights letter.

There is also no record of what transpired at the October pretrial scheduling conference with Arbitrator Patterson, other than the fact that a final hearing date was set for January 22 and 23, 2007. Yet, three months following Arbitrator Patterson’s appointment and two months after the pretrial scheduling conference, Integrity recognized that a reasoned award was critical to determining coverage. Consequently, on January 10, 2007—a mere twelve days before the final hearing was to begin—Integrity sent RDI a second reservation of rights letter, now stating for the first time:

The purpose of this correspondence is to alert you of your duties in this matter. *It will be up to you and your counsel to fashion an arbitration award form that addresses the coverage issues and your respective burden. If, for example, the arbitration award ultimately rendered makes it impossible to determine whether any of the damages awarded involve “property damage” that occurred during the Integrity policy period, Integrity will not be responsible to indemnify an ambiguous award.* Also, by way of further illustration but not limitation, Integrity Mutual will not be responsible for an ambiguous award that fails to identify the subcontractor found to be liable and the damages allocated specifically to that subcontractor. *Please be advised that Integrity Mutual will be requesting that the arbitration proceedings be transcribed.* You have the right to request that a court reporter be present at the arbitration hearing under the Rules promulgated by the American Arbitration Association. We expect that you make an independent request of the arbitrator in this regard.

(AA 194–95 (emphasis added).)

Mr. Elliot was copied on this second reservation of rights letter. (AA 195.) Significantly, nowhere does the policy itself state that it is the insured's obligation or responsibility to obtain a reasoned award or verdict. There is no evidence in the record that Mr. Elliot requested a reasoned award before the final arbitration hearing.

**5. The Arbitration Hearing & The Simple Form Award.**

On January 22 and 23, 2007, RDI and the Provenzanos participated in a final arbitration hearing. (AA 196.) Mr. Elliot represented RDI, whose principle defense was that the damage was caused by the negligence of the original builder and the lack of proper maintenance by the Provenzanos, not the result of any work or negligence by RDI. (AA 3.) LeGran Homes was not a party to the arbitration because the statute of limitations on any claims against it had lapsed. (AA 3.) On or about February 23, 2007, Arbitrator Patterson issued an award (the "Award"), finding for the Provenzanos and awarding them the following damages:

Basic house repairs	\$45,000.00
Flat roof repair	\$2,000.00
Replacement window costs	\$0.00
Final cleaning	\$1,000.00
NDS inspection costs	\$0.00
Design costs	\$0.00
Construction management fees	\$3,000.00
<b>Total</b>	<b>\$51,000.00</b>

(AA 196–97.)

The Award was in the “simple award” format, containing no reasoning or apportionment based upon theory of liability or portion of the home damaged.<sup>7</sup>

(*Id.*)

**6. Integrity Requests A Reasoned Award.**

On or about February 23, 2007, Mr. Elliot sent a letter to Arbitrator Patterson, for the first time requesting a reasoned award. (AA 198.)<sup>8</sup> On or about March 20, 2007, the Arbitrator responded that “[t]he parties did not request an explanation of the Award in writing prior to the appointment of the arbitrator as required by [Rule 42(b) of the American Arbitration Association Rules]. Therefore, no such explanation is required, nor is one permitted after issuance of the Award.”<sup>9</sup> (AA 198.)

**7. Integrity Declines Coverage.**

Two days later, on March 22, 2007, Integrity informed RDI that it declined to cover any portion of the Award. Despite the lack of any apportionment or

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<sup>7</sup> The only specific aspect of the arbitration award is the \$2,000.00 award for the flat roof repair, which was a part of the RDI addition project, and the parties stipulate that this portion of the claim is not covered. (AA 196.)

<sup>8</sup> Mr. Elliot’s letter was not included in the record to the district court. However, it is mentioned in Arbitrator Patterson’s reply letter of March 20, 2007, which is part of the record at the district court and here.

<sup>9</sup> AAA Rule 42(b) provides: “The arbitrator need not render a reasoned award unless the parties request such an award in writing prior to appointment of the arbitrator or unless the arbitrator determines that a reasoned award is appropriate.” (AA 199.)

explanation in the Award, Integrity took the insupportable position that the Arbitrator rejected all the Provenzano's claims related to damage to the original portion of the home. (AA 200–01.) Integrity denied coverage for the following reasons:

- Integrity contended all of the awarded damages were related to the work of RDI and subject to the “your work” exclusion of the contract.
- Integrity claimed that, even if a portion of the damages awarded related to damage to the original house, it would not involve an occurrence or activity subject to the “products completed operations hazard,” and the damage did not occur during the policy period.
- Integrity claimed that final cleaning and design costs did not constitute damage under the policy, but did not provide any reasons for this decision.

*(Id.)*

After Integrity declined coverage, RDI paid the Provenzanos \$51,000.00 to satisfy the Award. (AA 4.)

