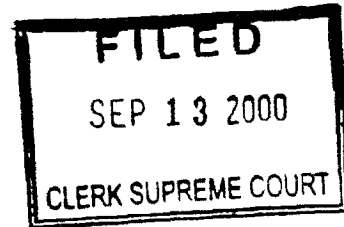


IN THE COURT OF APPEALS OF IOWA

No. 0-389 / 99-0864
Filed September 13, 2000

**LEE COUNTY MENTAL HEALTH
CENTER INC., d/b/a RIVER CENTER
FOR COMMUNITY MENTAL HEALTH,**
Plaintiff-Appellant,



vs.

**LEE COUNTY BOARD OF SUPERVISORS,
A Body Politic Incorporate,**
Defendant-Appellee.

Appeal from the Iowa District Court for Des Moines County, John G. Linn,
Judge.

The plaintiff appeals from adverse rulings in its action for breach of
contract and fraudulent nondisclosure. **AFFIRMED.**

John M. Loeschen of Loeschen & Loeschen, Burlington, for appellant.

Douglas H. Napier of Napier, Wolf & Napier, Fort Madison, for appellee.

Considered by Huitink, P.J., and Mahan and Zimmer, JJ.

MAHAN, J.

The plaintiff, Lee County Mental Health Center, Inc. d/b/a River Center For Community Mental Health, appeals from adverse rulings in its action for breach of contract and fraudulent nondisclosure. The plaintiff claims the trial court erred in prohibiting it from presenting evidence of the defendant's, Lee County Board of Supervisors, understanding of the terms of the contract at the time it was breached. The plaintiff also contends the court erred in granting defendant's motion for directed verdict on plaintiff's fraudulent nondisclosure claim. The plaintiff claims there was sufficient evidence to prove it relied upon the county attorney's representations, and the defendant had a duty to disclose its alleged modification of the operating agreement. We affirm.

In 1988, River Center For Community Health (River Center) and the Lee County Board of Supervisors (Lee County) entered into an operating agreement (hereinafter contract) whereby River Center would operate the Lee County Mental Health Center (later renamed Eagle Summit) for an annual fee in excess of \$1,000,000 per year. Indigent physically and mentally disabled persons were cared for at Eagle Summit with county funds. The contract allowed Lee County to contract out or "privatize" the operation of Eagle Summit.

A consultant hired by both parties drafted the contract. The contract provided either party with the right to terminate the contract for cause at any time with a provision that allowed the party subject to termination ninety days to cure any deficiencies claimed as a basis for the termination. If after such time, the

deficiency was not corrected to the satisfaction of the party seeking to terminate the contract, the contract could be terminated.

The contract, dated August 18, 1988, provided the following "Option to Renew Agreement":

Operator shall have the option to renew this Agreement for four (4) three (3) year periods commencing July 1, 1991 subject only to County's right to review the performance of Operator prior to the first renewal of this agreement. County shall during the 1990 calender [sic] year hold a public hearing. At that hearing the Board of Supervisors shall review all annual accreditation reports for the Operator as issued by the Iowa Department of Human Services and Iowa Department of Health; it shall solicit and review comments from residents, families of residents, staff and members of the general public concerning the operation of Facility by Operator. County may thereafter permit Operator to exercise its option to renew this contract, or County may, for any reason, vote to terminate this contract without permitting renewal. No cause of action shall accrue to Operator as a result of any action taken by the Board of Supervisors in considering, approving or rejecting the renewal of the contract at this time.

In the event Operator thereafter desires to exercise its option to renew this Agreement for the July 1, 1991 to June 30, 1994 period, notice of the exercise of such option must be served upon the Auditor of Lee County, Iowa, no later than December 15, 1990. The exercise of any additional option shall require a notice to be served in the same manner and within similar time constraints, relative to the commencement of each of the four (4) three (3) year renewal periods.

