

NO. A11-1145

State of Minnesota
In Court of Appeals

Auto-Owners Insurance Company,

Appellants,

vs.

Second Chance Investments,

Respondents,

RESPONDENT SECOND CHANCE INVESTMENT'S BRIEF AND APPENDIX

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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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LEGAL ISSUE

Minnesota's Standard Fire Policy prohibits any policy provision "limiting the amount to be paid in case of total loss on buildings * * * to less than the amount of insurance on the same." It allows appraisal "except in case of total loss on buildings." Nonetheless, Auto-Owners asserts that "total loss" issues are appraisable. Should the district court have ordered appraisal of whether Second Chance's building suffered a "total loss" within the statutory meaning?

No. Appraisers do not have jurisdiction to decide whether a property has suffered a "total loss" within the statutory meaning.

PROCEDURAL HISTORY

On March 12, 2009, Auto-Owners filed a complaint in the district court asking it to compel Second Chance to submit its claim of total loss to appraisal. (RA-03). Second Chance sought to dismiss the complaint initially, then filed an amended answer asserting a counterclaim for breach of contract.¹ (RA-12.)

On November 30, 2010, Auto-Owners filed a motion to compel appraisal. (RA-29.) In response, Second Chance moved for partial summary judgment declaring the Kings Point Road property a total loss. (RA-39.) Second Chance also moved to amend its counterclaim to seek taxable costs for bad faith under Minn. Stat. § 604.18 and prejudgment interest under Minn. Stat. § 60A.0811.

The district denied Auto-Owners' motion to compel appraisal on April 11, 2011. (RA-237.) The court also denied Second Chance's motion for partial summary judgment, but granted its motion to amend its counterclaim to add a claim for taxable costs for bad faith under Minn. Stat. § 604.18. (*Id.*)

On May 3, 2011, Auto-Owners asked Second Chance to join it in moving the district court to amend the scheduling order. (Moline Affidavit in Support of Motion to Dismiss Appeal, Exhibit 8, Charles M. Austinson letter of 5/3/11.) Auto-Owners then wrote the court a letter on May 19th requesting dismissal of its complaint for appraisal.

¹ The caption for this pleading inadvertently omitted the word "Counterclaim"; however, numerous other documents refer to the counterclaim, the district court allowed its amendment to add bad faith, Auto-Owners responded to it, and the district court has stayed resolution of it pending the decision on this appeal.

Second Chance received this letter Friday May 20th, without the proposed Supplemental Order. (Moline Aff., Exhibit 9, Charles M. Austinson letter of 5/19/11; Moline Aff.) The following Monday, May 23rd, the District Court entered the Supplemental Order dismissing the complaint for appraisal. (Moline Aff., Exhibit 10, Supplemental Order of 5/23/11.) On Tuesday, May 24th, the district court entered an amended scheduling order. Second Chance wrote to the court on May 27th to confirm that the suit was still active on the breach-of-contract counterclaim and bad-faith taxable costs claim. (Moline Aff., Exhibit 11, Letter to Judge Blaeser of 5/27/11.)

Auto-Owners filed the instant appeal on June 22, 2011. (RA-231). Second Chance moved to dismiss Auto-Owners' appeal. This court denied that motion on August 29, 2011, ruling that the order was appealable as a final declaratory judgment. (RA-255).

STATEMENT OF FACTS

The insured premises and loss

Second Chance Investments owned a property at 3406 Kings Point Road in Minnetrista, Minnesota. (*See* App-01). On September 26, 2008, Second Chance purchased from Auto-Owners a “Dwelling Insurance Policy,” number 46 570380 00, effective from September 26, 2008 to September 26, 2009. (*Id.*) Consistent with Minnesota’s Standard Fire Insurance Policy, which is a “valued policy law,” the policy’s Minnesota Amendatory Endorsement contained a “Valuation Clause” that promised to pay the full policy limits in the event of a “total loss.” (App-21).

Auto-Owners appraised the property’s value at \$2,095,000, and stated this amount in the Declarations as the limit of insurance for Coverage A, Dwelling. (App-01). Auto-Owners also provided a “Coverage C” Personal-Property limit of \$3,000. (*Id.*) Auto-Owners’ \$4,962.81 premium was underwritten based (in part) on these values. (*See id.*) It is not disputed that Second Chance paid its premium.

On November 12, 2008, the Kings Point Road property burned as the result of a fire that was likely caused by a defective air exchanger in the basement. (RA-57; RA-146.). The fire spread within the building’s walls, consuming them and causing sections of floor and ceiling to collapse. (RA-145). Floor joists, wall beams, sheet materials, doors, and windows were consumed, charred, shrunken, warped, delaminated, heat-damaged or smoke-damaged by the blaze, and further damaged by the water used to

extinguish it. (RA-57; RA-66-68; RA-145). The state fire marshal noted the need to “frame the area for safety reasons, as second level walls above the utility room did not have any support.” (RA-146). A Wolf commercial-quality cooking range with a value exceeding the personal-property policy limit of \$3,000 was destroyed in the blaze. (See Figure 68, RA-109).

