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STATE PUNITIVE DAMAGES STATUTES: A PROPOSED ALTERNATIVE

*Sandra N. Hurd**
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I. INTRODUCTION

The continued assessment of punitive damages will mean the end of civilization as we know it. That is the well-orchestrated message of tort reformers and business lobbies. If the claims about the havoc punitive damages wreak can be believed, then they are responsible for the loss of competitiveness of U.S. businesses, the inability to bring life-saving drugs to market, and the financial ruin of major corporations. In opposition, consumer groups and others claim that the allegations are exaggerated, unsupported by facts, and inappropriately restrict plaintiffs' rights. They cite eye-glazing studies of numbers and size of awards to counter the assertions of the tort reformers.

The debate is not merely academic discourse. Claims and counterclaims about the effect of punitive damages are cited to induce major changes in the approach the law takes to their assessment. The battle raged, for a time, at the U.S. Supreme Court level. Over five years' time the Court considered three punitive damages actions as defendants waged constitutional arguments against them. In *Browning-Ferris Industries v. Kelco Disposal, Inc.*¹ the Court concluded that punitive damages awards do not violate the Eighth Amendment's protection against excessive fines. However, the Court virtually invited a challenge based on the due process clause, which was forthcoming in *Pacific Mutual Life Insurance Co. v. Haslip*.² In *Haslip*, the Court held that a punitive damages award handed down by an Alabama jury was reasonable and did not violate the defendant's due process rights.³ In dicta the Court noted that the award, which was four times the actual damages, was "close to the line" separating permissible and impermissible awards.⁴ Taking a cue from that language, the most recent case, *TXO Production Corp. v. Alliance Resources Corp.*,⁵ challenged as a violation of the due process clause a punitive award that was over 500 times the compensatory award. Despite the dicta in *Haslip*, the Court upheld the award as reasonable under a *Haslip* analysis.⁶ Except to review isolated and unique state law provisions, the Supreme Court is not likely to engage in extensive review of punitive damages cases in the foreseeable future.⁷

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1. 492 U.S. 257 (1989).

2. 499 U.S. 1 (1991).

3. *Id.* at 34.

4. *Id.* at 37.

5. 113 S. Ct. 2711 (1993).

6. *Id.* at 2718.

7. *See* *Honda Motor Co. v. Oberg*, 114 S. Ct. 2331 (1994). At the end of the 1994 term, the

The decision in *TXO* did not put to rest the debate, however. For more than a decade, the claims of tort reform groups have been made in statehouses across the country to effect change in the legislative treatment of punitive damages. The lobbying effort has been largely successful, and many states have amended their common law statutorily to restrict the assessment of punitive damages. With the *TXO* outcome, one can expect a renewed effort to be directed at the state level to work even greater change in the name of tort reform.

Amid the rhetoric and emotion of the debate about punitive damages, a basic notion has been lost. The claims of "too many," "too high," and "too often" have drowned out the original reasons for punitive damages and the role they play in establishing social norms. The idea behind punitive damages is simple. When actors engage in truly outrageous civil misconduct, they should be required to pay not only the actual damages their conduct engenders, but an additional penalty designed to punish their conduct and to deter them and others from engaging in such conduct in the future. Although the penalty is paid to the plaintiff, it is not compensation for the harm caused to the plaintiff. It is an assessment against the maliciousness and wantonness of the defendant, and is designed to communicate that society will not tolerate such behavior. In the rush to limit or eliminate punitive damages altogether, the idea of punishment and deterrence seems to have given way to discussions about predictability and economy. Accountability for bad conduct is noticeably absent from the discourse.

In this article we attempt to return to the basic notions of punitive damages. After reviewing the most recent Supreme Court decision on the subject, we examine state statutes for their ability to advance the punishment and deterrence policies so basic to punitive damages. Finally, we propose model legislation that attempts to respond to the concerns of those seeking change, while keeping faith with the historic tenets of punitive damages.

