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IN THE SUPREME COURT OF THE STATE OF IDAHO

AMERICAN WEST ENTERPRISES, INC., an Idaho Corporation,) Supreme Court No. 40230-2012
Plaintiff-Appellant,) District Court No. CV-2011-238
V.)
CASE NEW HOLLAND, INC.,))
Defendant- Respondent.)))

APPELLANTS BRIEF

Appeal from the District Court of the Fifth Judicial District of the State of Idaho, in and for Minidoka County

Honorable Jonathan P. Brody, District Judge

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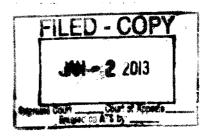


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I. STATEMENT OF THE CASE

i. Nature of the Case

The nature of this case on appeal seeks a review as to whether the District Court erred in awarding Summary Judgment in favor of respondent/cross-appellant.

ii. Course of Proceedings Before the Lower Court and its Disposition

On March 18, 2011, the plaintiff/appellant, American West Enterprises, Inc. (hereinafter "American West") filed its *Complaint* in Minidoka County District Court.

The *Complaint* improperly named Case New Holland, Inc., as defendant. American West alleged breach of the implied warranties of merchantability and fitness for a particular purpose and additionally demanded reimbursement for the cost of parts and labor.

On May 16, 2011, the defendant filed its *Answer to Complaint and Demand for Jury Trial* in the name of CNH America, LLC, (hereinafter "CNH"). CNH's defense included the assertion that American West's claims were barred by a lack of privity between the parties.

On May 4, 2012, CNH filed a Motion for Summary Judgment, Memorandum in Support of Motion for Summary Judgment and Affidavit of William A. Fuhrman in Support of Motion for Summary Judgment. (Tr. pg. II.) American West filed an Objection to Motion for Summary Judgment, Affidavit of Frank Jensen, Affidavit of Hal Anderson, Affidavit of Chuck Simmons, and Motion for Leave to Amend Complaint. (Tr. pg. II.) Oral argument on the motion for summary judgment and motion for leave to amend complaint was heard before the Honorable Jonathan Brody on June 11, 2012.

On July 13, 2012, the District Court issued its Memorandum Decision Granting

Defendant's Motion for Summary Judgment and Denying Plaintiff's Motion for Leave to

Amend Complaint. (Tr. pg. 70.) The Memorandum Decision granted CNH's motion for summary judgment and denied American West's motion to amend the complaint. The District Court found that privity of contract is required to recover for economic loss for breach of an implied warranty and that there was no privity of contract between the two parties. The District Court further found that American West was not a third party beneficiary to any contract between Pioneer Equipment and CNH and was therefore not entitled to enforce any contract between Pioneer and CNH. Lastly, the District Court found that Pioneer Equipment, although an authorized dealer of CNH, was not an agent of CNH. American West appeals each of these findings.

On July 18, 2012, the District Court issued its Judgment dismissing American West's claims. (Tr. pg. 80.)

iii. Concise Statement of Facts

On June 26, 1997, American West purchased a Case IH 3394 tractor (hereinafter "tractor") from Cameron Sales, Inc., which was CNH's authorized dealer and repair center. Subsequent to the purchase, Cameron Sales, Inc. was bought out by Pioneer Equipment Co., which remained CNH's authorized dealer and repair center.

In 2007, American West determined to sell the tractor but realized it needed a new engine. American West therefore hired Pioneer Equipment to install a new engine in the tractor. American West further requested that Pioneer Equipment order a new engine from CNH to install in the tractor. The new engine was obtained and installed in the tractor at a cost to American West of \$11,955.04.

After the engine was replaced, American West decided to keep the tractor and did so for two years. In that time, American West only used the tractor occasionally and put

approximately ten engine hours on the new engine. In the spring of 2009, the tractor was sold to Frank Jensen. Mr. Jensen put approximately five engine hours on the tractor before the engine blew up. Mr. Jensen returned the broken tractor to American West, which refunded him his purchase price and returned the tractor to Pioneer Equipment in order to diagnose the engine problem. The new engine in the tractor only had approximately fifteen hours on it at the time it blew up.