Auto-Owners’ policy included a Minnesota Amendatory Endorsement, which provided that Auto-Owners would pay undisputed amounts within five business days of receiving the insured’s proof of loss:

OUR PAYMENT OF LOSS

We will adjust any loss with **you**, and pay **you** unless another payee is named in the policy. We will pay within five business days after we receive **your** proof of loss and the amount of loss is finally determined by an agreement between **you** and **us**, a court judgment or an appraisal award.

(App-23). The Minnesota Amendatory Endorsement also amended Auto-Owners’ appraisal provision to emphasize that that provision did not apply in the event of a “total loss”:

APPRAISAL

If **you** and **we** fail to agree on the **actual cash value** or amount of loss, *except in the case of total loss to the dwelling insured under Coverage A*, either party may make a written demand for appraisal. * * *

The appraisers shall then appraise the loss, stating separately the **actual cash value** and loss to each item. * * *

(App-23, 16 (italics added)). Finally, the policy’s Minnesota Amendatory Endorsement made the deductible inapplicable in the event of a “total loss.” (App-23).

Proofs of loss and evidence of total loss

On January 9, 2009, Second Chance filed a proof of loss with Auto-Owners stating that the property was a “total loss,” and that Second Chance therefore sought payment of the policy limits plus the cost of demolition, and lost rent at \$5,000 per month. (See RA-160.). On January 12, 2009, Auto-Owners’ expert, EFI Global, gave Claims Representative Cheryl Kintop a written report on the loss. (RA-148.).

EFI explained that fire destroys flammable building materials by consuming them and by charring them, which changes their physical properties. (RA-152.). EFI found “considerable char” in the floor joists at Kings Point Road, stating that: “Essentially, the southern three-fourths of the floor joists on the main level of this dwelling were charred by the fire”; “The southern two-thirds or so of the floor joists for the third level (second story) were charred by the fire”; and “The east and south exterior walls in the southeast room on the main level of this dwelling were partially charred by the fire.” (RA-153.). EFI assumed that the roof was constructed of prefabricated wooden I-joists and plywood sheathing,” and that the roof was not damaged in the fire, yet its report admitted that the roof’s actual framing was “unknown and not seen.” (RA-150). EFI also assumed that no damage occurred to stringers/girders, but again noted that these elements were “Unknown and not seen — none of the stringer lines were uncovered due to the fire.” (*Id.*). EFI’s report to Auto-Owners likewise noted that removing interior walls and floor joists required extensive temporary framing to shore up each level, from fourth floor and roof assemblies down to first and second level floor joists:

To be able to remove these interior walls and floor joists, it will be required to shore up (shoring frames) the framing of the fourth level floor/roof assemblies of this dwelling. This action will have to be done prior to any

demolition of any of these elevated floors and interior walls of this dwelling.

EFI recommends that the walls on each level of this dwelling need to be temporarily braced. That is, all of the exterior walls need to be braced at the elevation of the first and second level floor joists.

(RA-154). The EFI report highlights the extent of the necessary framing effort, which would have included bracing the basement walls when the earth supporting them was removed, and extended to the upper levels of the structure:

[T]he first level (basement) walls are especially critical because three of the four wall elevations are resisting earth loads and the load is continually present until the earth is removed *off* these walls. Thus the tops of the basement walls need to be braced for this condition or at the elevation of the second level floor assembly.

The top of the second level wall assembly needs to be braced since a hinge exists in the wall framing when the floor joists are removed. Thus, another level of bracing needs to occur at the level of the third level floor framing.

(*Id.*). EFI opined that “All buildings, no matter what condition they are in, are salvageable, and thus this residential structure is salvageable.” (*Id.*). EFI also opined that the shell, exterior walls, roof, and floor assembly were “able to be reused.” (*Id.*). But EFI nonetheless concluded that, due to economic concerns, the “best option” would be to demolish the building:

Thus, EFI has concluded that the best option would simply be to demolish the entire wooden framing of this dwelling. That is, all of the wooden framing of this dwelling needs to be demolished from the top down. It appears to EFI that it would not be economical to reuse the exterior shell of this dwelling due to the requirement of shoring up the upper level roof and floor framing and the need to brace exterior walls of this dwelling.

(RA-154-155.).

On January 22, 2009, Lindstrom Cleaning and Construction, d.b.a. Lindstrom Restoration, produced an “Xactimate” report generating materials and labor costs to perform work on a home with dimensions comparable to the Kings Point Road property. (RA-161.). Auto-Owners admitted below that it received this report by February 9, 2009. (RA-46.). Lindstrom’s calculation of \$1,654,841.74 expressly excluded any work on the roof, stating that “any roofing repair within the estimate has been left open.” (RA-190.). Lindstrom’s report also excluded fees for a licensed structural engineer, which the insurer’s expert “highly recommend[ed]” should any attempt to rebuild the property be undertaken. (*See* RA-161-192; RA-155.).

