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**UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF CALIFORNIA**

In re  
ORCA TECHNOLOGY, INC.  
Debtor.

Case No. 92-52037  
MEMORANDUM DECISION

**I. Introduction**

Orca's objection to the claim of MagTron, Inc. arises in the context of a solvent chapter 7 case. From the sale of its technology, Orca Technology, Inc., will pay all creditors in full with interest and will return a dividend to its equity interests. However, Orca and MagTron, as manufacturing partners, were unable to compete successfully in the disk drive industry. Now both corporations are defunct, asserting offsetting claims, and blaming each other for their respective failures.

**II. Facts**

The technology for a 760 megabyte disk drive was developed by Priam, Inc in the late 1980's. However, overwhelmed by its research and development costs, Priam filed bankruptcy in 1989. With thirty years of experience in the disk drive industry, Michael Warner believed that Priam's technology could be developed into a profitable family of drives. Warner incorporated Orca for that purpose and became its first Chief Executive Officer. In June 1990, a little more than a year after the technology was developed by Priam, Orca purchased the patents, product designs, tools, fixtures, manufacturing,

1 pilot lines and documentation for the 760 megabyte disk drive and prototypes for a 1.2 gigabyte disk  
2 drive, together called the Falcon drives, at Priam's bankruptcy sale for \$10,000 plus royalties.

3 Recognizing that the disk drive market was rapidly developing, immediately after the purchase  
4 Warner created a business plan and began to search for a manufacturing partner for Orca. Orca's Vice  
5 President of Sales and Marketing, Richard Reiser, testified that the "strategy was to do what is now  
6 fairly popular in the [Silicon Valley] and, that is, put together what's called a 'fables' corporation."  
7 He explained that since Orca did not have a means of production, but had established engineering, sales  
8 and marketing personnel, Orca would need to find a manufacturing partner with the ability to  
9 manufacture disk drives cost-effectively. Warner testified that Orca sought to establish a manufacturing  
10 relationship in Korea, Japan or Taiwan. As stated in Orca's business plan, this strategy was designed  
11 to "[e]stablish an off shore production capability with a manufacturing partner for high volume low cost  
12 manufacturing" in order to reach efficiencies of scale. Around that time, Orca was contacted by  
13 MagTron, a disk drive manufacturer based in Taiwan. Warner testified that MagTron's President  
14 represented that it had financial backing of \$8 to \$10 million to support such a production and that it  
15 could competently manufacture Orca's Falcon drives. Orca began negotiating with MagTron, while  
16 continuing to look for other suitable manufacturers.

17 After weeks of negotiation, and with no other manufacturing partner in sight, on December 28,  
18 1990, Orca and MagTron signed an agreement. The agreement, which was labeled the "agreement  
19 document," was drafted by both parties without assistance from counsel. By the terms of the  
20 agreement document, MagTron received the exclusive right to manufacture the 760 megabyte disk  
21 drive, but if MagTron was unable to meet the quality requirements or the production or delivery  
22 schedule, Orca could use another manufacturer. Orca agreed to purchase "a minimum of 5,000 drives"  
23 during the first year of production. As part of the agreement, MagTron was to receive the tooling and  
24 equipment created by Priam. The agreement document stated that Orca would transfer the  
25 "technology, manufacturing rights and related technical data to enable MagTron to manufacture and  
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1 market this product.” If MagTron stopped producing the Falcon drives, MagTron was required to  
2 return the production line to Orca. If Orca abandoned the project, MagTron would retain the rights  
3 to the transferred technology and ownership of the transferred tooling and equipment. The agreement  
4 document provided that it could only be modified by a written agreement signed by the parties.

