

## Punishing Patterns Of Misconduct

By William Shernoff and Joel Cohen

In *TXO Production Corp. v. Alliance*, the United States Supreme Court approved a punitive damage ratio of 526 to 1 for a pattern of misconduct. The jury found that TXO engaged in a fraudulent scheme to deny Alliance's title to property that contained valuable oil and gas rights. The jury awarded Alliance \$19,000 in compensatory damages and \$10 million in punitive damages.

On certiorari to the Supreme Court, TXO argued that the \$10 million punitive damages award violated due process. The Supreme Court rejected TXO's argument and concluded that the ratio was merely part of a broader analysis: "For instance, a man wildly fires a gun into a crowd. By sheer chance, no one is injured and the only damage is to a \$10 pair of glasses. A jury reasonably could find only \$10 in compensatory damages, but thousands of dollars in punitive damages to teach a duty of care. We would allow a jury to impose substantial punitive damages in order to discourage future bad acts."

The Supreme Court continued: Taking account of the potential harm that might result from the defendant's conduct in calculating punitive damages was consistent with the views we expressed in *Haslip, supra*. In that case we endorsed the standards that the Alabama Supreme Court had previously announced, one of which was "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."

Thus, *TXO* established a powerful precedent for augmenting the baseline compensatory damage calculation, by including actual and potential harm, and for multiplying the award of punitive damages based on evidence of a corporate defendant's similar tortious conduct causing harm to others.

In recent years, however, courts have turned more frequently to subsequent Supreme Court discussions of punitive damage calculations, most notably *State Farm Mutual Insurance Co. v. Campbell* and *Philip Morris USA v. Williams*. But neither *Campbell* nor *Williams* call into question *TXO*'s analysis. In fact, both decisions reaffirm its vitality. When contemplating punitive damages awards in instances of widespread corporate misconduct with potential harm to others, courts must embrace *TXO* and reach punitive damages awards that fit the nature and scope of the wrongdoing.

Neither *Campbell* nor *Williams* dispute this point.

*Campbell* arose from a third party insurance action against State Farm's insureds. The Campbells sued State Farm for refusing to settle the third party action, which exposed them to a judgment exceeding policy limits. The Campbells were awarded \$1 million in compensatory damages and \$145 million in punitive damages. The Supreme Court reversed.

First, the punitive award reflected punishment of State Farm for supposed misconduct in other parts of the country that was dissimilar to the type of conduct that harmed the Campbells and not unlawful where it occurred. The Supreme Court cited with approval *TXO*'s statement that it is proper to consider a defendant's conduct, which is similar to the conduct that harmed the particular plaintiff. But there was little evidence of repeated misconduct of the sort that harmed the Campbells.

Second, the Supreme Court found the 145 to 1 ratio of punitive damages was not reasonable. The Campbells were awarded \$1 million for 18 months of emotional distress for an economic injury that State Farm ultimately paid. Further, there was no evidence of similar conduct directed at others. In its decision, the Supreme Court stated that single-digit multipliers are more likely to satisfy due process. However, again citing *TXO*, the Supreme Court reiterated that it would not set a "brightline ratio which a punitive damages award cannot exceed." Rather, the award must be based on the facts and circumstances of each case.

*Williams* arose from a wrongful death action against Philip Morris. The jury found that Phillip Morris engaged in deceitful marketing of cigarettes. The plaintiff argued that the jury should consider not only the harm caused to the plaintiff but also the harm caused to other Oregon smokers who used Philip Morris' products. The jury awarded \$79.5 million in punitive damages and compensatory damages of approximately \$821,000, a ratio of nearly 97 to 1.

The Supreme Court reversed, finding that the trial court should have given a jury instruction specifying that Philip Morris could not be punished for harm caused to other smokers who were not parties to the action. However, it was a Pyrrhic victory for Philip Morris because the Supreme Court also held that the identical evidence was proper for the jury to consider in evaluating the *reprehensibility* of Philip Morris' conduct. "[W]e recognize that conduct that risks harm to many is likely more reprehensible than conduct that risks harm to only a few. And a jury consequently may take this fact into account in determining reprehensibility."

