Legal Opinion Letter

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APPEALS COURT TO REVIEW DEFIANT PUNITIVE DAMAGES RULING

by
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Some courts just can't take a hint.

In November 2001, the United States Court of Appeals for the Ninth Circuit vacated a $5 billion punitive damage award imposed against Exxon Corporation for its conduct leading to the *Exxon Valdez* oil spill. The Ninth Circuit held that the award was unconstitutionally excessive and remanded to the district court with directions to reduce it. *In re the Exxon Valdez*, 270 F.3d 1215 (9th Cir. 2001).

On December 9, 2002, the district court issued an opinion that can only be characterized as defiant. Openly disagreeing with the Ninth Circuit's legal reasoning and conclusions, the court adhered to its view that a $5 billion award was not excessive, but — at the suggestion of the plaintiffs' lawyers — reduced the award to $4 billion in order to comply with what it viewed as the literal terms of the Ninth Circuit's mandate. *In re the Exxon Valdez*, 236 F. Supp. 2d 1043 (D. Alaska 2002).

The district court's approach is not atypical. In the seven years since the Supreme Court expressly recognized the constitutional limitations on punitive damage awards in *BMW of North America, Inc. v. Gore*, 517 U.S. 559 (1996), many courts have diluted or even nullified these protections. Consequently, despite the Supreme Court's recent emphasis that *BMW* must be enforced with rigor, *see Cooper Industries, Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424 (2001), corporate defendants are all too often stripped of their constitutional rights and subjected to arbitrary and grossly excessive punishments. *See, e.g.*, *Romo v. Ford Motor Co.*, 99 Cal. App. 4th 1115 (2002) (reinstating $290 million punitive damage award against Ford) (petition for certiorari filed Jan. 21, 2003).

The Ninth Circuit's Decision. After reviewing the $5 billion award under *BMW* and *Cooper Industries*, the Ninth Circuit concluded that the penalty was unconstitutional and "must be reduced." 270 F.3d at 1246. The court's analysis rested on *BMW*'s three "guideposts" that determine whether a punitive damage award is unconstitutionally excessive: (1) the reprehensibility of the defendant's conduct; (2) the ratio of the punitive damage award to the actual harm suffered by the plaintiff; and (3) the difference between the award and the amount of any civil or criminal penalties that could be imposed for comparable misconduct. *See BMW*, 517 U.S. at 580-83.

The Ninth Circuit began by identifying a variety of facts that reduced the reprehensibility of Exxon's conduct. It noted, for example, that Exxon did not spill the oil on purpose, it did not kill anyone, and there was

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no "executive trickery to hide or facilitate the spill." 270 F.3d at 1242-43. The court then held that the high ratio of compensatory to punitive damages (up to 17:1) was further evidence of an excessive award, particularly in light of the cleanup and settlement costs Exxon had already incurred. *Id*. at 1243-44. Finally, the court concluded that a $5 billion punishment vastly exceeded any civil or criminal sanction that could be imposed for comparable misconduct, noting that the Trans-Alaska Pipeline Act imposed a $100 million ceiling on liability arising from the discharge of oil from a vessel. *Id*. at 1245.

The District Court's Decision. On remand, the district court agreed that the $5 billion award was "breath-taking," but held, contrary to the Ninth Circuit's conclusion, that the award was not unconstitutional. The court first held that Exxon's conduct was "highly reprehensible" because, although it was non-violent and unintentional, it demonstrated "reckless disregard" for the property and safety of others. 236 F. Supp. 2d at 1054-57. The court focused on "what might have happened" — rather than what actually *did* happen — and reasoned that Exxon's reprehensibility was "appreciably aggravate[d]" because a fire could have (but did not) erupt during the cleanup process. *Id*. at 1057.

Next, the district court turned to "what it has found to be the most troubling aspect of the decision of the court of appeals": its holding that the amount a defendant pays in voluntary settlements should not be incorporated in the ratio analysis as a way of allowing a heightened punitive damage award. *Id*. at 1060 (quoting 270 F.3d at 1244). The district court concluded on the basis of its own "independent research" that "a contrary argument is more logical" and consequently "[i]n this case, the general rule adopted by the circuit should not apply." 236 F. Supp. 2d at 1060-61. The district court then addressed the Ninth Circuit's observation that ratio analysis helps avoid overdeterrence, *i.e*., the danger that disproportionate punitive damage awards will render certain activities unacceptably risky, thus leading corporations to avoid engaging in socially beneficial activities (such as providing fuel for consumers at moderate expense). The district court condemned the Ninth Circuit for adopting an "economic analysis [that] makes sense in the abstract or academic world," but not in the "real world" where "reckless corporate officials" are not deterred by "what it theoretically takes to deter a rational business person." *Id*. at 1064. In sum, the court concluded, a high ratio of punitive to compensatory damages was necessary to punish and deter an "economic powerhouse" like Exxon, whose worldwide profits "go into the billions of dollars each year." *Id*. at 1065.

Finally, the district court held that the comparable civil and criminal penalties supported a $5 billion award. Although the Ninth Circuit had specifically held that the $100 million cap on liability under the Trans-Alaska Pipeline Act was "instructive," the district court rejected this judgment, going so far as to label the statute "not instructive" because it limited "strict liability" rather than "civil liability." *Id*. at 1067. The court further reasoned that "because we are concerned about notice of what *could be*, Exxon is fairly chargeable with knowledge that reckless conduct on its part could result in the spill of the entire cargo of a tank vessel such as the *Exxon Valdez*" — and that the fines resulting from such a hypothetical spill (rather than the partial spill that actually occurred) could exceed $5 billion. *Id*.

The district court was thus left with a dilemma. Although the Ninth Circuit had held the $5 billion award grossly excessive and unconstitutional, and directed the district court to reduce it, the district court had reached a contrary conclusion: that the award was "not grossly excessive so as to deprive Exxon of . . . its right to due process." *Id*. at 1068. Given this conclusion, the court explained, it did not "perceive any principled means by which it can reduce [the] award," and thus adopted the suggestion of plaintiffs' counsel to cut the award to the arbitrary amount of $4 billion. *Id*. The court emphasized that it was "adopt[ing] the plaintiffs' position as the means of resolving the conflict between its judgment and the directions of the court of appeals," adding that "if Exxon chooses to take a further appeal for the purpose of seeking a more generous reduction of the jury's punitive damages award, then the court urges the plaintiffs to cross-appeal" and seek reinstatement of the full $5 billion. *Id*. at 1068 & n.88.

Conclusion. The district court acknowledged that it reached its result through means that were not "principled." That assessment is accurate: Had the court properly construed the Ninth Circuit's mandate and faithfully applied the principles of *BMW*, it could never have approved a $4 billion award, let alone the $5 billion verdict it wished to uphold. Exxon is again appealing the district court's ruling, and we likely have not heard the last from the Ninth Circuit.

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