5 Orca shipped the production line to MagTron in Taiwan in February 1991. MagTron forwarded  
6 Falcon drives to Orca’s headquarters for testing in March and thereafter shipped 150 drives in May at  
7 a wholesale price of \$1330 per drive. At the end of May, Reiser acknowledged in a letter to “whom  
8 it may concern” that the drives exceeded specifications and performed well. Reiser stated that they  
9 “feel very lucky to have made this agreement with MagTron, especially at such a critical time in the  
10 development of Orca Technology.” Favorable comments were also reflected in a memo to MagTron  
11 by Orca’s Director of Operations, Bob Deardorff, dated June 1991, regarding the success of the initial  
12 production of Falcon drives. Deardorff wrote that the fact that the “760 program” had been “shut  
13 down in a relatively uncontrolled manner by Priam, shelved for approximately 1.5 years and then  
14 resurrected to production in less than 6 months is a testimony to both MagTron and Orca’s competence  
15 and commitment to the program . . . .” Deardorff’s memo, however, also expressed his concern that  
16 MagTron’s production schedule would not produce the contractually specified 5,000 drives in the first  
17 year of production.

18 The principals of Orca discovered in late May or June 1991 that MagTron was having  
19 difficulties paying suppliers and that it had not ordered sufficient parts to produce 5,000 drives. Many  
20 parts were not readily available from suppliers, requiring seven to eight months from the time ordered  
21 until delivery. Because of Warner’s concern that parts be available for assembly, Orca began ordering  
22 and purchasing parts for later production by MagTron.

23 During 1991, 300,000 drives were sold worldwide. Competitive forces in the marketplace  
24 drove the retail price for 760 megabyte disk drives down to \$1500 in the summer of 1991. Orca had  
25 wanted to gain a large share of the market. However, by the summer of 1991, Orca had only sold  
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1 several hundred drives.

2 In November 1990, Warner became acquainted with Bisser Dimitrov. Dimitrov had extensive  
3 experience in the disk drive industry in Eastern Europe and, at trial, professed to have been a member  
4 of the KGB, the CIA and the Russian Mafia. When Dimitrov joined Orca in July 1991, his role was  
5 to assist Orca in increasing its market share and in raising additional capital for production. Dimitrov  
6 brought in a group that invested approximately \$3 million in Orca in late 1991 and then occupied a  
7 significant position on Orca's Board of Directors.

8 In November 1991, only six months after the first Falcon drives were ready for shipment, the  
9 market suffered what was described as an "abnormal" price drop for 760 megabyte disk drives. It  
10 became apparent to both Orca and MagTron that the technology was moving to that of the 1.2 gigabyte  
11 disk drive. Orca and MagTron agreed to conclude production of the 760's and to concentrate on the  
12 development of the 1.2's so that Orca's engineers could catch up with its competitors in developing this  
13 technology. The parties signed a written agreement on November 13, 1991, that reduced the number  
14 of 760 megabyte disk drives Orca was required to purchase to a maximum of 750. MagTron agreed  
15 to reduce the wholesale price to \$1,000 for each drive, and Orca waived royalty payments.

16 By January 1992, Dimitrov's investors were upset with the direction Orca was taking since the  
17 money they had invested was spent to purchase materials for production by MagTron. Dimitrov's  
18 investors would only provide more capital if Warner were replaced as CEO. At that point, Warner was  
19 asked to resign by the Board and Peter Kearns became the acting CEO.

20 Despite the change in management, Orca and MagTron continued the negotiations that had  
21 begun the previous September to award MagTron the exclusive right to produce the 1.2 gigabyte disk  
22 drives. Although MagTron and Orca considered sharing profits equally, they drafted an agreement that  
23 was similar to the agreement for the 760's and that included an identical royalty schedule. However,  
24 as Orca's decline became more evident, the draft agreement was never executed by either party.

25 Nonetheless, MagTron and Orca agreed at a meeting in February 1992 to operate under a letter  
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1 of intent. The parties contemplated a joint venture, where Orca's subsidiary, Orca (Europe), and  
2 MagTron would contribute revenue to fund research and development at Orca. The parties  
3 contemplated that MagTron would sell 1.2 gigabyte disk drives to both Orca and Orca (Europe).

