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17-2107, 17-2111 (XAP)

United States Court of Appeals for the Second Circuit

THE STATE OF NEW YORK, THE CITY OF NEW YORK,

Plaintiffs-Appellees/Cross-Appellants,

v.

UNITED PARCEL SERVICE, INC.,

Defendant-Appellant/Cross-Appellee.

On Appeal from the United States District Court
for the Southern District of New York
Case No. 15-cv-1136

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF DEFENDANT/APPELLANT, URGING REVERSAL

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, *amicus curiae* Washington Legal Foundation (WLF) states that it is a nonprofit corporation organized under § 501(c)(3) of the Internal Revenue Code. WLF has no parent corporation, issues no stock, and no publicly held company enjoys a 10% or greater ownership interest.

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INTEREST OF *AMICUS CURIAE*

The Washington Legal Foundation (WLF) is a nonprofit, public-interest law firm and policy center with supporters in all 50 states, including New York.[1] WLF devotes a substantial portion of its resources to defending and promoting free enterprise, individual rights, limited government, and the rule of law. To that end, WLF has long appeared as *amicus curiae* in federal courts to contest the award of disproportionate and grossly excessive fines, penalties, and punitive damages. *See, e.g.*, *Exxon Shipping Co. v. Baker*, 554 U.S. 471 (2008); *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408 (2003); *Cooper Indus., Inc. v. Leatherman Tool Grp., Inc.*, 532 U.S. 424 (2001).

In addition, WLF's Legal Studies division, the publishing arm of WLF, regularly produces original research on a variety of issues related to constitutionally excessive monetary awards. *See, e.g.*, Gregory A. Brower, *Rolling the Dice for Deep Pockets?: Why Nevada Courts Should Find $500 Million Punitive Award Excessive*, WLF Legal Backgrounder (September 16, 2010); John T. Boese, *Court Finds False Claims Fines Subject to Constitutional Challenge*, WLF Counsel's Advisory (April 6, 2001).

WLF believes that economic development and consumer welfare are impeded by

[1] Pursuant to Federal Rule of Appellate Procedure 29(a)(4)(E), *amicus curiae* WLF states that no party's counsel authored this brief in whole or in part; and that no person, party, or party's counsel—other than WLF and its counsel—contributed money that was intended to fund the preparation or submission of this brief. All parties to this dispute have consented to the filing of this brief.

improper and unduly excessive punitive awards. Such outsized monetary penalties are not only unfair to the particular business defendant to which they are aimed, but they also harm investors and consumers, who invariably pay the price in the form of lower stock values and increased costs for goods and services. WLF agrees with UPS that the district court's bench trial and resulting judgment below were riddled with myriad reversible legal errors. WLF writes separately to contend that—even if the district court's deeply flawed liability determinations withstand this Court's review—the gargantuan penalty awarded in this case is disproportionate to any measure of harm and grossly excessive.

STATEMENT OF THE CASE

United Parcel Service (UPS) is the world's largest package delivery company. In 2015, the State and City of New York filed suit against UPS alleging that it knowingly shipped untaxed cigarettes from Indian reservations to consumers in violation of state and federal law. This appeal arises from the subsequent judgment entered by Judge Katherine Forrest of the U.S. District Court for the Southern District of New York.

Following a bench trial, the district court found that UPS had "constructive" knowledge of the transportation of cigarettes and was liable under four claims: (1) contractual breaches of the 2005 Assurance of Discontinuance (AOD) that UPS entered into with the New York Attorney General; (2) violation of New York Public Health Law (PHL) § 1399-*ll*, which prohibits "any common or contract carrier" from knowingly transporting cigarettes to anyone other than statutorily authorized recipients; (3) violation of the Prevent All Cigarette Trafficking (PACT) Act, 15 U.S.C. §§ 375-378; and (4) violation of the Contraband Cigarette Trafficking Act (CCTA), 18 U.S.C. §§ 2341- 2346, which prohibits the knowing transportation of more than 10,000 "contraband cigarettes" (*i.e.*, cigarettes lacking evidence required by state law that state cigarette taxes were paid).

Although earlier acknowledging that it was unable to calculate damages and penalties on the basis of the record before it, the district court nonetheless went on to award the State and City a total monetary award of $246,975,614. The only causation evidence admitted at trial showed that, at *most*, only 5.4% of any lost tax revenue was attributable to UPS's delivery of packages. Yet the district court relied on its own arbitrary "reasonable approximation" to attribute 50% of the lost tax revenue for the shipped cigarettes to UPS, yielding $9,400,614 in compensatory damages. The district court then triple counted for the same conduct under the AOD, the PACT Act, and the NYPHL to award combined penalties of $237,575,000.

