WLF Washington Legal Foundation
Advocate for freedom and justice®
2009 Massachusetts Avenue, NW
Washington, DC 20036
202.588.0302

February 4, 2005

CALIFORNIA SUPREME COURT AGREES TO REVIEW $500 MILLION DAMAGES AWARD

(City of Hope Medical Center v. Genentech, Inc.)

The Washington Legal Foundation (WLF) scored a major victory when the California Supreme Court agreed yesterday to review 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 owed to City of Hope Medical Center for developing synthesized DNA material. WLF had argued that if the lower court decision were left intact, businesses involved in contract disputes, particularly those in the high-tech field, would be exposed to 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 disputed contract provision regarding the amount of royalties owed to City of Hope for certain DNA products developed by Genentech and licensed to third-parties for sale. After a second lengthy trial, the jury ruled 9-3 against Genentech for breach of contract and awarded City of Hope $300 million in contract damages which Genentech appealed.

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 the contract imposed a fiduciary duty on Genentech. Because the breach of a fiduciary duty is a tort, the jury imposed an unprecedented $200 million punitive damages award after being told that this would be only a small percentage of the company's net worth.

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 also argued that excessive punitive damages inflict public harms such as higher costs 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 also argued that punitive damages should not be based on the wealth of a publicly-held corporation because it would unfairly punish innocent shareholders.

The court of appeal had 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 disproportionally high because it only amounted to two-thirds of the compensatory damages award, and therefore, allegedly within the guidelines set by the U.S. Supreme Court.

"Businesses in California and the rest of the country will be following this landmark case very carefully," said Paul Kamenar, WLF's Senior Executive Counsel. "Hopefully, the California Supreme Court will see it our way and rule that simple contract disputes should not be governed by tort law nor be subject to punitive damages," Kamenar said.

The Court has not yet set a briefing schedule in the case, but it is expected that the case will be briefed this spring and argued later this year.

* * *

For further information, contact WLF Senior Executive Counsel Paul Kamenar at 202-588-0302. WLF's brief is available on its website at www.wlf.org.