S282968

IN THE

SUPRREME COURT OF CALIFORNIA

NEW ENGLAND COUNTRY FOODS, LLC,

Plaintiff-Appellant,

VANLAW FOOD PRODUCTS, INC.,

Respondent.

ON A CERTIFIED QUESTION FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT
CASE NO. 22-55432

RESPONDENT'S ANSWER BRIEF ON THE MERITS

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STATEMENT OF THE ISSUE

The certified question from the United States Court of Appeal for the Ninth Circuit is as follows:

> Is a contractual clause that substantially limits damages for an intentional wrong but does not entirely exempt a party from liability for all possible damages valid under California Civil Code § 1668?

INTRODUCTION

The answer to the certified question is: *Yes*. In fact, if the question is not answered in the affirmative, there would be a major chilling effect on businesses who freely and knowingly enter into similar clauses with other businesses on a regular basis in this State, expressing their clear desire to *mutually limit* their liability to one another.

Contrary to what Plaintiff-Appellant NEW ENGLAND COUNTRY FOODS, LLC ("NECF") asserts in its Opening Brief on the Merits ("OBM"), Defendant-Respondent VANLAW FOOD PRODUCTS, INC. ("VanLaw") is not seeking to entirely eliminate its liability to NECF based upon a limitation-of-liability clause contained in the parties' agreement. Rather, VanLaw relied upon bargained-for *fully mutual* limitation-of-liability clauses, the *impact* of which was to bar NECF's claims *because it did not suffer any damages available to it.* NECF is incorrectly interpreting the law to mean that, if the plaintiff did not suffer any available damages,

then the clause must be invalidated Civil Code Section 1668 ("Section 1668").

The District Court correctly found that *Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118 (which involved two parties to a commercial transaction with equal bargaining power, a very similar limitation of liability clause, no public interest, and other important similarities to the present case) is good law and that it completely barred all claims (contract and tort) *because NECF admittedly did not suffer any damages available under the contract and instead only alleged damages that were barred by the parties' agreement.* (1-ER-6–8.)

VanLaw's contention is that the plain meaning of Section 1668 and the cases on the subject (including *Food Safety*) collectively authorize enforcement of the mutual limitation-of-liability clauses to bar all claims NECF filed against VanLaw in the case. They also collectively stand for the proposition that limitation-of-liability clauses and their application to Section 1668 must be decided on a case-by-case basis, and there is no reason for this sound approach to change.

STATEMENT OF THE CASE

As a preliminary matter, much of NECF's Statement of the Case is not relevant to the certified question, nor is it necessary to provide "context" to the certified question, as NECF suggests. It is largely the same

Statement of the Case that NECF provided to the Court of Appeals for the Ninth Circuit in its Opening Brief [see Appellant's Opening Brief – "AOB," pp. 15-27], despite the fact that one of the main issues NECF raised (and focused heavily on in the Statement of the Case) in its Ninth Circuit Opening Brief (issue preclusion[1]) is not relevant to the certified question.

Nonetheless, out of an abundance of caution, VanLaw's Statement of the Case is structured to *mirror NECF's headings* (even if it does not agree with the characterization in those headings) in its Statement of the Case and is intended to avoid duplication or repetition and to instead supplement, clarify, or refute NECF's version of the Statement of the Case.

A. The Core Factual Allegations At Issue

The First Amended Complaint ("FAC") (which is the operative pleading that was dismissed with prejudice as a result of VanLaw's motion to dismiss) arises entirely out of the Operating Agreement (which incorporates and makes part of the Operating Agreement a Mutual Nondisclosure Agreement ("the NDA")). (See 2-ER-132–135, ¶¶7-27 for General Allegations; and 2-ER-135–138, ¶¶28-59 for Claims.)

[1] See, NECF's Ninth Circuit Opening Brief, pp. 14, 30-31.

1. The NDA

Every claim in the FAC describes the unlawful act as an offer/attempt to clone, and the prohibition against cloning arises solely out of the NDA, under the so-called reverse-engineering clause. (2-ER-132–138, ¶¶10, 15-27, 31, 35-38, 43-45, 52, 53, 56, 57, 58.)

The pertinent clause states in its entirety:

> *Neither party (nor any of its agents) shall reverse engineer, disassemble or decompile any prototypes, software or other tangible objects which embody the other party's Confidential Information and which are provided to the party hereunder without the express written consent of the Discloser*. (2-ER-111, ¶3.)

2. The Operating Agreement

The Operating Agreement contains the following pertinent provisions:

- "[VanLaw] will provide manufacturing, shipping, billing and collection services in support of sales of NECF's product, [BBQ Sauce], to Trader Joe's Markets ('TJ's') or any of TJ's designated suppliers. [VanLaw] will pay a royalty fee to NECF as detailed below….

- The [NDA] into which the parties entered on 12/2/13 is incorporated into this Agreement as Exhibit A…

- *To the extent allowed by applicable law: (a) in no event will either party be liable for any loss of profits, loss of business, interruption of business, or for an indirect, special, incidental or consequential damages of any kind, even if such party has been advised of the possibility of such damages; and (b) each party's entire liability to the other party for damages concerning performance or nonperformance by such party in any way related to the subject matter of this Agreement, and regardless of the form of any claim or action, will not exceed the amount of gross revenues earned by [VanLaw] or NECF from the Products,*

whichever is greater, for the twenty-four (24) months prior to the events giving rise to the alleged liability….

- *[I]n no event shall either party be liable for any punitive, special, incidental or consequential damages of any kind (including but not limited to loss of profits, business revenues, business interruption and the like), arising from or relating to the relationship between [VanLaw] and NECF, regardless of whether the claim under which such damages are sought is based upon breach of warranty, breach of contract, negligence, tort, strict liability, statute, regulation or any other legal theory or law, even if either party has been advised by the other of the possibility of such damages…*"[2] (2-ER-114, 117, 118, 120, ¶¶1, 12, 13, 20.)

The FAC alleges that when the Operating Agreement was about to expire and VanLaw determined the parties could not agree upon renewal terms, it decided to work with Trader Joe's to attempt to clone NECF's barbeque sauce recipe. Ultimately, it alleges that VanLaw and Trader Joe's were *unsuccessful* in the effort to clone, but it nonetheless seeks in excess of $6,000,000.00 in past and future lost profits from VanLaw, because it blames VanLaw (and its alleged inability to clone the recipe) for Trader Joe's decision to stop selling the BBQ sauce. (2-ER-132–135, ¶¶7-27.)

The FAC discloses [in its Exhibit B at 2-ER-118, 120, ¶¶13, 20], and attempts to plead around [in ¶¶26 and 27 at 2-ER-134 and 135], that the parties agreed that neither would be liable to the other for, among other

[2] **Notably, VanLaw and NECF included two limitation-of-liability clauses that expressed a clear intent of the parties to limit damages despite knowing that it could incur such damages. This, combined with the contractual prohibition against reverse-engineering in the NDA at paragraph 3, shows a knowing election on the part of both parties to limit the relief available to one another for the exact conduct that NECF alleges in its FAC.**

things, lost profits or punitive damages, but yet the sole damages sought in the FAC are *lost profits* and *punitive damages*. (2-ER-134, 135, 138, 139, ¶25, 26, 27, and Prayer.)

B. Procedural Posture – The State Court Action

1. VanLaw's December 21, 2017 Complaint In State Court

VanLaw's state court Complaint was prepared on a Judicial Council Form, and contained causes of action for breach of contract and common counts. (3-ER-324–329.) It sought damages for an unpaid invoice in the amount of $27,441.00 related to bottles it purchased for NECF; and separately, it sought storage fees in an unspecified amount (a request which it ultimately did not pursue at trial – see directly below, Section 2). (3-ER-326, ¶¶BC-1, BC-2, BC-4, BC-6.)

2. VanLaw's Explanation of Its December 21, 2017 State-Court Complaint in Its State-Court Trial Brief

VanLaw's state court trial brief is contained at 3-ER-606–608 – 4-ER-610–624. It makes clear that VanLaw is only seeking $27,441.25 for its actual damages on its invoice, and it does not seek any storage fees for the unused bottles. (3-ER-607, lines 2-10, 608, lines 12-28; 4-ER-610, lines 1-2, 620, line 4–621, line 3, 623, lines 2-3.)

3. NECF's February 19, 2019 Cross-Complaint In State Court

NECF's Cross-Complaint was filed more than one year into the case, and it contained causes of action for breach of contract and accounting. (3-ER-336–343.)

4. NECF's State Court Cross-Complaint, According To VanLaw

VanLaw's trial brief, which was filed in the state court on July 9, 2021 [see 3-ER-606], provides an overview of NECF's Cross-Complaint at 4-ER-610, line 3–612, line 14.

