9-16-2008

Aardema v. U.S. Dairy System, Inc. Respondent's Brief 2 Dckt. 35218

IN THE SUPREME COURT FOR THE STATE OF IDAHO

DON AARDEMA, an individual, RON AARDEMA, an individual, and DONALD J. AARDEMA, an individual, and doing business as AARDEMA DAIRY; DON AARDEMA, an individual, and RON AARDEMA, an individual, doing business as DOUBLE A DAIRY,

Plaintiffs/Respondents/
Cross-Appellants,

vs.

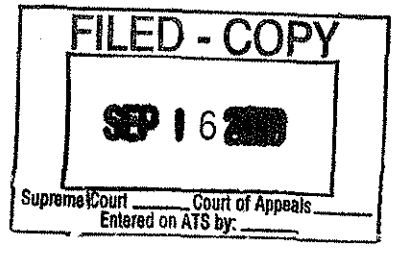
U. S. DAIRY SYSTEMS, INC., an Idaho corporation, doing business as Automated Dairy Systems, Inc., WESTFALIASURGE, INC., a foreign corporation, and EARL PATTERSON, an individual,

Defendants/Appellants/
Cross-Respondents,

FREEDOM ELECTRIC, INC., an Idaho corporation, JOHN DOE and JANE DOE, husband and wife, I through X, and BUSINESS ENTITIES I through X,

Defendants.

Supreme Court Docket No. **35218**



RESPONDENTS'/CROSS-APPELLANTS' BRIEF

Appeal from the District Court of the Fifth
Judicial District for Twin Falls County

Honorable G. Richard Bevan, District Judge, presiding

Robert A. Anderson
Matthew O. Pappas
ANDERSON, JULIAN & HULL, LLP
250 S. 5th St., Suite 700
P. O. Box 7426
Boise, ID 83707-7426
Attorneys for Appellant/Cross-Respondent
U.S. Dairy Systems, Inc.

Thomas B. High
BENOIT, ALEXANDER, HARWOOD,
HIGH & VALDEZ, L.L.P.
126 Second Avenue North
P. O. Box 366
Twin Falls, ID 83303-0366
Attorneys for Appellants/Cross-Respondents
WestfaliaSurge, Inc. and Earl Patterson

Brice A. Tondre
BRICE A. TONDRE, P.C.
215 S. Wadsworth Blvd.
Lakewood, CO 80226
Attorneys for Appellants/Cross-Respondents
WestfaliaSurge, Inc. and Earl Patterson

Kenneth L. Pedersen
Jarom A. Whitehead
PEDERSEN and WHITEHEAD
161 5th Avenue South, Suite 301
P. O. Box 2349
Twin Falls, ID 83303-2349
Attorneys for Respondents/Cross-Appellants
Don Aardema, Ron Aardema, Donald J.
Aardema, Aardema Dairy and Double A Dairy

Ken M. Peterson
MORRIS, LAING, EVANS, BROCK
& KENNEDY, CHARTERED
Old Towne Square
300 Mead, Suite 200
Wichita, KS 67202-2722
Attorneys for Respondents/Cross-Appellants
Don Aardema, Ron Aardema, Donald J.
Aardema, Aardema Dairy and Double A Dairy

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I. STATEMENT OF THE CASE

A. Introduction

This proceeding is procedurally unique in that it is an interlocutory appeal from the denial of summary judgment. In the current case, Plaintiffs state claims for negligence against Defendants related to the sale and installation of a ProFORM Pulsation Control System ("ProFORM System"). The system was negligently designed, installed and maintained in such a manner that it was defective and unreasonably dangerous. As a result of its defective condition, the ProFORM System did not operate properly and caused identifiable physical injury to Plaintiffs' dairy cows. As a result of this injury, the dairy cows produced less milk and produced lower quality milk, directly resulting in lost profits to Plaintiffs. Defendants argue that Plaintiffs have not demonstrated injury to their dairy cows, that Plaintiffs' damages are therefore purely economic in nature and are therefore barred by the "economic loss rule" in Idaho.

Plaintiffs have offered ample evidence of physical injury to their dairy cows. Indeed, the district court noted this evidence, and properly viewing the facts in a light most favorable to Plaintiffs, found that there are genuine issues of material fact precluding summary judgment regarding Plaintiffs' claim that their dairy cows have been injured. Defendants repeatedly invite this Court to second guess the district court's factual findings. These factual findings are not properly within the scope of this Court's review on interlocutory appeal. Defendants also ask the Court to expand the existing "economic loss rule" by way of the current interlocutory appeal. As demonstrated below, the expansion proposed by Defendants runs contrary to existing law and public policy concerns and must be rejected.

After denying Defendants motion for summary judgment, the district court expressed willingness to consider certifying interlocutory appeal. Plaintiffs opposed interlocutory appeal

because, in addition to arguing that the economic loss rule facially does not bar their claims, Plaintiffs had pled that there is a "special relationship" between the parties. This special relationship exception is a separate exception to the economic loss rule standing alone. Plaintiffs argued that because there were factual issues in the record regarding the existence of a special relationship, interlocutory appeal would not help efficiently dispose of the current case and was therefore inappropriate. Despite these factual issues, the district court summarily found that there was no evidence of a special relationship and entered judgment in favor of Defendants on this issue. **See** Tr., Vol. I, 72:24-73:2. Plaintiffs were the only party to present any evidence regarding the special relationship exception to the district court. Therefore, Defendants failed to meet their burden of showing the lack of genuine issues of material fact and the district court's grant of summary judgment on the special relationship issue constitutes error.

Additionally, Defendant U. S. Dairy never filed a summary judgment motion regarding the economic loss rule or the special relationship exception. Instead, at the summary judgment hearing on January 25, 2008, U. S. Dairy simply made an oral motion for summary judgment on the same bases and facts as set forth by Westfalia. Therefore, U. S. Dairy never set forth specific facts relevant to U. S. Dairy which would arguably entitle it to summary judgment. Moreover, U. S. Dairy failed to follow proper procedures for summary judgment motions, and as a result, Plaintiffs did not have the opportunity to respond to U. S. Dairy's arguments in support of summary judgment. Plaintiffs therefore cross-appealed from the court's entry of summary judgment in favor of U. S. Dairy on the special relationship issue. **See** R., Vol. I, pp. 185-189.

B. Course of Proceedings in the District Court

Plaintiffs filed its initial Complaint in this case against Defendants for negligence, breach of contract, breach of warranty, equitable estoppel and attorney fees. **See** R., Vol. I, pp. 26-34.

Plaintiffs subsequently amended their Complaint, alleging an additional claim for negligent design. **See** R., Vol. I, pp. 60-61.

Defendant Freedom Electric, Inc. ("Freedom") moved for summary judgment on November 21, 2007. **See** R., Vol. I, pp. 82-95. Westfalia joined in Freedom's motion for summary judgment and later filed its own motion for summary judgment on December 21, 2007. **See** R., Vol. I, pp. 96-98; pp. 99-104, respectively. U.S. Dairy also filed a motion for summary judgment regarding Plaintiffs' contract claims. **See** R., Vol. I, pp. 105-113. On January 4, 2008, Plaintiffs voluntarily dismissed their breach of contract and breach of warranty claims. **See** R., Vol. I, pp. 129-131. Plaintiffs also filed a motion to amend to add a claim for punitive damages against Westfalia. **See** R., Vol. I, pp. 132-134. All of the above motions were heard by the district court on January 25, 2008. **See** Tr., Vol. I, pp. 1-86. At the hearing and without briefing the issue, U.S. Dairy requested permission to join in Westfalia's motions for summary judgment based upon the economic loss rule. **See** Tr., Vol. I, p. 70. Over Plaintiffs' objections, the court permitted U.S. Dairy to join Westfalia's motion. **See** Tr., Vol. I, p. 73.

The district court denied Defendants' motions for summary judgment, finding that Plaintiffs had stated claims for damages to property, and there were sufficient issues of fact to preclude summary judgment. **See** R. Vol. I, pp. 175-177. The district court then entered an order approving interlocutory appeal by permission. **See** R., Vol. I, pp. 159-163. This Court granted Defendants' motion for permission to appeal the district court's denial of Defendants' summary judgment motions. **See** R. Vol. I, pp. 164-165. Defendants filed an initial notice of appeal and an amended notice of appeal on May 1, 2008. (**See** R., Vol. I, pp. 166-171, 178-184), and Plaintiffs filed a notice of cross-appeal on May 2, 2008. **See** R., Vol. I, pp. 185-189.

C. Statement of Facts

Plaintiffs are owner-operators of the Double A Dairy located in the Twin Falls area. Defendant Westfalia is controlled by a European conglomerate known as GEA. **See** R. Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit B to Aff., Foster Dep. 7:7-12). Westfalia is one of the largest manufacturers of milking equipment components in the world. The ProFORM Pulsation Control System ("ProFORM System") is manufactured by Westfalia. The specialized equipment components of this pulsation system are complex, have specified electrical wiring requirements, and can only be installed by dealers trained and certified by Westfalia. Defendant U.S. Dairy is the sole authorized and certified dealer representative for Westfalia in Idaho. Plaintiffs purchased several million dollars of ProFORM System milking equipment components for their Double A Dairy.

The ProFORM System was designed in the 1970's and was intended to accommodate dairies with smaller milking parlors. **See** R. Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit B to Aff., Foster Dep. at 18:21-20:1). While the smaller parlors contain double 10 or 12 configurations for milking, the modern Double A Dairy has double 50 configurations in each of its four parlors/pits. (A double 12 contains 24 milking stalls while a double 50 has 100 milking stalls.) A complex system of pulsators control milking in this system. Each pulsator contains two coils. Rather than containing 48 coils per parlor (as would be the case with a double 12), the double 50 has 200 coils per parlor. This means substantially increased electrical loads on the milking system. All Westfalia did to adjust to modern dairy size needs was to essentially quadruple the number of pulsators that were controlled by the coils. Unfortunately for Plaintiffs and the dairy industry, this resulted in electrically overextending the pulsation system and caused the pulsators to malfunction. **See** R., Vol. I, p. 193, Exhibits, Neubauer Aff. 5, 1/4/08. The

result of the malfunction was damage to the cows and decreased milk production. Westfalia did not test its overextended system to determine whether it would function properly without damaging cows. **See** R. Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit A to Aff., Snyder Dep. 20:15-19).

The ProFORM System purchased by Plaintiffs for the Double A Dairy was negligently designed, constructed and installed by Westfalia and/or U. S. Dairy. **See** R., Vol. I, pp. 60-61, ¶¶ 25-34. Each individual pulsator that makes up part of the pulsation control system contains two coils that, when energized, create an electric magnetic effect that causes a metal plunger to activate. When de-energized the plunger falls. This process alternatively allows vacuum or atmosphere into the pulsation system that in turn operates to milk the cow. **See** R., Vol. I, p. 193, Exhibits, Neubauer Aff. 3, 1/4/08. When Westfalia overextended its milking equipment system to attempt to accommodate a modern dairy such as Double A, it caused the pulsators to malfunction. Id. at 4–5. This in turn caused physical injury to the cows. Contrary to the statements of Defendants, Plaintiffs specifically pled that the malfunctioning equipment was "causing damage to Plaintiffs' dairy cows due to poor and/or inadequate wiring designed and/or installed by defendants." **See** R., Vol. I, p. 59, ¶24; **see also** R., Vol. I, p. 60-61, ¶¶ 27, 30-31.

Westfalia representatives conceded that malfunctioning pulsators cause physical injury to dairy cows. One such witness was Jeffrey Snyder who was in charge of coordinating training for Westfalia dealers regarding the ProFORM System. **See** R. Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit A to Aff., Snyder Dep. 17:7-15). Another Westfalia representative was Earl Patterson, a co-defendant and the Westfalia ProFORMance Sales Specialist for Westfalia. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit C to Aff., Patterson Dep. 17:4-17). Patterson "went through quite a bit of training" when he joined Westfalia to learn the "technical

aspects" of what he was selling. *Id.* at 16:24-17:3. Snyder and Patterson left no doubt that malfunctioning pulsators injure cows:

- Milk letdown occurs in conjunction with the letdown hormone known as oxytocin. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit A to Aff., Snyder Dep. 27:22-28:5). When inadequate milk letdown occurs "you don't get the full level of oxytocin, the letdown hormone, so the cow holds her -- her milk and [it] is not released for harvest." *Id.* It is essential that the dairy cow be properly milked out to prevent inadequate milk letdown.
- The pulsation system must work correctly in order "to properly milk the cow." **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit A to Aff., Snyder Dep. 25:12-18). "[P]roper pulsation is required to milk the cow without injuring her." *Id.* at 30:2-15. An improperly functioning pulsation system can "injure the ...cow's teats or udder" which leads to increased somatic cell counts and reduced production. *Id.* at 26:1-23, 27:10-20. The ProFORM Pulsation system is direct acting with a piston arrangement which is supposed to have a ratio of milking and rest to relieve milk from the cow without injuring her. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit C to Aff., Patterson Dep. 23:20-24:5). If the ratio is too aggressive and "you're trying to remove the milk too quickly" the cow can be damaged by "a breakdown of the teat canal, of the tissue thereof." *Id.* at 24:6-19.
- Clinical evidence of injury to cows from improperly functioning milking equipment includes increased somatic cell count, increased mastitis and decreased milk production. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit

C to Aff., Patterson Dep. 25:18-26:21). Increased somatic cell count appearing in milk tests results in lower quality milk and reduced prices.

Larry Neubauer is one of Plaintiffs' experts and is a licensed Master Electrician. He has investigated over 1000 dairy farms for electrical issues affecting dairy cows. **See** R., Vol. I, p. 193, Exhibits, Neubauer Aff., 1/4/08 (Exhibit A to Aff., Report of Lawrence C. Neubauer, p. 1). Mr. Neubauer investigated the Westfalia milking equipment at Double A Dairy. He concluded the pulsators malfunctioned and damaged the dairy cows as evidenced by increased somatic cell count, decreased production and decreased quality of milk. **See** R., Vol. I, p. 193, Exhibits, Neubauer Aff., 1/4/08 (Exhibit A to Aff., Report of Lawrence C. Neubauer, p. 9–10). Plaintiffs also have engaged two veterinarians who have rendered opinions that the cows have suffered injuries from the malfunctioning pulsators.

Michael Behr, Ph.D., an agricultural economist, has rendered his opinion regarding the damages flowing from the injured cows as manifested by increased somatic cell counts, decreased quality and decreased quantity of milk. **See** R., Vol. I, p. 193, Exhibits, Behr Aff., 1/4/08 (Exhibit A to Aff., Report of Michael Behr, Ph.D., at p. 3). "Capital Loss" to the herd alone amounts to $450 per head x 14,450 cows or $6,502,500. *Id.* at p. 63. It is little wonder that Plaintiffs' damages are so large given the enormous size of the dairy herd. In *Mike Vierstra and Susan Vierstra, d/b/a Vierstra Dairy v. Idaho Power Company* (District Court of the Fifth Judicial District, State of Idaho, in and for the County of Twin Falls, Case No. CV 00-3408), the jury returned an actual damages verdict in excess of $6.6 million for the same type of losses claimed at bar. **See** Appendix, Special Verdict, *Vierstra v. Idaho Power*. In *Vierstra*, the herd size was less than 1500 cows, a factor of at least nine times less than the Double A herd. Given the increased milk prices and the size of the dairy herd, actual damages of $34 million are

verifiable.

At the hearing on January 25, 2008, the lower court announced its ruling denying Westfalia's motion for summary judgment, which motion was based upon the economic loss rule and stated in part as follows:

> So I don't think there's any question in this record as to the fact that the plaintiffs have alleged that their cattle were injured by the property [milking equipment] which was the subject of the transaction; ...
>
> In this case, there clearly was no calamitous event; but there was, in this court's view, a dangerous failure of the product....I note and I have read, in terms of preparing for the motion relative to punitive damages, that agents of the defendants had noted the injuries that may occur to the cattle themselves as a result of defective products. ...
>
> With that said, then, I conclude that the damages here are noneconomic, sufficient, and parasitic to the injury to the cattle to allow this case to proceed to trial.

See Tr., Vol. I, 51:16-20, 52:18-53:10; 54:3-6.

Defendants conceded the following facts relevant to the issue of a "special relationship":

1. Before dealers are allowed to install the ProFORM System they must be certified by Westfalia. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit A to Aff., Snyder Dep. 75:1-76:9). Recertification occurs every five years. *Id.* at 78:3-9.

2. Westfalia knows more about its own equipment than the dairy farmer does and in fact has "superior knowledge" to that of the dairy farmer. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit C to Aff., Patterson Dep. 67:2-16).

3. Westfalia has superior knowledge to that of the dairy farmer regarding the design of its own milking equipment system. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit D to Aff., Schuring Dep. 22:1-5, 9-13, 16).

The above evidence presented by Plaintiffs went unrefuted. U. S. Dairy, Westfalia's

authorized dealer, failed to present any evidence that there was not a special relationship between it and Double A Dairy. In fact, U. S. Dairy never complied with any of the procedural requirements for summary judgment on this issue.

II. STANDARD OF REVIEW

Defendants set forth the incorrect standard of review in their brief. Defendants' proposed standard of review would be proper if the current appeal was not an interlocutory appeal; for instance if the current appeal was taken from a final grant of summary judgment. In such circumstances, the appellate court uses the same standard for reviewing a district court's decision on summary judgment. A party is entitled to summary judgment if "there is no genuine issue as to any material fact and the moving party is entitled to a judgment as a matter of law." I.R.C.P. 56(c). In determining a motion for summary judgment, the court must construe all facts in a light most favorable to the non-moving party and make all appropriate inferences in favor of the non-moving party. *Pratt v. State Tax Commission*, 128 Idaho 883, 920 P.2d 400 (1996).

The current appeal is taken from the "unusual posture" of interlocutory appeal from a district court's denial of summary judgment. *Winn v. Frasher*, 116 Idaho 500, 501, 777 P.2d 722 (1989). As a result, the scope and standard of the Court's review is different from a review of a final order on summary judgment. Plaintiffs address issues regarding the scope and standard of review in more detail in later sections in this brief. (See Infra Section IV.A.2.). The standard of review on an interlocutory appeal is limited. The Court must accept the facts assumed by the district court when denying summary judgment and determine only the pure legal issues properly before the court. *See Winn*, 116 Idaho at 501, 777 P.2d 722 ("Because of the unusual posture of the case, we are constrained to rule narrowly and address only the precise question that was framed by the motion and answered by the trial court.").

III. ADDITIONAL ISSUES PRESENTED ON APPEAL

1. Does this Court have jurisdiction on interlocutory appeal to review the district court's factual findings, including its finding that, viewed in a light most favorable to Plaintiffs, Plaintiffs have stated a claim for injury or damage to their property and resultant parasitic economic loss?

2. Should this Court affirmatively expand Idaho's "economic loss rule" to preclude recovery in tort if the product sold causes damage to other property which may "foreseeably" interact with the product sold?

3. Whether the district court erred in finding there is no evidence of a special relationship between Plaintiffs and Defendants?

4. Whether the district court erred in granting Defendant U.S. Dairy's motion for summary judgment on the issue of a special relationship without receiving any briefing and without U.S. Dairy providing a statement of relevant facts on the issue?

IV. ARGUMENT

A. The Economic Loss Rule Does Not Bar the Recovery of Plaintiffs' Damages in the Current Case.

1. Plaintiffs May Recover Economic Losses that are "Parasitic" to any Injury to Property Other than the Subject of the Transaction.

Under Idaho law, "unless an exception applies, the economic loss rule prohibits recovery of purely economic losses in a negligence action because there is no duty to prevent economic loss to another." *Blahd v. Richard B. Smith, Inc.*, 141 Idaho 296, 300, 108 P.3d 996 (2004) (citing *Duffin v. Idaho Crop Improvement Ass'n.*, 126 Idaho 1002, 1007, 895 P.2d 1195 (1995)); *Tusch Enters. v. Coffin*, 113 Idaho 37, 41, 740 P.2d 1022 (1987); *Clark v. International Harvester Co.*, 99 Idaho 326, 336, 581 P.2d 784 (1978). The origin of the economic loss rule

generally is traced to *Seely v. White Motor Co.*, 45 Cal.Rptr. 17, 403 P.2d 145 (1965), in which the court denied the plaintiff recovery of lost profits allegedly resulting from the failure of a defective truck. The *Seely* court stated the following with respect to economic losses recoverable in tort:

> The distinction that the law has drawn between tort recovery for physical injuries and warranty recovery for economic loss is not arbitrary and does not rest on the 'luck' of one plaintiff in having an accident causing physical injury. The distinction rests, rather, on an understanding of the nature of the responsibility a manufacturer must undertake in distributing his products. He can appropriately be held liable for physical injuries caused by defects by requiring his goods to match a standard of safety defined in terms of conditions that create unreasonable risks of harm. He cannot be held for the level of performance of his products in the customer's business unless he agrees that the product was designed to meet the consumer's demands. A consumer should not be charged at the will of the manufacturer with bearing the risk of physical injury when he buys a product on the market. He can, however, be fairly charged with the risk that the product will not match his economic expectations unless the manufacturer agrees that it will. Even in actions for negligence, a manufacturer's liability is limited to damages for physical injuries and there is no recovery for economic loss alone.

45 Cal. Rptr. at 23, 403 P.2d at 151. Based on this reasoning, the Idaho Supreme Court adopted the economic loss rule in 1974. *Clark*, 99 Idaho at 334–35, 581 P.2d 784 (quoting *Seely*, 45 Cal. Rptr. at 23, 403 P.2d at 151).

Consistent with the reasoning in *Seely*, Idaho law has always recognized as an exception to the economic loss rule that "**economic loss is recoverable in tort as a loss parasitic to an injury to person or property.**" *Duffin*, 126 Idaho at 1007, 895 P.2d 1195 (emphasis added) (citing *Just's, Inc. v. Arrington Constr. Co., Inc.*, 99 Idaho 462, 468, 583 P.2d 997 (1978); *See* Restatement (Second) of Torts § 766C cmt. b ("If there is physical harm to the person or land or chattels of the plaintiff, ... there may be recovery for negligence that results in physical harm .... When recovery is allowed, the loss of expected profits or other pecuniary loss may, in an appropriate case, be recovered as 'parasitic' compensatory damages"). Idaho courts have defined

"economic loss" to include "costs of repair and replacement of defective property which is the subject of the transaction, as well as commercial loss of inadequate value and consequent loss of profits or use," and have defined "property damage" to encompass "**damage to property other than that which is the subject of the transaction.**" *Salmon Rivers Sportsman Camps, Inc. v. Cessna Aircraft Co.*, 97 Idaho 348, 351, 544 P.2d 306 (1975) (emphasis added); *Clark*, 99 Idaho at 332, 581 P.2d 784. Therefore, the question is whether Plaintiffs have suffered damage to property other than that which is the subject of the transaction as defined by Idaho law.

Idaho law is clear: economic losses may be recoverable in tort if a defectively dangerous product causes injury to property other than that which is the subject of the transaction and the economic loss is parasitic to that injury. *Duffin*, 126 Idaho at 1007, 895 P.2d at 1195. Defendants would like to change this clear rule, and seek to do so by way of the current interlocutory appeal. In doing so, Defendants ask this Court to resolve numerous issues which are not appropriate for interlocutory review. In this case, the trial court correctly found that Plaintiffs have pled and the record demonstrates a genuine issue of material fact that Plaintiffs' economic losses are parasitic to injury or damage to Plaintiffs' property, and therefore remediable in tort. This finding is founded upon substantial facts in the record. Therefore, it must be accepted by the Court and cannot be reviewed in the context of an interlocutory appeal.

2. Defendants Improperly Ask the Court to Review the Factual Record and Findings of the District Court.

Appeal from interlocutory orders is allowed in Idaho when the appeal "involves a controlling question of law as to which there is substantial grounds for difference of opinion and in which an immediate appeal from the order or decree may materially advance the orderly resolution of the litigation." I.A.R. 12(a). Rule 12 implements a similar set of procedures and

principles governing interlocutory appeal as its federal counterpart, 28. U.S.C. 1292(b). *Budell v. Todd*, 105 Idaho 2, 3, 665 P.2d 701 (1983). Federal authority is therefore instructive on how I.A.R. 12(a) should be interpreted and applied.

On interlocutory appeal, the Court is only permitted to determine "controlling questions of law." I.A.R. 12(a); *Kindred v. Amalgamated Sugar Co.*, 118 Idaho 147, 149, 795 P.2d 309 (1990). To insure that courts only examine controlling questions of law on interlocutory appeal, the reviewing court must accept the factual findings as set forth by the district court. *Amundsen v. Jones*, 533 F.3d 1192, 1199 n. 3 (10th Cir. 2008), *Barella v. City of Philadelphia*, 501 F.3d 134, 136 n. 2 (3rd Cir. 2007), *Valdes v. Crosby*, 450 F.3d 1231, 1236 (11th Cir. 2006). Therefore, this Court must accept the district court's findings of the facts and pleadings as viewed in the light most favorable to Plaintiffs (the non-moving party) and only answer pure legal questions based upon the factual findings set forth by the district court.

In this case, Plaintiffs' damages consist both of loss or damage to property, injury to Plaintiffs' herd of dairy cows, and damages parasitic to that injury in the form of lost milk production. Contrary to the statements of Defendants, Plaintiffs specifically pled that the malfunctioning equipment was "causing damages to Plaintiffs' dairy cows due to poor and/or inadequate wiring designed and/or installed by defendants." **See** R., Vol. I, pp. 59-61, ¶¶ 24, 27, 30-31. Representatives of Westfalia, Jeffrey Snyder and Earl Patterson, both admitted during their depositions that malfunctioning pulsators will cause injury to dairy cows. Snyder testified that a malfunctioning pulsation system can injure the cow's teats or udders. **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit A to Aff., Snyder Dep. 26:8-10, 17-23). If the pulsation system is not working properly, Patterson testified that the milking equipment in essence is attempting to remove the milk too quickly and in turn causes damage to the cow by

causing "a breakdown of the teat canal, and the tissue thereof." **See** R., Vol. I, p. 193, Exhibits, Whitehead Aff., 1/4/08 (Exhibit C to Aff., Patterson Dep. 24:6-19). This results in an increase in the condition of mastitis in the dairy cows, and increased somatic cell count, which decreases the quality of the milk produced. Eventually, the injured dairy cows suffer also from decreased milk production as a result of the injury. Representatives of both Plaintiffs and Defendants, as well as veterinary doctors engaged by Plaintiffs, have testified that the defective pulsators would in fact cause physical injury to the dairy cows.