River Center maintains if Lee County renewed the contract after the first three-year option period, River Center held the exclusive right to terminate the contract after each of the remaining three-year periods. According to River Center, Lee County did not have any right to revoke or terminate River Center's option in the event it chose to continue with the contract. In contrast, Lee County argues after the first three-year period it had the right to terminate the contract, renew it unchanged, or enter into a new contract. Lee County contends it chose to

renegotiate the contract with River Center after the first three-year period. Members of the Board of Supervisors testified at trial that by renegotiating the contract, Lee County intended to reserve the right to terminate it every three years.

In 1991, the parties signed a document that provided the following "Option to Renew Agreement":

Operator shall have the option to renew this Agreement for three (3) three (3) year periods commencing July 1, 1994. County may thereafter permit Operator to exercise its option to renew this contract, or County may, for any reason, vote to terminate this contract without permitting renewal. No cause of action shall accrue to Operator as a result of any action taken by the Board of Supervisors in considering, approving or rejecting the renewal of the contract at this time.

In the event Operator thereafter desires to exercise its option to renew this Agreement for the July 1, 1994 to June 30, 1997 period, notice of the exercise of such option must be served upon the Auditor of Lee County, Iowa, no later than December 15, 1993. The exercise of any additional option shall require a notice to be served in the same manner and within similar time constraints, relative to the commencement of each of the three (3) three (3) year renewal periods.

In 1994, the parties signed a document containing essentially the same "Option to Renew Agreement." Lee County claims the 1991 and 1994 documents represented new contracts (a separate contract or a modification and substitution of the old one) that gave either party the right to terminate the contract once every three years. River Center claims the 1991 and 1994 documents were simply extensions of the 1988 contract, intended to reflect the remaining option periods available to the parties. According to River Center, the 1988 contract was still in effect in 1997, when Lee County gave notice to River Center of its

intention not to renew the contract for the period from July 1997 through June 30, 2000.

River Center filed suit against Lee County, alleging: (1) breach of contract based on Lee County's termination of the 1988 contract; and, in the alternative, (2) fraudulent nondisclosure, based on Lee County's failure to inform River Center of the alleged modification or substitution of the contract in 1991. Specifically, River Center claimed Lee County made no public disclosure of its intent to negotiate and obtain a contract that would allow it to terminate the contract once every three years. Lee County Attorney Mike Short accomplished Lee County's objective on its behalf. However, River Center maintains, Mr. Short never told Mr. Steve Miller, River Center's Executive Director, about the County's objective, and no public meeting took place to provide River Center with notice. Moreover, County Attorney Short was serving as an active board member for River Center during the time period in question. Lee County pled a counterclaim against River Center for breach of contract.

At trial, the court excluded evidence obtained by River Center from Lee County and granted Lee County's motion for directed verdict on River Center's claim of fraudulent nondisclosure. A jury returned verdicts in favor of Lee County, awarding River Center nothing on its breach of contract claim and awarding Lee County \$505,728 on its counterclaim. River Center appeals.

I. Exclusion of Evidence. We review the exclusion of evidence for correction of errors of law. Iowa R. App. P. 4. The decision whether to admit evidence is within the sound discretion of the trial court, and such decisions will

not be disturbed on appeal unless the discretion has been abused and a substantial right of a party has been affected. *Vaughan v. Must, Inc.*, 542 N.W.2d 533, 542 (Iowa 1996).

As a preliminary matter, we address Lee County's assertion River Center failed to preserve error by making an insufficient offer of proof at trial. An offer of proof serves both to give the trial court a more adequate basis for its evidentiary ruling and to make a record for appellate review. *Strong v. Rothamel*, 523 N.W.2d 597, 599 (Iowa App. 1994). The burden of making an offer of proof to preserve error is on the party that urges the evidence should have been admitted. *Id.* Immediately after the trial court sustained Lee County's objection to River Center's proposed line of questioning, the following exchange took place:

MR. LOESCHEN: Your Honor, we've made a record on it. Would it – do you think, will that be sufficient, do I need to make an offer of proof?

THE COURT: I would consider this record to be in the form of an offer of proof, so I've got your record.