Pioneer Equipment tore down the engine to diagnose the problem and discovered that the engine supplied by CNH had a faulty valve spring that broke and caused the valve to drop down and contact the piston. This caused metal to be sent to the other pistons and valves resulting in catastrophic damage to the engine. It was also discovered by Pioneer Equipment that some of the valve springs in the new engine were used and out of character with the new engine. Pioneer Equipment than contacted CNH field representative Jeff Jensen and requested that the engine be warranted due to the faulty engine valve spring, but was told that the engine would not be warranted. Further attempts to obtain warranty service on the engine were unsuccessful and this action was commenced March 21, 2011.

II. ISSUES ON APPEAL

1. WHETHER THE DISTRICT COURT ERRED WHEN IT GRANTED SUMMARY JUDGMENT FINDING THAT PRIVITY OF CONTRACT IS REQUIRED TO RECOVER FOR ECONOMIC LOSS FOR BREACH OF AN IMPLIED WARRANTY.

A. Idaho Cases/Law

CNH relied heavily upon the Salmon Rivers Sportsman Camps, Inc., v. Cessna Air Co., and the subsequent line of cases in their argument that privity of contract is

required in an action to recover economic loss for breach of implied warranties. *Salmon Rivers* 97 Idaho 348, 544 P.2d 306 (1975). The District Court, relying upon *Nelson v. Anderson Lumber Co.*, found in its *Memorandum Decision* that the Idaho Court of Appeals has reaffirmed, as recently as 2004, that privity of contract is required to recover economic loss for breach of implied warranties. *Nelson* 140 Idaho 702, 707 (Idaho Ct. App. 2004). The District Court further wrote that while it was "sympathetic to the possibility that the economic loss rule coupled with the privity requirement may result in little or no recovery for American West, it is not this court's prerogative to ignore precedent. *Memorandum of Decision* p.5. The District Court does not address the holdings of *State v. Mitchell Const. Co.* or *Tusch Enterprises v. Coffin*.

In *Mitchell Const. Co.*, this Court did not directly address the issue of privity in relation the economic loss rule in its holding, rather Summary Judgment was affirmed on other principles. *State v. Mitchell Const. Co.*, 108 Idaho 335, 699 P.2d 1349 (1984). However, in *dictum* three Justices voice their opinion that the previous holding in *Salmon Rivers* was no longer valid.

Chief Justice Donaldson expressly did not concur with the majority opinion in regards to *Salmon Rivers*. *Id.* at 337, 1351. Rather, Chief Justice Donaldson wrote that he could not concur in the adoption or approval of the previous holding in *Salmon Rivers*. *Id.* at 338, 1352. In reaching his decision, he relied upon an Alaskan Supreme Court case:

It is not the merchant who has defectively manufactured the product. Nor is it usually the merchant who advertises the product on such a large scale as to attract customers. We have in our society literally scores of large, financially responsible manufacturers who place their wares in the stream of commerce not only with the realization, but with

the avowed purposes, that these goods will find their way into the hands of the consumer. Only the consumer will use these products; and only the consumer will be injured by them should they prove defective.

Morrow v. New Moon Homes, Inc., 548 P.2d 279 (Alaska 1976) citing Kassab v. Central Sova, 432 Pa. 217, 246 A.2d 848, 853 (1968).

Justice Huntley, in his dissenting opinion, wrote that the "continued validity of *Salmon Rivers* is questionable—the requirement... of privity in implied warranty for economic loss did not make sense when the decision was written and its application has resulted in substantial injustice to many litigants in Idaho since 1975. We should simply overrule that case at this time." *Mitchell Const.* at 339, 1353.

Upon rehearing the case after remand, Chief Justice Donaldson and Justice Huntley continued to adhere to their previous opinions. Justice Bistline, however, changed positions and wrote: "I now fully agree with the view earlier expressed by Chief Justice Donaldson and Justice Huntley that *Salmon Rivers* should be overruled, and so vote." *Id.* at 341, 1355. Justice Bistline continued: "Unless I misread Judge Schroeder's opinion, he would not have granted the summary judgment if *Salmon Rivers* had not been in place. If, as it appears, there are three votes to overrule that case, the summary judgment should be reversed and the case remanded to the district court for reconsideration." *Id.*

The result of the *Mitchell Const.* case was there were three votes out of five to overturn the privity requirements set out in *Salmon Rivers*. The requirement of privity in cases that dealt solely with economic loss had been overturned; however there was no clear statement from this Court articulating this result.

