IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

DIAMOND J EQUIPMENT INTERNATIONAL, LLC, Plaintiff,	§	
vs.	§	CIVIL ACTION NO. H 06-0577
MICROBIAL ENHANCED OIL RECOVERY, LLC, Defendant.	§	JURY

Microbial Enhanced Oil Recovery, LLC's
Motion for Summary Judgment

Defendant Microbial Enhanced Oil Recovery, LLC ("MEOR") files this Motion for Summary Judgment. MEOR bases this motion on (1) Diamond J's lack of evidence of damages and (2) the limitation of liability cause in the contract at issue. MEOR makes this motion without waiving its contract defenses such as equitable estoppel and fraudulent inducement.

I. Nature and Stage of the Proceeding

This case involves the breach-of-contract claim for over $6 million in future lost profits and other relief of plaintiff Diamond J Equipment International, Inc. ("Diamond J"). Diamond J claims that MEOR breached a distributor agreement under which Diamond J would sell MEOR's oil-recovery product. (Diamond J also seeks damages for expenses incurred in performing the Distributor Agreement, loss of goodwill and business reputation, and lost business opportunities, attorneys' fees and costs. Complaint ¶ 18, at 4, Instr. 1.) A copy of the Distributor Agreement is attached to the Appendix as Exhibit 1. (References to the summary judgment evidence is "Exh. __." The summary judgment evidence is authenticated in the Declaration of Crag Coukoulis, MEOR's President, at Exh. 7.)

Diamond J paid nothing to MEOR to enter into the Distributor Agreement. Coukoulis Aff. ¶ 4 (Exh. 2). The agreement gave Diamond J no right of exclusivity except to the limited extent Diamond J arranged a sale or trial test, in which case Diamond J would have six-month exclusivity rights to the customer that would continue only if Diamond J secured additional purchases from the customer. *See generally* Exh. 1, at 1.

Diamond J admits that its damages are speculative. It characterizes its lost-future-profits claim as "difficult to ascertain, because the losses involve future sales." Aff. of D. Adatia (Exh. 3, at 3). Diamond J further admits that it is "impossible to quantify" Diamond J's claims for loss of reputation and goodwill. *Id.*

Recognizing that it will never prove its damages claim with admissible evidence, Diamond J pulls from the thin air the two central elements of any lost future profits claim: revenue and overhead. First, Diamond J assumes that it would have had precisely $31,928,519 in gross sales, the minimum amount of MEOR product that the parties listed as performance goals. *See* Diamond J's disclosure (Exh. 4, at 4-5); *Cf.* Exh. 1, App. B. Because Diamond J never made a sale, this number defies verification. It is unknowable.

Second, Diamond J assumes its overhead (its "[e]xpenses, discounts, and sales commissions to resellers") would eat up exactly "half" of Diamond J's revenues (which under the Distributor Agreement are 40% of gross sales, MEOR getting the other 60%). *See id.* Diamond J's "half" of 40% of $31,928,519 equals lost future profits of $6,385,702.80. Again, Diamond J's assumption of "half" bears no relationship to reality: Diamond J has no operating history on which to base this unverifiable figure. *Id.*

In summary, Diamond J's claim rests on assumptions more akin to astrology than accounting.

The parties have had enough discovery for the Court to grant this motion. In May 2006, the Court heard Diamond J's motion for temporary injunction in which Diamond J unsuccessfully asked the Court to require MEOR to perform under the Distributor Agreement on the grounds that it had no other adequate remedy at law. (MEOR cites testimony from the hearing in this motion without citation and will supplement with pages of the hearing transcript upon receipt.) Diamond J sought injunctive relief for the same reason MEOR asks this Court for summary judgment: Diamond J has and will never have legally sufficient evidence of "lost profits" or other similar damages. Accordingly, no additional discovery will overcome Diamond J's unverifiable damages model.