4 Kearns acknowledged at the February meeting, which was also attended by Ron Shieh,  
5 MagTron's Vice-President, that Orca owed MagTron about \$285,000. A document, entitled  
6 "Reconciliation of MagTron Inc. and Pacific MagTron accounts of 10 Feb. 1992," shows a balance  
7 owed to MagTron of \$329,003.98 and a balance owed to Orca by MagTron's subsidiary, Pacific  
8 MagTron, of \$37,355.09. The balances were offset to arrive at the net sum of \$284,998.89. Kearns  
9 testified that this document was meant to reconcile the accounts payable and accounts receivable  
10 between Orca and MagTron. Shieh signed on behalf of MagTron, indicating his assent to the  
11 reconciliation.

12 Shortly thereafter, Deardorff, still serving as Orca's Director of Operations, wrote an internal  
13 memo on March 11, 1992, outlining the status of Orca's relationship with MagTron. Deardorff  
14 recognized that the number of 760 megabyte disk drives that could be produced was determined by the  
15 availability of the Adic chip that was "obsoleted" by its supplier prior to Orca's purchase of the Priam  
16 technology. Deardorff also noted that the engineering required to develop the 1.2 gigabyte disk drive  
17 was "substantially more than indicated by the initial 1.2 prototypes," and that significant resources were  
18 needed to make improvements to the yield, which was then only 30%. Deardorff stated that MagTron  
19 had approximately 3500 complete sets of the inventory necessary to produce these drives as of  
20 February 1, 1992. MagTron ultimately produced approximately 800 760 megabyte disk drives, but only  
21 shipped 550 drives to Orca. The record is silent as to MagTron's disposition of the remaining 250  
22 drives. Deardorff acknowledged that after the decision was made to shift production to the 1.2  
23 gigabyte disk drives, the remaining sets of inventory were to be committed to the production of the  
24 1.2's.

25 Thereafter, as reflected in MagTron's invoices through February 10, 1992, MagTron shipped  
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1 110 of the 1.2 gigabyte disk drives to Orca for testing. Deardorff stated in his March 1992 memo that  
2 “in order to expedite the program initial units were shipped to Orca without complete testing . . . .”  
3 Of the 110 drives received by Orca, only forty were shipped to customers because of quality assurance  
4 concerns. Orca introduced into evidence invoices from April, May and July 1992 reflecting that  
5 MagTron sent an additional 242 1.2 gigabyte disk drives to Orca (Europe). Orca never received  
6 royalties for these drives. Dimitrov testified that MagTron displayed Falcon 1.2 gigabyte disk drives  
7 at the Hanover Fair in Germany. However, Dimitrov did not know how many Falcon drives were sold  
8 by MagTron, if any.

9 In attempting to quantify its damages, Orca introduced a memo dated June 3, 1992, wherein  
10 Ron Shieh, a Vice President at MagTron, wrote that MagTron “made over 350 1.2 gigabyte drives to  
11 your [Orca’s] specifications . . . .” Warner estimates that 106 drives were sold by MagTron at the  
12 Hanover Fair, since Orca received invoices for 244 1.2 gigabyte drives, leaving at least 106 of the 350  
13 drives unaccounted for. Warner testified that “we have reason to believe MagTron was selling those  
14 units.” However, Warner did not address whether the initial 110 drives invoiced through February  
15 1992 made up the balance of the 350 drives produced. Based on the record before the court, it is not  
16 clear whether the 106 drives were unaccounted for or whether they were among the initial 110 drives  
17 shipped to Orca for testing.

18 In support of Orca’s position that it could have sold more drives if MagTron had produced  
19 more, Dimitrov testified that he had “hard” orders on the East Coast and in Europe and that he was  
20 selling drives in the thousands. He stated that he had orders “exceeding the numbers which you are  
21 talking about here.” Dimitrov believed he could have sold thousands of Orca’s 760 megabyte disk  
22 drives, since he had sold several thousand similar drives produced by Maxtor.

23 On March 24, 1992, Orca filed its chapter 11 petition, but the principals of Orca and MagTron  
24 continued to explore the possibility of a joint venture. In an April 1992 memo to MagTron, Pacific  
25 MagTron and Orca (Europe), as well as MagTron’s major investor, Chang-Hong Chemical, Kearns  
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1 summarized the current situation of the companies and outlined what was needed to pursue a joint  
2 venture. Kearns recognized that the 1.2 gigabyte disk drives needed additional engineering before  
3 MagTron could produce a commercially saleable product. Kearns suggested establishing a new  
4 company that would keep the current engineering and management team together.