On March 9th, Auto-Owners finally responded to Second Chance’s January 9th proof of loss, stating that Auto-Owners was “returning” the proof of loss because it did not “set out the Actual Cash Value of the damages nor does it provide a written estimate of repair to support your claim.” (RA-160.). The March 9th letter did not acknowledge Second Chance’s claim that the property was a total loss. (*See id.*). Auto-Owners did not explain how its “written estimate of repair” requirement squared with Minnesota’s Standard Fire Policy, which explicitly states that insureds need not state the actual cash value in the event of a “total loss.” (*See id.*); *compare* Minn. Stat. § 65A.01, Subd. 3 (2010). (“In case of any loss under this policy, the insured shall give immediate written notice to this company of any loss, protect the property from further damage, and a statement in writing, signed and sworn to by the insured, shall within 60 days be rendered to the company, setting forth the value of the property insured, *except in case of total loss on buildings the value of said buildings need not be stated * * **.” (emphasis added)).

Auto-Owners' March 9, 2009, letter further stated that any future proof of loss would be "considered an entirely new document and will be accepted or rejected in connection with the matters and items contained therein." (*Id.*)

On March 20, 2009, Auto-Owners paid Alliance Bank's mortgage amount of \$1,038,677. (RA-51.). On July 27, 2009, Second Chance filed a second proof of loss, again describing the property as a "total loss." (RA-57). Second Chance's second proof of loss, totaling 80 pages, included: a two-page letter from counsel outlining why the property was considered a "total loss"; a completed "Personal Property Inventory"; a forensic engineering report by Mark Blazevic of Encompass, Inc.; a Draft Field Report for Initial Fire Loss Investigation by Bryan Oakley and Thomas Irmeter of Forensic Building Science, including 101 photos of the loss; a demolition estimate from Veit, Inc.; and a replacement estimate from AAA Exteriors that offered to do the work necessary to tear down and rebuild the property for \$2,127,000, which was more than the policy's limits. (*Id.*)

The Encompass Engineering report, included with Second Chance's July 27th proof of loss, noted that "joists installed at the first and second floors exhibited severe fire damage to web members; at numerous locations webs are either severely charred or are completely burnt through." (RA-66.). Encompass found waviness and sagging in first and second level floor joists away from significantly charred framing, and concluded that the joists were likely subject to heat migration through the floor diaphragm, which softens the adhesives in oriented strand board and permanently deforms it. (*Id.*) Encompass observed that a majority of the damage to wall framing affected a central

load-bearing wall supporting the first floor, second floor and roof joists. (RA-67.). Encompass also noted that a majority of windows in the basement and first floors were significantly damaged from charring and excessive water exposure. (*Id.*). Encompass reported that second floor windows were darkened from smoke and had peeling finishes, and other windows had failed insulated glass seals. (*Id.*). Encompass also found water seeping into the interior through the roof membrane at various locations. (RA-66.). The mineral/fiberboard below the roofing was observed by Encompass to be soft and soggy. (*Id.*). Finally, Encompass cautioned that “The economic feasibility of repairing the structure as compared to that of total replacement should be reviewed prior to onset of any remedial work.” (RA-68.).

Forensic Building Science examined the premises on June 9th, June 16th, and July 7th, and did water-intrusion analyses. (RA-71.). FBS observed cracking and mold growth in some visible areas of the basement’s concrete masonry. (RA-72.). In several locations, foundation blocks tested for moisture with a “Delmhorst meter set,” registered a “wet” reading. (*Id.*). FBS observed that the intersection of the slab floor and the outer foundation was not sealed, which may have allowed the water used to douse the fire to collect under the slab, where it could displace soil and slab support after numerous freeze-thaw cycles. (RA-73.). FBS further observed damage to the roof, resulting from buckling of the roof joists due to heat from the fire. (*Id.*). Further roof damage observed by FBS included wet sheathing and wet underlayment in the roof. (*Id.*). FBS explained that the roof and floor system was comprised of engineered “I” joists, which bear on the exterior walls and on an interior center bearing wall. (RA-74.). The exterior walls, FBS

noted, utilize platform or “California style” construction, where each wall section and floor assembly is built independent of the section above but relies on the completed wall and floor system for diaphragm and shear strength. (*Id.*) Repairing such a system in sections is complicated and costly, requiring a temporary support system the installation and removal of which would double the job’s framing costs:

This type of design, while easier to construct, is more complicated and costly to repair by sections, especially if lower sections are damaged. . . . In effect, to replace a structural component such as the first floor bearing walls, the contractor would have to build a temporary system to keep all structural systems above in place while the 1st floor bearing wall is replaced. After all the structural components are completed, the temporary shoring system would have to be removed. This would come close to doubling the framing costs of starting over.

