No. S256927

IN THE SUPREME COURT OF CALIFORNIA

IXCHEL PHARMA, LLC,
Plaintiff and Appellant,

v.

BIOGEN, INC.
Defendant and Respondent.

On Certified Questions From The United States Court Of Appeals For The Ninth Circuit, Case No. 18-15258
Judge William B. Shubb, Case No. 2:17-CV-00715-WBS-EFB

ANSWER BRIEF ON THE MERITS

ROPES & GRAY LLP
Mark S. Popofsky, SBN 175476
Mark.Popofsky@ropesgray.com
2099 Pennsylvania Avenue, NW
Washington, DC 20006
Telephone: (202) 508-4624

ROPES & GRAY LLP
Rocky Chiu-Feng Tsai, SBN 221452
Rocky.Tsai@ropesgray.com
Three Embarcadero Center
San Francisco, California 94111
Telephone: (415) 315-6358

GREINES, MARTIN, STEIN & RICHLAND LLP
*Laurie J. Hepler, SBN 160884
lhepler@gmsr.com
50 California Street, Suite 1500
San Francisco, CA 94111
Telephone: (415) 315-1774

Attorneys for Respondent Biogen, Inc.

No. S256927

IN THE SUPREME COURT OF CALIFORNIA

IXCHEL PHARMA, LLC,
Plaintiff and Appellant,

v.

BIOGEN, INC.
Defendant and Respondent.

On Certified Questions From The United States Court Of Appeals For The Ninth Circuit, Case No. 18-15258
Judge William B. Shubb, Case No. 2:17-CV-00715-WBS-EFB

ANSWER BRIEF ON THE MERITS

ROPES & GRAY LLP
Mark S. Popofsky, SBN 175476
Mark.Popofsky@ropesgray.com
2099 Pennsylvania Avenue, NW
Washington, DC 20006
Telephone: (202) 508-4624

ROPES & GRAY LLP
Rocky Chiu-Feng Tsai, SBN 221452
Rocky.Tsai@ropesgray.com
Three Embarcadero Center
San Francisco, California 94111
Telephone: (415) 315-6358

GREINES, MARTIN, STEIN & RICHLAND LLP
*Laurie J. Hepler, SBN 160884
lhepler@gmsr.com
50 California Street, Suite 1500
San Francisco, CA 94111
Telephone: (415) 315-1774

Attorneys for Respondent Biogen, Inc.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

PAGE

State Cases

Federal Cases

Non-California Cases

Federal Statutes

State Statutes

State Rules

Other Authorities

ISSUES PRESENTED

The Ninth Circuit certified and this Court accepted these questions:

> Is a plaintiff required to plead an independently wrongful act in order to state a claim for intentional interference with a contract that can be terminated by a party at any time, or does that requirement apply only to at-will employment contracts?
>
> Does section 16600 of the California Business and Professions Code void a contract by which a business is restrained from engaging in a lawful trade or business with another business?

As explained in Biogen's August 2, 2019 letter response to the certification order, and pursuant to California Rule of Court 8.516, this Court should address the following fairly-included issues:

> Does a claim for intentional interference with contract under California law require pleading an independently wrongful act when the defendant, in seeking a relationship with a third party, induces that third party to terminate its at-will contract with the plaintiff?
>
> Does California Business & Professions Code section 16600 apply the antitrust rule of reason in assessing whether a restraint imposed by one business on the trade or business of another is void?

This Court has issued no order limiting the briefing. (See Cal. Rules of Court, rule 8.520 (b).)

INTRODUCTION

Section 16600 seemingly voids every "restrain[t]" on "engaging" in a "business." But just as the rule of reason governs similarly-sweeping antitrust statutes, because "[e]very agreement concerning trade ... restrains" (*Chicago Board of Trade v. United States* (1918) 246 U.S. 231, 238; *In re Cipro Cases I & II* (2015) 61 Cal.4th 116, 146), so too section 16600 applies the rule of reason to numerous commercial collaborations, including here.

Defendant/Respondent Biogen, Inc. settled intellectual property ("IP") disputes with Forward Pharma FA Aps. The agreement aimed to remove the clouds cast by Forward's IP rights over Biogen's Tecfidera product, which Forward Pharma alleged infringed its IP. Pursuant to an ongoing Patent Settlement and License Agreement ("Patent License"), Biogen paid Forward over $1 billion to settle the IP disputes and license Forward's IP that relates to Tecfidera's active ingredient, dimethyl fumarate ("DMF").

To protect those rights, section 2.13 of the Patent License imposed a limited restriction: one barring Forward from contracting with *third parties* to develop DMF drugs. Forward retained the right to market *self*-developed DMF drugs. In accordance with section 2.13, Forward terminated its at-will Collaboration Agreement with Plaintiff/Petitioner Ixchel Pharma

LLC. That terminated agreement called for developing DMF-related IP rights, confirming section 2.13's legitimate purpose: Why would Biogen pay over $1 billion to license Forward's IP, if Forward could undermine that license by working with others to place new patent clouds over Tecfidera?

Section 2.13 thereby protected Biogen's use of the very rights Biogen licensed. The provision also marked Forward's exercise of its long-held option, spelled out in Forward's at-will contract with Ixchel, to switch commercial partners. So Ixchel did not sue Forward. Ixchel, instead, sued Biogen for alleged tortious interference with its at-will contract. The federal district court granted Biogen's motion to dismiss.

Ixchel's appeal to the Ninth Circuit has brought two issues to this Court. First, whether a claim for intentional interference with contract requires pleading an independently wrongful act when the defendant induces a new business partner to terminate an at-will contract with the plaintiff. Second, how Business and Professions Code section 16600—Ixchel's last remaining ground for asserting wrongful means—applies to a restraint placed on business operations.[1]

At stake here is nothing less than the preservation of competition in California.

On the first issue: When parties choose to make their contract contestable (at-will), the law should support and enforce that choice. Policies promoting commerce favor protecting

[1] Unlabeled statutory references are to this code.

outsiders' ability to offer either party the opportunity to forge new relationships, absent wrongful conduct. Otherwise, competing for customers or suppliers in at-will contracts will risk interference claims, and firms (like Forward here) will think twice before signing even at-will contracts, for fear of limiting future options. Protecting the ability to vie for relationships is precisely why this Court required wrongful means for interference with prospective economic advantage in *Della Penna v. Toyota Motor Sales, U.S.A., Inc.* (1995) 11 Cal.4th 376, and is the key reason why this Court required wrongful means for intentional interference with contract in *Reeves v. Hanlon* (2004) 33 Cal.4th 1140 (*Reeves*), where one employer recruited at-will employees from another.

The same rationale warrants requiring wrongful means here. Biogen convinced Forward to partner with Biogen instead of continuing its at-will contract with Ixchel, and Forward exercised its bargained-for termination opportunity. The policy of promoting outsiders' ability to offer better terms to parties in at-will contracts is not, as Ixchel contends, confined to the *Reeves* employment setting. Adopting Ixchel's position—that intentional interference with contract *never* requires wrongful means outside *Reeves'* setting—would largely outlaw competition.

Countervailing policies require no such commerce-chilling outcome. The wrongful means element sufficiently protects society's modest interest in the stability of at-will contracts. Ixchel relies on two distinguishable appellate decisions that involved firms acting *with* wrongful means to sabotage relationships, not (as here) to forge new ones. Addressing these and other inapposite settings should await another case. The Court can require wrongful means for Ixchel's claims without deciding whether "all" claims of intentional interference with an at-will contract require that element. (OB pp. 6-7.)

As to the second issue: Biogen does not contest that section 16600 can govern restraints on businesses. Biogen and Ixchel instead dispute *how* to apply section 16600. Section 16600's text, evolution, and legislature-ratified judicial construction all confirm that the appropriate standard is the rule of reason—the same test enshrined in the Cartwright Act.

Application of section 16600 has proceeded on two tracks, an approach this Court should continue. Section 16600's *per se* track voids, absent statutory exception: (i) naked non-competes and (ii) restraints incident to a *separation*, such as the post-employment non-compete voided in *Edwards v. Arthur Andersen LLP* (2008) 44 Cal.4th 937 (*Edwards*). By contrast, section 16600 applies the antitrust rule of reason to other restraints, including restraints that induce or support *business collaborations*. This Court recently summarized the rule of reason as an inquiry into "whether an agreement harms competition more than it helps." (*In re Cipro Cases I & II* (2015) 61 Cal.4th 116, 146 (*Cipro*), superseded on other grounds by Health & Saf. Code, § 134002, subd. (a)(1).) Because section 2.13 is neither a naked non-compete agreement nor a restraint incident to a separation, section 16600's rule of reason governs.

Clarifying how section 16600 applies to a restraint one business places on another is critical to California. After all, "[*e*]*very* agreement concerning trade ... restrains." (*Cipro*, 61 Cal.4th at p. 146, emphasis in *Cipro*, internal quotations omitted.) Ixchel misreads section 16600 to void *every* contract between businesses that imposes *any* nontrivial restraint on a counterparty. This approach would nullify the Cartwright Act and inhibit routine and procompetitive contracts—whether exclusive dealing, franchises, or patent licenses.

Section 16600 requires no such upheaval. "'Statutes are interpreted in the light of reason and common sense.'" (*Great Western Distillery Products, Inc. v. John A. Wathen Distillery Co.* (1937) 10 Cal.2d 442, 446 [upholding a business-to-business restraint under section 16600's predecessor by applying the rule of reason].) The common-sense application of section 16600 here accords with the Cartwright Act, comports with *Edwards*, and avoids commercial disorder. It also resolves this case. Ixchel alleged no rule of reason violation, and therefore no violation of section 16600.

STATEMENT OF FACTS AND PROCEEDINGS BELOW

The district court dismissed Ixchel's complaints on motions under Federal Rule of Civil Procedure 12(b)(6). Courts "accept as true all facts alleged in the complaint and draw all reasonable inferences in favor of the plaintiff" but disregard "conclusory allegations in [Ixchel's] complaint or legal claims asserted in the form of factual allegations." (*In re Tracht Gut, LLC* (9th Cir. 2016) 836 F.3d 1146, 1150; *Evans v. City of Berkeley* (2006)

38 Cal.4th 1, 6 [same on review of demurrer dismissal].) Courts also can consider documents incorporated by reference in the complaint or matters of judicial notice. (*U.S. v. Ritchie* (9th Cir. 2003) 342 F.3d 903, 908; *Dreiling v. American Exp. Co.* (9th Cir. 2006) 458 F.3d 942, 946, fn. 2; *Evans*, 38 Cal.4th at pp. 6, 20 [dismissal affirmed where "noticeable and conceded facts contradict[ed] the complaint's assertions"].) The district court properly considered the Ixchel/Forward Collaboration Agreement and the Biogen/Forward Patent License because Ixchel's complaints extensively referenced and were based upon them. (ER 14-15, fns. 1, 3.)[2]

A. Forward's At-Will Agreement with Ixchel

In January 2016, Forward and Ixchel inked a Collaboration Agreement to develop a potential DMF-based drug for Friedreich's ataxia. (ER 94-96.) Forward assumed *all* commercial risk. If Forward decided that it could conduct feasible and cost-effective clinical trials, and trials proceeded, Forward had the obligation to pay for them. (SER 34-35, §§ 4.1-4.4.) If trials succeeded, Forward controlled "in its sole discretion" the right to apply for FDA approval, bearing responsibility for regulatory compliance. (SER 34-35, §§ 4.3-4.4.) If approval resulted in a commercially viable drug, Forward "[a]t

[2] The Biogen/Forward Patent License is publicly available at <https://www.sec.gov/Archives/edgar/data/1604924/000110465917002473/a17-2604_1ex99d2.htm>, as of December 6, 2019. The district court took judicial notice of this agreement (ER 15, fn. 3), as Biogen separately asks this Court to do.

its own expense" would "be solely responsible for, and shall control all decisions related to, the development, manufacturing and Commercialization." (SER 35, § 4.6.) Ixchel, by contrast, committed certain IP rights that would revert upon a termination like the one here (SER 33, § 3.2; SER 51, § 12.7.2), and agreed to "cooperate with and provide reasonable assistance to Forward" as requested (SER 34, § 4.1; ER 96, ¶ 32). Forward would pay Ixchel a royalty on any successful products. (ER 96, ¶ 33.)