**B. Procedural Posture.**

**1. The District Court.** On or about May 17, 2010, RDI initiated this action against Integrity in Hennepin County district court, asserting a single claim for breach of the parties' insurance contract. (AD 5; AA 203–11.) On or about June 7, 2010, Integrity answered RDI's complaint with a general denial. (AA 212–17.) On or about August 25, 2010, counsel for the parties appeared before the Hon. Gary Larson for hearing on the parties' cross-motions for summary judgment. (AD 1; AA 218–80.) On or about September 30, 2010, Judge Larson issued an order

and memorandum granting RDI's motion and denying Integrity's cross-motion. (AD 1–11.) In so doing, the district court first held that, in the absence of a reasoned arbitration award, it could not determine the issue of coverage as a matter of law, and any attempt to do so would be an improper exercise in speculation. (AD 7–8.) Unable to determine coverage, the district court proceeded to hold Integrity responsible for the failure to obtain a reasoned award, and the resulting prejudice to RDI constituted a breach of the parties' contract. (AD 9–10.) In so doing, the district court recognized this was a matter of first impression in the State of Minnesota, and relied substantially on the Oregon court of appeals opinion in *Stumpf v. Continental Cas. Co.*, 794 P.2d 1228 (Or. Ct. App. 1989). (*Id.*) Accordingly, the district court ordered the entry of judgment in RDI's favor in the amount of \$49,000.00. (AD 1–2.)

**2. The Court Of Appeals.** On November 9, 2010, Integrity served its Notice of Appeal, seeking review of the district court's decision. (AA 281–82.) On June 21, 2011, the court of appeals issued its published decision reversing the district court and ordering the entry of judgment in favor of Integrity on its cross-motion for summary judgment. (AD 12.)

In so doing, the court of appeals first held that the district court erred in holding Integrity responsible for the lack of a reasoned award and in its reliance on foreign decisional law. (AD 18–22.) Finding that this Court's decision in *Pine Island Farmers Co-op v. Erstad & Riemer, P.A.*, 649 N.W.2d 444 (Minn. 2002) controlled, the court of appeals held that, absent defense counsel's dual

representation of Integrity and RDI, he owed no duty to Integrity to obtain a reasoned award, and Integrity could not be held responsible for his failure to do so. (AD 22.)

The court of appeals then proceeded to hold, as a matter of law, that none of the Provenzano's claims or damages were covered under the policy, or were subject to policy exclusions. (AD 22–30.) In so doing, the court of appeals first reasoned that the Provenzano's claim that RDI negligently failed to inform them of pre-existing defects in the original part of the house was not an "occurrence" as defined by the policy.<sup>10</sup> (AD 23–26.) Addressing the balance of the Provenzano's property damage claims, the court of appeals made two findings. First, as related to any defect or damage to those portions of the home on which RDI actually performed work, those claims fell within the "Business Risk Doctrine" as embodied in the "your work" exclusion of the policy.<sup>11</sup> (AD 28–29.) Next, while

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<sup>10</sup> For purposes of this appeal, RDI does not contest this finding as it relates to the "failure to warn" portion of the Provenzano's claims. Yet, in limiting its holding regarding the contract definition of an "occurrence" to the "failure to warn" aspect of the claim, the court of appeals implicitly agreed that any collateral damages to the home spilling out of RDI's defective workmanship satisfied the contract definition of an "occurrence."

<sup>11</sup> Again, for purposes of this appeal RDI does not contest this finding. It is RDI's position in this appeal that if there is *any* potential claim or damage that falls within the indemnity provision of the policy, RDI has borne its burden of demonstrating coverage and the burden of proof shifts to Integrity to prove an exclusion. In this instance, RDI has satisfied its burden by demonstrating that the Provenzano's claims included damage to the structure of the existing home (that RDI did not touch) resulting from RDI's defective work on window trim and flashing. As this brief will demonstrate, RDI clearly presented this issue to the district court.

the court acknowledged that the “your work” exclusion would not foreclose coverage for structural, rot and mold damage to the walls of the existing home (on which RDI performed no work), resulting from water intrusion flowing from RDI’s negligent work on the window flashing and trim, it nevertheless held that this “contention was outside the scope [RDI’s] pleadings” at the district court. (*Id.*) According to the court, “RDI never argued to the district court that it incurred liability to the Provenzanos for property damage to the original part of the home created by its own defective work.” (*Id.*) As a result, the court of appeals held that, as a matter of law, coverage was properly denied under exclusion “m” of the policy.<sup>12</sup> (*Id.*)

On July 20, 2011, RDI petitioned this Court for review of the court of appeals’ decision. On August 4, 2011, Integrity filed its opposition to the petition for review. On September 20, 2011, this Court issued an order granting RDI’s petition for review.

