No. S191550
(Court of Appeal Nos. B202789 & B205034)
(Los Angeles Super. Ct. No. BC209992 (related to No. BC263701))

IN THE SUPREME COURT
OF THE STATE OF CALIFORNIA

SUPREME COURT
FILED

APR 18 2011

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Deputy

SARGON ENTERPRISES, INC.,
Plaintiff and Appellant,

v.

UNIVERSITY OF SOUTHERN CALIFORNIA et al.,
Defendants and Appellants.

After A Decision By The Court Of Appeal Second Appellate District, Division One

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REPLY TO ANSWER TO PETITION FOR REVIEW

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INTRODUCTION

Respondent Sargon Enterprises, Inc. ("Sargon") asserts that the decision below does not warrant review because the decision "is of significance only to Sargon and USC." (Answer 1.) That is wholly incorrect. As the letters submitted by *amici* supporting review demonstrate, whether a trial court has meaningful discretion to exclude expert testimony that is based upon a speculative and unreliable methodology is an issue of widespread significance not only to the State's great research universities but also to a wide variety of corporations and other entities that routinely face expert testimony in civil litigation. Moreover, it presents an ongoing conflict in the lower courts that remains unresolved long after this Court granted review to resolve it in the *Lockheed Litigation Cases*.

Sargon tries to sidestep the grant of review in the *Lockheed Litigation Cases* by asserting that the conflict the Court sought to resolve in that case concerned only medical testimony about causation. But this Court's grant of review was not so limited. Rather, the conflicting decisions that this Court sought to resolve in the *Lockheed Litigation Cases* interpreted section 801 of the Evidence Code, which governs the

admissibility of *all* expert testimony and provides no special evidentiary rules for medical causation testimony. The Court of Appeal here, no less than in the *Lockheed Litigation Cases*, placed in issue whether a trial court may exclude expert testimony that is based on unreliable methodologies. Moreover, this case squarely presents this issue in a frequently recurring and readily understood factual context, making it an excellent vehicle for considering anew the issue presented in the *Lockheed Litigation Cases*.

Sargon's remaining arguments are unavailing as well. For example, Sargon asserts that it is improper to grant review based upon the conflict between the decision below and published decisions concerning lost profits testimony because the decision below is unpublished. This Court, however, has granted review in other cases presenting conflicts between published and unpublished decisions, and there is no reason not to do so here. Sargon also asserts that review is premature because the decision below remanded the case for trial. But this Court has granted review in prior cases in that procedural posture, and awaiting the outcome of a trial to decide

whether the testimony of Sargon's expert was properly excluded would force USC to litigate under the specter of a damages award of up to $1.2 billion—an amount that would cripple the University. The issue is thus ripe and appropriate for resolution now.

Accordingly, review should be granted.

LEGAL DISCUSSION

I. SARGON FAILS TO DISPEL THE CONFLICTS WITH THE EVIDENCE CODE AND OTHER COURT OF APPEAL DECISIONS THAT WARRANT REVIEW HERE AS IN THE *LOCKHEED LITIGATION CASES*.

The petition explained that the decision below contradicts the Evidence Code, deepens the existing conflict over trial court discretion to exclude speculative expert testimony that this Court sought to resolve in the *Lockheed Litigation Cases*, and creates a new conflict over expert testimony concerning lost profits. (Pet. 16-30.) Sargon fails to dispel any of these conflicts. In addition, contrary to Sargon's assertions, this case is an excellent vehicle for addressing those conflicts, because it presents them in a context—expert testimony concerning lost profits—that recurs frequently in civil litigation and

that is particularly amenable to judicial oversight in order to prevent juror confusion.

A. Sargon Fails To Reconcile The Decision Below With The Evidence Code.

The petition showed that the decision below contradicts section 801(b) of the Evidence Code. That section requires trial court judges to act as gatekeepers and affords them discretion to exclude expert testimony that is based upon speculative and unreliable methodologies. The decision below, by contrast, held that it is up to the jury to determine whether the lost profits calculations of Sargon's expert were based upon a speculative and unreliable methodology. (Pet. 13-16.) Sargon fails to dispel this conflict.