Based on this factual record, the district court correctly found that Plaintiffs' claims are not precluded by the economic loss rule and denied Defendants' motion for summary judgment. Consistent with the pleadings and the facts revealed in discovery, the district court held that Plaintiffs have alleged their dairy cows were injured by the defective milking equipment, and held that this injury is a result of a dangerous failure of the milking equipment. Importantly, the court noted the admissions by Mr. Snyder and Mr. Patterson that a malfunctioning pulsation system would cause injury to Plaintiffs' dairy cows. Properly viewed in a light most favorable to Plaintiffs, the district court held that there is at least a genuine issue of material fact as to whether Plaintiffs' dairy cows have suffered physical injury and whether Plaintiffs' economic losses are parasitic to such injury. The district court held that, as pled by Plaintiffs, this injury is specific property damage and the economic losses due to reduced quality and quantity of milk is parasitic to that property damage. **See** Tr., Vol. I, 54:3-6. This is the established factual basis upon which the current appeal must rest.

In contravention of proper procedure for an interlocutory appeal, Defendants repeatedly invite this Court to reexamine factual findings and to weigh facts in the record in conjunction with the current appeal. Contrary to the district court's determination of the facts in the record

viewed in a light most favorable to Plaintiffs, Defendants repeatedly argue that Plaintiffs did not state a claim for damage to property sufficient to support an award of parasitic economic losses. For instance, Defendants specifically argue that the report of Plaintiffs' expert, Dr. Michael Behr, "conclusively demonstrates that all of the damages sought by the [Plaintiffs] are nothing more than economic losses" and that "[t]here is no expression of a claim for property damage." (App. Br. 16). This argument is directly contrary to the district court's findings of the facts viewed in a light most favorable to Plaintiffs. To resolve this question would require this Court to reexamine the record in the district court and reevaluate the factual foundation upon which this appeal is based.

This Court may not pursue such a broad scope of review on interlocutory appeal. With respect to the scope of interlocutory review, one court stated the following:

> [interlocutory appeals are] intended, and should be reserved, for situations in which the [reviewing court] can rule on a pure, controlling question of law without having to delve beyond the surface of the record in order to determine the facts. The antithesis of a proper [interlocutory] appeal is one that turns on whether there is a genuine issue of fact or whether the district court properly applied settled law to the facts or evidence of a particular case....The legal question must be stated at a high enough level of abstraction to lift the question out of the details of the evidence or facts of a particular case and give it general relevance to other cases in the same area of law.

McFarlin v. Conseco Services, LLC, 381 F.3d 1251, 1259 (11th Cir. 2004). As the United States Supreme Court put it more succinctly, "a question of 'evidence sufficiency,' i.e., which facts a party may, or may not, be able to prove at trial" is not answerable on interlocutory appeal. *Johnson v. Jones*, 515 U.S. 304, 313 (1995).

The restraint exhibited by this Court in *Winn v. Frasher*, 116 Idaho 500, 777 P.2d 722 (1989), reflects the proper limited scope of interlocutory appeal. In *Winn*, the Court recognized that a denial of a motion for summary judgment, the same type of order appealed from in this

case, is generally not reviewable on interlocutory appeal. 116 Idaho at 501, 777 P.2d 722. The Court, however, permitted review but limited the scope of review to answering the abstract legal question posed. As the Court stated, "[b]ecause of the unusual posture of the case, we are constrained to rule narrowly and address only the precise question that was framed by the motion and answered by the trial court." *Id.* The Court therefore answered the abstract legal question presented, but refused to engage in a review of the trial court's factual findings or to apply their ruling on the abstract legal question to the facts as presented by the trial court's findings. *Id.*

As demonstrated by Defendants' "Issues Presented on Appeal," Defendants would have this Court engage in essentially an unlimited review of the district court's decision in this case. Defendants list the following issues for review by this Court:

> A. Whether the district court erred in holding that the economic loss rule did not bar Respondents' tort claims.
>
> * * *
>
> C. Whether the economic loss rule bars recovery in tort when all of the alleged damages are economic losses and there no [sic] losses claimed for damage to other property.
>
> D. Whether there is any evidence of special circumstances or special relationship exempting Respondents from application of the economic loss rule.

(App. Br. 8–9). These issues simply cannot be decided without a reexamination of the record and an in depth review of the district court's factual findings. In fact, Issue C assumes facts that "all of the alleged damages are economic losses and there are no losses claimed for damage to other property," which are **directly contrary to the factual findings made by the district court**. These factual arguments do not reflect the district court's determination of the facts viewed in the light most favorable to Plaintiffs, and they contradict the district court's findings,

which serve as the factual basis upon which this appeal is taken.

The only issue that is sufficiently legal and does not encompass factual issues and findings is the issue of "[w]hether the economic loss rule bars recovery in tort for losses arising from commercial transactions when there is damage to other property, the possibility of which should have been foreseen and made a subject of the transaction if the purchaser wanted to be protected from the risk of such damage and its consequences." (App. Br. 8). As is required by I.A.R. 12(a), however, there is no "substantial grounds for difference of opinion" as to the law in Idaho regarding this issue. There has been a long-standing exception to the economic loss rule in Idaho for economic losses parasitic to particular injury to property. Idaho law is settled in this area. Defendants, however, attempt to inject controversy into the settled law by citing opinions from other jurisdictions. This does not demonstrate a difference of opinion sufficient to support interlocutory appeal. *See Judicial Watch, Inc. v. Nat'l Energy Policy Devel. Grp.*, 233 F. Supp. 2d 16 (D.D.C. 2002)("A litigant cannot create a 'substantial ground for difference of opinion' justifying interlocutory appeal simply by arguing for a particular interpretation or extension of existing law."). Idaho law is clear, and the current interlocutory appeal is not an appropriate vehicle to actively expand the economic loss rule.

The Court must exercise restraint and limit its review to those issues which are appropriate for interlocutory appeal. Factual issues and a review of the district court's factual findings are not appropriate for an interlocutory appeal. Moreover, interlocutory appeal is not an appropriate means for seeking expansion or reversal of existing law. None of the issues presented by Defendants constitute "a controlling question of law as to which there is substantial grounds for difference of opinion" as required under I.A.R. 12(a). Therefore, the Court should not engage in active reformation of existing established law and should remand the current case

to the district court for trial.

3. Plaintiffs' Losses are Parasitic to Particular Injury to Plaintiffs' Herd and are Recoverable Under Idaho Law.

As the district court found in this case, viewed in a light most favorable to Plaintiffs, the losses claimed by Plaintiffs are parasitic to an identifiable injury to property. As demonstrated above, the district court's finding is not properly reviewable within the current interlocutory appeal. Nevertheless, Plaintiffs will demonstrate that they have pled a specific injury to their dairy cows and parasitic economic loss for which Idaho tort law provides a remedy.

In this case, Plaintiff Double A Dairy contracted to purchase electrical milking equipment to be used in its dairy operations. There should be no question that the Plaintiffs' herd of dairy cows constitute "property other than that which is the subject of the transaction" under Idaho law. Indeed, Defendants do not actually argue in their brief that the herd is not property other than that which is the subject of the transaction between the parties. This is not an "integrated system" case in which a component part causes damage to an integrated system (*Salmon Rivers*, 97 Idaho 348, 544 P.2d 306); nor is this a case in which a defect in a product used in construction of a building or a home causes damage to the building as a whole (*Blahd*, 141 Idaho 296, 108 P.3d 996). Therefore, there is no real issue that the Plaintiffs' dairy cows constitute "other property," and the milking equipment is the property which is the subject of the transaction. The real question is whether the dairy cows have been injured or damaged and whether Plaintiffs' economic loss is parasitic to such injury or damage. As demonstrated below, both questions must be answered in the affirmative, and as such, Plaintiffs may recover their economic losses.

As discussed in detail in the previous section, Plaintiffs' damages consist both of loss or damage to property, injury to Plaintiffs' herd of dairy cows, and damages parasitic to that injury

in the form of lost milk production. The economic loss rule does not preclude Plaintiffs from recovering damages for lost production which is parasitic to an injury to their dairy cows. *Duffin*, 126 Idaho at 1007, 895 P.2d 1195. Defendants argue, however, that the injury to Plaintiffs' dairy cows is not an injury to "other property," but is rather related to Plaintiffs' disappointed expectations regarding the performance of the milking equipment. Again, as discussed previously, it is inappropriate for the Court in the current proceeding to engage in the reexamination of the pleadings, record and factual findings of the trial court necessary to answer this question.

Notwithstanding this fact, it is apparent that Defendants' arguments plainly misrepresent the character of Plaintiffs' claims in this case. As the record demonstrates, Plaintiffs have not only pled a specific physical injury to their dairy cows, but the facts in discovery demonstrate that Plaintiffs' dairy cows were in fact injured by the milking equipment that was manufactured, sold and maintained by the Defendants in a defective condition such that it was unreasonably dangerous to Plaintiffs' property. Such an injury constitutes "property damage" under Idaho law, and Plaintiffs may therefore recover damages parasitic to such injury.

First, contrary to the statements of Defendants, Plaintiffs specifically pled that the malfunctioning equipment was "causing damages to Plaintiffs' dairy cows due to poor and/or inadequate wiring designed and/or installed by defendants." **See** R. Vol. I, pp. 59-61, ¶¶ 24, 27, 30-31). Representatives of Westfalia, Jeffrey Snyder and Earl Patterson, both admitted during their depositions that malfunctioning pulsators will cause injury to dairy cows, including causing a breakdown of the teat canal and tissue. In addition, veterinary doctors engaged by Plaintiffs have testified that the defective pulsators would in fact cause physical injury to the dairy cows. This injury results in an increase in the condition of mastitis in the dairy cows, and increased

somatic cell count, which decreases the quality of the milk produced. Eventually, the injured dairy cows also suffer from decreased milk production as a result of the injury.

Defendants' argument that Plaintiffs' claims for damage to the dairy cows are not in the form of property damage are plainly inaccurate. Plaintiffs' expert Dr. Behr provided opinions regarding Plaintiffs' damages in this case. Dr. Behr places the Plaintiffs' losses into three main categories: (1) reduced milk production, (2) loss of price premiums from reduced milk quality, and (3) loss of dairy capital. **See** R., Vol. I, p. 193, Exhibits, Behr Aff., 1/4/08 (Exhibit A to Aff., Report by Michael Behr, Ph.D. at p. 3). As to capital loss, Dr. Behr states that "[t]he value of the herd is below normal because of its reduced milk production." In an amount of $450 per cow, or $6,502,500. **See** R., Vol. I, p. 193, Exhibits, Behr Aff., 1/4/08 (Exhibit A to Aff., Report by Michael Behr, Ph.D., at p. 63). Although this loss in value may be related to the loss in productivity of the cows over time, this loss is separate and apart from Plaintiffs' claims for lost profits or lost milk production. This capital loss represents a loss in value of the cows as a result of the injury caused by the defective milking equipment. This injury constitutes damage to property other than that which is the subject of the transaction.

Defendants also erroneously argue that this physical injury is merely a result of a failure of the milking equipment to meet commercial expectations. Defendants argue, therefore, that this injury is not cognizable in tort, but is instead subject only to remedies in contract. In support of this argument, Defendants cite language in *Myers* in which the Court found that the plaintiff did not allege property damage because the plaintiff's alleged damages "did not result from a calamitous event or dangerous failure of the product," but instead "arose from the failure of the product to match the buyers' commercial expectations." 114 Idaho at 437, 757 P.2d 695.

As previously discussed, based on the factual record the district court dismissed

Defendants arguments and held that Plaintiffs have in fact alleged their dairy cows were injured by the defective milking equipment. Relying on the above quoted language in *Myers*, the district court held that this injury is a result of a dangerous failure of the milking equipment. The district court held that this injury to the cows is specific noneconomic property damage and the loss in milk production is parasitic to that property damage. This holding is not reviewable on interlocutory appeal, and Defendants arguments that this finding was incorrect are futile. Moreover, this holding properly draws the line between property damage and parasitic loss, which is recoverable in tort, and expectancy damages which are relegated to contract remedies.

The distinctions between *Myers* and the current case demonstrate why the injury to Plaintiffs' dairy herd is "property damage" sounding in tort and not contract. In *Myers*, the plaintiff stated numerous claims, including negligence and strict products liability, related to alleged defects in a feed storage and delivery silo used in the plaintiffs' dairy operations. The plaintiff in *Myers* claimed that the defective feed storage and delivery silo caused reduced quality in the feed which caused a decline in milk production of the herd. Essentially, in *Myers*, the Court held that the plaintiff's claims related to the failure of the product to do what it was purchased to do: properly store feed for the dairy herd. This failure, the Court held, was related to the commercial expectations of the plaintiff and not a legal duty owed by the defendant to consumers to assure that the defendant's products will not cause damage to person or property.

By contrast, in the current case, Plaintiffs' claims do not arise merely out of the failure of the milking equipment to do what Plaintiffs purchased the equipment to do. Instead, Plaintiffs' claims arise from **a specific injury to the herd** caused by the **dangerous defect** in the milking equipment. This injury manifested as **physical damage** caused by the equipment and **recognizable injury to the udders and tissue of the dairy cows**. As a result of and parasitic to

this physical injury, the productivity of Plaintiffs' dairy cows and the quality of the milk produced markedly decreased.

Importantly, the district court specifically noted these distinctions in denying Defendants' motion for summary judgment. As the district court stated:

> So I don't think there's any question in this record as to the fact that the plaintiffs have alleged that their cattle were injured by the property which was the subject of the transaction; and the reason I distinguish this case from both the federal case, *DeVries* and *Myers*, frankly, is that I don't believe in any of those cases – and perhaps the federal case is not directly that way – but in *Myers* and the cases cited in *Myers*, they all involve feed issues, where feed damaged production of milk and where that milk production, being damaged, therefore, caused a loss.

(Tr. 51:16–52:4). This Court simply cannot reexamine the district court's application of *Myers* to the facts of the current case within an interlocutory appeal and Defendants arguments that Plaintiffs' claims should fail under *Myers* are beyond the jurisdiction of this Court.

Moreover, the district court's holding is substantively consistent with general principles of product liability law. As a general matter, "[o]ne who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property ...." Restatement (Second) of Torts § 402A(1) (1965). A claim for such damages sounds in tort, not contract. Under Idaho law, economic losses parasitic to such physical harm caused to the consumer's property are recoverable. *Duffin*, 126 Idaho at 1007, 895 P.2d 1195. The language of *Myers* relating to a "calamitous event or dangerous failure of the product" simply reflects the fact that, for a plaintiff's claims for economic losses to be based in tort, there must be physical harm caused to the plaintiff's property that is the result of an unreasonably dangerous condition of the product. Plaintiffs have overcome this threshold, as demonstrated above, by showing that the milking equipment physically harmed their herd.

Finally, Defendants cite *DeVries v. De Laval, Inc.*, 2006 WL 1582179 (D. Idaho 2006), in support of their general argument that Plaintiffs' claims are precluded by the economic loss rule. *DeVries* appears to arise out of similar circumstances as are present in the current case, and it is therefore intriguing at first blush. In truth, however, *DeVries* is not helpful to the necessary analysis in the current appeal. First, *DeVries* is an unpublished opinion from a federal magistrate judge, and therefore carries little precedential value. Moreover, the opinion provides no insight as to what facts the record contained regarding the plaintiffs' claims for injury to the plaintiffs' dairy cows, nor does it specify what facts the court determined were important to its ultimate holding. Therefore, the record in *DeVries* cannot be compared with the record in the current case. Most importantly, comparing the record in the current case to the record in **any** previous case is not an appropriate inquiry for this Court on interlocutory appeal. Therefore, Defendants' reliance on *DeVries* is misplaced.

As set forth above, Plaintiffs have demonstrated a physical injury to their property. Idaho law has consistently drawn a bright-line between losses that are parasitic to injury or damage to "other property" and those which are the result of shortcomings in the performance of the product sold. Here, Plaintiffs' claims arise out of injury and damage to Plaintiffs' property as a result of a dangerous defect in the milking equipment. Therefore, Plaintiffs' claims arise out of Defendants' duty as a manufacturer and seller of the milking equipment to take care that the products they sell will not be unreasonably dangerous and will not cause injury to person or property. Thus, this duty and Plaintiffs' claims are based solely in tort and are not precluded by the economic loss rule.

B. The Court Should Not Expand the Economic Loss Rule to Preclude Recovery of Plaintiffs' Losses.

1. Defendants Failed to Present Arguments for the Proposed Expansion of the Economic Loss Rule at the Trial Court.

Defendants' only purely legal argument relates to whether this Court should expand Idaho's economic loss rule to preclude recovery for property damage and parasitic economic loss when it is "foreseeable" that the purchased product will interact with the damaged property at the time of the purchase. In making this argument, Defendants rely heavily on the analysis from two fellow state supreme courts in *Neibarger v. Universal Cooperatives*, 486 N.W.2d 612 (Mich. 1992) and *Grams v. Milk Prod's, Inc.*, 699 N.W.2d 167 (Wis. 2005). Defendants never made this argument for the expansion of the economic loss rule, nor did they cite the *Grams* or *Neibarger* decisions at the district court level. Therefore, Defendants are attempting to apply this expanded "foreseeability" analysis to the economic loss rule for the first time on appeal. It is axiomatic that the Idaho Supreme Court "will not consider arguments raised for the first time on appeal." *Allen v. Reynolds*, 145 Idaho 807, 186 P.3d 663, 668 (2008). Consistent with well-established Idaho law, this Court must not consider Defendants' "foreseeability" argument, which was raised for the first time in the context of the current interlocutory appeal.

First, because Defendants' "foreseeability" arguments were not raised to the district court, the district court clearly could not have considered Defendants' proposed "foreseeability" expansion in denying summary judgment. It is inappropriate for Defendants to ask this Court to overturn the district court's denial of summary judgment for reasons which were never before the district court for adjudication in the first place.

More importantly, the question of foreseeability of harm or damages is a question of fact for the jury. *Hunter v. State Dept. of Corrections*, 138 Idaho 44, 49, 57 P.3d 755 (2002); *Appel v.*

LePage, 135 Idaho 133, 137, 15 P.3d 1141 (2000). Even if this Court accepts the Defendants' foreseeability analysis, a jury must determine issues of fact relevant to whether it was foreseeable that Plaintiffs' herd would be injured by the milking equipment. Defendants attempt to argue, without any factual basis, that such an injury is foreseeable, and Plaintiffs' claims for economic losses should therefore be excluded under their expanded version of the economic loss rule. However, there has been no discovery or factual development directly on this issue, nor is there any record to speak of in the district court as to whether the injury to Plaintiffs' herd is "foreseeable" in the context of Defendants' proposed new rule. Defendants cannot be allowed to alter the rules in midstream to the obvious detriment of Plaintiffs.

Moreover, as a purely legal matter, Defendants present no reason why Idaho's well-established precedent regarding the economic loss rule and the "other property" exception should be altered or discarded in the first place. "[T]he rule of stare decisis dictates that we follow it, unless it is manifestly wrong, unless it has proven over time to be unjust or unwise, or unless overruling it is necessary to vindicate plain, obvious principles of law and remedy continued injustice." *Houghland Farms, Inc. v. Johnson*, 119 Idaho 72, 77, 803 P.2d 978 (1990), *Greenough v. Farm Bureau Mut. Ins. Co. of Idaho*, 142 Idaho 589, 592, 130 P.3d 1127 (2006). Defendants ignore the constraints of stare decisis and hastily argue for a sweeping expansion of the economic loss rule. Defendants do not and cannot argue that Idaho's established precedent on the economic loss rule is manifestly wrong or unjust. As demonstrated below, the current precedent is properly tailored to conform to sound policies and principles underlying product liability law and the origin of the economic loss rule. Therefore, there is no basis for any argument that the established rule is at odds with clear principles and policies of the law.

Defendants' brief plainly begs an important question: why does the economic loss rule

need to be expanded? No sound reason has been provided. Again, Defendants are plainly attempting to inject controversy into a well-established rule of Idaho law and improperly utilize interlocutory appeal to challenge established Idaho law. Defendants dive into an analysis of their proposed "foreseeability" expansion without even discussing why they believe the rule should be changed in the first place. As demonstrated below, there is no colorable reason in support of an expansion of the economic loss rule beyond its well-reasoned boundaries as established by existing Idaho precedent. More importantly, Defendants have completely failed to make the threshold showing that the established Idaho precedent needs a reworking. Therefore, Defendants' arguments for an expansion of the economic loss rule must be rejected.

2. Expansion of the Economic Loss Rule is Inconsistent with the Fundamental Principles of Product Liability and Tort Law and Would Allocate the Risk of Economic Loss Resulting from Dangerous Defects in Products to the Consumer.

Defendants' only purely legal argument in the current appeal improperly seeks to expand the economic loss rule where there is no difference of opinion as to Idaho law. As previously demonstrated, under well-established prior Idaho law, Plaintiffs' claims for damages are recoverable in tort. (See Infra Sections IV.A.1. & 2.). Defendants, however, propose that the Court affirmatively expand Idaho's economic loss rule to preclude recovery for Plaintiffs in the current case. As discussed in more detail below, Defendants proposed expansion of the economic loss rule is completely undefined and fails to provide any discernable rule or workable standard which could be applied consistently by lower courts.

In addition to being undefined, Defendants' proposed expansion of the economic loss rule is directly at odds with sound public policy and basic principles of product liability and tort law. Defendants' arguments in support of their proposed expansion of the economic loss rule

originate in language from the *Neibarger* and *Grams* cases in which the courts held that the economic loss rule should apply when "preventing the subject risk was one of the contractual expectations motivating the purchase of the defective product." *Grams*, 699 N.W.2d at 534. Defendants therefore propose to expand the economic loss rule to preclude recovery for losses if the purchased product "is expected and intended to interact with other products and property" and it causes damage to that other property. *Id.* at 535. In addition to providing a wholly unworkable standard, the proposed expansion is inconsistent with important public policy considerations which form the basis of product liability law.

As a matter of public policy, products liability law is designed to encourage the manufacture of safer products by placing the responsibility to reduce the hazards of dangerously defective products on the manufacturer, which is the party most capable of diagnosing and preventing possible defects and dangers. *Saratoga Fishing Co. v. J.M. Martinac & Co.*, 520 U.S. 875, 881 (1997); *East River Steamship Corp. v. Transamerica DeLaval, Inc.*, 476 U.S. 858, 866-67 (1986). According to this sound policy, "the seller, by marketing his product for use and consumption, has undertaken and assumed a special responsibility toward any member of the consuming public who may be injured by it...that public policy demands that the burden of accidental injuries caused by products intended for consumption be placed upon those who market them ...." Restatement (Second) of Torts § 402A, cmt c. Defendants propose an expansion of the economic loss rule that, contrary to this well-accepted public policy, would place the risk of losses flowing from property damage caused by a defective product at the feet of the consumer.

Citing the *Grams* case, Defendants argue that the economic loss rule should preclude liability if a product is expected and intended to interact with other property. Defendants in fact

go so far as to espouse a rule which would "simply bar[] tort claims in commercial settings and relegate[]their resolutions to the UCC." (App. Br. 5). This would be a dramatic expansion of the economic loss rule to the detriment of consumers. Under Defendants' expanded interpretation of the economic loss rule, the consumer, not the manufacturer or seller, must become aware of all of the prospective dangers of the products it purchases and the ways in which such products can damage its property. In this case, for instance, Plaintiffs, the operators of a dairy, must not only become familiar with veterinary medicine, but also must be knowledgeable in the area of electrical engineering such that it can understand the operation of the milking equipment and be prepared for any damages a defect might cause.

The responsibility for this kind of intimate knowledge and education regarding products sold in commerce is properly allocated to the manufacturer, who is more familiar with the products it sells. As the court stated in *Seely*, "[a] consumer should not be charged at the will of the manufacturer with bearing the risk of physical injury when he buys a product on the market." 45 Cal. Rptr. at 23, 403 P.2d at 151. As a maxim of product liability law, this risk is best borne by the manufacturer. Therefore, Defendants' proposed expansion is directly contrary to sound public policy and must be rejected.

3. Defendants' Proposed Expansion of the Economic Loss Rule Does Not Promote Any of the Policies Motivating the Adoption of the Rule.

The economic loss rule was adopted in Idaho in order to avoid blurring the line between tort recovery and warranty recovery. *Clark v. International Harvester Co.*, 99 Idaho 326, 333–35, 581 P.2d 784 (1978). Generally, it was crafted to prevent a party from recovering economic losses in tort related to the performance of the product, losses which are within the scope of contract and warranty law. *Id.* Courts have determined that damages which are *purely* economic

losses without any concomitant injury or damage to person or property are most likely attributable to the failure of the product to perform as expected. Therefore, courts have drawn the line that without any other damage or injury to person or property, such economic losses are relegated to the dealings of the parties and to contract or warranty remedies.

On the other hand, "'[t]here can be no doubt that the seller's liability for negligence covers any kind of physical harm, including not only personal injuries, but also property damage...as well as damage to any other property in the vicinity.'" *Id.* at 333 (quoting W. PROSSER, HANDBOOK ON THE LAW OF TORTS, § 101 at 665 (4th ed. 1971)). This liability arises out of a common law duty owed to all consumers who purchase the seller's goods, and is remediable in tort. A negligent party is generally liable for all damages that are the natural and ordinary result of such negligence. *Jacobson v. McMillan*, 64 Idaho 351, 132 P.2d 773 (1943). Therefore, as demonstrated above, Idaho law has permitted recovery of economic losses if they are parasitic to such physical harm to other property. *Duffin*, 126 Idaho at 1007, 895 P.2d 1195. These damages arise directly out of a breach of this very common law duty to protect consumers from injury to person or property. Despite their economic character, therefore, economic losses related to physical harm to person or property do not stem from warranty, but are properly grounded and recoverable in tort.

