STATE OF MINNESOTA
IN COURT OF APPEALS
A12-0182
A12-0214

Northern National Bank, n/k/a Frandsen Bank & Trust,
Appellant (A12-182),
Respondent (A12-214),

vs.

North Star Mutual Insurance Company,
Respondent (A12-182),
Appellant (A12-214),

Brian Hanson, et al.,
Respondents (A12-182),
Defendants (A12-214).

Filed September 17, 2012
Affirmed in part and reversed in part
Rodenberg, Judge

Cass County District Court
File Nos. 11CV102113; 11CV102436

Anthony T. Smith, Alexander M. Jadin, Hellmuth & Johnson, PLLC, Edina, Minnesota (for appellant Northern National Bank)

Marcus J. Christianson, Jennifer Lurken, Maschka, Riedy & Ries, Mankato, Minnesota (for respondent North Star Mutual)

John E. Valen, Walker, Minnesota (for respondents Hanson, et al.)

Considered and decided by Bjorkman, Presiding Judge; Johnson, Chief Judge; and Rodenberg, Judge.

U N P U B L I S H E D O P I N I O N

RODENBERG, Judge

Appellant, an insured mortgagee claiming under a homeowner's insurance policy issued by respondent, challenges a district court order confirming an appraisal award, arguing that the district court erred by (1) concluding that the policy provision for payment of the actual cash value of a fire loss is determined as of the date of the loss and (2) concluding that the claim was resolved in the appraisal proceedings and thus declining to award attorney fees and costs for denial of benefits without a reasonable basis under Minn. Stat. § 604.18 (2010). Respondent, by notice of related appeal, argues that the district court erred in finding (1) that it did not have a reasonable basis for denying benefits and (2) that appellant was the prevailing party. We affirm in part and reverse in part.

FACTS

Brian and Jayne Hanson owned a home in Walker, Minnesota, which was damaged by fire on January 10, 2008. Although named as parties, the Hansons did not participate in the litigation below or in this appeal.

Appellant Northern National Bank n/k/a Frandsen Bank & Trust was the mortgagee on the home at the time of the loss. Respondent North Star Mutual Insurance Company insured the home against, among other risks, fire damage.

The Hansons contacted respondent after the fire and reported the fire loss. Respondent concluded after an investigation that the fire loss had been sustained as a result of a fire intentionally set by the Hansons. It therefore denied their claim.[1]

In an initial report, dated August 12, 2008, respondent concluded that the replacement cost value (RCV) of the loss was $116,308.74 and the actual cash value (ACV) of the loss was $96,577.61. On October 9, 2008, the initial report was amended and the RCV of the loss was determined to be $142, 644.22 and the ACV of the loss was determined to be $118,847.40.

Appellant arranged for a different company to prepare an estimate to repair the property. The estimate obtained by appellant was dated October 6, 2008, and indicated an RCV of $228,112.72. Appellant did not promptly notify respondent of this estimate.

Respondent tendered a payment to appellant as named mortgagee in the amount of $118,847.40 based upon the ACV at the time of the loss.[2]

Almost a year after obtaining the independent estimate, on August 24, 2009, appellant sent respondent a letter stating that appellant was involved in foreclosure proceedings concerning the property. The letter asked whether respondent "could

[1] The cause of the fire was not litigated in this case, and the record before this court does not address respondent's determination.

[2] The date the money was tendered and whether the tendered funds were accepted do not appear explicitly in the record. However, examination of the file leads us to conclude that the bank accepted the payment at some point prior to January 5, 2010. The complaint, signed on that date, alleged that respondent had "tendered an insurance payment to [appellant] in the amount of $118,847.40" at an unspecified time. The complaint sought recovery of amounts in excess of the amount already tendered, and asserted that additional amounts above $118,847.40 were properly payable under the insurance policy.

confirm that the issue of any additional money to be paid to the bank would be put on hold until the bank c[ould] regain possession of the property and examine it."

On December 9, 2009, appellant sent respondent a letter requesting an appraisal hearing to value the loss, and advising respondent that "there is a six-month period of redemption from and after the order to be entered confirming today's [foreclosure] sale that must expire before the mortgagee will have possession of the property and access to it for purposes of appraising this loss." Respondent denied the request in a letter dated December 22, 2009, noting that appellant was not a named insured under the policy and concluding that the appraisal procedure was therefore not available to it.

Appellant sued by complaint dated January 5, 2010, seeking a declaratory judgment that appellant was entitled to an appraisal hearing, and also seeking damages for breach of contract. Respondent served appellant with its answer on February 3, 2010. Appellant did not file the complaint in district court until September 27, 2010.