The Collaboration Agreement gave Forward an unconditional right to terminate at any time. (SER 50, § 12.4.) The terms described above suggest the reason. Ixchel did not allege that Forward had ever commercialized any drug. (See ER 93, ¶ 15.) No rational firm in Forward's position would lock itself into funding and implementing a costly, risky, and multi-year undertaking if it could instead bargain for the right to change course for any reason.

Ixchel averred that a hypothetical Friedreich's ataxia drug might threaten Biogen if physicians prescribed it "off-label" for multiple sclerosis, the disease Tecfidera treats. (ER 94, ¶ 23; OB p. 11.) Ixchel did not disclose that promoting a drug for off-label use can be deemed a criminal offense. (21 U.S.C. § 352(a), (f).)

B. Biogen's Patent License with Forward

A year after signing the Collaboration Agreement, Forward resolved certain IP disputes with Biogen by licensing its DMF-related IP to Biogen. (ER 98-99, ¶ 43.)

To achieve this, the Patent License granted Biogen three categories of rights: (i) rights relating to certain patent assertions that Forward withdrew[3]; (ii) rights contingent on Forward attaining favorable litigation outcomes (FER 9-13, §§ 4.02-4.03); and (iii) licenses to all other Forward IP rights "related to the treatment of any human disease or condition using [DMF]" and to Forward's experimental FP-187 product (SER 14-15). Biogen obtained a co-exclusive license with Forward in the U.S. and exclusive licenses elsewhere. (ER 77-78, §§ 3.01-3.03; SER 18, § 3.03.) For all of these rights, Biogen paid Forward $1.25 billion. (ER 98, ¶ 43.)

The Patent License contains provisions designed to prevent Forward from undermining the license it granted. (See, e.g., SER 16, §§ 2.02-2.03 [restrictions on encumbrances and contesting validity].) This case concerns one such provision, section 2.13.

In that provision, Forward agreed not to continue or enter into any new contracts "related to the development" of DMF products. (ER 99, ¶ 45.) Section 2.13 prohibits *development agreements with others*. It does not bar Forward from competing via *self-developed* DMF products to treat any disease. Nor does it bar Forward from making contracts to support self-development; on the contrary, section 3.01 of the Patent License authorizes Forward to enter into contracts to "'manufacture or import products and to perform wholesale and distribution services'"

[3] For example, in section 2.01, Forward agreed to terminate proceedings concerning certain European patents. (See *ante*, fn. 2.)

under a co-exclusive license. (ER 8; ER 77-78, § 3.01.) Based on this plain language, the district court saw that "§ 2.13 clearly does not prevent Forward from developing and selling any pharmaceutical products containing DMF" and "cannot be classified as a 'non-compete covenant.'" (ER 8.)[4]

Section 2.13, as the court also recognized, is "subordinate" to the Patent License's "larger, lawful" purpose (ER 8) of enabling Biogen "to continue selling its Tecfidera product ... without fear of infringing on Forward's [purported] intellectual property rights" (ER 99, ¶ 43 [Ixchel's allegation]). The Ixchel/Forward agreement contemplated development of DMF-related intellectual property rights "jointly by the Parties." (SER 25, § 1.6; SER 31, § 1.62.) These were among the IP rights Biogen licensed, and the Collaboration Agreement's "Field" included multiple sclerosis, the disease Tecfidera treats. (SER 27, § 1.27.) If Forward could work with third parties in relationships excluding Biogen to develop IP rights implicating Tecfidera, those agreements would recreate the very "fear of [Tecfidera] infringing" that the larger, lawful deal was designed to remove. (ER 99, ¶ 43.)

The Patent License bound Forward and Biogen in an ongoing relationship. It created a joint IP Advisory Committee to

[4] Ixchel alleged that section 2.13 "effectively prevents" Forward from "engaging in its entire business." (ER 99-100, ¶¶ 50, 52; OB p. 12.) Ixchel still relies on this incorrect legal conclusion, arguing that section 2.13 prohibits "any" contracts "with respect to [the DMF] field." (OB p. 12.) But section 2.13 restricts "development" contracts, not "any" contracts. (ER 77.)

formulate "strategy and actions with respect to the filing, maintenance, prosecution and defense of the" licensed IP in regular meetings, and created ongoing rights and obligations relating to these issues. (Patent License, §§ 5.02-5.04; see fn. 2, *ante.*) Forward committed to keep itself extant and solvent, and the parties secured audit rights. (SER 17, § 2.04(a); see also Patent License, §§ 2.08-2.09, 4.07.) The Patent License contemplated potential royalties through the last expiring applicable IP rights (FER 9-13, §§ 4.02-4.03), and provided Biogen conversion and purchase options (SER 18-20, §§ 3.06-3.07).

Section 2.13's scope comports with the parties' obligations. The licenses granted are worldwide and perpetual (ER 77-78, §§ 3.01-3.02; SER 18, § 3.03), subject to replacement by Biogen's purchase of the IP. Certain provisions continue indefinitely, protecting, among other things, the IP rights Biogen licensed from Forward both during the license periods and after any Biogen purchase of the licensed IP. (E.g., Patent License, §§ 2.01-2.02, 2.03(iv), 2.04(b), 2.06, 2.07, 2.14, 8.02.) Section 2.13, too, is worldwide and, as with these other protective obligations, specifies no duration. (ER 100, ¶ 51.)[5] Just as Biogen licensed

---

[5] Under either California law or New York law (which governs the Patent License's construction, ER 101, ¶ 60), section 2.13's obligations conclude when the last IP rights protected by that provision expire, an "ascertainable event" that "necessarily implies termination." (*Lura v. Multaplex, Inc.* (1982) 129 Cal.App.3d 410, 414-415; see also *Haines v. City of New York* (N.Y. 1977) 364 N.E.2d 820, 822-823 [explaining that "the law

rights from Denmark-based Forward outside the U.S. (ER 74; SER 18, § 3.03), section 2.13 applies to Forward's foreign affiliate (ER 87).

C. Ixchel's Claims and the District Court's Dismissals

Shortly after executing the Patent License in January 2017, Forward notified Ixchel that it was terminating the Collaboration Agreement, and ceased working with Ixchel. (ER 101-102, ¶¶ 62, 63.) Ixchel did not sue Forward. Ixchel instead sued Biogen for (i) violations of the Sherman Act and Cartwright Act; (ii) intentional interference with contract and intentional and negligent interference with prospective economic advantage; and (iii) violations of California's Unfair Competition Law ("UCL"), section 17200. (ER 104-109, 119-123.)

The district court twice dismissed Ixchel's claims; only the interference claims and a derivative UCL "unlawful" claim remain. (See *Ixchel Pharma, LLC v. Biogen, Inc.* (9th Cir. 2019) 930 F.3d 1031, 1034-1036 (*Ixchel*).) As for intentional interference with contract, the court required Ixchel to plead wrongful means because "interference with an at-will contract has been viewed as functionally equivalent to interference with a prospective economic advantage, which does require a pleading of wrongful means." (ER 20, citing *Reeves, supra*, 33 Cal.4th at p. 1152; ER 5, fn. 2.)

---

will not imply" a "perpetual" contract and instead inferring termination of obligation when "no longer needed"].)

The district court rejected Ixchel's grounds for asserting wrongful means. First, in unappealed rulings, the court found no allegations that Biogen induced Forward to breach its agreement with Ixchel. (ER 5-6, 22.)[6] Second, the court rejected Ixchel's assertion that section 2.13 violated section 16600. (ER 7-11.) Characterizing section 2.13 as "ancillary" to the "larger, lawful" Patent License, the court ruled that "court[s] would analyze [section 2.13's] legality under the antitrust law's Rule of Reason and not the narrower rule of per se illegality [that] § 16600 applies to non-compete agreements in employment contracts." (ER 8-9.) Applying the rule of reason, the court held that Ixchel failed to allege the required "harm to competition." (ER 10-11.)

D. The Parties' Arguments to the Ninth Circuit and Ensuing Certification

Ixchel appealed to the Ninth Circuit. Ixchel argued that establishing intentional interference with an at-will, non-employment contract never requires wrongful means. Biogen countered that Ixchel's position would outlaw competition. Biogen contended that the rationale underlying *Reeves* compelled a wrongful-means requirement here, where Biogen induced Forward to partner with Biogen rather than Ixchel.

---

[6] The court rejected Ixchel's contention (ER 102, ¶ 62; OB pp. 10, 13) that Forward breached a supposed post-termination obligation to conduct clinical trials. The agreement's survival clause omits the asserted obligation. (SER 52, § 12.7.6.) Ixchel also failed to plead that Biogen induced Forward to breach the agreement's notice provisions. (Compare ER 5-6 with OB p. 13.)

As for section 16600, Ixchel argued that *Edwards'* per se rejection of post-termination employee non-compete provisions meant that section 16600 equally voided *all* restraints placed on a business. Biogen responded that Ixchel's one-size-fits-all approach would chill commerce by foreclosing numerous ordinary contracts. Biogen argued that the rule of reason governs section 16600's application to section 2.13. Biogen did *not* assert that section 16600 applies only in the employment context. (Contra *Ixchel*, *supra*, 930 F.3d at p. 1036.)

Against this backdrop, the Ninth Circuit certified the questions that this Court agreed to consider. The Ninth Circuit stressed that its "phrasing of the questions should not restrict the Court's consideration of the issues involved" and welcomed this Court to "rephrase the questions as it sees fit in order to address the contentions of the parties." (*Id.* at p. 1033.)

ARGUMENT

I. INDUCING A NEW BUSINESS PARTNER TO TERMINATE AN AT-WILL CONTRACT IS NOT INTENTIONAL INTERFERENCE, ABSENT WRONGFUL MEANS

A. This Court Should Resolve the Narrower Fairly-Included Question

The first issue presented is narrow but important: Can inducing a new business partner to terminate an at-will contract amount to intentional interference with contract, absent allegations that the defendant engaged in an independently wrongful act ("wrongful means")? "[A]n act is independently wrongful if it is unlawful, that is, if it is proscribed by some constitutional, statutory, regulatory, common law, or other determinable legal standard." (*Korea Supply Co. v. Lockheed Martin Corp.* (2003) 29 Cal.4th 1134, 1159.)

Ixchel asks this Court to decide the broader question of whether claims for interference with "all at-will contracts" require wrongful means. (OB pp. 7, 29-31.) The evolution of the economic interference torts—"interference with contract and its sibling, interference with prospective economic relations" (*Della Penna v. Toyota Motor Sales, U.S.A., Inc.* (1995) 11 Cal.4th 376, 381 (*Della Penna*))—would, as shown below, support an affirmative answer.