II. *TXO PRODUCTION CORP. v. ALLIANCE RESOURCES CORP.*

On June 25, 1993, the United States Supreme Court weighed in yet again on the punitive damages debate when it announced its decision in *TXO Production Corp. v. Alliance Resources Corp.* In 1985, TXO Production Corp. (TXO) filed a complaint in a West Virginia court seeking to remove a cloud on title to oil and gas development rights. Respondent Alliance Resources Corp. (Alliance) counterclaimed for slander of title. The jury returned a verdict against TXO for \$19,000 in actual damages and \$10 million in punitive damages. The trial court and the Supreme Court of Appeals of West Virginia affirmed the verdict. The Supreme Court granted certiorari⁸ to review TXO's claim that the punitive damages award violated the due process clause of the Fourteenth Amendment as interpreted in *Pacific Mutual Life Ins. Co. v. Haslip*.⁹ The Court upheld the award, applying the *Haslip* reasonableness test.¹⁰ The Court's deference to the state court's analysis will remove federal due process consideration from

Supreme Court issued a decision in *Oberg*, holding that judicial review of punitive damages, or a similar procedural safeguard against arbitrariness, is required by the due process clause. The case involved an Oregon state rule, unique to that state, prohibiting judicial review of punitive damages awarded by a jury. Relying on *Haslip*, the Court overturned the rule as violative of the Fourteenth Amendment.

8. 113 S. Ct. 594 (1992).

9. 499 U.S. 1 (1991).

10. 113 S. Ct. at 2720-22; See text accompanying note 13.

most awards of punitive damages, substantially reducing the number of cases that will be reviewed by the Court. The outcome will return responsibility to the states to articulate the standards for punitive damages awards.

The facts of the case reveal an extreme example of nefarious corporate activity. In 1984, TXO geologists recommended that the company obtain certain oil and gas development rights controlled by Alliance. Alliance accepted TXO's offer of \$20 per acre and 22% of the oil and gas revenues in royalties, and agreed to assign its interest in the Tract to TXO. Alliance agreed also to return the purchase price if TXO's attorney determined that title had failed. TXO subsequently advised Alliance that there was the "distinct possibility or probability" that its title had failed,¹¹ with full knowledge that such claim was frivolous. Attempting to lend substance to its claim, TXO obtained a quitclaim deed from Alliance's predecessor in interest and unsuccessfully tried to obtain a false affidavit about rights conveyed under an earlier deed. When TXO's attempt to renegotiate the royalty agreement with Alliance failed, TXO sued. TXO appealed the jury verdict for Alliance, arguing that the verdict violated its due process rights.¹² The West Virginia Supreme Court of Appeals applied the "reasonable relationship" test of *Haslip*, considering "(1) the potential harm that TXO's actions could have caused; (2) the maliciousness of TXO's action; and (3) the penalty necessary to discourage TXO from undertaking such endeavors in the future."¹³ The West Virginia court held that each of the factors supported the punitive damages award.¹⁴

In its appeal to the United States Supreme Court, TXO raised substantive and procedural due process arguments. It argued, first, that the punitive damages award was so grossly excessive as to amount to a deprivation of property.¹⁵ It argued, second, that the jury was not adequately instructed on punitive damages, the verdict did not receive adequate review by either the trial or appellate court, and TXO did not have advance notice either that the jury could return so large an award or that the jury could rely on potential harm in calculating the amount of punitive damages.¹⁶

The Supreme Court held that the \$10 million punitive damages award was not so excessive as to be beyond the power of the state to allow.¹⁷ Acknowledging that the Fourteenth Amendment does impose a limit "beyond which penalties may not go," the Court rejected both Alliance's proposed rational basis¹⁸ and TXO's proposed heightened scrutiny¹⁹ tests for assessing the constitutionality of punitive damages awards

11. *Id.* at 2715.

12. *Id.* at 2717.

13. 419 S.E.2d 870, 889 (W. Va. 1992).

14. 113 S. Ct. at 2718.

15. *Id.*

16. *Id.* at 2723.

17. *Id.* at 2722-23.

18. The test proposed by Alliance is "the same standard of rational basis scrutiny that is appropriate for reviewing state economic legislation." *Id.* at 2719.

