

NO. A07-155

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**STATE OF MINNESOTA  
IN SUPREME COURT**

Lester Building Systems, a division of Butler Manufacturing Company,  
and Lester's of Minnesota, Inc.,

Appellants,

v.

Louisiana-Pacific Corporation,

Respondent.

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**REPLY BRIEF AND SUPPLEMENTAL APPENDIX OF  
APPELLANTS LESTER BUILDING SYSTEMS  
AND LESTER'S OF MINNESOTA, INC.**

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The appendix to this brief is not available for online viewing as specified in the *Minnesota Rules of Public Access to the Records of the Judicial Branch*, Rule 8, Subd. 2(e)(2).

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## I. INTRODUCTION

In its opening brief, Lester explained why a reseller of a defective product, with a demonstrated business injury and need to repair the product, should be permitted to recover the cost to repair from the manufacturer, which sold the product through fraud. If the law is, as LP concedes it should be, “fair and reflect[ing] common sense,” (Resp. Br. at 2), the law should permit a reseller to recover the costs of repairs made in order to save its customer base, salvage its business, and do the right thing.

In its response brief, LP argues that a defrauded reseller should have no right to recover such costs unless the reseller proves its own legal liability to its customers. In LP’s view, business necessities and moral obligations are irrelevant. LP relies on *DeGidio v. Ace Eng’g Co*, 225 N.W.2d 217 (Minn. 1974), but that case does not go so far. Rather, the principles underlying the *DeGidio* decision evince sound public policy in favor of holding manufacturers responsible for putting defective products in the stream of commerce and not artificially limiting manufacturers’ liability at their victims’ expense.

Aside from *DeGidio*, LP offers no legal authority supporting its proposed rule of law, and either ignores or tries to distinguish the scholarly commentary and case law cited by Lester. The scholars and courts that Lester cites refuse to ignore the business practicalities of redressing breaches of commercial contracts and business fraud. They recognize that proof of business need should be sufficient to support recovery of costs to repair.

Given the weight of authority contrary to its general position, LP seems to ask this Court to carve out an exception for cases involving settlements. Lester does not quarrel

with the principle favoring settlements, but that principle has no application here. Lester did not settle with LP. Lester's customers were made members of a class action that was settled and for which the opt-out period had passed, *before* Lester's customers' claims were even ripe. Those customers received virtually nothing from LP through the class action. Lester was not a member of the class, and *its* claims against LP were not, and could not be, affected by the settlement. Rather than presenting a classic "settlement" case, LP's position turns on a legal construct peculiar to class actions that LP says should allow it to avoid full responsibility for defrauding Lester and causing thousands of barns throughout Minnesota and Iowa to rot. There is no principled reason to distinguish the "business need" rule in this case from any other such case. Indeed, it is LP's failure to redress or settle Lester's customers' claims directly that created the pressing need for Lester to do so.

LP also argues that it should not have to pay the costs to repair because – in its view – it has paid Lester or its customers "enough." Defendants, for obvious reasons, ordinarily do not get to decide what is enough. That reality is especially apropos in this case. Citing the class action settlement and its satisfaction of Lester's judgment for lost profits and costs to restore goodwill, LP calls up the spectre of "double recovery." But there is no duplication. As proven at trial, LP paid Lester's customers virtually nothing in the class action, so there is no double recovery as between Lester and Lester's customers. Likewise, there is no risk of double recovery by Lester itself, because the lost profits, costs to restore goodwill, and cost to repair elements of damages were not duplicative. Indeed, in the first appeal, the Court of Appeals recognized that Lester

received no award for future lost profits (presumably because the repairs would eliminate that prospect) and held that Lester was entitled to recover each element of damage, including cost to repair (the \$2 million indisputably outside the class action).

Further, on the matter of proof at trial of its “class action defense,” LP argues that it had no burden to present any evidence to the jury because the class action release’s “total protection” of Lester from legal liability was purportedly “self-evident.” (Resp. Br. at 28.) If the Court concludes, as Lester contends, that Lester’s legal liability to its customers is not dispositive, then the Court need not reach this “burden of proof” issue. If, however, the Court elects to depart from the weight of authority and conclude that the prospect of legal liability is a prerequisite for Lester’s “cost of repair” recovery, then the Court should recognize that the release did not actually obviate Lester’s liability to its customers. The release left open significant factual issues regarding its scope and effect, including which parties and claims were covered by the release. LP took a calculated risk at trial to present virtually no proof of its affirmative defense of release. That tactic backfired when the jury decided the factual issues against LP, and there is no basis for reversing the jury’s findings of fact.

Finally, LP devotes ten pages of its brief to two new “res judicata” theories that appear for the first time in this eight-year-old case. In the courts below, LP proffered a res judicata argument premised on a “virtual representation” theory espoused by some federal courts of appeals. Less than a month ago, however, the Supreme Court rejected that theory in *Taylor v. Sturgell*, \_\_\_ U.S. \_\_\_, 2008 WL 2368748 (June 12, 2008). LP’s novel efforts to distinguish *Taylor* come too late and lack merit in any event.

LP's fraud and breach of warranties wreaked havoc on Lester's fifty-year-old business. Lester had an undisputed business need and moral obligation to repair its customers' defective barns, whether or not the customers could or would sue Lester for damages. The jury and the trial court properly held LP responsible – the party that knowingly made and sold the defective Inner-Seal.