The trial court accepted River Center's explanation of the proposed testimony as a formal offer of proof. The trial court and the parties understood the basis for River Center's inquiry and the line of questioning it wished to pursue. Lee County's argument is without merit.

At trial, River Center sought to ask supervisors Matthew Mohrfeld and Tracy Vance about statements made during a "closed session meeting" held by the Lee County Board of Supervisors on April 1, 1997. River Center asserted the line of questioning was necessary to determine the supervisors' intentions in

terminating the contract in 1997, whether the supervisors believed they could terminate the contract, and/or whether they were trying to get out of the contract. Lee County objected to River Center's proposed line of questioning, arguing in part that the supervisors' motives, intentions, or understanding of the contract in 1997 were not probative or relevant to what the parties' intended when the documents were drafted and executed in 1988 and 1991. The trial court sustained Lee County's objection, refusing to allow River Center to ask questions regarding statements made during the closed session meeting.

We agree the testimony proposed by River Center expresses the supervisors' concerns with renewing Lee County's contract with River Center for another three years. The requested testimony at most describes Lee County's motivation for not wanting to renew the agreement. It does not explain the parties' intentions when the contract was executed in 1988 and renewed or modified in 1991. Supervisors Mohrfeld and Vance were not on the board in either 1988 or 1991, and were not privy to Lee County's intentions at the time the original agreement was executed or three years later when it was modified and renewed. The supervisors' intent at the time of the alleged breach of contract and their motivation for not renewing the contract were not relevant to River Center's breach of contract claim. The trial court did not abuse its discretion by refusing to allow the proposed testimony.

Even assuming the district court ruling was in error, we find no prejudice. The district court's evidentiary ruling precluded River Center from presenting testimony of the supervisors on the proposed issue. It did not apply to testimony

presented for impeachment purposes. River Center had the opportunity to cross-examine supervisor Tracy Vance. The direct examination of Vance by Lee County certainly opened the door for River Center's use of the proposed testimony for impeachment purposes. We have carefully reviewed the direct and cross-examination of Vance. The district court allowed River Center to explore this disputed area and sustained only one objection on the ground the question had been asked and answered. We affirm the district court on this issue.

II. Directed Verdict. We review the trial court's decision to direct a verdict for the correction of errors of law. Iowa R. App. P. 4; *Hasselman v. Hasselman*, 596 N.W.2d 541, 545 (Iowa 1999). A defendant's motion for directed verdict should be denied if there is substantial evidence to support the plaintiff's claim. *Id.* Evidence is substantial when a reasonable mind would accept it as adequate to reach a conclusion. *Id.*

As an alternate theory of liability, River Center pled that if the jury determined River Center and Lee County had formed a new contract of three-year duration (or modified the 1988 contract), Lee County was liable to River Center for the tort of fraudulent nondisclosure. River Center asserted if the contract was modified in 1991, the modification was done surreptitiously and with the specific intent to mislead River Center into believing the contract had not been changed. Specifically, River Center claimed Mike Short, Lee County Attorney, intentionally concealed information from River Center in 1991, failed to advise River Center of the meaning of the terms of the 1991 document, and failed to disclose the meaning of Lee County's interpretation of the document to

River Center. River Center alleged a "special situation" existed between Mike Short and River Center because Mr. Short was serving as a member of the River Center's Board of Directors at the time, thereby entitling River Center to rely on his nondisclosure. Due to the "special situation" and a relationship of trust and confidence between Mr. Short and River Center, it alleged the tort of fraudulent nondisclosure.

At the close of River Center's case, the trial court granted Lee County's motion for directed verdict on the fraudulent nondisclosure claim. The court later denied a motion by River Center to reconsider its ruling on the motion for directed verdict. The trial court concluded: (1) River Center presented no substantial evidence it relied on Mr. Short's nondisclosure; and (2) even if Mr. Short, as a member of River Center's Board of Directors, did have a duty to act in the best interest of River Center either (a) to the extent Mr. Short was acting within the scope of his employment as county attorney when he sat on the River Center Board of Directors, prosecutorial immunity applied to Mr. Short, and therefore the county; or (b) any duty of disclosure Mr. Short had as a board member did not flow to Lee County.