Regarding NECF's allegation that it is entitled to damages for VanLaw's alleged failure to use commercially reasonable efforts to ship its goods, VanLaw argued, among other things, that damages stemming from that alleged wrong would violate the limitation-of- liability clauses in the Operating Agreement. (4-ER-622, para. ii.)

Before VanLaw filed its trial brief, VanLaw filed Motion in Limine No. 1, seeking to exclude evidence relating to VanLaw's alleged failure to use commercially reasonable efforts to ship goods because NECF disclosed this alleged unlawful act and resulting damages for the first time just before trial. (3-ER-430.) Motion in Limine No. 1 explained in detail (with evidence) why VanLaw contended it was learning about this theory for the first time just before trial. (3-ER-429–594.) *The point here is not to suggest that the Supreme Court (or any Court) needs to decide the issue as to whether the evidence should have been excluded from the state court*

action; rather, it shows that VanLaw's position going into trial was that it was learning about this claim for the first time, and therefore had not been given a chance to fully litigate the issue. And to be clear, VanLaw is only addressing this here out of an abundance of caution because NECF's Statement of the Case delves into issues that are not relevant to the certified question, but were raised in the Ninth Circuit on the issue preclusion argument.

NECF opposed Motion in Limine No. 1, providing its position as to why it believed VanLaw *should have known* about its claim for damages stemming from VanLaw's failure to use commercially reasonable efforts to ship goods. (3-ER-595–605.)

The state court did not announce a ruling on Motion in Limine No. 1. Rather, it indicated in its Statement of Decision (after trial had concluded) that the Motion was denied. (2-ER-237.)

5. <u>NECF Unsuccessfully Seeks Leave To Amend Its Cross-Complaint In Early 2021 To Add the Allegations Now Contained In The June 16, 2021 Federal Complaint</u>

VanLaw agrees that NECF did indeed seek (and was denied) leave to amend its Cross-Complaint in the state court action; and that ultimately it pursued those claims that it was not permitted to add to the state court Cross-Complaint in the federal action. In other words, the issue of whether the limitation-of-liability clauses barred the *federal claims (those that form*

the basis of the present appeal) was never before the state court, and never decided by the state court. (3-ER-350, 427.)

6. NECF Prevails At Trial, Including On VanLaw's "Limitation of Liability" Defense

NECF's Section B.6. heading and discussion fails to mention that: (1) *both parties* prevailed in full on their respective claims against one another [2-ER-215]; and (2) the state court specifically found that the limitation-of-liability clauses *did not bar NECF's $35,047.60 claim for unpaid royalties related to VanLaw's alleged failure to use commercially reasonable means to ship goods at the end of the relationship between the parties*. (2-ER-240–245.) Regarding point (2), there was no finding that the clauses are unenforceable generally or that they are inapplicable to NECF's $6,000,000.00 claims asserted in the federal action for lost profits related to VanLaw's alleged failed attempts to clone NECF's recipe after the parties' relationship ended.

7. VanLaw Appealed The Judgment And Award Of Fees, And Both Decisions Were Affirmed In Full

NECF accurately describes in its OBM at pp. 22-23 the outcome of VanLaw's appeals of the state court action.

C. Procedural Posture – The Federal Action

1. NECF Commences This Action On June 16, 2021

NECF commenced this action just before the trial commenced in the state court action (2-ER-215, line 1.)

2. The First Motion To Dismiss Is Granted With Leave to Amend

NECF's discussion regarding VanLaw's first motion to dismiss as to the original Complaint focuses largely on VanLaw's assertion of claim and issue preclusion in its first motion to dismiss; an issue which has no bearing on the present appeal or relevance to the certified question. It also glosses over the fact that the first motion to dismiss was also based upon the bar created by the limitation-of- liability clauses. (OBM, pp. 23-25; See also 2-ER-287, 297, 298, 299.)

NECF also fails to point out that in VanLaw's Reply to NECF's Opposition to VanLaw's first motion to dismiss, VanLaw emphasized just how clear it was (based upon NECF's Opposition) that NECF had no ability to amend its Complaint to plead around the limitation-of-liability clauses:

> *[VanLaw] is compelled to first address the limitation of liability clauses. This issue is the starting point of this reply because NECF's opposition establishes that: (1) it is in fact a complete defense to the action; and (2) NECF cannot plead around it. In other words, this Court can and should dismiss the action on these grounds alone, without even deciding whether this action is a compulsory cross-complaint that should have been filed in the State Court Action*. (2-ER-193.) [Emphasis added]

The district court's order on VanLaw's first motion to dismiss is misconstrued by NECF. It expressly refused to "hypothesize" about the availability of "direct damages," and it made clear that NECF would need to amend the Complaint to either: (1) seek remedies that are in fact available under the Operating Agreement, or (2) plead why the available remedies are so deficient or unavailable as to effectively exempt VanLaw from liability. (2-ER-149.) The clear message was that if NECF could do neither, the claims could not survive.

3. The Complaint Is Amended To Plead Facts The First Ruling Suggested Were Sufficient To Defeat A Motion to Dismiss

NECF's C.3. heading is misleading in that the district court expressly refused to hypothesize about (and certainly did not *suggest*) what specific allegations NECF might be able to add to the Complaint in order to plead around the limitation-of-liability clauses. (2-ER-149.)

NECF (as reflected in the two new paragraphs that were added to the FAC) erroneously believed that it could simply indicate that because the *type of damage it happened to suffer* (lost profits) were not available under the Operating Agreement, then the limitation-of-liability clauses should not apply. (2-ER-134-135.) To be clear, as set forth in more detail herein, NECF mistakes (and has continued to mistake) the fact that *it did not suffer any available damages to mean that the clause itself is an exculpatory one.* The test is not whether the plaintiff *suffered* the types of damages available

under the contract. The test is whether the contract exempts a party from responsibility for certain specific acts (such as fraud and statutory violations). The district court correctly applied this standard. (See discussion in C.4. below)

4. The Second Motion To Dismiss Is Granted Without Leave To Amend Despite Pleading Facts The First Ruling Suggested Were Sufficient To Defeat A Motion To Dismiss

NECF's C.4. heading is again misleading. The district court never suggested what facts NECF could plead to defeat the limitation-of-liability clauses.

The following excerpt from VanLaw's Motion to Dismiss the FAC sums up exactly why the FAC should have been (and ultimately was) dismissed with prejudice:

> NECF's FAC should be dismissed pursuant to F.R.C.P. 12(b)(6) because:
>
> 1. The limitation of liability clauses set forth in the Operating Agreement (FAC, Exh. B) completely bar the claims and relief sought in this action.
>
>   a. The Limitation on Liability section in the Operating Agreement expressly forbids, among other things, either party from recovering '*loss of profits, loss of business, interruption of business, or…any indirect, special, incidental or consequential damages of any kind*.' It also states: '*[I]n no event shall either party be liable for any punitive, special, incidental or consequential damages of any kind*…' (FAC, Exh. B, ¶¶13, 20) The *only* damages NECF seeks in the Complaint are: (1) '*past and future lost profits*' and (2) punitive damages. (FAC, ¶¶25, 32, 39, 46,

54, 59, and Prayer). All such damages are alleged to have emanated from a single act: namely, *an alleged attempt (that never came to fruition nor resulted in any benefit to Defendant or Trader Joe's) on the part of Defendant to reverse engineer Plaintiff's barbeque sauce for the benefit of Trader Joe's.* (FAC, ¶¶7-25)

b. Therefore, on its face, the FAC discloses a complete defense to all claims and relief sought. The Court already agreed with this with respect to the original Complaint and *granted* Defendant's Motion to Dismiss the original Complaint, with leave to amend, as follows: 'the Court GRANTS Defendant's Motion based on the limitation on liability provision and DISMISSES Plaintiff's Complaint. Plaintiff is given leave to amend its Complaint to seek remedies permitted under the Operating Agreement and/or to plead why the available remedies are unavailable or so deficient as to effectively exempt Defendant from liability.' (Order Granting Motion to Dismiss, Docket 25, pp. 7-8) In response, Plaintiff added the following two paragraphs to the FAC, and made no other changes:

    i. '26. Upon information and belief, all of Plaintiff's harm from the wrongful conduct alleged herein is a form of lost profits (both past and future). Further, the only possible harm to Plaintiff from the wrongs committed by Defendant are a loss of profits.

    ii. 27. As such, the putative limitation-of-liability provisions in the Operating Agreement (Ex. B, Dkt. 1-2, §§ 13, 20), if applied, would completely exempt Defendant from liability from the wrongs alleged herein because said provisions purport to bar all claims for, 'loss of profits.' Defendant should be judicially estopped from claiming otherwise because it filed a motion to dismiss the entire complaint on the ground of said limitation-of-liability provisions, inter alia. (Mot. 31:14-17: ' 'the limitation of liability clauses disclose a complete defense in that they bar all of the claims and remedies sought in the Complaint.' ' (Dkt. 14.)) And said motion was granted by the Court on that ground (with leave to amend). (Dkt. 25.)'

c. It is clear that Plaintiff mistakes the fact that *it did not suffer any available damages to mean that the clause itself is exculpatory*. In other words, Plaintiff seems to argue that a clause such as the one in this case could never act as a complete bar to an action (even when the plaintiff *bargained for* such a clause) because plaintiffs could simply assert that they did not suffer any damages available under the contract, and therefore the clause is unfair/unenforceable. That position is not consistent with the law. For example, and as explained in more detail herein:

i. The most factually similar case that Defendant found is *Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118. It involved two parties to a commercial transaction with equal bargaining power, a very similar limitation of liability clause, no public interest, and (perhaps most importantly) it completely barred all claims (contract and tort) *because the plaintiff did not suffer any damages available under the contract and instead only alleged damages that were barred by the agreement...* (2-ER-82–85.)