(*Id.*) The basement walls also were subject to water and heat damage as a result of the fire and the water used to douse it, and FBS opined that rebuilding on the existing block foundation was “not reasonably possible.” (RA-73.).

Claims representative Kintop again “returned” Second Chance’s July 27th proof of loss on August 13, 2009, again claiming that it did not comply with the policy provisions because it allegedly failed to “set out the Actual Cash Value of the damages.” (RA-193). As before, Auto-Owners’ August 13th letter did not explain how such a requirement squared with Minnesota’s Standard Fire Policy, which explicitly states that insureds need not state the actual cash value in the event of a “total loss.” (*See Id.*); *compare* Minn. Stat. § 65A.01, Subd. 3 (2010). Auto-Owners’ August 13th letter also asserted a new requirement — one not contained in its policy — that Second Chance’s “written estimate of repair” had to be “supported by a trade break down of rebuilding for your claim.”

(RA-193). Auto-Owners' August 13th letter did not acknowledge any of Second Chance's evidence showing that the property was a "total loss." (*See id.*).

On September 3, 2009, Auto-Owners sent Second Chance another letter, claiming that Auto-Owners could wait 30 business days before paying the undisputed amount of Second Chance's claim. (RA-194). The letter did not explain why the payment period was 30 days rather than the 5 days set forth in the policy. (*Compare id. with App-23*). Auto-Owners' September 3rd letter acknowledged that Minnesota law required that, if it was "unable" to "accept or deny" Second Chance's claim, Auto-Owners must advise why. (RA-194). Auto-Owners stated that its reason for non-payment was that it was "awaiting the following items previously requested: Proof of Loss Form." (*Id.*). The September 3, 2009 letter did not acknowledge Second Chance's two prior proofs of loss, nor that Second Chance was seeking to recover for a "total loss." (*See id.*).

On October 8, 2009, Second Chance's counsel wrote to Auto-Owners to challenge Auto-Owners' purported "rejections" of Second Chance's proofs of loss, and its inexcusable delay in failing to *at least* tender the undisputed amount, i.e., the difference between the Lindstrom report and the amount paid to Alliance Bank, or \$616,697.74. (RA-157). Second Chance demanded that Auto-Owners pay the full amount owed — the policy limits minus the amount paid to Alliance Bank, or \$1,000,500 — within 30 days, noting that if forced to litigate, it would seek extra-contractual damages. (RA-157-159). In response to Second Chance's demand, Auto-Owners attempted to negotiate a full release in exchange for payment of the undisputed amount minus the deductible:

We are willing to offer damages to your client of repair \$1,654,841.74 plus personal property loss \$3,000.00 plus board up expenses of \$5,484.50 for a total of \$1,657,841.74 minus the \$2,500.00 policy deductible and the amount paid to the mortgage carrier of \$1,038,644.00 leaving a net payable of \$616,697.74

We enclose a Proof of Loss in this amount and again reiterate that a proper proof of loss has not been filed as of this date.

(RA-195). It did not acknowledge that under MN law, the deductible was inapplicable to “total loss.” (*See Id.*; App-23); *see* Minn. Stat. § 65A.01 Subd. 5 (2010).

Second Chance rejected Auto-Owners’ “offer,” and Auto-Owners finally tendered the undisputed amount. (RA-53.)

Auto-Owners’ demands for appraisal

On October 29, 2009, Auto-Owners’ counsel wrote to Second Chance to state that Auto-Owners was demanding appraisal. (App-43). Auto-Owners’ counsel did not explain how appraisal was appropriate, given that Second Chance’s claim involved a “total loss.” (*See id.*).

On November 19, 2009, Second Chance disputed whether appraisal was appropriate, but it appointed an appraiser in order to preserve its right to do so. (App-44). On February 24, 2010, one day before the scheduled appraisal, Auto-Owners shifted positions and advised Second Chance that Auto-Owners would not proceed with the appraisal that Auto-Owners had itself initiated. (RA-200-201; RA-33). Having already incurred expenses to prepare for the appraisal, Second Chance stated that it intended to proceed as planned. (*See* RA-201).

On the date scheduled for appraisal, February 25, 2010, Auto-Owners' counsel appeared and joined the scheduled site walk-through, but did not participate in the appraisal. (RA-56).²

On March 12, 2009, Auto-Owners filed its complaint, asking the district court to compel Second Chance to submit to appraisal. (RA-04). Auto-Owners conceded that it had no coverage or liability defenses. (RA-34.). Second Chance filed an amended answer asserting a counterclaim for breach of contract. (RA-14.)