The district court did not meaningfully consider whether that penalty was excessive under either federal common law standards or under the constitutional limits imposed by the Fifth and Eighth Amendments. Instead, the district court insisted that due process considerations apply only to punitive damage awards, not to statutory penalties. Accordingly, a "hefty fine" would not be unlawful or unconstitutional but was required to "cause changes in practices and procedures." Corrected Opinion and Order ("Liability Op.") at 198. Ultimately, the court concluded that only a nine-digit penalty far in excess of any compensatory damages "would capture the attention of the highest executives in the company." *Ibid.*

UPS appeals from the district court's liability findings as well as the court's calculation and award of damages and penalties. For the reasons that follow, the order of the district court should be reversed.

SUMMARY OF ARGUMENT

While there may be borderline cases in which it is difficult to determine whether a civil penalty is unduly excessive, this is not one of them. The $237 million civil penalty in this case is so unmoored from any conceivable notion of proportionality or predictability that—even if the district court's deeply flawed liability determinations survive this Court's review—reversal is warranted based on the enormous size of the penalty alone. Indeed, notwithstanding the district court's myriad errors below, this Court should be especially vigilant when scrutinizing a massive civil penalty premised on a poorly defined theory of liability that provides the defendant with no notice of its total exposure.

In federal court proceedings involving federal statutory claims, *federal law* governs the issue of whether the aggregate penalty imposed on the defendant is excessive. Congress is entitled to enact statutes specifying minimum and maximum penalties that may be imposed for statutory violations. But when, as here, Congress has not addressed that issue, courts look first to federal common law to determine limits on aggregate liability—because case law is clear that there is always *some* federal-law limit on permissible penalties in federal court proceedings.

In *Exxon Shipping Co. v. Baker*, 554 U.S. 471 (2008), the Supreme Court comprehensively addressed federal common-law limitations on punitive sanctions in federal proceedings. The Court concluded that "the stark unpredictability of punitive awards" was a "real problem" and held that—in the absence of a contrary congressional command—federal courts should adopt common-law limitations to ensure "consistency across punitive awards in cases involving similar claims and circumstances." 544 U.S. at 499, 501. The Court concluded that "the best insurance against unpredictable outlier[ ]" awards was to impose numerical limits pegged to the actual damages suffered by the plaintiff. *Id.* at 504, 506. The Court held that the appropriate maximum ratio of punitive sanctions to actual damages in the case before it (involving a defendant responsible for a massive oil spill) was 1:1, *id.* at 513, but recognized that under a different set of facts involving particularly culpable defendants the appropriate ratio might be slightly higher. *Id.* at 510-11.

The district court's decision here never cited *Exxon Shipping*, nor did it ever discuss common-law limitations on aggregate penalties. The court imposed a $237.6 million penalty on UPS, an amount more than 25 times greater than the $9.4 million in damages (in the form of lost tax revenues) it determined that Appellees suffered as a result of UPS's conduct. A 25:1 ratio of penalties to actual damages (or any ratio much above 1:1) is impermissible under federal common law even when (unlike here) the defendant has acted maliciously with an intent to injure.

The district court's penalty award also exceeds maximums imposed by the U.S. Constitution. The Eighth Amendment's Excessive Fines Clause prohibits a civil penalty that is grossly disproportionate to the nature and amount of harm caused by the defendant's conduct. Under the Excessive Fines Clause, the Supreme Court has found unconstitutional a $357,000 forfeiture for a "reporting offense" that resulted in "minimal" or "minor" harm to the government. *United States v. Bajakajian*, 524 U.S. 321, 337-40 (1998). It should follow that a $237 million civil penalty in a case with *no* proof of actual harm or injury to the government is also unconstitutional.

Even accepting at face value the district court's unproven and exorbitant estimate of economic harm in the form of "diverted" tax revenues, the $237 million penalty cannot stand. Although the Supreme Court has indicated that a 4:1 ratio between a penalty and the actual harm being punished is "close to the line of constitutional impropriety," the penalty in this case is more than *25 times* the amount of compensatory damages already awarded for the same conduct. Because the district court's massive nine-figure penalty in the face of—*at most*—$ 9.4 million in economic harm runs afoul of the Constitution's guarantee of due process, the judgment below should be reversed.

ARGUMENT

I. The District Court's Civil Penalty Is Excessive Under the Federal Common Law

In assessing $237.6 million in penalties against UPS, the district court rejected UPS's contention that the U.S. Constitution imposes meaningful limits on the permissible aggregate penalty that may be imposed. Liability Op. 198-206; Damages Op. 2-3 (stating, "The Court concludes that the measure of damages and penalties awarded is fair and appropriate and comports with all applicable constitutional requirements."). The court failed, however, to give any consideration to whether the huge penalty it assessed comported with limits on aggregate penalties imposed by federal common law. That failure was clear error. As explained below, federal common law imposes constraints on aggregate penalties awarded by federal courts that are significantly more stringent than those imposed by the U.S. Constitution. These common-law constraints limit the permissible penalty in this case to no more than $9.4 million, the amount of damages that (according to the district court) Appellees suffered as a result of UPS's conduct.