The exception to the economic loss rule as announced in *Duffin* properly draws the line between contract and tort remedies. It best assures that parties will not be able to collect damages in a tort suit for the failure or breach of a duty that is within the realm of contract. Simply stated, a consumer should "fairly be charged with the risk that the product will not match his economic expectations;" but "[a] consumer should not be charged at the will of the manufacturer with bearing the risk of physical injury when he buys a product on the market."

Clark, 99 Idaho at 334, 581 P.2d 784 (quoting *Seely*, 45 Cal. Rptr. at 23, 403 P.2d at 151.). All damages resulting from that physical injury should therefore be recoverable in tort. The characterization of the loss as economic is not the primary inquiry in the application of the economic loss rule. "'The distinction rests, rather, on an understanding of the nature of the responsibility a manufacturer must undertake in distributing his products.'" *Id.*

The "other property" exception, which allows recovery of economic loss only when it is parasitic to damage or injury to person or property, is a proper expression of the policies underlying the adoption of the economic loss rule. It properly protects against recovery of damages for contract-related claims in tort action by precluding recovery of *purely* economic losses, which courts have viewed as more properly protected by contract law. At the same time, it does not erode or invade on the right of consumers to recover all damages attributable to a manufacturer's or a seller's negligence in a tort action. This rule strikes the proper balance between tort and contract law. As previously demonstrated, Defendants are unable to articulate any reason why this well-established rule should be altered in any way.

Conversely, Defendants' proposed expansion of the rule would erode and invade upon tort law. Simply stated, Defendants' proposed expansion of the economic loss rule is contrary to basic assumptions underlying the relationship between consumer and seller/manufacturer, and it would eliminate remedies which are important to the protection of consumers and their property. Consequently, Defendants' proposed expansion of the economic loss rule does not serve the purposes underlying the adoption of the rule and should be rejected.

4. Defendants' Proposed Expansion of the Economic Loss Rule is Ambiguous and Unworkable and Fails to Provide any Clear Standard.

As stated above, Defendants cite *Neibarger* and *Grams* for their argument in favor of an

expansion of the economic loss rule in Idaho. Defendants argue that the Court should abandon the bright-line standard set forth in *Duffin* and *Myers* allowing recovery of economic losses when they are parasitic to injury to other property. In truth, it is difficult to divine any discernable standard for the scope of the economic loss rule from the arguments Defendants have proposed in their brief. At the very least, it can be said that Defendants, relying on *Grams*, argue the Court should adopt some flexible standard in which the "other property" exception does not include property which is expected to and foreseeably may interact with the product purchased. Defendants provide no definition or direction as to when it is foreseeable that other property may interact with a purchased product, other than that Defendants believe this "foreseeability" caveat should apply in the current case. Defendants' proposed "foreseeability" expansion of the economic loss rule fails to delineate any standard that can be applied from case to case, is undefined and is highly problematic.

First, Defendants' arguments rely heavily on the *Grams* decision from the Wisconsin Supreme Court, a decision that has been subject to broad criticism from judges and commentators for its limitless expansion of the economic loss rule. As the dissenting branch of the Wisconsin Supreme Court on this issue has stated, "[l]ike the ever-expanding, all-consuming alien life form portrayed in the 1958 B-movie classic *The Blob*, the economic loss doctrine seems to be a swelling globule on the legal landscape of this state." *Grams*, 699 N.W.2d at 539 (Abrahamson, C.J., dissenting). Later opinions, noting the globular expansion of the economic loss rule as a result of *Grams*, warn that "jurisprudence continues to devour unsuspecting tort claims that it finds in its path. Like the Blob, the more it eats, the more it grows." *1325 North Van Buren, LLC v. T-3 Group, LTD*, 716 N.W.2d 822 (Wis. 2006) (Bradley, J., dissenting). One commentator observed that, in part as a result of *Grams*, "[o]ver the last decade ... the [economic

loss rule's] application has been radically expanded, narrowing and in some cases effectively eliminating a variety of common law tort causes of action." Cane, R. Thomas & Sullivan, Sheila, *More Litigation to Come: Exceptions to the Economic Loss Doctrine*, 78-NOV Wis. Law. 10, 10 (2005).

Not only has the decision in *Grams* resulted in an elimination of viable common law tort causes of action, it has also resulted in an increased number of published cases in Wisconsin regarding the economic loss rule. *1325 North Van Buren*, 716 N.W.2d at 841 (Wis. 2006) ("Only Florida rivals Wisconsin in its use of the economic loss doctrine")(Bradley, J., dissenting). The dismantling of the economic loss rule in Wisconsin by *Grams*, therefore, has resulted in increased uncertainty as to the meaning of the rule, increased litigation regarding the meaning of the rule at the highest courts in the state, and necessarily, a dramatic increase in litigation costs for consumers. Therefore, the effects of the *Grams* decision are clear: the court's artificial expansion of the economic loss rule eliminated viable and deserving tort claims and created an increase in litigation due to confusion as to the meaning of the rule.

These same dangers are evident in Defendants' attempts to apply *Grams* to preclude Plaintiffs' claims in the current case. As demonstrated above, Plaintiffs have stated a viable claim for economic losses based in tort under established law. It is difficult to determine how Defendants' proposed "foreseeability" expansion would apply in the current case. What types of property damage caused by the milking equipment are "foreseeable"? Is it foreseeable that the milking equipment will interact with the various buildings on the dairy farm? Does this extend to other machinery used in the dairy operations? Where should the Court draw the line?

As the dissent in the *Grams* case discussed, "foreseeability" and "disappointed expectations" must not pollute the inquiry into whether other property has been damaged:

> To my mind, "disappointed expectations" and "other property" are not mutually exclusive principles. Take, for example, a car dealer's defective car that spontaneously lurches backwards even though the motor has been properly turned off. The defective car driving in reverse destroys the garage door. Since the expectation is that the car will operate only when engaged, will not be self-operating in reverse, and will not spontaneously destroy anything behind it, the majority opinion's disappointed expectations rule would, if applied literally, bar recovery in tort for damage to the garage door.

Grams, 699 N.W.2d at 185 (Abrahamson, C.J., dissenting). As Chief Justice Abrahamson continued, this "interpretation of the 'other property' exception is so narrow that it is unworkable; almost nothing will qualify for the exception. If applied literally, the majority's articulation of the "other property" exception might completely eliminate the exception to the economic loss doctrine." *Id.* at 184. There is simply no way to adopt a workable standard based on Defendants' arguments in this case.

On the other hand, as stated above, Idaho law as set forth in *Duffin* and *Myers*, has established essentially a bright-line and highly manageable rule: if the defective condition causes injury to property other than the product purchased, that injury sounds in tort and economic losses parasitic to that injury are recoverable. This rule is practical and manageable, and it provides a standard which can be applied easily from case to case. On the other hand, Defendants' "foreseeability" standard has no explicit bounds and cannot be applied consistently from case to case. Courts, therefore, will not be able to apply this foreseeability standard without engaging a fact-intensive and case-by-case analysis of the intent and considerations of the parties at the time of the transaction. Defendants' proposed "foreseeability" analysis would leave the courts without a discernable standard with which to apply the economic loss rule.

Defendants have failed to provide any persuasive reason to throw the economic loss rule into flux. The expansion Defendants argue for is inconsistent with fundamental policies of

product liability and tort law. Furthermore, the expansion does not promote any of the policies motivating the adoption of the economic loss rule. Under these circumstances, the Court should not affirmatively expand the economic loss rule.

5. Other Courts have Considered and Rejected the Defendants' Proposed Expansion of the Economic Loss Rule.

As stated previously, Defendants rely primarily on the *Grams* and *Neibarger* cases in arguing for expansion of the economic loss rule. When faced with the same or similar arguments, numerous other courts have considered and rejected the approach of the *Grams* and *Neibarger* courts espoused by Defendants in the current case. *See 2-J Corp. v. Tice*, 126 F.3d 539 (3d. Cir. 1997); *Gunkel v. Renovations, Inc.*, 822 N.E.2d 150 (Ind. 2005); *Mariposa Farms, LLC v. Westfalia-Surge, Inc.*, No. CIV-03-0779, 2005 WL 6104101 (D. N.M. 2005); *Hamilage Farms, L.L.C. v. Westfalia-Surge, Inc.*, No. 4:01CV3327, 2003 WL 1824932 (D. Neb. 2003); *Pacific Indemnity Co. v. Whaley*, 2008 WL 3914896 at * 3 (D. Md. 2008)("I am not persuaded ... that the Maryland courts would apply the 'foreseeability' . . . approach . . . ."). As the court in *2-J* stated, "[w]e are aware that a number of courts ... have ruled that the economic loss doctrine bars tort recovery where the 'other property' damaged was always likely to have been injured upon the failure of 'the product' itself. However, it is also true that numerous courts have rejected this expansion of the economic loss doctrine. We find the latter cases more pursasive .,." 126 F.3d at 544 n. 4 (citations omitted).

Like Idaho, Kansas has adopted the economic loss rule. *Prendiville v. Contemporary Homes, Inc.*, 83 P.3d 1257, 1259-60 (Kan. Ct. App. 2004). Also like Idaho, Kansas courts allow recovery of economic loss when there is physical damage to other property. *Elite Professionals, Inc. v. Carrier Corp.*, 827 P.2d 1195 (Kan. Ct. App. 1992); *Northwest Arkansas Masonry, Inc. v.*

Summit Specialty Prods., Inc., 31 P.3d 982, 987 (Kan. Ct. App. 2001) (*citing Saratoga Fishing*, 520 U.S. 875, 879). Kansas courts have generally faced the same types of issues Idaho courts have faced with respect to the scope and application of the economic loss rule. *See, e.g., Prendiville*, 83 P.3d at 1264 (holding that damage to one portion of a home caused by defective construction of another portion is barred by the economic loss rule because the home is one product); *Blahd*, 141 Idaho at 301, 108 P.3d 956 (same). Experience in Kansas, like Idaho, has shown that this approach best equips courts with the capability to address issues raised by the economic loss rule and best reconciles the underlying policies which cause tension in the rule.

In general, sound application of basic tort based principles such as causation and duty can eliminate confusion and avoid the apparent need for an artificial expansion of the economic loss rule as devised by Defendants in this case. The approach taken by the *Neibarger* and *Grams* courts and for which Defendants argue here is not the best approach. The favorable approach, other states have found, is one which reconciles policies underlying product liability law with those underlying the principles which precipitated the adoption of the economic loss rule in the first place. Additionally, the favored approach must adopt a standard which can be applied consistently. Settled Idaho law as expressed in *Duffin* reflects such an approach. The expansion to the economic loss rule for which Defendants argue in this case, therefore, must be rejected.

C. Genuine Issues of Fact Exist Regarding Exceptional Circumstances or a Special Relationship as an Exception to the Economic Loss Rule.

Regardless of the Court's determination of the issues relating to the "other property exception," there has been a long-standing exception to the economic loss rule where a "special relationship" exists between the parties. *Duffin*, 126 Idaho at 1007, 895 P.2d 1195; *McAlvain v. General Ins. Co. of America*, 97 Idaho 777, 554 P.2d 955 (1976). Generally, the case law

permits recovery of economic losses in tort actions when the plaintiff establishes a "special relationship" between the parties. *Id.* A special relationship is one in which it would be equitable to impose a duty upon the defendant to exercise due care to avoid purely economic loss and allocate the risk of such loss to the defendant. *Duffin*, 126 Idaho at 1007, 895 P.2d 1195.

In the current case, the lower court determined that there were not sufficient facts to send the current case to the jury regarding the special relationship exception to the economic loss rule. Defendants now argue that there is no evidence of exceptional circumstances or a special relationship in the record. As demonstrated below, there is ample evidence of a special relationship in the record that demonstrates a genuine issue of material fact regarding the existence of a special relationship. If the Court reexamines the record with respect to the district court's findings regarding damage or injury to property as Defendants suggest, the Court must also review the district court's determination of the special relationship issue. Upon such a review, it is apparent that summary judgment on this issue was not proper.

As an initial matter, the existence of a "special relationship" as an exception to the economic loss rule in this case involves numerous questions of fact. As to the existence of a legal duty, courts in Idaho have held that a special relationship exists "where an entity holds itself out to the public as having expertise regarding a specialized function, and by doing so, knowingly induces reliance on its performance of that function." *Blahd*, 141 Idaho at 301, 108 P.3d 996 (citing *Duffin*, 126 Idaho at 1008, 895 P.2d 1195). In such cases where there is no legally established special relationship, i.e. a doctor/patient or attorney/client relationship, the existence of a special relationship necessarily involves questions of fact to determine whether the entity holds itself out to the public as having sufficient expertise and whether it knowingly induces reliance on such expertise. *See Blickenstaff v. Clegg*, 140 Idaho 572, 578, 97 P.3d 439

(2004)(holding that genuine issues of fact regarding the existence of a special relationship precluded summary judgment); *General Fire & Cas. Co. v. Guy Carpenter & Co, Inc.*, 2006 WL 3239365 (D. Idaho 2006)("there exist genuine issues of material fact as to whether [the defendants] were in a special relationship such that the economic-loss rule would not apply").

The court's analysis in *Duffin* demonstrates that the determination of whether a special relationship exists in this context inherently involves questions of fact. In *Duffin*, the court engaged in a factual analysis to determine whether a special relationship existed, including reviewing the facts related to whether the defendant held itself out as having specialized expertise to induce reliance on that specialized expertise by the public. *Duffin*, 126 Idaho at 1008, 895 P.2d 1195. This determination is inherently factual, and cannot be made without a proper review of the factual record.

Eventually, in *Duffin* the court found that a special relationship existed between the plaintiffs, a family farm, and the Idaho Crop Improvement Association ("ICIA"), an organization authorized by the state to certify agricultural products. The plaintiffs sued the ICIA alleging negligence in the certification of certain seed. In finding the existence of a special relationship, the court stated the following:

> Although *McAlvain* dealt with the existence of a professional or quasi-professional relationship, we do not limit the "special relationship" exception exclusively to such cases. ICIA has held itself out as having expertise in the performance of a specialized function; it is the only entity which can certify seed potatoes in the state of Idaho. ICIA knows that seed is sold at a higher price based on the fact that it is certified. Indeed, it has engaged in a marketing campaign, for the benefit of its members, the very purpose of which is to induce reliance by purchasers on the fact that seed has been certified. Under such circumstances, ICIA occupies a special relationship with those whose reliance it has knowingly induced.

Duffin, 126 Idaho at 1007, 895 P.2d 1195.

Similar circumstances as those described in *Duffin* are present in the current case. For instance, before dealers are allowed to install the ProFORM milking system they must be certified by Westfalia, and must be recertified every five years. Furthermore, it is uncontroverted that Westfalia has superior knowledge regarding the operation of the ProFORM system, and is more knowledgeable regarding the ProFORM system than dairy farmers such as the Plaintiffs in this case. There is uncontroverted testimony from Mr. Patterson that dairy farmers trust and rely upon Westfalia about how to repair and install the ProFORM system.

The above facts demonstrate at the very least a genuine issue of material fact regarding the existence of a special relationship between Plaintiffs and Westfalia. Indeed, Plaintiffs are the only party to present any facts relevant to determining the special relationship issue. In their brief to this Court, and in the limited briefing on summary judgment, Defendants simply relied on blanket conclusory statements that no evidence of a special relationship exists. As demonstrated above, this is flatly contrary to the facts in the record.

Contrary to the district court's finding and Defendants' arguments here, there is substantial evidence of a special relationship between Plaintiffs and Westfalia. This evidence demonstrates a genuine issue of material fact for trial. Therefore, Plaintiffs should be permitted to take their claims of a special relationship to a jury.

D. The District Court Erred in Granting U. S. Dairy's Oral Motion for Summary Judgment Without Briefing or Factual Statements in Support.

Each of the original Defendants in this case, Freedom Electric, Inc., Westfalia, Earl Patterson and U.S. Dairy, filed separate motions for summary judgment in this case. Westfalia's motion and briefing argued that Plaintiffs' claims are barred by the economic loss rule and by the *Myers* case, and that the special relationship exception to the economic loss rule does not apply

to this case. **See** R., Vol. I, pp. 99-104, 147-151. Defendant U.S. Dairy, however, filed its own motion for summary judgment, which was explicitly limited to Plaintiffs' breach of contract and breach of express or implied warranty claims. **See** R., Vol. I, pp. 105-113. U.S. Dairy provided absolutely no briefing as to the issue of the economic loss rule at the district court level, and made no statement of relevant facts regarding its relationship with Plaintiffs. For the first time at the hearing on January 25, 2008, U.S. Dairy's counsel argued that Plaintiffs' claims against U.S. Dairy were barred by the economic loss rule. For the first time, U.S. Dairy argued that there is no special relationship between Plaintiffs and U.S. Dairy, and raised evidence and argument which was well beyond the scope of its motion for summary judgment and not set forth in its statement of relevant facts in support of its motion for summary judgment.

Particularly, on the issue of special relationship, U.S. Dairy completely failed to provide any factual basis from which the district court could analyze the relationship between Plaintiffs and U.S. Dairy; counsel simply stated during the argument, without briefing or reference to a factual record, that "[w]ith respect to the special relationship, I agree with Westfalia." **See** Tr., Vol. I, 25:5–6. U.S. Dairy's "me too" approach ignores the fact that, even if Westfalia demonstrated there was not a sufficient factual record to send the issue of special relationship between Plaintiffs and **Westfalia** to a jury, those facts have absolutely nothing to do with the facts regarding the relationship between Plaintiffs and U.S. Dairy.

Despite the fact that U.S. Dairy had not filed a motion for summary judgment on the issue of the economic loss rule or the existence of a special relationship, the district court allowed U.S. Dairy to make arguments on these matters. Although Plaintiffs had no opportunity to make arguments as to the factual record, the district court entered summary judgment in favor of U.S. Dairy finding that there were no facts which would suggest a special relationship.

Idaho Rules of Civil Procedure require that the motion with supporting affidavits and facts and a supporting brief be served at least 28 days prior to the hearing on summary judgment. I.R.C.P. 56(c). Summary judgment motions must be decided upon the relevant facts as shown in the record, not upon facts which might have been shown. *Verbillis v. Dependable Appliance Co.*, 107 Idaho 335, 689 P.2d 227 (1984). The procedure for summary judgment requires a party to present its factual and legal bases for summary judgment so that the opposing party may have an opportunity to respond. In this case, Plaintiffs had no opportunity to respond to U.S. Dairy's "me too" motion at the hearing.

While the court may rule for either party, and may even grant summary judgment in favor of the non-moving party when appropriate, a district court may only rule on the issues placed before it pursuant to a valid motion. *Harwood v. Talbert*, 136 Idaho 672, 677, 39 P.3d 612 (2001). In *Thomson v. Idaho Ins. Agency, Inc.*, 126 Idaho 527, 887 P.2d 1034 (1995), the plaintiff sued the defendant for negligence. The defendant filed for summary judgment, claiming there was no genuine issue of fact regarding the issues of duty and breach. Although the district court found that genuine issues of fact existed as to the issues of duty and breach, the court *sua sponte* entered summary judgment in favor of the defendant, finding that there were no genuine issues of material fact regarding the issue of proximate causation. In overturning the district court's entry of summary judgment, the Court stated the following:

> This Court has consistently held that when a party moves for summary judgment, the initial burden of establishing the absence of a genuine issue of material fact rests with that party. Thus, it follows that if the moving party fails to challenge an element of the nonmovant's case, the initial burden placed on the moving party has not been met and therefore does not shift to the nonmovant. In the present case, not only was there no evidence showing a lack of proximate cause, but no argument was even offered to the district court on this element of negligence by respondents. The district court improperly seized upon the proximate cause issue *sua sponte*. The burden never shifted to [the plaintiffs] to provide evidence of

> proximate causation because the respondents never raised the issue in the first place.

Thomson, 126 Idaho at 531, 887 P.2d 1034. The same is true of the district court's grant of summary judgment in favor of U.S. Dairy on the issue of special relationship in this case.

U.S. Dairy never filed a motion for summary judgment on the issue of the economic loss rule. Moreover, U.S. Dairy never submitted a statement of facts or a factual record relevant to the relationship between Plaintiffs and U.S. Dairy. Plaintiffs never had an opportunity to respond to any arguments U.S. Dairy may present regarding the existence of a special relationship. As many courts have found, this opportunity to respond is a matter of due process. *Portsmouth Square, Inc. v. Shareholders Protective Committee*, 770 F.2d 866, 869 (9th Cir. 1985)(holding that due process requires that "the party against whom [summary] judgment was entered had a full and fair opportunity to develop and present facts and legal arguments in support of its position.").

The only support U.S. Dairy presented for its "motion" were conclusory statements that it believes a special relationship does not exist. U.S. Dairy did not even discuss the facts pertaining to its specialized knowledge of the milking equipment or Plaintiffs' reliance on such knowledge. As such, U.S. Dairy never met its initial burden of showing a lack of genuine issues of fact, and therefore failed to shift the burden to refute that showing to Plaintiffs. Under these circumstances, as was the case in *Thomson*, the district court "improperly seized upon" the issue of special relationship between Plaintiffs and U.S. Dairy and improperly entered summary judgment against Plaintiffs. The district court's holding as to special relationship between Plaintiffs and U.S. Dairy, therefore, must be overturned.

V. CONCLUSION

For the above and foregoing reasons, this case must be remanded for trial. As a threshold matter, Defendants invite the Court to engage a scope of review that is beyond the Court's jurisdiction on interlocutory appeal. Additionally, as a substantive matter, Plaintiffs have stated a valid tort-based claim for property damage and economic loss parasitic to that property damage. Plaintiffs' claims for such damages are therefore not precluded by the economic loss rule. Furthermore, Defendants' arguments for expansion of the economic loss rule must be rejected. Finally, there are factual issues precluding summary judgment on the issue of special relationship, and the district court's grant of summary judgment in favor of Defendants on this issue, especially in favor of US Dairy who had not filed a summary judgment issue pertaining to this issue, constitute error. The Court must therefore reject Defendants' arguments and remand the case for trial.

DATED this 15th day of September, 2008.

PEDERSEN and WHITEHEAD

By _____
Jarom A. Whitehead, ISB #6656
Attorney for Respondents/Cross-Appellants

CERTIFICATE OF SERVICE

Jarom A. Whitehead, a resident attorney, hereby certifies that on the 15th day of September, 2008, he caused two true and correct copies of the within and foregoing RESPONDENTS'/CROSS-APPELLANTS' BRIEF to be forwarded with all required charges prepaid, by the method(s) indicated below, to the following:

Robert A. Anderson
Matthew O. Pappas
Anderson, Julian & Hull, LLP
P. O. Box 7426
Boise, ID 83707-7426
(208) 344-5510 (Facsimile)
raanderson@ajhlaw.com (E-Mail)
mpappas@ajhlaw.com (E-Mail)
Counsel for U.S. Dairy Systems

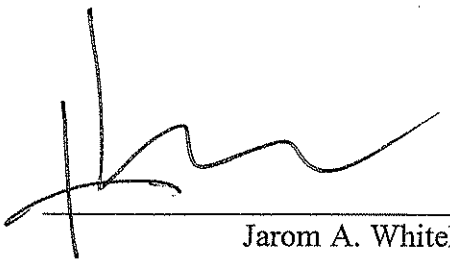
[✓] U.S. Mail
[ ] Overnight Courier
[ ] Facsimile Transmission
[✓] E-Mail Transmission
[ ] Hand Deliver

Thomas B. High
Benoit, Alexander, Harwood,
High & Valdez, LLP
P. O. Box 366
Twin Falls, ID 83303-0366
(208) 734-1438 (Facsimile)
high@benoitlaw.com (E-Mail)
Counsel for WestfaliaSurge, Inc.
and Earl Patterson

[✓] U.S. Mail
[ ] Overnight Courier
[ ] Facsimile Transmission
[✓] E-Mail Transmission
[ ] Hand Deliver

Brice A. Tondre
Brice A. Tondre, P.C.
215 S. Wadsworth Blvd, Ste 500
Lakewood CO 80226
(303) 986-4857 (Facsimile)
briceatondrepc@msn.com (E-Mail)
Counsel for WestfaliaSurge, Inc.
and Earl Patterson

[✓] U.S. Mail
[ ] Overnight Courier
[ ] Facsimile Transmission
[✓] E-Mail Transmission
[ ] Hand Deliver



Jarom A. Whitehead

APPENDIX

IN THE DISTRICT COURT OF THE FIFTH JUDICIAL DISTRICT OF THE
STATE OF IDAHO, IN AND FOR THE COUNTY OF TWIN FALLS

MIKE VIERSTRA and SUSAN VIERSTRA, d/b/a VIERSTRA DAIRY,

Plaintiffs,

vs.

IDAHO POWER COMPANY,

Defendant.

Case No. CV-00-3408

SPECIAL VERDICT

We, the jury, answer the questions submitted to us in this Special Verdict as follows:

QUESTION NO. 1: Was there negligence on the part of Idaho Power Company which was a proximate cause of the Vierstra's claimed damages?

ANSWER: X YES _____NO

If you answered the above question "Yes," please continue. If you answered the above question "No," please skip Questions 2, 3, 4, 5, and 6, and go to Question No. 7.

QUESTION NO. 2: Do you find any negligent act or acts of defendant, to have occurred after August 11, 1997?

ANSWER: X YES _____NO

QUESTION NO. 3: Was there negligence on the part of the Plaintiffs Mike Vierstra and Susan Vierstra doing business as Vierstra Dairy, which was a proximate cause of their claimed damages?

ANSWER: X YES _____NO

QUESTION NO. 4: Do you find other individuals such as Steve Dahlquist or Steve Foust negligent and, if so, such individual's negligence was a proximate cause of plaintiffs' damages?

ANSWER: ____YES X NO

As to those persons you find to be negligent, you are asked to determine the percentage of fault for that party or person, and enter the percentage on the appropriate line. If you find one of the listed parties or persons is not negligent, place a zero next to that party or person. Your total percentages must equal 100%.

QUESTION NO. 5: What is the percentage of fault (if any) you assign to each of the following:

To Idaho Power Company	85 %
To Plaintiffs Mike and Susan Vierstra	15 %
To others (Steve Dahlquist or Steve Foust)	Ø %
Total must equal	100 %

QUESTION NO. 6: What is the total amount of compensatory damages sustained by the plaintiffs Mike Vierstra and Susan Vierstra doing business as Vierstra Dairy from August 11, 1997, to December 31, 2003, as a result of negligence?

