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WLF URGES CALIFORNIA SUPREME COURT TO REVERSE $500 MILLION DAMAGES AWARD

(*City of Hope Nat'l Medical Center v. Genentech, Inc.*)

The Washington Legal Foundation (WLF) filed a brief last week with the California Supreme Court urging it to reverse a court of appeal ruling that upheld a compensatory damages award of $300 million along with an unprecedented $200 million punitive damages award against Genentech, a biotech company. The company was involved in a contract dispute over royalties with City of Hope Medical Center which developed synthesized DNA material. If not overturned on appeal, businesses involved in typical contract disputes risk debilitating lawsuits by plaintiffs' attorneys not only for normal contract damages, but also for multimillion dollar punitive damages awards.

In this case, the City of Hope Medical Center sued Genentech, Inc., over a dispute about the meaning of a 1976 contract provision as to what royalties should be paid to City of Hope over certain DNA products developed by Genentech and licensed to third-parties for sale. After a second lengthy trial (the first trial ending with a hung jury), the jury ruled against Genentech for breach of contract and awarded City of Hope $300 million in compensatory damages and $200 million in punitive damages. Genentech is appealing both awards.

Under California law and other jurisdictions, punitive damages are not allowed to be assessed in breach of contract cases; rather, they are reserved for certain intentional torts committed with malice or fraud. Accordingly, the plaintiffs' attorneys made a novel argument that a fiduciary duty arose out of the contract relationship between the parties, and that Genentech breached those duties. Because the breach of a fiduciary duty is a tort, the jury imposed an unprecedented $200 million punitive damages award after being told by the plaintiffs' attorneys that this would be only a small percentage of the company's net worth.

The court of appeal devoted only five pages of its 59-page opinion to the issue of punitive damages. Although punitive damages are rarely awarded in contract disputes, the court of appeal ruled that punitive damages can be awarded in this case because the underlying contract dispute involved the breach of fiduciary duties. Accordingly, the award of punitive damages was permissible. As to the amount of the award, the court upheld the unprecedented award of $200 million as not being disproportionately high because it amounted to only two-thirds of the compensatory damages award, and therefore, allegedly fell within the ratio guidelines set by the U.S. Supreme Court in *State Farm v. Campbell*.

In its brief, WLF decried the pernicious practice of "tortification" of contract law, which would adversely affect typical business and contract relations, leaving companies subject to astronomical punitive damages in contract cases. WLF devoted most of its brief arguing that excessive punitive damages inflict public harms such as higher costs and prices of goods and services, reduced professional services, disincentives to enter into intellectual property agreements, decreased product development, loss of jobs, gratuitous wealth transfers through windfall awards, and public disrespect for the lottery-like civil justice system.

WLF argued that no punitive damages should be assessed at all because California law prohibits the award of punitive damages in actions that "arise out of" a contract obligation. Accordingly, even if there were a fiduciary obligation, that obligation arose out of the contractual relationship between the parties, and hence, is not subject to punitive damages. Alternatively, WLF argued that the conduct of Genentech was not so reprehensible; rather, its interpretation of the contract was objectively reasonable between two sophisticated business entities, and thus, under *State Farm v. Campbell*, punitive damages awards should not be imposed. Finally, WLF argued that if punitive damages could be imposed, the amount awarded here was grossly excessive. WLF argued that the amount not be based on the wealth of a publicly-held corporation, that it would unfairly punish innocent shareholders and workers, and that a much smaller award would still serve the purposes of punishment and deterrence.

The California Supreme Court will hear this case later this spring and may decide the case by the end of this year.

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For further information, contact WLF Senior Executive Counsel Paul Kamenar at 202-588-0302. WLF's brief filed in the case is posted on its website at *www.wlf.org.*