On November 1, 2010, the district court, upon motion by appellant, ordered the parties into appraisal proceedings to determine the value of the loss.[3] Before the appraisal hearing, appellant sold the home "as is" to a third party.

Because the parties could not agree on whether respondent was required to pay the ACV or the RCV of the loss, and were unable to agree whether the amount properly payable under the policy should be determined as of the date of the loss or the date of the

[3] Appellant appears to have first disclosed the existence of its own appraisal of the loss in the complaint.

appraisal hearing, the parties asked the appraisal panel to determine both the ACV and RCV for both dates.

On January 17, 2011, the appraisal panel determined that the ACV at the time of loss was $147,931.06 and the RCV at the time of loss was $176,108.40. The appraisal panel determined that the ACV at the time of the hearing was $178,996.59 and the RCV at the time of the hearing was $213,091.16.

On January 24, 2011, appellant sent respondent a letter requesting payment in the amount of $178,996.59. On February 16, 2011, appellant filed a motion to confirm the appraisal award, which was accompanied by a memorandum arguing that respondent was required to pay $213,091.16.

On March 7, 2011, appellant filed another motion, seeking to amend the complaint to include a claim for taxation of costs under Minn. Stat. § 604.18.

On March 21, 2011, respondent deposited a check for $29,083.65 with the Cass County Administrator's Office pursuant to Minn. R. Civ. P. 67.01. That amount represented the difference between the amount originally tendered and the ACV at the time of the loss as determined by the appraisal panel. On April 21, 2011, the district court granted appellant's motion to confirm the appraisal award in the amount of $147,931.06 (the ACV at the time of the loss), and awarded appellant costs and disbursements as a prevailing party. The district court stated that it determined appellant was the prevailing party "*sua sponte* without granting [appellant]'s motion to amend the Complaint because costs and disbursements were included in the prayer for relief."

On June 3, 2011, appellant filed a notice and application for taxation of costs and disbursements, which requested $43,273.33 in Minn. Stat. § 604.18 costs and attorney fees.

On July 7, 2011, the district court issued an order granting appellant's motion to amend the complaint to include a request for taxable costs under Minn. Stat. § 604.18. Following a hearing on the question of the taxable costs, the district court dismissed the claim for taxable costs under Minn. Stat. § 604.18 in an order dated August 26, 2011. Although it found that respondent "acted in bad faith in not agreeing to the appraisal process . . . and for the delay in making payment," the district court nevertheless concluded that taxable costs under that section were not appropriate because the claim was resolved or confirmed by appraisal. *See generally* Minn. Stat. § 604.18, subd. 4(c) ("An award of taxable costs under this section is not available in any claim that is resolved or confirmed by arbitration or appraisal.").

Both the bank and the insurer appealed, and this court consolidated the appeals by order dated February 14, 2012. Having perfected its appeal first, the bank is designated herein as appellant and the insurer is designated as respondent and its appeal constitutes a cross-appeal.

D E C I S I O N

Appellant challenges the district court's determination that it was entitled to the ACV at the time of the loss. Respondent challenges the district court's determination that appellant was the prevailing party. Both parties challenge the district court's application of Minn. Stat. § 604.18.

I.

Appellant argues that the language of the insurance policy entitled it to recover the actual cash value of the loss on the date of the appraisal hearing. This is different from the argument that appellant made below, where it argued that it was entitled under the policy to the replacement cost value at the time of the appraisal hearing. The district court awarded appellant the actual cash value at the time of the loss.

Contract interpretation is a question of law and is reviewed de novo. *Travertine Corp. v. Lexington-Silverwood*, 683 N.W.2d 267, 271 (Minn. 2004). The district court's task in interpreting a contract is to determine and enforce the intent of the parties. *Motorsports Racing Plus, Inc. v. Arctic Cat Sales, Inc.*, 666 N.W.2d 320, 323 (Minn. 2003). Where the terms of the contract have been reduced to a clear and unambiguous writing, then "the intent of the parties is determined from the plain language of the instrument itself." *Travertine Corp.*, 683 N.W.2d at 271. Ambiguities in an insurance contract "are to be resolved against the insurer and in accordance with the reasonable expectations of the insured." *Caledonia Cmty. Hosp. v. St. Paul Fire & Marine Ins. Co.*, 307 Minn. 352, 354, 239 N.W.2d 768, 770 (1976).