5. NECF Appealed The Dismissal Of The Complaint

The parties agree as to the timeliness of the appeal.

6. The Ninth Circuit Court Of Appeals Requested That This Court Decide A Question of California Law, And This Court Granted That Request

The parties agree as to the procedural history leading to the certified question.

ARGUMENT

A. The Plain Language Of Section 1668 Is Clear

Section 1668 provides: "All contracts which have for their **object, directly or indirectly,** to ***exempt*** anyone from ***responsibility*** for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against the policy of the law." [Emphasis added]

The plain meanings of the key words are as follows:

- "Object" means "the goal or end of an effort or activity." Synonyms include "purpose" and "objective."[3]
- "Directly" means "in a direct manner," "stemming immediately from a source" as in a "*direct result*." Synonyms include "straightforward" or "natural."[4]
- "Indirectly" means "not direct, such as: not directly aimed at or achieved." Example: *indirect consequences.* Synonyms include: "roundabout" or "circular."[5]

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[3] See, https://www.merriam-webster.com/dictionary/object, noun definition 3.a.

[4] See, https://www.merriam-webster.com/dictionary/directly, definition 1.a.; and https://www.merriam-webster.com/dictionary/direct, adjective definitions 2.a. and 3.

[5] See, https://www.merriam-webster.com/dictionary/indirectly, definition c.; and https://www.merriam-webster.com/thesaurus/indirect

- "Exempt" means "free or released from some liability or requirement to which others are subject." Examples include: being exempt from jury duty, taxes, or military duty. Synonym: "immune."[6]
- Responsibility means "something for which one is…liable to be called on to answer" or "able to answer for one's conduct and obligations." Synonyms include "liability" and "accountability."[7]

Stated differently, contracts which have for their o*bjective or purpose* (either in a *straightforward* or *roundabout* way) to *immunize* someone from *liability or accountability* for fraud, willful injury to another's person or property, or willful or negligent violations of law, are unenforceable.

VanLaw's position is that the limitation-of-liability clauses involved in the present dispute are fully enforceable under the plain meaning of Section 1668, and any other outcome would have a chilling effect on businesses who freely enter into similar clauses with other businesses on a regular basis in this State.

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[6] See, https://www.merriam-webster.com/dictionary/exempt; and https://www.merriam-webster.com/thesaurus/exempt

[7] See, https://www.merriam-webster.com/dictionary/responsibility, definition 2; https://www.merriam-webster.com/dictionary/responsible, definitions 1.a. and 2.a.; and https://www.merriam-webster.com/thesaurus/responsibility

B. NECF's Argument About Legislative Intent Is Highly Flawed

NECF argues that the Legislature could not have intended for parties to "effectively eliminate" damages and thus "practically obviate Section 1668." It goes on to illustrate the point by arguing that the Legislature could not have intended for parties to limit their exposure to one another to one penny or an apology. (OBM, pg. 29.)

But NECF fails to address the reverse of that logic: The Legislature could not have intended that two businesses of equal bargaining power who negotiated mutual limitation-of-liability clauses (e.g., agreeing to not sue one another for lost profits and/or limiting the amount of damages) could be subject to *unlimited damages* simply because one of the parties later decided it did not like the limitation-of-liability clauses and wanted to pursue a form of relief that was not available under its bargained-for contract, and then couched a breach of contract as a tort to invoke Section 1668.

In terms of *legislative intent*, West's Annotated California Codes' "Notes of Decisions" for Section 1668 cites to three cases for "Legislative Intent." The annotations state, *verbatim*:

- "The purpose of the statute providing that a contract releasing a party from responsibility for fraud, willful injury to property or a person, or violation of law is against public policy is to prohibit parties from granting themselves licenses to commit future aggravated wrongs (or future negligent acts when certain public policies are implicated). Castelo v. Xceed Financial Credit

Union (Cal.App. 2 Dist. 2023) 308 Cal.Rptr.3d 611. Contracts [] 114"

- "The statute describing contracts that are contrary to policy or law is meant to prohibit contracts releasing liability for future torts, not to prohibit settlements of disputes relating to past conduct. Daneshmand v. City of San Juan Capistrano (App. 4 Dist. 2021) 275 Cal.Rptr.3d 245. Contracts [] 114"

- "Statute providing that contracts releasing one from responsibility for certain acts are against public policy does not represent an implied legislative determination to allow releases of liability for other misconduct, such as gross negligence, as long as the release does not affect the public interest. City of Santa Barbara v. Superior Court (2007) 62 Cal.Rptr.3d 527, 41 Cal.4th 747, 161 P.3d 1095. Contracts [] 114"

Importantly, none of the above cases cited for "Legislative Intent" involves a business-to-business bargained-for limitation-of-liability clause. Rather, each involves unequal bargaining power and one-sided complete releases of all liability (employee signing a separation agreement at the time of termination: *Castelo v. Xceed Financial Credit Union* (2023) 308 Cal.Rptr.3d 611; individual ratepayers entering into standard releases with the City upon receipt of a refund: *Daneshmand v. City of San Juan Capistrano* (2021) 275 Cal.Rptr.3d 245; individuals entering into a traditional waiver, disclaimer, and release of *all liability for "any negligent act*" with the City: *City of Santa Barbara v. Superior Court* (2007) 62 Cal.Rptr.3d 527.)

The Legislative intent and the plain meaning of the statute do not even remotely suggest that parties like VanLaw and NECF are barred from

limiting their damages to one another in the future should they choose to bargain for that result. And NECF's fantastical hypotheticals about assaults on the moon [OBM, pg. 30] have no place in this discussion. Indeed, because the clauses at issue in this case (like so many other similar clauses that are agreed to between businesses every day) do not have for their object (neither directly nor indirectly) to eliminate responsibility for future torts or illegal conduct, they do not even come close to comparing to the outrageous example of no damages being available except for an assault that occurs on the moon.

There is simply no indication that the Legislature intended to prevent parties like VanLaw and NECF from freely entering into clauses like the ones at issue in this case, and then using such clauses in a case like the present one. To the contrary, case law makes clear (as discussed below) that these clauses can and should be enforced without running afoul to Section 1668.

C. Public Policy Supports VanLaw's Interpretation Of Section 1668, Not NECF's Interpretation

In its OBM at pp. 31-32, NECF seems to suggest, citing to *City of Santa Barbara v. Superior Court* (2007) 62 Cal.Rptr.3d 527 (which involved the tragic drowning death of a disabled child), that "freedom of contract" has only a small role in this discussion. Rather, it suggests that the concept of "human rights" should have a greater role in this business-

versus-business lawsuit. In fact, NECF essentially suggests that businesses' rights to freely enter into contracts should be disregarded and that businesses should be treated like naïve consumers or uninformed citizens who are presented with confusing contracts of adhesion.

The public policy behind protecting individuals with unequal bargaining power while balancing parties' rights to enforce their contracts often comes up in the context of unconscionability. For example, *A & M Produce Co. v. FMC Corp.* (1982) 135 Cal.App.3d 473, 486–487 provides as follows:

> Of course the mere fact that a contract term is not read or understood by the non-drafting party or that the drafting party occupies a superior bargaining position will not authorize a court to refuse to enforce the contract. Although an argument can be made that contract terms not actively negotiated between the parties fall outside the 'circle of assent' which constitutes the actual agreement [Citations.], commercial practicalities dictate that unbargained-for terms only be denied enforcement where they are also *substantively* unreasonable. [Citations.] No precise definition of substantive unconscionability can be proffered. Cases have talked in terms of 'overly-harsh' or 'one-sided' results. [Citations] One commentator has pointed out, however, that '... unconscionability turns not only on a 'one-sided' result, but also on an absence of 'justification' for it.' [Citations], which is only to say that substantive unconscionability must be evaluated as of the time the contract was made. (See U.Com.Code, § 2–302.) The most detailed and specific commentaries observe that a contract is largely an allocation of risks between the parties, and therefore that a contractual term is substantively suspect if it reallocates the risks of the bargain in an objectively unreasonable or unexpected manner. [Citations] But not all unreasonable risk reallocations are unconscionable; rather, enforceability of the clause is tied to the procedural aspects of unconscionability (see *ante,* pp. [485–486]) such that the greater the unfair surprise or inequality of bargaining power, the less unreasonable the risk reallocation

which will be tolerated. [Citations]

The foregoing illustrates the important policy behind honoring parties' contracts, especially where there is little-to-no unconscionability.

