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IN THE SUPREME COURT OF THE STATE OF IDAHO

APRIL BEGUESSE, INC.,

An Idaho Corporation,

Plaintiff/Counterdefendant/Respondent,

v.

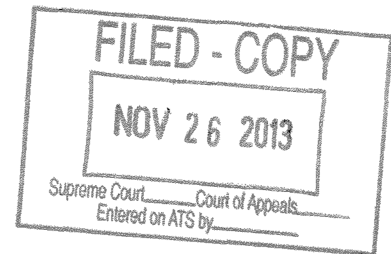
KENNETH RAMMELL, an individual, and CHRISTA BEGUESSE, INC., an Idaho Corporation,

Defendants/Counterclaimants/Appellants.

Supreme Court Docket No. 40212

Seventh Judicial District Court

Docket No. CV-2009-2767



APPELLANTS' REPLY BRIEF

Appeal from the District Court of the Seventh Judicial District

of the State of Idaho, in and for the County of Bonneville

Honorable Joel E. Tingey, District Judge, Presiding

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TABLE OF CONTENTS

Table of Authorities 2

Argument 3

1. Falsity with respect to ownership of the files. 3

2. Falsity with respect to the "proprietary software." 6

3. Materiality and justifiable reliance. 7

4. Damages 8

5. Attorney fees pursuant to Idaho Code § 12-121 12

Conclusion 13

TABLE OF AUTHORITIES

Cases

Bank of Commerce v. Jefferson Enters., LLC, 303 P.3d 183, 192 (2013) 2, 10
Burrus v. Wilkinson, 31 Miss. 537, 544 (Miss. 1856) 5
Chandler v. Chandler, 136 Idaho 246, 249-250 (2001) 9
Chavez v. Barrus, 146 Idaho 212, 223, 192 P.3d 1036, 1047 (2008) 2
Gillette v. Storm Circle Ranch, 101 Idaho 663 (1980) 9
Hitchcock v. Tollison, 213 Ga. App. 477, 479 (Ga. Ct. App. 1994) 4
Hodges v. Wilkinson, 111 N.C. 56, 61 (N.C. 1892) 4, 5
Nab v. Hills, 92 Idaho 877, 884 (1969) 9
Rino v. Statewide Plumbing & Heating Co., 74 Idaho 374, 378 (1953) 8
Sanchotena v. Tower Co., 74 Idaho 541, 546 (Idaho 1953) 12
Shrives v. Talbot, 91 Idaho 338, 345, 421 P.2d 133, 140-41 (1966) 7, 8, 10
Standing v. Midgett, 850 F. Supp. 396, 400-401 (E.D.N.C. 1993) 5
Walston v. Monumental Life Ins. Co., 129 Idaho 211, 216 (1996) 7, 8
Weitzel v. Jukich, 73 Idaho 301, 251 P.2d 542 (1952) 8

ARGUMENT

This Court recently held that for a fraud claim to succeed a plaintiff must "establish nine elements with particularity: (1) a statement or a representation of fact; (2) its falsity; (3) its materiality; (4) the speaker's knowledge of its falsity; (5) the speaker's intent that there be reliance; (6) the hearer's ignorance of the falsity of the statement; (7) reliance by the hearer; (8) justifiable reliance; and (9) resultant injury." *Bank of Commerce v. Jefferson Enters., LLC*, 303 P.3d 183, 192 (2013), *citing Chavez v. Barrus*, 146 Idaho 212, 223, 192 P.3d 1036, 1047 (2008).

In *Jefferson Enterprises, supra,* the Court examined in detail the alleged false statements made by bank representatives, and concluded that the plaintiff's evidence showed only his understanding, his hopes, his "hunches," but not the bank's representations with sufficient clarity on which to find a material misrepresentation of fact. *Id. at 193*. Similarly, in the instant case, April Beguesse testified at length as to her "understanding" and "belief," but presented no clear and convincing evidence that either Mr. Rammell or Christa Rammell made an intentional, false, material statement of fact that April justifiably relied on to her resultant injury.