## II. REPLY ARGUMENT

### A. DeGidio Does Not Require Proof Of Legal Liability.

LP first argues that this Court already has decided the principal issue on this appeal – whether proof of legal liability is a prerequisite to a reseller's recovery for cost to repair. LP says: “Under this Court's decision in [*DeGidio*], Minnesota law requires a reseller to show potential liability to customers before it can recover breach-of-warranty or consequential damages for repair or replacement costs.” (Resp. Br. at 2.)

In *DeGidio*, this Court did *not* hold that proof of legal liability was a prerequisite for such recovery. Rather, the Court held that the reseller of defective products could recover the cost to repair the products it sold to its customers and, in so doing, simply noted that the reseller faced potential legal liability from its customers. This description of the factual situation in that case did not create a new rule of law, as LP suggests. Indeed, there is no indication that *DeGidio* ever conceded – or that the jury or the trial court ever concluded – that *DeGidio* actually faced legal liability to its customers.

In its brief, LP attempts to take the remittitur of a small portion of the jury award in *DeGidio* and transform it into a requirement that a reseller must face a risk of potential liability in the future. (Resp. Br. at 19.) That attempt is fanciful. The remittitur in

*DeGidio* had nothing to do with any legal liability *DeGidio* might have had to its customers. The Court simply said that it believed the jury verdict suggested a duplication of damages in an amount of the cost of the defective product, and the Court addressed that matter by remittitur. The Court did not deny any general category of damages, including the replacement cost, due to the perceived duplication. 225 N.W.2d at 224. In this case, LP's challenge to the allegedly duplicative nature of Lester's right to recover the cost of the Inner-Seal was finally decided on the first appeal, and it was decided against LP. *See infra*, at 13. As to the cost to repair, LP did not challenge on the first appeal Lester's right to recover as duplicative the \$2 million in repair costs for the buildings constructed in or after 1996 and should have no right to challenge the remainder of the repair costs (\$11.2 million) as duplicative. There is no reason why the pre-1996 building repair costs would be duplicative if the post-1996 were not. Indeed, a contrary ruling would result in inconsistent decisions in this case. In any event, monies paid to repair customers' barns to meet Lester's business need to do so in order to keep its business are distinct, non-duplicative monies from the original purchases of the Inner-Seal.<sup>1</sup>

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<sup>1</sup> LP also suggests that the requirement of proof of legal liability should, under *DeGidio*, turn on whether the repairs have actually been made or remain to be made. (Resp. Br. at 19.) This distinction has no legal basis. Moreover, it would make the legal requirements turn on whether the plaintiff has the funds to make the repair or has no funds and cannot make the repairs until it received recovery from the manufacturer. The law generally does not make elements of a claim turn on the wealth of the plaintiff. Here, Lester did not have the funds to make the repairs and that is one reason it sued LP. Tr. 610-12, Supp. App. 563-65.

In an analogous case involving fraud, this Court held that a reseller of ponies could recover monies paid to his customers who received falsely registered ponies, noting among other things that such payments “were necessary to protect plaintiff from litigation and thus *to mitigate the injury to plaintiff’s reputation and business goodwill.*” *Lowrey v Dingmann*, 86 N.W.2d 499, 502 (Minn. 1957) (emphasis added).

In short, although this Court has recognized that the existence of a legal obligation is a fact supporting recovery of repair costs under the UCC, this Court has not held in *DeGidio* or elsewhere that legal liability is a prerequisite for such recovery.

**B. Proof Of Business Need Is Sufficient For Recovery.**

In its opening brief, Lester cites legal authority showing that most courts and scholars agree that when a company sells a defective product to its customers and faces loss of its customer base or destruction of its business, the company is entitled to repair the defective products and may look to the manufacturer for damages reflecting those efforts. (Lester Br. at 27-31.)

LP either ignores such authority (in the case of Professors White & Summers) or fails to offer any counter authority. LP thus tacitly concedes that Lester’s authority “has the virtue of recognizing practical obligations that require business persons to conform to custom and usage in their trade in order to stay in business” (White & Summers, § 10-4). Cost to repair damages should be recoverable where the repairs are necessary to retain the customer and “taking care of problems [is] necessary in order to survive in the business.” *Tremco, Inc. v. Valley Aluminum Prods. Corp.*, 831 S.W.2d 156, 160 (Ark. Ct. App. 1992).

LP's efforts to distinguish authority cited by Lester are unsuccessful.<sup>2</sup> LP tries to suggest that this case is different because it involves a settlement by the manufacturer that purported to remove Lester's legal liability. (Resp. Br. at 25-26.) But LP offers no logic or policy reason why extinguishing legal liability by a settlement should be treated differently from cases where legal liability is extinguished on some other ground. The key concern should be whether there is a compelling business need to make the repairs to avoid further injury, not whether a settlement is involved. LP derives no help from the

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<sup>2</sup> LP argues incorrectly that *Woodbury Chemical Co. v. Holgerson*, 439 F.2d 1052, 1055 (10th Cir. 1971), supports a requirement of legal liability because the court noted that the repair there – respraying of herbicide – was an action that the middleman took in accordance with “accepted practice in this business.” (Resp. Br. at 26 n.17.) But “accepted practice in the business” is not the equivalent of legal liability. Indeed, the testimony at trial in this matter was similar – Lester was faced with a business need to make repairs because of the nature of the hog barn market – a close-knit, “repeat customer” market where companies like Lester provide their own personal warranty with each sale. Tr. 701-02, App. 407-08; App. 541-42; Tr. at 1700-01, Supp. App. 566-67. Citations to Lester's Supplemental Appendix are referred to herein as “Supp. App.” and followed by the specific page numbers. The Supplemental Appendix begins at page 562.