A. Federal Common-Law Constraints on Aggregate Penalties Imposed on a Defendant Are More Demanding Than Those Imposed by the Constitution

In a line of case stretching back more than 20 years, the Supreme Court has recognized that the Due Process Clauses of the Fifth and Fourteenth Amendments impose limitations on the size of punitive sanctions awardable in judicial proceedings. The Court has recognized that when such awards can fairly be categorized as "grossly excessive" in relation to the government's interests in punishment and deterrence, they "enter the zone of arbitrariness that violates the Due Process Clause." *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 568 (1996).

At the same time, however, the Supreme Court has been cognizant that States have legitimate interests in imposing punitive damages for purposes of punishment and deterrence. Accordingly, the Court has repeatedly expressed federalism-based warnings that its due process standards are not intended to dictate to state courts all facets of their punitive-sanction jurisprudence but instead impose bare minimum standards designed to prevent only those awards that most clearly constitute nothing more than arbitrary punishment. Thus, in *BMW*, the Court explained, "In our federal system, States necessarily have considerable flexibility in determining the level of punitive damages that they will allow in different classes of cases and in any particular case." *Id.* *See also Cooper Industries*, 532 U.S. at 433 ("As in the criminal sentencing context, legislatures enjoy broad discretion in authorizing and limiting permissible punitive damages awards.").

By way of contrast, in lawsuits where (as here) it is *federal* law that primarily provides the rule of decision, there are no federalism-based reasons for federal courts to restrict themselves to adopting bare-minimum fairness standards, and every reason to adopt rules to ensure that punitive damages awards are serving their proper purposes. As this Court has explained:

> [A] federal appellate court (including the Supreme Court), reviewing a federal district court's ruling on [the alleged excessiveness of punitive sanctions], ha[s] considerably more supervisory authority than the Supreme Court has over the decisions of the highest courts of a state.

Payne v. Jones, 711 F.3d 85, 97 (2d Cir. 2013). *See also Turley v. ISG Lackawanna, Inc.*, 774 F.3d 140, 164 (2d Cir. 2014) ("We are required to review the district court's refusal to grant a more substantial remittitur as to the punitive damages award under federal common law, pursuant to the federal appellate courts' supervisory authority over trial courts.").

The Supreme Court has stated repeatedly that punitive damages serve two legitimate purposes only: deterrence and retribution. *State Farm*, 538 U.S. at 419 (punitive sanctions should be awarded only "if the defendant's culpability, after having paid compensatory damages, is so reprehensible as to warrant the imposition of further sanctions to achieve punishment or deterrence."); *BMW*, 517 U.S. at 568, 584-85; *Pacific Mut. Life Ins. Co. v. Haslip*, 499 U.S. 1, 19 (1991). The Second Circuit concurs. *See, e.g.*, *Lee v. Edwards*, 101 F.3d 805, 809 (2d Cir. 1996) (purpose of punitive sanctions is "to punish the defendant and to deter him and others from similar conduct in the future") (quoting *Vasbinder v. Scott*, 976 F.2d 118, 121 (2d Cir. 1992)).

Moreover, the proper level of deterrence and retribution is an issue of law to be determined by Congress and the courts—not simply handed off to the finder of fact with instructions to do its best to come up with a result that it deems "fair." As the Supreme Court explained in *Cooper Industries,* it is wholly appropriate for courts to impose strict limits on the size of permissible punitive sanctions in federal-law cases and to review sanctions awards carefully to ensure that trial courts adhere to those limits; unlike the measure of actual damages suffered, "the level of punitive damages is not really a fact tried by the jury." *Cooper Industries*, 532 U.S. at 437.

Congress is the ultimate decision-maker when it comes to establishing maximum permissible penal sanctions that may be imposed under federal law in federal-court proceedings. *See, e.g., Exxon Shipping*, 544 U.S. at 489-90. But Congress rarely exercises its authority to establish maximum-authorized penal sanctions.[2] Rather, when Congress adopts legislation authorizing the award of penal sanctions, it has left to the courts the job of fleshing out federal common-law rules governing the maximum aggregate size of penalties and punitive damages awards.[3]

In accord with that pattern, the federal statutes at issue here—the PACT Act and the CCTA—are silent regarding maximum aggregate penalties that may be imposed against a single defendant. The PACT Act provides that a common carrier that violates

[2] For example, only a handful of federal statutes provide explicit caps on punitive damages awards. *See, e.g.,* 42 U.S.C. § 1981a(b)(3) (imposing $300,000 monetary cap on punitive damages in cases filed under Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e *et seq.*).

[3] *See, e.g.,* 15 U.S.C. § 1681n(a)(2) (providing for award of punitive damages in such amount "as the court may allow" against one who "willfully fails to comply" with provisions of the Fair Credit Reporting Act, 15 U.S.C. §§ 1681, *et seq.*).

the statute is subject to a penalty not to exceed $2,500 for a "first violation," and $5,000 for "any violation within 1 year of a prior violation." 15 U.S.C. § 377(b)(1)(B). But it is silent regarding what constitutes a separate "violation" and the maximum penalty that may be imposed when governments seeking to enforce the PACT Act aggregate multiple alleged violations into a single proceeding.

