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REPORT FROM WASHINGTON

The Supreme Court Limits Punitive Damages Award In The *Exxon Valdez* Case To 1:1 Ratio To Compensatory Damages

June 27, 2008

TO VIEW THE SUPREME COURT'S OPINION IN *EXXON SHIPPING CO. V. BAKER*, NO. 07-219, — S. CT. —, 2008 WL 2511219 (JUNE 25, 2008), PLEASE CLICK HERE.

In a closely-watched case this week, *Exxon Shipping Co. v. Baker*, No. 07-219, — S. Ct. —, 2008 WL 2511219 (June 25, 2008), a 5-3 majority of the Supreme Court vacated a $2.5 billion punitive damages award, and instead limited punitive damages to a ratio no greater than 1:1 to the compensatory damages in federal maritime cases. The Court's holding does not apply directly to awards of punitive damages in state law cases and did not involve application of the Due Process Clause. State law governs punitive damages in all but rare cases, although subject to the limits of constitutional due process. Nevertheless, the Court's analysis may provide significant insight into its thinking regarding restrictions that should be placed on punitive damages awards more generally.

BACKGROUND

The *Exxon* case arose from well-known facts: In 1989, the *Exxon Valdez* supertanker ran aground off the Alaska coast and spilled millions of gallons of crude oil into Prince William Sound. The spill occurred after the tanker's captain, who had been drinking heavily, piloted the tanker into treacherous waters and then inexplicably left the bridge. Exxon had been aware that the captain had a history of alcohol abuse.

Exxon spent approximately $2.6 billion in cleanup efforts, and paid approximately: (i) $125 million for criminal violations of the Clean Water Act, Refuse Act, and Migratory Bird Treaty Act; (ii) $900 million under a consent decree with the United States and the State of Alaska for environmental damage; and (iii) $303 million in voluntary settlements with some fishermen, property owners, and other private parties. The remaining civil cases, brought by commercial fishermen, Native Alaskans, and landowners, were consolidated into a class action with over 32,000 class members.

At trial, Exxon stipulated that it had been negligent and was responsible

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(Opinion of the Court)

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(Opinion of the Court)

for compensatory damages resulting from the spill. Plaintiffs argued that the company had been reckless, and should be liable for punitive damages. In all, the district court calculated total relevant compensatory damages to be $507.5 million, and the jury awarded punitive damages of $5 billion against Exxon.

The Ninth Circuit agreed with the district court that Exxon could be liable under federal maritime law for punitive damages arising from acts of its managerial agents, but remitted the award to $2.5 billion under Supreme Court precedent holding that excessive punitive awards violate due process. The Supreme Court decided to hear the case to consider three issues: (i) whether maritime law allows corporate liability for punitive damages on the basis of acts of managerial agents, (ii) whether the Clean Water Act forecloses any award of punitive damages in maritime spill cases, and (iii) whether the punitive damages awarded against Exxon were excessive as a matter of maritime law.

THE DECISION

Justice Souter's majority opinion, which was joined in by Chief Justice Roberts and Justices Scalia, Kennedy, and Thomas, held that the punitive damages award in the case could not exceed a ratio of 1:1 to the compensatory damages, or $507.5 million.[1] The decision reflects the Court's strong desire to eliminate the uncertainty that defendants face in connection with claims for punitive damages.

Because maritime law is federal and Congress has not addressed punitive damages in maritime law, the Court decided the case in the manner of a common law court, and examined the common law standard — as opposed to the constitutional due process standard – of excessiveness. It surveyed the history of punitive damages, and international as well as state practices, and found that "the consensus today is that punitives are aimed not at compensation but principally at retribution and deterring harmful conduct." As a result, American courts apply punitive damages when a defendant's conduct is outrageous, willful, reckless, results from gross negligence, or is similarly culpable, although punitive damages also are used when wrongdoing is hard to detect, or when compensatory damages are small, providing little incentive to sue.

Rejecting the assertion that punitive damage awards have grown excessively large, the Court surveyed academic literature and determined that the historical ratio of punitive to compensatory rewards has remained less than 1:1. The Court observed that: "The real problem, it seems, is the stark unpredictability of punitive awards." Addressing this issue, the majority concluded that "a penalty should be reasonably predictable in its severity, so that even Justice Holmes's 'bad man' can look ahead with some ability to know what the stakes are in choosing one course of action or another."