LP's suggestion that the decisions in *Tremco, supra*, and *Coastal Modular Corp. v. Laminators, Inc.*, 635 F.2d 1102 (4th Cir. 1980), turned on the existence of the reseller's legal liability is fallacious. In *Tremco*, the appellate court upheld a jury award because making the repairs was necessary to retain the customer and “to survive in business.” *Id.* at 160. The court did not cite any testimony concerning the customer's intent (or ability) to sue, and the issue of the reseller's legal liability appears nowhere in the decision. In *Coastal*, the court did not pass on the question of whether legal liability was necessary for a reseller to recover consequential damages for cost to repair. Rather, the court decided whether there was evidence of reasonably foreseeable damages so that the reseller did not need to wait until the repairs were completed before asserting its claims against the manufacturer. *Id.* On that point, the court found in the affirmative, as noted by Lester in its opening brief. (Lester Br. at 30-31.)

proposition that the law favors settlements. (*See* Resp. Br. at 25.) There is nothing in the jury verdict in this case that threatens to undermine parties' ability to settle cases.

Indeed, if anything, it is *LP's* proposal that would foster protracted litigation. *LP* would require resellers like Lester either to join their customers in the litigation or to seek to establish their own liability to their customers and thereby complicate and confuse a trial in which the real issue should be the manufacturer's liability for producing defective products, not the plaintiff's downstream concerns. Worse, *LP's* proposal could reward manufacturers of defective products with decreased liability by encouraging resellers to weigh their potential liability to their end customers before doing the right thing and making their customers whole.

**C. LP's Class Action Did Not Cure Lester's Injury.**

*LP's* argument regarding "settlement" really goes to a different question, one ignored in *LP's* response brief: Why did Lester have a compelling business need to make the repairs when *LP* supposedly had already addressed the need by settling the class action? Indeed, as *LP* tells it, "the \$11.2 million that Lester seeks is to repair buildings that *LP* already paid to repair." (Resp. Br. at 20; *see also* Resp. Br. at 25 ("there is no valid reason why Minnesota law should make a manufacturer pay a middleman to repair goods that the manufacturer has already paid to repair once before.").)

*LP's* statements are contrary to the evidence at trial. The evidence showed that Lester had its compelling business need notwithstanding – and indeed, in no small part as a result of – *LP's* class action. As Lester stated in its opening brief, the class action settlement did nothing for Lester and little or nothing for its farmer-customers. It

certainly did not pay for the repair of the Lester buildings. For those very few Lester customers who could (and did) seek compensation from the class settlement, the remedy fell far short. Tr. 419, 691, 1032, 1103-04, App. 394, 403, 444, 448-49. Some received nothing because LP rejected their claims or had not yet fully funded the settlement; a few received pennies on the dollar. The vast majority received nothing. Tr. 420, 698, 711-12, 1031-32, App. 395, 406, 410-11, 443-44. As many as 90% of the approximately 2600 barns at issue – those with failures after January 1, 2003 – were outside the settlement period, and therefore the farmers were not entitled to *a single penny* from the class action settlement to repair those barns. In short, the so-called “settlement” left Lester’s customers holding “the bag” for their out-of-pocket costs to repair the defective LP Inner-Seal on their buildings. Tr. 692, 711-12, 1031-32, App. 404, 411-12, 443-44.

LP sets up a straw man by asserting that “Lester fails to cite a single case in which a reseller sought repair costs after a manufacturer settled end users’ claims and obtained a release in favor of the reseller.” (Resp. Br. at 26.) The fact that cases discussing business compulsion are not typically found in the context of a settlement and release is not surprising. In most instances, settlements involve the parties to the lawsuit and provide compensation to the injured party. Here, Lester was not a party to the settlement, and Lester derived no benefit from the settlement. Likewise, Lester’s customers received little or no benefit from the settlement. This is not a case where Lester’s “business need” involves customers who, having already had their buildings repaired by LP, are still angry with Lester. To the contrary, their anger principally comes not from having defective siding, but from not being able to repair their buildings. Farmers repeatedly

testified that they expected Lester to repair their buildings, regardless of the outcome of the legal dispute between Lester and LP. One farmer testified, “I just want them fixed. I just want them fixed. The product did not last. Who’s [sic] fault it is, that’s up for someone else to decide, but I just want my barns fixed.” Tr. 424, Supp. App. 562; *see also* Tr. 1013-14, App. 441-42 (Q: And so, therefore, if they had fixed the problem, that would have been enough for you to consider Lester’s future buildings, correct?” A: Yes”).

Finally, LP’s characterization in its brief of the operation and fairness of the class action (Resp. Br. at 4-6), at least as to Lester’s customers, is diametrically at odds with the facts. The class action did not resolve Lester’s business need because it did not provide any real remedy to Lester’s customers. First, at the time the settlement was reached, and thereafter when the “opt-out” period occurred (April – May 1996), there were but a handful of failures on Lester’s customers’ buildings, and LP agreed then to reimburse Lester for repairs to those buildings. Hence, no Lester customer even had a claim for compensation by reason of a building failure at the time of the “class settlement.” Indeed, there was no evidence that they, or Lester for that matter, were aware of or understood the applicability of the class action to them. Indeed, to suggest, as LP does (Resp. Br. at 4-5), that Lester’s customers somehow knowingly negotiated and settled claims with LP in 1996 is wrong. In reality, it was not until September 1998, more than two-and-a-half years after the opt-out period had run, that LP abruptly stopped reimbursing Lester for replacement of defective Inner-Seal, Tr. 193, App. 378, and

advised Lester that it should “send” its customers to the class settlement for recovery. Tr. 147, App. 373.