ANSWER: $1,170,175 80/

QUESTION NO. 7: Did the defendant, Idaho Power Company create a nuisance which proximately caused plaintiffs' claimed damages?

ANSWER: X YES ____NO

If your answer to Question No. 7 is "No," then do not answer Questions 8, 9, 10, 11, 12, or 13, but go to Questions 14 and 15, and answer them, if applicable. If your answer to Question No. 7 is "Yes," please continue.

QUESTION NO. 8: Do you find any act by defendant Idaho Power, which proximately caused the nuisance, occurred after August 11, 1996?

ANSWER: X YES _____NO

QUESTION NO. 9: If you found that Idaho Power Company created a nuisance which proximately caused plaintiffs' claimed damages, is such nuisance abatable/correctable?

ANSWER: X YES _____NO

QUESTION NO. 10: Did the plaintiffs lose profits as a result of nuisance from January 1, 1997, to December 31, 2003?

ANSWER: X YES _____NO

If your answer to Question No. 10 is "No," please continue but do not answer Question No. 11. If your answer to Question No. 10 is "Yes," please continue, and answer Question No.11.

QUESTION NO. 11: What amount of profits did the plaintiffs lose as a result of nuisance from January 1, 1997, to December 31, 2003 (remember you can't award damages for both negligence and nuisance for the same period of time)?

ANSWER: $1006.379 58/

QUESTION NO. 12: Did the plaintiffs suffer interference with their enjoyment of their property and with the enjoyment of their lives while using the property, as a result of nuisance from January 1, 1997, to December 31, 2003?

ANSWER: X YES ____ NO

If your answer to Question No. 12 is "No," please skip Question No. 13. If your answer to Question No. 12 is "Yes," please continue.

QUESTION NO. 13: What amount of money do you award to compensate the plaintiffs for the interference with their enjoyment of their property and with the enjoyment of their lives while using the property, as a result of nuisance from January 1, 1997, to December 31, 2003?

ANSWER: $ 210,000

If, but only if you found Idaho Power negligent, and its negligence proximately caused damage to the plaintiffs (Question No. 1), may you consider punitive damages, and answer the next questions.

QUESTION NO. 14: Were any of the acts of Idaho Power which proximately caused damage to the plaintiffs, an extreme deviation from reasonable standards of conduct, wanton or grossly negligent, such that you wish to assess punitive damages against the defendant, Idaho Power Company?

ANSWER: X YES ____ NO

If you answered Question No. 14 "No," please sign the verdict. If you answered Question No. 14 "Yes," please answer Question No. 15.

QUESTION NO. 15: What is the total amount of punitive damages that should be awarded the plaintiffs in order to punish the defendant and deter the defendant and others from engaging in similar conduct in the future?

ANSWER: $ 10,000,000

DATED this 10th day of February, 2004.

Presiding Juror

Nikki Donnelley

Carol L. Lerga

Mary Ellen Smart

Slip Copy, 2006 WL 1582179 (D.Idaho), 60 UCC Rep.Serv.2d 154

Motions, Pleadings and Filings

United States District Court,
D. Idaho.
Abraham DeVRIES, an individual; Curtis Devries, an individual; and Marvin Devries, an individual, Plaintiffs,
v.
DeLAVAL, INC., a Delaware corporation; Blue Diamond DeLaval LLC, dba Dairy Services, a Delaware limited liability company, Defendants.
No. CV 04-136-S-EJL.
June 1, 2006.

REPORT AND RECOMMENDATION

MIKEL H. WILLIAMS, Magistrate Judge.

INTRODUCTION

***1** Plaintiffs Abraham DeVries, Curtis DeVries, and Marvin DeVries (collectively "DeVries") filed this action against Defendants DeLaval, Inc. and Blue Diamond DeLaval, LLC (collectively "DeLaval"), alleging claims for breach of contract, strict liability, and fraud. Currently pending before the Court for its consideration are the following motions:

(1) Defendants' Motion for Summary Judgment (Docket No. 23), filed on January 5, 2006; and

(1) Plaintiffs' Motion to Amend/Correct to Add Claim for Punitive Damages (Docket No. 32), filed on January 6, 2006. On March 24, 2006, the Court heard oral argument on the motions.

Having reviewed all briefing submitted, as well as other pertinent documents in the Court's file, the Court enters the following Report and Recommendation as follows.

REPORT

I.

Background

Plaintiff Abraham "Abe" DeVries is the owner of a large dairy operation in the state of California. In 1998, he started the DeVries Dairy Facility near Kuna, Idaho and funded the startup of a dairy operation for his two sons, Plaintiffs Curtis and Marvin DeVries in the same area. Curtis DeVries, in partnership with his father operates his dairy farm under the name of Carousel Farms. Marvin DeVries, also in partnership with his father, operates his dairy farm under the name of Syringa Farms. Both Carousel Farms and Syringa Farms share the DeVries Dairy Facility although both the operations are maintained separately.

In May 1998, Abe DeVries agreed to purchase a rotary milking system manufactured by DeLaval. (Purchase Agreement). The purchase price for the dairy equipment, including installation of that

equipment, was $599,999. Abe DeVries purchased the equipment at a discount price because this was the first DeLaval rotary system installed in the region and DeLaval hoped it would help with their marketing in this area.[FN1] Soon after the DeVries began milking cows with the DeLaval dairy equipment, they began to experience problems with the equipment. The DeVries' complaints focused primarily on problems relating to the vacuum system, milk-line, takeoffs and related components. As the equipment was not working correctly, it was causing some injury to the cows' udders, which resulted in related "mastitis" infections, which had to be treated by a veterinarian.

> FN1. Plaintiff Abe DeVries testified that he obtained a substantial discount for the purchase of the system from DeLaval. His other two bids were at least $700,000 higher than DeLaval.

In the early months of 2000, DeLaval engaged in extensive efforts to remedy the problems the DeVries had been experiencing. The DeVries asked the DeLaval technicians to examine and repair the automatic milk machine take-offs, computer ID system, sort gate, the shield on the rotary and the design flaw that allowed the cows to consistently break stalls on the rotary. Despite the technicians' efforts, the DeVries continued to experience problems with the DeLaval dairy equipment.

In November 2000, in an effort to remedy the continuing problems, representatives of DeLaval met with Curtis DeVries, Marvin DeVries, and other members of the DeVries family to discuss how to resolve the problems caused by the dairy equipment. Ultimately, the DeVries and DeLaval executed settlement agreements in February 2001 entitled "Releases" by which DeLaval agreed to remove the ALPRo system then installed at the DeVries dairy and replace it with new equipment as detailed in Exhibit B attached to the Release ("New Equipment"). Exhibit B described the New Equipment as: (1) 60 Right-hand EcoDetachers; (2) 60 Detacher controls/valves; (3) 60 Pulsators with individual controls; and (4) a four-amp power supply. In addition, DeLaval agreed to provide:

***2** • Cash payments of $150,000 to Curtis DeVries, $50,000 to Marvin DeVries, and $50,000 to Abe DeVries, for a total of $200,000 in cash payments.

• A $69,999 credit to Abe DeVries to cover the remaining amount due to DeLaval for the system.

• Payment of up to $8,370 to a third party fo the cost of moving a piece of equipment.

• Free standard scheduled service for the New and Original Equipment for one year, and a 10% discount of such service for two more years.

• DeLaval also agreed to supply all of the DeVries' needs for cleaners, sanitizers, teat dips, liners and filters for a period of three years after the date the Releases were signed-at no charge the first year.

In exchange, Curtis and Marvin DeVries signed a release agreement with DeLaval as follows:

That he releases and gives up any and all claims and rights, known and unknown, which he now has or may have in the future against Dealer or DeLaval or any of their officers, employees or affiliated companies including, but not limited to claims for breach of warranty, misrepresentation, lost income, lost milk production, injury to cattle, increased expenses, or consequential damages of any kind caused by or related in any way, directly or indirectly, to the installation, use, operation or maintenance of any of the Original Equipment.

Abe DeVries executed a similarly worded release. In defining "Original Equipment," the release documents reference the original Purchase Agreement, which itemizes the equipment installed.

In addition, the DeVries agreed that the New Equipment would be covered by DeLaval's standard one-year Limited Warranty, which the parties agreed to extend to a term of three years. The Limited Warranty warrants the equipment to be "free from defects in material and workmanship." Through

the Limited Warranty, DeLaval agreed to repair or replace any item of Equipment which was not as warranted. If DeLaval was unable to repair the equipment, it agreed to refund the purchase price (excluding the cost of installation labor). The Limited Warranty further excluded any other remedies, specifically precluding the DeVries from recovering damages of any kind in excess of a refund of the purchase price refund remedy.

The DeVries maintain that they only signed the release agreements because they "were desperate to fix the problems with the dairy," (Pl's.Rsp.Br.4), as they had allegedly suffered more than $1.5 million in damages at the time they entered into the Releases. During the time the DeVries and DeLaval were negotiating the release agreement, the DeLaval told the DeVries that it was committed to making the dairy equipment work properly. The DeVries further allege that DeLaval assured them that they would make the equipment work "no matter what it took, and no matter what the cost ." (Pl's.Rsp.Br.3.) According to the DeVries, they reasonably believed that DeLaval had taken the necessary steps to ensure the recommended changes in the dairy system would cause it to function properly in the future based on DeLaval's assurances and because the "DeLaval dairy equipment was fully integrated and had been designed, manufactured and installed by DeLaval." *Id.* The DeVries state they relied upon DeLaval's representations that it would solve the continuing problems with the dairy equipment.

***3** DeLaval began the installation of the New Equipment after the execution of the three Releases. The installation purportedly took much longer than anticipated by the DeVries. Without inspecting the facility, Mr. Steve Ramer, a DeLaval employee in the Kansas City location, had earlier recommended the installation of the EcoDetachers. The DeVries allege that Mr. Ramer was aware that DeLaval had experienced significant problems with the EcoDetachers at the time he recommended their installation at the DeVries' already problematic dairy facility. In support of this contention, the DeVries cite to an April 11, 2001 email sent by Mr. Ramer to Mr. Storm, in which Mr. Ramer wrote, "Universal has never design[ed] an option for a remote start circuit for an EcoDetacher in a parlor.... There are a number of design steps that must be taken prior to this work being done ... [f]ailure to take these steps almost insures there will be problems later." *See* Kurtz Aff., Ex. D, Ex. 18. According to the DeVries, DeLaval never informed them of this potential problem.

In further support of their allegation that DeLaval improperly installed the EcoDetachers despite its alleged problems, the DeVries refer to another internal email sent on June 13, 2001 by Mr. Storm to Bill Thompson, then Vice-President of DeLaval. Mr. Storm informed Mr. Thompson in the email that the DeVries were experiencing problems with the EcoDetachers and that Mr. Ramer had informed him that morning that "this was not a new problem" and that the problem had been going on for 3-4 months. *See* Kurtz Aff, Ex. D, Ex. 16. Mr. Storm continued, "[i]t would have been nice if someone could have given us some warning of this problem before we were blind sided out at this particular dairy." *Id.*

The next day, on June 14, 2001, DeLaval sent an in-house veterinarian, Jeff Durkin, to test the system. Durkin informed the DeVries that the system appeared to be functioning properly. The DeVries maintain Durkin did not mention any potential problems with the EcoDetachers at this time. In addition, another DeLaval employee, Jim Hipwell, purportedly conducted pulsation tests that indicated the equipment fluctuated beyond acceptable levels and that this could cause damage to the dairy cow teats. DeLaval allegedly did not inform the DeVries of this problem; instead, DeLaval criticized the DeVries' dairy practices, calling the DeVries "a bunch of whiners" and poor managers who could not be pleased. (Hipwell Depo. 62: 18; 64:17-20, Ex. C to Kurtz Aff.).

The DeVries further allege that the newly installed DeLaval equipment never functioned properly, although the DeVries concede DeLaval made repeated attempts to solve the problems through March of 2002. Despite DeLaval's attempts to fix the problems, the DeVries maintain that both Curtis and Marvin's dairy operations continued to experience high bacteria counts in their milk. Apparently, the DeVries saw the somatic cell counts ("SCC") increase from the range of approximately 300,000 to 700,000 to 900,000 SCC. The expected SCC for a dairy operation in Southern Idaho is less than 200,000 with a SCC number higher indicative of injuries to the dairy herd.

***4** The DeVries' complaints are not limited to the dairy equipment. The DeVries also allege that

DeLaval supplied the DeVries' dairy farms with mislabeled and defective farm chemicals in order to fulfil DeLaval's obligation to supply chemical and supplies free of charge for the first year to the DeVries pursuant to the terms of the Release. Chris Rich, an employee of DeLaval, testified in his deposition that DeLaval's General Manager, Tom Storm, had instructed him to mix expired or nearly expired teat dips with differing levels of iodine (a main ingredient in teat dip) in a container for another brand of teat tip. (Rich Depo. 51-53, Ex. A to Kurtz Aff). Mr. Storm allegedly instructed Mr. Rich to "dump" the expired teat dip on the DeVries. It is undisputed that the mislabeling of teat dip violates the Federal Food Drug & Cosmetics Act and is a misdemeanor. 21 U.S.C. § 331, et seq.

On March 15, 2002, the DeVries informed DeLaval that they had decided to purchase chemicals and supplies from another company because of the problems of continually high SCC counts, the extensive teat damage, and the high incidence of mastitis, which persisted even with the New Equipment. The DeVries maintain that the SCC counts and the mastitis in the cows began to decrease and the sediment problems were reduced after they discontinued the use of DeLaval products.

On March 28, 2002, Mr. Ramer drafted a "Milker Service Bulletin" to be sent to DeLaval Dealers regarding the dismantling and reinstallation of certain part, including the replacement of diaphragms and relocation of the milk valve, to ensure the EcoDetacher system would function properly. It does not appear that the DeVries waited for DeLaval to upgrade their EcoDetacher system. Instead, the DeVries recruited Norm Zuidema of Valley Equipment Co., Inc. out of Ontario, California to come to the DeVries Dairy Facility to evaluate the system.[FN2]

FN2. Mr. Zuidema had sold dairy equipment to Abe DeVries' California dairy operation. He has also been designated an expert witness by the DeVries.

Valley Equipment's first inspection revealed that the vacuum fluctuation for the DeLeval equipment was substantially in excess of acceptable industry maximum fluctuation standards, which resulted in substantially more "squawking" in that barn than would be expected of an operation that size. Mr. Zuidema opines that because the fluctuations in the vacuum he observed exceeded industry standards to such a degree that cows milked on that system would have suffered extreme discomfort during the milking process. After further tests and attempts to fix the problems with the milking system, Valley Equipment recommended that the automation and pulsation equipment be replaced because DeLaval had been unable to make the equipment work properly. The new equipment recommended by Valley Equipment was installed in March 2003.

Furthermore, Valley Equipment recommended the installation of a 4" stainless steel pipeline to replace the 3" stainless steel pipeline that was currently installed in order to allow the dairy facility to operate at an appropriate level. The original Purchase Agreement had provided that DeLaval would install a 4" stainless steel pipeline.

***5** Apparently, with the installation of the 3" pipeline, the wash-up system installed by DeLaval did not function properly. When a wash-up system does not function properly, it is likely to cause of a build-up of bacteria in the milk system. Because of this, Valley Equipment made the decision to replace the wash-up system. The total cost for the work performed and the equipment supplied by Valley Equipment was $419,874.29. The DeVries contend that since the changes made by Valley Equipment, the injuries to the cows manifested by the high somatic cell counts have steadily and significantly been reduced and milk production has greatly increased.

On July 2, 2003, DeLaval sent a letter to Abraham DeVries offering to pay $51,554 as the full purchase price of the EcoDetachers, power supplies and pulsators. The DeVries refused the offer, arguing that this figure did not represent the full purchase price of the equipment installed pursuant to the Releases. In his deposition, Tom Storm estimated the cost of the equipment to be $90,000. (Storm Dep. 122:6, Ex. B to Points Aff.). Furthermore, the DeVries allege that they have suffered more than $1.5 million in damages caused by the defective DeLaval equipment. Thus, they suggest damages should be the value of those claims less the amount of approximately $300,000 paid to the DeVries.

II.

Motion for Summary Judgment

A. Standard of Review

When reviewing a motion for summary judgment, the proper inquiry is whether "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed.R.Civ.P. 56(c) (1993). A moving party who does not bear the burden of proof at trial may show that no genuine issue of material fact remains by demonstrating that "there is an absence of evidence to support the non-moving party's case." *Celotex Corp v. Catrett*, 477 U.S. 317, 325, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). Once the moving party meets the requirement of Rule 56 by showing either that no genuine issue of material fact remains or that there is an absence of evidence to support the non-moving party's case, the burden shifts to the party resisting the motion who "must set forth specific facts showing that there is a genuine issue for trial." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 256, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986). It is not enough for the [non-moving] party to "rest on mere allegations of denials of his pleadings." *Id.* Genuine factual issues must exist that "can be resolved only by a finder of fact because they may reasonably be resolved in favor of either party." *Id.* at 250.

"When determining if a genuine factual issue ... exists, ... a trial judge must bear in mind the actual quantum and quality of proof necessary to support liability." *Id.* at 249-250. "The mere existence of a scintilla of evidence in support of the [defendant's] position will be insufficient; there must be evidence on which the jury could reasonably find for the [defendants]." *Id.*

***6** The Ninth Circuit has consistently applied the standard for granting summary judgment. *Musick v. Burke*, 913 F.2d 1390 (9th Cir.1990); *Pelletier v. Federal Home Loan Bank*, 968 F.2d 865 (9th Cir.1992); *Bieghler v. Kleppe*, 633 F.2d 531 (9th Cir.1980).

In determining whether a material fact exists, facts and inferences must be viewed most favorably to the non-moving party. To deny the motion, the Court need only conclude that a result other than that proposed by the moving party is possible under the facts and applicable law. *Aronsen v. Crown Zellerbach*, 662 F.2d 584, 591 (9th. Cir.1981).

The Ninth Circuit has recently emphasized that summary judgment may not be avoided merely because there is some purported factual dispute, but only when there is a "genuine issue of material fact." *Hanon v. Dataproducts Corp.*, 976 F.2d 497 (9th Cir.1992).

In order to withstand a motion for summary judgment, the non-moving party:

(1) must make a showing sufficient to establish a genuine issue of fact with respect to any element for which it bears the burden of proof; (2) must show that there is an issue that may reasonably be resolved in favor of either party; and (3) must come forward with more persuasive evidence than would otherwise be necessary when the factual context makes the non-moving party's claim implausible.

British Motor Car Distrib. Ltd. v. San Francisco Automotive Indus. Welfare Fund, 882 F.2d 371 (9th Cir.1989).

B. Analysis

DeLaval moves for summary judgment on several grounds. DeLaval first argues that all but one of the DeVries' claims for breach of contract and strict liability are barred by the Releases executed in February 2001 since the problems reported by the DeVries relate to the Original Equipment Installed

by DeLaval. Second, DeLaval argues that the DeVries' remaining claim relating to the pulsators (New Equipment) is subject to DeLaval's limited warranty providing only for repair, replacement, or refund of the purchase price. DeLaval asserts that it offered to refund the purchase price of the New Equipment it installed and argues that it has satisfied its obligations under the Limited Warranty with respect to the pulsators. Finally, DeLaval argues that DeLaval's strict liability claim must fail because the DeVries only seek damages for a purely economic loss, which are barred in products liability actions sounding in tort.

A. The DeVries argue that the releases have no legal effect.

While DeLaval argues that all but one of the DeVries' claims for breach of contract and strict liability are barred by the Releases executed in February 2001, the DeVries contend that DeLaval fraudulently induced them into entering into the February 2001 Releases, therefore the Releases are not enforceable.

Specifically, the DeVries allege DeLaval employees falsely represented that the installation of the New Equipment would solve the problems at the DeVries Dairy Facility and that DeLaval remained committed to making the dairy equipment function properly. Second, the DeVries argue the Releases should be set aside because "DeLaval failed to disclose its knowledge that the EcoDetachers did not function properly." *(See Plaintiffs' Opposition to Defendant's Motion for Summary Judgment, p. 17.)* Third, the DeVries allege DeLaval intentionally delivered mislabeled teat dip after the Releases were signed and that "it is reasonable to infer that [DeLaval] ... intended to deliver the mislabeled teat dip at the time it entered into the Releases." *Id.* In addition, the DeVries argue that DeLaval "fraudulently concealed test results showing the dairy equipment was not functioning during and immediately following the installation of that equipment." *Id.* Finally, the DeVries allege that DeLaval failed to disclose that it had installed a 3" milk line before the Releases were signed, and the President of Delaval, Mr. Maharay, admitted that it did not intend to obtain a release from its obligation to deliver a 4" milk line when he signed the Release in February 2002.

***7** Idaho courts recognize that "[a]n agreement to settle a legal dispute is a contract and its enforceability is governed by familiar principles of contract law. Jeff D. v. Andrus, 899 F.2d 753, 759 (9th Cir.1989). In accordance with standard principles of contract law, a release may be set aside if induced by fraud, undue influence, mistake, or deceit. Mortas v. Korea Ins. Corp., 840 F .2d 1452 (9th Cir.1988); *see also* Heath v. Utah Home Fire Ins. Co., 89 Idaho 490, 491 (1965). Thus, in order to survive summary judgment, the DeVries must establish a genuine issue of material fact that they were fraudulently induced into executing the Releases for those claims based on their arguments that the Original Equipment, as defined in the Purchase Agreement, was defective.

Establishing a claim of fraud requires a plaintiff to prove the following elements:

(1) a representation; (2) its falsity; (3) its materiality; (4) the speaker's knowledge of its falsity or ignorance of its truth; (5) the speaker's intent that it should be acted on by the person and in the manner reasonably contemplated; (6) the hearer's ignorance of its falsity; (7) the hearer's reliance on the truth; (8) the hearer's right to rely thereon; and (9) the consequent and proximate injury.

G & M Farms v. Funk Irrigation Co., 119 Idaho 514, 518, 808 P.2d 851, 855 (1991) (citations omitted). A party alleging fraud must plead with particularity the factual circumstances constituting fraud for each of these elements. *Id.* Once the party alleging fraud reaches trial, it carries the burden of proving each element by clear and convincing evidence. *Id.*

1. Representation that New Equipment Would Solve the Problems at the Dairy Operation

The DeVries contend DeLaval fraudulently induced them into executing the February 2001 releases by representing that the installation of the New Equipment would solve the problems at the DeVries Dairy Facility and that DeLaval remained committed to making the dairy equipment function properly. The DeVries further contend that DeLaval never conducted any analyses or engineering study to determine whether the recommended changes in the dairy equipment would result in the dairy facility functioning properly as DeLaval allegedly promised; thus, DeLaval had no reasonable basis for

believing the installation of the proposed equipment would solve the problems of the DeVries Dairy Operation.

The Court has serious concerns whether the alleged statements made by DeLaval that it "was committed to making the dairy equipment work properly" and it "would do whatever was necessary to make that happen, no matter what it took, and no matter what the cost" may serve as a legitimate predicate for a claim of fraud. As a general rule, fraud cannot be based upon statements promissory in nature that relate to future actions or upon the mere failure to perform a promise or an agreement to do something in the future. Pacific States Auto. Fin. Corp. v. Addison, 45 Idaho 270, 261 P. 683 (1927). The allegedly false representation must concern past or existing material facts. *Moroun v. Wyreless Systems, Inc.*, 141 Idaho 604, 114 P.3d 974 (2005); *see also, In re Syntex Corp. Secs. Litig.*, 95 F.3d 922, 934 (9th Cir.1996) (Predictions proved to be wrong in hindsight do not render the statements untrue when made). Here, DeLaval's alleged statements relate to an event occurring in the future, and thus may not serve as a basis for fraud.

***8** The Court reaches this conclusion despite the DeVries attempt to analogize this case to *G & M Farms v. Funk Irrig. Co.*, 119 Idaho 514, 808 P.2d 1045. In *G & M Farms,* the plaintiff negotiated the purchase of an agriculture irrigation system from the defendant manufacturer and dealer. During the course of the negotiations, the defendant dealer made certain representations to the plaintiff that it would work and that they had "thousands" of these irrigations systems that had been a "great success" and had been operating with no customer complaints. *Id.* at 519, 808 P.2d at 856. While the trial court concluded the dealer's statements could not serve as a basis for fraud because they related to future events, the Idaho Supreme Court reversed, finding that the dealer's failure to disclose known facts relating to the flawed design and likely malfunctioning of the irrigation system fell within the category of intentional misrepresentation cases based on nondisclosure of material information. *Id.* at 520, 808 P.2d at 857.

The Idaho Supreme Court based its conclusion on two indemnity agreements entered into by the dealer indicating the dealer knew the equipment ordered by the plaintiff was not designed for its particular farm and that the irrigation system possessed certain operational characteristics which might cause it to malfunction or shut down under normal conditions. At the time the plaintiff agreed to purchase the irrigation system, only the dealer knew of the operational and design defects and such defects were not readily discoverable to the plaintiff, thus giving rise to the inference that the parties were not dealing on equal footing. Furthermore, the court did not construe the dealer's statements that there were "thousands of these machines around" as mere "trade talk" or "puffing" because the court held that this rule does not apply when the parties are on unequal footing and record indicated there were only twenty-five or thirty of "these machines around" and only four of the precise type the plaintiff purchased-not "thousands."

The Court does not find the circumstances in *G & M Farms* analogous to this case. In *G & M Farms,* the plaintiff submitted two indemnity agreements entered into by the dealer indicating it knew the irrigation system would not work, as well as deposition testimony concerning the extensive troubled history with the irrigation system purchased by the plaintiff. Conversely, in this case, the DeVries rely solely on the fact that DeLaval has not produced any documents demonstrating that DeLaval conducted any analysis or had any basis for believing that it could fix the problems at the dairy. Simply because DeLaval did not conduct an extensive study to determine whether the recommended changes in the dairy equipment would ensure the proper functioning of DeVries dairy facility does not prove that DeLaval believed its equipment would not work, or that it was reckless in believing its equipment would work. The DeVries were obligated to submit sufficient evidence to raise an issue of material fact that DeLaval had no present intention of following through on the representations of which the DeVries complain at the time the statements were made in order for the statements to be actionable. Yet, the DeVries have not submitted any evidence that DeLaval knew the new equipment would not solve the problems at the dairy. Nor have the DeVries submitted any evidence that DeLaval did not intend to keep its alleged promise to do whatever it took and at whatever the cost to ensure the equipment would not work properly. For these reasons, the DeVries may not rely on these alleged statements of future events as a basis for their fraud claim.