In the present case, NECF has never asserted (either by way of its FAC or its argument) that any unconscionability is present. And in fact, the District Court gave NECF an opportunity to amend its Complaint and make such an allegation, and NECF did not. (2-ER-149.)

So, this appeal really does come down to whether parties who freely enter into bargained-for mutual limitation-of-liability clauses can have such clauses invalidated any time they *do not suffer any damages available to them under the contract*. Can litigants simply *allege* that a breach of a provision in a contract (here, the reverse engineering clause at paragraph 3 of the NDA) that forms the entire gravamen of their case amounted to a tort, invoke Section 1668, and declare the limitation-of-liability clauses completely unenforceable? In other words, should this Court ignore freedom of contract in favor of excusing NECF from its contractual obligations simply because it wishes it would have (in hindsight) bargained for more forms of available relief in its contract? Like the District Court correctly pointed out with respect to NECF's public policy argument, the answer is, *no*:

> [NECF] can bring its claims only if the Limitation provision is invalidated by California Civil Code § 1668, which bars limitations on damages for intentional or grossly negligent conduct as against

> public policy. [NECF]'s argument as to public policy appears to be that '[f]or every wrong there is a remedy.' Opp'n at 5 (quoting CAL. CIV. CODE § 3523). ..
>
> [NECF] responds that enforcing the Limitation on Liability effectively renders the reverse-engineering provision nugatory. Opp'n at 3. But with the Limitation provision in place, [VanLaw] is still liable for unpaid royalties or direct damages from reverse-engineering [NECF]'s product, and [NECF] could seek injunctive relief to stop [VanLaw] selling its reverse-engineered sauce. The provision does not bar all liability, just liability for specific types of relief.
>
> The Court understands the frustrating position [NECF] finds itself in, having allegedly been wronged but not in a form compensable by the contract. But [NECF] makes no suggestion that the contract is invalid or the product of unequal bargaining power. Indeed, the contract places the same limitations on [VanLaw]'s remedies, were [NECF] to reverse-engineer [VanLaw]'s sauce in turn. The Court may not erase bargained-for contract provisions simply because one party now wishes they were different. (1-ER-7–8.)

D. The Statutes And The Common Law That NECF Cites In The OBM Do Not Support NECF's Position

At pages 32-37 of its OBM, NECF cites to seven statutes or common-law doctrines that it contends support its request to have the limitation-of-liability clauses invalidated. None of the seven examples is compelling.

1. Section 533 Of The Insurance Code

NECF argues that because the Insurance Code prohibits insurances companies from insuring against willful acts, so too should private businesses like NECF and VanLaw be prohibited from enforcing a limitation-of-liability clause as a complete defense to a case (one that is

rooted in a contract provision) seeking damages that are barred by their agreement. (OBM, pp. 32-33.) In fact, NECF argues that the limitation-of-liability clauses that VanLaw seeks to enforce are actually worse than an insurance policy that purports to insure against willful torts (assuming Section 533 did not exist) because at least an insurance policy has limits. (OBM, pg. 33.)

This argument defies logic. Indeed, there is a major difference between a heavily-regulated industry (insurance) that has its own "Code" of laws, including Section 533 purporting to protect an unsuspecting victim (who is not a party to the insurance contract) from intentional wrongdoing; and two businesses who bargain for their own mutual limitations of liability to one another. Perhaps more importantly, Section 533 of the Insurance Code, like Section 1668, prohibits contracts where the *object* is to avoid all liability as a future tortfeasor. Conversely, the limitation-of-liability clauses in this case did not have that object and merely had the impact of providing a complete defense to the allegations by NECF due to the nature of the relief sought.

2. Intentional Tortfeasors

NECF next argues that because intentional tortfeasors are not entitled to contribution or the benefit of several liability under the Code of Civil Procedure, it follows that the clauses in this case should be unenforceable. (OBM, pp. 34-35.) Again, NECF misses the point. The

obvious purpose of this codified concept is to protect the unsuspecting victim of an intentional tort. This is no way compares to two businesses who made a choice to enter into a contractual relationship and expressly limit the damages available to one another despite knowing (and explicitly acknowledging) that those damages could arise in the future. (See 2-ER-118, 120, ¶¶13, 20.)

3. Punitive Damages

NECF next argues that it "believes" parties are not permitted to limit punitive damages, but admittedly could not find a case that confirms that belief. If its belief is correct, then NECF argues that Section 1668 should also prohibit parties from limiting compensatory damages. (OBM, pg. 35.)

Needless to say, NECF's beliefs about punitive damages limitations have no place in this appeal. The law is well-settled that limitation of liability clauses are enforceable so long as they do not violate Section 1668. This means that, assuming the limitation-of-liability clauses are enforceable, then there is no entitlement to any damages, including punitive damages.

4. Implied Covenant Of Good Faith And Fair Dealing

NECF next argues that because the implied covenant of good faith and fair dealing cannot be waived, then the limitation-of-liability clauses should not be enforced. (OBM, pg. 36.)

But breaches of the covenant of good faith implied within contracts are not tortious outside the context of insurance policies, which means that the covenant can only be breached if the underlying contract is breached. (*Cates Construction, Inc. v. Talbot Partners* (1999) 21 Cal.4th 28, 43.) It follows that if a breach of contract claim is barred by a limitation-of-liability clause, the breach of covenant of good faith and fair dealing claim would also be barred. (*Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118, 1127.)

5. Section 3523 Of The Civil Code

NECF next cites to Section 3523 of the Civil Code, which provides that, for every wrong, there is a remedy. This is true, and it is also true that remedies can take on many forms, both legal and equitable. And it is well-settled that parties can *limit* available remedies.

NECF is essentially seeking *anticipated* lost profits, which is admittedly barred by the clauses. Importantly, the limitation-of-liability clauses would not stop NECF from seeking, for example, direct damages such as disgorgement of profits actually earned by VanLaw/Trader Joe's or royalties (calculated consistent with the Operating Agreement) on barbeque sauce sold by VanLaw to Trader Joe's. The FAC admits that no such damages were suffered *because the reverse engineering never actually occurred, and no one benefitted from the alleged attempted recipe clone.* But this would not stop NECF from seeking to have the reverse-

engineering clause enforced either by way of an injunction or declaratory relief, which are both considered "remedies."

6. Contract Interpretation

NECF next argues that the rules of contract interpretation would prevent a party from waiving liability for violating an express contract provision. (OBM, pg. 36.)

But NECF again misses the point and assumes that every breach of a contract clause results in the non-breaching party suffering damages. It is not uncommon for a breach of a contract provision to not result in damages, even in the absence of a limitation-of-liability clause. An example would be if a party used another party's confidential information in violation of an express provision in a contract, with the non-breaching party not suffering harm as a result. In that scenario, the party might need a court order to enjoin the use of confidential information. And this is often the only remedy available for such a violation, but it serves its purpose in any event.

Again, every claim in the FAC describes the unlawful act as an offer/attempt to clone, and the prohibition against cloning arises solely out of the NDA, under the so-called reverse-engineering clause at paragraph 3. And the reality is that NECF suffered no form of available damages for that alleged violation, but it has never been prevented from enforcing that provision in the NDA. It simply chose not to, and instead opted to sue

years after the alleged breach, couching the alleged breach of the express contract provision as a tort, hoping to invoke Section 1668.

7. Illusory Promise

NECF next argues that the reverse-engineering clause would constitute an illusory promise if it cannot recover its *anticipated* lost profits. (OBM, pg. 37.) This argument fails for the exact same reasons as set forth directly above in Section D.6.

E. The Relevant Court Of Appeal Decisions

1. The Pertinent Cases Cited By The Ninth Circuit, Plus Two Additional Pertinent Cases

It is not disputed that, in general, limitation of liability clauses are permissible. (Order Certifying Question filed Dec. 6, 2023, pg. 6, citing *Lewis v. YouTube, LLC* (2015) 244 Cal. App. 118, 125; see also, *Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118, 1126: "Generally, 'a limitation of liability clause is intended to protect the wrongdoer defendant from unlimited liability.' (1 Witkin, Summary of Cal. Law (10th ed. 2005) Contracts, § 503, pp. 552-554.) Clauses of this type 'have long been recognized as valid in California.' (*Markborough California, Inc. v. Superior Court* (1991) 227 Cal.App.3d 705, 714, 277 Cal.Rptr. 919.)")