Second, although LP touts the benefits of the class settlement, it fails to acknowledge that those benefits generally did not extend to Lester’s customers. According to LP’s own estimate at trial in Minnesota, LP paid \$640,000 (at most) to farmers facing \$11.2 million in repair costs for the more than 2400 Lester buildings built with Inner-Seal before 1996. *Compare* Tr. 2812-14, App. 512-14 *with* Resp. Br. at 6 (“[t]he settlement thus ‘resulted in the payment of more dollars to Claimants faster than almost every other product class action settlement, all at no cost or expense to Claimants.’”). Whatever its appeal to LP, or class counsel (which received more than \$26 million in fees for a few months’ work), or other claimants, the settlement that LP reached in Lester’s absence indisputably left Lester responsible in the eyes of its customers for substantial unrepaired damage to buildings sold by Lester with LP’s defective product.

In short, the evidence showed and the jury properly found that LP’s class action settlement did not obviate Lester’s compelling business need (and moral obligation) to repair its customers’ buildings. That factual conclusion justifies recovery, according to both the legal scholars and the courts.

**D. There Is No “Double Recovery.”**

In an attempt to blunt the clarity of Lester’s right to recover its full damages, LP sounds the alarm of purported “double recovery.” LP argues that Lester’s cost-to-repair

damages duplicate monies already paid to class members and duplicate elements of the damages award already granted to Lester by the jury at trial. LP is mistaken.

In *Jacobs v. Rosemount Dodge-Winnebago South*, this Court held that “an award based upon a bona fide effort to compensate for the consequences of the defects that established the breach of warranty is a remedy the U.C.C. seeks to provide.” 310 N.W.2d 71, 77-78 (Minn. 1981). As *DeGidio* makes clear, Lester’s cost-to-repair damages belong to Lester, not class members, and are permissible even though Lester’s customers might seek such costs directly from LP. *DeGidio*, 225 N.W.2d at 222.

In any event, as explained above, LP’s own evidence showed there was no actual double recovery from LP. Lester’s customers received a pittance from the class action settlement.<sup>3</sup> Indeed, if Lester cannot recover these damages, it is LP – the tortfeasor – that will receive an enormous windfall of \$11.2 million, not Lester or its customers.

LP also argues that the cost to repair award of \$11.2 million duplicates other elements of the jury’s award to Lester. Specifically, LP claims that “[a]ny harm Lester’s business may have suffered is adequately addressed by the jury’s awards for lost profits and goodwill damages.” (Resp. Br. at 20.) Again, LP is mistaken. The jury awarded Lester \$29.6 million. The components of the damages were, as described in the jury

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<sup>3</sup> The evidence showed that LP paid at most \$640,000 towards repairs of Lester’s customers’ buildings. Tr. 2812-14, App. 512-14. Lester’s experts testified that their calculation of the repair costs of \$13.2 million was conservative. Thus the jury would have been within its rights to discount the amount LP claimed it had paid from the class action. If there is any duplication at all – and Lester submits there is none – it is limited to \$640,000. That amount could be addressed by remittitur, but it should not abrogate the remainder of the jury’s award.

award: \$3.4 million for the cost of the Inner-Seal; \$10.2 million for lost profits; \$2.8 million for cost to restore goodwill; and \$13.2 million for costs to repair the buildings. App. 100. LP's duplication argument fails procedurally and substantively.

Procedurally, LP never argued at trial, or on the first appeal, that the costs to repair duplicated Lester's lost profits, costs to restore goodwill, or cost of the Inner-Seal. LP has therefore waived this issue. *Sauter v. Wase Miller*, 389 N.W.2d 200, 201-02 (Minn. 1986). The only "duplicative" argument that LP preserved and made, as it notes in its response brief (Resp. Br. 18 n.12), was whether the cost of the Inner-Seal (\$3.4 million) was duplicative because Lester had resold that defective Inner-Seal to its customers. That argument was rejected on the first appeal. *Lester Bldg. Sys. v. Louisiana-Pac. Corp.*, A03-48, 2004 WL 291998, at \*7 (Minn. Ct. App. Feb. 17, 2004). This Court denied review of that decision. There is no reason for a different result here.

Even if not waived, LP's "duplication" argument fails substantively. The lost profit award was for *past* lost profits only. It did not include future harm or loss of profits. The Court of Appeals so held on LP's first appeal:

...the jury only awarded Lester its actual profits. The testimony presented by Lester's damages expert was that Lester suffered \$10.2 million in past lost profits, and Lester anticipated losing an additional \$2.7 million of profits during 2003. The jury entered \$10.2 million on the special-verdict form next to the category entitled 'Lost Profits.' Viewing the evidence in the light most favorable to the verdict, the jury awarded Lester its actual lost profits and did not award anticipated lost profits.

*Id.* at \*7. Presumably, the jury concluded that by awarding Lester costs of repair, it would enable Lester to repair the buildings and avoid future profit losses. Hence, the jury award regarding lost profits and cost to repair are clearly complementary, not duplicative.

Similarly, by subtly changing the wording of the goodwill award to loss of goodwill or “goodwill damages,” LP misstates the nature of the award. The \$2.8 million award was not, as LP would have the Court believe, for loss of goodwill in the traditional sense. Rather, it was, as stated in the verdict, “cost to restore goodwill.” App. 100. This phrase was purposeful. Lester’s damage expert and president testified at trial that it would be necessary for Lester to institute a marketing and incentive plan to attempt to salvage Lester’s goodwill and business reputation. Tr. 1602-05, Supp. App. 576-79; Cost to Restore Lester’s Goodwill, Supp. App. 580; Tr. 1720-23, Supp. App. 568-71. The program had five specific elements, one of which was to advertise Lester’s repair program. Tr. 1604, Supp. App. 578; Supp. App. 580. None of the elements of the program were for cost to repair damages or compensation for damage to Lester’s reputation. The cost of this program would be in excess of \$5 million. The jury awarded Lester part of those costs. As compensation for a future plan to avoid future losses, the jury’s award of those damages was consistent with and complementary to the cost to repair award. There is no duplication.