#### **IV. STANDARD OF REVIEW.**

Generally, “[o]n appeal from summary judgment, this court reviews the record to determine whether there are any genuine issues of material fact and whether the lower court erred in their application of the law.” *Medica, Inc. v. Atlantic Mut. Ins. Co.*, 566 N.W.2d 74, 76 (Minn. 1997). However, where—as

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<sup>12</sup> Relying on these conclusions, the court of appeals further held the district court erred in reasoning that it was impossible to determine coverage without a reasoned award.

here—the parties file cross-motions for summary judgment, they “tacitly agree that there exist no genuine issues of material facts” in dispute. *Am. Family Mut. Ins. Co. v. Thiem*, 503 N.W.2d 789, 790–91 (Minn. 1993); *Frey v. United Servs. Auto. Ass’n*, 743 N.W.2d 337, 344 (Minn. App. 2008). Correspondingly, where the parties do not dispute the relevant facts, a *de novo* standard of review is applied to determine whether the lower court erred in its application of the law. *Medica, Inc.*, 566 N.W.2d at 76.

## V. ARGUMENT.

### A. ***INTEGRITY’S FAILURE TO OBTAIN A REASONED ARBITRATION AWARD WAS A BREACH OF ITS DUTY TO DEFEND RDI.***

#### 1. **The District Court Was Correct That No Coverage Determination Could Be Made.**

At the conclusion of its opinion, the Court of Appeals dismissed the key determination made by the district court—that the absence of a reasoned award made it impossible to determine, as a matter of law, whether the award was covered under the policy or subject to the “your work” exclusion. As Judge Larson adroitly observed:

Despite the apparent certainty of the parties as to whether or not coverage applies under the contract, the Court is not convinced by either argument. The arbitration award contains no explanation as to the damages and no one can say with any certainty what the arbitrator awarded damages for and why. Without further explanation, we are simply left to make an educated guess. Because of this, the Court cannot determine exactly what the damages were awarded for, why they were awarded and what the arbitrator considered in making the award.

(AD 8.)

Based on this conclusion, the district court declined to speculate whether the Provenzanos' claims and the resulting award were an "occurrence" falling within the broad liability indemnification provision of the policy (Policy Section II (A)(1) at AA 39); whether all or part of these claims were barred from coverage by the "your work" exclusion (Policy Section II B(k)(5) & (6) at AA 41, 43-44); or whether all or part of these claims fell within the "products completed operations hazard" carve-out to the "your work" exclusion (Policy Section II (F)(16) AA 51-52.) Rather, the district court correctly proceeded to consider the threshold issue at the very heart of this dispute: which party should bear responsibility for the absence of a reasoned award by which coverage might have been determined.

**2. Obtaining a Reasoned Award Was Part Of Integrity's Duty To Defend.**

Under the unique facts of this case, Integrity was responsible for defense counsel's failure to obtain a reasoned award, and this failure constituted a breach of its contract with RDI. The policy granted Integrity the exclusive right to evaluate, investigate, settle or defend the Provenzano's claims. (Policy Section II (A)(1) at AA38.) Included in this right was Integrity's discretion to employ and direct defense counsel of its choosing. (Policy Section II (A)(1)(a) at AA 38.) The insurer's exclusive right to direct the defense of a claim—even one accepted under a reservation of rights—is well known in Minnesota law. *See Shelby Mutual Ins. Co. v. Kleman*, 255 N.W.2d 231, 235 (Minn.1977); *Pine Island Farmers Co-op v. Erstad & Reimer*, 649 N.W.2d 444, 450 (Minn. 2002); *Hooper v. Zurich Am. Ins.*

Co., 552 N.W.2d 31, 36–37 (Minn. App. 1996); *Bryan v. Anfield*, No. C8-98-1206, 1998 WL 912142, \*1 (Minn. App. 1999) (“Accompanying the duty to defend is the insurer’s right to *exclusive control* over the litigation” (emphasis added)). Correspondingly, RDI had a contractual duty to cooperate with Integrity in the defense of the litigation. (Policy Section II (E)(2) at AA 48–49.)

The relationship that arises between the insurer, its insured, and insurance defense counsel, when an insurer undertakes a duty to defend, is known as the “tripartite relationship.” This Court has long recognized that the tripartite relationship creates the potential for conflicts of interest, and these conflicts are prevalent. *Pine Island Farmers Co-op*, 649 N.W.2d at 450 (citing *Atlanta Intern. Ins. Co. v. Bell*, 475 N.W.2d 294, 297 (Mich. 1991)).<sup>13</sup> As this Court recognized in *Pine Island Farmers Co-op*: “The danger is that, if a conflict of interest does arise, the nature of the tripartite relationship makes it likely that defense counsel will tend to favor interest of the insurer at the expense of those of the insured.” 649 N.W.2d at 450. The potential for such conflict is exacerbated when the insurer

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<sup>13</sup> In *Atlanta Intern. Ins. Co.*, the court stated that “courts and commentators recognize universally that the tripartite relationship between insured, insurer, and defense counsel contains rife possibility of conflict” and that the “interest[s] of the insured and the insurer frequently differ.” 475 N.W.2d at 297; *see also In re Rules of Prof'l Conduct*, 2 P.3d 806, 813 (Mont. 2000) (recognizing the “stark reality that the relationship between an insurer and insured is permeated with potential conflicts”); Robert E. Keeton & Alan I. Widiss, *Insurance Law* § 7.6(a)(1), at 809–10 (1988) (noting the “very substantial prospect that actual or potentially conflicting interests between an insurer and an insured will exist in regard to almost any tort claim that may be covered by liability insurance” and listing common sources of conflict).