In opposition to the various arguments raised by the Appellants (hereinafter "Rammell"), the Respondent ABI argues that the evidence was sufficient to prove the elements of falsity, materiality and reliance, justifiable reliance, and damages. ABI's arguments must fail.

1. Falsity with respect to ownership of the files.

A quick review of the testimony cited by ABI shows that April testified to what she "understood"[1] and what she "thought,"[2] but not at all as to what Ken or Christa Rammell *said* that was intentionally false. Fraud is premised on an intentional misrepresentation of fact, which must be proven with clear and convincing evidence; evidence of what the other party *believed* may be relevant to show reliance, or the lack of reliance, but it does not prove an intentional misrepresentation. Without showing the alleged false statements in clear and convincing detail, the fraud claims must fail.

[1] R. Brief 14, 15, 16; T. 116:6-12; 119:13-25; 239:18-240:14

[2] R. Brief 15, T. 119:13-25

In addition, ABI failed to prove that the statements about ownership of the "library of files," if they were ever made, were in fact false. The Rammell defendants stand by their arguments in their prior brief that the very concept of "ownership" of the computer files is meaningless under these circumstances, where the files have value only to a typesetter who is engaged to provide services to the copyright owner, and the copyright owner is always given a copy of the most current version of the files. Under those circumstances, the files cannot be sold except as one of the necessary assets needed by a purchaser of the typesetting business. They have no value apart from the typesetting business. They cannot be sold even to the copyright owner, because they already have a copy.

However, even assuming that "ownership" as asserted by ABI is relevant in this case, and that the Rammells made a representation that they owned the files, ABI failed to prove that some other party actually "owns" the files. The testimony presented was only that the president of division of West Publishing that owns the copyrights claims that West "owns" the files because it owns the copyrights[3], and ABI cannot transfer the files to a third party without her approval.[4] This does not amount to even a claim of "ownership" of the files, but only a claim for protection of copyrights. Even if it can be taken as a claim of ownership of the files, a mere competing claim to ownership is insufficient to establish that the Rammells' claim of ownership was intentionally false.

Given that the fraud alleged here is based on a competing claim of ownership of the property sold, proof that the Rammells' claim of ownership was false would necessarily prove that they breached a warranty of title. Therefore, it is reasonable to look at cases involving claims for breach of warranty of title to determine whether proof of a mere competing interest is sufficient to establish the claim, because fraud requires a higher level of proof. It would be untenable that a plaintiff could prove a fraud on evidence that would not suffice to prove a breach of warranty.

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[3] T. 303, Deposition of Linda Diamond Raznick 38.15-.18

[4] T. 302, Deposition of Linda Diamond Raznick 37.6-.19

Courts have recognized that the warranty of title to chattels is analogous to, and subject to the same analysis as, the covenant for quiet enjoyment of land. *Hodges v. Wilkinson*, 111 N.C. 56, 61 (N.C. 1892). Thus, cases involving land are instructive.

It is generally the rule that, in a breach of warranty of title case, the existence of a competing interest is insufficient to prove breach of warranty in the absence of the buyer's actual dispossession or some other proof of the validity of the competing claim. Thus, the Georgia Court of Appeals held that a breach of the covenant of warranty of title requires "an eviction or an equivalent disturbance by title paramount must occur, and that the mere existence of an outstanding paramount title will not constitute a breach." *Hitchcock v. Tollison*, 213 Ga. App. 477, 479 (Ga. Ct. App. 1994). In other words, even proof that the competing title was superior was not sufficient proof. The same court went on to hold that, with regard to warranties against encumbrances, "no actual eviction was necessary. ... However, a showing of mere existence of an encumbrance has been held to be insufficient. ... In order to recover on a warranty of seizin, the loss of seizin (that is, eviction,) had to be proved. . . . On a covenant against encumbrances, the only condition precedent to a right of action [is] the outstanding of a valid encumbrance at the date of the covenant affecting the property conveyed, and its discharge by the covenantee." *Id.* at 479-480 (citations omitted).