On November 30, 2010, Auto-Owners filed a motion to compel appraisal. (RA-29). In response, Second Chance filed a motion for partial summary judgment declaring the Kings Point Road property a total loss, and a motion to amend its pleading to seek taxable costs under Minn. Stat. § 604.18 and prejudgment interest under Minn. Stat. § 60A.0811. (RA-39).

On April 11, 2011, the district court issued an order denying Auto-Owners' motion to compel appraisal. (RA-237). The court's order also denied Second Chance's motion for partial summary judgment, but granted its motion to amend its counterclaim to add a claim for taxable costs for bad faith under Minn. Stat. § 604.18. (*Id.*) This appeal follows.

² Second Chance has since demolished and removed the charred remains of the structure at 3406 Kings Point Road.

ARGUMENT

I. Auto-Owners' argument is anathema to the plain language and the purpose of Minn. Stat. § 65A.01, Subd. 3, which mandates that fire policies be "valued policies" and excepts "total loss" issues from appraisal.

Auto-Owners acknowledges that Minn. Stat. § 65A.01 is a "valued policy" law, that such statutes are remedial, and that the statute must therefore be construed in favor of its remedial purpose. (*See* Appellant's Brief, 7, 9). But then Auto-Owners' turns century-old law on its head because it willfully ignores the purpose of "valued policy" laws. Appraisal of "total loss" issues is anathema to that purpose.

"Valued policy" laws were designed to eliminate post-claims underwriting:

The so-called 'valued policy law,' section 203.21 of the [Wisconsin] Statutes is a legislative expression of the public opinion against the practice by fire insurance companies of writing excessive amounts of coverage, collecting high premiums, and then reducing the amounts of recoveries to a minimum when losses occur.

Winfield V. Alexander, *Insurance: The Wisconsin "Valued Policy" Law*, 10 Wis. L. Rev. 248, 248 (1934-35) (included in Respondent's Appendix beginning at RA-208 because article is old and difficult to find). At the time that such statutes were first passed in the late 1800s, they were considered "drastic," but were "justified by a very exaggerated condition of unfair practice on the part of insurers * * *." *Id.*; *see also Curo v. Citizens Fund Mut. Fire Ins. Co.*, 186 Minn. 225, 226, 242 N.W. 713, 713 (1932) (stating Minnesota's "'valued policy statute' * * * first came into our law as a part of L. 1895, P. 392, c. 175, § 25."). It is of course no accident that such laws were passed (and that most of the caselaw developing them was decided) during economic downturns,

because that is when insurers tend to reap the greatest windfalls from avoiding full-limits payments.

Appraisal provisions were already commonplace at that time, and, in fact, insurers regularly used them to avoid and delay paying policy limits on claims. *See, e.g., Gasser v. Sun Fire Office*, 42 Minn. 315, 316-17, 44 N.W. 252, 253 (1890) (Construing “open” policy for personal property and noting, “The contention of the plaintiff is that * * * the arbitration clause, by its terms, cannot apply to cases where personal property covered by the policy is wholly destroyed.”); *Northwestern Mut. Life Ins. Co. v. Rochester German Ins. Co. of Rochester, N.Y.*, 85 Minn. 48, 50, 88 N.W. 265, 266 (1901) (“[I]t was claimed by respondent that within the terms of the policy there was a total loss. This appellant denied * * * and demanded a submission of the amount of the loss to appraisers, according to the provisions of the policies. Respondent refused to comply with the demand for arbitration, and brought this action to recover the entire amount covered by the policies.”).

So when states, including Minnesota, began to enact standard fire policies, many of them specifically excepted “total loss” issues from otherwise allowable appraisal provisions. *See, e.g.,* 1923 Minn. Laws 580 (“In case of loss, except in case of total loss on buildings, under this policy and a failure of the parties to agree as to the amount of the loss, it is mutually agreed that the amount of such loss shall, as above provided, be ascertained by two competent, disinterested and impartial appraisers * * *.”). In fact, the New York dissenting opinion on which Auto-Owners so heavily relies complains that the majority failed to consider that New York had no similar statutory provision. *Lee v.*

Hamilton Fire Ins. Co., 167 N.E. 426, 427 (N.Y. 1929) (“All those decisions are based upon statutes the operation of which is of course limited to their respective States.”).

But even states (like New York) that did *not* have such specific statutory provisions nonetheless held that “total loss” issues were not appraisable for what should be obvious reasons:

It seems clear that the appraisal was to cover only ‘loss or damage’ less than a total loss. If the insured under such a policy claims a total loss and the insurer a partial loss, and the latter insists on an appraisal, the granting of the appraisal by the insured cannot estop him from litigating the question of a total loss. If it be decided that the loss was not total, then the appraisal stands, but if it be decided that the loss was total, then under the valued policy the plaintiff would be entitled to receive the amount of the policy. *Any other construction disregards the fact that the policy is a valued policy and treats it as an open policy.*

Id. at 427 (emphasis added). Commentators in Minnesota have noted that appraisal clauses are inconsistent with “valued policy” laws. *Cf.* Case Notes, XIV Minn. L. Rev., 301-02 (1930) (“A stipulation to arbitrate contained in such a valued policy, even though made a condition precedent to recovery, is generally considered inoperative in case of total loss.”) (Beginning at RA-250). And so have commentators in other jurisdictions:

C. Policy Provisions Inconsistent with the Statute

As previously stated, the provisions of the policy are controlled by section 203.21 where the two are in conflict. This is so even though the policy be statutory and passed subsequent to the valued policy law. There are several such provisions.