19. TXO asserted that "punitive damage awards should be scrutinized more strictly than legislative penalties because they are typically assessed without any legislative guidance expressing the considered judgment of the elected representatives of the community." *Id.* They proposed a two-step process for review. In the first step, the court would examine four criteria to determine whether a punitive damages award presumptively violates the fundamental fairness notions inherent in due process:

- (1) awards of punitive damages upheld against other defendants in the same jurisdiction,
- (2) awards upheld for similar conduct in other jurisdictions,
- (3) legislative penalty decisions with respect to similar conduct, and
- (4) the relationship of prior punitive awards to the associated compensatory awards.

and confirmed the *Haslip* test:

We return to what we said two terms ago in *Haslip*: "We need not, and indeed we cannot, draw a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable that would fit every case. We can say, however, that [a] general concern[n] of reasonableness . . . properly enter[s] into the constitutional calculus."²⁰

Applying a reasonableness test to the facts of this case, the Court first decided that the trial court's instruction that allowed the jury to consider potential as well as actual harm was appropriate. Despite authority to the contrary in a number of states, it is proper, in determining a punitive damages award, to consider the magnitude of the potential harm to the intended victims if the scheme had succeeded, as well as possible harm to others that might result if like conduct is not deterred.²¹ From the evidence presented at trial, the jury could well have believed that TXO was seeking a multimillion dollar gain in its share of royalties. In light of the amount of money at stake, TXO's bad faith, the fact that this conduct was part of a pattern, and TXO's wealth, the punitive damages award, although large, does not "jar one's constitutional sensibilities."²²

The Supreme Court rejected TXO's procedural due process arguments as well. First, it found that TXO had failed to raise the issue of the inadequacy of the jury instructions in state court.²³ Second, it found that the reviews by both the trial and appellate court were adequate. Although the trial court failed to articulate the basis for denying TXO's post trial motions, the judge indicated from the bench that he agreed with the jury's appraisal of the egregiousness of TXO's conduct. The appellate court decision was unanimous and carefully considered relevant precedents, including *Haslip*.²⁴ Finally, the West Virginia Supreme Court of Appeals had held, prior to this conduct, that a defendant could be liable for punitive damages in the absence of compensatory damages, effectively putting TXO on notice that potential harm may be considered in determining the amount of punitive damages.²⁵

In spite of the hopes of business interests and tort reformers that the Supreme Court would adopt a new test for reviewing punitive damages, the Court did not break new ground with its decision in *TXO*. In refusing to create a bright line and reaffirming its *Haslip* reasonableness test, the Court has effectively limited federal review of punitive damages awards and moved the debate back to the state level, which continues to be the scene of legislative wrestling with punitive damages.

In the second step, an arbitrary and excessive award must be struck down unless there is a compelling and particularized justification for it. *Id.*

20. *Id.* at 2720 (citing *Haslip*, 499 U.S. at 18).

21. *Id.* at 2721.

22. *Id.* at 2722 (citing *Haslip*, 499 U.S. at 18).

23. *Id.* at 2723.

24. *Id.* The West Virginia Supreme Court of Appeals stated:

We have examined all of the punitive damages opinions issued since *Haslip* was decided in an attempt to find some pattern in what courts find reasonable. Generally, the cases fall into three categories: (1) really stupid defendants; (2) really mean defendants; and (3) really stupid defendants who could have caused a great deal of harm by their actions but who actually caused minimal harm.

419 S.E.2d at 887-88.

25. The West Virginia Supreme Court of Appeals subsequently changed this ruling in *Garnes v. Fleming Landfill*, 413 S.E.2d 897 (W. Va. 1991), but this was after TXO's activities under discussion.

III. STATE STATUTES

The tort reform movement and the interest in civil justice reform have produced flurries of state statutes addressing punitive damages, first as a response to the insurance crisis of the 1980s and then again after *Haslip*. Based on the perception that punitive damages are out of control, all the statutes limit their assessment, either by circumstance or amount. As of this writing, more than half of the states have produced some sort of statutory treatment of punitive damages.²⁶ Appendix A displays the states and the substantive provisions of their statutes. While each is different in scope and effect, discernible patterns emerge that permit categorization. For purposes of this discussion we have identified the major categories and discussed representative statutes under each.

