RENDERED: March 11, 2005; 2:00 p.m.
NOT TO BE PUBLISHED

Commonwealth Of Kentucky

Court Of Appeals

NO. 2002-CA-002174-MR

LEE HARMELING — APPELLANT

v.

APPEAL FROM JEFFERSON CIRCUIT COURT
HONORABLE STEPHEN P. RYAN, JUDGE
ACTION NO. 98-CI-002897

THE NATIONAL MARKETING GROUP, INC. — APPELLEE

OPINION
AFFIRMING IN PART,
VACATING IN PART,
AND REMANDING

** ** ** ** **

BEFORE: COMBS, CHIEF JUDGE; DYCHE AND KNOPF, JUDGES.

KNOPF, JUDGE: Lee Harmeling appeals from a judgment of the Jefferson Circuit Court confirming a jury verdict which awarded damages to the National Marketing Group, Inc. (National Marketing) on its contract and breach-of-loyalty claims. Harmeling argues that the evidence did not support an award of damages on the breach-of-loyalty claim, and that the verdict was obtained through false testimony by National Marketing's president. Because we agree with Harmeling on the former issue,

we affirm in part, vacate in part, and remand for entry of a new judgment.

National Marketing is a Canadian corporation with its principal office in Waterloo, Ontario. In 1995, National Marketing acquired the exclusive rights to distribute a line of Scottish-made vinyl flooring products in the United States under the brand name "Nairn Floors."[1] In August of that year, National Marketing hired Harmeling as a sales agent. Under the terms of their oral agreement, Harmeling would act as an agent for National Marketing to find distributors for Nairn Floors in the eastern United States. Harmeling would pay his own expenses and would receive a 5% commission on net sales within his territory. Harmeling testified that the agreement was for a five-year period, while National Marketing's president, Paul Smith, testified that there was no fixed term for the agreement.

Shortly after entering into the agreement, Harmeling brought Tri-State Flooring (Tri-State), a company located in Evansville, Indiana, to National Marketing as a potential distributor. Harmeling told Smith that he had done business with Tri-State in the past. National Marketing initially rejected Tri-State, concluding that they were a bad credit risk.

[1] Nairn Floors are manufactured by Forbo-Nairn, Ltd., a division of Forbo International, S.A.

In response, Harmeling signed a personal guaranty of payment for shipments to Tri-State. Based on this guaranty, National Marketing began shipping goods to Tri-State. However, Tri-State failed to pay National Marketing for all of the products shipped to it. Sometime in the fall of 1996, Harmeling took direct control of Tri-State and moved its inventory to Louisville. Harmeling made two payments to National Marketing on the amounts that Tri-State owed, reducing the balance of its debt to $30,843.77.

Shortly thereafter, on October 28, 1996, Harmeling signed a note to National Marketing for that amount. Although the exact terms of the note are in some dispute, the parties agree that National Marketing began withholding Harmeling's commissions and applying those amounts to the balance of the note. In November 1997, National Marketing terminated Harmeling's employment. At that point, the balance on the note had been reduced to $17,344.00.

On May 26, 1998, National Marketing filed a complaint against Harmeling seeking to recover the balance due on the note. In response, Harmeling asserted that National Marketing fraudulently induced him to sign the note. He also filed a counterclaim to recover the $13,446.00 in commissions which were applied toward the note, and to recover commissions on sales to his territory for a five-year period.

Subsequently, National Marketing filed an amended complaint against Harmeling to include a breach-of-loyalty claim. In support of this claim, National Marketing alleged that Harmeling had failed to disclose his relationship with the principals of Tri-State and with another distributor, Distinctive Flooring. National Marketing further alleged that Harmeling had improperly disposed of the inventory of Tri-State after he took control of that company. As damages for this breach-of-loyalty claim, National Flooring sought a return of everything received by Harmeling while in breach, including all commissions.

The matter proceeded to a jury trial beginning on February 8, 2002. The jury rejected Harmeling's claims and awarded damages to National Marketing totaling $38,979.29. Of this amount, $17,344.00 was for the contract claim and $21,635.00 was for the breach-of-loyalty claim. On February 25, 2002, the trial court entered a judgment in this amount, including prejudgment interest for the balance due on the note.

On March 7, 2002, Harmeling filed motions for a judgment notwithstanding the verdict, for a new trial,[2] and to alter, amend or vacate the judgment.[3] In support of his motion, Harmeling asserted that the National Marketing's president, Paul

[2] CR 59.01.