defends under a reservation of rights. In this situation, subsumed within an insurer's duty to defend and its right to control the litigation must be the concomitant obligation not to prejudice the insured's later claim to coverage.<sup>14</sup>

While this is a matter of first impression in Minnesota, numerous courts in other jurisdictions have addressed the question directly. For example, the federal Tenth Circuit, in *Magnum Foods, Inc. v. Continental Casualty Co.*, stated:

[A]n insurer who undertakes the defense of a suit against its insured must meet a high standard of conduct. *Duke v. Hoch*, 468 F.2d 973, 978 (5th Cir.1972); *Gay & Taylor, Inc. v. St. Paul Fire & Marine Ins. Co.*, 550 F.Supp. 710, 714-16 (W.D.Okla.1981). The right to control the litigation carries with it certain duties. *Traders & Gen. Ins. Co. v. Rudco Oil & Gas Co.*, 129 F.2d 621, 627 (10th Cir. 1942). One of these is the duty not to prejudice the insured's rights by failing to request special interrogatories or a special verdict in order to clarify coverage of damages. *See Gay & Taylor*, 550 F.Supp. at 716. The reason for this is that when grounds of liability are asserted, some of which are covered by insurance and some of which are not, a conflict of interest arises between the insurer and the insured. If the burden of apportioning damages between covered and non-covered were to rest on the insured, who is not in control of the defense, the insurer could obtain for itself an escape from responsibility merely by failing to request a special verdict or special interrogatories. *Duke*, 468 F.2d at 979.

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<sup>14</sup> In fact, in deciding between an insured and insurer who should bear the onus for failing to obtain a special verdict or reasoned opinion, several courts have held that the issue turns on which of the parties "controlled the defense" of the litigation. *See, e.g., Med-Marc Cas. Ins. Co. v. Forest Healthcare, Inc.*, 199 S.W.3d 58, 62-63 (Ark. 2004); *Camden-Clark Memorial Hosp. Ass'n v. St. Paul Fire and Marine Ins. Co.*, 682 S.E.2d 566, 577, (W. Va. 2009). Undeniably, Integrity controlled the defense of the claims brought by the Provenzanos, nor did RDI have the benefit of independent or *Cumis* counsel. Consistent with these cases, the district court therefore properly held that Integrity bore the burden to obtain a reasoned award, and its failure to do so was a breach of the parties' contract.

*Magnum Foods, Inc.*, 36 F.3d 1491, 1498–99 (10th Cir. 1994). In the similar context of a settlement with no allocation between covered and non-covered claims, the federal Third Circuit explained the inherent risks to the insured when it held:

To reach the opposite conclusion could result conceivably in an insured never being indemnified in a suit that its insurer settles where the insurer defends under a reservation of rights. In such a situation, it would behoove the insurer to reserve its rights and to settle the suit to avoid both the costs of litigation and, at the same time, the costs of indemnification. Such a strategy should not be countenanced. We are persuaded that the approach adopted by the district court cannot be faulted because it is justified by both rational and pragmatic considerations.

*Pacific Indem. Co. v. Linn*, 766 F.2d 754 (3rd Cir. 1985). The failure of the insurer to fulfill this duty is a clear breach of its contract with the insured.

The principles announced in these decisions are squarely applicable to the instant case. Integrity undertook to defend RDI under a reservation of rights. When it did so, Integrity hired Mr. Elliot and assumed exclusive control over the litigation and the defense of the claims brought by the Provenzanos. Bound up in the exclusive right to investigate, settle or defend these claims was the corresponding obligation to ensure that a reasoned award was issued which would allow a coverage determination. By its failure to do so, Integrity has breached the parties' contract with RDI, and the court of appeals should be reversed.

**3. Integrity Was Responsible For Defense Counsel's Failure To Request A Reasoned Award.**

The district court was also correct in its determination, under these unique facts, that Integrity was responsible for the failure of its agent, defense counsel, to obtain a reasoned award. Accordingly, the court of appeals' rejection of this holding should be reversed. Under Rule 42(b) of the AAA rules, a party seeking a reasoned arbitration award must request it before an arbitrator is appointed. (AA 199.) On or before September 7, 2006, Integrity hired Mr. Elliot to defend RDI. On September 21, 2006, the AAA, with Mr. Elliot's full participation, issued an order appointing the arbitrator, John G. Patterson, Esq. On this same date, the AAA sent a Report of Preliminary Hearing and Scheduling Order, which included a section for "form of award" which allowed counsel to select from three forms: a standard award, a reasoned award, or findings of fact and conclusions of law. Despite having announced to RDI that there was a potential coverage dispute, neither Mr. Elliot nor Integrity requested a reasoned award. Following the final hearing and issuance of his award, Arbitrator Patterson—citing AAA Rule 42(b)—declined Mr. Elliot's untimely request for a reasoned award. As a result of Integrity's inaction, it not only waived RDI's right to have a reasoned award, but forever prejudiced its ability to have coverage fairly determined. Therefore, the district court also correctly found that Integrity was responsible for Mr. Elliot's failure to request a reasoned award, and it was liable to RDI for the resulting breach of contract.