2. EcoDetachers

***9** In addition, the DeVries predicate their claim for fraud based on the DeLaval's alleged failure to disclose its knowledge that the EcoDetachers were defective. To prove that DeLaval knew the EcoDetachers were defective, the DeVries submit an April 11, 2001 email wherein Mr. Ramer wrote to Mr. Storm cautioning him regarding the installation of a remote start on the EcoDetachers being installed at the DeVries dairy facility. Specifically, Mr. Ramer wrote in the email, "Universal has never design[ed] an option for a remote start circuit for an EcoDetacher in a parlor. There are a number of design steps that must be taken prior to this work being done ... [f]ailure to take these steps almost insures there will be problems later." *(See* Kurtz Aff, Ex. D, Ex. 18.)

Then, on June 13, 2001, Mr. Storm wrote an email to Bill Thompson stating the DeVries were having problems with the EcoDetachers and that he was informed that morning by Mr. Ramer that "this was not a new problem ... and that it had been going on for 3-4 months." FN3 (Kurtz Aff, Ex. D, Ex. 16.) Mr. Storm continued, "Devries hit us real hard this morning about premature failure on the units already there [sic] comment was 'this is what we expected'.... It would have been nice if someone could have gave us some warning of this problem before we were blind sided out at this particular dairy." *Id.* The installation of the EcoDetachers was completed in July 2001. Nearly a year later, on March 28, 2002, after the DeVries had employed another company to fix the milking system, Mr. Ramer distributed a "Milker Service Bulletin" to all DeLaval dealers regarding the dismantling and reinstallation of certain parts to "upgrade" the EcoDetacher system so that it would function properly.

> FN3. The importance of the email which mentioned problems with the EcoDetachers going back 3 or 4 months is that this would put DeLaval on notice of possible problems with the equipment as early as February 13/March 13, 2001. The Releases were executed on February 28, 2001.

In response, DeLaval maintains that only after the Releases were signed did its employees realize that they may encounter problems with the EcoDetachers at the DeVries' dairy facility. Steve Ramer testified that he probably was the first person to become aware of the problems with the EcoDetachers when he began receiving some calls from dealers. Ramer further testified that when DeLaval begins receiving complaints regarding its equipment, it follows a certain process to determine if the problem is systemic or restricted to a few isolated instances. During the course of this process, DeLaval checks the numbers on the warranty to confirm how many complaints regarding the equipment it had actually received. Then it performs tests on the equipment and contacts the supplier to try to determine the exact nature of the problem. Thus, according to Mr. Ramer, it can take 3-4 months to ascertain whether a significant problem with the equipment actually exists.

In the Court's estimation, the DeVries have failed to show that DeLaval knew the EcoDetachers were defective when they signed the Releases. In fact, Ramer testified he believed the EcoDetachers would work properly at the DeVries dairy facility. Furthermore, DeLaval was able to effectively and promptly remedy the problem by replacing each of the diaphragms, which were causing the problems. Because there is not sufficient evidence to raise a genuine issue of material fact as to whether DeLaval knew the EcoDetachers would not work at the time it signed the Releases, the DeVries may not rely upon the subsequent problems with the EcoDetacher as a basis for their claim of fraudulent inducement.

3. Installed 3" as opposed to 4" Milk Line

***10** The DeVries next argue that DeLaval fraudulently concealed the installation of the 3" milk line when the original Purchase Agreement required the installation of a 4" milk line at the DeVries Dairy. Tom Storm admitted that he knew that only a 3" milk line had been installed at the DeVries Dairy Facility before he signed the February 2001 Releases. According to the DeVries, instead of informing the DeVries of this fact and attempting to correct the problem, Tom Storm engaged in a "cover-up" and attempted to convince the DeVries that the removal of the ALPro system and the installation of the EcoDetachers was all that was needed to correct the problems at the DeVries Dairy Facility.

The Court agrees that the February 2001 Release should not apply to any claim regarding the milk line, assuming the truth of the DeVries' allegations that DeLaval failed to disclose it had installed a 3" milk line rather than the 4" milk line. DeVries had a right to rely on DeLaval's nondisclosure when it agreed to release any claims regarding the milk line. However, the DeVries may not rely upon DeLaval's nondisclosure regarding its installation of a 3" milk line rather than a 4" milk line as a basis for invalidating the Releases in their entirety.

4. Mislabeled Teat Dip

The DeVries also contend DeLaval fraudulently supplied mislabeled teat dip-an udder hygiene product used to sanitize the cow's teats prior to and after milking, which is used to kill bacteria and prevent mastitis and is crucial to a dairy operation. As part of the Release agreement, DeLaval agreed to supply farm chemicals, including teat dip, to the DeVries without charge for a period of one year. The record suggests Tom Storm, DeLaval's General Manager, ordered Chris Rich, an employee, to deliver to the DeVries 250 gallons of teat dip that had expired and was mislabeled in violation of the Federal Food, Drug and Cosmetic Act, 21 U.S.C. § 331. Specifically, Mr. Rich testified that Mr. Storm told him, "[t]his stuff you are going to have a hard time selling. Just take it out to the DeVries' and dump it." *(See* Kurtz Aff., Ex. A, 52:6-23.)

Mr. Rich contacted Bill Vandersluis, the District Sales Manager for DeLaval during the relevant time period, to inform him that he had been instructed to deliver and did deliver mislabeled and expired teat dip. Mr. Vandersluis failed to convey this information to the DeVries and Mr. Vanersluis conceded this failure was "not the right thing to do." *(Id.* 46:9-12.)

While the Court agrees that Mr. Storm's conduct, if true, is especially egregious, it does not necessarily agree with the DeVries' contention that it is reasonable to infer that Mr. Storm planned to "dump" mislabeled and expired teat dip when he signed the Releases. Therefore, the DeVries cannot use this alleged conduct as a basis for their claim that there were fraudulently induced into entering the Releases.

5. Pulsators

Finally, the DeVries argue DeLaval fraudulently concealed the results of the test conducted by Mr. Hipwell indicating that the pulsators were not functioning properly. On June 14, 2001, before DeLaval had completed the installation of the EcoDetachers, DeLaval sent Jeff Durkin, the in-house veterinarian, to test the DeVries dairy equipment. The DeVries allege that Mr. Durkin reported that the equipment was functioning properly and the DeVries suggest Mr. Durkin should have informed the DeVries of the new information Mr. Storm had acquired from Mr. Ramer in the June 13, 2001 email regarding the problems with the EcoDetachers. During this same time period, DeLaval's employee, Jim Hipwell, ran several tests which allegedly revealed that the equipment was fluctuating beyond acceptable levels that could result in physical damage to the dairy cows' teats. However, Mr. Hipwell purportedly did not notify the DeVries of the test results, but instead attributed the problems to the DeVries dairy practices.

***11** Essentially, the DeVries seem to argue that Mr. Hipwell's failure to inform them of the problems with the pulsators, as well as DeLaval's furnishing them with mislabeled teat dip, was part of DeLaval's ongoing fraud to convince the DeVries that it had evaluated the problems at the DeVries' dairy, identified the problems, and knew which remedy would work. However, all of this conduct occurred after the Releases were signed on February 28, 2001 and cannot serve as a basis for fraudulent inducement to execute the Releases.

B. Limited Warranty

DeLaval next argues any claim relating to the New Equipment is subject to the provisions of DeLaval's limited warranty, which limits remedies for complaints about the equipment to repair, replacement or refund of the purchase price. DeLaval maintains it has satisfied its obligation under the limited warranty with its offer to pay the DeVries the amount of $51,554 for the full purchase price of the New Equipment.[FN4] The DeVries, however, respond that DeLaval's attempt to limit the

remedy for the delivery of the defective equipment to repair and replacement or return of the purchase price failed of its essential purpose. As a result of this purported failure, the DeVries argue they are entitled to all the remedies for breach of contract allowed under the Uniform Commercial Code despite the separate provision precluding the recovery of any damages, whether direct, indirect, or consequential.[FN5]

FN4. DeLaval contend that it has expended in excess of $576,000 in direct payments, materials, and equipment to satisfy the DeVries' concerns over the dairy equipment.

FN5. The text of the Limited Warranty reads as follows:

EXCLUSION OF OTHER WARRANTIES

Other than this Limited Warranty * * * **DELAVAL AND SELLER MAKE NO OTHER WARRANTY FOR THE EQUIPMENT OR THE SYSTEM IN WHICH IT IS USED, EXPRESS OR IMPLIED, INCLUDING BUT NOT LIMITED TO THE IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE**

EXCLUSION OF OTHER REMEDIES

THE REMEDIES SET OUT ABOVE ARE THE DAIRY PRODUCER'S (AND IF DIFFERENT, DAIRY OWNER'S) EXCLUSIVE REMEDIES FOR BREACH OF THIS LIMITED WARRANTY. IN NO EVENT SHALL DAIRY PRODUCER (OR DAIRY OWNER) BE ENTITLED TO RECOVER DAMAGES OF ANY KIND, WHETHER DIRECT, INDIRECT OR CONSEQUENTIAL (INCLUDING BUT NOT LIMITED TO DAMAGES DUE TO DELAYS IN DELIVERY, LOSS OF PRODUCTION, LOSS OF PROFIT, LOSS OF PREMIUMS, EXCESS CULLING, INCREASED COSTS OF OPERATION, AND LOSS OF, INJURY TO, OR ILLNESS OF LIVESTOCK) IN EXCESS OF THE PURCHASE PRICE REFUND REMEDY SET OUT ABOVE.

1. Failure of its Essential Purpose

A seller of a product may limit its warranty obligation to the repair and replacement of defective parts. *See* I.C. § 28-2-719(1)(a). However, Idaho Code § 28-2-719(2) *further provides* "where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this act." An exclusive repair or replacement remedy is meant to ensure that a purchaser receives a product free from defects, and if it becomes evident during the warranty period that the product is defective, this triggers the seller's obligation to cure the defective product within a reasonable time. *See Clark v. Int'l Harvester Co.*, 99 Idaho 326, 340, 581 P.2d 784, 798 (1978); *see also* I.C. s 28-2-309(1). "If, however, the seller is subsequently unable or unwilling to repair or replace a defective part within a reasonable time, the buyer is left with a defective product not conforming to the warranty and the limited remedy has not achieved its purpose." *Clark*, 99 Idaho at 340, 581 P.2d at 798. *Proof of negligent or wilful dilatory conduct is not required under* Idaho Code § 28-2-719(2); rather, the section applies even in circumstances where an exclusive remedy seemed fair and reasonable when the contract was executed, "but as a result of later circumstances operates to deprive a party of a substantial benefit of the bargain." *Id. (citing* I.C. § 28-2-719, Official Comment 1). Conversely, a plaintiff must also act in good faith to provide a defendant with a reasonable time to repair or replace defective parts. *Clark*, 99 Idaho at 340, 581 P.2d at 798.

***12** Here, although DeLaval limited its warranty obligation to repairing or replacing defective

parts, if the milking equipment was defective and DeLaval failed to cure those defects within a reasonable time after being afforded an opportunity to do so, it would seem the DeVries would be entitled to pursue their general remedies under the UCC pursuant to I.C. § 28-2-719(2). The Court finds a question of fact exists as to whether the New Equipment provided to the DeVries was defective at the time it was delivered and installed in the DeVries' dairy farms, and, if so, whether DeLaval was able to cure those defects within a reasonable time.

2. Damages

However, this does not necessarily end the inquiry. Assuming the DeVries are able to prove at trial that the warranty to repair or replace defective parts failed of its essential purpose, the issue remains as to what effect the failure of the limited warranty has on the other contractual provisions excluding liability for all other damages. As noted above, the DeVries suggest that the failure of the limited warranty automatically entitles them to "the full array of remedies provided by the UCC, including the recovery of consequential and incidental damages." *Clark*, 99 Idaho at 342 (*citing* I.C. § 28-2-714 and § 715). However, the *Clark* court also recognized that in certain commercial contexts, "the failure of an exclusive remedy does not automatically require disregard of other limitations on liability provided by the agreement." *Id.*

In *Clark*, the plaintiff purchased a tractor for his custom farming business. In the plaintiff's first year of owning the tractor, several breakdowns in the tractor's engine occurred. Under the warranty, the defendant seller repaired the problems free of charge. *Id.* at 330, 581 P.2d at 788. A year and a half after purchasing the tractor, the plaintiff noticed a loss of power in the tractor, which prevented him from working the fall season with its poor field conditions and he was only able to work the tractor on a limited basis in the spring. *Id.* When the defendants failed to remedy the plaintiff's problems with the tractor, the plaintiff filed a claim against the defendants for negligent design and manufacture and breach of implied and express warranties. *Id.* With respect to the breach of warranty claim, the plaintiff argued the exclusive remedy of repair and replacement of defective parts failed of its essential purpose as a result of defendant's failure to repair the tractor in a reasonable time. *Id.* at 338, 581 P.2d at 796.

The *Clark* court found a genuine issue of material fact existed whether the defendants failed to cure the tractor's defect within a reasonable time. The court, however, did not end its inquiry there. Rather, the court considered whether the contractual provision excluding liability for incidental and consequential damages would still be enforceable assuming the failure of the repair or replacement remedy to achieve its purpose. *Id.* at 341, 581 P.2d at 799. To decide this question, the *Clark* court looked to the applicable UCC provisions, as well as to the decisions of other courts, which had also considered this same issue. In conducting this review, the *Clark* court commented, "[t]he majority of the courts in cases involving the failure of an exclusive remedy contained in a warranty provision which also excludes liability for consequential damages have ruled that the provisions limiting liability fail also and that the plaintiffs are entitled to the full array of remedies provided by the UCC, including the recovery of consequential and incidental damages." *Id.* Courts reaching this conclusion reason that sellers " 'cannot at once repudiate their obligation under their warranty and assert its provisions beneficial to them.' " *Id. (quoting Adams v.. J.I. Case Co.*, 261 N.E.2d (1970); *see also Jones & McKnight Corp. v. Birdsboro Corp.*, 320 F.Supp. 39 (N.D.Ill.1970).

***13** Before applying this reasoning to the facts of that case, the *Clark* court also noted that other courts have distinguished this line of cases of not allowing the defendant seller to shelter itself behind the provisions in a warranty, when allegedly repudiating its limited obligations under the same warranty. For example, in *Am. Elec. Power Co. v. Westinghouse Electric Corp.*, 418 F.Supp. 435 (S.D.N.Y.1976), the court upheld a contractual provision limiting liability for consequential damages despite an alleged failure of the exclusive repair or replacement warranty to achieve its purpose. 418 F.Supp. at 458. In *Westinghouse*, the Court felt that a better approach would be to ignore the exclusive remedy clause in the case of its failure "while other clauses limiting remedies in less drastic manners and on different theories would be left to stand or fall independently of the stricken clause." *Id.* at 457 (internal quotation marks and citation omitted). In adopting this approach for that case, the *Westinghouse* court found no reason to disturb the consensual allocation of business risk embodied in the contract, especially in an agreement that was painstakingly negotiated between two

industrial giants over two years, involving "a highly complex, sophisticated, and in some ways experimental piece of equipment." The *Westinghouse* court also found the fact that the plaintiff was still entitled to recover the price of the equipment pursuant to a separate provision in the contract particularly significant; thus, even if the repair and remedy failed entirely, the plaintiff was at least left with a minimum adequate recovery.

The *Clark* court, however, distinguished *Westinghouse* from the case pending before it, reasoning that the tractor was not a highly complex or experimental piece of equipment, but a standardized piece of farm equipment, "which the plaintiffs were fully entitled to expect would be delivered to them free of defects which could not be cured within a reasonable time." Furthermore, the *Clark* court noted there was a significant disparity between the parties and the terms of the contract were contained in printed form and not the result of painstaking negotiations. For these reasons, the *Clark* court concluded:

Under these circumstances a seller who fails to comply with its obligations under the warranty, such as the repair or replacement duties, cannot receive the benefit of the other provisions, which in part at least were premised on the assumption that the seller would fulfill its obligations. The failure of the limited remedy in this case would materially alter the balance of risk set by the parties in the agreement. In such a situation, we conclude that the other limitations and exclusions on the seller's warranties and liability must be disregarded and that the general provisions of the UCC should govern the rights of the parties.

Id. at 343-44, 584 P.2d at 801-02.

The question the Court must answer in this case is whether the circumstances here more closely resemble those in *Clark* or those in *Westinghouse.* In asking this question, the Court may also examine the remedy provisions to determine whether DeLaval's alleged default caused a loss to the DeVries which was not part of the bargained-for allocation of risk. Here, the dairy equipment is arguably more complex than the tractor in *Clark.* However, it does not amount to the highly complex, sophisticated, and in some ways experimental piece of equipment involved in *Westinghouse.* And, while not unsophisticated, the DeVries hardly amount to an industrial giant. Yet, DeLaval also agreed to refund the purchase price of the New Equipment in the case of default, and, thus, the DeVries are not left without a remedy. Nonetheless, the Court finds the facts of this case more analogous to *Clark* than *Westinghouse.* Therefore, the Court recommends that the DeVries be able to pursue their available remedies under the UCC pursuant to I.C. § 28-2-719(2) if they are able to prove that the limited warranty failed of its essential purpose.

C. Strict Liability

***14** DeLaval also moves summary judgment with respect to the DeVries' claim for strict liability on the basis that the DeVries seek recovery of purely economic loss.

While a manufacturer may be held liable for "physical harm" to person or property caused by its defective product, a manufacturer's liability does not extend to encompass purely economic loss. *See, e.g.* *Clark v. Int'l Harvester Co.*, 99 Idaho 326, 333, 581 P.2d 784, 791 (1978). "[A] contrary rule, which would allow compensation for losses of economic advantage caused by the defendant's negligence [or defective product], would impose too heavy and unpredictable a burden on the defendant's conduct." *See, e.g.*, *Just's, Inc. v. Arrington Contr. Co., Inc.*, 99 Idaho 462, 468, 583 P.2d 997, 1003 (1978). The Idaho Supreme Court further articulated the rationale for the economic loss doctrine, quoting *Seely v. White Motor Co.*, 63 Cal.2d 9, 45 Cal.Rptr. 17, 403 P.2d 145 (1965), as follows:

The distinction that the law has drawn between tort recovery for physical injuries and warranty recovery for economic loss is not arbitrary and does not rest on the 'luck' of one plaintiff in having an accident causing physical injury. The distinction rests, rather, on an understanding of the nature of the responsibility a manufacturer must undertake in distributing his products. He can appropriately be held liable for physical injuries caused by defects by requiring his goods to match a standard of safety defined in terms of conditions that create unreasonable risks of harm. He cannot be held for the level

of performance of his products in the consumer's business unless he agrees that the product was designed to meet the consumer's demands. A consumer should not be charged at the will of the manufacturer with bearing the risk of physical injury when he buys a product on the market. He can, however, be fairly charged with the risk that the product will not match his economic expectations unless the manufacturer agrees that it will. Even in actions for negligence, a manufacturer's liability is limited to damages for physical injuries and there is no recovery for economic loss alone. (Citations omitted).

Clark, 99 Idaho at 334, 581 P.2d at 792, *quoting* Seely, 45 Cal.Rptr. at 23, 403 P.2d at 151.

In the context of the economic loss doctrine, the Idaho Supreme Court defines "economic loss" includes "costs of repair and replacement of defective property which is the subject of the transaction, as well as the commercial loss for inadequate value and consequent loss of profits or use, Salmon River Sportsman Camps, Inc. v. Cessna Aircraft Co., 97 Idaho 348, 351, 544 P.2d 306, 309 (1975), while "property loss" includes "damage to property other than which is the subject of the transaction." *Id.*

The DeVries attempt to circumvent the economic loss doctrine by asserting that the DeLaval equipment caused substantial property damage to the DeVries' dairy herd. The Court, however, believes this issue was properly resolved in Myers v. A.O. Smith Harvestore Products, Inc., 114 Idaho 432, 432, 757 P.2d 695, 697 (Ct.App.1988). In *Myers,* the plaintiffs purchased a feed storage and delivery system, which consisted of a silo and power-operated unloading unit, from the defendant seller and defendant manufacturer. The silo failed to function as promised and the hay stored in the silo deteriorated and the plaintiffs' combined dairy herd began to suffer from decreased milk production. The plaintiffs sought help from the defendant seller but the seller was unable to cure the defects. The plaintiffs then filed an action against defendants for, *inter alia,* negligence and strict liability. In affirming the district court's decision to grant summary judgment in favor of defendants as to negligence and strict liability, the *Myers* court noted that the plaintiffs had not "plead any specific damages due to losses in the feed or cattle value." *Id.* at 436, 757 P.2d at 699. Because "[t]he losses suffered as a result of feed deterioration and cattle illness were manifested by income changes brought on by reduced milk production, the court held that the defendants were not liable to plaintiffs in negligence or strict liability as the plaintiffs' claims were for economic losses properly addressed as predicated upon contract claims rather than as tort claims. *Id.*

***15** Despite the DeVries' best efforts to distinguish *Myers* from the circumstances of this case, the Court finds the facts of *Myers* strikingly analogous the facts of this case. As in *Myers,* the damages to the cattle in this case arose from the failure of the product to match the buyers' commercial expectations and were manifested by lost profits and consequential business losses resulting from alleged failures of the milking equipment and decreased milk production. And as in *Myers,* although the DeVries did allege property damage of a sort, the essence of their claim is the loss of a contractual benefit of a properly functioning milking system in addition to consequential damages. "When a loss results from mere product ineffectiveness, it is the law of contracts and commercial transactions, rather than strict products liability, which fixes responsibility for the loss. Myers, 114 Idaho at 436, 757 P.2d at 699 *(quoting* Purvis v. Consolidated Energy Products Co., 674 F.2d 217, 223 (4th Cir.1982). Therefore, as the Idaho Court of Appeals held in *Myers,* the Court finds these economic losses may be properly addressed as predicated upon the contract claims, not in tort.

III.

Motion to Amend

The DeVries seek to amend the Complaint to add a claim for punitive damages. Idaho law permits an amendment to add a claim for punitive damages when the plaintiff has established a reasonable likelihood of proving facts at trial that the defendant acted in a manner that was an extreme deviation from reasonable standards of conduct and that the act was performed by the defendant with an understanding of or disregard for its likely consequences. Weaver v. Staford, 134 Idaho 691, 700, 8

P.3d 1234, 1243 (2000). The justification of punitive damages must be that the defendant acted with an extremely harmful state of mind, whether that be termed "malice, oppression, fraud or gross negligence"; "malice, oppression, wantonness"; or simply "deliberate or wilful." *Highland Enters., Inc. v. Barker*, 133 Idaho 330, 348-349, 986 P.2d 996, 1014-15 (1999). Therefore, to support a motion to add punitive damages under I.C. § 6-1604, the DeVries must establish a reasonable likelihood they could prove by a preponderance of the evidence that DeLaval acted oppressively, fraudulently, wantonly, maliciously or outrageously. *See Vaught v. Dairyland Ins. Co.*, 131 Idaho 357, 362, 956 P.2d 674, 679 (1998). The Idaho courts have defined malice as the general disregard for the truth or falsity of a statement. *Stafford,* 134 Idaho at 700, 8 P.3 d at 1243.

The Court finds that the DeVries have established a reasonable likelihood of proving facts at trial sufficient to support a claim for punitive damages. If the DeVries are able to prove at trial that DeLaval deliberately delivered mislabeled and expired teat dip in violation of the law, and deliberately concealed that it had installed a 3" milk line rather than a 4" milk line in violation of the terms of the original purchase agreement, this would constitute an extreme deviation from reasonable standards of conduct and justify an award for punitive damages.

***16** However, by recommending that the amendment be allowed does not automatically translate into allowing the matter to be presented to the jury. The trial court will be in the best position to evaluate whether the jury should be instructed as to punitive damages after it has heard all of the testimony at the trial. The Court would further recommend that even if the issue of punitive damages is to be presented at the trial, that the trial court consider bifurcating that issue from liability and other damages.

RECOMMENDATION

Based on the foregoing, the Court being otherwise fully advised in the premises, **IT IS HEREBY RECOMMENDED that:**

1) Defendants' Motion for Summary Judgment (Docket No. 23), filed on January 5, 2006, be GRANTED IN PART and DENIED IN PART.

2) Plaintiffs' Motion to Amend/Correct to Add Claim for Punitive Damages (Docket No. 32), filed on January 6, 2006, be GRANTED.

Written objections to this Report and Recommendation must be filed within ten (10) days pursuant to 28 U.S.C. § 636(b)(1) and Local Rule 72.1(b), or as a result of failing to do so, that party may waive the right to raise factual and/or legal objections to the United States Court of Appeals for the Ninth Circuit.

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Not Reported in F.Supp.2d, 2006 WL 3239365 (D.Idaho)

Motions, Pleadings and Filings

United States District Court,
D. Idaho.
GENERAL FIRE & CASUALTY CO. and GF & C HOLDING CO., Plaintiffs,
v.
GUY CARPENTER & CO., INC., Defendant.
No. CV 05-251-S-LMB.
Nov. 7, 2006.

John F. Kurtz, Kim C. Stanger, Hawley Troxell Ennis & Hawley, Boise, ID, for Plaintiffs.

James T. McDermott, Dwain Mark Clifford, Ball Janik LLP, Portland, OR, for Defendant.

MEMORANDUM DECISION AND ORDER

LARRY M. BOYLE, District Judge.

*1 Currently pending before the Court is Guy Carpenter's Motion for Summary Judgment Against GF & C's Claims (Docket No. 37). Having carefully reviewed the record, considered oral arguments, and otherwise being fully advised, the Court enters the following Memorandum Decision and Order.

I.

