

CLIENT ALERTS

Buyer Must Prove That a Part Was Defective to Obtain Indemnity from Its Supplier

Client Alert

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In *Nissan North America, Inc., v. Continental Automotive Systems, Inc.*, the federal Court of Appeals for the Sixth Circuit (which includes Michigan) determined that Nissan was not entitled to indemnification from Continental for damages recovered from Nissan by an injured driver in an earlier lawsuit, because Nissan was not able to establish that the Continental part was defective and caused the driver's injury.

Before explaining further, a few preliminary points. First, the case was about the interpretation of particular (although common) contract language. The case does not hold that an OEM or other buyer can never obtain indemnity from a seller absent supplier fault, but only that the Nissan contract language at issue did not allow it to do so. Second, the case was decided under Tennessee contract law, so it would not be binding under Michigan law. Finally, the factual background is somewhat complicated and will not be fully summarized in this short Alert, although certainly the full facts should be understood before relying on the case in an actual dispute.

The indemnity claim arose out of a California lawsuit filed against Nissan and Continental following a fatal accident allegedly caused by a defective braking system. Portions of the braking system were supplied by Continental. Continental chose to settle before trial. Nissan was then found liable at trial for substantial damages to plaintiffs. The jury found that the braking system was defective, but the jury was not asked to determine whether Continental's portion of the system was defective.

Nissan then sought indemnification from Continental for losses totaling almost \$25,000,000 based on a contract provision in Nissan's standard PO terms requiring indemnity for:

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- “All cost incurred [by Nissan] as a result of . . . damages or cost arising **from claims** of personal injury or property damages caused directly or indirectly by defective parts supplied by Seller.”

Nissan first argued that Nissan’s damages arose from a “claim” in which Continental’s parts were alleged to be defective, so Nissan was entitled to indemnity without having to prove that Continental’s parts in fact were defective. The Court of Appeals rejected Nissan’s arguments, finding that this is not what the indemnity provision meant under Tennessee contract interpretation rules. The court then found that the California verdict did not establish that the Continental part was defective, because the jury was not asked that question. Finally, the court held that Nissan could not prove that the part was defective in the indemnification lawsuit as a result of strategic litigation decisions it had made. Thus, Nissan was not entitled to indemnity. As a corollary, Continental escaped liability without having to prove that its part was not defective.

There are several significant takeaways from this decision. First, the decision was based on contract language, and contract language can be changed. It is possible that OEMs (and other buyers) may attempt to adjust the language of their terms to expand their indemnity rights in response to this decision. It always is prudent to monitor for changed terms, whether in new contracts or in modifications to old ones. Second, for the seller, once the contract terms are agreed to (including potentially acceptance by performance), the ship probably has sailed. Stated differently, the time to deal with risks is at the front end, not when a problem or dispute arises down the road. Butzel’s Automotive Team has decades of experience in supply chain contracting and stands ready to assist you in protecting your interests.

Please feel free to contact the authors of this Client Alert or your Butzel attorney for more information.

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