The Supreme Court of Mississippi, in an old case, held that "a covenantee may recover upon such a warranty, though he may have yielded the possession voluntarily, provided the title to which he yielded be good and paramount to that of his warrantor; because against such a title he is not obliged to submit to a law suit, upon a claim which must certainly prevail. But in such a case, the burthen of proof of the paramount title is upon him." *Burrus v. Wilkinson*, 31 Miss. 537, 544 (Miss. 1856).

The Supreme Court of North Carolina held the same in *Hodges v. Wilkinson, supra.*

In a more recent case out of North Carolina, involving the sale of a boat, the U.S. Court for the Eastern District of North Carolina held that a claimed competing lien, even though it was ultimately held to be inferior to the purchaser's title, was sufficient to establish a breach of warranty where the seller knew of the lien and failed to disclose it. *Standing v. Midgett,* 850 F. Supp. 396, 400-401 (E.D.N.C.

1993). However, the Court went on to hold that no damages were recoverable until the buyer either paid the outstanding lien, or was deprived of possession by the lien, or alleged and proved some special damages resulting from the lien – such as the cost of successfully defending his possession of the boat against the lienholder. *Id.*

In all of these cases, proof of a breach of the warranty or covenant of title requires some proof that goes beyond a mere competing claim. When the claim is fraud based on the same facts, namely, a false statement as to ownership, the proof must be no less (and in fact, the proof required is much greater). In this case, the proof at trial was merely this: that Linda Diamond Raznick claimed that West owns the copyright and therefore ABI can't sell its files without West's permission. This is at best merely a competing claim, and insufficient to prove breach of warranty, much less fraud. ABI failed to prove a false statement with respect to ownership of the files.

2. Falsity with respect to the "proprietary software."

The evidence adduced at trial fails to show a false statement of fact regarding "proprietary software" by the Defendants. The Plaintiff acknowledges that it received not only the PageMaker software, but "strings of macros and commands" that were developed over many years of work by Christa Beguesse, which enabled her to conduct her business with great speed and efficiency. As discussed in Rammells' previous brief, these strings of macros and commands, even if they were developed within PageMaker, constitute computer software and protectable trade secrets under Idaho law. A trade secret is, by definition, proprietary.

The sole evidence of a particular false statement produced at trial was that Christa once told a civic group that she had developed special software to speed her workflow, which gave her a competitive edge. She freely acknowledged, perhaps with some trepidation because it was a trade secret, that this software was not created from scratch, but was developed within the typesetting software she regularly used. Whether April heard this statement or not, it establishes that Christa told the truth about the nature of the software to total strangers in April's presence. This is inconsistent with a conclusion that she intentionally misled April about the nature of the software for five years. The fact that April was able to

discover the truth about the software merely by reading the manual also in inconsistent with the existence of a scheme to mislead her. It is consistent with simple ignorance on the part of April, but not with malice and deception on the part of Christa. Therefore, a reasonable jury could not have concluded on the basis of this evidence that there was clear and convincing evidence of an intentional false statement of fact.

3. Materiality and justifiable reliance.

ABI in its brief highlights a few vague statements that supposedly caused April to understand that she would "own" the files and could later sell them. Resp. Brief at 17-18. She contends these show she relied on these statements. But this ignores the fact that she admitted she knew she could not sell the files without West's agreement to work with the purchaser, which rendered any question about ownership moot. It does not matter to ABI or to a potential buyer who "owns" the files when the only relevant question is whether the customer will continue to work with the buyer.

ABI argues that April expected she could sell the files to West at the time West quit doing business with her, but this beggars belief. West already had the files, since CBI, and ABI (after it took over the business), routinely provided West with copies of the latest PageMaker version, which West used to create a CD-ROM version of the publication.[5] ABI does not and cannot explain why April would think West would pay ABI anything for computer files she had already handed over to them free.

Thus, the alleged statements, at least as April now characterizes them, were not material, and could not be reasonably relied on in the way April now claims.