* * *

(3) Arbitration

Likewise, provisions for arbitration as to the amount of indemnity and for the appraisal of the property destroyed to determine the amount of loss are

void as being in conflict with the statute. *This result is obvious, since the amount of recovery and the value of the property destroyed are fixed at the face value of the policy, and there is no need for arbitration or appraisal.*

Alexander, 10 Wis. L. Rev. at 251-53 (Emphasis added; beginning at RA-208).

Minnesota's Standard Fire Policy is thus typical in that it specifically states that "total loss" issues are not appraisable. Minn. Stat. § 65A.01, Subd. 3 (2010). It does so because (like other coverage issues) such issues necessarily entail resolving a threshold statutory or contractual-interpretation problem, namely, "what does it mean for a building to be a 'total loss' within the statute's (and policy's) meaning?" *Cf., Quade v. Secura Ins.*, 792 N.W.2d 478, 480-81 (Minn. App. 2011) (holding that coverage issues are not appraisable). This basic legal issue is not something that individual appraisers (many of whom are not attorneys) are capable of deciding. This is because courts have defined the phrase "total loss" such that it has "acquired a legal significance which, in some cases, seems to vary from the literal interpretation which would be given by a layman." Alexander, 10 Wis. L. Rev. at 249. A lay appraiser might be persuaded to (for example) follow some test other than Minnesota's — called the "restoration to use" test — and thereby deprive the insured of his contractual right under the policy and Minnesota law. *See, e.g., Northwestern*, 85 Minn. 48, 50, 88 N.W. 265, 266 (1901) (asking whether prudent insured would restore under circumstances). So "total loss" questions *are* coverage issues requiring determination of a threshold legal question under a valued policy.

Appraisers are distinct from arbitrators in that they are not permitted to decide coverage issues, (which would include "total loss" issues), as even the appraisers in this

case recognized. (RA-203-204; RA-242.); *see also Quade*, 792 N.W.2d at 482. Rather, their inquiries are limited to “fact question[s] free of confusion with regard to legal issues.” *See Quade*, 792 N.W.2d at 482. And, in any event, it would be grossly unfair for courts to defer to appraisers’ judgment on that question, which is what would happen if “total loss” questions were subject to appraisal, because appraisers’ “value” determinations are reviewable on only a limited basis. *See id.* at 483.

So Auto-Owners has not hit on some novel, heretofore-never-considered theory here. As its own authority demonstrates, its arguments have been considered and soundly rejected by courts all over the country. Auto-Owners does not and cannot offer a single case that has accepted its position. In fact, the only authority that it claims supports it is an Eighth Circuit decision from 1903, applying Missouri law to an open (i.e., not a valued) policy. *See generally, Williamson v. Liverpool & London & Globe Ins. Co.*, 122 F. 59 (8th Cir. 1903). The policy thus explicitly authorized appraisers to determine the “actual cash value” of the building at the time of the total loss:

It is further expressly understood and agreed that, in determining the sound value and the loss or damage upon the property hereinbefore mentioned, the said appraisers are to make an estimate of the total cash cost of replacing or repairing the same or the actual cash value thereof at and immediately preceding the time of the fire, and in case of depreciation of the property from use, age, condition, location, or otherwise a proper deduction shall be made therefor.

Id. at 61. *Williamson* does not support Auto-Owners’ position here.

Auto-Owners surely knows by now that its argument is meritless; and if it doesn’t, it should. It has no excuse for continuing this battle, the only outcome of which can be to delay payment of Second Chance’s claim. Insureds should not have to incur tens of

thousands of dollars in attorneys' fees in order to educate insurers and their coverage counsel about a fundamental precept of insurance law that has been in place for a century. Nor should they have to wait *years* (this loss occurred three years ago!) to resolve disputes while insurers demand to have courts revisit settled doctrine.

Auto-Owners' position is in bad faith. It is frivolous. It has literally zero support in the law. And it has directly harmed Second Chance's interests by forcing Second Chance to incur unnecessary litigation expenses (not to mention lost opportunity costs due to delayed recovery), as well as wasted this court's resources. Because delay equals gain for insurers, other insurers are sure to jump on the bandwagon unless this court soundly rejects Auto-Owners' arguments here. Second Chance urges this court to do so.