5 Orca and MagTron continued negotiating through May 1992, but an agreement was never  
6 reached. On July 9, 1992, Orca converted its case to a Chapter 7 bankruptcy. MagTron thereafter  
7 dissolved. A proof of claim asserting it was owed \$425,229 was filed on behalf of MagTron in April  
8 1994.

9 The court takes judicial notice of the events surrounding the liquidation of Orca's technology.  
10 In the application for sale, counsel noted that

11 . . . [T]he likely motivation of prospective buyers . . . is either offensive or  
12 defensive; that is, the buyer either intends to commence patent infringement  
13 litigation against hard disc drive manufacturers . . . or the buyer perceives  
14 exposure to an infringement action and wishes . . . to protect itself against  
such a suit. As a consequence, unsuccessful bidders might well fear that  
their bids would identify them as potential targets in infringement suits  
brought by the successful bidder.

15 In order to prevent the potential that fear of a future infringement  
16 action would chill the bidding, the Trustee assured all prospective bidders  
that he was prepared to sell to agents representing undisclosed principals,  
and was otherwise willing . . . to assure the anonymity of all potential  
bidders.

17 It is significant in understanding the dynamics of the competition faced by Orca and MagTron to  
18 recognize the interest in Orca's technology even after its demise.

### 19 **III. Contentions of the Parties**

20 MagTron now asserts a claim for \$336,400, which includes the amount reflected in the  
21 reconciliation in February 1992 that Orca owed MagTron without offsetting the amount that Pacific  
22 MagTron owed Orca, and adding approximately \$7,400 that was invoiced after the reconciliation date.  
23 MagTron contends that the reconciliation is an account stated that releases MagTron from all other  
24 claims related to the sale of drives to Orca and finally determines the amount that is owing between the  
25 parties. However, MagTron asserts that even if the reconciliation did not release all other claims, there  
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1 are no legitimate offsets.

2 Orca asserts numerous offsetting claims in excess of MagTron's claim. Orca claims that  
3 MagTron is liable for the breach of their contract, patent infringement and fraud. Orca calculates more  
4 than \$1 million in offsetting damages against MagTron for the loss of its production line, lost profits,  
5 the value of Orca as a going concern and for unpaid royalties. With respect to the value of the  
6 production line, Orca represents that Priam's book value was \$2,760,000, the estimated replacement  
7 cost was \$1 million and the contract price with MagTron for the purchase of the line was \$325,000.  
8 In support of its position that it is entitled to going concern value and lost profits, Orca provides  
9 estimates from its business plan, a multiple of Orca's revenue, a market share comparison and a  
10 valuation by MagTron. To determine royalties due, Orca provides invoices for an additional 242 1.2  
11 gigabyte disk drives sold to Orca (Europe) by MagTron and an estimate that 106 drives were sold by  
12 MagTron at the Hanover Fair. Orca contends that the various letters and memos indicating Orca's  
13 satisfaction with MagTron's performance were only written to encourage investment by MagTron in  
14 the inventory needed to manufacture the Falcon drives and to enable MagTron to deal more effectively  
15 with its suppliers.

#### 16 IV. ANALYSIS

17 To resolve this matter, the court will consider, in sequential order, the nature of the contract  
18 for the 760 megabyte disk drives, whether a breach of contract occurred, and whether Orca is entitled  
19 to offset its claims for royalties and lost profits against MagTron's claim. However, before analyzing  
20 the agreement document and its terms, it is first necessary to consider whether the parties agreed to an  
21 account stated, releasing all other claims.