The clear and concise statement regarding the continued validity of the *Salmon Rivers* privity requirement came from Justice Bistline in his concurrence in *Tusch Enterprises v. Coffin.* Justice Bistline wrote: "Having concurred in the majority opinion, I write only to inform the trial bench and bar that the *Salmon Rivers v. Cessna Aircraft Co.* case, which is recognized as having continued by doubtful validity in the opinion for the Court, was specifically overruled in the *State v. Mitchell* case..." *Tusch Enterprises v. Coffin,* 113 Idaho 37, 740 P.2d 1022 (1987).

In the *Tusch Enterprises* case, this court addressed but did not decide the issue of privity in relation to the economic loss rule. Rather, the Court decided the issue of privity in relation to subsequent purchasers of residential dwellings and the ability of subsequent purchasers to rely upon the implied warranty of habitability. *Id.* at 1035, 50. Specifically, the court overturned any requirement of privity of contract between a builder and subsequent purchasers of residential dwellings who suffer purely economic losses from latent defects that manifest themselves within a reasonable amount of time. *Id.* The Court expressed that any other holding would lead to an "absurd result." *Id.* at 1036, 51.

The *Tusch Enterprises* court relied upon its previous decision in *Clark v. International Harvester Co.*, in reaching its decision. *Id.* at 1035, 50. In *Clark*, the court held that a party suffering only economic losses could not recover under a negligence theory. *Clark v. International Harvester Co.*, 99 Idaho 326, 581 P.2d 784 (1978). The *Tusch Enterprises* court explained this decision: "The rationale behind that decision was to allow the law of contracts to resolve disputes concerning economic losses. If, however, in the area of pure economic losses, negligence is to be preempted by contract

principles, as we ruled in *Clark*, then contract principles must be given a freer hand to deal with injuries the law has typically redressed." *Tusch Enterprises* at 1035, 50. The *Tusch Enterprises* court continued: "Therefore, we decline to extend the privity requirement enunciated in *Salmon Rivers* to the facts at hand. The instant case is not a goods case, and the question regarding the continued vitality of *Salmon Rivers* in such cases is better left to another day when a response on our part would be something more than mere dictum." *Id.* (emphasis added).

In 1999, this Court again addressed the issue of privity of contract in cases of economic loss in *Ramerth v. Hart. Ramerth v. Hart*, 133 Idaho 194, 983 P.2d 848 (1999). In that case, the Court wrote that "Salmon Rivers has been the subject of substantial debate regarding the desirability of the rule that it announced as well as its continuing validity." *Id.* at 198, 852. The *Ramerth* Court, however, read the *Tusch Enterprises* decision that the question regarding the continued vitality of *Salmon Rivers* in [cases of economic loss] is better left to another day when a response would be something more than dictum as continued affirmation of the *Salmon Rivers* rule. *Id.* The Court wrote: "Despite Justice Bistline's opinion, however, the majority opinion in *Tusch* recognized the continuing validity of *Salmon Rivers*… We conclude, therefore, that *Salmon Rivers* remains valid. We are not persuaded that the rule announced in *Salmon Rivers* should be further relaxed to allow a claim for breach of implied warranty on the facts of this case."

The *Salmon River* string of cases has resulted in consumers being put in a difficult position. The *Clark* case found that a party suffering only economic loss could not recover under a negligence theory. This left contract theory as the sole means of redress

for plaintiffs suffering only economic loss. *Tusch Enterprises* relaxed the privity requirement in a very narrow instance as it "would lead to an absurd result." *Tusch Enterprises* at 1036, 51. Dictum in both *Tusch Enterprises* and *Mitchell Const.* indicate that *Salmon Rivers* and its privity requirement have been overruled. The *Ramerth* Court concluded that *Salmon Rivers* remains valid and shouldn't be relaxed on the facts that were before the court.

Therefore, it appears that American West has no redress through negligence theory given the holding of *Clark*. Furthermore, American West has no redress through contract theory because of the holdings of *Salmon Rivers* and *Ramerth* which exclude American West's claim due to a lack of contractual privity with the manufacturer of the engine, CNH. However, this appears to be the set of facts, as this is a "goods case" for which there is only economic loss, which the *Tusch Enterprises* Court had in mind in order for the Court to respond with a concise decision that would be "more than mere dictum." *Tusch Enterprises* at 1035, 50.