**E. Even If Legal Liability Is Required, The Judgment Entered On The Jury’s Award Should Be Reinstated.**

If the Court concludes, as a matter of law, that Lester is entitled to recover costs to repair based on a compelling business need (regardless of legal liability to customers), the judgment should be reinstated without more. In the event that the Court decides to adopt LP’s position, Lester still should prevail because LP failed to prove its defense. Indeed, as LP notes, the District Court accepted LP’s legal position. (Resp. Br. at 10.) The District Court differed with LP only on the scope of the release and what the evidence

showed regarding which buildings were covered by the release and LP's likelihood of fully funding the settlement. *See* Tr. 2942-43, Supp. App. 574-75. The District Court instructed the jury that Lester's claims reflecting costs to repair were barred unless: (i) the buildings were constructed after January 1, 1996; (ii) the buildings would have failures after January 1, 2003; or (iii) the claims were for failures that were unpaid and would not be funded. The jury clearly found these exceptions to apply.

LP claims, however, that the District Court erred in instructing on the latter two exceptions. LP relies on a March 15, 1996 letter signed by class counsel and LP's counsel, which was attached to an amendment to the settlement agreement in the class action. Based on that letter, LP contends that Lester faced no potential legal liability from its class-member customers even if LP did not fund the settlement or even if the class members got no remedy in the class action. (Resp. Br. at 30-31.) Whatever LP and class counsel may have intended to achieve regarding the release of entities like Lester under such circumstances, the letter confirms the more important point – that class members would not be provided any remedy in exchange for such release, and thus its legal effect was far from clear. *See, e.g., Karnes v. Quality Pork Processors*, 532 N.W.2d 560, 562 (Minn. 1995) (“As with any contract, a release requires consideration, voluntariness, and contractual capacity.”)

The District Court recognized this fundamental principle. If a customer of Lester was entitled to no recovery from the class settlement because his building failed after January 1, 2003 (the cut-off date for claims in the settlement) or because LP chose not to fund the settlement to pay for all for pre-2003 failures, the release would have no effect

and would not, in fact, relieve Lester of liability. The District Court explained: “I don’t think it [the release] would ever stick because once that funding is stopped that leaves no remedy and as far as I’m concerned you would be violating due process, equal protection and a breach of the contracts...they essentially gave no remedy to the end users against the builder....” Tr. 2933, Supp. App. 573. The evidence at trial (in October 2002) was that the circumstances that would trigger these two exceptions to the release were likely to occur.<sup>4</sup>

LP next argues that, even if the District Court correctly instructed the jury, (i) the District Court erred in failing to provide guidance on how to apply the exceptions (Resp. Br. at 10-11); or (ii) to the extent guidance was provided, “the jury quite plainly did not follow it.” (Resp. Br. at 42.) As usual, LP seeks to blame everyone but itself. LP would like to disclaim any responsibility to prove and argue its defense. The defense of “release” is a classic affirmative defense for which the defendant bears the burden of proof. *See* Minn. R. Civ. P. 8.03; *Karnes*, 532 N.W.2d at 563 (“A release is an affirmative defense to a cause of action.”) *Brekke v. THM Biomedical, Inc.*, 683 N.W.2d 771, 779 (Minn. 2004) (the defendant carries the burden to prove the factual elements of affirmative defenses).

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<sup>4</sup> LP asks the Court to take judicial notice of the fact that, after the conclusion of the trial, LP did fund the settlement. (Resp. Br. at 6 n.6.) This proposal makes little sense. A jury verdict should be reviewed on the evidence at trial, not what occurred thereafter. LP had the opportunity to present evidence at trial that it would fund the settlement. Instead, during the trial regarding the full funding of the class settlement, LP’s Chairman said imperiously, “I haven’t made up my mind.” Tr. 2134-35, App. 482-83. Based on this testimony, the jury’s finding that LP likely would not fund the settlement was both understandable and well within the jury’s prerogative.

At trial, LP made no effort to carry the burden. It made the tactical decision to employ an “all-or-nothing” approach to whether it had “honored its warranty” by settling the class action. The result of LP’s strategy, however, was that LP left the jury with little alternative but to accept LP’s theory *in toto* or reject it. The jury chose to reject it.

The evidence at trial supported the jury’s decision. Lester showed that there were more than 2600 buildings with defective Inner-Seal, and each building inevitably would fail. Tr. 207, 800, 1384-86, App. 381, 427, 461-63. Lester had provided its own warranty with each of these buildings, and its customers were clamoring for Lester to honor its warranty. App. 541-42. For buildings constructed after 1996, and indisputably not covered by the release, Lester’s expert calculated the cost for repairs at \$2 million. Moreover, there was evidence that as many as 90% of the 2600 buildings had not yet failed, and thus it was likely the failures would occur after January 1, 2003 – the cut-off date for claims under the settlement. App. 407, 516. Under the second exception, therefore, the jury could have found that as much as 90% of the total \$13.2 million cost of repair (*i.e.*, nearly \$11.9 million) was unaffected by the class action. The jury likewise could have found that the remainder of the cost to repair was for post-1996 buildings or for past, unpaid claims that LP would never fund. At the time of trial, there were thousands of claims, worth many millions of dollars, that remained unpaid in the class action. Given a chance to remove the uncertainty as to whether these claims would be paid, LP’s chairman instead testified that he had not made up his mind whether to fully fund the settlement. *See* Tr. 2134-35, App. 482-83.

