

## Dismissal of manufacturer's product liability claim vs. supplier reversed

*1st Circuit: trial judge applied tort standard to contract-based claim*

By: Eric T. Berkman © July 3, 2019



The plaintiff produced power supply units for EMC Corp. to use in its data storage devices. The plaintiff claimed thousands of microcircuits it purchased from its supplier were defectively designed.

A manufacturer that alleged another company breached the implied warranty of merchantability by selling it defectively designed parts was not required to prove the defect was foreseeable by reasonable testing in order to sustain its claim, the 1st U.S. Circuit Court of Appeals has ruled.

Plaintiff AcBel Polytech, which produced power supply units for EMC Corp. to use in its data storage devices, claimed that thousands of re-designed microcircuits it purchased from its own supplier, defendant Fairchild Semiconductor Corp., to serve as voltage regulators for the units, were defectively designed, causing EMC's devices to falter and resulting in economic harm to the plaintiff.

The microcircuits apparently did not malfunction when subjected to industry-standard testing, and Fairchild's expert testified at a bench trial that the failure could only be duplicated by creating extreme conditions.

After trial, a U.S. District Court judge dismissed AcBel's claim, holding that the plaintiff failed to show that Fairchild could have discovered that the product was either dangerous or defective through reasonable testing.

But the 1st Circuit reversed, holding that reasonableness of testing is "inconsequential" in a breach of implied warranty case that alleges harm only to the product itself.

"By considering foreseeability by reasonable testing for its analysis of the ... implied warranty of merchantability test, the district court improperly commingled contract-based and tort-based theories of implied warranty," Judge Juan R. Torruella wrote for the court. "When economic loss is the only injury that is claimed, recovery for breach of an implied warranty should be construed as contract-based, not tort-based, under Massachusetts law."

The 40-page decision is *AcBel Polytech, Inc. v. Fairchild Semiconductor International, Inc., et al.*, Lawyers Weekly No. 01-152-19. The full text of the ruling can be found [here](#).

### Important clarification

Zeb Landsman of New York, lead counsel for the plaintiff, said he was pleased the 1st Circuit agreed that there is no foreseeability requirement when bringing a contract claim for breach of implied warranty of merchantability.

"We look forward to prosecuting our breach and fraud claims before the District Court," Landsman added.

Matthew Iverson of Boston, who represented the defendant, did not respond to requests for comment.

But David B. Mack, a business litigator in Burlington, said the 1st Circuit has drawn a clear distinction between tort-based and contract-based implied warranty of merchantability claims.



Sees ruling as 'groundbreaking'

"This appears to be a groundbreaking decision in that no court had used that distinction to cast aside the manufacturer's reasonable testing defense," he said. "It will be interesting to see if other courts take the 1st Circuit's lead."

Aliki Sofis of Boston, who litigates product liability claims and complex commercial disputes, agreed that the decision provides important clarification.

"Massachusetts recognizes the economic loss doctrine, which this opinion cites to, and if a plaintiff is claiming money damages or economic loss, they're left with only a contract claim and not a tort claim," she said. "In that case the plaintiff has to show that its use of the product was reasonably foreseeable, not that the defect itself was reasonably foreseeable."

Sofis added that while it is easy to "blur the lines" in this area of the law, the decision "really crystallizes what the law is and the differences between a contract theory and a tort theory."

Boston attorney David L. Ferrera, who defends drug and device manufacturers in tort-based product liability claims, said that in the cases he handles, industry-accepted testing and what industry professionals like the Food and Drug Administration and international standards organizations have to say carries significant weight.

Because companies rely so heavily on industry standards during their manufacturing processes, Ferrera found it potentially problematic that in a contract-based action, the reasonableness of testing would be deemed "inconsequential" by the court.

"In a high-tech, complex business economy like Massachusetts, having lay juries decide these questions rather than allowing companies to rely on industry-accepted standards seems unfair to businesses who rely on certainty in establishing their design and manufacturing processes," Ferrera said.

David A. Barry, a Boston attorney who also handles product liability cases, said the distinction between tort-based and contract-based claims is unique to Massachusetts. He also said that distinction can have consequences beyond applicability of the foreseeability of reasonable testing requirement.



"The court's opinion is a reminder to Massachusetts practitioners that important consequences follow depending upon which type of breach of warranty of merchantability ... is involved in their particular case."