4. Damages

ABI argues in its brief[6] that because April Beguesse was able to put a number to the supposed value of the business as of the day in January 2004 that she took it over, that is sufficient evidence for a jury to award damages. ABI's argument is wrong for a number of reasons: it is the wrong measure of damages, the wrong time for measuring damages, and it ignores the actual financial success of the

[5] T. 165.22-166.13
[6] Beginning at p. 20

business over the period of the contract; it fails to show that the damages resulted from the alleged fraud; and it is speculative and unproven, because it relies on assumed facts that have not been proven.

a. Wrong measure of damages.

April Beguesse testified that the business as she received it on January 1, 2004, had a value of "about $250,000.00."[7] She reached this number by adding the value of the physical assets to the value of the training and mentoring she received, and assuming no value for the "library of files" because she did not own them.[8] April then claims damages based on the difference between this January 2004 value and the amount she paid for the business over the ensuing five years.[9]

The damages ABI claims is based on a very mechanistic application of the so-called "out-of-pocket rule," citing *Walston v. Monumental Life Ins. Co.*, 129 Idaho 211, 216 (1996)(*citing Shrives v. Talbot,* 91 Idaho 338, 345, 421 P.2d 133, 140-41 (1966)). ABI focuses on the supposed value of the business as of the day she took over, compared to the total amount she paid for it, without taking into account the actual financial performance of the business in the ensuing years.

In *Walston*, *supra,* and in *Shrives, supra,* this Court cautioned trial courts and lawyers that the "out-of-pocket rule" and the "benefit of the bargain rule" are not exclusive, and that the actual measure of damages in a given case was whatever was appropriate under the facts of the case:

> The underlying principle is that the victim of fraud is entitled to compensation for every wrong which is the natural and proximate result of the fraud. The measure of damages which should be adopted under the facts of a case is the one which will effect such results.

Walston, supra at 346, (quoting *Weitzel v. Jukich*, 73 Idaho 301, 251 P.2d 542 (1952). Furthermore, the Court should note that the "out-of-pocket rule" is not a special measure of damages used only in fraud cases; it is also used in breach of contract and warranty cases. *See Rino v. Statewide Plumbing & Heating Co.,* 74 Idaho 374, 378 (1953). It should therefore not be necessary to add that the proper measure of

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[7] T. 158.15
[8] T. 156.19 to 158.15
[9] T. 158.16-.19

damages in a fraud case, as in a breach of contract case, should not compensate the "victim" for wrongs not suffered, or fail to take into account the benefits received.

In this case, every penny that ABI paid for the business was generated by the business. ABI was not "out of pocket" anything.[10] *After* paying $708,000.00 to CBI, and all other expenses, ABI made, in profits and salary paid to April Beguesse, in excess of $1,057,000.00 between 2004 and 2011.

ABI would like this Court to ignore these facts, and argues that the "out-of-pocket rule" measures damages as of the date of the transaction, and subsequent events are irrelevant. But this information is nevertheless relevant to determining how much ABI was actually damaged by this transaction. Because of the transaction at issue in this case, and only because of this transaction, April Beguesse found herself the proprietor of a business that created $1,765,000.00 in salary and profits from 2004 to 2011, only $708,000.00 of which was paid to the Defendants.

First, it is not credible that a business which creates such wealth can be valued at only $250,000.00. This is an indication that ABI chose the wrong measure of damages, one which focuses on book values of assets rather than the value of a business as a going concern. April Beguesse knew that the principal asset, the "library of files," had *no* value apart from its use to typeset files for the customer.[11] Therefore, the business should have been valued as a going concern, with its actual past performance calculated in as the value of intangible assets such as goodwill.

> Two values must be considered when determining the overall value of a business: intangible assets and tangible assets. The value of the business is determined when the two factors are combined. "Goodwill" (an intangible asset) is an appropriate factor in determining the value of a business. .... Goodwill represents "the advantage or benefit, which is acquired by an establishment, beyond the mere value of the capital, stock, funds, or property employed therein, in consequence of the general public patronage and encouragement which it receives from constant or habitual customers, on account of its local position, or common celebrity, or reputation for skill or affluence ..."