##### 22 A. The February 10, 1992 Reconciliation Does Not Release All Other Claims

23 Under California law "[a]n account stated is an agreement, based on the prior transactions  
24 between the parties, that the items of the account are true and that the balance struck is due and owing  
25 from one party to another." *Gleason v. Klamer*, 103 Cal. App. 3d 782, 786-87 (1980); *see generally*  
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1 1 B.E. Witkin, Summary of California Law, Contracts, §917 (9th ed.). An essential element of an  
2 account stated is that both parties have assented to its terms. Restatement (Second) of Contracts §282.  
3 If there is no evidence that both parties agreed to a stated sum, the document is not an account stated.  
4 *See Zinn v. Fred R. Bright Co. Inc.*, 271 Cal. App. 2d 597, 600 (1969) (noting a requisite element of  
5 an account stated is “an agreement between the parties, express or implied, on the amount due from  
6 the debtor to the creditor”). This is particularly true where statements are routinely sent as part of a  
7 continuing business relationship between the parties. *See American Fruit Growers, Inc. v. Jackson*,  
8 203 Cal. 748, 751 (1928).

9 Generally, an account stated is viewed as a new contract and forecloses further dispute as to  
10 the items which comprise the account stated. *See Gleason v. Klamer*, 103 Cal. App. 3d at 787. Since  
11 an account stated constitutes a new contract that supersedes and extinguishes the original obligation,  
12 mutual assent is an essential element. *Id.* at 786-787. However, the parties to an account stated are  
13 not bound as to matters that were not contemplated, even though those matters existed when the  
14 account was stated. *See California Milling Corp. v. White*, 229 Cal. App. 2d 469, 478-79 (1964). To  
15 further complicate the issue, there may be a partial settlement and account stated as to only some  
16 transactions between the parties. *Id.* at 477.

17 Here, there is insufficient evidence to conclude that the principals of Orca and MagTron  
18 intended to treat the February 1992 “reconciliation” as an account stated. The record is devoid of any  
19 reference to a release of other claims. The document entitled “Reconciliation of MagTron Inc. And  
20 Pacific MagTron Accounts” merely acknowledges specified outstanding obligations between Orca,  
21 MagTron and Pacific MagTron. As Peter Kearns testified, the February 1992 document was intended  
22 to reconcile the payables and the receivables between Orca and MagTron. The reconciliation itemizes  
23 the receivables and payables by month, invoice number and invoice amount. The totals are reflected  
24 in the “Monthly Reconciliation Report” of MagTron’s Suspense Account and comprise the balance due  
25 between MagTron and Orca as of February 10, 1992. There is evidence from the minutes of the  
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1 meeting held on February 8-9, 1992, signed by the principals of both Orca and MagTron, that “Orca  
2 acknowledged that at this time monies are due and payable to MagTron. The reconciliation shows a  
3 net figure of circa \$285,000 with circa \$156,000 due now.” On its face, the itemization and the  
4 acknowledgment establish only a reconciliation and not a release of any other claims.

### 5 **B. The Agreement Document Is Not Voidable**

6 “A contract is an agreement to do or not to do a certain thing” and gives rise to an obligation  
7 or legal duty, enforceable in an action at law. *See* Cal. Civil Code §§ 1549, 1427-1428. The California  
8 Civil Code enumerates the essential elements for the existence of a contract under California law:  
9 parties capable of contracting, their consent, a lawful object, and a sufficient cause or consideration.  
10 *See* Cal. Civil Code § 1550. On December 28, 1990, Orca and MagTron entered into an agreement  
11 for the production of 760 megabyte 5 1/4 inch disk drives. The contract is supported by sufficient  
12 consideration since the agreement contemplated the sale of the disk drives by MagTron in exchange  
13 for payment by Orca. The agreement document meets the essential elements for a contract under  
14 California law.

15 Although Orca alleged the contract was voidable because of fraudulent representations  
16 concerning MagTron’s financial wherewithal, Orca did not produce any evidence to establish  
17 MagTron’s financial ability during the relevant contract negotiations or that MagTron misrepresented  
18 its financial ability to purchase components. Without this evidence, the court is not able to find that  
19 MagTron misrepresented its financial ability to Orca.