Sargon denies that the decision below contradicts section 801(b) (Answer 6), but offers little explanation for this bald denial beyond a reference to a later section of the Answer (*ibid.* [referencing Section I(C)]) that does not mention section 801(b) (see *id.* at pp. 8-11). And while Sargon concedes that trial courts should be able to exclude expert testimony that is based upon speculative or unreliable methodologies

(*id.* at pp. 1-2 [calling the issue a "straw man"]), it does not explain how, if that is the case, the trial court abused its discretion here.

Notably absent from the Answer is any attempt to show that the testimony of Sargon's expert is based upon a reliable methodology. Sargon asserts that its expert "used traditional and long-recognized methods to protect Sargon's lost profits." (Answer 10.) But it fails to cite any precedent for the "market driver" hypothesis that its expert used to compare a tiny startup to established industry leaders thousands, and in some respects millions, of times larger, and to hypothesize that, if a single 23-person clinical study had been completed, Sargon would have earned hundreds of millions and perhaps more than a billion dollars in profits. Sargon fails to square such "field of dreams" conjecture with the text of the Evidence Code, which requires that expert opinion testimony be based on "matter ... that is of a type that *reasonably* may be relied upon by an expert in forming an opinion on the subject to which his testimony relates." (Evid. Code, § 801, subd. (b), italics added.)

B. Sargon Cannot Deny The Persisting Conflict Among Court Of Appeal Decisions Since *Lockheed* On Trial Court Discretion Over Unreliable Expert Testimony.

Sargon does not (and cannot) dispute that a conflict persists among Court of Appeal decisions over the issue that this Court sought to resolve in the *Lockheed Litigation Cases*—namely, whether trial courts have discretion to exclude expert testimony for using speculative or unreliable methodologies. As two leading experts on California evidence law observe, "it is widely recognized that the decisions of the California Court of Appeal are divided regarding trial court discretion to examine an expert's methodology." (Letter of David L. Faigman and Edward J. Imwinkelried, April 11, 2011, at p. 2; see Pet. 17-18 [citing commentators].) One line of cases, exemplified by the two decisions in the *Lockheed Litigation Cases,* (2004) 115 Cal.App.4th 558 and (2005) 23 Cal.Rptr.3d 762, the latter of which this Court granted review to consider, permits a trial court to examine an expert's specific methodology and exclude the expert's testimony if the court finds that methodology speculative or unreliable. (Pet. 18-21.) Another line of cases, exemplified by *Roberti v. Andy's Termite & Pest Control, Inc.* (2004) 113 Cal.App.4th 893, prohibits a trial court from examining the

reliability of an expert's specific methodology and permits it to examine only the "type" of matter upon which the expert relied. (Pet. 21-22.) Although Sargon describes this conflict as "claimed" or "supposed" (Answer 7 & fn. 7), it makes no attempt to reconcile the *Lockheed* and *Roberti* lines of cases. To the contrary, it "assum[es] the existence of such a conflict" in its arguments (*id.* at p. 7), thereby effectively acknowledging the conflict.

Rather than disputing the persistence of the conflict over trial court discretion to exclude expert testimony for using speculative or unreliable methodologies, Sargon asserts that this case is not a proper vehicle for resolving that conflict. According to Sargon, because the *Lockheed Litigation Cases, Roberti* and most of the other conflicting decisions involved testimony by medical experts concerning causation, the conflict among those decisions is "from an unrelated area of the law." (Answer 6-8.) That is wrong. There is no special evidentiary rule governing medical testimony concerning causation: section 801 of the Evidence Code applies whenever "a witness is testifying as an expert" (Evid. Code, § 801), and therefore both *Roberti* and the Court of