[3] CR 59.05.

Smith, had given false testimony at trial. Harmeling further argued that the damages were excessive, that the judgment was based on insufficient evidence, that the contract claim was invalid due to lack of consideration, and that the judgment improperly included prejudgment interest on the note. In an order entered on September 20, 2002, the trial court denied the motions. However, the trial court agreed with Harmeling that prejudgment interest was not appropriate and it modified the judgment accordingly. This appeal followed.

Harmeling does not challenge the jury verdict for National Marketing on the note. Likewise, he does not challenge the adverse verdict on his counterclaims. Rather, Harmeling focuses on the evidence supporting the verdict and damages for National Marketing's breach-of-loyalty claim.

Harmeling first argues that Paul Smith gave false testimony at trial which was material to the breach-of-loyalty claim. National Marketing alleged that Harmeling had failed to disclose his relationship with Tom Otten of Distinctive Flooring. Otten is Harmeling's brother-in-law. At trial, Smith testified that at one point, Distinctive Flooring was $8,652.00 in arrears in payment of its account. He further testified that Distinctive Flooring ultimately defaulted on the account and, after payment of insurance, National Marketing had an unreimbursed loss on that account in the amount of $865.20.

In an affidavit accompanying Harmeling's motion for a new trial, Otten disputed this testimony. Otten stated that, in September 1997, he had paid Distinctive Flooring's entire balance due on its account. As attachments to his affidavit, Otten included National Marketing's September 25, 1997, invoice to Distinctive Flooring, showing a balance due of $5,559.92, and he included a credit card statement showing charges totaling this amount to an Ontario restaurant. Otten stated that he had made these payments to the restaurant at Smith's direction.

In a supplemental memorandum in support of his motion for a new trial, filed on May 30, 2002, Harmeling asserted that Smith misrepresented National Marketing's relationship with Nairn Floors. At trial, Smith testified that National Marketing has an ongoing and successful business relationship with Nairn. He also testified that National Marketing's sales of Nairn Floors improved after Harmeling was terminated. He went on to testify that National Marketing had hired ten or eleven new agents to service Harmeling's former territory, and that some of those agents were still working for him.

Harmeling presented an affidavit from Kieran Fowley, vice-president for North American sales and marketing for Forbo-Nairn. In his affidavit, Fowley states that National Marketing's sales of Nairn floors were "disappointing." Fowley added that Forbo-Nairn's distribution agreement with National Marketing

expired in October 2000 and was not renewed. Fowley further added that while some of National Marketing's sales agents still sell Nairn floors, they all work for Forbo-Nairn and not for National Marketing.

The trial court declined to consider Harmeling's perjury allegations, finding that supporting affidavits were not timely or properly filed. National Marketing asserts that, while Harmeling's CR 59 motions were timely, the supporting affidavits were not filed until more than ten days after the judgment was entered. The trial court also noted that Harmeling's supplemental memorandum, filed on May 30, 2002, was not signed. Based on these deficiencies, National Marketing argues that the trial court was not authorized to consider this evidence.

As an initial matter, we note that the affidavit of Tom Otten was filed along with Harmeling's original CR 59 motion on March 7, 2002. Although this affidavit was timely, the trial court did not address it in the order denying Harmeling's motions. National Marketing concedes this point, but points out that CR 59.01(g) allows a trial court to grant a new trial based on "[n]ewly discovered evidence, material for the party applying, which he could not, with reasonable diligence, have discovered and produced at the trial." A party cannot invoke CR 59 to raise arguments and introduce evidence that could and should have been

presented during the proceedings before entry of the judgment.[4] Since Harmeling had the opportunity to present this evidence at trial, National Marketing argues that the trial court was not required to consider it as a basis for a new trial.

The record is not entirely clear on this point. During his rebuttal testimony at trial, Harmeling stated that Distinctive had paid its account as asserted in Otten's affidavit. However, he admitted that he did not have the credit card receipts. National Marketing's counsel objected, arguing that the testimony was improper unless Harmeling could produce either Otten or the receipts. Harmeling informed the trial court that he could have the receipts in several days, but the trial court wanted the receipts produced that same day. When Harmeling stated he could not provide the receipts so quickly, the trial court instructed him to stop testifying about them.