The Court then considered three approaches to avoiding "outlier" awards and fostering predictability: (1) providing verbal guidance to judges and juries; (2) imposing dollar caps on damages; and (3) "pegging punitive to compensatory damages using a ratio or maximum multiple." Of these options, the Court favored the latter. It expressed skepticism

[1] This Report focuses on the portions of the Supreme Court's opinion relating to punitive damages. As to the other issues on appeal, the Court split 4-4 as to whether maritime law permits punitive damages for corporate liability based on the acts of managerial agents (which leaves standing the ruling below that it does), and the Court unanimously rejected the argument that the Clean Water Act preempted punitive damage awards in maritime spill cases.

"[G]iven the need to protect against the possibility . . . of awards that are unpredictable and unnecessary, either for deterrence or for measured retribution, we consider that a 1:1 ratio . . . is a fair upper limit in such maritime cases."

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that jury instructions could provide "systemic consistency" when awards are not tied to any specific item of damages, such as medical costs. It reasoned that tort and contract injury are not conducive to being assigned a particular dollar figure. Finally, it concluded that experience with criminal sentences suggested that only a quantified approach would produce consistent results. The Supreme Court accordingly held under maritime law that where the conduct was reckless, but not intentional or malicious, the punitive award should be near the median ratio of punitive to compensatory damage awards across a variety of cases, as calculated by several studies, or about 0.65:1. Furthermore, "given the need to protect against the possibility . . . of awards that are unpredictable and unnecessary, either for deterrence or for measured retribution, we consider that a 1:1 ratio . . . is a fair upper limit in such maritime cases."

Although Justices Scalia and Thomas joined the majority's decision based upon prior precedent, Justice Scalia submitted a separate concurrence, joined by Justice Thomas, in which he noted his continued belief that the Due Process Clause provides no substantive protections against excessive punitive awards.

Justices Stevens and Ginsburg wrote separate opinions, both concurring and dissenting in part, in which they argued that capping punitive damages in maritime law was more appropriately left to Congress.

Justice Breyer, also concurring in part, generally agreed with the Court's application of a 1:1 ratio, but noted that an exception was warranted here because Exxon's conduct could be considered particularly egregious.

Justice Alito did not participate in consideration of the case.

IMPLICATIONS

Exxon provides an unprecedented look at the Supreme Court's views regarding appropriate levels for punitive damage awards, and the considerations that courts should take into account in assessing whether punitive awards further the purposes of punitive damages. In contrast to earlier cases in which the Court's decisions limiting punitive damages were decided under the United States Constitution's Due Process Clause, in this case the Court was not limited to determining the upper bounds under the federal Constitution of punitive damage awards granted under state law. Rather, the Court was free to act as a common law court in fashioning an approach to further policy considerations, specifically the importance of "fairness and consistency" in awarding punitive damages while fulfilling the retribution and deterrence purposes of such damages.

In providing a clear signal of its desire to limit the inconsistency with which punitive damages are awarded the Court no doubt hopes that legislatures and other courts will follow its direction, including by offering clearer guidance and more specific limitations to the juries and judges determining whether to impose punitive damages, and at what level. State courts have proven somewhat resistant to the Supreme Court's efforts to influence the law of punitive damages, however, and thus it may take time for the *Exxon* approach to be reflected in state law.

In the wake of its decision, it remains unclear whether the Supreme Court, when faced with a punitive damage award exceeding a 1:1 ratio, will invalidate such award pursuant to the Due Process Clause. Instead, the Court may continue to follow the more flexible (but less predictable) standard articulated in *State*

Farm Mutual Automobile Insurance Co. v. Campbell, 538 U.S. 408 (U.S. 2003). In *State Farm*, the Court recognized that the constitutional limit to the ratio will vary with the facts and circumstances of cases, many of which will involve conduct more egregious that the recklessness found in Exxon. The Court's decision noted that, when compensatory damages are substantial, perhaps only punitive damages equal to compensatory damages would satisfy due process. Nevertheless, the Court declined to impose a bright-line ratio that a punitive damages award cannot exceed, notwithstanding its observation that, in practice, few awards exceeding a single-digit ratio between punitive and compensatory damages satisfy due process.

Finally, it is worth noting that among the considerations that the majority opinion described as pertinent to the "relevant degrees of blameworthiness" that factor into punitive damage awards, was whether the defendant's action or omission was committed "in order to augment profit," which would increase the degree of "punishable culpability."

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