The Ninth Circuit cited four cases at page 8 of its December 6, 2023 Order in support of its position that California's lower courts are split on

the issue presented by the certified question. Those cases are addressed directly below (E.1.a.-d.). Furthermore, there are two other cases (addressed below at E.1.e.-f.) not mentioned by the Ninth Circuit that are relevant to the issues.

All of the cases can be harmonized with one another. Collectively, they stand for the proposition that whether a limitation-of-liability clause violates Section 1668 must be decided on a case-by-case basis, after consideration of various factors as applied to the unique facts of each case.

a. *Farnham v. Superior Ct. (Sequoia Holdings, Inc.)* (1997) 60 Cal. App. 4th 69 (**Limitation-Of-Liability Clause Enforced**).

The first case cited by the Ninth Circuit is *Farnham v. Superior Ct. (Sequoia Holdings, Inc.)* (1997) 60 Cal. App. 4th 69.

Farnham worked for Sequoia Holdings, Inc. as an Executive Vice President and Chief Operating Officer. (*Id.* At 71.) His employment contract stated that, in the event of a breach of any terms by Sequoia, the sole remedy was binding arbitration in Los Angeles, California. (*Id.* At 72.) By signing the contract, Farnham also waived any right he had to file a lawsuit for damages against any shareholder, director, officer, or employee for any claim, cause of action, damage, cost, or expense arising from, in connection with, or in relating to the terms of the agreement or any breach thereof. (*Id.* At 72.) Farnham sued two shareholders, officers, and directors

of Sequoia Holdings, Inc., Edward R. Whitehurst and Joseph H. Brown, claiming they defamed him after he led an investigation against them uncovering a "penny stock fraud" scheme of which they were a part. (*Id.* At 72.)

Farnham's claims against Sequoia Holdings were compelled to arbitration, while the claims against Whitehurst and Brown were severed and presumably stayed by the Superior Court pending the outcome of the arbitration. (*Id.* At 72.) Thereafter, the arbitrator awarded Farnham $1.5M against Sequoia. (*Id.* at 72.) Whitehurst and Brown filed (and the Superior Court sustained) a demurrer in the Superior Court action, based upon Farnham's agreement to the "sole remedy" provision, despite the fact that this meant Farnham had no remedy against Whitehurst and Brown:

> As a practical matter, Whitehurst and Brown contended Farnham had no remedy against them because they were not bound by the arbitration agreement and because Farnham had waived his right to bring a 'lawsuit.' Farnham opposed the demurrer, contending Whitehurst and Brown were acting in their individual capacities at the time they defamed Farnham. (*Id.* at 73.)

Farnham appealed, relying upon Section 1668.

The Court of Appeal affirmed the ruling on the demurrer, noting that this appeared to be the first case of its kind:

> Although exemptions from *all* liability for intentional wrongs, gross negligence and violations of the law have been consistently invalidated…, we have not found any case addressing a *limitation* on liability for intentional wrongs, gross negligence or violations of the law. (See *Wheeler v. Oppenheimer* (1956) 140 Cal.App.2d 497, 499, 295 P.2d 128 [a provision restricting recovery to actual 'costs and

> expenses' is a limitation on liability, not a provision for liquidated damages, because it is 'not intended to prescribe a definite liability,' only to impose a 'limitation within which damages might be proved']; see also *Tunkl v. Regents of University of California* (1963) 60 Cal.2d 92, 101, 32 Cal.Rptr. 33, 383 P.2d 441 ['no public policy opposes private, voluntary transactions in which one party, for a consideration, agrees to shoulder a risk which the law would otherwise have placed upon the other party'].) (*Farnham,* 60 Cal. App. 4th at 74-75.)

b. *CAZA Drilling (Cal.), Inc. v. TEG Oil & Gas U.S.A., Inc.* (2006) 142 Cal.App. 4th 453 (**Limitation-Of- Liability Clause Enforced**).

The second case cited by the Ninth Circuit is *CAZA Drilling (Cal.), Inc. v. TEG Oil & Gas U.S.A., Inc.* (2006) 142 Cal.App. 4th 453.

CAZA, like the present appeal, involved a business-to-business transaction. TEG Oil & Gas U.S.A., Inc. ("TEG") hired CAZA Drilling (California), Inc. ("CAZA") to drill an oil well. (*Id.* at 457.) The contract stated that "[e]xcept for such obligations and liabilities specifically assumed by [CAZA], [TEG] shall be solely responsible and assume liability for all consequences of operations by both parties." (*Id.* at 459.) CAZA specifically assumed obligations and liabilities including damages to its equipment, injury to its employees, and certain environmental concerns. (*Id.* at 459-460.) The contract also stated that CAZA was required to use "all reasonable means" to prevent well blowouts and to comply with all federal, state, and local government laws, rules, and regulations. (*Id.* at 459.) There was a blowout, destroying the well. (*Id.* at 457.)

CAZA filed a complaint against TEG for breach of contract. (*Id.* at 458.) TEG filed a cross-complaint seeking compensation for economic loss and physical harm to equipment and facilities in connection with the drilling blowout. (*Id.* at 457-458.) The Superior Court of Los Angeles granted CAZA summary judgment as to the cross-complaint based on the limitation of liability clauses between the parties. (*Id.* at 464.) CAZA argued (and the Superior Court agreed) that the limitation of liability provisions in the parties' agreement precluded the recovery of the types of damages sought in the cross-complaint. (*Id.* at 464.)

TEG filed an appeal. The Court of Appeal affirmed the granting of summary judgment in favor of CAZA, finding that no public interest was involved in the contract between CAZA and TEG, and, as a result, the clause relieving CAZA from the consequences of its own negligence could be enforced. (*Id.* at 468-469.) The Court of Appeal also noted that TEG made no serious effort to identify a specific law or regulation potentially violated by CAZA so as to trigger application of section 1668. (*Id.* at 476.)

c. *Klein v. Asgrow Seed Co.* (1966) 246 Cal.App.2d 87 (**Limitation-Of-Liability Clause Not Enforced**).

The third case cited by the Ninth Circuit is *Klein v. Asgrow Seed Co.* (1966) 246 Cal.App.2d 87.

Bud Klein, Louis Mersaroli and Reginald Mersaroli were individual plaintiffs and joint venturers engaged in tomato growing. (*Id.* at 89.) They

obtained a judgment in the sum of $14,439.32 against Associated Farm Supplies, a corporation, for breach of warranty in the sale of tomato seed in 1962, specifically related to the tomato seed not being of the variety it was represented to be (VF-36). (*Id.* at 89-90.) Associated, the immediate supplier, on a cross-complaint, obtained a judgment against its supplier of the seed, Ranch Supply, Inc., which in turn obtained a judgment against its seller, Reed Lockhart, a seed broker. (*Id.* at 89-90.) Lockhart obtained a judgment against Asgrow Seed Company, the manufacturer of the seed. (*Id.* at 90.) All judgments were in the same amount; and all judgments (in the chain of succession of sales and purchases) were on the theory of breach of both express and implied warranty by each seller to each buyer. (*Id.* at 90.) Because none of the parties except for Lockhart was in privity with Asgrow, the trial court refused to award damages to any party against Asgrow (except for Lockhart). (*Id.* at 90.)

Asgrow appealed the judgment in favor of Lockhart, and all other parties (except plaintiffs) also appealed, arguing that they should have been awarded damages against Asgrow. (*Id.* at 90.) Asgrow argued that a limitation-of-liability clause between it and Lockhart limited Asgrow's liability to Lockhart to the price of the seed.

The Court of Appeal refused to enforce the limitation-of-liability clause for the following reasons:

- There was an express warranty and representation that the seed was VF-36. (*Id.* at 99.)
- "[T]here was no agreement between any of the parties that Asgrow's warranty was to be drawn back (i.e., limited to a price refund) if and when Asgrow knowingly and deliberately sold a mixed seed as VF-36; nor was there a custom or course of dealing to that effect… Had there been such an agreement it would have been void." (*Id.* at 99.)
- "Asgrow placed this seed on the market warranting it to be VF-36 *when it knew that it was not VF-36 but an intermixture of VF-36 with 'rogues,' the percentages of each being unknown.*" (*Id.* at 99.)
- Had Asgrow attempted to limit its liability for expressly violating a *representation and warranty* regarding the seeds, it would have violated Section 1668, particularly in light of Agricultural Code 914, which provides in part: "It is unlawful to ship, deliver, transport, or sell any agricultural or vegetable seed within this State: ... (4) Having a false or misleading labelling, or pertaining to which there has been a false or misleading advertisement." (*Id.* at 100.)
- "The express warranty that the seed was VF-36 when it was in fact mixed and Asgrow's knowledge of falsity of that statement creates the liability. Civil Code section 1668 makes the statement of limitation of liability void as against public policy." (*Id.* at 100-101.)

d. *Health Net of California, Inc. v. Department of Health Services* (2003) 113 Cal.App.4th 224 (**Limitation-Of-Liability Clause Not Enforced**).