The district court simply assumed that the absence of provisions in either the PACT Act or the CCTA specifying maximum aggregate penalties meant that no such maximum exists; by alleging a sufficiently large number of separate "violations," a government enforcer is theoretically permitted under federal law to seek imposition of penalties amounting to billions of dollars. That assumption has been squarely rejected by both the Supreme Court and this Court. *See, e.g.*, *Exxon Shipping*, 554 U.S. at 508 n.21 ("[W]e may not slough off our responsibilities for common law remedies because Congress has not made a first move, and the absence of federal legislation constraining punitive damages does not imply that there should be no quantified rule."); *Payne*, 711 F.3d at 98 ("surely there must be an upper limit" imposed by federal common law on aggregate penal sanctions); *Lee*, 101 F.3d at 808 (same).

B. In Order to Eliminate the Unpredictability of Punitive Awards, Federal Common Law Imposes Numerical Limits on Such Awards, Pegged to the Actual Damages Suffered by the Plaintiff

In *Exxon Shipping*, the Supreme Court comprehensively addressed federal common-law limitations on punitive sanctions in federal proceedings. The Court held that, to ensure consistent application of such sanctions, federal common law requires federal courts to peg the size of sanctions to the actual damages suffered by the plaintiff. 554 U.S. at 504, 506. It concluded that no purely verbal approach (such as rules requiring fact-finders to consider "the degree of heinousness" of the defendant's conduct or whether the conduct "shocks the conscience") was sufficient to ensure consistent application. *Id.* at 503-04.

Exxon Shipping closely examined the history of punitive damages in the American and European legal systems. The Supreme Court concluded that while "punitive damages are higher and more frequent in the United States than they are elsewhere, *id.* at 496, the available evidence suggested that "discretion to award punitive damages has not mass-produced runaway awards," and that "by most accounts the median ratio of punitive to compensatory awards has remained less than 1:1." *Id.* at 497-98. But while the Court saw no need to establish new common-law rules that would decrease the average size of punitive sanctions, it declared that "the stark unpredictability of punitive awards" is a "real problem." *Id.* at 499. It explained:

> Courts of law are concerned with fairness as consistency, and evidence that the median ratio of punitive to compensatory awards falls within a reasonable zone, or that punitive awards are infrequent, fails to tell us whether the spread between high and low individual awards is acceptable. The available data suggest it is not. ... [T]he thrust of these figures [regarding jury awards] is clear: the spread is great, and the outlier cases subject defendants to punitive damages that dwarf the corresponding compensatories. The distribution of awards is narrower, but still remarkable, among punitive damages assessed by judges.

Id. at 499-500. The court further concluded that the wide disparity in awards bore little or no relationship to the actual facts of each case but rather "was a reflection of the inherent uncertainty of the trial process." *Id.* at 500-01 (quoting *BMW of North America, Inc. v. Gore*, 646 So.2d 619, 626 (Ala. 1994)).

After stating that the wide disparity in punitive sanctions was not "acceptable," the Court considered several options for addressing the problem. It concluded that simply announcing a detailed list of factors that should be applied by the trier of fact would not eliminate the unacceptable variability in awards. It reviewed the jury instructions utilized by a number of States and concluded:

> These examples leave us skeptical that verbal formulations, superimposed on general jury instructions, are the best insurance against unpredictable outliers. Instructions can go just so far in promoting systemic consistency when awards are not tied to specifically proven items of damage (the cost of medical treatment, say).

Id. at 504.

Instead, the Court concluded that federal common law should address the disparity issue "by pegging punitive to compensatory damages using a ratio or maximum multiple." *Id.* at 506. The Court recognized that the precise maximum common-law ratio of punitive sanctions to actual damages could vary somewhat based on the facts of the case—perhaps reaching as high as 3:1 in cases involving particularly egregious conduct. *Id.* at 509-511. It stated, however, that in cases involving facts akin to those before the Court (a major oil spill brought about by the defendant's reckless conduct), federal common law counsels that "a median ratio of punitive to compensatory damages of about 0.65:1 probably marks the line near which cases like this one should be grouped." *Id.* at 513.

The district court did not cite *Exxon Shipping* and made no effort to peg its penalty award to the plaintiffs' actual damages. Instead, it relied on a pre-*Exxon Shipping* case to identify factors relevant to its penalty calculation. Damages Op. at 7 (citing *Advance Pharmaceutical, Inc. v. United States*, 391 F.3d 377, 399 (2d Cir. 2004)). All of the factors cited by *Advance Pharmaceutical*—the level of the defendant's culpability, the public harm caused by the violations, the defendant's profits from the violations, and the defendant's ability to pay a fine—are certainly relevant to a penalty calculation. But by failing to take account of *Exxon Shipping*, the district court failed to consider the common-law requirement to tailor its penalty analysis to the damages incurred by plaintiffs.

