

'Diamond' Errs in Application of 'Campbell' Damages Rules

Diamond Woodworks v. Argonaut Insurance Co., 109 Cal.App.4th 1020 (2003), is the first published decision in California to apply the standards for appellate review of punitive-damages awards announced by the U.S. Supreme Court in State Farm Mutual Automobile Insurance Co. v. Campbell, 123 S.Ct. 1513 (2003).

Diamond discerned in Campbell a constitutionally based 4-1 ratio between punitive and compensatory damages, even though Campbell expressly refused to adopt such a rigid ratio. But a review of Campbell and the decisions preceding it shows that the U.S. Supreme Court has neither suggested nor imposed a 4-1 ratio.

Diamond involved claims of fraud, breach of contract and insurance bad faith. Diamond Woodworks alleged that Argonaut Insurance improperly refused to defend or indemnify it for a workers' compensation claim, falsely claiming that its policy did not cover it.

The jury awarded Diamond Woodworks compensatory damages of \$424,100 and punitive damages of \$14 million for Argonaut's fraud. After Diamond Woodworks accepted the trial court's remittitur, the court entered judgment against Argonaut for compensatory damages of \$404,270 and punitive damages of \$5.5 million.

The Court of Appeal affirmed the judgment of fraud but determined that both the compensatory-damages award and the punitive-damages award should be further remitted. In adopting a 4-1 ratio between punitive and compensatory damages, the Diamond court first discussed the Campbell decision.

Diamond noted that Campbell declined to adopt a bright-line ratio; however, the Court of Appeal also noted that the Campbell court observed that earlier U.S. Supreme Court cases demonstrated that, in practice, "few awards exceeding a single-digit ratio between punitive and compensatory damages, to a significant degree, will satisfy due process."

Diamond next stated that the Campbell court - alluding to its decision in Pacific Life Insurance Co. v. Haslip, 499 U.S. 1 (1991), and a 700-year legislative history providing for sanctions of double, treble or quadruple damages - repeated the statement in Haslip that a punitive-damages award of more than four times compensatory damages "might be close to the line of constitutional impropriety."

Finally, Diamond mentioned that Campbell observed that the facts of a particular case could warrant a punitive-damages award that either exceeded or fell below the norm. Therefore, the Supreme Court advised state courts to ensure that the measure of punitive damages is reasonable and proportionate to the amount of harm to the plaintiff and the general damages recovered.

The Diamond court then endeavored to apply Campbell to the facts before it. The Court of Appeal went astray, however, in its effort to synthesize the principles that it had discussed.

The Diamond court acknowledged that the jury had found that Argonaut's conduct was fraudulent and reprehensible and deserved significant punitive damages. But the Court of Appeal concluded that the 13-1 ratio between compensatory and punitive damages, which increased to 21-1 after the compensatory

damages were remitted, was excessive.

The key paragraph in Diamond states, "Campbell, [BMW of North America Inc. v. Gore, 517 U.S. 559 (1996)] and Haslip all suggest that in the usual case, i.e., a case in which the compensatory damages are neither exceptionally high nor low, and in which the defendant's conduct is neither exceptionally extreme nor trivial, the outer constitutional limit on the amount of punitive damages is approximately four times the amount of compensatory damages. Taking into account the jury's determination in this case, we conclude that the ratio should approximate that outer limit."

However, neither Campbell, nor the decisions in Haslip or Gore, supports the 4-1 ratio adopted by Diamond. The pre-Campbell decisions concerning the outer limits of punitive damages did not plot a consistent arc, and Campbell did not bring absolute clarity to the field. But Campbell was clear in rejecting the type of bright-line ratio that the Diamond court adopted, stating that "[w]e decline again to impose a bright-line ratio which a punitive damages award cannot exceed."

The next sentence in the Campbell decision says, "Our jurisprudence and the principles it has now established demonstrate, however, that, in practice, few awards exceeding a single-digit ratio between punitive and compensatory damages, to a significant degree, will satisfy due process."

While the 4-1 ratio in Diamond is a "single-digit ratio," there is no reason to believe that this is the ratio that the Supreme Court had in mind when it made the statement above. Rather, by "single-digit ratio," the court likely was referring to ratios below 10-to-1.

Gore explains this, noting that the Supreme Court in TXO Production Corp. v. Alliance Resources Corp., 509 U.S. 443 (1993), affirmed a punitive-damages award that was 526 times the amount of compensatory damages. However, as explained by Gore, when potential harm to the TXO plaintiff was taken into account, "the relevant ratio was not more than 10 to 1."

Campbell cites TXO with approval, explaining that "we have consistently rejected the notion that the constitutional line is marked by a simple mathematical formula, even one that compares actual and potential damages to the punitive award." The ratio adopted in Diamond cannot be squared with these decisions.

Diamond relied on Campbell's reference to the Supreme Court's statement in Haslip that a punitive-damages award greater than four times the amount of compensatory damages "might be close to the line of constitutional impropriety." But a closer examination of Haslip and the cases decided after it shows that the Supreme Court neither adopted a 4-1 ratio, nor provided support for its use.

The Haslip award consisted of \$200,000 in compensatory damages and \$840,000 in punitive damages. Hence, the ratio of punitive to compensatory damages was slightly more than 4-1. But the central issue in Haslip was not whether the punitive-damages award was excessive. Rather, it was whether it was proper to impose punitive damages on an innocent employer based on respondeat superior.

Haslip involved the liability of an insurer for defalcations by an insurance agent. The court held that imposing liability upon the insurer for its agent's fraud under respondeat superior did not, based on the facts, violate due process.

The Haslip court disposed of the insurer's due-process challenge to the amount of the punitive-damages award in a single paragraph, stating that since the 4-1 ratio in the case was more than 200 times the plaintiff's out-of-pocket expenses and much in excess of the possible fine for insurance fraud, it "may be close to the line." But since the award was based on objective criteria, the Haslip court held that it did not cross the line

into constitutional impropriety.

In *Gore*, the court characterized its statement in *Haslip* concerning a 4-1 ratio as "dicta" and explained that *TXO* "refined this analysis by confirming that the proper inquiry is "whether there is a reasonable relationship between the punitive damages award and the harm likely to result from the defendant's conduct as well as the harm that actually has occurred.'" *Gore* noted that when the potential harm was factored into the ratio between compensatory and punitive damages, the *TXO* ratio was only 10-1.

Gore, like all the Supreme Court's punitive-damages decisions, expressly declined to adopt a bright-line ratio, stating that "[w]e need not, and indeed we cannot, draw a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable."

Instead, the *Gore* court observed that *Haslip* had noted that the 4-1 ratio "might" be "close" to the line but was not improper and that the *Haslip* approach was refined in *TXO*, which approved an award amounting to a 10-to-1 ratio.

In sum, neither *Campbell*, nor the cases preceding it, supports the adoption of a categorical 4-1 ratio. Rather, the most that reasonably can be deduced from *Campbell* and its predecessors is that punitive-damages awards that exceed a 10-1 ratio "by a significant degree" will be constitutionally suspect.

The *Diamond* court, however, ignored the *Campbell* court's instruction that there are "no rigid benchmarks" for punitive-damages awards and that "the precise award in any case, of course, must be based upon the facts and circumstances of the defendant's conduct and the harm to the plaintiff."