At the time Harmeling testified about the receipts, it was late on Thursday afternoon. Although Harmeling's offer to produce the receipts by Monday was not particularly timely, we question the trial court's insistence that Harmeling produce the receipts immediately. Nevertheless, Harmeling did not ask the court for a continuance so he might attempt to obtain the receipts earlier. Under the circumstances, Harmeling has failed

[4] Hopkins v. Ratliff, 957 S.W.2d 300, 301 (Ky.App. 1997).

to show that he was unfairly deprived of an opportunity to present this evidence at trial.

The May 30, 2002, supplemental memorandum and Fowley's affidavit present a different issue. As the trial court noted, Harmeling's supplemental memorandum and the certificate of service were unsigned. Consequently, the trial court was not obligated to consider Fowley's affidavit.[5] Therefore, we need not consider National Marketing's argument that that the late filing of Fowley's affidavit is a jurisdictional issue that would absolutely preclude trial court from considering the issue.[6]

Furthermore, we agree with the trial court that Fowley's affidavit would not mandate a new trial in this case. Fowley's affidavit addresses matters which occurred after the relationship between National Marketing and Harmeling ended.

---

[5] CR 11.

[6] *Citing* Ligon Specialized Hauler, Inc. v. Smith, 691 S.W.2d 902 (Ky.App. 1985). We note, however, that the purpose of the particularity requirement in CR 59.03 and 59.05 is to afford notice of the grounds for and relief sought to both the court and the opposing party so the opponent will have an opportunity to respond and the court will have enough information to consider the motion. *See* Registration Control Systems, Inc. v. Compusystems, Inc., 922 F.2d 805, 807 (Fed. Cir., 1990); *See also* Tennessee Products & Chemical Corp. v. Miller, 282 S.W.2d 52, 53 (Ky. 1955): (particularity requirement of CR 7.02 is not a mere technical form requirement but is designed to apprise the trial court of the specific basis upon which the party casts his request for a ruling). Since Harmeling's CR 59 motion was timely filed and stated his grounds with particularity, at least with respect to Otten's affidavit, the trial court retained jurisdiction to modify the judgment.

Although these matters may have affected the jury's view of Smith's credibility, they were not directly relevant to the merits of either of National Marketing's claims.

The central issue in this case concerns the sufficiency of the evidence on National Marketing's breach-of-loyalty claim against Harmeling. When evaluating the sufficiency of evidence on a motion for directed verdict or for a judgment notwithstanding the verdict, the trial court must consider the evidence in its strongest light in favor of the party against whom the motion was made and must give him the advantage of every fair and reasonable intendment that the evidence can justify. On appeal the appellate court considers the evidence in the same light.[7] The evidence presented at trial did not establish that Harmeling's conduct either amounted to a breach of loyalty or caused any damages to National Marketing apart from his contractual obligations.

A breach-of-loyalty claim is based on the existence of a fiduciary duty between a principal and an agent. One who acts as agent for another is not permitted to deal in the subject matter of the agency for his own benefit without the consent of the principal. Profits realized by an agent in the execution of his agency belong to the principal in the absence of an agreement

[7] Lovins v. Napier, 814 S.W.2d 921, 922 (Ky. 1991).

to the contrary. The agent is bound to a high degree of good faith toward his employer, and is not entitled to avail himself of any advantage that his position may give him to profit at the employer's expense beyond the terms of the employment agreement.[8]

Since Harmeling's agreement with National Marketing was oral, it is not clear to what extent he had a duty of loyalty. However, Harmeling did not object to the instructions informing the jury that he owed such a duty. Furthermore, we agree with the trial court that, even if Harmeling was an independent contractor, he had a duty not to use his position against National Marketing's interests.[9]

There was no proof that Harmeling sold competing products while he was working as an agent of National Marketing. Furthermore, the trial court determined that there was no evidence that Harmeling made any outside profits during the period he was employed. And National Marketing does not allege that Harmeling used confidential information to enrich himself. Rather, National Marketing focused on three specific areas: Harmeling's relationship with Tri-State; his conduct liquidating

[8] Stewart v. Kentucky Paving Co., Inc., 557 S.W.2d 435, 437 (Ky. App. 1977). *See also* Hoge v. Kentucky River Coal Corporation, 216 Ky. 51, 287 S.W. 226, 227 (Ky. 1926).

[9] Hoge v. Kentucky River Coal Corporation, *supra* at 227.

the assets of Tri-State; and his relationship and dealings with Distinctive Flooring.