But the Court need not go that far. Deciding the narrower question this case poses, fairly included within the question certified, suffices to protect competition and to reject Ixchel's claims. This case does not involve, for instance, procuring a contractual breach, disrupting performance, or inducing termination without forming a new relationship. Just as in *Reeves* and its forebears, this Court can leave other issues for cases requiring their resolution. (33 Cal.4th at p. 1153, fn. 7; *Pacific Gas & Electric Co. v. Bear Stearns & Co.* (1990) 50 Cal.3d 1118, 1128, fn. 4 (*PG&E*); *Della Penna*, 11 Cal.4th 376, 378, 392-393.)

B. Policies Promoting Commerce Warrant Requiring Wrongful Means for Intentional Interference Claims Based on Inducing a New Partner to Terminate an At-Will Contract

1. This Court Protects Contestability Over Stability When Partners Lack Assurance of Future Relations

This Court's elaboration of California's economic interference torts balances two interests. One is in "stable economic relationships"—an interest protected by both interference with contract and interference with prospective economic relations. (*PG&E, supra,* 50 Cal.3d at p. 1126; *Reeves, supra,* 33 Cal.4th at p. 1151.) The second, more vital interest is in promoting commerce in a "freely competitive economy"; this Court has long warned of "the dangers inherent in imposing tort liability for competitive business practices." (*PG&E*, 50 Cal.3d at pp. 1136–1137; see also *Della Penna, supra,* 11 Cal.4th at p. 390.)

These "dangers" are self-evident. If seeking new commercial partners always risked tort liability, competition would suffocate. The Court accordingly has resisted expanding the reach of the interference torts, and has progressed steadily toward protecting freedom of competition for economic relationships that are speculative or otherwise unprotected by definite-term contracts.

PG&E. Nearly 30 years ago, this Court considered both interference torts. (50 Cal.3d at p. 1126 & fn 2.[7]) *PG&E* concerned whether inducing potentially meritorious litigation could comprise interference with an at-will contract. It concluded that, although interference with an at-will contract can be actionable, neither tort extended to inducing another to undertake colorable litigation, absent an allegation of malicious prosecution. (*Id.* at p. 1137.) Although the Court noted that many cases and leading authorities "have treated claims of interference with voidable and terminable contracts as coming within the cause of action for interference with prospective

---

[7] *PG&E* stated the following elements for intentional interference with contract: (1) a valid contract; (2) defendant's knowledge of this contract; (3) defendant's intentional acts designed to induce breach or disruption of the contractual relationship; (4) actual breach or disruption; and (5) resulting damage. (50 Cal.3d at p. 1126.) Intentional interference with prospective economic advantage required essentially the same elements, but in lieu of a contract required "'an economic relationship between the plaintiff and some third party, with the probability of future economic benefit.'" (*Id.* at p. 1126, fn 2.) The Court, at the time of *PG&E*, had not addressed whether either tort required wrongful means.

advantage," it concluded that it "need not resolve that point here, in view of our conclusion that the activity complained of is not included within either tort." (*Id.* at p. 1128, fn. 4.)

Della Penna. In 1995, the Court undertook an in-depth analysis of the origins and development of the interference torts. *Della Penna* adopted the wrongful means element for interference with prospective economic relations, in light of "a doctrinal evolution" in the California appellate courts and nationally. (11 Cal.4th at pp. 378, 392.) Interference with prospective economic relations had previously required pleading the defendant's *subjective* intent to interfere with a relationship, leaving all considerations of legitimacy for the defense of justification. (*Buckaloo v. Johnson* (1975) 14 Cal.3d 815, 827-828.) The ease of establishing a *prima facie* case, critics observed, invited "time consuming and expensive" meritless actions "based on conduct that was regarded by the commercial world as both commonplace and appropriate." (*Della Penna*, 11 Cal.4th at p. 384.)

Agreeing with these critiques, *Della Penna* "recast" the tort to require that defendant's interference was *objectively* "wrongful by some measure beyond the fact of the interference itself." (*Id.* at pp. 392-393, internal quotations omitted.) This Court adopted the "wrongful means" requirement for interference with prospective economic relations to protect commerce when parties have only the expectation of forming a contract. The "social rewards of commercial contests," the Court explained, required the law to "draw lines of legal liability in a way that maximizes areas of competition free of legal penalties." (*Id.* at p. 392.) Further refinements to the wrongful means requirement, however, the Court left for "another day and a more appropriate case." (*Id.* at pp. 378, 393.)

Reeves. The Court took the next step in *Reeves*, requiring wrongful means to establish a claim for intentional interference by inducing termination of an existing, but at-will, employment contract. (33 Cal.4th at pp. 1144-1145.)

Reeves reasoned that the policy of promoting contractual stability is diminished when an outsider seeks to terminate an at-will contract. "[T]he economic relationship between parties to contracts that are terminable at will," this Court explained, "is distinguishable from" other binding contracts. (33 Cal.4th at p. 1151.) "[I]f a party to a contract" is "free to terminate," then inducing a party to take advantage of that right is "'primarily an interference with the future relation between the parties,'" to which the plaintiff "'has no legal assurance.'" (*Id.*, quoting Rest.2d Torts, § 768, com. i.) Equating the interest of a party in the continuation of an at-will relationship with that of a party seeking to form one (as in *Della Penna*), this Court reasoned that "an interference with an at-will contract *properly is viewed* as an interference with a prospective economic advantage." (*Id.* at p. 1152, relying on same; emphasis added.)

Echoing *Della Penna*, *Reeves* also recognized how the wrongful means element promotes commerce. Invoking the Second Restatement again, *Reeves* explained that a non-party is free to "'obtain the future benefits for himself by causing ...

termination'" of an at-will contract, including by "'offer[ing] better contract terms'" or "'mak[ing] use of persuasion or other suitable means, all without liability.'" (*Reeves, supra,* 33 Cal.4th at p. 1152, quoting Rest.2d Torts, § 768, com. i.) *Reeves* also cited the importance of promoting employee mobility. But the Court viewed enabling employees to benefit from third-party offers as a specific application of the more general principle "that certain competitive conduct is nonactionable when it interferes with the at-will contract relationships of another." (33 Cal.4th at pp. 1149, 1151.)

In short, the Court drew the wrongful means line to protect this zone of "competitive conduct" that is "nonactionable," "[c]onsistent with the decisions recognizing that an intentional interference with an at-will contract may be actionable, but mindful that an interference as such is primarily an interference with the future relation between the contracting parties." (*Id.* at pp. 1149, 1152.)

2. The Same Policies Warrant Requiring Wrongful Means for Inducing a New Partner to Invoke Termination Rights

This Court should take the next step and hold that the policies underlying *Reeves* and *Della Penna* warrant requiring plaintiffs to plead and prove wrongful means to establish intentional interference with contract when the defendant induces a new partner to terminate an at-will agreement.

The central policy underlying *Reeves*—enabling parties to an at-will contract to receive superior terms from outsiders—is not confined to employment agreements. Businesses need freedom to seek new partners, not just new employees. To the extent that potential new partners—whether suppliers, licensors, or customers—are parties to at-will contracts, they bargained for the freedom to negotiate replacement relationships. All of them, not just employees, benefit from new proposals. Just as in the employment setting, these vital commerce-promoting policies outweigh any interest in protecting parties in at-will contracts from outsiders' inducements to terminate.

Moreover, an interference with any "at-will contract," not just an employment contract, "properly is viewed as an interference with a prospective economic advantage." (*Reeves, supra*, 33 Cal.4th at p. 1152.) At-will contracts inherently leave the parties' future unsecured. Like the prospective economic relationships addressed in *Della Penna*, they "subsist in a zone where the rewards and risks of competition are dominant." (11 Cal.4th at p. 392.) The Restatement that *Reeves* invoked accordingly does not confine the wrongful means element to inducing termination of employment contracts. (See Rest.2d Torts, § 768, coms. c, i.)

The wrongful means requirement, whether in or outside the employment context, "strike[s] the proper balance" between promoting commerce—by permitting parties to vie for relationships that by design are contestable (at-will)—and protecting contracts against disruption by "unlawful methods."

(*Reeves*, *supra*, 33 Cal.4th at p. 1154.) Permitting outsiders to "offer better contract terms" or "make use of persuasion or *other suitable means*" (*id.* at p. 1152, emphasis added, internal quotations omitted) "draw[s] lines of legal liability in a way that maximizes areas of competition free of legal penalties" (*Della Penna*, *supra*, 11 Cal.4th at p. 392). The "wrongful means" line provides "a clearer guide to competitors in the conduct of their business affairs" than asserting privileges in defense to a claim established by subjective intent to interfere. (*San Francisco Design Center Assoc. v. Portman Companies* (1995) 41 Cal.App.4th 29, 43.)

To rule otherwise would mark a retreat from the principles underlying *Reeves* and *Della Penna*, hindering competition to the detriment of Californians. Suitors would hesitate before competing for suppliers, customers, or other business partners in at-will contracts with others, deterred by the risk of intentional interference suits. Firms such as Forward would think twice before entering into long-term contracts *even with at-will provisions*, for fear of constraining their future opportunities. A rule that enables firms to exercise bargained-for termination rights only *absent* inducement from others would fail to "maximize[] areas of competition free of legal penalties." (*Della Penna*, *supra*, 11 Cal.4th at p. 392.)

The great weight of authority nationwide is in accord.

- Citing the Restatement section that *Reeves* invoked, numerous states require wrongful means (or a similarly-formulated element) to sustain challenges to inducing termination of at-will contracts as intentional interference, both in and outside the employment setting.[8] As one court observed: "The plain language of the Restatement shows that the actor does not interfere improperly in the relation if, at the time he intentionally causes the third person not to continue an existing contract terminable at will, the actor does not employ wrongful means." (*Computers Unlimited, Inc. v. Midwest Data Systems, Inc.* (Ind.Ct.App. 1995) 657 N.E.2d 165, 170.)

---

[8] (See, e.g., *Fred Siegel Co., L.P.A. v. Arter & Hadden*(Ohio 1999) 707 N.E.2d 853, 861 [inducing clients to switch]; *ASDI, Inc. v. Beard Research, Inc.* (Del. 2010) 11 A.3d 749, 751 [similar]; *Prudential Ins. Co. of America v. Van Matre* (Ill.App.Ct. 1987) 511 N.E.2d 740, 744–745 [similar]; *Polk and Sullivan, Inc. v. United Cities Gas Co.* (Tenn. 1989) 783 S.W.2d 538, 543 [similar]; *Memorial Gardens, Inc. v. Olympian Sales & Management Consultants, Inc.* (Colo. 1984) 690 P.2d 207, 211 [similar]; *Nostrame v. Santiago* (N.J. 2013) 61 A.3d 893, 901-902 [similar; successor attorney]; *Macklin v. Robert Logan Associates* (Md. 1994) 639 A.2d 112, 118–119, 121 [rival tenant caused landlord to terminate lease]; *Feldman v. Green* (Mich.Ct.App. 1984) 360 N.W.2d 881, 890-891 [rival induced termination and breach of purchase option agreement]; *National Employment Service Corp. v. Olsen Staffing Service, Inc.* (N.H. 2000) 761 A.2d 401, 406 [inducing employee termination]; *Liebe v. City Finance Co.* (Wis. 1980) 295 N.W.2d 16, 18-19 [same]); *Tom's Foods, Inc. v. Carn* (Ala. 2004) 896 So.2d 443, 453-454, 458-459 [defendant interfered with service contract by repossessing property].)

