Legal Backgrounder

WLF Washington Legal Foundation

Advocate for freedom and justice®
2009 Massachusetts Avenue, NW
Washington, DC 20036
202.588.0302

Vol. 23 No. 4 February 22, 2008

EXXON SHIPPING PROVIDES COURT WELCOME OPPORTUNITY ON EXCESSIVE PUNITIVE DAMAGES

by

Evan M. Tager

Nineteen years ago, the *Exxon Valdez* ran aground on a reef in Prince William Sound, Alaska, spilling millions of gallons of oil and significantly damaging the ecosystem as well as the livelihoods of local fishermen. Although Exxon cleaned up the damage and paid hundreds of millions of dollars to compensate the fishermen for their economic losses, the inevitable class action was filed and a jury of Alaskans imposed a recordbreaking $5 billion punitive award. After several appeals and remands, the U.S. Court of Appeals for the Ninth Circuit eventually reduced the punitive award to a still recordbreaking $2.5 billion. In October 2007, the Supreme Court granted Exxon's petition for certiorari. The Court agreed to hear three issues: (i) whether, under maritime law, a ship owner can be vicariously liable for punitive damages based on the reckless conduct of the ship's captain; (ii) whether the remedial provisions of the Clean Water act preclude the imposition of punitive damages under federal maritime law; and (iii) whether the punitive damages are excessive under federal maritime law.

Some members of the media and the business community have minimized the significance of the grant of certiorari because the Court did not also agree to decide whether the punitive award is *unconstitutionally* excessive. But I think that the case holds the potential for a broadly applicable decision that could help rein in punitive damages in all cases, not just maritime ones.

To begin with**,** I would not read anything negative into the Court's decision not to grant review of the constitutional issue. The simplest explanation for that decision is that maritime law gives the Court all of the authority it needs to strike down this punitive award as excessive, making constitutional law entirely redundant. Put another way, it is inconceivable that the Court would hold that the $2.5 billion punitive award passes muster under maritime law, but nonetheless is unconstitutionally excessive. Hence, it is likely that the Court simply saw no point to having the parties brief an issue that would not in the end make any difference.

To me, this means not only that the Court hasn't given up on the Due Process Clause but also that whatever it says about excessiveness under maritime law could very well have spillover effects in cases involving state-law excessiveness, excessiveness under federal statutes, and constitutional excessiveness. After all, if the Court reaches the excessiveness issue in *Exxon Shipping*, it is hard to imagine that it will

---

Evan M. Tager is a partner in the Washington, D.C. office of Mayer Brown LLP. Along with his partner Andy Frey, Mr. Tager has been at the forefront of the development of the law of punitive damages in the Supreme Court. Tager and Frey authored an *amicus* brief for a coalition of organizations led by the American Petroleum Institute in the case that is the subject of this LEGAL BACKGROUNDER.

come up with an entirely different framework for evaluating excessiveness under federal maritime principles than it has painstakingly developed for due process cases. Indeed, although the Court in 1989 rejected the argument that the Eighth Amendment's Excessive Fines Clause places limits on private punitive damages awards (*see Browning-Ferris Indus. of Vt., Inc. v. Kelco Disposal, Inc.*, 492 U.S. 257 (1989)), it has borrowed from its Eighth Amendment jurisprudence when articulating the due process limits on punitive damages (*see, e.g., Cooper Indus., Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424, 433-35 (2001); *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 575-76 & n.24 (1996)). It would therefore not be at all surprising for the Court to borrow principles from due process, Eighth Amendment, and common-law cases when articulating the federal maritime limits on punitive damages. If it does so, it should follow that whatever it says on the subject would be relevant outside of the maritime context.

In short, *Exxon Shipping* provides the Court with an opportunity to continue refining the standards applicable to determining whether a punitive award is excessive—whether under federal statutory law, federal common law, state law, or the due process clause. Indeed, because the Ninth Circuit's decision is replete with the kinds of analytical and conceptual errors that characterize cases that have upheld outsized punitive awards, if the Supreme Court reaches the excessiveness issue, its decision could have a more far-reaching impact than any of its previous forays into this area.