C. Under Federal Common Law, Penal Sanctions Against UPS Are Limited to No More Than the Actual Damages Suffered by Plaintiffs

Even if this Court were to uphold the district court's liability findings, the lower court's failure take into account the federal common law's numerical limits on penal awards would at the very least require a remand for a recomputation of penalties. As an alternative to a remand, WLF urges the Court to undertake its own analysis of penalties. WLF agrees with UPS that under the facts of this case, the maximum permissible ratio of penalties to actual damages is 1:1. Because even under the district court's generous damages computation the plaintiffs suffered no more than $9.4 million in damages, the Court should reduce the aggregate penalty to no more than $9.4 million.

WLF explains at length in Section II of this brief why any larger penalty would be grossly excessive; we will not repeat that explanation here. Rather, we focus briefly on several key points. First, the $237.6 million penalty imposed by the district court is wildly out of line with penalties imposed in comparable cases. As UPS notes, whatever UPS's culpability may be for not preventing others from using its facilities to ship cigarettes, those shippers are far more culpable. Yet plaintiffs offered leniency to those "bad actors"—entities who intentionally violated the law—in return for their assistance in this lawsuit. WLF can draw only one conclusion: the plaintiffs are more interested in a large payday from a deep-pocketed corporation than they are in punishing wrongdoers or deterring future misconduct.

The district court cited no other cases involving penalties imposed for violations of the PACT Act, the CCTA, or the PHL. In the only other reported case of which WLF is aware involving penalties for shipments of unstamped cigarettes, companies were fined approximately $7 million each for intentionally selling more than 25 times the number of unstamped cigarettes that the district court determined were shipped by third parties using UPS facilities. *City of New York v. Milhelm Attea & Bros., Inc.*, No. 06-cv-3620, 2012 WL 3579568 (E.D.N.Y. Aug. 17, 2012).

Second, the district court sought to justify its $236.7 million penalty by stating that a penalty of that magnitude was necessary for deterrence purposes—to "capture the attention of the highest executives in the company." Damages Op. at 9. That assertion is uniformly rejected by economists. As Justice Breyer has noted, economic theory holds generally that proper deterrence will be achieved if defendants pay the total cost of the harm they cause. *BMW*, 517 U.S. at 592-93 (Breyer, J., concurring). When tort law requires defendants to compensate for such harm, it forces them to "internalize" the harm's cost, thereby providing appropriate incentives for them to invest in precaution (or scale back activities where accidents may occur) up to the point where social welfare is maximized, *i.e.*, where the marginal cost of increased precaution equals the marginal cost of reduced accidents. *See generally*, Landes & Posner, THE ECONOMIC STRUCTURE OF TORT LAW (1987). There is no empirical support for the assertion a corporation will not respond to those incentives simply because it is large and thus its company-wide earnings may not be substantially reduced by a moderate fine—even though the fine forces it to fully internalize the costs of the harms it causes. Moreover, numerous courts have cautioned against "over-deterrence": imposing fines that significantly exceed harms caused and thereby creating incentives for economically inefficient activities. *See, e.g.*, *Turley*, 774 F.3d at 162.

Finally, because the size of a punitive sanction does not raise an issue of fact, *Cooper Industries*, 532 U.S. at 427, there is little if any reason to defer to the district court's determination regarding the appropriate penalty in this case. This Court has repeatedly noted that a district court's discretion in assessing punitive sanctions is "relatively narrow." *See, e.g.*, *Payne*, 711 F.3d at 100.

The district court determined that UPS turned a blind eye to cigarette shipments, but it never suggested that senior corporate officials bore any responsibility. Management's responsibility for any violations was certainly far lower than the responsibility of management for the oil spill at issue in *Exxon Shipping*; moreover, the UPS conduct caused no injury to any persons or property. The Supreme Court held in *Exxon Shipping* that federal common law did not permit a ratio of punitive sanctions to actual damages of greater than 1:1. Given that UPS cannot plausibly be deemed *more* blameworthy than was Exxon, federal common law limits the maximum aggregate penalty in this case to no more than $9.4 million, the amount of damages to plaintiffs that the district court determined were caused by UPS's misconduct.

II. The District Court's Civil Penalty Is Excessive under Any Conceivable Constitutional Standard

A. A $237 Million Civil Penalty in the Face of—at *Most*—Only $9.4 Million in Compensatory Damages Violates the Due Process Clause

A punitive monetary award that is grossly excessive and disproportionate in relation to a defendant's wrongdoing or to the amount of harm caused to the plaintiff runs afoul of the Constitution. The Due Process Clauses of the Fifth and Fourteenth

Amendments require all punitive monetary awards—including statutory civil penalties—to bear some reasonable relationship to the harm caused. *See generally* Sheila B. Scheuerman, *Due Process Forgotten: The Problem of Statutory Damages and Class Actions*, 74 Mo. L. Rev. 103 (2009).