Appeal decision in the *Lockheed Litigation Cases* applied that section. (See *Lockheed Litigation Cases, supra,* 115 Cal.App.4th at p. 564; *Roberti, supra,* 113 Cal.App.4th at p. 906; see also *id.* at pp. 899-904 [holding the *Kelly-Frye* rule inapplicable].) Thus, the conflict at issue in the *Lockheed* and *Roberti* lines of cases concerns not only medical testimony on causation, but also expert testimony on lost profits, engineering, statistics, consumer surveys, and numerous other topics on which experts frequently opine. (See, e.g., *P & D Consultants, Inc. v. City of Carlsbad* (2010) 190 Cal.App.4th 1332, 1349 [citing *Lockheed Litigation Cases* in upholding exclusion of expert testimony regarding construction costs]; *Stephen v. Ford Motor Co.* (2005) 134 Cal.App.4th 1363, 1371 [citing *Lockheed Litigation Cases* in upholding exclusion of expert testimony regarding product manufacturing defect].)

Sargon points out that neither the majority nor the dissenting opinion discussed the *Lockheed* and *Roberti* lines of cases. (Answer 6-7.) But the majority opinion contains barely any discussion of the standards governing the admission and exclusion of expert testimony at all—much less any reasoned discussion of existing case law. (See

Typed Opn. 19-31.) This omission is not a reason to deny review but rather to grant it.

Moreover, the dissent effectively adopts the position expressed in the Court of Appeal's decision in the *Lockheed Litigation Cases*. The dissent recognized that trial judges should perform a "gatekeeping function" by excluding expert testimony that is "based upon speculative or conjectural factors" (Dissenting Opn. 2, 4) and that the "exclusion of the methodology used here was properly left to the trial court under the abuse of discretion standard" (*id.* at p. 7). In the *Lockheed Litigation Cases,* the Court of Appeal similarly concluded "that an expert opinion based on speculation or conjecture is inadmissible" and that an order excluding expert evidence for using an unreliable methodology is reviewed deferentially for abuse of discretion. (*Lockheed Litigation Cases, supra,* 115 Cal.App.4th at p. 564.) Thus, even though the *Lockheed Litigation Cases* and *Roberti* involved medical testimony concerning causation, the majority and dissenting opinions below present the same issue concerning the discretion of trial court judges to exclude unreliable and speculative expert testimony.

The case for review of this issue is strengthened, not weakened, by the fact that this case does not involve testimony from medical experts concerning causation. That is because medical testimony raises factual issues "fraught with considerable, and currently unresolvable, uncertainty." (Green et al., *Reference Guide on Epidemiology,* in Reference Manual on Scientific Evidence (2d ed. 2000), at p. 346; see also Egilman et al., *Proving Causation: The Use and Abuse of Medical and Scientific Evidence Inside the Courtroom—An Epidemiologist's Critique of the Judicial Interpretation of the Daubert Ruling* (2003) 58 Food & Drug L.J. 223, 229 [noting that epidemiology is "a complex discipline that is unintuitive and, . . . often does not describe what we want or think it describes"].) By contrast, expert testimony concerning lost profits, while more pervasive than medical testimony concerning causation and at least as likely to confuse a jury with its false appearance of precision, is more amenable to judicial evaluation because it involves less scientific complexity. This case therefore presents an excellent vehicle in which to consider whether trial courts have discretion to

exclude expert testimony for using speculative or unreliable methodologies.