Finally, it bears emphasis that LP never offered into evidence, and never produced in discovery (despite repeated requests), the opt-out list in the class action. On the crucial issue of who the class members actually were, LP presented only hearsay testimony by an employee about his review of the list of opt-outs. The jury surely could have disbelieved this representative of a corporation guilty of egregious fraud, especially because he failed to provide the best evidence – the actual opt-out list.<sup>5</sup> See, e.g., *Costello v. Johnson*, 121 N.W.2d 70, 76 (Minn. 1963) (weight and credibility of witness is for trier of fact to determine and jury is not compelled to believe *any* witness merely because his testimony is not directly contradicted); accord, *Backman v. Fitch*, 137 N.W.2d 574, 580 (Minn. 1965) (jury may disregard positive testimony of a witness although he is not contradicted by other witnesses if his testimony is impeached). App. 510-11; see also Tr. at 2883, Supp. App. 572 (The Court: “Claims by Lester’s customer[s] who opted out? I can see that [not being affected by the class action].”).

The jury’s verdict was consistent with the Court’s instruction and supported by the evidence. The judgment entered on that verdict therefore should be reinstated even if the Court adopts LP’s position on whether legal liability is a prerequisite for cost of repair recovery. “We will not interfere with the jury’s award of damages unless our ‘failure to do so would be ‘shocking’ and result in a ‘plain injustice.’” *Jacobs*, 310 N.W.2d at 79.

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<sup>5</sup> Indeed, the testimony of LP’s witness wasn’t even that no Lester customer had opted out – it was that he had reviewed “some documents supplied by the class action, I guess administrator” and that he “could not find any names that matched” the names on a list of Lester customers. Tr. at 2812, App. 512.

**F. Claim Preclusion Does Not Bar Lester's Repair Costs Claim.**

At the end of its brief, LP presents an argument that the Court of Appeals did not decide. LP argued below that the res judicata effect of the judgment in the Inner-Seal class action barred Lester's claim for repair damages because Lester was the "virtual representative" of its customers and the judgment in the class action resolved its customers' claims. Since the briefing in the Court of Appeals, the Supreme Court has rejected the doctrine of claim preclusion by reason of "virtual representation." *Taylor v. Sturgell*, \_\_\_ U.S. \_\_\_, 2008 WL 2368748, at \*16 (June 12, 2008). The Supreme Court stated: "The application of claim and issue preclusion to non-parties thus runs up against the 'deep-rooted historic tradition that everyone should have his own day in court.'" *Id.* at \*11 (citation omitted). The *Taylor* decision dispositively resolves and rejects LP's claim here.

Not deterred by the obvious, LP tries to shoehorn this case into an exception to the general rule that "one is not bound by a judgment *in personam* in a litigation in which he is not designated as a party or to which he has not been made a party by service of process." *Taylor*, at \*9 (quoting *Hansberry v. Lee*, 311 U.S. 32, 40 (1940)). LP's recast attempt to invoke res judicata – on arguments not made below – fails in the face of the Supreme Court's recent decision.

The res judicata effect of a federal judgment is a question of federal common law. *See California v. Chevron Corp.*, 872 F.2d 1410, 1416 (9th Cir. 1989). As with analogous state law, however, the federal common law of res judicata is subject to the limits of due process. *See Taylor*, \_\_\_ U.S. at \_\_\_, 2008 WL 2368748, at \*9. To succeed

on a res judicata defense, LP must establish that: (1) there was a prior final adjudication on the merits; (2) there is an identity between the claim previously adjudicated and the claim now asserted; and (3) there is an identity or “privity” between the parties such that one of the exceptions identified in *Taylor* applies. *See Taylor*, \_\_\_ U.S. at \_\_\_, 2008 WL 2368748, at \*10-11; *see, e.g., Marshall v. Inn on Madeline Island*, 631 N.W.2d 113, 119 (Minn. Ct. App. 2001) (holding that res judicata did not apply because there was not sufficient identity of parties).<sup>6</sup>

**1. There Is No Identity Of Claims.**

At the trial in this case, the jury found that LP defrauded Lester regarding the properties of Inner-Seal. Tr. 462, 734-41, 753-54, 1187, App. 398, 414-17, 421-22, 454; App. 521, 524-25, 529, 531, 534-40. The Court of Appeals upheld the jury’s finding. *Lester Bldg. Sys.*, 2004 WL 291998, at \*5. Lester’s fraud claim turned on representations made to Lester and Lester’s reliance. That claim belonged to and could be made solely by Lester. It was not made in the class action. If any fraud claims were “adjudicated” in the Inner-Seal class action, the claims were not Lester’s fraud claims, and were not

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<sup>6</sup> LP blurs two separate parts of the class action settlement – the release and the stipulated federal judgments – by arguing that “[w]hen the prior judgment was entered on a settlement agreement containing a release of claims, any subsequent claim within the scope of the release contained in the settlement agreement is subject to preclusion.” (Resp. Br. at 33.) In fact, a release itself has no res judicata effect. It is only the judgment that can have any such effect. The judgment in the class action did not purport to include claims against non-parties. In order to be a “Settled Claim” under the class action settlement agreement, a claim had to be, *inter alia*, “against any of the Defendants.” (Resp. Br. at 34.) Lester was not a defendant in the class action, so a claim against it would not fall under the definition of a “Settled Claim.” The accompanying release may have covered certain claims against resellers like Lester, but that does not mean that such claims were included in the judgment.

factually based on anything Lester did or did not do based on LP's conduct. The simple fact that the injuries of the class members and the injuries of Lester have the same root – LP manufacturing, selling, and promoting defective Inner-Seal – does not lead to the conclusion that the claims in the two suits are the same. *Sandpiper Vill. v. Louisiana-Pac. Corp.*, 428 F.3d 831, 848 n.25 (9th Cir. 2005).