B. Other Jurisdictions

Some jurisdictions have now abolished privity requirements in warranty actions where only economic losses were sought. In Nevada and Pennsylvania, the requirement has been done away with as there is "no reason to distinguish between recovery for personal and property injury, on the one hand, and economic loss on the other." *Hiles Co. v. Johnston Pump Co.*, 93 Nev. 73, 560 P.2d 154, 157 (1977); *accord Salvador v. Atlantic Steel Boiler Co.*, 256 Pa.Super. 330, 389 A.2d 1148 (1978).

In Missouri, the Court adopted the view that abolishing privity "simply recognizes that economic loss is potentially devastating to the buyer of an unmerchantable product

and that it is unjust to preclude any recovery from the manufacturer for such loss because of a lack of privity, when the slightest physical injury can give rise to strict liability under the same circumstances." *Groppel Co. Inc.*, v. U.S. Gypsum Co., 616 S.W.2d 49 (Mo.App.1981).

In Texas, the privity requirement is not needed to assert a claim for breach of an implied warranty against a remote manufacturer of a finished product. *Hininger v. Case Corp.*, 23 F.3d 124 (5th Cir. 1994).

In New York it was determined that a buyer from a dealer could sue the manufacturer for direct economic loss for defective breaking system in a truck. *Hubbard* v. *General Motors Corp.*, 39 U.C.C.2d 83 (S.D.N.Y. 1996).

The Court of Appeals for the Third District of Indiana summarized the purpose of privity as follows:

Generally privity extends to the parties to the contract of sale. It relates to the bargained for expectations of the buyer and seller. Accordingly, when the cause of action arises out of economic loss related to the loss of the bargain or profits and consequential damages related thereto, the bargained for expectations of buyer and seller are relevant and privity between them is still required.

Implied warranties of merchantability and fitness for a particular use, as they relate to economic loss from the bargain, cannot then ordinarily be sustained between the buyer and a remote manufacturer.

Richards v. Goerg Boar and Motors, Inc., 179 Ind.App. 102, 384 N.E.2d 1084 (Ind.App.1977).

The Indiana Supreme Court expounded upon this privity requirement in *Hyundai*Motor America, Inc. v. Goodin. In that case, the Court pointed out that the rationale of the privity requirement has "eroded to the point of invisibility as applied to many types of

N.E.2d 947, (2005). The *Hyundai* Court explained that the UCC recognizes an implied warranty of merchantability if "goods" are sold to "consumers" by one who ordinarily deals in this product. *Id.* at 958. The *Hyundai* Court further explained that doing away with the privity requirement simply gives the consumer the contract they expected, while the manufacturer is encouraged to build quality into its products. *Id.* at 989. The Court continued: "To the extent there is a cost of adding uniform or standard quality in all products, the risk of a lemon is passed to all buyers in the form of pricing and not randomly distributed among those unfortunate enough to have acquired one of the lemons. Moreover, elimination of privity requirement gives consumers... the value of their expected bargain." *Id.*

C. <u>Absurd Result Under Existing Law</u>

The privity requirement combined with the economic loss rule is draconian and ill-equipped to deal with the realities of today's market place. A majority of products purchased by consumers are not purchased directly from the manufacturer and the consumer generally has no relationship with the manufacturer. Rather, products typically reach the consuming public through intermediaries.

As it stands, if the consuming public suffers economic loss from a product they purchased, they must commence an action against the intermediary or distributor they purchased the product from who then must join the next intermediary or distributor until every intermediary or distributor that has been involved in the transaction, no matter how minimally, has been included in the chain of actions. Judicial efficiency and conflict resolution are clearly not advanced by the privity requirement.

In the case at hand, American West purchased, at great cost, a motor from an authorized dealer of CNH. CNH did not provide a warranty on the motor, therefore implied warranties attached to the engine. American West expected to have a new, good, and workmanlike motor. However, the motor self-destructed due to a faulty valve spring that appeared to not even be new. American West clearly did not receive the benefit of their bargain. CNH however, has no reason to fear making faulty, inferior or defective products because they rarely sell goods directly to the consuming public, and are therefore insulated from liability because of the privity requirement. Rather, CNH sells products through their authorized dealers.