If the trial court is held to have abused its discretion here in finding that the lost profits calculations by Sargon's expert were based upon a speculative and unreliable methodology, it is difficult to see how a trial court's exclusion of *any* lost profits analysis could *ever* be upheld. The expert here, an accountant with no experience in the dental implant industry (Typed Opn. 21; Tr. Ct. Opn. 22-23) concluded that one of the supposed "market drivers" in the dental implant industry is innovativeness and that, if a startup's first product was innovative enough, the startup could capture the same market share within ten years as multibillion dollar international corporations that currently dominate the market. (Pet. 6-11.) Although Sargon discusses its expert's qualifications (see Answer 2, fn. 2), and asserts that he used "traditional and long-recognized methods" (*id.* at p. 10), Sargon omits from the Answer any attempt to defend the "market driver" hypothesis at the core of its expert's testimony or otherwise show how the expert could reliably compare a tiny startup such as Sargon with

established industry leaders that have sales, budgets, revenues, and work forces thousands, and in some respects millions, of times larger than Sargon and therefore differ from Sargon "by any relevant, objective business measure." (Tr. Ct. Opn. 12.)

This case thus squarely presents the issue that this Court sought to resolve in the *Lockheed Litigation Cases* and provides an excellent vehicle for returning to that issue.

C. Sargon Cannot Sidestep The Conflict Among Court Of Appeal Decisions Over Expert Testimony On Lost Profits.

In addition to deepening the general conflict over trial court discretion to exclude expert testimony for using speculative or unreliable methodologies, the decision below creates a related conflict on the subject of expert testimony about lost profits. Specifically, the decision below conflicts with prior decisions permitting trial courts to exclude expert testimony concerning lost profits that is based upon speculative or unreliable comparisons between dissimilar companies. (Pet. 23-30.) In response, Sargon denies that the decision below conflicts with any reported decisions concerning lost profits (Answer 8-10) and asserts that in any event, a conflict between published cases

and an unpublished decision is not a proper ground for review (*id.* at pp. 5-6). Neither argument is persuasive.

First, as the petition explained, the decision below conflicts with *Parlour Enterprises, Inc. v. Kirin Group, Inc.* (2007) 152 Cal.App.4th 281, *Kids' Universe v. In2Labs* (2002) 95 Cal.App.4th 870, and *Berge v. International Harvester Co.* (1983) 142 Cal.App.3d 152, all of which held expert testimony inadmissible because it was based upon speculative and unreliable comparisons between dissimilar companies. (Pet. 23-26.) In asserting that the decision below does not conflict with any published decisions, Sargon simply ignores this authority. The Answer does not even mention *Kids' Universe* and *Berge,* and while *Parlour Enterprise* is mentioned three times (Answer at 5, 6, 11), Sargon never attempts to reconcile the decision's holding with the decision below.

This omission is telling, for *Parlour Enterprises* held that, in calculating lost profits, an expert improperly compared a fledgling ice cream parlor with a restaurant chain hundreds of times larger (152 Cal.App.4th at p. 290). By contrast, the majority below held that it was proper for Sargon's expert to compare a tiny startup to multinational

corporations thousands, if not millions, of times larger. The decision below is thus in square conflict with *Parlour Enterprises* over the admissibility of comparisons between vastly dissimilar companies.

Second, contrary to Sargon's suggestion, this Court can and does review cases involving conflicts between published and unpublished decisions. According to a leading treatise, 15-30% of the petitions granted review involve unpublished decisions. (Eisenberg et al., Cal. Practice Guide: Civil Appeals and Writs (The Rutter Group 2010) ¶ 13:18, p. 13-6 [rev. #1, 2009].) Many of these petitions assert conflicts between the unpublished decision and published decisions. Indeed, this Court recently decided two such cases. In *Century National Insurance Co. v. Garcia* (2011) 51 Cal.4th 564, the Court granted review of an unpublished decision that, according to the petition, conflicted with a published decision. (See Petition for Review, *Century Nat. Ins. Co. v. Garcia* (Cal. Jan. 8, 2010, No. S179252) at pp. 9-13.) Similarly, in *People v. Low* (2010) 49 Cal.4th 372, the petition asserted a conflict between the unpublished decision below and a published decision.

(Petition for Review, *People v. Low* (Cal. April 19, 2007, No. S151961) at p. 4.)