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[10] T. 185-186 for 2004; T. 204-209 for remaining years

[11] T. 234.25-236.18

Chandler v. Chandler, 136 Idaho 246, 249-250 (2001), *quoting Newark Morning Ledger Co. v. United States,* 507 U.S. 546, 555, 123 L. Ed. 2d 288, 113 S. Ct. 1670 (1993). The measure of damages testified to by April Beguesse refused to take into account the intangible assets that permitted her business to succeed as it did.

Second, it would be unjust to apply a measure of damages which looks only at the debit side of the ledger and ignores all benefits received by the "victim" in the transaction at issue. This Court has recognized the necessity for the trial court to "balance the equities" to avoid the unjust enrichment of a plaintiff in a fraud case when the plaintiff has received benefits which it cannot or will not return to the defendant. *Nab v. Hills*, 92 Idaho 877, 884 (1969).

In addition, this Court has held that it is the obligation of a plaintiff to provide both sides of the equation from which the proper measure of damages can be computed. In *Gillette v. Storm Circle Ranch,* 101 Idaho 663 (1980), which was an unjust enrichment case arising from the sale of agricultural property, the plaintiff put on evidence of the cost to him of certain work done on the land before the sale, but failed to produce evidence of the extent to which the defendant retained the value of that work. This Court reversed the award of damages in favor of the plaintiff. *Id.* at 667.

In this case, while the Plaintiff reluctantly provided the evidence of the benefits to ABI, the *measure of damages* testified to by April Beguesse failed to take it into account. It was this inadequate measure of damages which the Court below referred to when it entered judgment in this case. Thus, both the jury verdict and the judgment entered after acceptance of the remittitur are unsupported by sufficient evidence.

The Court below erred when it failed to grant directed verdict and permitted the case to go to the jury on insufficient evidence of damages.

b. The measure of damages does not result from the fraud.

The measure of damages testified to by April Beguesse results entirely from her testimony that the "library of files" has no value because ABI cannot sell them.[12] However, it is undisputed that ABI can sell them with the customer's approval,[13] and that April Beguesse was always aware that her customer's approval would be required before she could transfer the business to a third party.[14] Thus, the fraud found by the jury could not possibly relate to ABI's supposed inability to sell the files to a third party; yet the damages claimed in this case, and the sole evidence of damages testified to by the plaintiff, flow entirely from this cause.

The plaintiff in a fraud case must prove not only the fact of injury, and the amount of injury, but also that it was in fact caused by the fraud in question. In *Bank of Commerce v. Jefferson Enters., LLC*, 303 P.3d 183, 192, *supra,* the formulation used is "resultant injury." Other formulations that have been used include "consequent and proximate injury,"[15] the "damage occasioned thereby;" *Shrives v. Talbot, supra,* 91 Idaho at 344; and others. All of these formulations focus on the need to prove that the damages established resulted from the fraud, and not from some other source.

It is undisputed that the "damages" April testified to were not the result of fraud, but of a business risk known to the her at the time she entered into this transaction: namely, that she could not sell the business to just anyone who offered her money, but only to a buyer with whom the customer was willing to work. It was error for the trial court to deny directed verdict and permit the case to go to the jury when ABI failed to prove one of the elements of fraud.

ABI asserts that damages are based not only on the fact that it supposedly cannot sell the business and/or the files to a third party, but also on the fact that it cannot sell the files back to its customer.[16] However, April was aware at the time she entered into the transaction that the customer required CBI to

[12] T. 157.15-.18; 158.20-159.5

[13] T. 302, Deposition of Linda Diamond Raznick 37.6-.19

[14] This was the basis of the Trial Court's grant of summary judgment as to one fraud count. See R. 107.

[15] King v. McNeel, 94 Idaho 444, 446 (1971)

[16] Respondent's Brief, p. 8

hand over a free copy of the files in PageMaker format every time an update is completed.[17] She does not explain why any reasonable person would expect that the customer would later pay for the same files. Thus, there was no evidence in the record to support a finding of fraud on this theory.

c. Speculative and unproven damages.