### 20 **C. MagTron Did Not Breach Its Obligation To Produce 760 Megabyte Disk Drives**

#### 21 **1. MagTron Acted In Good Faith**

22 Every contract imposes upon each party a duty of good faith and fair dealing in its performance  
23 and its enforcement. *See Kendall v. Ernest Pestana, Inc.*, 40 Cal. 3d 488, 500 (1985). The burden  
24 imposed is "that neither party will do anything which will injure the right of the other to receive the  
25 benefits of the agreement." *Gruenberg v. Aetna Ins. Co.* 9 Cal. 3d 566, 573 (1973). The "precise  
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1 nature and extent of the duty imposed . . . will depend on the contractual purposes." *Egan v. Mutual*  
2 *of Omaha Ins. Co.*, 24 Cal. 3d 809, 818 (1979).

3 The best evidence of MagTron's good faith in the production of the 760 megabyte disk drives  
4 comes directly from Orca. In May 1991, Reiser stated that the production exceeded specifications and  
5 performed well. Reiser also stated that Orca "feel[s] very lucky to have made this agreement with  
6 MagTron, especially at such a critical time in the development of Orca Technology." As further proof  
7 of MagTron's good faith, Deardorff wrote MagTron in June, 1991, stating that "implementation of the  
8 process and initial production of the OT5-760 was extremely successful." Although Orca's counsel  
9 suggested that these letters may have been sent merely for the benefit of MagTron's investors, similar  
10 sentiments were expressed by Deardorff in the March 11, 1992 internal memo. Deardorff's memo to  
11 the file outlined the status of Orca's relationship with MagTron and stated that "[t]he core team remains  
12 solid and committed to the success of the program."

13 The record shows that a number of external factors affected MagTron's ability to produce 760  
14 megabyte disk drives. Included among these factors were the rapid changes in technology, the price  
15 reduction for the drives and the unavailability of necessary parts.

16 **2. The Contract Was Modified To Require Orca To Purchase**  
17 **A Maximum Of 750 Of The 760 Megabyte Drives**

18 The agreement document contemplated that Orca would "purchase from MagTron a minimum  
19 of 5000 [760 megabyte] drives the first year of production." Although the terms of the agreement  
20 address Orca's guaranteed purchase of a minimum of 5,000 drives in the first year, the agreement  
21 document is ambiguous as to whether MagTron was required to produce a specified quantity of drives.  
22 Reiser testified that Orca's agreement to purchase 5,000 drives obligated MagTron to produce 5,000  
23 drives, while Ted Li, Operations Manager of Pacific MagTron, testified that MagTron never agreed to  
24 produce a specified number of drives since the viability of production remained uncertain.

25 A contract measuring the quantity of goods by the output of the seller requires actual output  
26 as may occur in good faith. *See* Cal. Comm. Code § 2306. "Where parties contract with reference .

1 . . [to] the output of the seller, there is necessarily a degree of uncertainty of amount. The very  
2 circumstances which make it impossible for the parties to know definitely when the contract is made  
3 how much it will cover makes it necessary for each of them to assume the risk of future events beyond  
4 the control of either when acting in good faith, which may vary the quantity of the subject matter.”  
5 *Oregon Plywood Sales Corp. v. Sutherlin Plywood Corp.*, 246 F.2d 466, 469 (9th Cir. 1957).

6         Considering the circumstances surrounding the negotiation of the agreement document,  
7 including that the contract would only be economically viable if it met certain economies of scale, and  
8 on reviewing the protection clauses afforded to both contracting parties, the court finds that the  
9 agreement document required MagTron to use its best efforts to produce a minimum of 5,000 of the  
10 760 megabyte disk drives. However, implicit in the agreement is the understanding that future events  
11 beyond the control of either party might change the quantity of drives to be produced. *Id.* Although  
12 Dimitrov testified that he had “hard” orders for the 760 megabyte drives, the decision to cease  
13 production of the 760 megabyte drives was mutual. The record demonstrates that continuing  
14 production of the 760 megabyte disk drives would have resulted in losses for both Orca and MagTron  
15 and that there was no prospect of improvement in the market at the time Orca and MagTron agreed  
16 to cease production of the 760's. Good business judgment required that the agreement document be  
17 modified.

