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U.S. Supreme Court Provides Guidelines as to Range of Permissible Punitive Damage Awards

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The United States Supreme Court recently provided its most specific guidelines to date as to the constitutionally allowable range of punitive damages in a civil case. In a case in which the compensatory damages were \$1 million and punitive damages were \$145 million, the Supreme Court held that the punitive damages were excessive and violated the United States Constitution. For the first time, the Supreme Court provided some numerical guidelines for determining the size of allowable punitive damages. In so doing, the Court also emphasized that any award of punitive damages must be based upon conduct that harmed the plaintiff and not upon general unsavory business practices.

The case before the Supreme Court, decided on April 7, 2003, was *State Farm Mutual Automobile Ins. Co. v. Campbell*, 123 S. Ct. 1513 (2003). A state court jury in that case had determined that an insurer's decision not to settle an automobile accident case within the policy limits was unreasonable in light of the possibility of an excessive jury award. The jury awarded the plaintiffs \$2.6 million in compensatory damages and \$145 million in punitive damages. The trial court reduced the compensatory award to \$1 million and the punitive award to \$25 million. A state appeals court subsequently maintained the compensatory damage award of \$1 million but reinstated the \$145 million punitive damage award.

On *certiorari*, the Supreme Court found the punitive damage award to be excessive and therefore violative of the Due Process Clause of the 14th Amendment because it served no legitimate purpose and constituted an arbitrary deprivation of property. The Court went on to suggest that, in all but the most egregious cases, punitive damage awards of more than nine times the amount of a plaintiff's compensatory damages do not comply with due process. In so holding, the Supreme Court in *State Farm* appears to have taken a large step toward curbing the abuse of punitive damage claims and reducing the uncertainties facing companies involved in lawsuits in which punitive damages are sought.

Guidelines for Ratio of Punitive Damages to Compensatory Damages

In its ruling, the Supreme Court reiterated three guideposts established by prior case law in reviewing a punitive damages award: (1) the degree of reprehensibility of the defendant's misconduct; (2) the disparity between the actual or potential harm suffered by the plaintiff and the punitive damages award; and (3) the difference between the punitive damages awarded by the jury and the civil penalties authorized or imposed in comparable cases.

In discussing the second guidepost, the Supreme Court for the first time set forth guidelines as to permissible ratios between actual damages and punitive damages. While declining to provide a bright-

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line test, the Court noted that in practice, a “single-digit ratio” between punitive damages and compensatory damages is usually the amount that will be constitutionally acceptable. The Supreme Court stated that a “single-digit” multiplier comports with due process considerations and achieves the state’s goals of deterrence and retribution. It thus appears that, as a general rule, punitive damages must be no more than a multiple of nine times an award of compensatory damages to satisfy due process. While the Court noted that greater ratios may be acceptable when “a particularly egregious act results in only a small amount of economic damages,” it similarly noted that when compensatory damages are substantial, smaller ratios, “perhaps only equal to compensatory damages,” are required.

In discussing the appropriate ratio for punitive damages, the Court held that courts must ensure the measure of punishment is both reasonable and proportionate to the amount of harm to the plaintiff and to the general damages recovered. Where the compensatory award includes a component for emotional distress, the reviewing court must recognize that the punitive damages might likely be duplicated in the compensatory damages.

The foregoing guidelines will hopefully bring some order to what has heretofore been the “wild card” law of punitive damages. In all but the rare case, a ratio of no more than 9:1 should define the outer limits by which punitive damages may exceed compensatory damages. As articulated by the Supreme Court, if compensatory damages are large, that ratio should decrease; if compensatory damages are small, then the ratio may approach that outer limit.

Nature of Conduct Subject to Punishment

In addition to establishing some much-needed guidance regarding permissible amounts of punitive awards, the *State Farm* Court addressed the type of conduct which may permissibly be sanctioned. In this regard, the Court stated that the most important factor in determining the reasonableness of a punitive damages award is the degree of reprehensibility of the defendant’s misconduct. In determining reprehensibility, courts must consider whether: the harm caused was physical as opposed to economic; the tortious conduct evinced an indifference to or a reckless disregard of the health or safety of others; the target of the conduct had financial vulnerability; the conduct involved repeated actions or was an isolated incident; and the harm was the result of intentional malice, trickery, or deceit, or merely an accident. The mere existence of any one of these factors may not be sufficient to sustain an award of punitive damages, and the absence of all of these factors renders a punitive damages award suspect.

Importantly, the Supreme Court held that when a state court awards punitive damages to punish a corporation with operations throughout the United States, the court must be careful to punish the corporation only for its actions that harmed the plaintiff. A state court cannot punish a corporation for its out-of-state actions nor for its actions that bear no relation to the plaintiff’s harm. With respect to out-of-state actions, the Court reiterated its prior holding that a state cannot punish a defendant for conduct that may have been lawful where it occurred. The Court further noted that as a general rule, a state does not have a legitimate concern in imposing punitive damages to punish a defendant for acts committed outside of the state’s jurisdiction even if they are unlawful. Finally, the Court held that a defendant’s dissimilar acts, whether in-state or out-of-state, independent from the acts upon which liability was premised, may not serve as the basis for punitive damages. Due process does not permit courts, in the calculation of punitive damages, to adjudicate the merits of other parties’ hypothetical claims against a defendant under the guise of the reprehensibility analysis. Punishment on these bases creates the possibility of multiple punitive damages awards for the same conduct.

The Court’s rulings should go a long way toward curbing present discovery and evidentiary abuses in cases including a claim for punitive damages. Plaintiff’s counsel will doubtless argue that the Supreme Court has expressly observed that actions other than those directed to plaintiff may be probative when they demonstrate the deliberateness and culpability of a defendant’s actions toward plaintiff; however, the Court’s opinion gives defendants a lot of ammunition to support the exclusion of such evidence in most instances.

Conclusion

While the full impact of the *State Farm* decision remains to be determined, it appears clear, at a minimum, that the Supreme Court has taken a big step toward curbing the abuse of punitive damages and the corresponding leverage such claims currently provide to plaintiffs.

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