In *Waters-Pierce Oil Co. v. Texas*, 212 U.S. 86, 111 (1909), the Supreme Court confirmed that civil penalties could be unconstitutional where "the fines imposed are so grossly excessive as to amount of a depravation of property without due process of law." Similarly, the Supreme Court explained in *St Louis, Iron Mountain & Southern Railway Co. v. Williams* that a statutory penalty could "transcend the limitation" of due process "where the penalty prescribed is so severe and oppressive as to be wholly disproportioned to the offense and obviously unreasonable." 251 U.S. 63, 66-67 (1919) (citing *Waters-Pierce Oil*, 212 U.S. at 111).

Although *Waters-Pierce Oil* and *Williams* ultimately found no due process violation on their respective facts, the Supreme Court found just such a violation in *Southwestern Telephone & Telegraph Co. v. Danaher*, 238 U.S. 482 (1915). In that case, an Arkansas state court had levied penalties at a rate of $100 per day for sixty-three days against a telephone company for allegedly discriminating against one of its patrons by disconnecting her service for insufficient payment. 238 U.S. at 485-86. Finding "no intentional wrongdoing," the Court held that the penalty "was so plainly arbitrary and oppressive as to be nothing short of a taking of [the defendant's] property without due process of law." *Id.* at 491. *Danaher* thus makes it clear that a "plainly arbitrary and oppressive" civil penalty violates due process.

Most recently, the Supreme Court has applied the constitutional requirement of proportionality between damages and injury in the context of punitive damages. In *TXO Production Corp.*, *v. Alliance Resources Corp*., a plurality of the Court relied on *Waters-Pierce Oil*, *Williams*, and *Danaher* to determine that "the Due Process Clause of the Fourteenth Amendment imposes substantive limits 'beyond which penalties may not go.'" 509 U.S. 443, 453-54 (1993) (quoting *Seaboard Air Line Ry. v. Seegers*, 207 U.S. 73, 78 (1907)).

That constitutional principle was followed in *BMW of North America v. Gore*, which held that due process "prohibits a State from imposing a 'grossly excessive' punishment on a tortfeasor." 517 U.S. at 562 (citations omitted). Such a "grossly excessive" award, the Court warned, can "enter the zone of arbitrariness that violates the Due Process Clause," especially when it is "'grossly out of proportion to the severity of the offense.'" *Id*. at 568, 576 (quoting *TXO*, 509 U.S. at 453, 462); *see also Cooper Indus.*, 532 U.S. at 434 ("The Due Process Clause of its own force also prohibits the States from imposing 'grossly excessive' punishments on tortfeasors." (citations omitted)).

One of the "guideposts" that *BMW* established for reviewing punitive monetary awards under the Due Process Clause is the ratio of the punitive-damage award to "the actual harm inflicted on the plaintiff." *BMW*, 517 U.S. at 580 (1996); *see also State Farm*, 538 U.S. at 425 (stating that "single-digit multipliers are more likely to comport with due process, while achieving the State's goals of deterrence and retribution"). Indeed, under the Supreme Court's due process jurisprudence, the proportionality factor is "perhaps [the] most commonly cited indicium of an unreasonable or excessive punitive damages award." *BMW*, 517 U.S. at 580. The Court has noted that "few awards exceeding a single-digit ratio between punitive and compensatory damages … will satisfy due process." *State Farm*, 538 U.S. at 425.

Although *nothing* in the record supports the amount, the district court "estimated" Plaintiffs' compensatory damages in this case at $9.4 million. But as UPS demonstrates in its principal brief, that amount was not based on record evidence but rather was arbitrarily set by the court. Because any compensatory damages must be reduced from the district court's fictitious 50% diversion rate to, at most, a 5.4% diversion rate, the only measure of harm tied to UPS's conduct in this case (as established at trial) is $1 million. *See* Appellant's Br. at 103.

It is an understatement to say that a $237 million penalty is "disproportionate" to $9.4 million in compensatory damages—much less to the $1 million in compensatory damages actually supported by record evidence below. Such an award does not remotely come close to passing muster under the Due Process Clause. Even if $9.4 million is assumed, this Court has recognized that "when a compensatory award is particularly high, a 1:1 ratio between compensation and punishment may be the maximum award permitted by the Constitution." *Turley*, 774 F.3d at 167 (citing *State Farm*, 538 U.S. at 425). The $237 million penalty assessed in this case is "not simply excessive, but grossly so." *BMW*, 517 U.S. at 611.

B. A $237 Million Civil Penalty in the Absence of Any Showing of Actual Harm Violates the Excessive Fines Clause

The Eighth Amendment provides that "[e]xcessive bail shall not be required, nor excessive fines imposed, nor cruel and unusual punishments inflicted." U.S. Const. amend. VIII. The Excessive Fines Clause is "intended to prevent the government from abusing its power to punish." *Austin v. United States*, 509 U.S. 602, 607 (1993). The Clause "limits the government's power to extract payments," and "cuts across the division between the civil and the criminal law." *Id.* at 609-10 (quoting *United States v. Halper*, 490 U.S. 435, 447-448 (1989)).