— David A. Barry, Boston

For example, Barry said, the statute of limitations for contract-based breach of implied warranty is four years from the date of the breach, while it is three years from the date when the damage or injury occurs in tort-based claims.

"The court's opinion is a reminder to Massachusetts practitioners that important consequences follow depending upon which type of breach of warranty of merchantability ... is involved in their particular case," he said.

### **Alleged defect**

AcBel, a Taiwanese company, is the manufacturer of "Katina," a second-generation power supply unit custom-made for its client EMC to use in its data storage devices.

One of Katina's 400 components is the JA7805 voltage regulator, manufactured by Fairchild subsidiary FSC Korea and designed to emit a constant output of power.

In 2008, Fairchild's agent notified AcBel that the regulator was being redesigned as a "shrunk-die" version with certain components, including a small part called a "zener diode," being moved to accommodate a smaller die.

At the end of the redesign process, FSC Korea performed industry-standard testing and apparently encountered no failures.

Manufacture and shipment were halted in July 2010, several months after entering the market, when FSC Korea reported a quality incident. The defendant recommended that its subsidiary cease production and revert back to the larger die. AcBel and other Fairchild customers apparently were not notified of the switch.

Meanwhile, AcBel had purchased 195,000 shrunk-die units, all of which ended up in the Katina units it made for EMC.

In December 2010, while FSC Korea was investigating the quality issue, EMC informed AcBel that thousands of shrunk-die KA7805s had failed, causing EMC's data storage devices to fail as well. That resulted in 26,000 power supply units having to be replaced for EMC customers.

Ultimately, AcBel sued Fairchild in U.S. District Court alleging breach of the implied warranty of merchantability, fraud and negligent misrepresentation.

Judge Denise J. Casper granted summary judgment on the fraud and misrepresentation claims.

Casper held a bench trial on the implied warranty claim, at which AcBel presented expert testimony that Fairchild's product was defectively redesigned so that AcBel's industry-standard soldering of the microcircuits into the circuit boards of its power supply units caused the malfunction.

At the end of trial, however, the judge dismissed the claim on grounds that AcBel had failed to show that the alleged defect was foreseeable by reasonable testing. AcBel appealed.

### **Key distinction**

The 1st Circuit found that Casper erred in applying the foreseeability-by-reasonable-testing standard to the plaintiff's implied warranty claim.

That is because when economic loss is the only injury alleged, recovery should be construed as contract-based and not tort-based under the law of the commonwealth, Torruella said.

"Because the injury here was to the shrunk-die KA7805s — the product itself — it sounds in contract, not tort. As a result, the reasonableness of the testing of the shrunk-die KA7805 was inconsequential," the judge said. "Instead the district court's analysis should have been circumscribed to the foreseeability of the shrunk-die KA7805's use."

And assuming it was foreseeable that AcBel would use the microcircuit as it did, the lower court still had to make a determination as to causation, something it would now be in position to do at a re-trial with the benefit of the 1st Circuit's guidance on the proper inquiry for a contract-based implied warranty claim, the 1st Circuit found.

Accordingly, Torruella said, the panel vacated the trial judge's dismissal of AcBel's implied warranty of merchantability claim and remanded for trial "where the district court shall determine: whether the shrunk-die KA7805 had a defect or unreasonably dangerous condition that rendered it not suitable for the ordinary use for which it was sold; whether AcBel and EMC were using the shrunk-die KA7805 in a manner that Fairchild intended or could have reasonably foreseen; and whether a defect or unreasonably defective condition of the shrunk-die KA 7805 constituted the legal cause of AcBel's and EMC's injury."

### **AcBel Polytech, Inc. v. Fairchild Semiconductor International, Inc., et al.**

**THE ISSUE:** Was a manufacturer that alleged another company breached the implied warranty of merchantability by selling it defectively designed parts that resulted in economic loss required to prove the defect was foreseeable by reasonable testing in order to sustain its claim?

**DECISION:** No (1st U.S. Circuit Court of Appeals)

**LAWYERS:** Zeb Landsman, Richard Chassin and Jesse Travis Conan, of Becker, Glynn, Muffly, Chassin & Hosinski, New York (plaintiff)

Matthew Iverson, Daniel E. Rosenfeld, Stephen W. Hassink and Yasmin Ghassab, of DLA Piper, Boston; Jeffrey A. Rosenfeld of Alston & Bird, Los Angeles (defense)

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