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PERSPECTIVE

Analyzing Ixchel v. Biogen's new rules

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Last week, the California Supreme Court established two new pleading rules in *Ixchel Pharma, LLC v. Biogen, Inc.*, 2020 DJDAR 8084 (Aug. 3, 2020). For claims of tortious interference with at-will contracts, plaintiffs now must plead facts showing the defendant's conduct was itself illegal, apart from the "interference." For claims that certain noncompete contracts between businesses violate Business and Professions Code Section 16600, plaintiffs must plead facts suggesting the contracts were anticompetitive under the "rule of reason" standard.

Ixchel stemmed from a dispute involving three pharmaceutical developers. Two of them, Ixchel and Forward, contracted together to jointly develop a drug for neurodegenerative disorders, containing the active ingredient DMF. Their contract specified that either party could terminate it at-will. After they made substantial progress, to the point of planning clinical trials, Biogen entered the picture. It paid Forward $1.25 billion and received technology licenses in an otherwise unrelated legal settlement that also contained a term prohibiting Forward's continued or future work with Ixchel on the neurodegenerative disorder drug or any other drug containing DMF.

Ixchel sued Biogen in Federal Court for, among other things, tortious interference with an at-will contract and restraint of trade in violation of Section 16600. The District Court dismissed both claims for failure to state a claim, and Ixchel appealed to the 9th Circuit Court of Appeals, which certified two questions to the California Supreme Court.

The Court framed those issues as: (1) Whether a plaintiff is required to plead an independently wrongful act to state a claim for tortious interference with an at-will contract. (2) What is the proper standard for evaluating whether contracts restraining business conduct violate Section 16600?

Interference With At-Will Contracts

Its analysis of the tortious interference issue started with an explanation of the two traditional versions of such claims: interference with an actual contractual relationship and with a prospective economic relationship. The former requires an enforceable contract; the latter does not but is based on the hope and expectation of future economic benefits.

Historically, the elements of these two torts did not differ, except for the actual contract requirement. Then, in *Della Penna v. Toyota Motor Sales, U.S.A., Inc. (1995) 11 Cal.4th 376, 393*, the Court added an element to the prospective relationship tort: The defendant's conduct was "wrongful by some legal measure other than the fact of interference itself." Subsequently, in *Reeves v. Hanlon (2004) 33 Cal.4th 1140, 1149 – 1151*, the Court extended that requirement to claims involving at-will employment contracts. It reasoned that California has long favored the right of employees to choose opportunities freely, even those with employers who compete with their current employers; and, that the at-will employment context differed from "formally cemented economic relationships" for specific periods of time which were "deemed worthy of protection from interference by a stranger to the agreement."

The *Ixchel* court extended *Reeves* beyond employment contracts to at-will contracts between businesses. Quoting the Restatement of Torts, it reasoned that "'[l]ike parties to a prospective economic relationship, parties to at-will contracts have no legal assurance of future economic relations.'" Consequently, the Court concluded competitors are free to pursue a party to an at-will relationship without fear of potential liability, unless the pursuit itself is independently wrong.

B&PC Section 16600

The Court's analysis of the Section 16600 issue started with its confirmation that the statute applied to contracts between businesses and not just those involving individuals. The Court then evaluated the statute's history, its context in the statutory framework of antitrust law, and prior court interpretations. The Court highlighted that "two discernible categories of holdings emerged" from numerous prior interpretations of the statute and its predecessor: (1) agreements not to compete after the termination of employment or the sale of a business interest were invalid without regard to their reasonableness, that is, per se illegal; and, (2) agreements limiting commercial dealings and business operations were generally invalid only if they were unreasonable.

Looking at the statutory framework of antitrust law, the Court found similarities between the seemingly categorical prohibitions of Section 16600 and the Cartwright Act. For example, Cartwright Act Section 16722 states: "Any contract or agreement in violation of this chapter is absolutely void and is not enforceable at law or in equity." And, Cartwright Act Section 16726 provides: "Except as provided in this chapter, every trust is unlawful, against public policy and void."

The Court explained "we have not interpreted these provisions in a sweeping fashion. 'Though the Cartwright Act is written in absolute terms, in practice not every agreement within the four corners of its prohibitions has been deemed illegal.'" The Court noted that both the Cartwright Act and Section 16600 were enacted at a time when restraints of trade were evaluated against the common law standard of reasonableness; and, its interpretations of each have not departed from that standard.

The Court then explained how certain "restraints" may actually enhance competition. It noted how exclusive dealing contracts may support new market entry, incentivize new product marketing, reduce costs, stabilize long-term supply and price predictability, and enable long-term planning. Thus, the Court concluded, under Section 16600, not every contract between businesses is absolutely or per se unlawful, but instead should be evaluated under the "rule of reason."

Implications

The *Ixchel* decision makes pending and future tortious interference with at-will contract and Section 16600 claims more difficult and uncertain for plaintiffs. For example, a pending tortious interference claim may be subject to dismissal as a result of this change in the law. Also, what is an "at-will contract" subject to this new rule? As renewable, fixed-duration contracts approach expiration, do the parties to them have more than a mere hope of future economic benefits to which *Ixchel*'s rationale should apply?

Businesses and counsel considering the potential of Section 16600 claims must now consider substantially more information about how the contracts at issue impact competition and consumer welfare. Although *Ixchel* provides examples of competition-enhancing considerations, rule of reason claims often require detailed analysis and expert economic input. Further, note that businesses and counsel should exercise caution, as certain collaborative contracts between competitors might not be subject to the rule of reason, and instead may treated as per se illegal. ■

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