Lester's warranty claim was likewise based on warranties made orally, in letters, and in marketing materials and product descriptions sent directly to Lester. Tr. 461-62, 754, 1087, 1187, 1269-71, App. 397-98, 422, 446, 454, 457-59; App. 518-32, 540. For example, in a letter of February 13, 1991 to Lester, LP warranted that Inner-Seal was suitable for Lester's particular use. App. 533, 540. The judgment entered pursuant to the class action settlement may have resolved warranty claims (as set forth in that complaint), but they were not Lester's warranty claims. The claims in the class action were presumably based on distinct warranties that ran to those end-users, and not the specific warranties made to Lester. Those are separate claims. Again, the fact that the sale of a defective product breached different warranties made to different people does not make claims brought under those different warranties the same claim for res judicata purposes.

## **2. There Is No Identity Of Parties.**

Lester was not a party in the class action. LP's res judicata argument therefore runs headlong into the rule just re-confirmed by the Supreme Court, that "one is not bound by a judgment *in personam* in a litigation in which he is not designated as a party...." *Taylor*, \_\_\_ U.S. at \_\_\_, 2008 WL 2368748, at \*9. In an effort nevertheless to bind Lester to a judgment in a case to which it was not a party, LP previously argued that

Lester was the “virtual representative” of its customers, based on how it intended to spend money it recovered. Because the Supreme Court just rejected the doctrine of “virtual representation” in *Taylor*, that should be the end of the matter. LP now argues that, even though Lester was unquestionably not a party in the class action, it is “in privity” with its customers because their relationship allegedly fits within traditional exceptions identified in *Taylor*: (1) a pre-existing legal relationship between the person to be bound and a party to the prior judgment; and (2) acting as the designated representative of a party bound by the prior judgment. Neither argument has merit.<sup>7</sup>

a. **Lester’s Status As Reseller To Its Customers Does Not Give Rise To Preclusion.**

LP first claims that a sufficient “pre-existing legal relationship” existed between Lester and its end customers because its customers were allegedly third-party beneficiaries of the warranties LP made to Lester. LP’s argument fails on many levels.

First, LP’s argument finds no support in *Taylor*. The *Taylor* Court recognized that certain pre-existing legal relationships, including “preceding and succeeding owners of property, bailee and bailor, and assignee and assignor,” may be constitutionally sufficient to allow preclusion against a related party. *Taylor*, \_\_\_ U.S. at \_\_\_, 2008 WL 2368748, at \*10. The Court specifically cites Sections 43, 44, 52, and 55 of the Restatement (Second) of Judgments as support for this proposition. The *Taylor* Court does not,

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<sup>7</sup> As Judge Clifton stated in *Sandpiper Vill.*, 428 F.3d at 848, “[n]or were Lester’s interests sufficiently parallel to the class members’ interests such that privity could be implied.”

however, speak of third-party beneficiaries or cite Section 56, the Section on which LP relies. *Id.*

Second, there is no evidence that Lester's customers were third-party beneficiaries of the specific warranties LP made to Lester. Since the issue was never presented below, there is no factual finding to support LP's claim.

Third, even if Lester's customers were third-party beneficiaries, those customers did not bring warranty claims as third-party beneficiaries in the class action. Lester's customers were simply made class members by class counsel before they even had ripe claims. As such, their status, if any, as third-party beneficiaries has no relevance for preclusion purposes. Indeed, there is no evidence that the particular warranties made to Lester orally, in letters, or in marketing materials were even claimed or considered in the class action.

Fourth, and in any event, LP's third-party beneficiary argument has no applicability or effect on Lester's fraud claim. Because it was the fraud claim that the Court of Appeals found dispositive in the earlier appeal, *see Lester Bldg. Sys.*, 2004 WL 291998 at \*5, LP's res judicata argument has no applicability whatsoever to Lester's right to recover its damages in this case. Even LP cannot bring itself to argue that Lester's customers were the third-party beneficiaries of LP's fraud.

**b. Lester Did Not Designate Itself The Representative Of Its Customers.**

LP argues alternatively that Lester is bound by the class action judgment because Lester purportedly "declared itself" the representative of its customers in seeking repairs. LP's legal logic fails, and the argument is not consistent with the facts.

Lester is the real party in interest in this case, and the jury awarded the damages to Lester. Lester is not a statutory representative of its customers (as in *Chicago, R.I. & P. Ry. Co. v. Schendel*, 270 U.S. 611, 617-18 (1926)<sup>8</sup>); nor are Lester's customers merely using Lester's name as the nominal plaintiff in this case to circumvent a previous judgment (as in *United States v. Des Moines Valley R.R. Co.*, 84 F. 40 (8th Cir. 1897)<sup>9</sup>); nor was Lester appointed by its customers or any court as the designated representative of its customers.