- Additional state courts have reached that same result without citing the Restatement.[9]
- Other authorities require "improper" conduct or motive, beyond intent to interfere, to establish the tort.[10]

Consensus to require wrongful means for inducing termination of at-will contracts is sufficiently settled that the approved draft *Restatement (Third) of Torts: Liability for Economic Harm* ratifies *Reeves*' chief insight: that "an interference with an at-will contract properly is viewed as an interference with a prospective economic advantage." (33 Cal.4th at p. 1152; see Toboulidis, *Restatement of the Law Third, Torts: Liability for Economic Harm Approved* (May 21, 2018, The ALI Adviser.[11]) The new Restatement classifies intentional

---

[9] (See, e.g., *J.N.R. Enterprises, Inc. v. Frigidaire Co.* (Minn.Ct.App., June 1, 1999, No. C5-98-2281) 1999 WL 377747, at *3-4 [rival induced supplier to cancel distribution agreement]; *Lawrence-Picaso, Inc. v. Cosme* (N.Y.App.Div. 1996) 644 N.Y.S.2d 622 (Mem) [similar]; *Duggin v. Adams* (Va. 1987) 360 S.E.2d 832, 836 [similar; land sale contract]; *Bee v. West Virginia Supreme Court of Appeals* (W.Va., Nov. 8, 2013, No. 12-1111) 2013 WL 5967045, at *4, fn. 5 [employee termination].)

[10] (See, e.g., *Safeway Ins. Co. v. Guerrero* (Ariz. 2005) 106 P.3d 1020, 1025 [interference with insurance company's relationship with insured]; *Birkenwald Distributing Co. v. Heublein, Inc.* (Wash.Ct.App. 1989) 776 P.2d 721, 726 [distribution contract]; *Kinzel v. Discovery Drilling, Inc.* (Alaska 2004) 93 P.3d 427, 443 [employment termination].)

[11] Available at <http://www.thealiadviser.org/economic-harm-torts/the-american-law-institute-membership-approves-restatement-of-the-law-third-torts-liability-for-economic-harm/>, as of Dec. 8, 2019.

interference with *any* at-will contract as interference with prospective economic expectation, and requires wrongful means for inducing termination of any at-will contract, including where "the defendant convinces another party to terminate a contract according to its terms" or "when a party has a right to cancel and the defendant urges that the right be exercised." (See Rest.3d Torts, Liability for Economic Harm (Tent. Draft No. 3, Mar. 7, 2018) § 17, com. f; *id.*, § 16, com. j.)

This Court looks to other states, and the Restatements, in elaborating California tort law. (See, e.g., *Bily v. Arthur Young & Co.* (1992) 3 Cal.4th 370, 394 [adopting Restatement test endorsed by multiple states]; *Anderson v. Owens-Corning Fiberglas Corp.* (1991) 53 Cal.3d 987, 1000 [same]; *O'Keefe v. South End Rowing Club* (1966) 64 Cal.2d 729 [same].) The Court should do so here to "bring the law of California firmly and clearly in line with this array of judicial authority and sound critical thinking" (*id.* at p. 739), by holding that inducing a new partner to terminate an at-will contract is not intentional interference with contract absent wrongful means.

3. Requiring Wrongful Means for Inducing a New Partner to Terminate an At-Will Contract Resolves This Case

Under the above principles, Ixchel's intentional interference claim fails absent sufficient pleading of wrongful means. The Forward/Ixchel Collaboration Agreement gave Forward unconditional termination rights. (SER 50, § 12.4.)

Biogen persuaded Forward to exercise those bargained-for rights. (ER 98–99, ¶¶ 42-43; ER 101-102, ¶ 62.) Thus, as long as Biogen did not employ wrongful means to induce Forward's termination of the Collaboration Agreement with Ixchel, Biogen was free to "offer better contract terms" or "make use of persuasion or other suitable means, all without liability." (*Reeves, supra,* 33 Cal.4th at p. 1152, internal quotations omitted.)

To be sure, Biogen and Ixchel were not potential competitors in selling DMF drugs. (ER 17-19.) But that does not oust the commerce-promoting wrongful means requirement. Firms vie for all types of partners, in "other" ways for a range of purposes. (Rest.2d Torts, § 768, com. c; see also Rest.3d Torts, Liability for Economic Harm (Tent. Draft No. 3, *supra*) § 17, coms. a, f.) Here, Biogen succeeded in persuading Ixchel's at-will contract partner (Forward) to reach a multi-faceted deal with Biogen instead, one calling for Forward to exercise its termination rights. Forward bargained with Ixchel for the freedom to make that choice. If Biogen did not act with wrongful means in putting Forward to the choice of sticking with Ixchel or partnering with Biogen, it should have no tort liability.

The wrongful means line sufficiently protects the weaker interest in contractual stability that parties in Ixchel's position possess; it provides commercial actors notice of what conduct to avoid in offering new relationships; and it promotes commerce by enabling parties to receive attractive offers. Under this objective wrongful-means element, Ixchel's allegations regarding Biogen's subjective motives are irrelevant. (*Della Penna, supra,* 11 Cal.4th at p. 384; see also Rest.3d Torts, Liability for Economic Harm (Tent. Draft No. 3, *supra*) § 17, com. b.)

C. Ixchel's Unpersuasive Arguments for Dispensing With a Wrongful-Means Requirement Jeopardize Commerce

Ixchel asks this Court to confine the wrongful means element to the *Reeves* employment setting. The Court should reject that limitation.

1. Ixchel's Position Undermines Competition and Harms Californians

Ixchel contends that "no ... public policy" supports requiring wrongful means beyond *Reeves'* employment setting. (OB pp. 29-30.) Ixchel is wrong. As explained, requiring wrongful means to state a claim for intentional interference based on the defendant's inducement of a new partner to terminate an at-will contract "maximizes areas of competition free of legal penalties." (*Della Penna, supra*, 11 Cal.4th at p. 392; see also *Reeves, supra*, 34 Cal.4th at pp. 1151-1152.) To *dispense* with any such requirement would chill competition.

Ixchel's further contention—that requiring wrongful means here runs contrary to the "longstanding principle discouraging intentional interference with at-will business agreements" (OB p. 7)—fails to persuade. For one thing, as *Reeves* recognizes, the greater interest in promoting commerce prevails when outsiders offer attractive terms to parties lacking assurance of future relations. For another, Ixchel's contention that requiring wrongful means will "detrimental[ly] ... promot[e] third party interference with at-will contracts" and "dissuad[e] parties from entering into" such arrangements (OB p. 30) gets it backwards. Requiring wrongful means *promotes* at-will contracting. Ixchel's proposed rule would deter companies (like Forward here) from contracting with smaller entities like Ixchel in the first place, for fear of making themselves less attractive to future potential partners unwilling to risk the lawsuit. If an at-will arrangement would not protect later suitors, fewer companies in Forward's position would make deals with the Ixchels of this state.

In sum, (1) society has a relatively weak interest in protecting at-will contracts from outsiders vying to sway one party's free will; (2) strong public policy supports competitive freedom to make such inducements; and (3) the wrongful means line strikes the proper balance. Only when outsiders cross that line should the law provide legal recourse for interference with a terminable relationship.

2. Ixchel's Authorities Do Not Support Its Proposed Rule

The cases Ixchel cites provide no support for dispensing with wrongful means when a party induces a new partner to terminate an existing at-will contract.

PG&E, contrary to Ixchel's contention, sets no "default" rule dispensing with "an independently wrongful act." (OB p. 24.) The Court rejected a broader argument that "there can be no cause of action [at all] for inducing a contracting party to seek to terminate the contract according to its terms." (*PG&E, supra,* 50 Cal.3d at p. 1127.) In other words, unlike Biogen, the defendant argued that no interference claim could exist *even if* it acted with wrongful means. The Court never addressed whether to require wrongful means for either tort; instead, the issue was whether either of the interference torts could be based on the defendant persuading plaintiff's counterparty to sue plaintiff for declaratory relief. (*Id.* at p. 1123 [holding no].)

Rather than aid Ixchel, *PG&E* supports requiring wrongful means here. The Court recognized the need for "caution" in developing interference torts, lest courts improperly "protect[] the secure enjoyment of contractual and economic relations at the expense of our interest in a freely competitive economy." (*Id.* at p. 1136.) This very caution drove both *Della Penna* and *Reeves* to require wrongful means; the same policies support requiring wrongful means for inducing termination of an at-will contract to be "actionable." (*Reeves, supra,* 34 Cal.4th at p. 1152.)

Ixchel's invocation of *Quelimane Co. v. Stewart Title Guaranty Co.* (1998) 19 Cal.4th 26 to argue that interfering with a contract is "'a wrong in and of itself'" is equally unavailing. (OB pp. 25, 31.) *Quelimane* concerned the distinct problem of interference with the *performance* of a *non-terminable* contract. (19 Cal.4th at pp. 56-57.) In that setting, the plaintiff enjoyed a present right to ongoing performance. Here, Ixchel did not. Nor did *Quelimane* concern alleged interference by inducing termination; rather, it concerned obstructing pre-termination performance. Requiring proof of wrongful means to establish interference with an *at-will* contract does not offend *Quelimane.*

Ixchel mischaracterizes *Reeves* as a narrow employment-driven exception to otherwise trumping interests in contractual stability. (OB pp. 25-26.) Of course, the holding of *Reeves* centers on at-will *employment* contracts. But as explained, *Reeves'* central rationales apply here. Wrongful means should be required to establish intentional interference with contract based on inducing a new partner to terminate an at-will contract, regardless of the setting.

Last, *Popescu v. Apple Inc.* (2016) 1 Cal.App.5th 39 (*Popescu*) and *Redfearn v. Trader Joe's Co.* (2018) 20 Cal.App.5th 989 (*Redfearn*) do not support a "narrow application" of *Reeves.* (OB pp. 26-29.) Rather, they show that the wrongful means requirement sufficiently protects society's interest in contractual stability. Both cases held that the plaintiff "adequately alleged independently wrongful conduct." (*Popescu,* 1 Cal.App.5th at pp. 44-45, 65; *Redfearn,* 20 Cal.App.5th at p. 1005.) To the extent the conduct in those cases merited condemnation, the wrongful means requirement provided "legal recourse." (OB p. 30.)

Moreover, neither case presented the issue posed here. *Popescu* involved an "atypical" scenario: the defendant induced termination of the plaintiff's employment not to make a hire, but as part of alleged retaliation. (*Popescu, supra,* 1 Cal.App.5th at p. 62 [observing that "neither policy consideration that animated our high court's holding in *Reeves* is present"].) *Redfearn* involved the use of defamation to squeeze out an intermediary.

(See 20 Cal.App.5th at p. 994.) Unlike this case, the *Redfearn* defendant already dealt with one of the contracting parties *through* the plaintiff. The Court also held the contract *not* at-will. (See *id.* at p. 1005.) Neither case is comparable to Biogen's inducement of Forward to terminate its at-will contract with Ixchel and partner with Biogen.

Just as *Reeves* declined to decide whether to require wrongful means beyond the setting presented (*Reeves, supra,* 33 Cal.4th at p. 1153, fn. 7), this Court can leave for another day whether these distinct settings require wrongful means. It suffices to resolve this case to hold that a plaintiff fails to establish intentional interference with contract against a party that induces a new business partner to terminate an at-will agreement according to its terms, unless that party induced the termination through an independently wrongful act.