As I see it, the Ninth Circuit's most fundamental error was its failure to identify the standard for excessiveness. The Ninth Circuit's attempt to apply the three excessiveness guideposts set out by the Supreme Court in *BMW* was totally disconnected from any notion of what excessiveness means. Yet a meaningful standard for excessiveness is readily discernible from the Supreme Court's prior punitive damages opinions, cases addressing excessiveness under federal statutes and state common law, and basic logic: *A punitive award is excessive (whether under maritime law or otherwise) if it is greater than reasonably necessary to accomplish the governmental interests in deterrence and retribution*. A decision that makes this much crystal clear would go a long way toward constraining large punitive awards, as the Ninth Circuit is far from alone in failing to recognize that a punitive award that goes beyond the amount necessary to deter and punish is illegitimate and should be struck down.

Moreover, once the ultimate inquiry is clarified, it should be a simple matter to identify the questions courts should ask when undertaking that inquiry. In our amicus brief in *Exxon Shipping*, we identify (and apply) seven considerations that should be relevant in most cases involving organizational defendants. Note that some of these considerations overlap with the three *BMW* guideposts. Importantly, however, taken together they are much more focused on determining whether the punitive award exceeds the amount necessary to punish and deter than are the *BMW* guideposts, at least as those guideposts have been applied by most courts.

1. ***What is the conduct that is being punished?*** It is impossible to determine whether a punitive award exceeds the amount that is reasonably necessary to punish and deter without first clearly identifying the conduct that is being punished. In making that determination, courts should not simply accept the inferences that the plaintiff asked the jury to draw, as the Ninth Circuit did in *Exxon Shipping*. Instead, absent an express finding by the jury, courts should independently evaluate the evidence when identifying the punishable conduct. For example, in *Exxon Shipping* the Ninth Circuit assumed that Exxon knowingly put a relapsed alcoholic in charge of a tanker in dangerous waters, because that was the inference that the plaintiffs asked the jury to draw from evidence that Exxon knew that Captain Hazelwood had received a diagnosis of "alcohol abuse–episodic" and had been seen drinking socially on two occasions when he was off duty.[1] But that assumption is untenable both procedurally and logically. The jury was permitted to impose punitive damages against Exxon if it found that Hazelwood was reckless, so there is no reason to suppose that it found anything more than that. Even putting this obvious flaw in the Ninth Circuit's analysis aside, it is untenable to assume that Exxon entrusted Hazelwood with command of the Exxon Valdez with

[1] "Alcohol abuse–episodic" is a very different thing from alcoholism. The former description applies to many perfectly functional adults; the fact that someone with that diagnosis has had a few drinks is not a red flag.

knowledge that he was a relapsed alcoholic. No rational economic actor would risk millions of dollars of valuable cargo, a vessel worth many times that, and the lives of crew members by allowing an alcoholic to pilot the vessel in dangerous waters. At some point, a court has to say that, at least for purposes of punitive damages, absurd inferences will not be countenanced.

2. ***How wrongful was the conduct?*** This consideration entails determining the level of moral opprobrium that should attach to the defendant's conduct, placing particular weight on the defendant's state of mind. In *Exxon Shipping*, for example, the decision not to terminate an employee with a diagnosis of "alcohol abuse–episodic" cannot reasonably be treated as morally repugnant. Tempting though it may be to demonize Exxon because of the damage that befell Prince William Sound, Exxon did not deliberately contaminate that ecosystem; nor did it knowingly put that ecosystem at risk in a callous effort to save money. Objectively viewed, the decision to retain Captain Hazelwood, if wrongful at all, falls on the low end of the spectrum of reprehensibility—paling in comparison to virtually every other tort for which punitive damages are awardable. Yet applying the five reprehensibility factors identified by the Supreme Court in *State Farm Mutual Automobile Insurance Co. v. Campbell*, 538 U.S. 408 (2003), in checklist-like fashion, the Ninth Circuit managed to conclude that the reprehensibility of Exxon's conduct was in the "mid range." A holding by the Supreme Court rejecting the Ninth Circuit's conclusion would send a strong signal to lower courts to stop applying the reprehensibility factors in wooden fashion and instead to focus more directly on whether the defendant had an iniquitous state of mind.

3. ***Who committed the conduct?*** Companies can act only through their employees and management. Yet a punitive award against a company is borne by its shareholders, its workforce, and ultimately consumers of its products or services. Hence, it is both misguided and counterproductive to treat the company itself as the wrongdoer whose conduct needs to be punished. The right question instead is: "What is the amount of punitive damages needed to deter the person(s) within the company who perpetrated the tortious conduct?" In *Exxon Shipping*, the decision to retain Hazelwood was made by the president of Exxon Shipping. He may rank high in the corporate hierarchy, but there is little reason to think that a $2.5 billion exaction against the corporate parent's shareholders is necessary to change the conduct of the subsidiary's president. A statement to this effect by the Supreme Court could help focus lower courts on the extent to which a large punitive award really is needed to change the conduct at issue.