In addition, Sargon's effort to align the decision below with published decisions only highlights the existence of a conflict with *Parlour Enterprises, Kids' Universe*, and *Berge*. According to Sargon, the decision below "glides comfortably down the mainstream of reported case law." (Answer 8-10.) In support of this assertion, Sargon cites four cases—*People ex rel. Dept. of Transp. v. Clauser/Wells Partnership* (2002) 95 Cal.App.4th 1066, *Heiner v. Kmart Corp.* (2000) 84 Cal.App.4th 335, *Brandon & Tibbs v. George Kevorkian Accountancy Corp.* (1990) 226 Cal.App.3d 442, and *Arntz Contracting Co. v. St. Paul Fire & Marine Insurance Co.* (1996) 47 Cal.App.4th 464—that it claims establish that "criticisms of an expert's method of calculation is a matter for the jury's consideration in weighing that evidence" and that "the appropriateness of the particular methodology chosen by the expert to value a particular business is a factual question for the jury." (Answer 9, citations omitted.) If Sargon is correct and these published decisions require *juries* to determine all questions concerning the methodologies

used by experts in calculating lost profits, the decisions conflict with *Parlour Enterprises*, *Kids' Universe*, and *Berge*, which held that *trial courts* have discretion to exclude lost profits testimony based upon speculative or unreliable comparisons. Thus, even under Sargon's account of the lost profits case law, there is a conflict among Court of Appeal decisions warranting this Court's review.

II. SARGON FAILS IN ITS EFFORTS TO DOWNPLAY THE IMPORTANCE OF THE ISSUE PRESENTED.

As this Court recognized in granting review in the *Lockheed Litigation Cases*, the issue presented by the petition—namely, whether trial courts have discretion to exclude expert testimony that employs speculative and otherwise unreliable methodologies—is an important question of law that warrants review by this Court. Although expert testimony is a ubiquitous aspect of trial practice, jurors are often ill-equipped to evaluate such testimony, and it is therefore critical that judges act as gatekeepers with meaningful discretion to exclude expert testimony that employs speculative or unreliable methodologies. (Pet. 31-32.) Moreover, this gatekeeping function is especially important in the damages context, where expert testimony is presented in nearly

every case in which damages are sought, because such testimony is simultaneously easy to manipulate and especially difficult for juries to disregard because it presents a false illusion of precision. (*Ibid.*)

Sargon tries to downplay the importance of this case by asserting that the decision below "did not purport to impose new restrictions on the 'gatekeeping' function of the trial courts" and merely found that the trial court erred in excluding testimony "based upon the specific circumstances of this case." (Answer 3.) But Sargon fails to point to any aspect of the decision below that is based upon the specific circumstances of this case. To the contrary, as noted above, Sargon defends the decision below by asserting a blanket rule that *juries*, and not trial judges, must determine the outcome of all challenges to methodologies used by experts to calculate supposed lost profits. (See, *supra*, pp. 15-16.)

Sargon also tries to minimize the impact of its expert testimony in this case, again suggesting that this case presents narrow and fact-specific issues. Sargon asserts that its expert's "lost profits projections start, not at the $1.2 billion repeatedly emphasized by USC, but at

$120,011,000 for the period 1998 through 2009." (Answer 4.) In fact, the lost profits projections of Sargon's expert start at *$220 million,* nearly twice the amount Sargon asserts, because the expert estimated that Sargon would suffer an additional $100 million in lost profits after 2009. (Typed Opn. 25.) Even more important, Sargon's expert projects that Sargon's lost profits could be as high as the staggering sum of *$1.2 billion.* Requiring that such testimony go to the jury here not only makes this a bet-the-university case for USC, but also raises an issue of broad significance and widespread importance. If a trial court may not exercise discretion to exclude such lost profits testimony, then the testimony will expose defendants generally to the risk of staggering damages judgments at trial, which in turn will create coercive pressure for them to settle for extortionate amounts lacking any reasonable relation to lost profits. (See Letter of Washington Legal Foundation, April 12, 2011, at p. 5.)