II. SECTION 16600 APPLIES THE ANTITRUST RULE OF REASON TO THE CHALLENGED RESTRAINT

Ixchel's claims thus hinge on deeming "wrongful" the inclusion in the Biogen/Forward Patent License of section 2.13—calling for Forward to terminate its Collaboration Agreement with Ixchel—on the ground that section 16600 voids section 2.13. (See ER 98-106 [Second Amended Complaint].) Section 16600 states: "Except as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." As explained below, this Court should hold that section 16600 subjects section 2.13 to the antitrust rule of reason and not the *per se* invalidation of *Edwards v. Arthur Anderson LLP* (2008) 44 Cal.4th 937.

A. The Live Issue Is How, Not Whether, Section 16600 Applies To Restraints On Businesses

Biogen does not dispute "the applicability of Section 16600." (*Ixchel, supra,* 930 F.3d. at p. 1037.) Nor did it ever argue that "section 16600 applies only in the employment context." (Contra *id.* at p. 1036 and OB p. 19.) Section 16600 can govern a contractual restraint that one business places on the "trade[] or business" of another business (what we will call a business-to-business restraint). The parties instead dispute the standard by which those restraints should be assessed. Does the antitrust rule of reason govern, or does *Edwards*—which Ixchel reads to void *any* nontrivial restriction?

Resolving this "important question of law" (Cal. Rules of Court, rule 8.500 (b)(1) is vital to California commerce. How section 16600 applies to business-to-business restraints affects virtually every commercial contract governed by California law. The Ninth Circuit acknowledged the concern that, if *Edwards* governs here, "'then every joint venture, lease, distribution agreement, license agreement and many other widely used business agreements that fall under California law would be at substantial risk of invalidation under section 16600.'" (*Ixchel, supra,* 930 F.3d at p. 1037, quoting Perry & Howell, *A Tale of Two Statutes*: Cipro, Edwards, *and the Rule of Reason* (2015) 24 Comp: J. Antitrust, UCL & Privacy Sec. St. B. Cal. 21, 21-22 ("Perry & Howell").)

This Court should reject Ixchel's plea to duck the core disputed issue of what standard applies. (OB pp. 22-23.) The question certified—"*Does* section 16600" apply to a business-to-business restraint (*Ixchel, supra,* 930 F.3d at p. 1033, emphasis added)—fairly encompasses the question *how*. Biogen so explained in its August 2, 2019 letter urging acceptance of review, and this Court has not limited the issues.

Further, Ixchel's assertion that it has stated a claim if the statute applies to businesses (OB p. 22) is wrong. Ixchel cites a footnote to the certification order that *presumed*, without deciding, the applicable standard:

> We recognize that, should the California Supreme Court determine that section 16600 ... applies to businesses as well as to individuals *[in the same way as in Edwards]*, it need not reach [the *Reeves*] issue because Ixchel would have adequately pleaded an independently wrongful act.

(*Ixchel, supra,* 930 F.3d at p. 1037, fn. 6.) Absent the bracketed assumption, the footnote is incorrect, as we will show. In any event, the Ninth Circuit properly refused to "restrict the Court's consideration of the issues involved," instead urging this Court to rephrase them as needed to "address the contentions of the parties." (*Id.* at p. 1033.)

This Court should take up that invitation and address the section 16600 standard as reframed by Biogen's Statement of Issues. (See Cal. Rules of Court, rule 8.548 (f)(5) ["At any time, the Supreme Court may restate the question or ask the requesting court to clarify the question."].) As explained below, the appropriate section 16600 standard is the rule of reason.

B. Section 16600 Applies the Antitrust Rule of Reason to Section 2.13 of the Patent License

Section 16600's structure, co-location with the Cartwright Act, and adoption following a settled judicial construction of its substantively identical precursor (Civil Code section 1673), all establish that section 16600 applies the antitrust rule of reason to section 2.13.

1. Section 1673 Did Not Foreclose the Rule of Reason for Legitimate Restraints Supporting Collaborations

Just as in *Edwards*, we start with section 16600's substantively identical precursor, Civil Code section 1673. (See *Edwards, supra,* 44 Cal.4th at pp. 945-946.) As enacted in 1872, section 1673 provided: "Every contract by which any one is restrained from exercising a lawful profession, trade, or business of any kind, otherwise than is provided by the next two sections, is to that extent void." (See Biogen's Motion for Judicial Notice ("MJN"), p. JN 206.)

a. Section 1673's Text and Legislative History Reveal Displacement of Only Certain Common Law

Section 1673's text discloses a *limited* displacement of the common law rule of reason. The statute did not void all restraints of trade. The meaning of its language voiding contracts "by which anyone is restrained from exercising a lawful profession, trade, or business" must be found in "the context of the entire statute and the statutory scheme of which it is a part, harmonizing provisions relating to the same subject matter, to the extent possible." (*Satele v. Superior Court* (2019) 7 Cal.5th 852, 858-859, citations omitted; see also *Flannery v. Prentice* (2001) 26 Cal.4th 572, 577-578.)

In applying that canon of construction, the statute's exceptions hold the key—as Ixchel itself argues (OB pp. 17-19). (See also *Romasko v. City of Milwaukee* (Wis. 1982) 321 N.W.2d 123, 128 ["an exception puts into sharper relief the contours of the principal policy of the statute"], citing Hurst, Dealing with Statutes (1982) p. 60.) Section 1673's exceptions disclose that the statute aimed to displace common law for *only* two types of restraints.

Restraints incident to separations. Civil Code section 1674 permitted (as section 16601 permits today) a seller's agreement to "refrain from carrying on a similar business" in a limited area, upon sale of a business's goodwill, as long as the buyer "carries on a like business therein." (MJN, p. JN 207.) The need for this exemption shows that section 1673 voided restraints imposed upon *separation*: when an employee leaves an employer, an agent parts from a principal, an individual sells a business, or an association dissolves. Likewise, Civil Code section 1675 exempted (as section 16602 exempts today), agreements between partners that none will "carry on a similar business" where a dissolving partnership had operated. (MJN, pp. JN 207-208.)

The legislature thus exempted certain restraints incident to separations while voiding in section 1673 others falling within that class.

The *absence* of similar exceptions for restraints in *collaborations* is equally telling. Had the legislature intended to foreclose all restraints accompanying collaborations, one would expect further exceptions—for example, permitting an employer to restrain employees from pursuing other trades *during* employment. (See *Angelica Textile Services, Inc. v. Park* (2013) 220 Cal.App.4th 495, 509 [section 16600 does not "affect limitations on an employee's conduct or duties *while* employed" because "'[d]uring the term of employment, an employer is entitled to its employees' "undivided loyalty,"'" emphasis in original].)

Naked restraints. A "naked restraint of trade" is one "with no purpose except stifling of competition"—that is, one unrelated to any legitimate activity. (*Fisher v. City of Berkeley* (1984) 37 Cal.3d 644, 670, fn. 20 (*Fisher*), affd. (1986) 475 U.S. 260.) Section 1673's two exceptions involve post-separation restraints incident to legitimate activity. This implies that the legislature also intended, in section 1673, to void naked restraints on exercising a trade, profession, or business.

Section 1673's legislative history confirms reading the statute to displace the common law only as to these two types of restraints, and not others. The Code Commissioners expressed an intent to rein in common law that had allowed "restraint[s] of trade" to a "very dangerous extent"—citing *only two types* of examples: (i) restraints incident to separations (post-employment covenants and overbroad post-sale covenants); and (ii) naked restraints. (MJN, pp. JN 201, 206-207: Civil Code Vol. I (1872), annotated by Haymond and Burch of the Cal. Code Com. ("Annotated Code (1872)") pp. 502-503.) The Commissioners disapproved of cases allowing payment for a naked non-compete (*Cal. Nav. Co. v. Wright* (1856) 6 Cal. 258); a non-compete tied to the sale of boat (*Dunlop v. Gregory* (1851) 10 N.Y. 241); and a post-termination restraint on the practice of law (*Whittaker v. Howe* (1841) 3 Beav. 383). (See Annotated Code (1872) pp. 502-503.)

In contrast, the Commissioners *approved* of two cases recognizing the potential validity of reasonable post-sale limitations: *Wright v. Ryder* (1868) 36 Cal. 342 (see esp. pp. 357-358) and *More v. Bonnet* (1870) 40 Cal. 251. (See Annotated Code (1872) p. 503.) The Code Commissioners expressed no intent to foreclose the rule of reason for all restraints of trade.

Indeed, section 1673 is best read to alter the common law *only* as to restraints on *individuals*. Section 1674 described the buyer as a "him" and section 1675 concerned partners. Section 1673's "any one," therefore, is naturally read to encompass only individuals. In this reading, "trade" and "business" likely meant those of individuals, in parallel with the first-listed "profession." (See, e.g., *In re J.G.* (2019) 6 Cal.5th 867, 880 [applying canon that words draw meaning from the company they keep].) The legislative history decried contracts restraining "*an individual* from exercising a lawful trade" because they "tend[] to enforce idleness, and deprive[] the State of the services of its *citizens*." (Annotated Code (1872) p. 503, emphasis added.) All the examples cited concerned restraints on individuals. Section 1673's seeming limitation to natural persons makes it particularly appropriate to exercise caution in applying its successor, section 16600, to business-to-business restraints.

b. This Court Confirmed the Rule of Reason's Application to Restraints Supporting Collaborations

This Court applied Civil Code section 1673 and its exceptions stringently to the restraints they targeted: (i) restraints incident to separations; and (ii) naked restraints. We call this line of cases the *per se* track, because the case law reveals a distinct track governing restraints outside these two categories. For these other restraints, consistent with section 1673's text and legislative history, the common-law rule of reason governed. (See Perry & Howell, *supra*, at p. 23.)

In the *per se* track, this Court voided nontrivial restraints on individuals incident to separations, absent a statutory exception. Thus, in *Chamberlain v. Augustine* (1916) 172 Cal. 285 (*Chamberlain*), the Court voided a penalty on an individual for competing—agreed upon when he sold his stock in a foundry—because the penalty would restrain his participation in the foundry business. (*Id.* at pp. 287-288; see also, e.g., *City Carpet-Beating, Etc. Works v. Jones* (1894) 102 Cal. 506, 510-513 [voiding post-sale noncompete to extent it exceeded section 1674];

Edwards v. Mullin (1934) 220 Cal. 379, 381-382 [voiding post-dissolution non-compete exceeding section 1675].)