This, too, is a matter of first impression in the State of Minnesota, and the court of appeals erred when it held the district court's review of decisions from other jurisdictions for guidance was inappropriate. Rather, Judge Larson's reliance on the decisions in *Stumpf v. Continental Cas. Co.*, 794 P.2d 1228 (Or. Ct. App. 1989) and *Smoot v. State Farm Mut. Automobile Ins. Co.*, 299 F.2d 535, 530 (5<sup>th</sup> Cir. 1962) was correct.<sup>15</sup> Again relying on the insurance company's duty to defend and right to control litigation, in *Stumpf v. Continental Cas. Co.*, the Oregon Court of Appeals held:

According to Restatement (Second) *Agency*, §214: "A master or other principal who is under a duty to provide protection for or to have care used to protect others or their property and who confides the performance of such duty to a servant or other person is subject to liability to such others for harm caused to them by the failure of such agent to perform the duty." That duty may be created by

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<sup>15</sup> Undeniably, there may be a split of authority on this issue. Many courts have decided the issue favoring an insurer's liability under agency principles, *see Smoot v. State Farm Mut. Auto. Ins. Co.*, 299 F.2d 525, 530 (5th Cir.1962) (Georgia law); *Continental Ins. Co. v. Bayless & Roberts, Inc.*, 608 P.2d 281, 294 (Alaska 1980); *Stumpf v. Continental Cas. Co.*, 794 P.2d 1228, 1231-32 (Or. Ct. App. 1989); *Pacific Employers Ins. Co. v. P.B. Hoidale Co.*, 789 F.Supp. 1117, 1122-23 (D. Kan. 1992); *see also Boyd Bros. Transp. Co. v. Fireman's Fund Ins. Co.*, 729 F.2d 1407, 1409-11 (11th Cir.1984); others have found that an independent contractor relationship with defense counsel insulates the insurer in the context of legal malpractice and bad faith claims, *see Feliberty v. Damon*, 72 N.Y.2d 112, 531 N.Y.S.2d 778, 782, 527 N.E.2d 261, 265 (1988); *Aetna Cas. & Sur. Co. v. Protective Nat'l Ins. Co.*, 631 So.2d 305, 306 (Fla. Dist. Ct. App. 1993); *Brown v. Lumbermens Mut. Cas. Co.*, 90 N.C.App. 464, 369 S.E.2d 367, 371 (1988), *aff'd*, 326 N.C. 387, 390 S.E.2d 150 (1990); *Merritt v. Reserve Ins. Co.*, 34 Cal. App. 3d 858, 110 Cal. Rptr. 511, 526-27 (Ct. App. 1973). However, this Court should be aware that Integrity *never* argued to the district court that it was insulated from liability for Mr. Elliot's failure to obtain a reasoned award by reason of his status as an independent contractor. Integrity improperly presented this argument for the first time at the court of appeals. (See RDI Court of Appeals Br. 21-22 n.13.)

contract. See Restatement (Second) *Agency*, §214, comment e. Stiff's contract with CNA provided, in part: "The company shall have the right and duty to defend any suit against the insured seeking damages which are payable under the terms of this policy applicable to [professional liability] . . . and may make such investigation and settlement of any claim or suit as it deems appropriate." Given CNA's contractual duty and the degree of control that it retained over Stiff's defense, we apply what appears to be the rule in the majority of jurisdictions: An insurer may be vicariously liable for the actions of its agents, including counsel that it hires to defend its insured.<sup>16</sup>

*Stumpf v. Continental Cas. Co.*, 794 P.2d at 1232 (interpolation in original).

Application of the rule announced in *Stumpf*, and similar decisions, to the unique facts of this case is appropriate for several reasons. First, it dovetails elegantly with the principles and rules set forth in *Magnum Foods, Inc. v. Continental Casualty Co.* and the other cases cited previously regarding an insurer's duty to defend. Second, this case does not involve an issue of attorney malpractice (because the scope of Mr. Elliot's representation of RDI was limited to the defense of the claims brought by the Provenzanos—not the coverage dispute with Integrity), nor does this case involve allegations of bad faith.<sup>17</sup> Instead, this case

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<sup>16</sup> In light of this quote, the court of appeals' suggestion that the reasoning in *Stumpf* did not support the district court's imposition of liability on Integrity is also mistaken. (AD 19, n.1.)

