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August 15, 2007

**BY OVERNIGHT COURIER**

The Honorable Ronald M. George, Chief Justice  
Honorable Associate Justices  
Supreme Court of the State of California  
350 McAllister Street  
San Francisco, California 94102-3600

**Re: *Omari et al. v. Kindred Healthcare Operating, Inc. et al.*, Docket No. S154525  
Letter in Support of Petition for Review**

Dear Chief Justice George and Honorable Associate Justices of the California Supreme Court:

Pursuant to Rule 8.500(g) of the California Rules of Court, the Washington Legal Foundation (“WLF”) respectfully requests leave to file this letter in support of the Petition for Review in *Omari et al. v. Kindred Healthcare Operating, Inc. et al.*, No. B185113 (2d Dist. 2007).

WLF is a national non-profit public interest law and policy center. WLF is based in Washington, D.C., and has supporters nationwide, including many individuals and businesses in California. WLF devotes substantial resources to efforts to strengthen free enterprise and to promote reform of the civil justice system. WLF participates as *amicus curiae* in precedent-setting cases, and its Legal Studies Division publishes educational materials on the subject of legal reforms. Additional information about WLF and its work can be found on its website, at [www.wlf.org](http://www.wlf.org).

In particular, WLF has focused efforts on restraining the ability of juries and courts to impose excessive punitive damages awards. WLF has appeared as *amicus curiae* in matters before this Court, the United States Supreme Court, and courts of other jurisdictions where issues of runaway punitive damages awards are presented. *See, e.g., City of Hope National Medical Center v. Genentech, Inc.*, No. S129463; *Johnson v. Ford Motor Co.*, 35 Cal.4th 1191 (2005); *Simon v. San Paolo U.S. Holding Company*, 35 Cal.4th 1159 (2005); *Lane v. Hughes Aircraft Co.*, 22 Cal.4th 405 (2000); *State Farm Mutual Automobile Insurance Co. v. Campbell*, 538 U.S. 408 (2003).

While reasonable punitive damages in appropriate cases serve a public purpose, unbounded awards inflict public *harm*, in the form of increased costs and prices, reduced business services, decreased product development, loss of employment, gratuitous wealth transfers through windfall awards, and public disrespect for the civil justice system.

This case, in addition to condoning a large punitive award in the absence of the proof that is *required* by this Court, effectively allowed an award of punitive damages in a case that was inextricably tethered to a breach of a vendor contract. Both aspects of this runaway award merit this Court's review.

*First*, review is warranted in this case because the Court of Appeal's decision bucks the trend firmly away from the pernicious "tortification" of contract law. The decision here affirmed an award exceeding one million dollars in compensatory damages for "fraud," the gist of which was contractual in nature, namely, the defendant's failure to inform the plaintiff – the other party to arm's-length vendor contracts – of its intention to terminate those contracts (its unilateral right under the contracts' express terms) and the conversion of property that occurred when the defendant returned the medical equipment to the person who delivered it. But awarding damages, including punitive damages, for contracting parties' conduct toward each other regarding the performance of the contract is equivalent to the discredited "tort" of breach of the covenant of good faith and fair dealing. Absent some special circumstances imposing some higher duty of care toward one's contracting partner, such as in *Robinson Helicopter Co. v. Dana Corp.*, 34 Cal.4th 979 (2004) involving overt fraudulent misrepresentations, such conduct cannot meet the critical factor of reprehensibility contemplated in *State Farm Mutual Automobile Insurance Co. v. Campbell*, 538 U.S. 408 (2003).

In the instant case, the parties had no relationship at all other than the typical contractual one where any and all duties running from the defendant to the plaintiff arose from contract. The Civil Code should preclude any extension of punitive damages to this situation. *See* Civ. Code § 3294 (authorizing punitive damages in actions "not arising from contract"). If trial and appellate courts may sanction punitive awards against a contracting party for the conduct that occurred here, there is no limit to the availability of such awards. Virtually any unpleasant contract dispute will provide a platform to avoid the bargained-for monetary consequences of a breach and open the door to arbitrary and thoroughly unpredictable compensatory and punitive awards for a tort in an otherwise ordinary commercial context.

*Second*, review is needed to resolve confusion about the propriety of net worth evidence, if any, to determine punitive damages. *See Zaxis Wireless Communications, Inc. v. Motor Sound Corp.*, 89 Cal.App.4th 577, 582-83 (2001) ("Net worth is too easily subject to manipulation to be the sole standard for measuring a defendant's ability to pay."). *If* net worth is a relevant

indicator, then certainly a company's stock price is not.<sup>1</sup> See *Ramco Oil & Gas, Ltd. v. Anglo Dutch (Tenge) LLC*, 171 S.W. 3d 905, 914 (Ct. App. Tx. 2005) (company's market capitalization does not represent its net worth).

In *Adams v. Murakami*, 54 Cal.3d 105 (1991), this Court set forth the absolute rule that the plaintiff has the burden of proving that the defendant's financial condition is adequate to support a punitive damage award and to outline the size of such an award that the defendant could pay. That is a necessary element of the defendant's due process protection. Cases since *Adams*, including this one, have allowed plaintiffs to avoid their mandatory burden entirely. These cases work an unprincipled and open-ended exception to what this Court held was a firm, policy-grounded *rule*.

As this case shows, the failure to hold a plaintiff to its *Adams* burden of proof can result in dangerous and arbitrary consequences, which certainly threaten to run afoul of *State Farm's* due process concerns. Here, for instance, the "net worth" – actually, the stock market trading value on the day of the punitive phase of the testimony – of a *non-defendant* parent company was proffered as the basis for the jury's determination of punitive damages against two local hospitals, with no showing, or even suggestion, of alter ego. See *Tomaselli v. Transamerica Ins. Co.*, 25 Cal.App.4th 1269, 1282 (1994). Thus, shareholders, investors, customers and employees of the parent corporation, as well as its affiliates with no direct relationship to these named defendants and no relationship whatsoever to the circumstances of this case, are burdened with the cost of the punitive award.

Using the purported wealth of a non-defendant parent and measuring it in a way that bears no relationship to anyone's ability to pay the punitive award, similarly inflicts punishment in an arbitrary fashion "only [on] the [shareholders], who took no part in the commission of the tort." See *City of Newport v. Fact Concerts, Inc.*, 453 U.S. 247, 267 (1981). Furthermore, "[n]either reason nor justice suggests that such retribution should be visited upon the shoulders of blameless or unknowing [shareholders]." *Id.* And, because a corporation is a fictional entity, it likewise "can have no malice independent of the malice of its [officers, directors, managing agents, and employees] . . . . Damages awarded for *punitive* purposes, therefore, are not sensibly assessed against the [corporate] entity itself." *Id.* (emphasis in original). In particular, "[c]orporations are abstractions," and investors – in this case, investors in an entity not even named in the lawsuit – are those that must bear the financial burden of the award. *Zazu Designs v. L'Oreal, S.A.*, 979 F.2d 499, 508 (7th Cir. 1992). The result in this case discourages investment and damages businesses' ability to operate and to design their corporate structure for maximum efficiency.

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<sup>1</sup> WLF generally advocates for a legal standard by which the wealth of the defendant should not be a relevant consideration at all for the size of a punitive damages award, as it has argued to this Court in its *amicus* briefing in the pending *City of Hope* case and elsewhere.

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Thus, if the defendant's wealth is a factor to be considered, strict adherence to the dictates of *Adams* is necessary to ensure that factor's proper limited and proportionate role in the overall constitutionality calculus.

WLF respectfully requests that this Court grant review of the *Omari* decision.

Respectfully submitted,

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cc: See attached service list