Although the Excessive Fines Clause does not apply to awards of punitive damages in suits between private parties, there is no question that the $237 million "penalty" levied in this case is a "fine" payable to a "sovereign" as "punishment for some offense" within the meaning of the Eighth Amendment. *See Browing-Ferris Indus. of Vt., Inc. v. Kelco Disposal, Inc.*, 492 U.S. 257, 265 (1989); *Austin*, 509 U.S. at 609-610, 621-622. Indeed, "a civil sanction that cannot fairly be said solely to serve a remedial purpose, but rather can only be explained as also serving either retributive or deterrent purposes, is punishment, as we have come to understand the term." *Austin*, 509 U.S. at 610 (quoting *Halper*, 490 U.S. at 448). As this Court has recognized, the form of the "fine" for Eighth Amendment purposes "is irrelevant and may be a payment in kind, *i.e.*, a forfeiture, or a payment in cash." *von Hofe v. United States*, 492 F.3d 175, 182 (2d. Cir. 2007).

The "touchstone of the constitutional inquiry under the Excessive Fines Clause is the principle of proportionality: The amount of the forfeiture must bear some relationship to the gravity of the offense that it is designed to punish." *Bakajakian*, 524 U.S. at 334. Under the Supreme Court's framework, a penalty is unconstitutionally excessive if it is "grossly disproportional to the gravity of the defendant's offense." *Id.* at 337. In *Bajakajian*, the Supreme Court found unconstitutionally excessive a $357,144 forfeiture for a mere "reporting offense." *Id.* In its proportionality analysis, the Court noted that "[t]he harm that respondent caused was … minimal," and that "[f]ailure to report his currency affected only one party, the Government, and in a relatively minor way." *Id.* at 339. The Court thus concluded that the penalty "bears no articulable correlation to any injury suffered by the Government." *Id.* at 339-40.

The judgment below does not come close to satisfying *Bajakajian*'s standard of proportionality. Even a cursory review of the record in this case reveals that the district court's penalty is "grossly disproportional to the gravity of the defendant's offense." *Id.* at 337. UPS's conduct as a common carrier in this case—transporting packages from paying customers located on or near Indian reservations in upstate New

York—is not criminal. Even if criminality should somehow attach, UPS's conduct would not be *malum in se* but *malum prohibitum*—akin to the very sort of "reporting offense" at issue in *Bajakajian*. 524 U.S. at 337. And the district court itself conceded not only that UPS's relatively small profit "suggests a low amount of penalties" but also that UPS "bears a lower level of culpability" than those persons (traffickers, tax evaders, etc.) the relevant statutes are designed to punish. Liability Op. at 197.

Similarly, the district court never found that a corporate officer or high-level employee of UPS had actual knowledge that specific packages contained cigarettes. Rather, the district court imputed low-level knowledge to the company based solely on the theory of "conscious avoidance." *Ibid.* But that is precisely the kind of "turning a blind eye" that this Court—in rejecting a $124,000 fine as grossly excessive under the Eighth Amendment—has held "fall[s] at the low end of the [culpability] scale." *von Hofe*, 492 F.3d at 189.

While both Plaintiffs and the district court sought to frame UPS's conduct in terms of "a public health impact that the political branches have proscribed and the costs of which New Yorkers may bear," there is *no* record evidence showing that UPS's transportation of packages containing lawful products had any detectable impact on public health. Instead, as shown above, the only "harm" tied to the penalty in this case was economic harm in the form of diverted tax revenues. But any such harm was fully remedied by the district court's speculative and oversized compensatory damages "calculation."

Although the defendant's actions in *Bajakajian* resulted in minor or minimal harm to the government, that finding was insufficient to justify a $357,000 penalty. 524 U.S. at 339-40. The Eighth Amendment violation is even clearer in this case because the penalty is orders of magnitude greater than the unconstitutional one in *Bajakajian*—even though here there was *zero* proof adduced at trial that UPS's conduct actually harmed the government or anyone else. Nor did the district court even purport to compare the amount of its $237 million penalty to the gravity of UPS's offense. Rather, just as in *von Hofe*, "[w]ithout evidence indicating involvement beyond knowledge, the government finds itself characterizing [the defendant's] culpability in terms wholly unrelated to [its] actual conduct." *von Hofe*, 492 F.3d at 190.

C. UPS's Net Worth Cannot Justify an Otherwise Unconstitutionally Excessive Penalty

Contrary to the district court's reasoning below, corporate wealth "cannot justify an otherwise unconstitutional punitive damages award." *State Farm*, 538 U.S. at 427. The Supreme Court has repeatedly cautioned that an "emphasis on the wealth of the wrongdoer increase[s] the risk that the award may … [be] influenced by prejudice against large corporations." *TXO*, 509 U.S. at 464. This "risk" is "of special concern when the defendant is a nonresident." *Ibid*; *see also Honda Motor Co. v. Oberg*, 512 U.S. 415, 431-32 (1994) (considering "evidence of a defendant's net worth creates the potential that juries will use their verdicts to express bias against big business, particularly those without strong local presence”).