The fourth case cited by the Ninth Circuit is *Health Net of California, Inc. v. Department of Health Services* (2003) 113 Cal.App.4th 224.

This case involved the Two-Plan Medi-Cal model. In regions designated by Department of Health Services ("DHS"), health services are provided to Medi-Cal beneficiaries though no more than two prepaid health plans, a commercial plan or local initiative. (*Id.* at 228.) DHS designated Tulare County as one of the regions subject to the Two-Plan Model. (*Id.* at 228.)

Health Net operated the commercial plan pursuant to DHS's Standard Agreement. (*Id.* at 228.) In 1997, DHS began proposing amendments to the Standard Agreement. (*Id.* at 228.) Health Net *strenuously objected to one amendment*, but *reluctantly* signed in 1998 because DHS insisted that Health Net sign as a condition of receiving a legally required retroactive rate increase. (*Id.* at 228.)

The court described the limitation clause in the applicable agreement as follows:

> Amendment A07 revised Section 3.1 of the Standard Agreement (hereinafter Section 3.1)—the contractual clause at issue here. Section 3.1, headed 'Interpretation of Contract,' provides in its

> revised form as follows: 'If it is necessary to interpret this Contract, all applicable laws may be used as aids in interpreting the Contract. However, the parties agree that any such applicable laws shall not be interpreted to create contractual obligations upon DHS or Contractor [(Health Net)], unless such applicable laws are expressly incorporated into this Contract in some section other than this Section 3.1, Interpretation of Contract. Except for Section 3.19, Sanctions and Section 3.20, Liquidated Damages Provision, *the parties agree that any remedies for DHS'[s] or Contractor's non-compliance with laws not expressly incorporated into this Contract, or any covenants implied to be part of this Contract, shall not include money damages, but may include equitable remedies such as injunctive relief or specific performance.* In the event any provision of this Contract is held invalid by a court, the remainder of this Contract shall not be affected. This Contract is the product of mutual negotiation, and if any ambiguities should arise in the interpretation of this Contract, both parties shall be deemed authors of this Contract.' (Italics added.)
>
> Amendment A07 also deleted former Section 3.2 of the Standard Agreement. The pertinent effect of this deletion was to eliminate any reference in the agreement to the sections of the Welfare and Institutions Code regarding the Two–Plan Model (Welf. & Inst.Code, § 14087.305) and the related regulations promulgated by DHS (Cal.Code Regs., tit. 22, §§ 50185.5, 53800 et seq.), which the trial court found DHS had violated here. And as a result, Section 3.1 operated to prohibit the recovery of damages for DHS's violation of these statutory and regulatory provisions because that section bars the recovery of damages for the failure to comply with any laws *not expressly incorporated* into the contract." (*Id.* at 228-229.)

Health Net sued DHS for injunctive relief, breach of contract, and mandamus. (*Id.* at 230.) Health Net alleged that as a result of DHS's enrollment practices, Health Net had not received any default enrollees in Tulare County in April and May 1999, whereas Blue Cross had received thousands, in violation of Welfare and Institutions Code section 14087.305(j). (*Id.* at 230.) Health Net sought and obtained a temporary

restraining order prohibiting DHS from assigning any further default enrollees to Blue Cross. (*Id.* at 230.) Despite the violation of the Welfare and Institutions Code, the trial court refused to award damages to Health Net due to the limitation-of-liability clause at Section 3.1 of the parties' agreement. (*Id.* at 231-232.)

After a lengthy analysis of the applicable clause, *Health Net* concludes: "[the] exculpatory clause affects the public interest and therefore violates section 1668." (*Id.* at 239.) The court therefore refused to enforce this provision to bar the claims alleged, analyzing the issue as follows:

> While courts have often observed that the application of section 1668 is not as broad as its language suggests, they have nonetheless held that under the statute, 'a party [cannot] contract away liability for his fraudulent or intentional acts or for his negligent violations of *statutory* law.' [Citations] We see no reason why this settled interpretation of section 1668 should not be extended to cover *regulatory* violations in light of the fact that regulations, by definition, merely 'implement, interpret, or make specific' statutory law (Gov.Code, § 11342.600) and given that the language of section 1668 is not limited to statutory violations but more broadly refers to any 'violation of law.' It also makes no difference that the contractual clause here bars only the recovery of damages, and not equitable relief, because section 1668 can apply to a limitation on liability (*Klein v. Asgrow Seed Co.* (1966) 246 Cal.App.2d 87, 99–101, 54 Cal.Rptr. 609 (*Klein*)), at least where the limitation rises to the level of an 'exempt[ion] ... from responsibility for [a] ... violation of law' in the words of section 1668. An unqualified prohibition against the recovery of damages in the context of a commercial transaction certainly qualifies as such an exemption.…
>
> Based on these canons of statutory construction, we cannot construe section 1668 to invalidate all contracts that seek to exempt a party from responsibility for *any* violation of law, including any common law or contractual violation; otherwise, there would be no need for the statute to separately identify fraud or willful injury, in addition

to any 'violation of law,' as prohibited objects of an exculpation. Further, '[d]espite its purported application to '[a]ll contracts,' section 1668 does not bar either contractual indemnity or insurance, notwithstanding that (aside from semantics) the practical effect of both is an 'exempt[ion]' from liability for negligence.' (*Farnham v. Superior Court* (1997) 60 Cal.App.4th 69, 74, 70 Cal.Rptr.2d 85 (*Farnham*) ['Section 1668 is not strictly applied'].) Accordingly, '[d]espite its broad language, section 1668 does not apply to every contract' or *every* violation of law. (See *Vilner v. Crocker National Bank* (1979) 89 Cal.App.3d 732, 735, 152 Cal.Rptr. 850; *Farnham, supra,* 60 Cal.App.4th at p. 74, 70 Cal.Rptr.2d 85.)…

Accordingly, despite differences in the interpretation of the scope of section 1668, California courts have construed the statute for more than 85 years to at least invalidate contract clauses that relieve a party from responsibility for future statutory and regulatory violations. (See, e.g., *Union Constr. Co. v. Western Union Tel. Co.* (1912) 163 Cal. 298, 314–315, 125 P. 242 [statute requiring telegraph company to use great care and diligence in the transmission and delivery of messages]; *In re Marriage of Fell* (1997) 55 Cal.App.4th 1058, 1064–1065, 64 Cal.Rptr.2d 522 [statute requiring financial disclosures prior to marital settlement agreement]; *Halliday v. Greene, supra,* 244 Cal.App.2d at p. 488, 53 Cal.Rptr. 267 [general industry safety order requiring two escape exits from work area]; *Hanna v. Lederman* (1963) 223 Cal.App.2d 786, 792, 36 Cal.Rptr. 150 [municipal code section specifying sprinkler system alarm requirements]; see *Delta Air Lines, Inc. v. Douglas Aircraft Co., supra,* 238 Cal.App.2d at pp. 105–106, 47 Cal.Rptr. 518 [FAA regulation].)

In this instance, DHS has invoked Section 3.1 of the agreement to exculpate it from liability for damages to Health Net for the violation of statutory law (Welf. & Inst.Code, § 14087.305, subd. (j)), as defined by its implementing regulations (Cal.Code Regs., tit. 22, §§ 50185.5, subds. (b)(12), (g)(8), 53820). Such an exculpatory clause violates section 1668. (*Id.* at 227-236.)

e. *Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118 (**Limitation-Of-Liability Clause Enforced**).

Despite the District Court's reliance upon *Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118 in granting the Motion to Dismiss the Cross-Complaint, the Ninth Circuit did not mention it in its December 6, 2023 Order. It is, however, directly on point on this appeal.

Eco Safe sold ozone-based food disinfection equipment and engaged in preliminary discussions with Carl's Jr to provide such equipment to Carl's Jr. (*Id.* at 1121.) Appellant entered into an agreement with Food Safety, a testing agency. (*Id.* at 1122.) Under the agreement, Food Safety was to perform a "challenge study" of Eco Safe's equipment. (*Id.* at 1122.) Food Safety stated that it had examined the efficacy of Eco Safe's equipment in eliminating pathogenic bacteria from lettuce and tomatoes and made certain findings. (*Id.* at 1122.) Eco Safe issued a press release describing the study results as "excellent." (*Id.* at 1122.) Ultimately, Carl's Jr was not interested in using Eco Safe's equipment. (*Id.* at 1122.)