Claims for nondisclosure, misrepresentation (negligent or fraudulent) and fraudulent concealment, are all actions founded in tort. *Bob McKiness Excavating & Grading, Inc. v. Morton Bldgs., Inc.*, 507 N.W.2d 405, 409 (Iowa 1993). Concealment of or failure to disclose a material fact can constitute fraud in Iowa. *Cornell v. Wunschel*, 408 N.W.2d 369, 374 (Iowa 1987). To be actionable, the concealment must be by a party under a duty to communicate the

concealed fact. *Id.* The threshold question in any tort case is whether the defendant owes the plaintiff a duty of care. *Fry v. Mount*, 554 N.W.2d 263, 265 (Iowa 1996). Whether such a duty exists is always a question of law for the court. *Id.*; Restatement (Second) of Torts § 551 cmt. m, at 126 (1977).

The threshold question we must address is whether the Lee County Board of Supervisors owed any duty to River Center when negotiating the contract at arms length. River Center argues County Attorney Short, acting as an agent for Lee County, and as a member of River Center's Board of Directors, had a duty to disclose Lee County's intent to enter into a three-year contract with an option to terminate without permitting renewal by River Center. We disagree.

In its ruling on Lee County's motion for directed verdict, the trial court stated:

The theory that the plaintiff is proceeding on is that Mike Short had a duty to disclose information to the board because of his position on the Board of Directors of River Center, and that is a legitimate intention because board members do have a duty to act in the best interest of the corporation, whether it's a for profit corporation or nonprofit. . . . But the problem with [the fraudulent nondisclosure count] though is that the plaintiff wants to take that duty and extend it back to the Board of Supervisors. . . . The duty to disclose Mike Short may have had does not extend back to the Board of Supervisors who was the defendant in this case. . . . It's [the court's] conclusion there is no duty that flows back to the Board of Supervisors.

We agree with the trial court. Mike Short was never a party to River Center's lawsuit against Lee County. Mike Short's position on the Board of Directors for River Center was in his individual capacity as a private citizen, neither as the Lee County Attorney nor in anyway as a liaison or agent for Lee County. A duty, if any, owed by Mr. Short to River Center would arise by virtue of his status as a

board member of the non-profit corporation. See, e.g., *Mitchellville Co-op v. Indian Creek Corp.*, 469 N.W.2d 258, 263 (Iowa App. 1991) (directors of a corporation owe the corporation complete loyalty, honesty, and good faith). A breach of his duty as a board member might subject him to personal liability, but does not extend to his employer, Lee County.

Recovery in a fraud action is premised on plaintiff's ability to show by a preponderance of clear, satisfactory and convincing evidence each of the following elements: (1) representation; (2) falsity; (3) materiality; (4) scienter; (5) intent to deceive; (6) reliance; and (7) resulting injury and damage. *Cornell*, 408 N.W.2d at 374. River Center failed to meet its burden of proving fraudulent nondisclosure.

Specifically, River Center failed to present substantial evidence to support its assertion the board relied on Mike Short's nondisclosure when it signed the 1991 document. Mike Short never acted or purported to act as the attorney for River Center in its negotiations and dealings with Lee County. Rather, Mr. Short abstained from any discussion of or voting on the contract between Lee County and River Center, in an effort to avoid any potential conflict of interest. River Center board members testified they relied on Steve Miller, who represented to the board the 1991 document was "routine." At least one board member was not even aware Mr. Short was an attorney. Further, the testifying River Center board members admitted they did not read the contract before signing it. If Mr. Miller had questions or concerns about the 1991 document, he could have consulted with River Center's counsel before presenting the document to the board for its

approval. The trial court correctly granted Lee County's motion for directed verdict.

AFFIRMED.