Sargon dismisses these concerns on the ground that USC can post a bond pending appeal. (Answer 12.) A bond, however, only suspends the enforcement of judgment pending appeal; it does not

provide any assurance that the judgment will be overturned. Moreover, the cost of the bond needed for the judgment Sargon is seeking would be enormous. A supersedeas bond must be at least one and one-half times the judgment (Code Civ. Proc., § 917.1, subd. (b)), and the premium on such bonds range from 1% to 5% per year (see, e.g., California Surety Bond, Jane Bond Insurance Agency, at http://www.janebond.mobi/California_Surety_Bonds.html [as of April 18, 2011]). Thus, if Sargon were awarded $1.2 billion in lost profits, USC would have to post a $1.8 billion bond to stay the judgment, and the premium for that bond would run from $18 million to $90 million a year. In addition, USC would have to secure the bond with assets equal to the value of the bond. As a consequence, far from alleviating the pressure to settle, the huge expense of such a bond would pressure USC to forgo even a meritorious appeal.

The dilemma that the decision below creates for USC thus has grave implications for all entities, corporate or non-profit, that might be faced with speculative claims by any would-be startup that it would have been a global market leader but for some act or omission by the

defendant. This dilemma is particularly acute for research universities in the State, which foster scientific inquiry and innovation through research agreements that could become ripe targets for contract actions like Sargon's if unlimited lost profits lotteries were allowed at jury trials, beyond trial courts' ability to control. (See Letter of American Council on Education ("ACE") et al., April 11, 2011, at pp. 3-5 [noting the adverse impact that the decision below will have on research agreements and the importance of such agreements to the California economy].) As *amici* ACE, its fellow organizations and Stanford University and the California Institute of Technology explain, "[o]f the hundreds of companies that enter into clinical research agreements with universities, the number that go on to replicate the commercial successes of industry leaders is small," and thus, an expert's "comparison to industry success stories" invites a jury to make "a grossly inflated probability judgment." (*Id.* at p. 4.)

For these reasons, Sargon should not be heard to diminish the broad importance of the decision below.

III. THE ISSUE PRESENTED IS RIPE AND APPROPRIATE FOR CONSIDERATION NOW.

Finally, Sargon argues that review of the decision below now would be premature because the decision remanded the case for a trial at which its expert's testimony might be rejected. (Answer 3-4, 11-12.) There can be no doubt, however, that the admissibility of the testimony of Sargon's expert is ripe for consideration: the trial court conducted an eight-day hearing in which the basis for the expert's lost profits calculations were thoroughly examined, resulting in an exhaustive 33-page opinion that gives this Court an ample basis to consider the issue presented. (Pet. 9-11.) Sargon fails to suggest any way in which the issue presented would be clarified on remand.

Moreover, this Court has recognized that it is appropriate to grant review to consider the admissibility of testimony on interlocutory review prior to the completion of trial. (See, e.g., *Metropolitan Water Dist. of S. Cal. v. Campus Crusade for Christ, Inc.* (2007) 41 Cal.4th 954 [reviewing Court of Appeal decision that reversed exclusion of expert testimony on the fair market value of property and remanded for new trial considering that testimony]; *Elsner v. Uveges* (2004) 34 Cal.4th 915

