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Are Punitive Damages Too Damaging?

by Jill M. Albrecht, Esq.*

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Jill M. Albrecht of Dickie, McCamey & Chilcote in Pittsburgh discusses the ramifications of the U.S. Supreme Court's decision in *Exxon v. Baker*—one of the most famous punitive damage cases in modern history—and the “bad man” principle behind the trend toward reduction of such damages.

The final resolution of *Exxon Shipping Co. v. Baker*, 128 S. Ct. 2605, 171 L. Ed. 2d 570 (2008), perhaps the most famous punitive damage award case in modern history, has brought the issue of punitive damage awards under increased scrutiny.

The courts in this case reduced the initial punitive damage award from \$5 billion to \$500 million over 19 years of appeals. This would appear to be part of a trend in insurance defense cases where the courts have reduced punitive damage awards.

In recent years, many courts have begun applying the “bad man” principle, first enunciated by U.S. Supreme Court Justice Oliver Wendell Holmes. This principle holds that even a bad man should be able to foresee the worst possible consequences of his actions, which the current, freewheeling punitive damage award model does not allow. In other words, the severity of a penalty must be reasonably predictable, even to a “bad man.”

Some states have gone so far as to limit punitive damages to a fixed amount or

an amount equal to the original damages claim, but the states vary widely in their use of this legal penalty.

There is much to discuss when considering the current state of laws on awarding punitive damages, particularly in Pennsylvania. What the most recent decisions mean for future caselaw in Pennsylvania and the federal circuit accounts for much speculation in trends in assessing and enforcing punitive awards.

As state courts grapple with the often controversial punitive damage laws, standards fall across the scale. A recent decision ending *Exxon v. Baker* once again brings punitive damages into the spotlight.

Exxon v. Baker stems from litigation that began after the Exxon Valdez tragedy that occurred off the coast of Alaska in 1989. Eleven million gallons of oil were spilled into the pristine ecosystem of that area, and as a result, a jury originally awarded \$5 billion in punitive damages.

The Ninth U.S. Circuit Court of Appeals eventually reduced the damages amount to \$2.5 billion. Punitive damages were awarded to compensate those individuals affected by the oil spilled when the oil tanker crashed and 1,500 miles of the Alaskan coast were slicked with oil. Of the spilled oil, 35% is said to have evaporated, 40% was deposited on local beaches, and 25% entered the Gulf of Alaska and migrated to the sea.

During the course of this litigation, which has spanned nearly 20 years, the Supreme Court decided *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 123 S. Ct. 1513, 155 L. Ed. 2d 585, 60

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Fed. R. Evid. Serv. 1349, 1 A.L.R. Fed. 2d 739 (2003). This well-known but unusual case stems from a car accident. After the plaintiffs' offer to settle for the \$50,000 policy limit was refused, a jury returned a verdict for more than three times the policy limit.

The verdict included \$2.6 million for the bad-faith claim for the plaintiffs' suffering 1½ years of emotional distress stemming from the "outrage and humiliation" of going through the litigation.

The jury also awarded \$145 million in punitive damages. The trial court reduced these amounts to \$1 million and \$25 million, respectively. The Utah Supreme Court reinstated the \$145 million punitive award, and the U.S. Supreme Court reversed that decision in 2003.

The Supreme Court used three factors in reducing the punitive award: the degree of reprehensibility, the disparity between the harm suffered and the award amount, and the difference between the punitive damages award and the civil penalties authorized or imposed in comparable cases. The high court instructed appellate courts to consider these three factors *de novo*. The most important indicia is the degree of reprehensibility of the defendant.

In this case, the high court instituted a single-digit maximum ratio for civil penalties compared to punitive damages, except in the most exceptional cases. The court said that a penalty must be reasonably predictable in its severity, so even Justice Holmes' quintessential "bad man" would be able to look ahead with some ability to know what the stakes are in choosing a course of action.

This decision brings us to the *Exxon* case, which is different because *State Farm* dealt with a Utah state court that applied substantive state law. The 14th Amendment applied and helped to shape the court's decision. In *Exxon*, the courts dealt with federal maritime law and other federal statutes. The 14th Amendment did not apply since it was a matter of federal common law shaping the judge-made maritime law. In applying the *State Farm* standard to *Exxon*, a punitive-to-compensatory ratio of 1-to-1 yields the maximum punitive damages in that amount.

The result in *Exxon*, with its \$5 billion punitive claim determined by the jury in 1994 (reduced to \$507.5 million in 2008), was the bigger decision. The court's rejection of *Exxon's* motion to throw out punitive damages is another indication that punitive damages are here to stay. This con-

cluded that phase of litigation, which had been in dispute for 19 years after the spill. While the *Exxon* litigation is over, the effect of the decision among the different states is just beginning to show.

As mentioned above, state regulations vary wildly on the scale of punitive damages award amounts. Some states, like Nebraska, do not award punitive damages and consider such awards unconstitutional. Other states, such as Ohio (2-to-1 ratio) and Colorado (1-to-1), limit them in the form of an absolute monetary cap.

It should be noted that punitive damages are higher and more frequent in the United States than anywhere else in the world. In fact, certain foreign countries consider punitive damages to be contrary to public policy.

In Pennsylvania, punitive damages are awarded for torts that are willful, malicious, or so careless as to indicate wanton disregard. Often in the state, the amount of punitive damages awards are left to the jury's discretion. In the state's Third Circuit, the courts have allowed punitive damages in a 7-to-1 ratio. The Third Circuit also considers the guideposts set in *State Farm*, including of the degree of reprehensibility.

In Pennsylvania's surrounding states, punitive awards vary. Ohio allows no punitive damages judgment in excess of twice the compensatory damages award. In the commonwealth of Virginia, the total punitive damages award cannot exceed \$350,000. In West Virginia, the punitive damages award must bear a reasonable relationship to the compensatory damages award.

How all these decisions fit into constitutional due process is a much-debated topic.

Due process is applicable to state court and its imposition of penalties and damages, but what happens with federal questions, as in the *Exxon* matter? It could be argued that any ratio that exceeds 1-to-1 would exceed the limit of the due-process guarantee. However, as it stands, it is up to the developing arguments in state and federal court cases to further limit punitive damages awards.

ENDNOTE

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