Also in the *per se* track, the Court condemned naked restraints of trade, including between businesses. (See *Vulcan Powder Co. v. Hercules Powder Co.* (1892) 96 Cal. 510, 515 [illegality of agreement among competitors to apportion the dynamite market and fix prices "too obvious to need argument, authorities, or elucidation"]; *Getz Bros. & Co. v. Federal Salt Co.* (1905) 147 Cal. 115, 118-119 [payment to exit].)[12]

In section 1673's rule of reason track, this Court *validated* reasonable restraints underlying collaborations. *Grogan v. Chaffee* (1909) 156 Cal. 611 (*Grogan*) upheld a minimum resale price requirement in a supply contract between a producer of olive oil and a grocer, finding "nothing either unreasonable or unlawful." (*Id.* at p. 614.) *Grogan* declared it "settled" that sections 1673-1675 must be read in light of common law principles set forth in U.S. Supreme Court and other precedents, and identified the core question as "whether, under the particular circumstances of the case, and the nature of the particular contract involved in it, the contract is, or is not, unreasonable." (*Id.* at pp. 614-615.) The Court used the same approach in *Associated Oil Co. v. Myers* (1933) 217 Cal. 297 for a gas station lease that forbade the owners from selling or advertising on the

---

[12] *Getz* also invalidated the restraint under the Sherman Act. (147 Cal. at pp. 119-120.) Notably, a key case establishing the Sherman Act's *per se* rule against price fixing invoked *Vulcan*. (*U.S. v. Trenton Potteries Co.* (1927) 273 U.S. 392, 400, fn. 1.)

property any products other than its counterparty's. (*Id.* at pp. 299-300.) The Court held section 1673 did not void this restraint, finding "nothing unreasonable" because "competition [was] not stifled." (*Id.* at p. 306.)

On the other hand, the Court condemned restraints in commercial supply contracts that the Court deemed anticompetitive—an analysis unnecessary if section 1673 voided all restraints on "business" without more. (See *Santa Clara Valley Mill & Lumber Co. v. Hayes* (1888) 76 Cal. 387, 392 [restraint designed "to suppress the supply and enhance the price of lumber in four counties"]; *Morey v. Paladini* (1922) 187 Cal. 727, 736-737 [restraint with "purpose" to secure "a monopoly" on lobster trade].)

Great Western Distillery Products, Inc. v. John A. Wathen Distillery Co. (1937) 10 Cal.2d 442 (*Great Western*) confirmed section 1673's distinction between void restraints incident to separations and reasonable restraints underlying collaborations. The Court distinguished *Chamberlain*—a post-separation restraint on an individual—as "directly within the contemplation" of section 1673. (*Id.* at p. 448.) By contrast, *Great Western* applied the rule of reason in evaluating an exclusive-agency restraint between businesses, concluding that "both the purpose and effect of the contract" were to create a market, not to restrict one. (*Id.* at pp. 446, 449-450.) "Statutes are interpreted in the light of reason and common sense," this Court explained, and "courts will not hold to be in restraint of trade a contract, ... the main purpose and effect of which are to promote and increase business in the line affected, merely because its operations might ... incidentally and indirectly restrict trade in such line." (*Id.* at p. 446.) Section 1673 instead proscribed restraints designed "to stifle competition or create a monopoly." (*Id.* at p. 449.)

In applying the rule of reason, *Great Western* cited seminal federal Sherman Act rule of reason decisions, including *Chicago Board of Trade v. United States* (1918) 246 U.S. 231, 238. (See generally Perry & Howell, *supra*, at pp. 30-32.) As noted commentators observed: "The thread running through all of these cases is that conduct or activity which unduly stifles competition or tends to create a monopoly is illegal; restraints which do not have that competitive effect were held to be legal." (Von Kalinowski & Hanson, *The California Antitrust Laws: A Comparison with Federal Antitrust Laws* (1959) 6 UCLA L.Rev. 533, 540.)

2. Section 16600 Applies the Rule of Reason to Restraints Supporting Business Collaborations

This Court should continue to apply the rule of reason to restraints underlying business collaborations. That approach reflects section 16600's ratification of previous judicial construction. It also harmonizes section 16600 with the simultaneously reenacted Cartwright Act—California's principal antitrust law—which itself codifies and carries forward the common law rule of reason.

a. Section 16600 Ratified Section 1673's Rule of Reason Track, and Courts Have Continued It

In 1941, the California Legislature renumbered Civil Code section 1673 as section 16600 without "substantively alter[ing]" the provision's wording (*Zamora v. Clayborn Contracting Group, Inc.* (2002) 28 Cal.4th 249, 257), and placed section 16600 in the same part of the Business and Professions Code as the then-reenacted Cartwright Act. (§ 16600, added by Stats. 1941, c. 526, § 1; § 16720 et seq., added by Stats. 1941, ch. 526, § 1.) The statute read then, as it does now: "Except as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void."

"[W]hen a statute has been construed by the courts and the Legislature thereafter reenacts the statute without changing the interpreted language, a presumption is raised that the Legislature was aware of and has acquiesced in that construction." (*People v. Bonnetta* (2009) 46 Cal.4th 143, 151.) Because the legislature enacted substantively-identical section 16600 against this Court's two-track construction of section 1673, section 16600 should be "given the same construction [section 1673] received." (*Marina Point, Ltd. v. Wolfson* (1982) 30 Cal.3d 721, 734.) That is, section 16600 should be construed: (i) to void naked and nontrivial restraints incident to separations (the *per se* track); but (ii) to maintain application of the common law rule of reason for other restraints of trade. Legislative history confirms the intent to "restate the existing law clearly and concisely, without change in legal effect and with the approval of those most vitally concerned." (Cal. Code Com., letter to Members of Bus. & Prof. Code Conference on Trade Regulation Law, Aug. 1940, at MJN p. JN 117; see also pp. JN 179-180 [Oct. 1940 supplement].)[13]

Cases since section 16600's enactment confirm adoption of the two-track approach. Where a contract places a nontrivial, post-separation restraint on a person's profession, trade or business, as in *Edwards*, section 16600 voids the restraint absent an exemption. (See generally *Edwards, supra*, 44 Cal.4th at p. 946 [citing cases].)

By contrast, California courts have applied the rule of reason to restraints within business relationships. For example, in *Dayton Time Lock Service, Inc. v. Silent Watchman Corp.* (1975) 52 Cal.App.3d 1 (*Dayton*), the court held an exclusive-dealing restraint between businesses in a franchise agreement lawful under section 16600, absent foreclosure of competition in a "substantial share of the affected line of commerce"—the test called for by the antitrust rule of reason. (See *id.* at pp. 6-7,

---

[13] Minor alterations to statutory exceptions upon section 16600's enactment—1674 became 16601 and 1675 became 16602, with changed geographic limitations—disclose no intent to change section 1673's fundamental scope. (See §§ 16601-16602, added by Stats. 1941, ch. 526, § 1.) Nor do later (and numerous) amendments to the exceptions, none of which amended section 16600. The 1994 amendment to section 16602.5 made the first reference to corporations. (See *infra* p. 60.)

citing *Standard Oil Co. v. United States* (1949) 337 U.S. 293, 314; see also *Rolley, Inc. v. Merle Norman Cosmetics Stokes & Smith* (1954) 129 Cal.App.2d 844, 847-850 [citing *Great Western* and federal antitrust precedents].)

Similarly, *Lafortune v. Ebie* (1972) 26 Cal.App.3d 72 held a vertical territorial restraint "susceptible to justification under the rule of reason" under both the antitrust laws and section 16600. (*Id.* at pp. 74-75; see also *Martikian v. Hong* (1985) 164 Cal.App.3d 1130, 1133-1134 [relying on "rule of reason" in upholding restraint in commercial lease].) Most recently, *Quidel Corp. v. Superior Court* (2019) 39 Cal.App.5th 530, review granted Nov. 13, 2019, S258283 (*Quidel*), called for a "full-blown anti-trust analysis" of a restraint incident to a collaboration, distinguishing "noncompete clauses that attempt to dilute or eliminate employee mobility." (*Id.* at pp. 540, 544-545, internal quotations omitted.)

Centeno v. Roseville Community Hospital (1979) 107 Cal.App.3d 62 (*Centeno*), explained why the common law rule of reason controlled its approval of an exclusive-dealing contract: "Section 16600 is basically a codification of the common law relating to contracts in restraint of trade. [¶] Where, as here, there is no express intent to depart from, alter, or abrogate the common law rules [for evaluating restraints incident to business collaborations], a statute purporting to embody such doctrine or rules will be construed in light of common law decisions on the same subject." (*Id.* at pp. 68-69, citations omitted.) As explained, this requires reading section 16600 to maintain the rule of reason as the standard for such restraints.

b. Applying the Rule of Reason to Restraints Supporting Business Collaborations Harmonizes Section 16600 With the Cartwright Act

As noted, the legislature placed section 16600 in the same Part of the same Code as the simultaneously reenacted Cartwright Act. Section 16600 must be read "in the context of ... the statutory scheme of which it is a part, harmonizing provisions relating to the same subject matter, to the extent possible." (*Satele v. Superior Court, supra,* 7 Cal.5th at pp. 858–859, citations omitted.)

"[T]he Cartwright Act and Sherman Act carry forward the common law understanding that 'only unreasonable restraints of trade are prohibited.'" (*Cipro, supra,* 61 Cal.4th at p. 146, quoting *Marin County Bd. of Realtors, Inc. v. Palsson* (1976) 16 Cal.3d 920, 930 (*Palsson*).) "Though the Cartwright Act is written in absolute terms," it "draw[s] upon the common law prohibition against restraints of trade" and therefore "in practice not every agreement within the four corners of its prohibitions has been deemed illegal." (*Cipro,* at pp. 136-137.) The rule of reason thus operationalizes the Cartwright Act's core prohibitions, *inter alia,* against "carry[ing] out restrictions in trade or commerce." (§ 16720, subd. (a).) Moreover, section 16725 of the Cartwright Act specifically declares that "'[i]t is not unlawful to enter into agreements ... the purpose and effect of which is to promote, encourage or increase competition'"—a provision this Court read to "codif[y]" the rule of reason. (*Cipro, supra,* 61 Cal.4th at p. 137 & fn. 5, citing *People v. Building Maintenance Contractors' Assn.* (1953) 41 Cal.2d 719, 726-727 (Traynor, C.J.).)

Under the Cartwright Act, restraints in collaborations or that induce collaborations—whether between manufacturers and distributors, customers and suppliers, or, as here, licensors and licensees—are routinely assessed under the rule of reason.[14] Accordingly, reading section 16600 to apply the rule of reason to such business-to-business restraints "harmonize[s]" section 16600 with the Cartwright Act, the interpretation this Court "always prefer[s]." (*Brown v. Mortensen* (2011) 51 Cal.4th 1052, 1067; *Brinker Restaurant Corp. v. Superior Court* (2012) 53 Cal.4th 1004, 1027.)

By contrast, reading section 16600 to void *all* restraints relating to business collaborations under the *Edwards* track would nullify much of the Cartwright Act by replacing the rule of reason with effective *per se* illegality. (See Perry & Howell, *supra,* at pp. 21-22, 38-39.) The legislature did not intend this

---

[14] (See generally Perry & Howell, *supra,* at pp. 38-39; see also e.g., *Flagship Theatres of Palm Desert, LLC v. Century Theatres, Inc.* (2011) 198 Cal.App.4th 1366, 1381 [restraint on film distribution]; *Exxon Corp. v. Superior Court* (1997) 51 Cal.App.4th 1672, 1680-1681 [requirements contract]; *Kim v. Servosnax, Inc.* (1992) 10 Cal.App.4th 1346, 1361 [exclusive license].)

"absurd consequence[]." (*City of San Jose v. Superior Court* (2017) 2 Cal.5th 608, 616, internal quotations omitted.)

Nor did this Court in *Edwards*. The Court's comment that section 1673 "rejected the common law 'rule of reasonableness'" (44 Cal.4th at p. 945) concerned restraints incident to separation, governed by section 16600's *per se* track (see 44 Cal.4th at pp. 941-942 [review limited to, and holding only that, "section 16600 prohibits employee noncompetition agreements"]). As explained, when a business-to-business restraint is neither naked nor imposed incident to a separation, the 1872 legislature expressed no intent to foreclose the rule of reason, and the 1941 legislature *preserved* case law applying the rule of reason.