Eco Safe then refused to pay Food Safety for the study, prompting Food Safety to file suit for an open book account, account stated, and services rendered, alleging it was owed $10,171.26 for conducting the study. (*Id.* at 1122-1123.) Eco Safe filed a cross-complaint, alleging breach

of contract, negligence, fraud, and related claims. (*Id.* at 1123.) The trial court granted summary judgment in favor of Food Safety on Eco Safe's cross-complaint, concluding that all claims failed in light of: (1) a limitation-of-liability clause in the parties' contract, (2) Eco Safe's failure to establish fraud or deceit, and (3) the absence of evidence that Respondent suffered damages from the study. (*Id.* at 1123.) The Court of Appeal affirmed.

The clause at issue in *Food Safety* was as follows:

> IN NO EVENT SHALL [FOOD SAFETY] BE LIABLE FOR INDIRECT, SPECIAL, INCIDENTAL OR CONSEQUENTIAL DAMAGES INCLUDING (BUT NOT LIMITED TO) DAMAGES FOR LOSS OF PROFIT OR GOODWILL REGARDLESS OF (A) THE NEGLIGENCE (EITHER SOLE OR CONCURRENT) OF [FOOD SAFETY] AND (B) WHETHER [FOOD SAFETY] HAS BEEN INFORMED OF THE POSSIBILITY OF SUCH DAMAGES. [Food Safety's] total liability to you in connection with the work herein covered for any and all injuries, losses, expenses, demands, claims or damages whatsoever arising out of or in any way related to the work herein covered, from any cause or causes, shall not exceed an amount equal to the lesser of (a) damages suffered by you as the direct result thereof, or (b) the total amount paid by you to [Food Safety] for the services herein covered. We accept no legal responsibility for the purposes for which you use the test results. (*Id.* at 1126)

The court analyzed the issues as follows:

- As a starting point, Eco Safe's negligence and bad faith claims asserted nothing more than a breach of Food Safety's contractual obligations, and Eco Safe's claim (or claims) for the breach of

these obligations failed in light of the contract provision limiting Food Safety's liability. (*Id.* at 1125-1126.)

- "With respect to claims for breach of contract, limitation of liability clauses are enforceable unless they are unconscionable, that is, the improper result of unequal bargaining power or contrary to public policy." (*Id.* at 1126.)
- "Furthermore, they are enforceable with respect to claims for ordinary negligence unless the underlying transaction 'affects the public interest' under the criteria specified in *Tunkl v. Regents of University of California* (1963) 60 Cal.2d 92, 98-100, 32 Cal.Rptr. 33, 383 P.2d 441 (*Tunkl*)." (*Id.* at 1126.) And limitation of liability clauses are ineffective with respect to claims for fraud and misrepresentation. (*Id.* at 1126.)
- "We further conclude that the clause effectively limits Food Safety's liability for breaches of contractual obligations and ordinary negligence, as nothing before us suggests that the clause is unconscionable or affects the public interest." (*Id.* at 1127.)
- Eco Safe did not assert that the clause was the product of unequal bargaining power, that it contravened public policy, or that it affected the public interest, as specified in Tunkl. Therefore, the clause regulated Eco Safe's potential recovery with respect to its

claims for breach of the contract and ordinary negligence. (*Id.* at 1127.)

- "Because it is undisputed that Eco Safe has paid nothing to Food Safety for the study,[8] the clause thus prohibits a recovery for breach of contract. This conclusion necessarily encompasses Eco Safe's bad faith claim, as breaches of the covenant of good faith implied within contracts are not tortious outside the context of insurance policies. [Citations]" (*Id.* at 1127.)
- Had Eco Safe alleged a claim for ordinary negligence, the limitation of liability clause would have precluded a recovery because it expressly encompassed "the negligence (either sole or concurrent) of" Food Safety. (*Id.* at 1128.)
- Finally and importantly:
    - ***Because the parties submitted no extrinsic evidence bearing on the meaning of the clause, its interpretation is a question of law.*** [Citations] ***We therefore inquire into the parties' intentions, as disclosed by the language of the contract.*** [Citations] As noted above, following the warranty provision, the clause states that '[i]n *no* event' is Food Safety liable for damages—including damages for negligence—'arising out of or *in any way related to* the

[8] In other words, it was undisputed that Eco Safe did not suffer either of the two forms of damages available under the agreement. Had it suffered such damages, the action would not have been barred. ***Similarly, in the present case, the FAC makes clear that Appellant did not suffer any form of damages that would be available to it under the agreements.*** For example, the FAC admits that neither Trader Joe's nor Appellee earned any money from the alleged attempted reverse engineering, meaning that there would be no direct harm to Appellant such as unpaid royalties under the Operating Agreement.

> work herein covered, *from any cause or causes.*' (Italics added.) ***In view of this broad and unqualified language, the clause must be regarded as establishing a limitation on Food Safety's liability sufficient to encompass Eco Safe's claims for breach of contract, bad faith, and negligence.*** (*Id.* at 1128.)

f. *Epochal Enterprises, Inc. v LF Encinitas Properties, LLC* (2024) 99 Cal.App.5th 44 (**Limitation-Of-Liability Clause Not Enforced**).

Epochal Enterprises, Inc. v LF Encinitas Properties, LLC (2024) 99 Cal.App.5th 44 could not have been addressed by the Ninth Circuit because it was just published in January of this year. But it does address the issues involved in this appeal and it discusses the majority of the cases on the issue.

The case involved a commercial lease which contained a limitation-of-liability clause. LF had purchased real property containing dilapidated greenhouses that it knew at the time of purchase contained asbestos and lead paint. (*Id.* at 50.) Despite having plans to modernize the greenhouses before leasing the property, it never did so. (*Id.* at 50.)

When LF presented the property to Epochal, it did not disclose the presence of asbestos or lead paint. (*Id.* at 50.) Epochal's position was that it did not believe it was required to make such a disclosure. (*Id.* at 50.) Epochal's principal had never even heard of asbestos. (*Id.* at 50-51.)

The lease was drafted by LF's attorney and it leased the real property to Epochal "as-is" for a period of five years. (*Id.* at 51.)

The lease contained the following limitation-of-liability clause:

> 10.6 Limitation of Liability: *Neither Landlord nor any affiliate of Landlord nor their respective members, principals, beneficiaries, partners, trustees, shareholders, directors, officers, employees, contractors or agents shall have any personal liability with respect to any of the provisions of the Lease or the Premises.* If Landlord is in breach or default with respect to Landlord's obligations under the Lease, Tenant shall look solely to the equity interest of Landlord in the Project for the satisfaction of Tenant's remedies or judgments. No other real, personal, or mixed property of any Landlord, wherever situated, shall be subject to levy to satisfy such judgment. Upon any transfer of Landlord's interest in this Lease or in the Project, the transferring Landlord shall have no liability or obligation for matters arising under this Lease from and after the date of such Transfer. *Landlord shall in no event be liable for any consequential damages or loss of business or profits and Tenant hereby waives any and all claims for any such damages.* (Italics added.) (*Id.* at 51-52.)

During the lease term, a storm damaged one of the greenhouses. (*Id.* at 52.) LF took it upon itself to hire an asbestos remediation company to do repairs, knowing that a pipe that had burst in the storm exposed asbestos. (*Id.* at 52.) Despite this knowledge, LF still did not inform Epochal about the asbestos. (*Id.* at 52.)

Thereafter, Epochal fell behind on rent payments, and LF filed an unlawful detainer action. (*Id.* at 52.) While the action was pending, Epochal learned for the first time that asbestos and lead paint were present. (*Id.* at 52-53.) Thereafter, Epochal sued LF for the damages caused by LF's

failure to disclose the asbestos and resulting damage to its orchids. (*Id.* at 53.)

The jury in Epochal's case returned a verdict in favor of Epochal, finding that LF engaged in premises liability and negligence. (*Id.* at 53.) Following trial, LF filed, and the trial court granted, a Motion for JNOV based upon the limitation-of-liability clause that did not allow for the damages that had been awarded to Epochal. (*Id.* at 53-54.)

Epochal appealed, and the Court of Appeal reversed, reasoning as follows:

- The Carpenter-Presley-Tanner Hazardous Substance Account Act (the Act; Health & Saf. Code, § 25300 et seq.) was enacted to "[e]stablish a program to provide for response authority for releases of hazardous substances, ... that pose a threat to the public health or the environment." (§ 25301.) Owners of non-residential property must disclose the presence of asbestos under the Act. Likewise, the Asbestos Notification Law (§ 25915 et seq.) sets forth a scheme for notifying employees, contractors and other persons providing services on a property of the presence of asbestos on that property. There is even a specific format to be used for the notification. "Any owner who knowingly or intentionally fails to comply with this chapter, or who knowingly or intentionally presents any false or misleading information to employees or any other owner, is guilty of

a misdemeanor punishable by a fine of up to one thousand dollars ($1,000) or up to one year in the county jail, or both." (§ 25919.7.) (*Id.* at 57-58.)