II. By their plain language, Minnesota's Standard Fire Insurance Policy and Auto-Owners' policy contemplate that courts, not appraisers, will decide whether a property has suffered a "total loss."

Minnesota's Standard Fire Insurance Policy is dictated by Minn. Stat. Ch. 65A, and it unambiguously requires that insurers pay the full policy limits in the event of a "total loss." *See generally*, Minn. Stat. § 65A.01 (2010). It allows for appraisals to determine "actual cash value," but the appraisal clause contains an explicit exception for "total loss." *Id.* Auto-Owners' own appraisal clause is consistent with the statutory requirement, in that it also clearly excepts "total loss" situations from appraisal:

APPRAISAL

If **you** and **we** fail to agree on the **actual cash value** or amount of loss, *except in the case of total loss to the dwelling insured under Coverage A*, either party may make a written demand for appraisal. * * *

The appraisers shall then appraise the loss, stating separately the **actual cash value** and loss to each item. * * *

(App-16 (italics added)). “Total loss” therefore presents a statutory and policy-interpretation issue that must be decided by *courts*, not appraisers.

As commentators have repeatedly observed, court determination of “total loss” is the only procedure that is consistent with the statutory scheme as a whole. Alexander, 10 Wis. L. Rev. at 251-53 (Beginning at RA-208); Case Notes, XIV Minn. L. Rev., 301-02 (1930) (“A stipulation to arbitrate contained in such a valued policy, even though made a condition precedent to recovery, is generally considered inoperative in case of total loss.”) (Beginning at RA-250). For example, Minn. Stat. § 65A.01, Subd. 5 expressly prohibits any “provision” that permits paying less than policy limits when there has been a “total loss.”

Subd. 5. Provision prohibited, total loss; limiting amount to be paid.
No provision shall be attached to or included in such policy limiting the amount to be paid in case of total loss on buildings by fire, lightning or other hazard to less than the amount of insurance on the same.

Minn. Stat. § 65A.01, Subd. 5 (2010). One need only imagine a hypothetical scenario to understand why this provision cannot tolerate submission of a “total loss” issue to appraisers. Suppose that in a particular case, a court applying Minnesota law would conclude that a particular loss is a “total loss,” but a panel of appraisers awards less than the policy limits based on the appraisers’ own theory about what “total loss” means. The policy’s appraisal provision would then be a “provision” that violated Minn. Stat. § 65A.01, Subd. 5, and would be void under Minn. Stat § 65A.01, Subd. 1 (2010) (“No policy or contract of fire insurance shall be made, issued or delivered by any insurers * *

* on any property in this state, unless it shall provide the specified coverage and conform as to all provisions, stipulations, and conditions, with such form of policy * * *.”).

Practically speaking, appraisers can never have the last word regarding “total loss.”

The plain language of the statutory appraisal clause supports this interpretation, insofar as explicitly excepts “total loss”:

In case the insured and this company, *except in case of total loss on buildings*, shall fail to agree as to the actual cash value or the amount of loss, then, on the written demand of either, each shall select a competent and disinterested appraiser and notify the other of the appraiser selected within 20 days of such demand.

Minn. Stat. 65A.01, Subd. 3 (2010) (emphasis added). Auto-Owners claims that this “total loss” exception only applies when the parties *agree* that there has been a total loss. (Appellant’s Brief, 7-8). This argument is nonsensical. If the parties agree that there has been a total loss, then there is no need for an appraisal of “actual value,” because “actual value” is irrelevant. So the appraisal provision would *never* come into play in that event, and the exception would be completely superfluous. Minnesota law does not condone a statutory interpretation that renders a provision superfluous. *See* Minn. Stat. § 645.17 (2010) (in ascertaining legislative intent, courts should presume legislature intends entire statute to be effective and certain).

The statute also expressly limits appraisers to deciding *actual value*, not “scope,” as Auto-Owners argues. *Id.* (“The appraisers shall then appraise the loss, stating separately actual value and loss to each item * * *.”). Again, Auto-Owners’ policy is in accord. (App-16). But “actual value” has no meaning if there has been a “total loss”

under the statute; this is why insureds are relieved of having to state “actual value” in proofs of loss in which they claim “total loss”:

In case of any loss under this policy the insured shall give immediate written notice to this company of any loss, protect the property from further damage, and a statement in writing, signed and sworn to by the insured, shall within 60 days be rendered to the company, setting forth the value of the property insured, *except in case of total loss on buildings the value of said buildings need not be stated * * **.

Minn. Stat. § 65A.01, Subd. 3 (2010) (emphasis added). Appraisers cannot assess “actual value” in the event of a “total loss.”