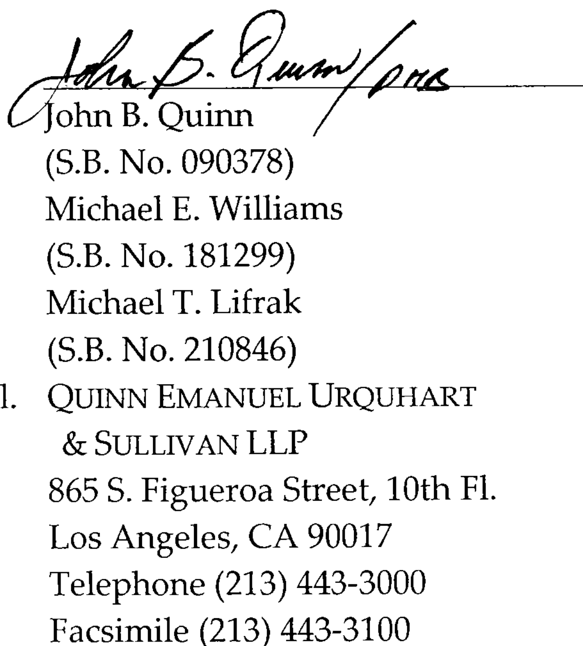
[reviewing Court of Appeal decision that reversed the exclusion of expert testimony on custom and remanded for new trial considering that testimony].) Sargon itself recognized the significance of the issue here at the pre-trial stage by stipulating to judgment and appealing the trial court's exclusion of its expert's testimony rather than proceeding with the trial on lost profits without it.

In contrast, delaying review until after a trial would have potentially devastating consequences for petitioner USC, because, as noted above, it would subject USC to the threat of a judgment so crippling to the University's mission that it would create strong pressure to accept an extortionate blackmail settlement. (See, *supra*, p. 18.) Thus, review is appropriate now, especially as the issue may evade review if not taken up while the case is still in a pre-trial posture.

CONCLUSION

The petition for review should be granted.

DATED: April 18, 2010 Respectfully submitted,



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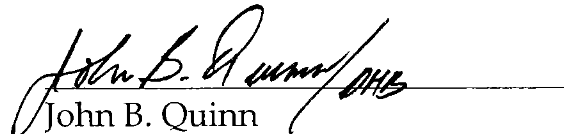
CERTIFICATE OF COMPLIANCE

(Cal. Rules of Court, rule 8.204)

Pursuant to California Rule of Court 8.204, the foregoing Reply to Answer to Petition for Review is double spaced and printed in proportionally spaced 13-point Palatino Linotype typeface. It is 23 pages long and contains 4,109 words (excluding the tables, this certificate, and the proof of service). In preparing this certificate, I relied upon the word count generated by Microsoft Word 2003.

Executed on April 18, 2011, at Los Angeles, California.



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PROOF OF SERVICE

I am employed in the County of San Mateo, State of California. I am over the age of eighteen years and not a party to the within action; my business address is 555 Twin Dolphin Drive, 5th Floor, Redwood Shores, California 94065-2139.

On April 18, 2011, I served true copies of the following document(s) described as **REPLY TO ANSWER TO PETITION FOR REVIEW** on the interested parties in this action as follows:

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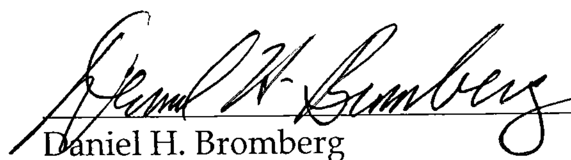
BY MAIL: I am "readily familiar" with the practices of Quinn Emanuel Urquhart & Sullivan, LLP for collecting and processing correspondence for mailing with the United States Postal Service. Under that practice, it would be deposited with the United States Postal Service that same day in the ordinary course of business. I enclosed the foregoing in sealed envelope(s) addressed as shown above, and such envelope(s) were placed for collection and mailing with postage thereon fully

prepaid at Redwood Shores, California, on that same day following ordinary business practices.

BY OVERNIGHT DELIVERY: I deposited such document(s) in a box or other facility regularly maintained by the overnight service carrier, or delivered such document(s) to a courier or driver authorized by the overnight service carrier to receive documents, in sealed envelope(s) or package(s) designated by the overnight service carrier with delivery fees paid or provided for, addressed to the person(s) being served.

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

Executed on April 18, 2011, at Redwood Shores, California.



Daniel H. Bromberg