It was not Pioneer Equipment, the authorized dealer, who defectively manufactured the product. Nor was it Pioneer Equipment that was injured economically by its defect. However, under the privity requirement Pioneer Equipment should have been sued for the faulty motor. As the Court in the *Tusch Enterprises* case found, this would result in an "absurd result." *Tusch Enterprises* at 1036, 51.

2. WHETHER THE DISTRICT COURT ERRED WHEN IT FOUND THAT AMERICAN WEST WAS NOT A THIRD PARTY BENEFICIARY.

CNH argues that as there is no written contract between any of the parties in this case, there is no ambiguity regarding the intent of the contract and the circumstances surrounding any agreement between the parties intent may not be considered. *Reply Memorandum in Support of MSJ* p. 3. The District Court however, believed that the facts were sufficient to provide enough evidence to construe the contract between Pioneer Equipment and CNH. *Memorandum Decision* p. 6. The District Court found that there

was no evidence that the contract between Pioneer Equipment and CNH reflected intent to benefit American West. *Id*.

In reaching its Decision, the District Court found that although American West argued that the engine was ordered specifically for the benefit and use of American West, the fact that Pioneer Equipment charged \$3,000 for labor shows that Pioneer Equipment intended only to benefit itself. *Id*.

The District Court did not address the Affidavit of Hal Anderson or the Affidavit of Chuck Simmons in its Memorandum Decision.

In making its Decision, the District Court relied upon *Idaho Power Co. v. Hulet*, which provides that the issue of whether a party is an intended beneficiary is one of contract construction. *Idaho Power Co. v. Hulet*, 140 Idaho 110 (2004). In construing a contract, a court should look to the "apparent purpose the parties are trying to accomplish." *Id.* at 113. The District Court wrote that as there is no written contract, there is no document to construe to determine whether the contract itself reflects intent to benefit American West. *Memorandum Decision* p. 5-6. Therefore, under the District Courts decision, there can never be an intended third party beneficiary in the absence of a written agreement.

Chuck Simmons is the service manager for Pioneer Equipment and as such oversaw the ordering, installation, and diagnosis of the new engine. In his affidavit Mr. Simmons explains that "the engine and core were ordered specifically for the benefit of American West Enterprises, Inc., and for use in their Case IH 3394." *Affidavit of Chuck Simmons* ¶ 5. Mr. Simmons continued: "That due to cost, it is not customary to order new engines and cores unless they are ordered for specific customers for use in specific

equipment." *Id.* at ¶ 6. Hal Anderson expresses in his affidavit "I requested Pioneer Equipment to order a new engine from CNH to install in American West's Case IH 3394." *Affidavit of Hal Anderson* ¶ 8. Therefore, we have both Mr. Simmons (CNH's authorized dealer service manager) and Mr. Anderson expressing the "apparent purpose the parties are trying to accomplish," which was to benefit American West with a working engine in its tractor. *Idaho Power Co.* at 113.

The District Court relied upon the *Nelson v. Anderson Lumber Co.* case in reaching that decision. In that case, the Court analogized the relationship between property owners, the general contractor, and the subcontractors. *Nelson v. Anderson Lumber Co.*, 140 Idaho 702 (2004). That case is no analogous to the case at hand. American West did not hire a general contractor to do general construction work for them. Rather, American West expressly requested the authorized dealer of a manufacturer to special order an engine for American Wests' use and benefit.

In *Reed v. City of Chicago*, the United States District Court for the Northern District of Illinois found that since the benefit of paper gowns were for the protection of potentially suicidal detainees, privity was not required as the detainees were the intended beneficiaries of the paper gowns. *Reed v. City of Chicago*, 263 F.Supp.2d 1123 (N.D. Illinois 2003). In that case, the mother of an inmate sued the manufacturer of paper gowns that were used by the City of Chicago to clothe potentially suicidal inmates, after her son committed suicide with a paper gown that did not tear away. *Id.* The Court wrote in its findings:

The beneficiary of any warranty made by the manufacturer and designer of the gown is necessarily a potentially suicidal detainee like Reed. If protection is not provided to plaintiffs like Reed, any warranty as to the safety of the gown would have little, if any, effect. In designing and manufacturing the gown, the defendants contemplated that the users of the gown would be detainees... For these reasons, a detainee of the City like Reed must be able to enforce the protections of any warranties made by the manufacturer and designer of the gown.