As part of its discussion, the Supreme Court again (as in *Campbell*) cited *TXO's* holding that consideration of potential and actual harm to others is constitutionally permissible.

On remand, the Oregon Supreme Court held that Philip Morris' proposed jury instruction did not comport with Oregon law and reaffirmed the punitive damages award. The Supreme Court initially granted certiorari but later dismissed the case. As a result, the ratio of 97 to 1 stands.

As can be seen, properly understood, neither *Campbell* nor *Williams* detract from *TXO's* analysis, where a pattern of wrongdoing that harms others is shown. The High Court continues to refuse to set any "brightline" rule limiting the ratio of punitive to compensatory damages. Indeed, the compensatory damages calculation properly includes actual and potential damages - which may well lead to a substantial baseline for damages before even considering how much of a multiplier should be applied to the punitive award. Additionally, evidence of a defendant's similar misconduct directed at others is clearly admissible and properly considered by the jury in evaluating the reprehensibility of a defendant's conduct.

The California Supreme Court also supports the conclusion that a pattern of misconduct by a defendant is a significant factor in justifying a large punitive damage ratio. In the post *Campbell* decision of *Johnson v. Ford Motor Co.*, the trial court found that Ford committed fraud and violated consumer laws by concealing from the plaintiff the history of repairs that had been made to his automobile's transmission. The jury awarded nearly \$18,000 in compensatory damages and \$10 million in punitive damages. Based on *Campbell*, the Court of Appeal reduced the punitive award to approximately \$53,000, about three times the amount of the compensatory damages.

The Supreme Court reversed, stating: "California law has long endorsed the use of punitive damages to deter continuation or imitation of a corporation's course of wrongful conduct, and hence allowed consideration of that conduct's scale and profitability in determining the size of award that will vindicate the state's legitimate interests." The appellate court had not "adequately considered how the scale and profitability of Ford's repeated conduct reflects on its reprehensibility." The Supreme Court distinguished *Campbell* because, in that case, it was improper to consider evidence of business practices that were dissimilar to the conduct that harmed the plaintiffs. Moreover, while *Campbell* requires that there be a reasonable ratio between punitive and compensatory damages, the High Court also recognized that reasonableness varies according to the individual case and that repeated wrongful conduct requires "strong medicine" to deter its continuation.

On the same day that *Johnson* was filed, the Supreme Court also filed its opinion in *Simon v. San Paolo U.S. Holding Co., Inc.* In *San Paolo*, the plaintiff sued the defendant company for breach of contract and fraud in connection with a letter of intent for the plaintiff's purchase of commercial real property. The jury awarded \$5,000 in compensatory damages and \$1.7 million in punitive damages. The Supreme Court found that the 340 to 1 ratio between punitive and compensatory damages was constitutionally excessive. The facts demonstrated a single fraud, with no evidence of similar misconduct directed at others, causing

\$5,000 in economic harm to the plaintiff. As such, \$50,000 in punitive damages, a ratio of 10 to 1, was the maximum permissible award that satisfied due process.

In *San Paolo* the Supreme Court, again, stated that *Campbell* did not place a constitutional limit of 10 to 1 on the ratio of punitive to compensatory damages. It also agreed, citing *TXO*, that potential harm is properly considered in calculating compensatory damages.

The resolutions in *Johnson* and *San Paolo* are also instructive. In *Johnson*, on remand from the Supreme Court, the Court of Appeal awarded punitive damages of \$175,000, almost 10 times the amount of compensatory damages. The nearly double-digit multiplier is significant because the Supreme Court found there was no evidence of actual harm to others. In *San Paolo*, the Supreme Court ordered a double-digit ratio of punitive to compensatory damages *in the absence of* potential harm to the plaintiff and a pattern of similar misconduct by the defendant. Thus, it appears, in appropriate cases in California, a 10 to 1 ratio might be viewed as a threshold for a punitive damages award, not a limit.