II. Undisputed Facts

As a business, Diamond J appears to provide no demonstrable value to anyone. Diamond J's "members" purport to work from a phantom "facility" in Bellaire that is in reality nothing but a mail drop. Hrg., 5/12/06, at __ (transcript pending). Diamond J has no expenses, has no inventory of products, and markets through a website created a computer kept in the bedroom of the founder's daughter. *Id.* (The founder acquired his knowledge about the oil business from managing a hotel in Huntsville. *Id.*)

As of May 2006, Diamond J has never made a single sale of anything to anybody. *Id.* Diamond J's website "celebrates its early successes" and touts its "quality assurance department" and "customer service department," none of which exist. *See* Exh. 5 (website). Diamond J has failed to produce a single order showing a ready, willing, and able purchaser of MEOR's products or anything else.

III. Statement of Issues to Be Ruled on by the Court and Standard of Review

MEOR moves for summary judgment on two grounds: (1) Diamond J has no evidence of direct or consequential damages, and (2) the contract under which Diamond J sues bars its damage claims. Because Diamond J's damage claims fail as a matter of law, MEOR is entitled to summary judgment. Diamond J bears the burden of proof on its damages claims and therefore must come forward with evidence supporting those claims to avoid summary judgment. *Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986).

The appellate courts apply a *de novo* standard of review of district court rulings on motions for summary judgment. *Wyatt v. Hunt Plywood Co.*, 297 F.3d 405, 408 (5th Cir. 2002). The Court may grant summary judgment where there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c).

IV. Argument

A. Diamond J Cannot Show Evidence of Damages

Diamond J seeks the following damages: (1) expenses incurred in performing the Distributor Agreement; (2) lost profits; (3) loss of goodwill and business reputation; (4) lost business opportunities; (5) reasonable attorney's fees; and (6) costs of court and expenses related to the suit. Complaint, Instr. 1, ¶ 18, at 4. This Court should grant summary judgment as to each claim.

Item (1): Expenses incurred in performing the Distributor Agreement

Diamond J provides no explanation of any legal theory that would justify this element of damages. As discussed below, the Distributor Agreement defines MEOR's "maximum liability" to Diamond J to "the amount actually paid by DISTRIBUTOR to MEOR for the Product purchased hereunder." Exh. 1, at 5 (top).

Thus, the only item for which Diamond J could have sought recovery was the $1000 check it sent to MEOR for a supposed demonstration to a potential customer – not even a real sale. *See* Exh. 6. In any event, MEOR returned this check to Diamond J. *See* Exh. 7. Diamond J has incurred no other losses in connection with its performance the Distributor Agreement, which bars recovery of any other losses. Exh. 1, at 4-5 (limiting MEOR's "maximum liability to [Diamond J] . . . under this Agreement" to no more than "the amount actually paid by [Diamond J] to MEOR for the Product purchased hereunder").

Items (2)-(4): Lost profits, loss of goodwill/business reputation, and "lost business opportunities"

As a company with no operating history, no revenue, and no orders for MEOR's products, Arizona law precludes Diamond J's claim for lost profits and other consequential damages. (For purposes of this motion, Arizona law governs Diamond J's claim, as provided in the Distributor Agreement. Exh. 1, at 6.)

a. Lost Profits

Under Arizona law, plaintiffs in every lost profits case (1) must supply some reasonable basis for computing the amount of damage and (2) must do so with such precision as, from the nature of his claim and the available evidence, is possible. *See Gilmore v. Cohen,* 386 P.2d 81, 83 (Ariz. 1963). In *Gilmore*, plaintiffs had an agreement that entitled them to buy various tracts of land from defendants. Defendants sold six tracts to plaintiffs, who then built on them and resold them, apparently turning some profit. At that point, defendants terminated the contract.