Id. at 1126.

Similar to the *Reed* case, CNH does not manufacture engines for the benefit of their Authorized Dealers. If that were so, they would have gone out of business long ago as the Authorized Dealers have no need for engines other than to install them in intended third parties tractors. Rather, CNH manufactures engines for the benefit of tractor owners such as American West.

It is clear from the *Affidavit of Chuck Simmons* and the *Affidavit of Hal Anderson*, that American West was the intended beneficiary of the transaction.

3. WHETHER THE DISTRICT COURT ERRED WHEN IT FOUND THAT PIONEER EQUIPMENT WAS NOT AN AGENT OF CNH AMERICA.

The District Court found in its *Memorandum Decision* that the question of whether Pioneer Equipment was an agent of CNH was a question of fact as the facts relied upon to establish the existence of an agency relationship were undisputed.

Memorandum Decision p. 7. The District Court based this decision on the fact that there was no dispute in the record that Pioneer Equipment was CNH's agent. *Id.* at 8.

In *Adkinson Corp v. American Bldg. Co.*, this Court found that proof of implied agency is generally found in the acts and conduct of the parties, rather than from an oral or written contract which establishes the agency relationship. *Adkinson Corp. v. American Bldg. Co.*, 107 Idaho 406, 690 P.2d 341 (1984). The *Adkinson* Court further

found that the existence of an agency relationship is a question for the trier of fact to resolve from the evidence. *Id.* at 409, 344.

In *Adkinson*, the plaintiffs brought suit against a manufacturer of metal buildings for economic damages from the late delivery of a defective building. ABC was the manufacturer of the building and RSI was its authorized dealer. The lawsuit was originally brought against both ABC and RSI but RSI was dismissed from the suit after filing bankruptcy. The District Court found that there was no principal-agency relationship between ABC and RSI. *Id.* This Court, however, found that the evidence was such that reasonable minds could differ as to the conclusion to be reached from the evidence. The case was remanded to the trial court for a new trial on the merits. *Id.*

Among the evidence that was established in the *Adkinson* case was the fact that RSI was an authorized dealer for ABC, that RSI participated with ABC in advertising ABC buildings, that RSI was supplied with ABC brochures and order forms and instructions, that RSI employees were given some training at an ABC plant, that ABC representatives were frequently in contact with the RSI office, and that RSI ordered the building in question from ABC. *Id*.

These facts are parallel to the facts of the case at hand. Pioneer Equipment was an authorized dealer of CNH and that Pioneer Equipment ordered the engine from CNH. It is apparent that Pioneer Equipment receives training from CNH on installation and maintenance of its products, that CNH and Pioneer Equipment jointly advertise CNH products, and that CNH and Pioneer Equipment are in constant communication. It is clear from the record that CNH acting through Jeff Jensen, told Pioneer Equipment that the engine would not be warranted. *Affidavit of Chuck Simmons* ¶ 15-16.

It is clear that at a minimum, Pioneer Equipment is CNH's implied or apparent agent. The question of agency should have been allowed to proceed at trial where a full

body of evidence could have been established, much like it was in Adkinson.

III. ATTORNEY FEES ON APPEAL

If American West is found to be the prevailing party on appeal, American West

requests that attorney fees be awarded for costs and fees reasonably incurred in the

appeal.

IV. <u>CONCLUSION</u>

Therefore, American West respectively requests that this Court remand the case

back to the District Court finding that the granting of summary judgment was improper

for the above-mentioned reasons and that the matter be permitted to proceed to trial as

material issues of fact remain.

DATED this 3 (day of December, 2012.

ROBINSON, ANTHON & TRIBE

Dy./ • (*)

For Brent T. Robinson

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CERTIFICATE OF MAILING

I hereby certify that on this 31st day of December, 2012, I served a copy of the within and foregoing **Appellants Brief** upon:

William A. Fuhrman TROUT JONES GLENDHILL FUHRMAN GOURLEY P. O. Box 1097 Boise, Idaho 83350

by depositing a copy thereof in the United States mail, postage prepaid, in an envelope addressed to said attorney at the foregoing address.

For Brent T. Robinson