The relevant terms of the policy at issue in this case state that:

> **1. Property Coverages**
>
> **a. Our Limit**—Subject to the deductible or other limitation that applies, "we" pay the lesser of:
>
> 1) the "limit" that applies;
> 2) "your" interest in the property; or
> 3) the amount determined under the applicable Loss Settlement Terms.
>
> . . . .

e. Loss Settlement Terms—Subject to the "terms" shown above, losses are settled according to the Replacement Cost Terms. If the Replacement Cost Terms do not apply, losses are settled according to the Actual Cash Value Terms.

1) Replacement Cost Terms That Apply to Coverages A and B Only

. . . .

d) "We" pay the cost to repair or replace the damaged part without deduction for depreciation. . . .

. . . .

e) When the cost to repair or replace exceeds the lesser of $2,500 or 5% of the "limit" on the damaged building, "we" do not pay for more than the actual cash value of the loss until repair or replacement is completed.

f) "You" may make a claim for the actual cash value of the loss before repairs are made. A claim for an additional amount payable under these "terms" must be made within 6 months after the date of loss.

. . . .

3) Actual Cash Value Terms—Actual cash value includes a deduction for depreciation, however caused.

a) The Actual Cash value terms apply to all property not subject to the Replacement Cost Terms.

> b) The smaller of the following amounts is used in applying the "terms" under Our Limit:
>
> (1) the cost to repair or replace the property with materials of like kind and quality to the extent practical; or
>
> (2) the actual cash value of the property at the time of loss.

Appellant argues that terms 1(e)(1)(e) and 1(e)(1)(f) define "actual cash value" when repairs have not yet been completed, and that, unlike term 1(e)(3)(b)(2), do not include a date for determining the actual cash value. Appellant argues that this creates an ambiguity that must be construed against respondent to mean that the loss is valued at the date of the appraisal hearing.

Appellant misreads the policy. The Actual Cash Value terms are the only part of the contract providing a definition of the term "actual cash value." The reading proposed by appellant would render them superfluous.

The only property coverages available under the policy are A, B, and C. Of these, replacement cost terms for most A and B items appear in term 1(e)(1). Replacement cost terms for coverage C items and the remaining coverage A and B items appears in term 1(e)(2), which contains language analogous to that in 1(e)(1)(e) and 1(e)(1)(f). Under the interpretation of the policy advanced by appellant, the actual cash value of property would never be calculated under the Actual Cash Value terms, because the language in 1(e)(1) or 1(e)(2) would control the valuation of any property damage. That is not a reasonable interpretation of the contractual language.

The only reasonable interpretation of the policy is that it requires the insurer to pay actual cash value, calculated pursuant to the Actual Cash Value terms in 1(e)(3), until actual repair or replacement takes place. Reading the policy in this fashion necessitates concluding that actual cash value is calculated at the time of the loss.

This interpretation of the policy language is consistent with long-standing case law. Minnesota case law establishes that the term "actual cash value" means the "actual market value at the time of destruction." *Brooks Realty, Inc. v. Aetna Ins. Co.*, 276 Minn. 245, 253, 149 N.W.2d 494, 500 (1967); *see also* Minn. Stat. § 65A.01, subd. 3 (2010) (stating, as a term of the Minnesota Standard Fire Insurance Policy, that, except in cases of total loss, the amount of loss or damage is "to be estimated according to the actual value of the insured property at the time when such loss or damage happens.") "A party's rights to insurance proceeds are determined by the status of the party's interests at the time of the fire." *Anderson v. State Farm Fire & Cas. Co.*, 397 N.W.2d 416, 417 (Minn. App. 1986), *review denied* (Minn. Feb. 18, 1987); *cf. also Winberg v. Md. Cas. Co.*, 434 N.W.2d 274, 277 (Minn. App. 1989) (holding that mortgagee's right to insurance proceeds vested at the time of loss), *review denied* (Minn. Feb. 10, 1989); *Minn. Fed. Sav. & Loan Ass'n v. Iowa Nat'l Mut. Ins. Co.*, 372 N.W.2d 763, 767 (Minn. App. 1985) (holding that proceeds recoverable by mortgagee were limited to amount owed on note at the time of the loss), *review denied* (Minn. Nov. 1, 1985).

Finally, appellant's argument goes against logic and public policy. In determining the actual cash value, payable before repair or replacement, it would make no sense to make the parties bear the risk and uncertainty of an increased or decreased recovery

based on the date of a hypothetical future appraisal hearing that may never come to pass. Such an arrangement would invite abuse, as one side would often have an incentive to delay proceedings to increase its recovery or reduce its liability.

The district court did not err in concluding that the amount that respondent was required to pay was the actual cash value at the time of the loss. That conclusion is supported by the policy language and settled statutory and case law.