Applying the rule of reason to business-to-business restraints, moreover, does not implicate section 16600's policy "that every *citizen* shall retain the right to pursue any lawful employment and enterprise of their choice." (*Edwards, supra*, 44 Cal.4th at p. 946, emphasis added, internal quotations omitted.) Such restraints do not threaten any citizen's "*practice* of a profession, business, or trade." (*Id.* at p. 945, emphasis added.) Indeed, until long after its enactment, no textual basis existed for reading Civil Code section 1673 or its successor section 16600 to govern non-natural persons at all. Section 1673, as explained (*supra*, § II-B-1-a.), most naturally applied only to individuals. Section 16602.5, as Ixchel notes, added an "it." (OB p. 19.) But until that 1994 addition, section 16600—especially when viewed in light of its exceptions—also read most easily to govern real persons.[15]

These considerations further imply favoring the rule of reason when courts entertain any doubt about whether a restraint is (a) naked or incident to separation (governed by *Edwards*) or (b) a potentially legitimate restraint underlying a collaboration (governed by the rule of reason). The co-equal Cartwright Act applies the rule of reason to *all* restraints of trade (see § 16725), while section 16600 *per se* voids only naked restraints and restraints incident to separations based on a core policy of protecting individuals. Thus, when the question of characterization is close, only a business is restrained, and no section 16601-16602.5 exception governs the conduct, the Cartwright Act's rule of reason should apply.[16]

---

[15] Contrary to Ixchel's contention (OB pp. 17-18), reading section 16601 as limited to natural persons does not render surplusage any part of its "owner of a business" definition, added in 2002. (§ 16601, as amended by Stats. 2002, ch. 179, § 1.) "Partner," "member," or "owner of capital stock" all can be natural persons. Notably, section 1674/16601 has always contained "him" or "his," and later "her."

[16] Restraints incident to sales, dissolutions, and terminations present easy cases—all are restraints incident to separations. Restraints that last the length of a collaboration, conversely, fall within the rule of reason track. Harder questions may arise when business-to-business restraints start at a collaboration's onset and endure past its end. Firms may choose not to form procompetitive contracts absent limited restraints on business partners that outlast collaborative activity. Accordingly, the rule of reason should govern a business-to-business restraint that induces a collaboration, even if the restraint endures post-

Alternatively, but for the same reasons, this Court should hold that section 16725 provides a defense to restraints imposed on businesses that section 16600 otherwise voids. Treating section 16725 as an implied exception to section 16600 furthers the purpose of both of these related statutory schemes, which is to promote competition (compare *Edwards, supra,* 44 Cal.4th at p. 945 with *Cipro, supra,* 61 Cal.4th at p. 146), while leaving *Edwards* fully applicable to restraints on individuals.

c. Section 16600 Applies the Same Rule of Reason as the Cartwright Act

Harmonizing the Cartwright Act with section 16600 further requires concluding that both statutes apply the *same* rule of reason—one that is dynamic and context-dependent, and draws from the same rich body of law.

First, as explained, the Cartwright Act "carr[ies] forward the common law understanding that only unreasonable restraints of trade are prohibited." (*Cipro, supra,* 61 Cal.4th at pp. 146-147, internal quotations omitted.) So too, "[s]ection 16600 is basically a codification of the common law relating to contracts in restraint of trade." (*Centeno, supra,* 107 Cal.App.3d at p. 68.) Courts' reliance on antitrust rule of reason decisions in applying sections 1673 and 16600 confirms that both statutes apply the same rule of reason. (See, e.g., *Great Western, supra,* 10 Cal.2d at pp. 448-

---

collaboration. It is unreasonable to conclude the legislature intended to exempt restraints necessary to induce sales (in section 16601) yet void restraints that induce procompetitive collaborations.

449; *Dayton, supra,* 52 Cal.App.3d at p. 6; *Lafortune v. Ebie, supra,* 26 Cal.App.3d at pp. 74-75.) If the Cartwright Act's rule of reason exonerates a restraint, so too should section 16600's "codification" of the same principle in the statute's rule of reason track.[17] Second, because section 16600 and the Cartwright Act both implement the same rule of reason, section 16600's rule of reason—like the Cartwright Act's—is dynamic and context-dependent.

As to the first: The rule of reason "invokes the common law itself" along with its "dynamic potential." (*Business Electronics Corp. v. Sharp Electronics Corp.* (1988) 485 U.S. 717, 732.) "The term 'restraint of trade' in the statute, like the term at common law, refers not to a particular list of agreements, but to a particular economic consequence, which may be produced by quite different sorts of agreements in varying times and circumstances." (*Id.* at p. 731.) The same is true of the Cartwright Act's rule of reason. (See *Cipro, supra,* 61 Cal.4th at pp. 146-147 [explaining how rule of reason under the Cartwright Act has evolved like the Sherman Act's]; *Speegle v. Board of Fire Underwriters of the Pacific* (1946) 29 Cal.2d 34, 43 [noting that "Congress did not intend 'to freeze the proscription of the Sherman Act within the mold of the then current judicial

[17] The Cartwright Act was not modeled on the federal antitrust laws. (See *Clayworth v. Pfizer, Inc.* (2010) 49 Cal.4th 758, 772-773.) But both codify the same common law of restraints of trade. (*Cipro, supra,* at pp. 136-137.)

decisions'" and that "[t]he Cartwright Act is couched in similarly comprehensive language"].)

As to the second: The rule of reason is not "one-size-fits-all," but rather calls for an "enquiry meet for the case." (*Cipro, supra,* 61 Cal.4th at pp. 146-147). The flexible rule of reason typically requires the challenger seeking invalidation to show "substantially adverse effect on competition" that "outweighs [a restraint's] procompetitive effects." (*Exxon Corp. v. Superior Court* (1997) 51 Cal.App.4th 1672, internal quotations omitted; accord *Cipro,* at p. 146.) *Dayton* illustrates section 16600's dynamic and context-dependent rule of reason. Asked to decide the legitimacy of a contract requiring exclusive dealing during its term, the court applied antitrust principles developed for that kind of restraint. (*Dayton, supra,* 52 Cal.App.3d at pp. 6-7 [no evidence that contract would "foreclose competition in a substantial share" of the relevant market].) The court did *not* ask how earlier expressions of the common law rule of reason would have analyzed the restraint.

The recent *Quidel* decision correctly concluded that a research-and-development restraint incident to a joint venture required a "'full-blown anti-trust analysis,'" including whether the restraint "tends to restrain trade more than promote it" (*Quidel, supra,* 39 Cal.App.5th at 535, 544-545)—a classic articulation of the rule of reason. (See *Cipro, supra,* 61 Cal.4th at p. 146.) But *Quidel* did not explain the role played in that particular case by factors it drew from other cases: whether a restraint (i) "forecloses a substantial share of the line of commerce" or (ii) is "necessary to protect the parties in their dealings" with each other. (39 Cal.App.5th at p. 545.) Both can inform the rule of reason, but they are *not* the rule of reason itself.

Substantial foreclosure, as *Dayton* illustrates, can help establish anticompetitive effects under the rule of reason. As for whether "'the restraint upon one party is not greater than protection to the other requires,'" that principle once stood at the center of the common law's rule of reason. (*Grogan v. Chaffee, supra,* 156 Cal. at p. 615, quoting *Gibbs v. Consolidated Gas Co.* (1889) 130 U.S. 396, 409; see also *D. Ghirardelli Co. v. Hunsicker* (1912) 164 Cal. 355, 362 (*Hunsicker*) [summarizing common law]; *U.S. v. Addyston Pipe & Steel Co.* (6th Cir. 1898) 85 F. 271, 282 [same].) Today, by contrast, *harm to competition,* not an imperfect fit, is the touchstone of rule-of-reason analysis. Only *after* a challenger identifies an anticompetitive restraint "likely to be of significant magnitude," and the defendant offers evidence of the restraint's pro-competitive effects, do courts consider whether those "legitimate objectives can be achieved in a substantially less restrictive manner." (*Bhan v. NME Hospitals, Inc.* (9th Cir. 1991) 929 F.2d 1404, 1413 [Sherman Act rule of reason]; *O'Bannon v. National Collegiate Athletic Assn.* (9th Cir. 2015) 802 F.3d 1049, 1070 [same]; *Palsson, supra,* 16 Cal.3d at pp. 937-939 [Cartwright Act; analyzing "purported necessity" of "possible justifications" after identifying "anticompetitive effects"].)[18]

---

[18] Reasonable necessity plays the same role in section 16600's

Cases such as *Great Western*, therefore, cited the "not greater than protection to the other requires" principle because, at that time, it controlled the rule of reason's operation. (10 Cal.2d at pp. 448-449; see also *Hunsicker, supra,* 164 Cal. at pp. 361-362 [same under Cartwright Act].) But as *Great Western*'s invocation of *Chicago Board of Trade v. United States* makes plain, the underlying test is the rule of reason *itself*, not the static content the rule of reason then mandated.

* * *

In sum, section 16600 does void *some* contracts by which a business "is restrained from engaging in a lawful ... trade, or business" without rule-of-reason analysis. But such voiding is—and should remain—confined to restraints incident to separations (viz., post-dissolution, post-contract, and post-sale restraints) and naked restraints. Restraints underlying legitimate collaborations may "restrain" a non-natural "person" "from engaging in a lawful ... trade, or business" in some way—*but*, absent a rule of reason violation, not in the sense the statute condemns. Just as courts do not read the antitrust statutory prohibition on "restraints of trade" woodenly because "[e]*very* agreement concerning trade ... restrains" (*Cipro, supra,* 61 Cal.4th at 146, internal quotations omitted), so too section 16600's prohibition must be read "'"in the

---

exceptions. If section 16600 voids a restraint (that is, deems the restraint unreasonable), and an exception applies (analogous to establishing a legitimate justification under the contemporary rule of reason), courts then assess a restraint's reasonable necessity. (See, e.g., *Swenson v. File* (1970) 3 Cal.3d 389, 395-396.)

light of reason and common sense.'" (*Great Western, supra*, 10 Cal.2d at p. 446.)

3. The Rule of Reason Controls Section 16600's Application to Section 2.13

Under the above principles, section 16600's rule of reason, and not the *per se* rule of *Edwards*, governs section 2.13. First, section 2.13 is not a naked restraint—one with "no purpose except stifling of competition." (*Fisher, supra*, 37 Cal.3d at p. 670, fn. 20.) Rather, section 2.13 is an "ancillary" restraint, one "imposed by a legitimate business collaboration, such as a business association or joint venture, on nonventure activities." (*Texaco Inc. v. Dagher* (2006) 547 U.S. 1, 7; *Fisher, supra*, 37 Cal.3d at p. 665 ["incidental to another legitimate purpose"].)

The Biogen/Forward Patent License, as explained, launched a productive collaboration. Ixchel averred that the Patent License's purpose was "to allow Biogen to continue selling its Tecfidera product for the treatment of multiple sclerosis without fear of infringing on Forward's [purported] intellectual property rights." (ER 99, ¶ 43.) This alleged purpose was valid; "clearing blocking positions" posed by others' patents is "procompetitive." (U.S. Dept. of Justice and Federal Trade Com., *Antitrust Guidelines for the Licensing of Intellectual Property* (Jan. 12, 2017), p. 30.)[19] Section 2.13 served that purpose by narrowly precluding third-party development agreements—which

[19] Available at <https://www.justice.gov/atr/IPguidelines/download>, as of Dec. 8, 2019.

threatened to recreate the very blocking positions that Forward's licenses to Biogen removed. (See Facts § B.) Thus, agreements before this Court show section 2.13 is an "ancillary restraint, ... subordinate to the larger, lawful agreement." (ER 8.)