The Arizona Supreme Court sustained the trial court's findings that plaintiffs had failed to present evidence of future lost profits. The court observed that "plaintiffs seemed uncertain that they had ever shown a profit from the operation or that future profits were likely to accrue." *Id.* The court emphasized that "[t]he requirement of 'reasonable certainty' in establishing the

amount of damages applies with ***added*** force where a loss of ***future*** profits is alleged." *Id.* at 82 (emphasis added). This reasonable certainty must "approximate[] mathematical precision." *Id.*

The other Arizona cases follow *Gilmore*. *See, e.g., Rancho Pescado v. Northwest. Mut. Life Ins.*, 680 P.2d 1235, 1245-47 (Ariz. App. 1984) (rejecting lost profits claim in "highly risky industry" of catfish farming); *Weiner v. Ash,* 756 P.2d 329, 331-32 (Ariz. App. 1988) (holding that mere success in past does not mean plaintiff would have realized future profits).

Here, Diamond J has an even weaker claim than the losing plaintiffs in these leading Arizona cases, which involved past sales, past revenues, and at times past profits. For example, in *Gilmore*, plaintiffs successfully sold, at some profit, six of the thirteen tracts defendant allegedly promised to supply. *Gilmore*, 386 P.2d at 82. Here, Diamond J never made a single sale of MEOR products or anything else. *Cf. Texas Instruments v. Teletron Eng. Mgt.*, 877 S.W.2d 276, 280 (Tex. 1994) (rejecting lost profits claim where plaintiff's "expectations were at best hopeful; in reality, they were little more than wishful").

Further, Diamond J must quantify its losses with "reasonable certainty" that "approximates mathematical precision." *Gilmore*, 386 P.2d. This standard applies "with added force" when the plaintiff alleges lost future profits. *Id.* Without any money spent or money received, Diamond J cannot begin to establish a claim for lost future profits under this strict standard.

b. Loss of goodwill and business reputation

Diamond J also seeks relief for "loss of goodwill and business reputation." However, Diamond J's president abandoned this claim when he stated under oath: "The economic value of the injury to Diamond J's business reputation and good will is impossible to quantify." Adatia Aff. (Exh. 3, at 3).

Moreover, as a matter of law, this quantum of damages is not recoverable for breach of contract. Although the Arizona courts say little about this element of damages, Texas and other courts have consistently rejected this claim. *See Rubalcaba v. Pac./Atl. Crop. Exch.*, 952 S.W.2d 552, 559 (Tex. App.—El Paso 1997, no writ); *In re Teledyne Def. Contract. Deriv. Lit.*, 849 F. Supp. 1369, 1372 n.1 (C.D. Cal. 1993) (rejecting RICO claim for injuries to "business reputation").

c. Loss of business opportunity

Diamond J also seeks damages for "loss of business opportunity." This measure of damages appears to have no real legal precedent separate from a lost profits claim. In any event, Diamond J has not quantified the claim and it does not appear capable of quantification.

Items (5)-(6): Attorney's fees and costs

Diamond J also asks for its attorney's fees and costs. However, under Arizona law, the Court has discretion to award attorney's fees, and "there is no requirement that the trial court grant attorney's fees to the prevailing party in all contested contract actions." *Associated Indem. Corp. v. Warner,* 694 P.2d 1181, 1184 (1985); Ariz. Rev. Stat. § 12-341.01(A) (empowering court, in its discretion, to award fees to "the successful party"). Moreover, when a plaintiff fails to recover damages on a breach of contract claim, courts routinely reject that plaintiff's claims for attorney's fees. *Associated Indem.*, 694 P.2d at 1184 (listing success on merits as factor); *cf. Green Int'l v. Solis*, 951 S.W.2d 384, 390 (Tex. 1997) (no fees if plaintiff fails to obtain damages award). Indeed, Arizona law gives the Court authority to award MEOR, as the successful party, its attorney's fees upon MEOR's successful defense of this case.

In sum, because Diamond J is not entitled to any damages on the merits of its claim, it is not entitled to attorney's fees or expenses.