II.

Respondent argues that the district court erroneously held that appellant was a prevailing party.

A district court has the discretionary authority to determine which party to a dispute is the prevailing party. *Haugland v. Canton*, 250 Minn. 245, 254, 84 N.W.2d 274, 280 (1957). This authority arises from the district court's powers as a court of equity. *Id.* Accordingly, this court will only reverse the district court's determination as to the prevailing party if the district court abused its discretion. *Posey v. Fossen*, 707 N.W.2d 712, 714 (Minn. App. 2006). That discretion is abused where the district court's determination went "against logic and facts on the record," was "arbitrary or capricious," or was based on "an erroneous view of the law." *Id.* (quotation omitted). The party challenging the determination has the burden of demonstrating that "no reasonable person would agree" with the determination. *Id.*

In determining the prevailing party in a dispute, "the general result should be considered, and inquiry made as to who has, in the view of the law, succeeded in the action. The prevailing party in any action is one in whose favor the decision or verdict is

rendered and judgment entered." *Borchert v. Maloney*, 581 N.W.2d 838, 840 (Minn. 1998) (quotation omitted).

In this case, respondent ultimately paid appellant $29,083.65 more than it had originally tendered, after appellant brought suit and moved the district court for an order compelling an appraisal hearing. Given this result, and despite appellant having not prevailed on the question of the proper measure of recovery under the policy, the district court could reasonably conclude that appellant succeeded in the action. The determination that appellant prevailed was a reasonable conclusion and not an abuse of discretion.

III.

Respondent argues that the district court erred in finding that it knowingly denied appellant the benefits of the insurance policy without a reasonable basis in violation of Minn. Stat. § 604.18, subd. 2(a), based upon respondent's "not agreeing to the appraisal process to resolve the claim . . . and for the delay in making payment." Appellant argues that the district court erred in concluding that appellant was entitled to recover taxable costs under subdivision 2, an account of respondent's bad faith. Respondent further argues that those costs are not recoverable because appellant's claim was "resolved or confirmed by arbitration or appraisal." Minn. Stat. § 604.18, subd. 4(c).

A. Reasonableness of respondent's conduct

Section 604.18 allows for a discretionary award of attorney fees and additional costs not normally recoverable in certain enumerated circumstances. However, the district court is not entitled to exercise that discretion unless the insured can show "the

absence of a reasonable basis for denying the benefits of the insurance policy" and "that the insurer knew of the lack of a reasonable basis for denying the benefits of the insurance policy or acted in reckless disregard of the lack of a reasonable basis for denying the benefits of the insurance policy." Minn. Stat. § 604.18, subd. 2(a). Whether either of these requirements is met is a question of fact. *See Mullins v. Churchill*, 616 N.W.2d 764, 768 (Minn. App. 2000) ("[R]easonableness tests are often termed questions of fact."), *review denied* (Minn. Nov. 15, 2000). We review the district court's factual findings for clear error. *Goldman v. Greenwood*, 748 N.W.2d 279, 284 (Minn. 2008). A district court's findings of fact are clearly erroneous when, "despite viewing [the] evidence in the light most favorable to the [district] court's findings," we are left with "the definite and firm conviction that a mistake was made." *Vangsness v. Vangsness*, 607 N.W.2d 468, 474 (Minn. App. 2000).

Here, it is undisputed that respondent promptly adjusted the loss and tendered a payment of $118,847.40 to appellant before appellant acquired title to the property through foreclosure proceedings. It was almost two years after the loss before appellant gave any indication to respondent that appellant was disputing the amount paid.

There was a dispute between the parties as to the availability of arbitration or appraisal in the circumstances of a mortgagee claiming under a policy issued to the named mortgagors. That dispute was resolved in favor of appellant upon its motion to the district court.

Once the arbitration panel made its award, respondent deposited funds with the district court in the amount of the difference between what it had already paid and the

appraised ACV at the time of the loss. That was the amount that respondent owed under the policy. Had appellant been willing to accept the amount it was properly owed, rather than advancing an incorrect and indeed strained interpretation of the policy language, it could have received the funds deposited with the court. Although respondent should have paid the amount it agreed that it owed directly to appellant, the deposit of the funds under Minn. R. Civ. P. 67.01 did not amount to a denial of the benefits that respondent owed.[4]