<sup>17</sup> These reasons have been the basis for denying vicarious liability in those decisions turning on the actions of independent contractors. See *Merritt v. Reserve Ins. Co.*, 34 Cal. App. 3d 858, 110 Cal. Rptr. 511 (Ct. App. 1973) (holding that an insurance company is not vicariously liable for the malpractice of the attorney it selects to defend the insured) and *Feliberty v. Damon*, 72 N.Y.2d 112, 531 N.Y.S.2d 778, 527 N.E.2d 261 (1988) (holding that an insurance company is not liable for bad faith in excess verdict resulting from negligence of defense

involves insurance defense counsel's failure, in his capacity as an *agent* of Integrity, to obtain a reasoned award that would allow RDI the opportunity to demonstrate coverage, and his failure in this regard prejudiced RDI's legal position in the coverage dispute. As a result, applied to the facts of this case, the rule announced in *Stumpf v. Continental Cas. Co.* is on point; the district court's decision was well reasoned; and the court of appeals should be reversed.

***B. THE COURT OF APPEALS' RELIANCE UPON AND EXTENSION OF THE PINE ISLAND FARMERS CO-OP DECISION WAS ERRONEOUS.***

The court of appeals declined to address the district court's analysis of *Stumpf v. Continental Cas. Co.*, and *Smoot v. State Farm Mut. Automobile Ins. Co.*, and held, instead, that the district court's reliance on these decisions from foreign jurisdictions conflicted with existing Minnesota decisional law, particularly this Court's decision in *Pine Island Farmers Co-op v. Erstad & Reimer*, 649 N.W.2d 444 (Minn. 2002). (AD 19–20.) The court of appeals reasoned that, absent defense counsel's dual representation of both RDI and Integrity, counsel had no duty of loyalty to Integrity, and therefore Integrity could not be liable for counsel's failure to obtain a reasoned award. (AD 22.) Practically, the court of appeals' decision extends *Pine Island* and thereby allows an insurer to evade indemnification by acquiescing in defense counsel's failure to obtain a reasoned award or a special verdict. In fact, operating under this analysis, absent

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counsel)). These cases were the backbone of Integrity's position here at the Court of Appeals. (Integrity Mutual Court of Appeals Br. 33-37.)

bad faith, an insurer bears no responsibility for the actions of defense counsel—so long as there is no dual representation of insurer and insured.<sup>18</sup> Because both the logic and result are misguided, the court of appeals should be reversed.

The court of appeals' application of *Pine Island* to the facts of this case was incorrect. *Pine Island* dealt with the discrete question of whether an insurer had standing to assert a legal malpractice claim against counsel it hired to defend its insured; this case does not. 649 N.W.2d at 445. The question presented by the facts in *Pine Island* required an analysis of dual representation of an insured and an insurer; the facts of this case do not.<sup>19</sup> *Id.* at 448–52. This case involves the

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<sup>18</sup> While it is RDI's position that the court of appeals erred in applying the "dual representation" analysis of *Pine Island* to this case, one cannot ignore the ramifications of the court's dicta construing Minn.R.Prof.R. 1.7. The court's opinion does not make room for the fact that an impermissible conflict of interests can arise out of the "tripartite relationship" even if there is no dual representation. (AD 19–21.) Put another way, the court's opinion could be construed to hold that, if there is no dual representation, no conflict of interest arises out of the "tripartite relationship"; defense counsel's complete fidelity is to the insured; and the insurer bears no liability for a betrayal of this fidelity, even when that betrayal inures to the insurer's benefit. Yet Rule 1.7(a)(2) does not limit the existence of conflicts to an attorney-client relationship; the Rule specifically recognizes the existence of a conflict between a current client and a "third person" or a "personal interest" of an attorney. It is precisely this type of conflict that arises for counsel undertaking defense of an insured in the context of a reservation of rights case. Even more problematic, the court's decision squarely places the onus directly on the insured—often a layman or small business person—to understand not only the existence of a potential conflict arising out of the "tripartite relationship," but also the danger inherent in an unwitting consent to any such conflict. This stands Rule 1.7(b) on its head. The Rule requires disclosure of the conflict by counsel and written consent to continued representation from the affected client.

<sup>19</sup> It is important to note that the question of "dual representation" was raised by neither party at the district court or the court of appeals. Instead, RDI's and the district court's analysis of the case revolved around defense counsel's role as an

scope of an insurer's defense obligations in the context of a reservation of rights; *Pine Island* did not. Notwithstanding that both cases involve the "tripartite relationship," on balance the facts and issues presented in the cases are discordant, and the court of appeals plainly erred in its reliance upon *Pine Island*.

Legally, the court of appeals' extension of the reasoning in *Pine Island* to this case is also logically dissonant. Shoehorning this case into *Pine Island's* dual representation rubric lead the court of appeals down the path to error, and this is reflected in its core holding:

Because RDI's attorney did not represent Integrity Mutual, the attorney had no duty toward Integrity Mutual to request an explanation of the arbitration award. Absent such a duty, Integrity Mutual cannot be held responsible for the attorney's failure to timely request an explanation of the arbitration award. The district court erred by presupposing an attorney-client relationship between RDI's attorney and Integrity Mutual that did not exist, and, in fact, would have been prohibited by *Pine Island*.

(AD 22.)