In *BMW of North America v. Gore*, the Supreme Court rejected the premise that the net worth of a corporate defendant justifies a disproportionately large award. Despite an undisputed finding that “the judgment ‘would not have a substantial impact on [BMW’s] financial position,’” the Court held that a mere $2 million punitive damages award against the company was unconstitutionally excessive. 517 U.S. 559, 566 (1996). In concurring with that result, Justice Breyer found any connection between wealth and deterrence difficult to comprehend given the “distant relation between a defendant’s wealth and its responses to economic incentive.” *Id.* at 591. (Breyer, J., concurring). In his view, the use of wealth as “an open-ended basis for inflating awards when the defendant is wealthy”—precisely the reasoning of the district court below—cannot be adequately counterbalanced by other factors that fail to “constrain significantly an award that purports to punish a defendant’s conduct.” *Id.*

In one of the earliest opinions to move beyond a superficial consideration of the issue, the Seventh Circuit explored at length the tenuous connection between wealth and deterrence in *Zazu Designs v. L’Oreal, S.A.*, 979 F.2d 499 (7th Cir. 1992). As Judge Easterbrook rightly noted, assessing punitive damages in light of net worth treats having a large net worth as though it, rather than the underlying misconduct, “were the wrong to be deterred!” 979 F.2d at 508.

Zazu went on to explain that whatever salience net worth may have when devising a punishment for natural persons, it is a particularly misguided benchmark where, as here, the defendant is a corporation:

> Corporate assets finance ongoing operations and are unrelated to either the injury done to the victim of the size of the award needed to cause corporate managers to obey the law. Net worth is a measure of the profits that have not been distributed to the investors. Why should damages increase because the firm reinvested its earnings?

Zazu, 979 F.2d at 508. Nor can the absolute size of the defendant's assets justify a bigger penalty in any given case:

> Absolute size, like net worth, also is a questionable reason to extract more per case …. If a larger firm is more likely to commit a wrong on any given transaction, then its total damages will increase more than proportionally to its size without augmentation in any given case; if a larger firm is equally or less likely to commit a tort per transaction, then the court ought to praise the managers rather than multiply the firm's penalty.

Id. at 508-09.

Likewise, scholarly commentary has long insisted that neither corporate size nor wealth is relevant to deterring future wrongdoing. *See, e.g.*, Bruce Chapman & Michael Trebilcock, *Punitive Damages: Divergence in Search of a Rationale*, 40 Ala. L. Rev. 741, 824 (1989) ("In the case of economic wrongs, the conventional economic theory of deterrence … suggests no role for corporate wealth in structuring an optimal deterrence regime."); Kenneth S. Abraham & John C. Jeffries, *Punitive Damages & the Rule of Law: The Role of Defendant's Wealth*, 18 J. Legal Studies 415, 415 (1989) ("In our view, the defendant's wealth is irrelevant to the goal of deterring socially undesirable conduct."); Gary T. Schwartz, *Deterrence and Punishment in the Common Law of Punitive Damages: A Comment*, 56 S. Cal. L. Rev. 133, 140 (1982) ("The wealth of the defendant bears no obvious relationship to deterrence goals.").

This is not to say that any consideration of a defendant's wealth is always inappropriate. For example, a fine can be constitutionally excessive if it destroys a defendant's future livelihood, and consideration of wealth may be appropriate in making that determination. *United States v. Viloski*, 814 F.3d 104, 112 (2016). But as this Court has recognized, "asking whether a [penalty] would destroy a defendant's future livelihood is different from considering as a discrete factor a defendant's present personal circumstances, including … financial situation." *Ibid*. Whereas "hostility to livelihood-destroying fines is deeply rooted in our constitutional tradition," *ibid*, naked considerations of wealth are not.

CONCLUSION

For the foregoing reasons, *amicus curiae* Washington Legal Foundation respectfully requests that the Court reverse the judgment below.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Pursuant to Federal Rule of Appellate Procedure 32(a)(5), I hereby certify that the foregoing brief is in 14-point, proportionately spaced Times New Roman font. Pursuant to Local Rule 29.1, I further certify that the foregoing brief complies with the length limitation established by that rule because, excluding those parts of the brief exempted by Federal Rule of Appellate Procedure 32(f), it contains 6,762 words, as determined by the word-count function of WordPerfect X5.

/s/ Richard A. Samp
Richard A. Samp

CERTIFICATE OF SERVICE

I hereby certify that on October 13, 2017, I filed an electronic copy of the foregoing brief with the Clerk of Court for the U.S. Court of Appeals for the Second Circuit using the appellate CM/ECF system. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

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