BACKGROUND

Plaintiff General Fire & Casualty Co. ("General Fire" or "GenFire") is an Idaho insurance company, wholly owned by Plaintiff GF & C (collectively "Plaintiffs"), an Idaho holding company. *Graham Decl.*, ¶¶ 2-3 (Docket No. 32, Att. 3). Defendant Guy Carpenter & Co., Inc. ("Defendant" or "Guy Carpenter") is a reinsurance intermediary incorporated in Delaware with offices in Washington, among other places. *Id.* at ¶ 4.

Reinsurance is "insurance for insurance companies." An insurance company, known in the industry as a primary or ceding company, cedes portions of its liability on risks to another insurance company, known as a reinsurer, to reduce the amount of possible loss incurred by the ceding company. *Plaintiffs' Statement of Facts*, ¶ 3 (Docket No. 36, Att. 1). Reinsurance is used because state statutes require insurers to maintain a certain ratio of policyholder surplus in relation to the amount of risk assumed by the insurer. *Graham Decl.*, ¶ 6 (Docket No. 32, Att. 3).

Reinsurance intermediaries like Guy Carpenter act as the middlemen between ceding insurers and reinsurers. *Id.* at ¶ 7. "A reinsurance intermediary assists the cedant to draw up a reinsurance program and then goes to the reinsurer 'market' to propose the cedant's terms, negotiate with reinsurers, and finalize the terms of the reinsurance agreements." *Id.*

General Fire commenced writing property/casualty insurance policies in January 1999. *Crandall Affidavit*, ¶ 5 (Docket No. 36, Att. 2). Guy Carpenter acted as the reinsurance intermediary for General Fire from 1999 until May 2005. *Graham Decl.*, ¶ 8 (Docket No. 32, Att. 3). GF & C alleges that Guy Carpenter provides services for it as well. *GF & C's Response to Motion for Summary*

Judgment Against GF & C's Claims, p. 3 (Docket No. 42).

Each year from 1999 to 2003, Guy Carpenter designed reinsurance programs that provided excess of loss ("XOL") reinsurance for General Fire policyholder claims in excess of a $1 million working layer of reinsurance (where most of General Fire's claims were expected to occur). *Crandall Afidavit,* ¶ 9 (Docket No. 36, Att. 2). Guy Carpenter recommended that General Fire purchase XOL reinsurance for casualty losses in blocks that provide coverage up to an aggregate limit of $4 million in any one year, with one or more "reinstatements" depending on the year. *Id.*

Each of the casualty XOL reinsurance contracts prepared by Guy Carpenter contains a reinstatement clause that provides for reinstatement of the excess coverage in return for payment of additional premium to the reinsurers. *Id.* at ¶ 10. General Fire understood that it would be required to pay a reinstatement premium to reinstate each successive layer of XOL coverage. *Id.* However, allegedly, there was a misunderstanding as to the nature and timing of the reinstatement premium obligations. *Id.* Based on Guy Carpenter's Loss Scenarios and general discussions, General Fire allegedly understood that it could *elect* to reinstate the XOL reinsurance coverage in exchange for payment of the reinstatement premium *if and when it determined that it needed the additional reinsurance coverage. Id.* at ¶ 11. However, in late 2003, when General Fire contacted Guy Carpenter to ask advice on whether it could exercise its right to reinstate the limits of coverage any time as the losses developed or instead must do so prior to the end of the 2003 accident year, it learned that reinstatement and reinstatement premiums were automatic, not optional elections. *Id.* at ¶ 15; *Dec. 30, 2003, E-mail (Bates Nos. GFC06177-79), Ex. 7 to Crandall Affidavit,* pp. 1-3 (Docket No. 36, Att. 9). Specifically, Guy Carpenter advised General Fire as follows:

*2 Reinstatement is not optional-it is automatic and there is an accompanying charge for it. The reinstatement premium is due when the loss is paid and is usually netted against the paid loss amount ....

...

One way to illustrate reinstatement is you start the year with a bucket filled with water. You dip into it (pay a loss), and the reinsurer immediately fills it back up so you still have a full bucket to deal with the next loss (simultaneously you pay him additional premium for the extra water he topped you off with).

Crandall Affidavit, ¶ 16 (Docket No. 36, Att. 2); *May 28, 2004, E-mail (Bates Nos. GFC10404-09), Ex. 7 to Crandall Affidavit,* pp. 4-9 (Docket No. 36, Att. 9). This advice was accompanied by specific numerical examples showing, allegedly for the first time, that for every dollar paid to General Fire by its reinsurers to cover a loss under the initial 4x1 layer of coverage, the reinsurers would offset or deduct from that payment the amount of premium required to reinstate the coverage whether or not General Fire needed or wanted the reinstatement at that time. *Crandall Affidavit,* ¶ 16 (Docket No. 36, Att. 2).

After receiving this advice, General Fire asked its auditors to consider the effect of Guy Carpenter's interpretation of the reinstatement provision of the 4x1 XOL reinsurance contracts. *Id.* at ¶ 17. The auditors concluded that the relevant contract language was ambiguous. *Id.* Nonetheless, they required General Fire to accrue for reinstatement premiums in the Company's 2003 financial statements, allegedly resulting in an approximately $1.8 million reduction in earnings due to increased reinsurance expenses for 2003. *Id.*

II.

PROCEDURAL HISTORY

On November 30, 2004, General Fire filed, in state court, its Complaint against Guy Carpenter, bringing the following counts: negligence, breach of fiduciary duty, breach of contract, and

misrepresentation. *Complaint,* pp. 4-13 (Docket No. 1, Att. 1).

On June 24, 2005, Guy Carpenter removed the action to the United States District Court. *Notice of Removal* (Docket No. 1).

On August 10, 2005, General Fire filed a first Amended Complaint (Docket No. 11), adding the following counts: constructive fraud (count five) and unjust enrichment and disgorgement (count six). *First Amended Complaint,* pp. 10-12 (Docket No. 11).

On August 31, 2005, the parties filed a Stipulated Motion for Leave to Amend and to Extend Time to File Answer or Responsive Motion (Docket No. 12), which the Court granted, *Order Granting Stipulated Motion for Leave to Amend and to Extend Time to File Answer or Responsive Motion* (Docket No. 13). Therefore, on September 14, 2005, General Fire filed its Second Amended Complaint and Demand for Jury Trial (Docket No. 14), in which GF & C was included as a plaintiff and which listed the counts as follows: negligence (count one); negligent misrepresentation (count two); breach of fiduciary duty (count three); breach of contract (count four); misrepresentation (count five); constructive fraud (count six); and forfeiture, disgorgement, and/or constructive trust (count seven).[FN1]

> FN1. Plaintiffs filed a Third Amended Complaint and Demand for Jury Trial (Docket No. 52) on July 20, 2006, for the purpose of articulating that the amount in controversy in this action exceeds $75,000, such that the exercise of diversity jurisdiction is appropriate. The Third Amended Complaint contains the same counts as the Second Amended Complaint.

***3** On July 18, 2006, the Court heard oral argument on the currently-pending motion, as well as on other motions. *Minute Entry* (Docket No. 56). Following the hearing, the Court dismissed the negligent misrepresentation claim and granted GF & C's Rule 56(f) motion. *Order and Notice of Continued Hearing,* p. 10 (Docket No. 58). Accordingly, the hearing was continued until October 30, 2006, to permit "additional discovery and briefing" in the interim. *Id.* That has now happened, and the case has been submitted for the Court's decision.

III.

MOTION FOR SUMMARY JUDGMENT AGAINST GF & C'S CLAIMS

On May 26, 2006, Guy Carpenter filed its Motion for Summary Judgment Against GF & C's Claims (Docket No. 37), arguing (1) that Idaho's "economic-loss rule" bars GF & C's recovery in its negligence claims because it seeks purely economic damages and because neither of the two limited exceptions to the rule apply and (2) that GF & C's other claims must fail because Guy Carpenter never agreed to perform any services or assume any duties at all in regard to GF & C. *Guy Carpenter's Memorandum in Support,* pp. 5-7 (Docket No. 37, Att. 1). GF & C opposes the motion. *GF & C's Memorandum in Opposition* (Docket No. 42).

A. *Summary Judgment Standard*

Motions for summary judgment are governed by Federal Rule of Civil Procedure 56, which provides, in pertinent part, that judgment "shall be rendered forthwith if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed.R.Civ.P. 56(c).

1. *Genuine Issue of Material Fact*

According to Rule 56, an issue must be both "material" and "genuine" to preclude entry of summary judgment. An issue is "material" if it affects the outcome of the litigation. *Hahn v. Sargent*, 523 F.2d 461, 464 (1st Cir.1975). That is, a material fact is

> one that is relevant to an element of a claim or defense and whose existence might affect the outcome of the suit. The materiality of a fact is thus determined by the substantive law governing the claim or defense. Disputes over irrelevant or unnecessary facts will not preclude a grant of summary judgment.
>
> *T.W. Elec. Serv., Inc. v. Pac. Elec. Contractors Ass'n*, 809 F.2d 626, 630 (9th Cir.1987) (citing *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986)).

On the other hand, an issue is "genuine" when there is "sufficient evidence supporting the claimed factual dispute ... to require a jury or judge to resolve the parties' differing versions of the truth at trial." *Hahn*, 523 F.2d at 464 (quoting *First Nat'l Bank of Ariz. v. Cities Serv. Co.*, 391 U.S. 253, 289 (1968)). Because factual disputes are to be resolved at trial, in ruling on summary judgment motions, the Court does not resolve conflicting evidence with respect to disputed material facts, nor does it make credibility determinations. *T.W. Elec. Serv., Inc.*, 809 F.2d at 630. Moreover, all inferences must be drawn in the light most favorable to the nonmoving party. *Id.* at 631.

2. *Moving and Nonmoving Parties' Burdens*

***4** The initial burden is on the moving party to show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. *See Steckl v. Motorola, Inc.*, 703 F.2d 392, 393 (9th Cir.1983); Fed.R.Civ.P. 56(c). If the moving party meets its initial burden, the nonmoving party must "produce 'specific facts showing that there remains a genuine factual issue for trial' and evidence 'significantly probative' as to any [material] fact claimed to be disputed." *Steckl*, 703 F.2d at 393 (quoting *Rufin v. County of L.A.*, 607 F.2d 1276, 1280 (9th Cir.1979)). In addition, the nonmoving party must make a showing sufficient to establish the existence of an element that is essential to the party's case and upon which the party will bear the burden of proof at trial; otherwise, summary judgment is required. *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986). If the nonmoving party fails to make such a showing on any essential element of the nonmoving party's case, "there can be 'no genuine issue as to any material fact,' since a complete failure of proof concerning an essential element of the nonmoving party's case necessarily renders all other facts immaterial." *Id.* at 323. *See also* Fed.R.Civ.P. 56(e).[FN2] So, to withstand a motion for summary judgment, a nonmoving party

> FN2. Rule 56(e) states that, in responding to a motion for summary judgment,an adverse party may not rest upon the mere allegations or denials of the adverse party's pleading, but the adverse party's response, by affidavits or as otherwise provided in this rule, must set forth specific facts showing that there is a genuine issue for trial. If the adverse party does not so respond, summary judgment, if appropriate, shall be entered against the adverse party.
>
> Fed.R.Civ.P. 56(e).

(1) must make a showing sufficient to establish a genuine issue of fact with respect to any element for which it bears the burden of proof; (2) must show that there is an issue that may reasonably be resolved in favor of either party; and (3) must come forward with more persuasive evidence than would otherwise be necessary when the factual context makes the non-moving party's claim implausible.

British Motor Car Distribs., Ltd. v. S.F. Auto. Indus. Welfare Fund, 883 F.2d 371, 374 (9th Cir.1989) (citation omitted).

In recent years, the Supreme Court, "by clarifying what the non-moving party must do to withstand a motion for summary judgment, has increased the utility of summary judgment." Cal. Architectural Bldg. Prods., Inc. v. Franciscan Ceramics, Inc., 818 F.2d 1466, 1468 (9th Cir.1987). Therefore, "[n]o longer can it be argued that any disagreement about a material issue of fact precludes the use of summary judgment." *Id.* Nonetheless, "if a rational trier of fact might resolve the issue in favor of the nonmoving party, summary judgment must be denied." T.W. Elec. Serv., Inc., 809 F.2d at 631; Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1986) (holding a motion for summary judgment must be denied when the "evidence is such that a reasonable jury could return a verdict for the nonmoving party").

B. *GF & C's Negligence Claims and Idaho's Economic-Loss Rule*

In Idaho, unless an exception applies, the economic-loss rule prohibits recovery of purely economic losses in a negligence action because there is no duty to prevent economic loss to another. Blahd v. Richard B. Smith, Inc., 141 Idaho 296, 300, 108 P.3d 996, 1000 (2005) (citing Duffin v. Idaho Crop Improvement Ass'n, 126 Idaho 1002, 1007, 895 P.2d 1195, 1200 (1995). In this case, as to GF & C's negligence claims, it is undisputed that GF & C seeks recovery purely for economic losses. *Guy Carpenter's Memorandum in Support,* p. 9 (Docket No. 37, Att. 1) (citing *Second Amended Complaint,* ¶ 32 (Docket No. 14) and contending that "GF & C alleges purely economic damages only," a contention GF & C has not denied). Therefore, GF & C's negligence claims are barred unless an exception to the economic-loss rule applies.

***5** There are two exceptions to the economic-loss rule: the existence of a special relationship between the parties and unique circumstances requiring a reallocation of the risk. Millenkamp v. Davisco Foods Int'l, Inc., 391 F.Supp.2d 872, 878 (D.Idaho 2005).

1. *Special Relationship*

A "special relationship" refers to situations in which the relationship between the parties is such that it would be equitable to impose a duty to prevent economic loss to another. *Id.* It is an "extremely limited group of cases where the law of negligence extends its protections to a party's economic interest." *Id.* (quoting Blahd, 141 Idaho at 301, 108 P.3d at 1001 (quoting Duffin, 126 Idaho at 1008, 895 P.2d at 1201)). The Idaho Supreme Court has recognized two situations in which the "special relationship" exception applies: (1) where an entity holds itself out to the public as having expertise regarding a specialized function and knowingly induces reliance on its performance of that function and (2) where a professional or quasi-professional performs personal services. Millenkamp, 391 F.Supp.2d at 878-79.

a. *Holding Out to Public*

As to whether Guy Carpenter held itself out to the public as having expertise regarding drafting reinsurance agreements and knowingly induced reliance by both General Fire *and* GF & C on its performance of that function, Guy Carpenter argues that its only relationship was with General Fire as General Fire's reinsurance intermediary, not with GF & C, the holding company, and that GF & C cannot present any evidence that Guy Carpenter "knowingly induced" *GF & C* to rely on any action or representation. *Guy Carpenter's Memorandum in Support,* pp. 13, 17 (Docket No. 37, Att. 1).

Guy Carpenter relies heavily on Duffin v. Idaho Crop Improvement Ass'n, 126 Idaho 1002, 895 P.2d 1195 (1995). *See Guy Carpenter's Memorandum in Support,* pp. 16-18 (Docket No. 37, Att. 1). In *Duffin,* the plaintiff had purchased seed potatoes that had been "certified" to be free of disease by both the Idaho Crop Improvement Association ("ICIA") and by Idaho's Federal-State Inspection Service. *Id.* at 1005, 895 P.2d at 1198. The seed, after being planted by the plaintiffs, turned out to be infected with bacterial ring rot. *Id.* The Idaho Supreme Court held the ICIA and the plaintiff were in a "special relationship," recognizing that the ICIA had "engaged in a marketing campaign, for the benefit of its members, the very purpose of which is to induce reliance by purchasers on the fact that seed ha[d] been certified." *Id.* at 1008, 895 P.2d at 1201. Thus, the Idaho Supreme Court held that the ICIA "occupies a special relationship with those whose reliance it has knowingly induced." *Id.*

In this case, Guy Carpenter's marketing material states that "[e]ffective reinsurance may add tangible value to an *insurance enterprise," Exhibit 1 to Stanger Affidavit,* p. 5 (Docket No. 36, Att. 11). Based on that and due to GF & C and General Fire's close relationship, a reasonable jury could conclude that Guy Carpenter engaged in a marketing campaign to induce reliance not only by the direct purchasers of the reinsurance, but also by those within an "insurance enterprise."

b. *Professional Performs Personal Services*

***6** As to whether Guy Carpenter provided personal services to GF & C so as to create a special relationship, Guy Carpenter presented the affidavits of several former, high-level employees of GF & C and General Fire, who state that GF & C never had any kind of a relationship with Guy Carpenter. *Bonneau Declaration,* ¶¶ 2, 5 (Docket No. 37, Att. 5) ("I was employed by General Fire & Casualty Co. from December 2001 until March 2005, including acting as Director of Claims, Vice President of Claims, and Senior Vice President, serving alongside Barbara Anderson and Dan Crandall as a member of General Fire's reinsurance committee.") ("GF & C Holding Company had no relationship at all with Guy Carpenter."); *Anderson Declaration,* ¶¶ 2, 5 (Docket No. 37, Att. 6) ("I was employed by General Fire & Casualty Co., including positions as the Chief Financial Officer, Chief Information Officer, Chief Operations Officer, Vice President for Actuarial and Statistics, and Executive Vice President, from General Fire's inception in 1998 until leaving the company in June 2005.") ("GF & C Holding Company had no relationship with Guy Carpenter. Guy Carpenter acted as a reinsurance intermediary only for General Fire. To my knowledge, Guy Carpenter has never performed any services for GF & C."); *Winston Declaration,* ¶¶ 2, 5 (Docket No. 37, Att. 7) ("I was employed by General Fire & Casualty Co. as its Chief Underwriting Officer from General Fire's inception in 1998 until January 2003. Throughout this time, I was closely involved in the development and implementation of General Fire's reinsurance program.") ("Guy Carpenter had no relationship with GF & C Holding Co. Guy Carpenter's client was General Fire only, and Guy Carpenter never performed any services for GF & C to my knowledge.").

On the other hand, GF & C also presented a substantial amount of evidence in support of its contention that Guy Carpenter performed services on its behalf. For example, there is evidence to support the following conclusions:

1) GF & C and General Fire

at all times understood and believed that Guy Carpenter's services were being provided to and for the benefit of the entire insurance enterprise, including both GF & C and GenFire, and that GF & C could and did reasonably rely on Guy Carpenter's representations and the proper performance of Guy Carpenter's services, including those representations concerning reinstatement premiums and the nature of the alleged Hannover Re treaty that form the basis for this litigation.

Second Crandall Affidavit, ¶ 45 (Docket No. 42, Att. 2).

2) "At all times after July 1, 2000 until late 2003, the personnel with whom Guy Carpenter dealt in designing and placing GenFire's reinsurance programs each year were employees of GF & C Holding Company, including myself, CFO Barbara Anderson, Chief Underwriting Officer Chad Winston and Claims Vice President Gary Bonneau." *Id.* at ¶ 43; *Exhibit 31 to Second Crandall Affidavit,* pp. 47-55 (Docket No. 42, Att. 5) (containing the "Management and Administrative Services Agreement," which states that General Fire "agrees to employee and retain" GF & C).

***7** 3) "Mr. Graham[, Senior Vice President of Guy Carpenter,] specifically linked placement of GenFire's reinsurance business with investment in GF & C to foster growth of GenFire." *Second Crandall Affidavit,* ¶ 32 (Docket No. 42, Att. 2).

4) Guy Carpenter required GF & C's financial statements in order to provide reinsurance to General Fire. *Id.* at ¶ 14 ("Guy Carpenter prepared a reinsurance renewal proposal for GenFire which included information concerning GF & C Holding Company and its capitalization, as well as GF & C's financial statements, because that information was requested by the reinsurers as part of their determination whether to provide reinsurance to GenFire and terms and conditions thereof."); *see Exhibit 11 to*

Second Crandall Affidavit, pp. 10-23 (Docket No. 42, Att. 3).

5) In connection with its reinsurance services, Guy Carpenter solicited minority investments in GF & C. *Second Crandall Affidavit,* ¶ 37 (Docket No. 42, Att. 2) ("Mr. Graham introduced us to each of these reinsurers and, on our behalf, solicited a minority investment in GF & C by each of these reinsurers *in connection with a reinsurance placement.")* (emphasis added); *see Exhibit 28 to Second Crandall Affidavit,* pp. 39-42 (Docket No. 42, Att 5).

6) "In early 2000, Guy Carpenter retained Reinsurance Solutions International, at Guy Carpenter's own expense, to assess UOC's reinsurance program and other due diligence information about UOC, and provided these results to GF & C *as part of its reinsurance intermediary services." Second Crandall Affidavit,* ¶ 27 (Docket No. 42, Att. 2) (emphasis added).

From all of this evidence, for purposes of the pending motion for summary judgment, a rational trier of fact could reasonably conclude that Guy Carpenter provided professional services to GF & C, as well as to General Fire, including services encompassing reinsurance-intermediary services. To conclude otherwise, the Court would have to weigh evidence or determine the credibility of witnesses, which would be inappropriate in addressing a motion for summary judgment. More specifically, from the evidence referenced above on both sides of the factual issue, a rational trier of fact could reasonably conclude that Guy Carpenter solicited and participated in investment transactions for GF & C as part of its rendition of reinsurance-intermediary services and that Guy Carpenter was fully aware of the close relationship between GF & C and General Fire, such that the improper provision of reinsurance-intermediary services would injure both GF & C and General Fire. With such conclusions in mind, it would be equitable to impose a duty on Guy Carpenter to prevent economic loss to GF & C as well as to General Fire; *see* Millenkamp, 391 F.Supp.2d at 878. Accordingly, a reasonable jury or trier of fact could reasonably conclude that GF & C and Guy Carpenter had a special relationship such that the economic-loss rule does not apply.

c. *Special Relationships Conclusion*

***8** GF & C has presented a sufficient amount of evidence from which a reasonable jury or trier of fact could reasonably conclude either that Guy Carpenter worked directly with both General Fire and GF & C, and that it held itself out to insurance *enterprises,* including holding companies like GF & C, as experts in reinsurance intermediary services or that Guy Carpenter provided professional services personally to GF & C as well as to General Fire in conjunction with its reinsurance intermediary services. Thus, there exist genuine issues of material fact as to whether GF & C and Guy Carpenter were in a special relationship such that the economic-loss rule would not apply. Accordingly, the Motion for Summary Judgment Against GF & C's Claims (Docket No. 37) is denied as to the negligence claim.

2. *Unique Circumstances*

Because there is a genuine issue of material fact as to whether GF & C and Guy Carpenter were in a "special relationship," the Court need not determine whether unique circumstances existed that would require a different allocation of risk between the parties. *See* Millenkamp, 391 F.Supp.2d at 879.

C. *GF & C's Other Claims*

As to GF & C's other claims, i.e., breach of fiduciary duty (count three); breach of contract (count four); misrepresentation (count five); constructive fraud (count six); and forfeiture, disgorgement, and/or constructive trust (count seven), Guy Carpenter argues that "[t]he lack of *any* relationship between Guy Carpenter and GF & C precludes all of GF & C's claims" particularly because the lack of a relationship precludes the presence of any duty owed by Guy Carpenter to GF & C. *Guy Carpenter's Memorandum in Support,* pp. 21-23 (Docket No. 37, Att. 1).

In regard to a motion for summary judgment, the initial burden is on the moving party to show that there is no genuine issue as to any material fact and that moving party is entitled to judgment as

a matter of law. *See* Steckl v. Motorola, Inc., 703 F.2d 392, 393 (9th Cir.1983); Fed.R.Civ.P. 56 (c). Further, pursuant to District of Idaho Local Civil Rule 7.1(b), a motion "must be accompanied by a separate brief ... containing *all* of the reasons and points and authorities relied upon by the moving party." Dist. Idaho Loc. Civ. R. 7.1(b)(1).

In moving for summary judgment on GF & C's non-negligence claims, Guy Carpenter relies almost exclusively on its contention that no relationship of any kind existed between Guy Carpenter and GF & C. However, if genuine issues of material fact exist, or if Guy Carpenter is not entitled to judgment as a matter of law, its motion must be denied in regard to the non-negligence claims.

As discussed above, based on the evidence presented by GF & C in opposing Guy Carpenter's motion on its negligence claim, a reasonable jury or trier of fact could reasonably conclude that Guy Carpenter solicited and participated in investment transactions for the benefit of GF & C as part of its overall rendition of reinsurance-intermediary services, and that Guy Carpenter was fully aware of the close relationship between GF & C and General Fire, to the extent that the improper provision of reinsurance-intermediary services would injure both GF & C and General Fire. Accordingly, for purposes of summary judgment, a reasonable jury or trier of fact could reasonably conclude that it would be equitable to impose a duty on Guy Carpenter to prevent a loss to GF & C. Thus, there remain genuine issues of material fact as to whether Guy Carpenter and GF & C had a relationship and whether, because of that relationship, Guy Carpenter owed duties to GF & C. As such, Guy Carpenter's motion for summary judgment is denied as to GF & C's non-negligence claims.

D. *Conclusion*

***9** There exist genuine issues of material fact as to whether Guy Carpenter and GF & C entered into a special relationship sufficient to be included within an exception to the economic-loss rule. Further, there remain genuine issues of fact as to whether Guy Carpenter and GF & C had a relationship such that Guy Carpenter owed duties to GF & C. Accordingly, Guy Carpenter's Motion for Summary Judgment Against GF & C's Claims (Docket No. 37) is denied.

IV.

ORDER

In accordance with the foregoing reasoning, IT IS HEREBY ORDERED that Guy Carpenter's Motion for Summary Judgment Against GF & C's Claims (Docket No. 37) is DENIED.