B. The Distributor Agreement Caps Diamond J's Damages at Zero.

The Distributor Agreement under which Diamond J seeks relief contains a typical "limitation of liability" provision that, as applied here, caps Diamond J's damages at zero. The agreement provides:

> DISTRIBUTOR will use its best efforts in negotiating contracts, which reduce liability for both DISTRIBUTOR and MEOR. ***In no event shall MEOR be liable for*** (i) any claims or damages arising directly or indirectly from the sale or use of the products hereunder, except as expressly provided for herein, or (ii) ***lost profits, incidental, consequential, special or indirect damages arising in connection with the sale*** or use ***of the Products.*** Not withstanding any contrary provision contained herein, ***MEOR's maximum liability to DISTRIBUTOR under this Agreement*** or in connection with the sale or use of this Product ***shall in no event exceed the amount actually paid by DISTRIBUTOR to MEOR for the Product purchased hereunder***. . . .

Distributor Agreement, at 4-5 (emphasis added) (Exh. 1).

In other words, the Distributor Agreement defines MEOR's "maximum liability" under the Agreement to the amount Diamond J "actually paid" MEOR for the product purchased under the Agreement. When MEOR terminated its relationship with Diamond J, it did just that. MEOR returned the $1000 down payment Diamond J delivered to MEOR on January 18, 2006, just as this dispute arose, for an order for an apparent demonstration that Diamond J appears to have placed itself to portray a semblance of otherwise nonexistent sales activity. *See* Exhs. 6-7 (correspondence and cashier's check).

Arizona courts have consistently upheld limitations of liability. *See, e.g., Roscoe-Gill v. Newman*, 937 P.2d 673 (Ariz. App. 1996) (enforcing earnest money provision over objection that it was too low, absent showing of duress, unconscionability, or fraud); *Miller v. Crouse*, 506 P.2d 659, 664 (Ariz. App. 1973) (upholding limitation of liability provision).[1] These cases

[1] Under Texas law, a contract clause limiting liability to "return of the amounts paid" will be enforced to preclude claims for lost profits. *See Southwest. Bell Tel. Co. v. FDP Corp.,* 811 S.W.2d 572, 577 (Tex. 1991).

follow the basic tenet of contract law that "[w]hen a contract is plain, certain, and unambiguous on its face, its interpretation is a matter of law for the court, and not one of fact for the jury." *See Miller Cattle Co. v. Mattice,* 298 P. 640, 643 (Ariz. 1931). The Arizona courts place particular confidence in provisions that provide some flexibility depending on the nature and extent of the alleged breach as opposed to fixed-sum liquidated damages provisions. *Id.* at 642.

Here, the limitation of liability provision in the Distributor Agreement provides clarity, certainty, and flexibility. First, it makes clear that "MEOR's maximum liability to the DISTRIBUTOR under this Agreement . . . shall in no event exceed the amount actually paid by DISTRIBUTOR to MEOR for the Product purchased hereunder." Exh. 1, at 4-5. The contract specifically excludes lost profits and other consequential damages. *Id.* The terms "maximum liability" and "shall in no event exceed the amount actually paid" make the limitation clear and certain. Plus, no question exists as to Diamond J's ability to understand the limitation of liability. Diamond J had its own in-counsel and others savvy in the world of contracts. *See* Diamond J webpage (Exh. 5) (describing expertise of in-house lawyer John Sanders and others on Diamond J's "Management Team").

Second, this language gives Diamond J a fair and flexible measure of damages: out-of-pocket payments Diamond J makes to MEOR. This easy-to-apply provision gives Diamond J more protection than ordinary liquidated-damages terms that the Arizona courts have upheld, like the earnest-money provision in *Roscoe-Gill*.

In fact, given Diamond J's role as a penniless startup e-commerce company purporting to sell a hodgepodge of products in the oil patch, the provision here gives Diamond J ample protection. The Court should enforce the contract, not rewrite it to accommodate Diamond J's unverifiable lost future profits model.

V. Conclusion and Prayer

Diamond J, as a matter of law, has no damages. Even if it did, the contract sets Diamond J's damages at zero. Accordingly, this Court should grant MEOR's motion for summary judgment and dismiss Diamond J's claims.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this the 19th day of October, 2006, a true and correct copy of the above and foregoing instrument was sent via electronic mail in accordance with the Electronic Court Filing System guidelines to the following counsel of record:

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