18         It is uncontroverted that the agreement document was modified only 11 months after it was  
19 executed, by a written contract, signed by the principals of both Orca and MagTron on November 13,  
20 1991, which reduced the production required to a maximum of 750 of the 760 megabyte disk drives.  
21 Sufficient consideration supported the modification of the agreement document to meet the  
22 requirements of California Civil Code sections 1698(a) and 1550. The modification was supported by  
23 new consideration since MagTron agreed to reduce the price and Orca agreed that no royalty payments  
24 would be required from MagTron. *See In re Mediscan Research, Ltd.*, 109 B.R. 392, 394 (B.A.P. 9th  
25 Cir. 1989).



1 contract, the parties entered into a letter of intent outlining their relationship. Further, the unexecuted  
2 agreement for the 1.2 gigabyte disk drives contemplated a royalty schedule identical to that for the 760  
3 megabyte disk drives. Using the royalty schedule, the royalties due Orca would be \$200 for each of  
4 the 242 1.2 gigabyte disk drives sold by MagTron to Orca (Europe). *See Oshkosh Truck Corp. v.*  
5 *Lockheed Missiles & Space Co.*, 678 F. Supp. 809, 811 (N.D. Cal. 1987) (stating that evidence of the  
6 royalty provision of the License Agreement provided a reasonable basis for the jury's damage verdict  
7 based on unjust enrichment).

8 Royalties on the remaining 106 1.2 gigabyte disk drives claimed by Orca to have been sold at  
9 the Hanover Fair are not awarded because Orca failed to meet its burden of proof. The record is  
10 unclear whether the disputed 106 1.2 gigabyte disk drives were included within the 110 drives  
11 previously shipped to Orca for testing. Further, royalties on the 3500 sets of materials are not awarded  
12 because Orca did not produce evidence that MagTron assembled 1.2 gigabyte disk drives using the  
13 3500 sets of materials.

14 **2. Orca's Claim For Lost Profits On The 1.2 Gigabyte**  
15 **Drive Is Too Speculative To Be Awarded As Damages**

16 Orca also claims that it is entitled to lost profits on the sale of the 350 1.2 gigabyte disk drives.  
17 However, the evidence presented is too speculative for lost profits to be awarded as damages. The loss  
18 of anticipated profits may be awarded only where there is an established business with a satisfactory  
19 basis for estimating probable earnings. *See Postal Instant Press, Inc. v. Sealy*, 43 Cal. App. 4th 1704,  
20 1710 (1996) (holding that lost future profits are only awarded when the court can calculate the amount  
21 with some degree of certainty).

22 An award of damages may not be based upon speculative evidence or mere conjecture. *See*  
23 *Lindy Pen Co., Inc. v. BIC Pen Corp.*, 982 F.2d 1400, 1407-08 (9th Cir. 1993), *cert. denied*, 114 S.Ct.  
24 64 (1993). If the anticipated profits are from a new business to be established, the difficulty of  
25 estimating lost profits has led the courts to classify damages as uncertain and speculative, and to deny  
26 recovery. *See* 1 B.E. Witkin, Summary of California Law, Contracts, § 826 (9th ed.).

1 Orca's evidence as to lost profits for the 350 1.2 gigabyte disk drives based on actual invoices  
2 for the months of April, May, July established a material cost of \$820 per unit. The material costs  
3 provide only an estimate and do not include overhead costs. Without this evidence, the record is  
4 inadequate to determine costs and there is no reasonable basis for computing MagTron's profit for the  
5 sales to Orca (Europe).

6 **V. Conclusion**

7 Orca has satisfied its burden of proving damages for unjust enrichment due to MagTron's sale  
8 of the 1.2 gigabyte disk drives to Orca (Europe) and Orca is entitled to offsetting damages for the sale  
9 of 242 drives at \$200 for each drive, for a total of \$48,400. No other offsetting claims are supported  
10 by the record. MagTron's claim is allowed at \$244,051.09 which is computed as the amount shown  
11 on the reconciliation, \$284,998.89, plus \$7,452.20 invoiced after the date of the reconciliation, less  
12 \$48,400 allowed for damages for unjust enrichment.

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14 Dated:

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16 UNITED STATES BANKRUPTCY JUDGE  
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