D.Idaho,2006.
General Fire & Cas. Co. v. Guy Carpenter & Co., Inc.
Not Reported in F.Supp.2d, 2006 WL 3239365 (D.Idaho)

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- 2007 WL 4444892 (Trial Motion, Memorandum and Affidavit) Guy Carpenter's Reply in Support of Motion for Summary Judgment Against Plaintiffs' Breach-of-Fiduciary-Duty and Disgorgement Claims (Jul. 3, 2007)
- 2006 WL 4015315 (Trial Motion, Memorandum and Affidavit) Guy Carpenter's Memorandum in Support of Motion for Summary Judgment Against Plaintiffs' Risk-Transfer-Related Claims (Dec. 6, 2006) Original Image of this Document (PDF)
- 2006 WL 4015316 (Trial Motion, Memorandum and Affidavit) Guy carpenter's Memorandum in Support of Motion for Summary Judgment Against Plaintiffs' Breach-of-Fiduciary-Duty and Disgorgement Claims (Dec. 6, 2006) Original Image of this Document (PDF)

• 2006 WL 2920506 (Trial Pleading) Third Amended Complaint and Demand for Jury Trial (Jul. 20, 2006)
• 2006 WL 1434655 (Trial Motion, Memorandum and Affidavit) Guy Carpenter's Memorandum in Support of Motion for Summary Judgment against Plaintiffs' Negligent-Misrepresentation Claims (Apr. 4, 2006) Original Image of this Document (PDF)
• 2005 WL 2868118 (Trial Pleading) Guy Carpenter & Co., Inc.'s Answer and Affirmative Defenses (Oct. 5, 2005) Original Image of this Document (PDF)
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• 1:05cv00251 (Docket) (Jun. 24, 2005)
END OF DOCUMENT

Not Reported in F.Supp.2d, 2003 WL 1824932 (D.Neb.)

Motions, Pleadings and Filings

Only the Westlaw citation is currently available.

United States District Court,
D. Nebraska.
HALIMAGE FARMS, L.L.C., a Nebraska Limited Liability Company, Plaintiff,
v.
WESTFALIA-SURGE, INC., Defendant.
No. 4:01CV3327.
April 8, 2003.

David A. Domina, James F. Cann, Domina Law Office, Omaha, NE, for Plaintiff.

Randall L. Goyette, Baylor, Evnen Law Firm, Lincoln, NE, Brice A. Tondre, Tondre Law Office, Denver, CO, for Defendant.

MEMORANDUM AND ORDER ON DEFENDANT'S MOTION TO DISMISS

WARREN K. URBOM, Senior District Judge.

*1 Before me is the motion of Defendant Westfalia-Surge, Inc. to dismiss a portion of the plaintiff's complaint pursuant to Federal Rule of Civil Procedure 12(b)(6). (*See* filing 70.) For the following reasons, the defendant's motion will be denied.

I. BACKGROUND

On December 12, 2001, the plaintiff, Halimage Farms, L.L.C., filed a three-count complaint against the defendant, Westfalia-Surge, Inc., alleging causes of action based upon "Breaches of Express Warranties," (Count I), "Breach of Implied Warranty," (Count II), and "Negligence," (Count III). (*See generally* Compl. and Jury Demand (hereinafter "Compl."), filing 1.) According to the complaint, the plaintiff, which is a "commercial dairy engaged in the production of milk and fluid dairy products for profit," (*id.* ¶ 5), negotiated with the defendant to purchase "plans, specifications, goods, materials and services for the erection of a rotary dairy parlor, milking platform, and machine," (*id.* ¶ 9). These purchases apparently led to the construction of a structure that formed part of a "new dairy operation." (*Id.* ¶ 9.) However, the plaintiff alleges that the defendant's breaches of various warranties and negligence have caused the plaintiff to suffer damages. (*See generally id.*)

On March 25, 2003, the defendant filed a "Motion for Partial Dismissal," filing 70, wherein it argues that the plaintiff's third claim must be dismissed pursuant to Federal Rule of Civil Procedure 12(b)(6). In support of its motion to dismiss, the defendant has filed an index of evidence containing a brief excerpt from the report of Michael Behr, Ph.D. (*See* Index of Evidence, filing 71.) The plaintiff has filed a brief in opposition to the defendant's motion. (*See* Pl.'s Br. in Opp'n to Def.'s Mot. for Partial Dismissal (hereinafter "Pl.'s Br."), filing 89.) My analysis of the parties' arguments follows.

II. STANDARD FOR MOTION TO DISMISS

Pursuant to Federal Rule of Civil Procedure 12(b)(6), "a motion to dismiss a complaint should not be granted unless it appears beyond doubt that the plaintiff can prove no set of facts which would entitle him to relief." *Morton v. Becker*, 793 F.2d 185, 187 (8th Cir.1986) (citation omitted); *see also Hishon v. King & Spalding*, 467 U.S. 69, 73 (1984). In resolving such motions, all well-pleaded allegations in the complaint must be taken as true, and the complaint and all reasonable inferences

arising therefrom must be weighed in favor of the plaintiff. Morton, 793 F.2d at 187. When considering a Rule 12(b)(6) motion to dismiss, the court has the discretion to decide whether it will accept materials outside the pleadings. *See* Skyberg v. United Food and Commercial Workers International Union, 5 F.3d 297, 302 n. 2 (8th Cir.1993). If the court accepts such materials, it must treat the motion to dismiss as if it were a motion for summary judgment brought pursuant to Federal Rule of Civil Procedure 56. *See* FED.R.CIV.P. 12(b).

III. ANALYSIS

***2** The defendant argues that the plaintiff's negligence claim must be dismissed because all of the plaintiff's claimed losses are "economic losses," and Nebraska law prohibits "recovery for economic loss alone in a product liability action based upon tort." (Mot. for Partial Dismissal, filing 70, at 1 (citing Hawkins Constr. Co. v. Matthews Co., Inc., 209 N.W.2d 643 (Neb.1973) and Neb.Rev.Stat. § 25-21, 180).) Preliminarily, I note that in its attempt to establish that the plaintiff's claimed losses are all solely "economic losses," the defendant has submitted a portion of the report of Michael Behr, Ph.D., an economist who analyzed "The Economic Loss to Halimage Dairy Due to Malfunctioning Milking Equipment." (*See* Mot. for Partial Dismissal, filing 70, at 1 (citing "the report of plaintiff's damages expert"); Index of Evidence, filing 71, "Item 1" at MB 000090.) It seems to me that this exhibit amounts to "written ... evidence ... in opposition to the pleading that provides some substantiation for and does not merely reiterate what is said in the pleadings," and therefore constitutes a "matter[ ] outside the pleading" within the meaning of Federal Rule of Civil Procedure 12 (b). Hamm v. Rhone-Poulenc Rorer Pharmaceuticals, Inc., 187 F.3d 941, 948 (8th Cir.1999) (quoting Gibb v. Scott, 958 F.2d 814, 816 (8th Cir.1992) and FED.R.CIV.P. 12(b)). Therefore, if I were to accept the defendant's evidence, I would then be required to treat the defendant's motion as one for summary judgment. *See* FED.R.CIV.P. 12(b). *See also* Hamm, 187 F.3d at 948-49. However, it appears that the defendant's motion, which was filed on March 25, 2003, would be untimely if it were treated as a motion for summary judgment. (*See* Order Setting Schedule for Progression of Case, filing 14 (setting deadline for filing of motions for summary judgment at thirty days prior to the date set for completion of depositions); Order, filing 37 ("The deposition deadline is continued to March 14, 2003 and other deadlines which use the deposition deadline as a point of reference are extended accordingly .").)

Furthermore, even if the defendant's motion were not untimely (or if I chose not to accept the defendant's evidence, and thereby declined to convert the defendant's motion into one for summary judgment), the motion would fail on its merits. In support of its motion, the defendant relies upon Hawkins Constr. Co. v. Matthews Co., Inc., 209 N.W.2d 643 (Neb.1973) for the proposition that, in cases where a party's losses are strictly "economic," that party may not recover damages under the law of torts. However, the Supreme Court of Nebraska has stated,

To the extent that Hawkins Constr. Co. v. Matthews Co., Inc., 190 Neb. 546, 209 N.W.2d 643 (1973), held that strict liability in tort may not be used to recover for physical harm to property only, it is disapproved. To hold otherwise would penalize the fortunate persons who escape personal injury and ignore the specific language of § 402 A of the Restatement and a virtually unbroken line of decisions of other courts.

***3** National Crane Corporation v. Ohio Steel Tube Company, 332 N.W .2d 39, 43-44 (Neb.1983). In *National Crane,* the plaintiff, a manufacturer of cranes, purchased steel tubing from the defendant and incorporated this tubing into its cranes. *See id.* at 41. However, after the portions of the cranes that contained the defendant's steel tubing failed repeatedly, the plaintiff initiated a retrofit program to replace that tubing in all of its cranes. *See id.* at 41-42. The plaintiff then filed a petition to recover the costs associated with the retrofit program. *See id.* at 41. The plaintiff's first cause of action was based upon a breach of express and implied warranties, the second was based upon negligent manufacture, and the third was based upon strict liability. *See id.* at 42. The plaintiff's petition was eventually dismissed in its entirety; specifically, the first cause of action was deemed barred by the applicable statute of limitations, while the second and third causes of action were found to be "not available for the recovery of economic loss." *Id.* The plaintiff appealed, arguing "that the principles of tort law should be extended to permit plaintiff to recover the economic losses incurred under the retrofit program involved here, and that plaintiff should not be limited to recovery on the contractual

basis of express or implied warranties." *Id.* The court affirmed the dismissal of the plaintiff's petition, stating, "We hold that the purchaser of a product pursuant to contract *cannot recover* economic losses from the seller manufacturer on claims in tort based on negligent manufacture or strict liability *in the absence of physical harm to persons or property caused by the defective product." Id.* at 44 (emphasis added). Since the damages sought by the plaintiff were only the costs associated with the replacement of the defective tubing, the court concluded that these damages did not result "from physical harm caused by the defective product," but "[i]nstead ... are damages resulting from the purchase of defective or unsatisfactory products." *Id.*

In the present case, the plaintiff is not seeking to recover the costs associated with the replacement of the allegedly defective products and services provided by the defendant. (*See* Compl. ¶ 28.) Instead, the plaintiff seeks damages to remedy the physical harm caused by these allegedly defective products or services. (*See id.*) Thus, it seems to me that the plaintiff's negligence claim is not barred under Nebraska law. *See* National Crane Corporation v. Ohio Steel Tube Company, 332 N.W.2d 39, 43-44 (Neb.1983).

IT IS ORDERED that the defendant's Motion for Partial Dismissal, filing 70, is denied.

D.Neb.,2003.
Halimage Farms, L.L.C. v. Westfalia Surge, Inc.
Not Reported in F.Supp.2d, 2003 WL 1824932 (D.Neb.)

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• 2002 WL 33511514 (Expert Deposition) Deposition of: Gerald R. Bodman, P.E. (Dec. 19, 2002)
• 2002 WL 33176695 (Expert Report and Affidavit) (Report or Affidavit of Dr. Sybren Y. Reitsma, P.Eng.) (Sep. 16, 2002)
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- 1999 WL 34573171 (Expert Report and Affidavit) (Report or Affidavit) (Jan. 28, 1999)

END OF DOCUMENT

Slip Copy, 2005 WL 6104101 (D.N.M.)

Motions, Pleadings and Filings

Only the Westlaw citation is currently available.

United States District Court,
D. New Mexico.
MARIPOSA FARMS, LLC, a New Mexico limited liability company, Plaintiff,
v.
WESTFALIA-SURGE, INC., an Illinois corporation, and Rota-Tech Dairy Sheds International, Ltd., a New Zealand company, Defendants.
No. CIV-03-0779 JC/LAM.
April 7, 2005.

David A. Domina, Esq., James F. Cann, Esq., Domina Law, P.C., Omaha, NE, Esteban A. Aguilar, Esq., Felicia C. Weingartner, Esq., Aguilar Law Offices, P.C., Albuquerque, NM, for Plaintiff.

M. Eliza Stewart, Esq., Madison, Harbour, Mroz & Brennan, P.A., Albuquerque, NM, Brice A. Tondre, Esq., Denver, CO, for Defendant Westfalia-Surge, Inc.

Patrick M. Shay, Esq., Kurt B. Gilbert, Esq., Rodey, Dickason, Sloan, Akin & Robb, P.A., for Defendant Rota-Tech Dairy Sheds International, Ltd.

MEMORANDUM OPINION AND ORDER

JOHN EDWARDS CONWAY, Senior District Judge.

*1 THIS MATTER comes before the Court on *Defendant Rota-Tech's Motion for Partial Summary Judgment,* filed October 1, 2004 (*Doc.94*). The Court, having considered the Motion, the parties' submissions, and the relevant authority, denies the motion in part and grants it in part [FN1].

> FN1. In a Pre-Trial Conference held on April 5, 2005, the Court made oral rulings on two of the three dispositive motions pending before it. The Court also instructed that written *memoranda and orders would follow.* To the extent that this Memorandum Opinion and Order diverges from any oral rulings, such oral rulings are vacated and superseded by this written Memorandum.

I. *Background*

This case arises from alleged deficiencies in a milking system installed at a commercial dairy located in New Mexico. In January 2000, Plaintiff and Rota-Tech entered into a Construction Agreement, though the document was never signed by Plaintiff. Plaintiff alleges that Defendant Rota-Tech designed, manufactured, installed and serviced commercial dairy milking equipment as part of the system that failed to perform as intended resulting in financial loss. Plaintiff brings claims sounding in both contract and tort.

II. *Legal Standard*

A party is entitled to summary judgment on all or any part of a claim as to which there is no genuine issue of material fact and as to which the moving party is entitled to judgment as a matter of law. Fed.R.Civ.P. 56(c). *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 247 (1986). For purposes of a summary judgment motion, the evidence is viewed in the light most favorable to the non-moving

party. *Id.* The moving party has the initial burden of showing that there is no genuine issue of material fact. *Id.* at 256. The movant may discharge this burden by pointing out the absence of evidence to support one or more essential elements of the non-moving party's claim, as "a complete failure of proof concerning an essential element of the non-moving party's case necessarily renders all other facts immaterial." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323-25 (1986).

Once the moving party has carried its burden under Rule 56(c), the non-moving party must do more than merely show that there is some metaphysical doubt as to the material facts. *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986). The party opposing the motion may not rest on mere allegations or denials of pleading, but must set forth specific facts showing a genuine issue for trial. *Anderson*, 477 U.S. at 248, 256. To meet this burden, the nonmovant must specify evidence in the record and demonstrate the precise manner in which that evidence supports its claims. *Gross v. Burggraf*, 53 F.3d 1531, 1546 (10th Cir.1995). Unsupported allegations, conclusory in nature, are insufficient to defeat a proper motion for summary judgment. *Id.* If the record, taken as a whole, could not lead a rational trier of fact to find for the non-moving party, there is no genuine issue for trial. *Matsushita*, 475 U.S. at 597.

III. *Discussion*

Defendant Rota-Tech Dairy Sheds International Ltd. ("Rota-Tech") moves the Court for summary judgment disposition in its favor on Plaintiff's tort claims and further requests a ruling limiting Plaintiff's maximum recovery to the price of the milking platform as stated in the Construction Agreement ("Agreement") between Plaintiff and Rota-Tech.[FN2] In support of its Motion, Rota-Tech asserts, and Plaintiff denies, that Rota-Tech and Plaintiff are parties to a written contract for the sale of goods governed by New Mexico's Uniform Commercial Code ("UCC"). Next, Rota-Tech asserts the undisputed fact that the damages allegedly suffered by Plaintiff are comprised of purely economic losses. Thus, Rota-Tech urges, Plaintiff's claims sounding in negligence and strict products liability are barred by the economic loss rule, which prohibits recovery in tort for purely economic losses in commercial settings. Further, Rota-Tech argues, the Agreement expressly precludes any recovery for incidental and consequential damages through its Limitation of Liability Clauses and caps the available recovery at $212,053.00, the purchase price of the rotary platform Rota-Tech sold to Mariposa Farms.

> FN2. Rota-Tech also requested summary judgment in its favor on Plaintiff's claim for punitive damages. That issue was mooted, however, upon filing of the parties' *Stipulation for Dismissal of Punitive Damages Claim* on February 22, 2005 (*Doc.195*).

***2** Plaintiff responds that the economic loss rule does not apply, for in New Mexico its preclusive effect is limited to claims for injuries to the product itself absent special circumstances not present here. The property damages Plaintiff suffered are to its herd of milking cows, not the milking machinery that was the subject of the its contract with Rota-Tech. Plaintiff also asserts that its relationship to Rota-Tech exceeded the mere sale of goods and thus the transaction is not governed exclusively by the UCC. In this vein, Plaintiff contends that Rota-Tech was the "principal designer of the platform, various components of the vacuum system, and the manner in which the equipment would integrate with Westfalia-Surge equipment." Resp. at 1-2. Finally, Plaintiff contends that the Limitation of Liability clauses in the contract relied upon by Rota-Tech to limit damages fail of their essential purpose and are unconscionable, for the defects in the equipment were latent and damages in excess of the contract price were already incurred by the time such defects were discovered. Plaintiff also challenges enforcement of the Limitation of Liability clauses arguing no mutual assent to those terms.

A. Economic Loss Rule

It is well-settled in New Mexico that the economic loss rule precludes tort claims for "economic losses from injury of a product to itself." *In re Consolidated Vista Hills Retaining Wall Litig., Amrep. Southwest, Inc. v. Shollenbarger*, 119 N.M. 542 (1995) (quoting *Utah Int'l, Inc. v. Caterpillar Tractor Co.*, 108 N.M. 539 (Ct.App.1989)). Indeed, the New Mexico Court of Appeals held that in commercial

transactions between parties with comparable bargaining power, damage to the product itself should be governed by contract law. Caterpillar, 108 N.M. at 542. The perplexing question here is whether the instant case presents the type of circumstances exhibited in Spectron Dev. Lab. v. Am. Hollow Boring Co., 123 N.M. 170 (Ct.App.1997) which would provide a rationale for applying the economic loss rule to the property damages allegedly suffered by Plaintiff. Rota-Tech asserts that the holding in *Spectron* is not limited to its unusual facts and is determinative. The Court, after much deliberation, disagrees with Rota-Tech's position on the state of the law and, for the reasons discussed briefly below, finds the underlying *Spectron* rationale lacking on the facts of this case.

Rota-Tech asserts that Plaintiff "seeks to turn *Spectron* on its head by arguing that tort remedies are available for property damage in commercial transactions unless a plaintiff possesses extraordinary sophistication regarding the product." Reply at 10. Rota-Tech instead reads *Spectron* as creating the opposite presumption, that "for the courts to interfere with the statutory scheme by superimposing tort rules, there must be sound policy reasons for finding the statutory scheme to be inadequate." Reply at 10 (*quoting* Spectron, 123 N.M. at 176). While this is true, the policy reasons supporting strict products liability were also discussed by the *Spectron* court and, at least to some extent, recognized to bear even on the "special situation" before it. *Id*.

***3** The *Spectron* court clearly stated that the "key feature" of the relationship between buyer and seller of the steel pump tube incorporated into a sophisticated light-gas gun in that case was that "[buyer] Titan was essentially the manufacturer of the [end product] light-gas gun, acting as the designer and general contractor who subcontracted out the production and assembly of component parts." *Id.* at 176. Moreover, the court noted that Titan was, in fact, the only company in the United States designing, manufacturing, and producing the highly sophisticated light-gas gun at that time, essentially characterizing Titan as the foremost authority on the end product itself. *Id.*

By contrast, the evidence before the Court indicates no similar, exclusive expertise on the part of Mariposa regarding the milking platform and system, notwithstanding Mr. Skelley functioning as general contractor for the start-up dairy project and his prior experience at another diary. Mr. Skelley stated that he had no knowledge, skill, or prior experience with Rota-Tech's Rotary Platform. Skelley Aff. at 2-3. Nor can Plaintiff be accurately described as the designer and manufacturer of the milking system, much less the only such manufacturer. Instead, Rota-Tech's Director, John Bowers, prepared all of the specifications for the milking system. Bowers Dep. at 15:9-12. Though Skelley undisputedly reviewed the specifications and had some input regarding modifications thereto, the Court finds Skelley's posture *vis-a-vis* Rota-Tech to be distinguishably different than that of the *Spectron* buyer to its seller.

The Court recognizes that the *Spectron* holding was not based solely upon the buyer's exceptional and superior expertise, though reiterates that it was "key." The Court of Appeals cited the economic loss rule; considered the highly remarkable knowledge and expertise on the part of the buyer; analyzed the four primary policy factors supporting strict liability; found that the UCC provided adequate response to those factors insofar as they applied to the "special situation" before it, and concluded that contract remedies alone were adequate on the facts of that case. Spectron, 123 N.M. at 175-177. In reaching its determination, the *Spectron* court quoted from Kaiser Steel Corp. v. Westinghouse Elec. Corp., 127 Cal.Rptr. 838, 845, but ultimately declined to decide "precisely when the UCC is the exclusive source of remedies for property damage ..." and limited its reliance on the *Kaiser* rule to reinforcing "the result we reach *today*." *Id.* at 177 (emphasis added).

The Court is mindful of the Michigan Supreme Court's ruling in the consolidated cases styled Neibarger v. Universal Cooperatives, Inc., 486 N.W.2d 612 (Mich.1992), which cases present facts remarkably similar to those at hand. As Rota-Tech reminds the Court, however, "the Court's primary concern in this diversity case [is] to apply New Mexico law as New Mexico would apply it." Reply at 16. In that very quest, the Court determines that even if the *Spectron* decision extended the doctrine of economic loss to other property damage as a presumption that may be rebutted by other policy considerations, it is simply not convinced that New Mexico courts would apply the limitation on the facts of this case. It bears repeating that the policies supporting strict products liability were determined to be adequately "addressed" by the UCC only in *Spectron's* "special situation." *Id.* At 176.

*4 That said, it is with some consternation that the Court declines to endorse Rota-Tech's more broad reading of the economic loss rule to preclude Plaintiff's strict liability and negligence claims under *Spectron.* However, the Court finds no unique circumstances present under which the UCC remedies adequately address the policies supporting strict liability here as they did in *Spectron.* Thus, the economic loss rule should not bar Plaintiff's tort law claims.

B. Sale of Goods

Given a mixed contract including sale of goods and services, the "primary purpose" test must be applied to determine whether the contract is governed by the UCC. Thus, the question is whether the Agreement was primarily for the sale of the equipment, involving incidental services such as installation and maintenance, or primarily for the rendition of those services, with the transfer of the equipment incidental to that purpose. *See* Kirkpatrick v. Introspect Healthcare Corp., 114 N.M. 706, 709-710 (1992) (applying test established in Bonebreak v. Cox, 499 F.2d 951 (8th Cir.1974). On the record before it, the Court determines as a matter of law that the Agreement's primary purpose was the sale of the goods, chiefly the milking carousel; the design, installation and service related thereto were secondary to that purpose. Thus, to the extent that the Agreement was in force, it is governed by the UCC.

C. Limitation Clauses

Rota-Tech seeks summary judgment determination that the Limitation of Liability clauses in the Construction Agreement are valid and enforceable as a matter of law. Plaintiff responds that the Limitation clauses are either unconscionable or fail in their essential purpose and, as such, are invalid. Plaintiff further argues that it never signed the Agreement and, despite testifying to its belief that it indeed had an agreement with Rota-Tech for design, construction, and installation of the platform, it never manifested assent to the terms of the Limited Liability clauses.

Lack of Signature by Plaintiff

First, the Court will discuss due execution of the Agreement. Plaintiff never signed the Agreement, but through Skelley's testimony it has acknowledged its belief that it had *an* agreement with Rota-Tech for the design, construction, and installation of the rotary platform. Skelley Dep. at 170:17. Plaintiff also asserts, however, notwithstanding its acknowledgment through its 30(b)(c) witness Skelley that *an* agreement existed, it did not assent to the Limited Liability terms of the Agreement Defendants seek to enforce against it. Further, Plaintiff argues, Rota-Tech did not itself sign the Agreement until January 2000 but had begun design of the parlor in July 1999. Because the design portion of the relationship preceded the Construction Agreement by five months, Plaintiff argues, it cannot be said that the design features were performed under the written Agreement limiting liability or that the Agreement embodied the complete relationship between the parties.

*5 Rota-Tech contends that whether the contract was duly executed despite the lack of signature by Marisposa is a question of law for the Court to determine on summary judgment. On this point, Rota-Tech references NMSA 1978 § 55-2-201(3)(b) providing that execution is unnecessary to satisfy the UCC statute of frauds when a party admits the existence of the contract in pleadings and testimony. Resp. at 6, n. 2. The Court finds, nonetheless, lingering questions of material fact making summary judgment disposition improper, for the real dispute is regarding the terms of the agreement and mutual assent thereto. Plaintiff contends that it had *an* agreement but denies that the Agreement before the Court embodies it. Absent a determination of mutual assent, a question of fact, the Court cannot rule that the Agreement was duly executed as a matter of law. Therefore, summary judgment on this issue is denied.

Essential Purpose/Unconscionability

If the evidence at trial establishes that there was due execution of the Agreement, Plaintiff's challenges to enforceability of the Limitation clauses on other grounds remain in need of resolution. Rota-Tech, never Plaintiff, identifies for the Court the three different clauses in question and provides

the proper standard for analyzing the challenges to each. The clauses at issue are (1) a clause excluding all consequential damages; (2) a clause excluding consequential damages related to death or injury to Plaintiff's animals; and (3) a clause limiting Rota-Tech's maximum liability to Plaintiff to an amount no greater than the purchase price of the Rotary Platform. Reply at 16 (citing Agreement ¶¶ 7.1, 7.1(c), 7.2). The first two clauses exclude consequential damages while the third is a limited remedy provision. Section 55-2-302 of the New Mexico UCC makes all contract clauses subject to unconscionability analysis while Section 55-2-719 provides that limited remedies are unenforceable if they fail of their essential purpose.

Whether the limitation of remedies clause fails of its essential purpose involves questions of fact. Plaintiff urges that it fails in purpose because the alleged defects in the equipment were latent and went undiscovered until significant damage was done. The question whether latent defects existed is clearly one of material fact. Plaintiff further asserts that enforcement of the limited remedy provision would deprive it of the substantial benefit of its bargain. Defendant argues that the latent defect theory upon which Plaintiff so heavily relies is, without more, insufficient to defeat a motion for summary judgment. The Court finds, however, that factual development at trial is necessary on this issue as well. Thus, summary judgment disposition is improper.

Similarly, whether any of the three clauses are unenforceable against Plaintiff as unconscionable requires factual development at trial. Indeed, Rota-Tech correctly identifies that under the UCC, unconscionability is an "absence of meaningful choice" for one party combined with "contract terms which are unreasonably favorable to the other party." *See* Bowlin's, Inc. v. Ramsey Oil Co., Inc., 99 N.M. 660, 668 (Ct.App.1983) (quoting Williams v. Walker-Thomas Furniture Co., 350 F.2d 445, 449 (D.C.Cir.1965)). Rota-Tech then swiftly asserts that the Court should determine the unconscionability questions as a matter of law at this summary judgment phase. The Court finds that factual development is necessary, however, before a reasoned and informed determination can be made on this issue. Thus, summary judgment on this issue of unconscionability will be denied.