LP's sole support for its "designated representative" argument is that Lester's president John Hill testified at trial that Lester would use monies it recovered to fix its customers' buildings if Lester prevailed at trial. (Resp. Br. at 39-40.) LP then cites *Schendel* and argues that the federal law of claim preclusion should preclude Lester's claim because Lester's end customers ultimately would benefit from Lester's recovery. *Schendel* did not hold that the second claim was precluded merely because the same

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<sup>8</sup> LP's reliance on *Chicago, R.I. & P. Ry. Co. v. Schendel*, 270 U.S. 611, 617-18 (1926), is misplaced. In *Schendel*, the identity of the parties requirement was satisfied because the first action involved the sole beneficiary as an actual party and the second action, which was precluded, involved her statutory representative solely on her behalf. Here, by contrast, Lester was not a party to the class action nor is Lester the statutory representative of its end customers.

<sup>9</sup> *United States v. Des Moines Valley R.R. Co.*, 84 F. 40 (8th Cir. 1897), is clearly inapposite. In *Des Moines Valley*, the government "'had no interest in the land' and had 'simply permitted [the landowner] to use its name as the nominal plaintiff'" to try to avoid a previous adverse judgment. *Taylor*, \_\_\_ U.S. at \_\_\_, 2008 WL 2368748, at \*13. The *Des Moines Valley* action was brought solely for the benefit of the landowner and "not for the purpose of redressing any wrong which has been done to the United States, or of recovering any property in which it now retains an interest." *Des Moines Valley*, 40 F. at 43. Unlike the plaintiff in *Des Moines Valley*, Lester has a claim for its own distinct injury from LP's breach of contract and fraud.

person would benefit. Instead, the Court held that the claim was precluded because the plaintiff in the second action was solely the statutory representative of the plaintiff in the first. That is not the circumstance here. The due process limits on the doctrine of res judicata do not permit the sweeping rule that LP proposes. Indeed, in rejecting preclusion by virtual representation, the *Taylor* Court was concerned about courts circumventing due process protections and precluding claims that should not be precluded – precisely as LP seeks to do here. *See Taylor*, \_\_\_ U.S. at \_\_\_, 2008 WL 2368748, at \*14.

In sum, the facts in the record demonstrate that Lester brought this action on its own behalf seeking redress for its own injuries resulting from LP's fraud (and breaches of warranty). The costs to repair buildings are *undeniably* tied to Lester's attempts to restore its own reputation and business. Lester's president clearly testified that Lester's cost to repair recovery was *for its own good*.

Q. (By Mr. Langdon – L-P Counsel): And as a result what you're essentially doing here with the lawsuit is attacking the class action?

A. I don't care about the class action. I'm looking at this and saying Lester *in order for it to survive* needs to go out and fix these problems.

Tr. 1734, App. 477 (emphasis added). As such, Lester was not the designated representative of its end customers, and its claims are not barred by res judicata.

**G. The District Court Properly Denied LP's Motion For A New Trial.**

Lastly, LP's request for new trial should be rejected. Trial courts have broad discretion in deciding whether a new trial is required, and no error is grounds for granting a new trial unless the refusal to do so is inconsistent with substantial justice. *Law v. Essick Mfg Co*, 396 N.W.2d 883, 888 (Minn. Ct. App. 1987). LP argued in its first appeal that the District Court's failure to direct a verdict in LP's favor with respect to the

costs to repair award for *all* pre-1996 buildings was grounds for a new trial. The Court of Appeals expressly rejected that argument, *Lester Bldg. Sys.*, 2004 WL 291998, at \*4 n.1, and there is no reason for a different result in this Court this time around.

There is nothing to be gained from a new trial on cost to repair. LP's liability for fraud was affirmed in the prior appeal, and as to damages, LP has never disputed that \$11.2 million was the correct cost to repair the subject buildings. LP presented no testimony suggesting a different figure. Rather, LP's argument was always that the class action barred *any* recovery of the \$11.2 million in repair costs. Accordingly, if the Court concludes that Lester is entitled to its cost to repair, as Lester respectfully submits it should do, LP has no right to contest the amount after failing to do so at the trial.

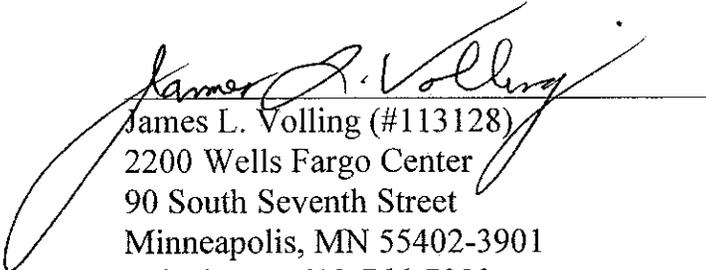
### III. CONCLUSION

For the foregoing reasons, Lester respectfully requests that this Court reverse the decision of the Court of Appeals and affirm the Amended Judgment below.

Respectfully submitted,

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Dated: July 3, 2008



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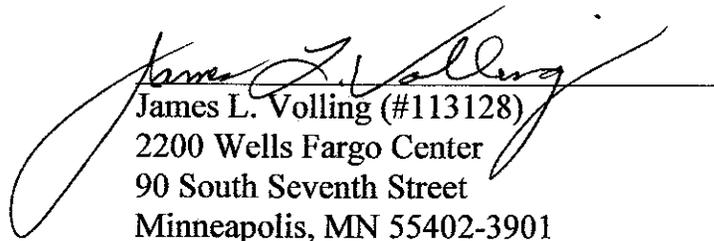
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**CERTIFICATION OF BRIEF LENGTH**

Pursuant to Minn. R. Civ. App. P. 132.01, subs. 1 and 3, I hereby certify that the length of this brief is 8,010 words and produced with a proportional font. This brief was prepared using Microsoft Word 2003. A motion for permission to file an enlarged brief accompanies this brief.

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