ABI's proof of damages is based on an unproven assumption: that it cannot sell the business and/or the files. The only evidence heard at trial on the issue of whether the business could be sold is this: that Linda Diamond Raznick, president of The Rutter Group, ABI's sole customer, testified that ABI could not sell the business or files without her permission, which implies that she could sell them with permission; and that CBI sold the business and files without difficulty to plaintiff ABI.

Since the only evidence presented at trial established that the business could be sold, damages premised on a belief that it could not be sold were unproven and insufficient to support a jury verdict. At the very least, April's belief she could not sell the business in the future is speculative, as previously argued.

Respondent argues that these damages are not speculative because they are based on an event that already took place: ABI's purchase of a business supposedly worth $250,000.00 for more than $700,000.00.[18] Yet this ignores that the $250,000.00 valuation placed on the business assumes that it cannot be sold in the future, an event which has not occurred and is purely speculative.

The Court below erred when it failed to grant directed verdict and permitted the case to go to the jury on speculative and unproven damages.

5. Attorney fees pursuant to Idaho Code § 12-121

Respondent argues that it is entitled to fees on the grounds that the appeal is frivolous.[19] ABI argues that the appeal merely asks the Court to reweigh the evidence. That is untrue. While certain arguments raised in this appeal ask this Court to examine the evidence, it is for the purpose of determining whether it is legally sufficient to support the jury verdict, or so deficient as a legal matter as

[17] T. 165.22-166.13
[18] Respondent's Brief at 23
[19] Respondent's Brief at 43

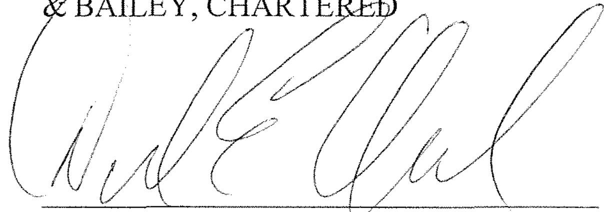
to require a directed verdict or grant of JNOV. The mere fact that an argument requires an examination of evidence, even conflicting evidence, does not make an appeal frivolous; such an examination is within the proper purview of an appellate court. *See, e.g., Sanchotena v. Tower Co.*, 74 Idaho 541, 546 (Idaho 1953).

CONCLUSION

With respect to other issues raised by the briefing herein, Appellant references and incorporates arguments raised in its previous brief. Appellant asks this Court to hold as a matter of law that the evidence presented at trial was not sufficient to prove the Plaintiff's claims, and reverse the judgment entered by the Court below with respect to the fraud and breach claims; also, that this Court reverse the judgment entered with respect to CBI's counterclaim, and remand to the trial court for an award of damages, or, in the alternative, that the counterclaim be remanded to the trial court for a new trial.

Dated this 25th day of November, 2013.

RACINE OLSON NYE BUDGE
& BAILEY, CHARTERED

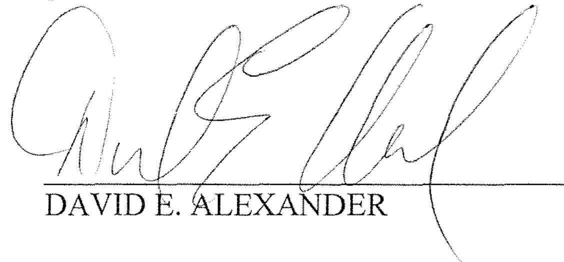


DAVID E. ALEXANDER

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 25th day of November, 2013, I served a true and correct copy of the above and foregoing document to the following person(s) as follows:

Jeffrey D. Brunson John M. Avondet BEARD ST. CLAIR GAFFNEY PA 2105 Coronado Street Idaho Falls, Idaho 83404-7495	[X] U. S. Mail Postage Prepaid [ ] Hand Delivery [ ] Overnight Mail [ ] Facsimile



DAVID E. ALEXANDER