Although over three years passed between the date of the loss and respondent tendering payment of the full ACV at the time of the loss, nearly all of that delay was occasioned by matters unquestionably not under respondent's control. Appellant acquired the property by foreclosure and was awaiting expiration of the redemption period. It received prompt payment for the ACV arrived at by respondent's initial adjustment of the loss. Appellant commissioned a second estimate of the loss, but opted for reasons of its own not to disclose that estimate for over a year. The essence of the dispute between the parties was the proper measure of recovery under the policy, an issue

[4] *See generally* Minn. R. Civ. P. 67.01 (permitting a party to a dispute over money to deposit any or all of the money with the district court pending resolution of the case). The invocation of rule 67.01 is somewhat unusual in a case such as this. A party making a deposit with the court pursuant to rule 67.01 generally does so in order to continue arguing that it is not required to pay that amount. *See Auto Owners Ins. Co., v. Valadez*, 481 N.W.2d 398, 401 (Minn. App. 1992) ("Minn. R. Civ. P. 67.01 permits a depositor to retain an interest in the property."). Respondent here was not disputing that it owed appellant that amount, and its motion papers relating to the deposit specifically identify the deposit as being "the amount North Star believes is due to the Bank." There having been no question that respondent owed at least $29,083.65 to appellant, respondent should have paid the money directly to appellant. However, as noted, appellant was not willing to release its claim upon payment in that amount. Respondent's resort to rule 67.01 was surely not a denial that it owed the $29,083.65.

on which respondent prevailed based upon the plain language of the policy and settled Minnesota law.

The only incorrect position taken by respondent during these proceedings was its initial resistance to the appraisal hearing based on its interpretation that appellant was not an "insured" within the meaning of the contract for purposes of the appraisal process.[5] Appellant prevailed on that issue. It was on this basis that the district court properly determined appellant to be the prevailing party.

However, the majority of the states with statutes similar to Minn. Stat. § 604.18 have adopted a "fairly debatable" standard when evaluating an insurer's denial of benefits. *Friedberg v. Chubb & Son, Inc.*, 800 F. Supp. 2d 1020, 1025 n.1 (D. Minn. 2011). Although ultimately found to be incorrect by the district court, under the unique circumstances of this case, respondent's position on the availability of appraisal was "fairly debatable."[6]

Almost two years had passed after the date of the loss before respondent received an appraisal demand from appellant. Nothing in the record indicates that, prior to requesting an appraisal, appellant had even informed respondent that it had obtained a

[5] Term 18 of the amendment of policy terms for Minnesota homeowners provided that if "you" or "we" did not agree on the amount of the loss, "you" and "we" could submit the dispute to a panel of three appraisers. The policy defined "you" as the named insureds; in this case, the Hansons. Appellant was not a named insured, but term 13 of the policy conditions provided that "[a]ll 'terms' of this policy apply to the mortgagee, secured party, or lender unless changed by this clause." The parties disputed whether term 13 of the policy conditions meant that appellant could be treated as an insured for purposes of term 18 of the amendment of policy terms for Minnesota homeowners.

[6] The issue of the propriety of the district court's order compelling appraisal is not before us. We will therefore assume for the purposes of our discussion that the right to demand an appraisal should be treated as a benefit under the policy.

different valuation of the loss. Thus respondent could not possibly have understood that there was disagreement on the value of the loss until its receipt of appellant's motion to compel appraisal proceedings. The record does not support the district court's finding of bad faith as there is no evidence that respondent's declination to submit to arbitration was without a reasonable basis.

Based on this unique set of circumstances, and despite viewing the evidence in the light most favorable to appellant, we are left with the definite and firm conviction that the district court erred in finding that respondent's conduct "in not agreeing to the appraisal process . . . and for the delay in making payment" amounted to bad faith. Therefore, the district court's finding that respondent violated Minn. Stat. § 604.18 was clearly erroneous.

B. Resolved or confirmed by arbitration or appraisal

Given our determination that the district court clearly erred in finding that respondent unreasonably denied the benefits of the insurance policy, we do not reach the question of whether the claim was "resolved or confirmed by arbitration or appraisal" within the meaning of Minn. Stat. § 604.18, subd. 4(c).

IV.

The district court correctly held that appellant was entitled to the actual cash value at the time of the loss and did not err in concluding that appellant was the prevailing party in this matter. However, the district court clearly erred in finding that, under the unique circumstances of this case, appellant demonstrated "the absence of a reasonable basis for denying the benefits of the insurance policy" and "that the insurer knew of the lack of a

reasonable basis for denying the benefits of the insurance policy or acted in reckless disregard of the lack of a reasonable basis for denying the benefits of the insurance policy." Minn. Stat. § 604.18, subd. 2(a).

Affirmed in part and reversed in part.