4. ***To what extent do compensatory damages, fines, and other costs borne by the defendant as a result of its conduct already satisfy the goals of deterrence and retribution?*** It is a matter of common sense—and has been recognized by the Supreme Court, other courts, and commentators—that conduct can be deterred and punished by means of compensatory damages, awards of attorneys' fees, fines, injunctions, and other costs (such as reputational harm) borne by a defendant as a result of its conduct. *Exxon Shipping* is the best imaginable illustration of the point. Exxon incurred over $3.4 billion in damages, settlements, remediation costs, and fines as a result of the spill. It also took a massive reputational beating. When these costs of the decision to allow Hazelwood to continue commanding oil tankers are considered, the conclusion should be self-evident that anything more than a nominal amount of punitive damages exceeds the amount *necessary to deter and punish*.

5. ***What penalties have the expert regulatory agencies determined to be appropriate to punish and deter the same or similar conduct?*** Another important indicium of whether a punitive award is greater than reasonably necessary to punish and deter is the penalties that expert regulatory agencies (and/or prosecutors) have imposed for the same or similar conduct. These agencies have the funding, expertise, investigative tools, knowledge of the law, and familiarity with the range of punishable conduct and with the consequences of overdeterrence to make a well-informed determination of the proper amount of punishment for particular conduct. Absent evidence of corruption or fraud on the agency, a punitive award that exceeds the fines imposed by the expert agencies (and/or prosecutors) for the same or similar conduct generally should be deemed to exceed the amount that is reasonably necessary to deter and punish. In *Exxon Shipping*, the punitive damages set by the Ninth Circuit exceed the fines collectively agreed on and imposed by the United

States and the State of Alaska by $2.375 billion. That is a compelling indication that the punitive award exceeds (by billions) the amount necessary to punish and deter.

6. ***How does the punitive award compare to prior punitive awards for comparable or more egregious conduct?*** Courts also should compare the punitive award to exactions imposed for comparable or more egregious conduct. If a punitive award is materially higher than punishments for similar or more egregious conduct, that is a powerful indication that it exceeds the amount necessary to punish and deter. For example, the punitive award in *Exxon Shipping* is $1.3 billion greater than the prior record holder, which was imposed in a class action against the Marcos regime alleging kidnapping, torture, and murder. A statement by the Supreme Court endorsing a comparative approach would help "'assure the uniform general treatment of similarly situated persons that is the essence of law itself'" (*Cooper Indus.*, 532 U.S. at 436 (quoting *BMW*, 517 U.S. at 587 (Breyer, J., concurring))).

7. ***Is the punitive award disproportionate to the harm to the plaintiff(s)?*** The Supreme Court has consistently observed that, when compensatory damages are not "small," a punitive award that is a substantial multiple of the harm or potential harm to the plaintiff is presumptively excessive. The converse, however, is not necessarily true: Even if a punitive award is a small multiple or (even a fraction) of the harm to the plaintiff, the factors discussed above may still indicate that it is excessive. *Exxon Shipping* is a perfect example. A punitive award that is equal to the harm to the plaintiff class (as measured by the Ninth Circuit)—*i.e.*, $504.1 million—would still be excessive because such an exaction would far exceed the amount that is reasonably necessary to punish and deter, given the non-iniquitous nature of the conduct, the massive costs already borne by Exxon, the fines that state and federal prosecutors deemed appropriate, and other factors discussed above. A statement to this effect would be enormously helpful when, as is becoming increasingly common, a jury has awarded a large amount of non-economic damages and/or attorneys' fees.

The discerning reader may recognize that this list of factors does not include the tortfeasor's financial condition. Most economists agree that an organizational defendant's financial condition is not relevant to the amount needed to punish and deter. Although the Supreme Court has thus far avoided enshrining the law-and-economics view as a due process rule, it has much greater leeway to reject the use of wealth under maritime law. Accordingly, this case presents the best opportunity to date for a clear statement by the Court that an organizational defendant's wealth should not be used in setting punitive damages.

In sum, although not a due process case, *Exxon Shipping* has the potential to provide greater constraints on punitive damages than any of the cases that have preceded it.

  ISBN 1056 3059