- "Negligence per se is a way to establish ordinary negligence by tying the standard of care to a specific 'statute, ordinance, or regulation of a public entity.' (Evid. Code, § 669, subd. (a)(1).)" And the parties were in agreement that the jury's findings of negligence were established via the doctrine of negligence per se (meaning a duty that formed its basis in a statute). (*Id.* at 58-59.)
- The negligence per se finding that was based upon violations of the Health and Safety Code disclosure requirements triggered Section 1668. (*Id*. at 60.)
- With these statutory requirements and findings in mind, the Court of Appeal provided:
    - Disclosure requirements are commonplace even for commercial transactions between sophisticated business entities, and all such laws reflect legislative judgments as to what information should be available for market participants to consider when negotiating or agreeing to a contract, even when one party 'could easily contract to secure that information' from the other party.' (*Beeman v. Anthem Prescription Management, LLC* (2013) 58 Cal.4th 329, 362, 165 Cal.Rptr.3d 800, 315 P.3d 71 (*Beeman*).) Disclosure statutes 'simply require disclosure of factual information in order to inform private or public decisionmaking in the economic or political marketplace. We may assume that the regulated entities would prefer not to make these disclosures, many of which run counter to their business interests. But the Legislature has determined that the information should be

made available in order to promote informed choice in the free market and in the development of sound public policy.' [Citations] (*Id.* at 61.)

- The trial court similarly misplaced its reliance on *CAZA Drilling (California), Inc. v. TEG Oil & Gas U.S.A., Inc.* (2006) 142 Cal.App.4th 453, 48 Cal.Rptr.3d 271, *Farnham v. Superior Court* (1997) 60 Cal.App.4th 69, 70 Cal.Rptr.2d 85, and *Peregrine Pharms., Inc. v. Clinical Supplies Mgmt.* (C.D. Cal. 2014) 2014 U.S. Dist. LEXIS 105756, 2014 WL 3791567 (*Peregrine*). *Caza* is distinguishable because appellants failed to identify a specific statutory or regulatory violation that led to their injury that would trigger the application of Civil Code section 1668. (*Caza*, at p. 476, 48 Cal.Rptr.3d 271.) Thus, no basis existed to invalidate the exculpatory provisions in the parties' contract. (*Ibid.*) In contrast here, plaintiff proved a violation of the Health and Safety Code. *Farnham* is distinguishable because the contract limited the liability of corporate directors for defamation arising out of their roles as directors while allowing the injured party to seek full redress from the corporation. (*Farnham*, at p. 77, 70 Cal.Rptr.2d 85.) (*Id.* at 62.)

2. NECF Incorrectly Argues That The "Root Cause" Of The Split Of Authority Is Courts' Reluctance To Apply Section 1668 To "Ordinary-Negligent" Violations Of Law

NECF contends that the Courts are split due to a reluctance to apply Section 1668 to ordinary-negligent violations of law. (OBM, pp. 46-49.) But this is not accurate. For example, the three cases that enforced the limitation-of-liability clauses do not fit this description: *Farnham* involved defamation, *CAZA* involved allegations of gross negligence, and *Food Safety* (like this case) involved allegations that purported to go beyond a

mere breach of contract or ordinary negligence despite emanating from a contractual provision:

> In asserting a claim for breach of contract, the FACC alleged that Food Safety had breached its contract with Eco Safe because the 'deeply flawed' study was 'not conducted as proposed' and 'provided unsupported conclusions.' Regarding the bad faith claim, the FACC alleged that Food Safety breached the implied covenant of good faith by employing 'slovenly procedures which seemed to be slanted towards a preconceived conclusion,' rather than 'modern day scientific and laboratory procedures.' Similarly, in connection with the negligence claim, the FACC alleged that Food Safety had 'failed to exercise due care in properly inoculating the [samples in] the last five tests as required under the [c]hallenge [s]tudy.' (*Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118, 1125.)

In the cases where the limitation-of-liability clauses were not enforced, the key characteristics involved some level of unconscionability or unfairness, such as unequal bargaining power or adhesion (*Health Net* and *Epochal*) or no privity of contract between the party seeking to enforce the clause and the parties suing (*Klein*); and blatant attempts to disclaim statutory or regulatory violations (*Health Net* and *Epochal*), or misrepresentations and express warranties (*Klein*).

If the *Food Safety-CAZA-Farnham* line of cases are not found to apply to the facts of this Appeal, then the clauses like the ones involved here will cease to have any meaning. Businesses will be forced to be exposed to one another for unlimited damages for virtually any alleged wrong (even those rooted in contract), despite their mutual *preference* to avoid such unlimited damages.

F. Section 1668's Application To Entities Versus Natural Persons

While VanLaw agrees that Section 1668 does not – on its face – distinguish between entities and natural persons in terms of providing protection under the statute, natural persons are more likely to be victims of contract provisions that have for their "object" to shield the other party from fraud, statutory violations, or willful injury to property or persons. This is best illustrated by traditional complete waivers contained in contracts of adhesion that are drafted by corporate attorneys and presented to the unsuspecting consumer. It is VanLaw's contention that Section 1668 was enacted in large part to protect those consumers and their property. It could not have been enacted to invalidate clauses like the one at issue in this case where two parties clearly intended to *limit* damages to one another, *including for either parties' breach of the reverse-engineering clause, even if said breach amounted to a tort*.

G. NECF Incorrectly Asserts That Section 1668 Does Not Distinguish Between Breach Of Contract And Tort

NECF appears (at pg. 52 of its OBM) to be asking the Supreme Court to *expand* Section 1668 to apply to all claims for breach of contract. So long as the party alleges that the other party "willfully violated" a contract (which is presumably an argument that can be made every time someone breaches a contract), Section 1668 should completely invalidate a limitation-of-liability clause, according to NECF. This is despite the fact

that the law treats breaches of contract differently than it treats torts (e.g., punitive and emotional distress damages are not available for a breach of contract). In effect, NECF is really asking the Supreme Court to apply Section 1668 to everything except for ordinary negligence and to apply it across the board any time a party to a limitation-of-liability clause finds itself in a position where it did not suffer the damages available to it under its fully-negotiated contract. The consequences of this approach would be unimaginable, and inconsistent with the plain meaning of Section 1668.

H. The Remaining Four Causes Of Action

A review of the FAC makes clear that every claim in this case arises exclusively out of (and cannot survive without) the Operating Agreement, including the NDA contained therein.

Nothing in the controlling cases distinguishes between an intentional breach of a contractual provision versus a negligent one. But worth noting is the fact that the allegations in *Food Safety* (all of which arose out of contractual provisions and would not have existed but for those contractual provisions) most definitely involved allegations of *intentional* acts, all of which were ultimately barred by the limitation of liability clause:

> In asserting a claim for breach of contract, the FACC alleged that Food Safety had breached its contract with Eco Safe because the 'deeply flawed' study was 'not conducted as proposed' and 'provided unsupported conclusions.' Regarding the bad faith claim, the FACC alleged that Food Safety breached the implied covenant of good faith by employing 'slovenly procedures which seemed to be slanted towards a preconceived conclusion,' rather than 'modern day

> scientific and laboratory procedures.' Similarly, in connection with the negligence claim, the FACC alleged that Food Safety had 'failed to exercise due care in properly inoculating the [samples in] the last five tests as required under the [c]hallenge [s]tudy.' *Food Safety Net Services v. Eco Safe Systems USA, Inc.* (2012) 209 Cal.App.4th 1118, 1125.)

The tort claims in the present Appeal constitute nothing more than an attempt to obtain tort recovery on an express contractual provision. Thus, the tort claims stand and fall with the contract claims, and are most definitely encompassed by the limitation-of-liability clauses. But, even if (*arguendo*) the tort claims could exist without the breach of contract claim, the clauses would still bar the action because parties can *limit* damages to one another so long as the clause does not "exempt" a party from the conduct described in Section 1668.

CONCLUSION

VanLaw contends that the Supreme Court can (and should) continue to allow Section 1668 to be applied on a case-by-case basis, and provide guidance that reconciles the various cases that are relevant to the certified question.

Dated: April 15, 2024

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CERTIFICATE OF WORD COUNT

I am the attorney for Respondent VANLAW FOOD PRODUCTS, INC. This brief contains 12,271 words, excluding items exempted by Cal. Rule of Court 8.520(c)(3).

I certify that the foregoing is true and correct.

Dated: April 15, 2024

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Supreme Court of California

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