The issue is not whether counsel owed Integrity a duty, but rather whether Integrity is liable for actions that prejudiced RDI's position in the coverage dispute. Certainly, the existence of an attorney-client relationship between Integrity and Mr. Elliot has no bearing on whether Integrity should bear the onus

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agent (directed and paid) of Integrity, and in this capacity his prejudice of RDI's ability to assert a claim for coverage. (*See* AA 218–80.) Certainly, representation of RDI in the coverage dispute was beyond the scope of defense counsel's attorney-client relationship with RDI, but his conduct nevertheless prejudiced RDI in the coverage dispute and benefited Integrity.

for this prejudice.<sup>20</sup> Because the court of appeals erred in its reliance upon *Pine Island*, it should be reversed and the district court's ruling should be reinstated.

**C. THE COURT OF APPEALS ERRED IN ITS CONSTRUCTION OF RDI'S PLEADINGS WITH RESPECT TO POTENTIAL COVERED CLAIMS NOT SUBJECT TO THE "YOUR WORK" EXCLUSION.**

Several courts have held "where any single claim will support coverage, the insurer's failure to obtain a verdict segregating the damage awards amongst the claims, mandates payment of the entire damage award." *Herrera v. C.A. Seguros Catatumbo*, 844 So.2d 664, 668 (Fla. Ct. App. 2003) (citing *Morrison v. Hugger*, 369 So.2d 614, 616 (Fla. Ct. App. 1979)); accord *Duke v. Hoch*, 468 F.2d 973, 978 (5th Cir. 1972); *Gay & Taylor, Inc. v. St. Paul Fire & Marine Ins. Co.*, 550 F.Supp. 710, 714-16 (W.D. Okla. 1981); *U.S. Concrete Pipe Co. v. Bould*, 437 So.2d 1061 (Fla. 1983). In this case, a large part of the damages sought by the Provenzanos related to structural decay, wood rot and mold infestation in the walls of the existing home, which was the result of water intrusion through windows on which RDI replaced the flashing and trim. While RDI's actual work on the windows would have been an item of damage excluded under the "your work" provision of the policy, damage to the surrounding wall structure (on which RDI did no work) would have been covered. As a result, because there was a damage claim falling within the indemnity provisions of the contract, and not subject to the "your work" exclusion, consistent with the holding of the above-cited cases, RDI

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<sup>20</sup> The profundity of this error is illuminated by the appellate court's final assertion, regarding the district court's "presupposing" a dual representation, when no such statement or analysis appears in the lower court's decision. (AD 22.)

has demonstrated the existence of a covered claim, and Integrity is liable for the entire, undifferentiated award.

The court of appeals implicitly agreed that this item of damage would not have fallen under “exclusion m” of the policy, but held:

The flaw in RDI’s contention is that it is outside the scope of its pleadings. In its complaint, RDI never alleged that its liability to the Provenzano’s arose from property damage to the original part of the home that was caused by its defective work....RDI never argued to the district court that it incurred liability to the Provenzanos for property damage to the original part of the home caused by its own defective work.

(AD 28–29.)

In so doing, the court misconstrued both the evidence supporting the Provenzano’s claims at arbitration as well as RDI’s submissions to the district court.

The Provenzanos’ pre-hearing brief specifically alleged that the defective work performed by RDI resulted in water intrusion and structural damage to the house included the following: improperly installed window trim, improperly re-installed master bedroom window, improperly installed patio door, improper installation of addition flat roof, improperly installed fenestrations, improperly flashed dormer roof, and improperly applied window trim.<sup>21</sup> (AA 180–81.)

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<sup>21</sup> The Provenzanos also alleged that RDI was negligent in its failure to report or remediate construction defects in the work performed by LeGran and water damage existing at the time RDI’s work was performed. (AA 181.) However, for the purposes of this appeal RDI does not contest the court of appeals’ determination that this theory was not an “occurrence” under the policy, but does so without prejudice to or conceding that there were other aspects of the Provenzano’s claims that were “occurrences” or “accidents” covered under the policy.

Moreover, the Provenzanos alleged that RDI's negligent work exacerbated the existing defects in the original LeGran work. (*Id.*) In support of these claims, the Provenzano's offered an extensive "Mold & Forensic Report" from its expert, NDS. This report's section on "Windows and Doors" details what it believed were defects in RDI's work, and in describing the damage stemming from this work, the report states:

This method of construction allowed water that penetrated the lap siding to contact the sheathing and intrude within the wall assembly. The installation methods omitted are common industry practices and normal manufacturer's specifications. Left unattended, the problem will consume the wall assembly and cause substantial damage to the wall assembly and structure of the home. The windows observed were not installed so as to provide a waterproof barrier for the exterior structural wall systems.

(AA 159.)

In the "Opinions" section of this report, NDS reiterated that it considered RDI responsible for damage to the walls of the original, when it stated:

This method of construction allowed water that penetrated the lap siding to continue its contract with the sheathing and intrusion into the wall assembly. The installation methods ignored and allowed to exist are common industry practices and normal manufacturer's specifications. An individual working as a licensed contractor would know that the ignored problems will exponentially consume the wall assembly and cause substantial damage to the wall assembly and the structure of the home; including the trim work that they just completed. The building code requires that all wood with mold or rot be removed and repaired.