IV. *Conclusion*

***6** In summary, the Court determines as a matter of law that the economic loss rule should not preclude Plaintiff from seeking recovery in both contract and tort on the facts of this case. The Court further finds the record before it sufficient for the Court to determine, as a matter of law, that the primary purpose of the Agreement was the sale of goods and as such it is governed by the UCC. The Court denies summary judgment on the issues of due execution and enforceablity of the Limitation of Remedies clauses against Plaintiff, finding genuine issues of material fact in need of resolution at trial.

WHEREFORE,

IT IS ORDERED that *Defendant Rota-Tech's Motion for Partial Summary Judgment,* filed October 1, 2004 (*Doc.94*) is GRANTED IN PART and DENIED IN PART as follows:

I. The economic loss rule does not preclude Plaintiff's tort claims;

II. The written Agreement is governed by the UCC; and

III. Due execution of the Agreement, and enforceability of the Limitation of Remedies clauses against Plaintiff involve questions of fact in need of resolution at trial.

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• 2003 WL 24574617 (Partial Expert Testimony) (Partial Testimony) (2003)
• 2003 WL 24574618 (Partial Expert Testimony) (Partial Testimony) (2003)
• 2003 WL 24574619 (Partial Expert Testimony) (Partial Testimony) (2003)
• 2003 WL 24590391 (Partial Expert Testimony) (Partial Testimony) (2003)
• 2003 WL 24590392 (Partial Expert Testimony) (Partial Testimony) (2003)
• 2003 WL 24590393 (Partial Expert Testimony) (Partial Testimony) (2003)
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--- F.Supp.2d ----, 2008 WL 3914896 (D.Md.)

Motions, Pleadings and Filings

Only the Westlaw citation is currently available.

United States District Court,
D. Maryland.
PACIFIC INDEMNITY COMPANY, As subrogee of Antoine and Emily van Agtmael, Plaintiff,
v.
Clay H. WHALEY, individually d/b/a C.H. Whaley & Son, Inc., Defendant.
Clay H. Whaley, individually d/b/a C.H. Whaley & Son, Inc., Third-Party Plaintiff
v.
Compton & Sons, Third-Party Defendant.
Civil No. JFM 07-826.
Aug. 25, 2008.

Background: Property insurer, as subrogee of its insured, brought suit against home contractor for negligence, breach of contract, and breach of warranty in removing and replacing roof on insured's residence. Contractor filed third party claim against subcontractor for contribution and indemnity. The United States District Court for the District of Maryland, 560 F.Supp.2d 425, denied subcontractor's motion for summary judgment on third-party claim. Subcontractor moved for reconsideration.

Holdings: The District Court, Motz, J., held that:
(1) economic loss doctrine did not preclude claim against roofing subcontractor for damages to house and its contents, and
(2) possibility under allegations of complaint that general contractor's negligence was passive permitted third-party indemnification claim.

Motion denied.

[1] KeyCite Citing References for this Headnote

⇦313A Products Liability
Economic loss doctrine prohibits a plaintiff from recovering in tort for purely economic losses, on other words, losses that involve neither a clear danger of physical injury or death, nor damage to property other than the product itself.

[2] KeyCite Citing References for this Headnote

⇦313A Products Liability
Under Maryland law, while recovery in tort is not permitted for damage to the defective item itself, recovery in tort is permitted for damage to items added to or used in conjunction with a defective item.

[3] KeyCite Citing References for this Headnote

⇦379 Torts
Under Maryland law, the economic loss doctrine did not shield roofing subcontractor who installed new roof on existing structure from tort liability for damages to the house and its contents, with the exception of the roof itself.

[4] KeyCite Citing References for this Headnote

⚿208 Indemnity

Under Maryland law, if the conduct attributed to the party seeking indemnification in the original plaintiff's complaint constitutes active negligence, or if it is clear from the complaint that this party's liability would only arise from proof of active negligence, then there is no valid claim for indemnity.

[5] KeyCite Citing References for this Headnote

⚿208 Indemnity

Under Maryland law, general contractor could pursue third-party indemnification claim against roofing subcontractor, where possibility existed under allegations of homeowners' complaint, charging that damage to their home was caused by negligence of general contractor "and/or" its subcontractor, that general contractor could be held liable for negligence that was solely passive.

Thomas M. Wood, IV, Neuberger Quinn Gielen Rubin and Gibber PA, Baltimore, MD, Sean P. O'Donnell, Cozen and O'Connor, Philadelphia, PA, for Pacific Indemnity Company.

Robert Leigh Hebb, Eric Michael Leppo, Semmes Bowen and Semmes PC, Baltimore, MD, for Clay H. Whaley.

Betty Sue Diener, Marks ONeill OBrien and Courtney PC, Towson, MD, for Compton & Sons.

MEMORANDUM OPINION

J. FREDERICK MOTZ, District Judge.

*1 In a Memorandum Opinion I issued on June 16, 2008, I denied third-party defendant Compton & Sons' motion for summary judgment. *Pac. Indem. Co. v. Whaley*, No. 07-CV-826, 2008 WL 2440711, at *1 (D. Md. June 16, 2008). Compton & Sons ("Compton") has moved for me to reconsider two of my conclusions: (1) that the economic loss doctrine does not shield Compton from tort liability; and (2) that third-party plaintiff Whaley's indemnification claim must survive summary judgment because plaintiff Pacific Indemnity Company's complaint did not specifically allege that Whaley was actively negligent.[FN1] (Compton Mem. at 2-4). For the reasons that follow, I will deny Compton's motion for reconsideration.

I.

[1] The economic loss doctrine "prohibits a plaintiff from recovering in tort for purely economic losses-losses that involve neither a clear danger of physical injury or death, nor damage to property other than the product itself." *Morris v. Osmose Wood Preserving*, 340 Md. 519, 667 A.2d 624, 630 (Md.1995). The Maryland Court of Appeals has further explained that "[e]conomic losses include such things as the loss of value or use of the product itself, the cost to repair or replace the product, or the lost profits resulting from the loss of use of the product." [FN2] *A.J. Decoster Co. v. Westinghouse Electric Corp.*, 333 Md. 245, 634 A.2d 1330, 1332 (Md.1994).

In my June 16 Memorandum Opinion, I concluded that the "product" that Compton was providing was the replacement of the van Agtmaels' roof, and thus that the economic loss doctrine does not shield Compton from tort liability because the physical damage in the instant case was to property other than the roof under construction. *Pac. Indem. Co.*, 2008 WL 2440711, at *4 n. 6. Compton argues that I erred in reaching this conclusion, contending that the "product" was the van Agtmaels' entire house, and thus that "all of the damages in the [instant] case are economic loss damages, including but not limited to the roof, the walls, the ceilings, the floors, the utilities, and the contents." (Compton's Mot. for Recons. at 1.)

A.

The majority of the Maryland cases that have addressed the economic loss doctrine are not helpful in resolving whether the damages in the instant case constitute property damage or economic loss, because in those cases there clearly had been no property damage.[FN3] In *Decoster,* however, the Maryland Court of Appeals did address whether the damages sought constituted property damage or economic loss. *Decoster,* 634 A.2d at 1333. The plaintiff, a commercial chicken and egg producer, had suffered loss of more than 140,000 chickens as a result of a power failure that interrupted the power supply to the ventilation system in plaintiff's chicken houses. *Id.* at 1331. Plaintiff filed suit against the manufacturer of the allegedly defective transfer switch, which had failed to activate the emergency backup power system. *Id.* The court explained that "[u]nder *Whiting Turner,* Decoster's ability to pursue an action in tort against Westinghouse for the loss of its chickens turns upon whether its damages are considered physical harm or economic losses and, if the latter, whether the defective switch caused a dangerous condition creating a risk of death or personal injury to humans." *Id.* at 1333. The court concluded that it

> ***2** need not reach the second part of this determination, because the death of the chickens is a loss of physical property, rather than economic loss. Decoster does not seek to recover for the loss of value of the switch, or its replacement or repair costs. Nor does it seek recovery of lost profits from its diminished egg production. These are all economic losses. Instead, Decoster seeks only the replacement of property that was damaged by the alleged defectiveness of the product manufactured by Westinghouse.

Id.

[2] Similarly, in *National Coach Works of Virginia v. Detroit Diesel Corp.,* 128 F.Supp.2d 821, 831 (D.Md.2001), Judge Blake of this court held that, under Maryland law, the purchaser of a bus could recover in tort from the manufacturer of the bus engine for damage to the bus after the bus's engine caught fire and destroyed the bus. The court held that although the economic loss doctrine barred recovery for the engine itself because it was the "defective product," Maryland law "plainly permit[ted]" recovery for "other property" damaged by the engine, including the bus. *Id.* The court relied on the Maryland Court of Appeals' holding in *Decoster,* and the fact that the United States Supreme Court, in *Saratoga Fishing Co. v. J.M. Martinac & Co.,* 520 U.S. 875, 880, 117 S.Ct. 1783, 138 L.Ed.2d 76 (1997), had cited *Decoster* for the principle that while recovery in tort is not permitted for damage to the defective item itself, recovery in tort is permitted for damage to "items added to or used in conjunction with a defective item...." [FN4] *Id.*

B.

As Compton correctly points out, the above Maryland case law does not directly address whether a house and its contents are considered "other property" for purposes of determining whether an allegedly negligent roof contractor is liable in tort for damages to them. (Compton Reply at 11.) For this reason, Compton contends that "Maryland law is ripe for a decision that would broaden the scope of what would be considered economic loss" by following what Compton submits is the "modern trend" in economic loss doctrine jurisprudence: precluding tort liability where damage to "other property" was "foreseeable" or where the damaged "other property" was "part of an integrated system." (Compton Reply at 3; Compton Mem. at 5-13.)

In support of the "foreseeability" approach, Compton cites the Eighth and Sixth Circuits for the rule that "tort remedies are unavailable for property damage experienced by the owner where the damage was a foreseeable result of a defect at the time the parties contractually determined their respective exposure to risk, regardless whether the damage was to the 'goods' themselves or to 'other property.' " *Dakota Gasification Co. v. Pascoe Bldg. Sys.,* 91 F.3d 1094, 1099 (8th Cir.1996); *see also Detroit Edison Co. v. NABCO, Inc.,* 35 F.3d 236 (6th Cir.1994) (applying the economic loss doctrine because it was foreseeable to the parties to the contract that pipes conveying high-pressure steam could explode, and that such an explosion would damage equipment surrounding the pipes).

*3 In support of the "integrated system" approach, Compton cites federal district court opinions for the rule that "damage by a defective component of an integrated system to either the system as a whole or other system components is not damage to 'other property.' " Superior Kitchen Designs, Inc. v. Valspar Indus. (U.S.A.), Inc., 263 F.Supp.2d 140, 145 (D.Mass.2003); see also Myrtle Beach Pipeline Corp. v. Emerson Elec. Co., 843 F.Supp. 1027, 1057 (D.S.C.1993) ("[If] the other property is merely a component part of the overall product itself[,] ... courts uniformly hold that the economic loss doctrine precludes recovery in tort against the manufacturer of the component because the component is integrated into the whole product and the purchaser bargained for the whole product, not merely a component of it."). Compton also cites as support the Maryland Court of Special Appeals' opinion in Pulte Home Corp. v. Parex, Inc., 174 Md.App. 681, 923 A.2d 971, 1004 (Md.Ct.Spec.App.2007), aff'd, 403 Md. 367, 942 A.2d 722 (Md.2008). In that case, plaintiff contended that the allegedly defective synthetic stucco exterior barrier product in the walls of homes caused damage not just to itself but also to the "substrate," to which it was attached, which consisted of "sheathing and framing." Pulte, 923 A.2d at 1003. The Court of Special Appeals upheld the trial court's rejection of plaintiff's argument, agreeing that the barrier product was "part of an 'integrated whole'-a completed home-when the damage occurred, and the damage was, thus, a 'harm to the product itself.' " Id. at 1004.

I am not persuaded, however, that the Maryland courts would apply the "foreseeability" or the "integrated system" approach to the instant case. Other than *Pulte,* Compton has cited no case in which Maryland has adopted either of these approaches. Further, neither approach can be reconciled with the precise distinctions between the "product" and "other property" drawn by the Maryland Court of Appeals in *Decoster* and Judge Blake in *National Coach* . [FN5] As for *Pulte,* the Maryland Court of Special Appeals reasonably concluded that in the sale of a new home, the barrier product was part of an integrated whole with the "sheathing and framing" of the home. 923 A.2d at 1003-04. In contrast, here, Compton's construction work on the van Agtmaels' already existing home was specifically limited to the roof, and thus can be far more easily distinguished as the "defective product" from the "other property" in the house, including the house's walls, interior ceilings, floors, utilities, and contents.

C.

Compton also cites case law applying the economic loss doctrine in defective roofing scenarios in support of its position. (Compton Reply at 6-8.) Two of the cases Compton cites are clearly distinguishable from the instant case. First, in Jones & Laughlin Steel Corp. v. Johns-Manville Sales Corp., 626 F.2d 280, 288-90 (3d Cir.1980), the court held that, under Illinois law, plaintiff steel mill could not recover in strict tort liability for a defective roof. However, unlike in the instant case, plaintiff sought only economic loss damages "for the failure of the product [the defective roof] to perform as it was expected, as distinguished from injuries to persons or other property caused by a defect in the product." Id. at 284. Second, in Citizens Insurance Co. v. Osmose Wood Preserving, Inc., 231 Mich.App. 40, 585 N.W.2d 314, 317 (Mich.Ct.App.1998), the court held that the economic loss doctrine applied to preclude liability for damages to real and business property as a result of the collapse of a defective roof. The court explained: "Unlike some jurisdictions, the economic loss doctrine applies in Michigan even when the plaintiff is seeking to recover for property other than the product itself." Id. at 316. Because Michigan law on this issue stands in direct contrast to Maryland law, it is of no help in determining whether the van Agtmaels' house was "other property."

*4 At first glance, another case cited by Compton, Chicago Heights Venture v. Dynamit Nobel of America, Inc., 782 F.2d 723, 729 (7th Cir.1986), provides support for its position. There, the Seventh Circuit held that, under Illinois law, defendant was shielded from tort liability for damage to other parts of the building caused by the lack of adequate roofing. Relying on *Jones & Laughlin,* the Seventh Circuit recognized that in that case the plaintiff "did not seek damages for any injury to property other than the roof itself." *Id.* However, the Seventh Circuit "believe[d]" that this distinction-that the plaintiff in *Jones & Laughlin* requested only damages for injury to the product while the plaintiff in *Chicago Heights Venture* requested damages for injury to the other property-would not be considered "legally significant" to the Illinois courts. *Id.* To the contrary, in United Air Lines, Inc. v.

CEI Industries of Illinois, Inc., 148 Ill.App.3d 332, 102 Ill.Dec. 1, 499 N.E.2d 558, 563 (Ill.App.Ct.1986), the Illinois Appeals Court expressly held such a distinction *was* legally dispositive. The court held that, under Illinois law, a warehouse owner could recover in tort for damage to a building caused by a defective roof because United "suffer[ed] damages to property other than the defective product as a result of the water leakage defect in the roof which caused the sudden and violent collapse of its interior ceiling upon its walls, furniture and furnishings. United has thus made a showing of harm above and beyond disappointed expectations." FN6 *Id.*

For these reasons, I am not persuaded that any of the case law Compton cites provides guidance as to what is "other property" for purposes of the economic loss doctrine in defective roof scenarios under Maryland law.FN7

D.

[3] In light of the Maryland Court of Appeals' decision in *Decoster* and Judge Blake's decision in *National Coach*, I conclude that, under Maryland law, the economic loss doctrine does not shield Compton from tort liability for damages to the van Agtmael's house and its contents, with the exception of the roof itself. Compton was allegedly negligent in replacing the van Agtmaels' roof, and thus is potentially responsible for all damage to "other property" resulting from that negligence, including damage to the house's walls, interior ceilings, floors, utilities, and contents. As I stated in my June 16, 2008 Memorandum Opinion, a subcontractor performing work owes "[a]t least reasonable care and precautions...." *See* Pac. Indem. Co., 2008 WL 2440711, at *4 n. 6 (quoting *Klein v. Dougherty*, 200 Md. 22, 87 A.2d 821, 825 (Md.1952)). In *Klein*, the court held that defendant subcontractors were liable under tort law for smoke damage caused by their negligent installation of a furnace smoke pipe into a chimney, because "[n]either of [the subcontractors] exercised such care as a qualified person would ordinarily have exercised under the circumstances of this case." Klein, 87 A.2d at 824-25. For this reason, and the reasons above, I conclude that if Compton is found to have been negligent, it is responsible in tort for damage to property other than the van Agtmaels' roof itself.

II.

***5** [4] [5] As to Whaley's indemnification claim, Compton argues again that it should be dismissed "because Whaley committed active negligence, and the plaintiff's complaint alleges active negligence with respect to Whaley." (Compton Mem. at 14.) As I stated in my June 16 Memorandum Opinion, neither of these contentions is accurate. Under Maryland law, if the conduct attributed to the party seeking indemnification in the original plaintiff's complaint constitutes active negligence, or if it is clear from the complaint that this party's liability would only arise from proof of active negligence, then there is no valid claim for indemnity. *Kelly v. Fullwood Foods, Inc.*, 111 F.Supp.2d 712, 714 (D.Md.2000). Pacific Indemnity Company's complaint alleges that the damage to the van Agtmael's property "was caused by the negligence ... of defendant Whaley ... and/or [his] subcontractors...." (Compl .¶ 18.) The conduct attributed to Whaley in the complaint does not constitute active negligence because the complaint specifically leaves open the possibility that Compton was the actively negligent party. Accordingly, Whaley's liability could arise from proof of passive negligence. Further, there is a genuine dispute on the summary judgment record as to whether Whaley and/or Compton were negligent, and, if so, whether their negligence was active or passive. *See* Pac. Indem. Co., 2008 WL 2440711, at *5. For these reasons, I held and continue to hold that Whaley's indemnification claim must survive summary judgment. *Id.*

For the foregoing reasons, I deny Compton's motion for reconsideration. A separate order to that effect is being entered herewith.

FN1. Compton also requests that I reconsider my conclusion that Compton owes a tort duty to the van Agtmaels. (Compton Mem. at 3.) In my June 16, 2008 Memorandum

Opinion, I cited the following language for the Maryland rule that contractual privity is not required to establish a tort duty: " 'The requirement of privity of contract has been abandoned as a basis for recovery by third parties for physical harm to themselves and tangible things against those who negligently supply, repair, or construct things so as to leave them in an unreasonably dangerous condition.' " *See* Pac. Indem. Co., 2008 WL 2440711, at *4 n. 6 (quoting *Council of Co-Owners Atlantis Condo., Inc. v. Whiting-Turner Contracting Co.*, 308 Md. 18, 517 A.2d 336, 341 (Md.1986)). As Compton correctly points out, no unreasonably dangerous condition existed in the instant case. However, I had meant this citation only for purposes of making clear that contractual privity is not required to establish a tort duty. I should have also cited the following language from the same case: "In following the modern trend, we hold that privity is not an absolute prerequisite to the existence of a tort duty." *Whiting-Turner*, 517 A.2d at 343.Under Maryland law, whether a tort duty should be recognized in a particular context depends on "two major considerations": (1) "the nature of the harm likely to result from a failure to exercise due care," and (2) "the relationship that exists between the parties." *Jacques v. First Nat'l Bank of Md.*, 307 Md. 527, 515 A.2d 756, 759 (Md.1986). "Where the failure to exercise due care creates a risk of economic loss only, courts have generally required [contractual privity or its equivalent] between the parties as a condition to the imposition of tort liability." *Id.* at 759-60. As I discuss *infra,* because I conclude that Compton's alleged negligence created a risk of (and ultimately resulted in) property damage, rather than purely economic loss, I hold that Compton owes a tort duty to the van Agtmaels notwithstanding their lack of contractual privity.

FN2. The Maryland Court of Appeals has explained the rationale behind the economic loss doctrine as follows: "A manufacturer may be held liable [under tort law] for physical injuries, *including harm to property, caused by defects in its products* because it is charged with the responsibility to ensure that its products meet a standard of safety creating no unreasonable risk of harm." *Lloyd v. Gen. Motors Corp.*, 397 Md. 108, 916 A.2d 257, 265 (Md.2007) (citation omitted) (emphasis added). By contrast, "*where the loss is purely economic,* the manufacturer cannot be charged with the responsibility of ensuring that the product meet[s] the particular expectations of the consumer unless it is aware of those expectations and has agreed that the product will meet them. Thus, generally, the only recovery for a purely economic loss would be under a contract theory." *Id.* (emphasis added).

FN3. For example, in *Whiting-Turner,* a condominium owners' association brought suit against a general contractor, developer, and architects of their building, alleging that defendants had negligently constructed defective vertical utility shafts in the building. 517 A.2d at 338. Because defendants' alleged negligence had not caused physical harm to any person or property, the Maryland Court of Appeals had to determine whether defendants had any tort duty to plaintiff based solely on the economic loss of reconstructing the utility shafts. *Id.* at 344-45. Recognizing that the economic loss doctrine would normally preclude tort liability, the court carved out an exception from the doctrine, concluding that notwithstanding the lack of personal injury or property damage, where the "risk generated by the negligent conduct ... is of death or personal injury the action will lie for recovery of the reasonable cost of correcting the dangerous condition." *Id.* at 345. Because the court found that the construction defects in the utility shafts created a serious risk of injury to residents of the building, it allowed recovery in tort to correct those defects.Since *Whiting Turner,* the Maryland Court of Appeals has in at least three other cases grappled with the issue of whether-although the alleged negligence of a defendant had not caused personal injury or property damage, but rather only economic loss-the risk of injury resulting from the negligence was serious enough to warrant tort liability. *See U.S. Gypsum v. Mayor & City Council of Baltimore*, 336 Md. 145, 647 A.2d

405, 410 (Md.1994) (holding that the risk of death or injury caused by asbestos-containing building materials was serious enough to warrant tort liability); *Morris*, 667 A.2d at 633 (holding that the risk of injury caused by defendant's alleged negligence in manufacturing defective plywood used in building houses was serious enough to warrant tort liability); *Lloyd*, 916 A.2d at 270 (holding that the risk of bodily injury because of the alleged negligent manufacturing of defective automobile seats was not serious enough to warrant tort liability).

FN4. In *Saratoga*, the Supreme Court held that under admiralty law, plaintiff (the second user/owner of a fishing vessel) could recover in tort from the manufacturer of the vessel's allegedly defective hydraulic system for damages to extra equipment added to the ship by the first user/owner of the vessel, because the extra equipment was "other property." 520 U.S. at 877. The Court stated:State law often distinguishes between items added to or used in conjunction with a defective item purchased from a Manufacturer (or its distributors) and ... permits recovery for the former when physically harmed by a dangerously defective product. Thus, the owner of a chicken farm, for example, recovered for chickens killed when the chicken house ventilation system failed, suffocating the 140,000 chickens inside. *[See Decoster*, 634 A.2d at 1330.]

Id. at 880, 634 A.2d 1330.

FN5. I note that the Third Circuit rejected the "foreseeability" and "integrated system" approaches in *2-J Corp. v. Tice*, 126 F.3d 539 (3d Cir.1997). In that case, a purchaser of a pre-engineered warehouse sued the warehouse's manufacturer for negligence, products liability, and breach of contract, alleging that the warehouse collapsed and damaged goods stored therein. *Id.* at 540. The court addressed the issue of "whether property becomes a part of the product itself solely because, after the sale to the initial user, it is foreseeably utilized in connection with the owner's use of the product." *Id.* at 544. The court held:[I]t seems apparent to us that if the fishing equipment foreseeably added to the ship by the initial user in *Saratoga Fishing[*, 520 U.S. at 880,] did not become a part of the 'product itself,' it necessarily follows that the inventory foreseeably stored by the initial user in the warehouse here did not become a part of the warehouse itself. Accordingly, we believe that the district court's 'integration' theory in this case is inconsistent with *Saratoga Fishing* and that it follows *a fortiori* from the holding in *Saratoga Fishing* that 2-J can recover for the loss of its inventory and other property stored in its warehouse.

Id. at 544.

FN6. I recognize that the different decisions in *Chicago Heights Venture* and *United Air Lines* were at least in part a result of the Seventh Circuit's and the Illinois Appeals Court's different interpretations of the Illinois Supreme Court's holding in *Redarowicz v. Ohlendorf*, 92 Ill.2d 171, 65 Ill.Dec. 411, 441 N.E.2d 324 (Ill.1982). While the Seventh Circuit understood *Redarowicz* to preclude liability for damage to other property resulting from a latent construction defect, *Chicago Heights Venture*, 782 F.2d at 729, the Illinois Appeals Court understood *Redarowicz* to preclude liability only for damage to the defective product itself, *United Air Lines*, 102 Ill.Dec. 1, 499 N.E.2d at 562. In any event, the conflict between these two cases demonstrates that Illinois law does not provide clear guidance on what is "other property" where a defective roof has caused damage.

FN7. I recognize also that the Maryland Court of Appeals noted in *Whiting-Turner* that a contractor's tort liability "is in general limited to situations where the conduct of the builder causes an accident out of which physical harm occurs to some person or tangible thing *other than the building itself that is under construction.*" 517 A.2d at 344 (emphasis added). I do not believe, however, that the court's language has any bearing on what is "other property" in defective roof scenarios, because, as discussed *supra*, plaintiff in *Whiting-Turner* did not allege that there was any damage to property other than the product itself. *Id.* Further, the court discussed the building as a whole because the defendants had negligently constructed defective vertical utility shafts in the entire building. *Id.* at 338. In the instant case, by contrast, Compton worked specifically only on the van Agtmaels' roof, not their entire house.

D.Md.,2008.
Pacific Indem. Co. v. Whaley
--- F.Supp.2d ----, 2008 WL 3914896 (D.Md.)

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