In particular, National Marketing asserts that Harmeling failed to disclose that his wife was a part owner of Tri-State, and that Tom Otten, the owner of Distinctive Flooring, was his brother-in-law. However, National Marketing does not allege that this information would have led it to reject these potential distributors. Indeed, National Marketing admits that it conducted its own evaluation of both of these companies. In short, National Marketing failed to prove that Harmeling's failure to disclose this information materially prejudiced its interests.[10]

Furthermore, when National Marketing initially rejected Tri-State as a distributor, Harmeling signed a personal guaranty for payment of Tri-State's account. Although Harmeling failed to disclose his relationship with one of Tri-State's principals, Harmeling's personal guaranty for Tri-State vitiated any conflict of interest with National Marketing's interests.

[10] National Marketing focuses on evidence that Harmeling was Distinctive Flooring's registered agent for service of process in Ohio. The form naming Harmeling as Distinctive Flooring's agent also lists Harmeling as Distinctive Flooring's president. However, this form was executed and filed in 1999 – well after National Marketing terminated its relationship with Harmeling. Harmeling's subsequent relationship with Distinctive Flooring is not relevant to the claim that Harmeling breached his duty of loyalty while employed by National Marketing.

National Marketing also argues that Harmeling breached his duty of loyalty by taking over the operations of Tri-State and by liquidating its inventory without ensuring that Tri-State's debt to National Marketing was paid. National Marketing also asserts that Harmeling failed to dispose of Tri-State's inventory as it directed him to do. If Harmeling was acting as National Marketing's agent when he took over the operation of Tri-State, then Harmeling would have had a duty to dispose of Tri-State's inventory as directed by National Marketing. However, National Marketing does not allege that Harmeling's operation of Tri-State was within the scope of his agency relationship. Furthermore, National Marketing was aware that Harmeling had taken over the operations of Tri-State. By failing to object to Harmeling's actions, National Marketing waived any conflict of interest.

Moreover, at National Marketing's direction, Harmeling signed the note agreeing to make payments on Tri-State's debt. Since Harmeling remained personally liable to National Marketing by virtue of the note, any damages which might have been caused by Harmeling's conduct related to Tri-State are not separate from the damages flowing from Harmeling's contractual obligations. In the absence of a showing of separate damages flowing from the breach of loyalty, National Marketing was not entitled to recover under both its contract and breach-of-loyalty claims.

Therefore, we conclude that Harmeling was entitled to a directed verdict on the breach of loyalty claim. However, the jury award of damages for this claim further demonstrates the insufficiency of the evidence. At common law, a faithless agent forfeits any right to compensation after the breach occurs. The Restatement (Second) of Agency § 469 (1958) follows this rule, but also calls for apportioning forfeitures when the agent's compensation is allocated to periods of time or to the completion of specified items of work.[11]

Harmeling did not request an apportionment instruction in this case. However, the jury did not order Harmeling to forfeit all compensation which he earned after the breach of loyalty was alleged to have occurred. Instead, it awarded National Marketing $21,635.29 - $10,000.00 less than the $31,635.29 in commissions which it paid to Harmeling. The jury's award bears no relationship to the evidence presented or the extent of Harmeling's alleged breach of loyalty. Consequently, even if the breach-of-loyalty claim had been properly presented

[11] Restatement (Second) of Agency § 456, comment b. *See also* Phansalkar v. Andersen Weinroth & Co., L.P., 344 F.3d 184, 207 (2d Cir., 2003), (applying common law rule to salaried employee, but noting that apportionment of forfeiture is appropriate in cases where the employee is paid on a transaction-by-transaction basis); and Radio TV Reports, Inc. v. Ingersoll, 742 F. Supp. 19, 23 (D.D.C., 1990) (limiting amount of forfeiture to compensation paid to employee during the month when breach of loyalty occurred).

to the jury, we would conclude that its award of damages was not supported by substantial evidence.

Accordingly, the judgment of the Jefferson Circuit Court is affirmed with respect to the award of contract damages, vacated with respect to the award of damages for breach-of-loyalty, and remanded for entry of a new judgment.

ALL CONCUR.

BRIEF FOR APPELLANT:

J. Warren Bruenderman
Louisville, Kentucky

BRIEF FOR APPELLEE:

Rocco J. Celebrezze
David Bryce Barber
Jeffrey L. Parrish
Celebrezze & Keeler
Louisville, Kentucky