Section 2.13 also is not a restraint on Forward's business incident to a separation. The provision took effect at the start of a patent license arrangement requiring extensive ongoing collaboration. (See Facts § B.) It did not spring into existence once the collaboration ended. This case presents no close characterization call. But even if it did, harmonizing section 16600 with the Cartwright Act warrants applying the rule of reason for the reasons set forth above. Accordingly, section 16600's rule of reason track governs section 2.13.

This Court can leave application of the rule of reason to the Ninth Circuit, if that court considers it necessary. Ixchel failed to preserve any argument that section 2.13 is anticompetitive under any rule of reason standard. The district court held that Ixchel alleged no rule of reason violation because it averred no "harm to competition." (ER11.) In the Ninth Circuit, Ixchel failed to contest that ruling.

C. Ixchel's Misconstruction of Section 16600 Threatens Commerce

Ixchel chose not to brief to this Court the fairly included question of *how* section 16600 applies to restraints on businesses, misreading the rules that govern the scope of review. (See *supra*,

§ II-A; OB p. 22.) Biogen thus addresses the position Ixchel took on this point in the Ninth Circuit and may take here.

1. This Court Should Reject Ixchel's One-Size-Fits-All Approach to Section 16600

Ixchel advanced in the Ninth Circuit a flawed construction of section 16600. Ixchel reads the statute to void *every* contract that imposes any nontrivial restraint—one of a "'substantial character'"—on a counterparty's business. (Ninth Circuit Opening Brief, pp. 40-41.) In Ixchel's view, if a contract restraining trade freedom exceeds a low bar for substantiality, section 16600 voids it absent a statutory exception. Put equivalently, Ixchel applies the rule of *Edwards* to *all* restraints. As shown, this is not the law.

Ixchel's misreading of section 16600 also cannot be right because it effectively nullifies the Cartwright Act. According to the Ninth Circuit, "it will be the rare contractual restraint whose effect is so insubstantial that it escapes scrutiny under section 16600." (*Golden v. California Emergency Physicians Medical Group* (2018) 896 F.3d 1018, 1024 (*Golden II*).) Applying *Edwards* to all limitations on trade freedom, as Ixchel proposes, would effectively substitute a rule of *per se* invalidity for the Cartwright Act's rule of reason, rendering the Act a dead letter. (See also Perry & Howell, *supra*, at pp. 38-39.)

Ixchel argued the Ninth Circuit had adopted the "'restraint of a substantial character'" language from this Court's 1916 decision in *Chamberlain, supra.* (Ninth Circuit Opening Brief, pp. 33-34, 40-41, citing *Golden v. California Emergency Physicians Medical Group* (2015) 782 F.3d 1083, 1091-1093 (*Golden I*).) *Great Western*, however, explains why the restraint in *Chamberlain*—a post-sale penalty on an individual for competing (172 Cal. at pp. 287-288)—does not imply *per se* illegality for restraints in business collaborations. (*Great Western, supra,* 10 Cal.2d at p. 448.)

Ixchel's other cases (OB pp. 20-21) likewise lend its misconstruction of section 16600 no support. *Fleming v. Ray-Suzuki, Inc.* (1990) 225 Cal.App.3d 574, 576, a section 16602 case, also involved a non-competition agreement incident to a sale. *Robinson v. U-Haul Co. of California* (2016) 4 Cal.App.5th 304, 309, concerned a restraint preventing an individual from competing following termination of his U-Haul dealership. Like *Fleming*, *Robinson* concerned a restraint incident to a separation, not a restraint in a collaboration.

Kelton v. Stravinski (2006) 138 Cal.App.4th 941, is inapposite for two reasons. First, it concerned (like *Edwards* and *Chamberlain*) a restraint on individuals. Second, the court viewed the restriction as a naked non-compete. The parties' partnership agreement expressly *allowed* competition against the partnership that their separate non-compete agreement precluded. (*Id.* at pp. 945, 947-948.) *Kelton* has no application to the ancillary restraint at issue here.

As for *Edwards*, this Court was "not persuaded" that cases outside "the employment context" provided any guidance. (44 Cal.4th at p. 950, fn. 5.) *Edwards* is equally inapplicable here.

"An opinion is not authority for propositions not considered." (*Kinsman v. Unocal Corp.* (2005) 37 Cal.4th 659, 680, internal quotations omitted.) Indeed, this Court expressly limited the scope of review in *Edwards* to "employee noncompetition agreements," and concluded only that "section 16600 prohibits employee noncompetition agreements" absent statutory exception. (44 Cal.4th at pp. 941-942.) *Edwards* does not control a restraint placed on a business.

2. Ixchel's Unitary Standard Would Chill Commerce

Declaring unlawful all contracts that impose a "substantial" restraint would make much commercial contracting impossible, and deter even more. As one set of commentators put it, under that approach to section 16600, "every joint venture, lease, distribution agreement, license agreement and many other widely used business agreements that fall under California law would be at substantial risk of invalidation under section 16600." (Perry & Howell, *supra*, at pp. 21-22.) Ixchel could not articulate any boundary for its position at the Ninth Circuit.

A few examples suffice to illustrate why Ixchel's section 16600 standard cannot be the law. Under Ixchel's test, a manufacturer could not confine a distributor's sales to a particular location to improve product support; the distributor could simply challenge the restriction as a "substantial" restraint on its trade or business. (Compare *Continental T.V., Inc. v. GTE Sylvania Inc.* (1977) 433 U.S. 36, 55, 59 [rule of reason governs].) Ford could not require its dealers to sell only Ford cars without facing a lawsuit, if a dealer contended that its "trade or business" involved selling multiple lines. (Compare *Rolley, Inc. v. Merle Norman Cosmetics, supra,* 129 Cal.App.2d at pp. 851-852 [validating similar restraint].) A mall operator could not condition a lease on not operating the same type of store as another tenant, if the lessee showed that this imposed a "substantial" restraint on its "business." (Compare *Martikian v. Hong, supra,* 164 Cal.App.3d at pp. 1133-1134 [rejecting section 16600 challenge].) A hospital could not grant a radiological group an exclusive contract, aimed at improving quality of care, for fear that a departing group member could invalidate the "substantial" restraint to which the hospital agreed. (Compare *Centeno, supra,* 107 Cal.App.3d at pp. 69-70 [rejecting section 16600 challenge].)

These examples are just the tip of an innovation and commerce-crushing iceberg. Section 16600, as demonstrated, inflicts no such horribles. Section 16600 applies the rule of reason, save for restraints incident to separations or naked restraints. This reading honors the statute's text, reflects the settled construction the legislature adopted, and harmonizes this statute with the Cartwright Act. Ixchel's contrary construction violates the elemental principle that section 16600 must be "'interpreted in the light of reason and common sense.'" (*Great Western, supra,* 10 Cal.2d at p. 446.)

3. Section 16600's Rule of Reason Is Not Confined to Exclusivity in Ongoing Relationships

To the extent Ixchel may argue that application of the rule of reason under section 16600 is restricted to the facts of cases such as *Great Western*, *Dayton*, and *Centeno*—exclusive dealing in ongoing business collaborations—it is incorrect.

First, application of the rule of reason does not turn on form but rather economic substance. (See *Cipro, supra*, 61 Cal.4th at p. 147; *Great Western, supra*, 10 Cal.2d at p. 448.) No principle confines the rule of reason to exclusive dealing in buy/sell relationships, so as to leave procompetitive licensing hobbled by *per se* invalidation.

For example, common licensing terms such as grantbacks (where licensors require licensees to grant improvement patents back to licensors) and fields of use (where the licensor reserves the right to employ a patent for some uses while licensing rights to employ it for others) have long been assessed, and routinely pass muster, under the rule of reason. (See *B. Braun Medical, Inc. v. Abbott Laboratories* (Fed.Cir. 1997) 124 F.3d 1419, 1426 [field of use]; *Transparent-Wrap Mach. Corp. v. Stokes & Smith Co.* (1947) 329 U.S. 637, 647 [grantbacks]; see also *Macom Technology Solutions Holdings, Inc. v. Infineon Technologies AG* (C.D.Cal. Oct. 31, 2016, No. 2:16-CV-02859-CAS(PLAx)) 2016 WL 6495373, at pp. *20-21 [rejecting section 16600 challenge because "no authority" deemed field-of-use licensing "anticompetitive"].) Such arrangements need not be exclusive; they can involve far less ongoing collaboration than the Biogen/Forward Patent License; and they restrict how licensees compete. The legislature did not saddle California's economy with a cramped rule of reason that condemns these and similar arrangements. Nor has this Court. It should not here.

Second, confining the rule of reason to supporting exclusivity in ongoing relationships would not dislodge the rule of reason's application to section 2.13. Biogen attained exclusive and co-exclusive licenses in an ongoing relationship calling for extensive cooperation. (See Facts § B.) Section 2.13 is ancillary to that relationship, helping it to succeed. (See *supra*, § II-B-3; ER 8.) The rule of reason should govern.

CONCLUSION

The Court should hold that: (1) A claim for intentional interference with contract requires pleading an independently wrongful act when the defendant, in seeking a relationship with a third party, induces that third party to terminate its at-will contract with the plaintiff; (2) The antitrust rule of reason governs section 16600's application to a restraint one business places on the trade or business of another, except for restraints incident to separations and naked restraints; and (3) Section 16600 subjects section 2.13 of the Biogen/Forward Patent License to the antitrust rule of reason, not to *per se* invalidation.

Respectfully submitted,

December 16, 2019

ROPES & GRAY LLP
Mark S. Popofsky

GREINES, MARTIN, STEIN & RICHLAND, LLP
Laurie J. Hepler

Attorneys for Respondent Biogen, Inc.

CERTIFICATION

Pursuant to California Rules of Court, rule 8.504(d)(1), I certify that this **ANSWER BRIEF ON THE MERITS** contains **13,971** words, not including the parts listed in rule 8.504(d)(3), counted by the word processing program used to generate it.

Dated: December 16, 2019

Laurie Hepler

PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the County of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is 5900 Wilshire Boulevard, 12th Floor, Los Angeles, California 90036.

On December 17, 2019, I served the foregoing document described as: **RESPONDENT BIOGEN, INC.'S ANSWER BRIEF ON THE MERITS** on the parties in this action by serving:

Christopher Banys (SBN 230038)
cdb@banyspc.com
BANYS, P.C.
567 Marsh Street
San Luis Obispo, CA 93401
Tel: (650) 308-8505

Counsel for Appellant ***IXCHEL PHARMA, LLC***

Clerk of the Court
Ninth Circuit Court of Appeals
The James R. Browning Courthouse
95 7th Street
San Francisco, CA 94102
Case No. 18-15258

( ) By Mail: I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. Under that practice, it would be deposited with United States Postal Service on that same day with postage thereon fully prepaid at Los Angeles, California in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date of deposit for mailing in affidavit.

(X) By Federal Express, I caused to be delivered such envelope via Federal Express Overnight to the office(s) of the addressee(s) noted above.

Executed on December 17, 2019, at Los Angeles, California.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Francene Wilson