(AA 173.)

As a result, the court of appeals' contention that the Provenzano's claims did not include damage to the walls of the existing home is mistaken, and must be reversed.<sup>22</sup> (AD 28–29.)

The court's contention that RDI's pleadings and submissions to the district court omitted discussion of this item of damage is also plainly wrong.<sup>23</sup> In fact, this very item of damage was the *sole* topic addressed in RDI's reply memorandum supporting its motion for summary judgment. (AA 242–47.) Consequently, the court of appeals holding that RDI had failed to present this issue to the district court is also factually incorrect.

While an appellate court can consider only such issues as have been raised by the pleadings or litigated by consent at the trial court, *Schlecht v. Schlecht*, 209 N.W. 883, 887 (Minn. 1926), this is counterbalanced by the axiom that “[p]leadings shall be construed as to do substantial justice.” Minn.R.Civ.P. 8.06. Moreover, issues litigated at the trial court, either by express or implied consent,

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<sup>22</sup> The court of appeals also suggested that counsel conceded this point at oral argument. (AD 29.) With all due respect, counsel disputes that any such concession was made.

<sup>23</sup> The allegations of RDI's complaint should also be construed to include this item of damage. Paragraph 13 of the complaint alleges that RDI may have been found liable for property damage caused by “defects in the addition project constructed by Remodeling Dimensions.” (AA 206.) Earlier, paragraph 5 of the Complaint clearly defines the term “addition project” as encompassing all work performed on the addition *and* the original home. (AA 204.)

are treated as if they had been raised in the pleadings.<sup>24</sup> *Roberge v. Cambridge Cooperative Creamery Co.*, 67 N.W.2d 400, 403 (Minn. 1954). Accordingly, a liberal construction of RDI's complaint combined with the parties' submissions on their cross-motions for summary judgment clearly demonstrate that the issue was presented to and litigated in the district court. Then, because even the court of appeals conceded that this type of damage was covered by the policy, RDI has borne any burden it may have had to demonstrate the existence of a single covered claim, and Integrity's theory of the case—that none of the Provenzanos' claims were covered—craters, and the court of appeals should properly be reversed.

***D. THE COURT OF APPEALS EXCEEDED ITS JURISDICTION AS AN ERROR CORRECTING COURT.***

The instances of the court of appeals searching the record to find facts, not considered by the district court, are manifold.<sup>25</sup> The most glaring of these was its finding that “the attorney appointed by Integrity Mutual to represent RDI in the arbitration proceeding did not have an attorney-client relationship with Integrity

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<sup>24</sup> According to this Court, this rule has “always” existed in Minnesota. *Roberge*, 67 N.W.2d at 403 n.10.

<sup>25</sup> This is particularly evident in the court of appeals' ruling on the question of whether any of the Provenzano's claims were covered by the indemnity provision of the policy or whether the “your work” exclusion applied. (AD 22-30.) In the event the court of appeals believed the district court erred in its conclusion that a coverage determination was not possible on the facts presented, the proper course should have been for the court of appeals to reverse, with directions that the district undertake further factual findings and undertake an application of those facts to the language of the contract. Certainly, by proceeding to search the record for facts and undertaking this contract construction itself, the court of appeals exceeded its role as an error correcting court.

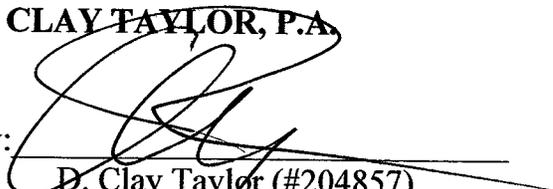
Mutual.” Notwithstanding the fact that this issue was never presented by the parties to either the district court or the court of appeals, the existence of an attorney-client relationship is an issue of fact that cannot be resolved by the court of appeals. *In re Paul W. Abbot Co., Inc.*, 767 N.W.2d 14, 18 (Minn. 2009) (“The existence of an attorney-client relationship is usually a question of fact dependent upon the communications and circumstances.”) “It is not within the province of [appellate courts] to determine issues of fact on appeal.” *Kucera v. Kucera*, 275 Minn. 252, 254–55, 146 N.W.2d 181, 183 (1966); *see also Wright Elec., Inc. v. Ouellette*, 686 N.W.2d 313, 324 (Minn. App. 2004) (stating that the Court of Appeals “cannot serve as the fact-finder” (citing *Kucera*, 275 Minn. at 254, 146 N.W.2d at 183 (1966)), *review denied* (Minn. Dec. 14, 2004)). Because it exceeded its jurisdiction as an error correcting court, the court of appeals should be reversed.

## **VI. CONCLUSION.**

Based upon all of the foregoing, Appellant respectfully requests that this Court issue an order reversing the opinion of the court of appeals, reinstating the order of the district court in its entirety, and awarding it such costs as may be allowed by law.

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