Both by its plain language, and when read as a whole, it is clear that “total loss” is a question for a court, because it ultimately involves a threshold policy and statutory-interpretation question about what “total loss” means. *E.g., Johnson v. Mutual Service Casualty Ins. Co.*, 732 N.W.2d 340, 346 (Minn. App. 2007) (“It is well settled that appraisal does not determine liability under a policy. Liability depends on a judicial determination.”) *rev. denied* (Minn., Aug. 21, 2007). These are quintessentially questions for courts, not appraisers. *See, e.g., Northwestern Mut. Life Ins. Co. v. Rochester German Ins. Co.*, 85 Minn. 48, 88 N.W. 265 (1901) (court decides “total loss” question); *Johnson v. Mut. Serv. Cas. Ins. Co.*, 732 N.W.2d 340, 346 (Minn. App.) (appraisers do not determine liability) *rev. denied* (Minn., Aug. 21, 2007); *Johnson v. Madelia Lake Crystal Mut. Ins. Co.*, 2004 WL 61057, *4-6 (Minn. App.) (enforcing “total loss” on summary judgment) *rev. denied* (Minn., March 16, 2004) (RA-262); *Dri-Kleen, Inc. v. Western Nat’l Mut. Ins. Group*, 2002 WL 1611507, *2 ([W]hether a total loss has occurred is generally a question of fact for a jury to decide.”) (RA-257). Auto-Owners

cannot point to a single decision that delegates the “total loss” question to appraisers. Certainly, none of its cited authority supports it.

III. Auto-Owners’ cited authority supports Second Chance’s position, not Auto-Owners’.

As noted above, the primary authority on which Auto-Owners relies supports Second Chance’s position, not Auto-Owners.

Moreover, Auto-Owners’ brief to this court does not even discuss critical (and unfavorable) Minnesota Supreme Court authority of which Auto-Owners is well aware. Below, Auto-Owners argued that *Northwestern Mut. Life Ins. Co. v. Rochester German Ins. Co.* compelled the district court to order Second Chance to submit the “total loss” issue to appraisal. (RA-35 (citing *Northwestern Mut. Life Ins. Co. v. Rochester German Ins. Co.*, 85 Minn. 48, 88 N.W. 265 (1901))). The gist of Auto-Owners’ argument was that, in *Northwestern*, the Minnesota Supreme Court concluded that “total loss” was a fact issue, ergo, Second Chance should be compelled to submit the issue to appraisal:

As defined by the Court, a total loss is a factual determination of the scope of the loss, i.e., the degree of the damage. Any dispute, therefore, as to the existence of a total loss is nothing more than a dispute over the scope of the loss. As stated below, it is the duty of appraisal boards to decide disputes with respect to the scope of the loss.

(RA-35). Somehow Auto-Owners managed to overlook the fact that, in *Northwestern*, the Minnesota Supreme Court concluded that, on those facts, “total loss” was a fact issue *for the jury* (as opposed to a question of law for the court), and that the court therefore remanded the case *for a new trial*, not appraisal. *Northwestern*, 85 Minn. at 63, 88 N.W. at 271 (“The trial court did not submit the case to the jury upon this theory of the law. *

* * For this error a new trial must be granted.”). And this was true, despite the fact that the policy at issue contained a substantially similar appraisal provision to Auto-Owners. *Id.* at 50, 88 N.W. at 266. *Northwestern* supported Second Chance, not Auto-Owners, as the district court concluded. (RA-242-43). Auto-Owners does not discuss this controlling adverse authority here.

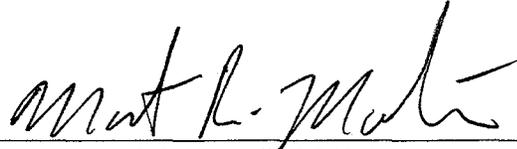
“Total loss” may present fact issues in certain cases, or it may be decided as a matter of law in others. *See id.* at 58, 88 N.W. at 269 (discussing case from another jurisdiction and stating, “However, tested by the facts of the case, it appeared, as a matter of law, that the destruction of the building as such was complete.”). If the undisputed facts demonstrate that the legal standard for “total loss” has been met or cannot be met, then one or another of the parties might be entitled to judgment as a matter of law. But regardless of whether “total loss” is an issue of fact or law in a particular case, it is nonetheless a question for *courts*, not appraisers.

Auto-Owners is trying to take away the consumer protection afforded by Minnesota’s Standard Fire Insurance Policy. Its position is not supported by the statute, its own policy, caselaw, or public policy, and was therefore correctly rejected by the district court.

CONCLUSION

Auto-Owners’ position is contradicted by Minnesota Statutes, its own policy language, abundant caselaw, and public policy. It does not have a single source of authority to support it. In fact, everything that it cites supports Second Chance’s position. The district court’s judgment should be affirmed.

Respectfully submitted,



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CERTIFICATION OF BRIEF LENGTH

I hereby certify that this brief conforms to the requirements of Minn. R. Civ. App. P. 132.01, subds. 1 and 3, for a brief produced with a proportional font. The length of this brief is 7,240 words. This brief was prepared using Microsoft Office Word 2007.

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