A. Caps and Multipliers

To address the concern that punitive damages awards have become excessive, a number of states have capped the amount of the award or tied it to the award for compensatory damages. At the extreme, Virginia has placed an absolute dollar limit of \$350,000 on punitive damages awards and permits no exceptions.²⁷ More typical is the Alabama design of enacting a dollar cap²⁸ and carving out exceptions for certain kinds of behavior²⁹ and certain kinds of torts.³⁰ A third variation is to tie the maximum permissible punitive damages award to compensatory damages³¹ or to some multiplier of the compensatory award, such as four to one,³² often with exceptions for particular types of cases.³³ Probably the most elaborate scheme is found in the Kansas statute, which prescribes that punitive damages be capped at the lesser of \$5 million or defendant's highest gross annual income earned for any one of the five years immediately before the act that is the basis of the claim occurred.³⁴ A different cap is imposed if the court finds that the defendant expected to make a profit in excess of the previously described cap, in which case damages cannot exceed 1.5 times the expected profit.³⁵

It is not possible to state a common figure or multiplier, or even a common set of exceptions that typify all the statutes. Clearly those states that have imposed some monetary limit on punitive damages have done so at the urging of tort reform interests

26. See AMERICAN TORT REFORM ASSOCIATION, LEGISLATIVE REFORM IN THE PUNITIVE DAMAGES AREA (1986-1989), PUNITIVE DAMAGES UPDATE, at 1-3 (Nov. 9, 1989), cited in Stephen Daniels & Joanne Martin, *Myth and Reality in Punitive Damages*, 75 MINN. L. REV. 1, 5 n.14 (1990); Michael Rustad & Thomas Koenig, *Punitive Damages in Products Liability: A Research Report*, 3 PROD. LIAB. L.J. 85 (1992).

27. VA. CODE ANN. § 8.01-38.1 (Michie 1992).

28. ALA. CODE § 6-11-21 (1993). The cap is set at \$250,000.

29. A pattern or practice of intentional wrongful conduct and conduct involving actual malice. *Id.*

30. Libel, slander, and defamation. *Id.* § 6-11-21(3).

31. See, e.g., OKLA. STAT. ANN. tit. 23, § 9(A) (West 1987).

32. See, e.g., TEX. CIV. PRAC. & REM. CODE ANN. § 41.007 (West Supp. 1993). Actually, Texas employs as a cap the greater of \$200,000 or four times the compensatory damages.

33. Florida does not invoke its three-to-one multiplier for class actions. FLA. STAT. ANN. § 768.73(1)(a) (West Supp. 1994). Nevada abandons its three-to-one multiplier for cases involving product liability, some types of housing discrimination, toxic spills and emissions, and defamation. NEV. REV. STAT. ANN. § 42.005(2) (Michie Supp. 1991).

34. KAN. STAT. ANN. § 60-3701(e) (Supp. 1992).

35. *Id.* § 60-3701(f) (Supp. 1992).

who have persuaded state legislators that business competitiveness depends on being able to predict future liabilities. That no magic number or common plan has emerged indicates that those states that have acted felt the pressure at different levels of intensity.

B. Payment to the State

Another criticism leveled at the current state of law is that punitive damages provide a windfall to the plaintiff.³⁶ It is axiomatic that punitive damages do not compensate for any loss the plaintiff suffered; rather they punish and deter the conduct engaged in by the defendant. When the plaintiff receives that amount in addition to the actual damages, it is perceived as a bonus.³⁷ To address the issue of windfall to the plaintiff, some states have enacted laws that require a percentage of any punitive award to be paid to the state. The percentages fall in a range from twenty to seventy-five percent. Some funds are earmarked,³⁸ but most are paid to the general treasury of the states.³⁹

Colorado passed such a statute, only to have it declared unconstitutional as violative of the takings clauses of the Colorado and federal constitutions.⁴⁰ Florida and Georgia courts have upheld similar provisions.⁴¹ In times of diminishing revenues, it may be tempting for states to enact such provisions. However, in light of the Colorado decision, all such statutory schemes are called into question.

C. Burden of Proof

A popular reform measure, adopted by many states, is to increase the burden of proving punitive damages. All of the states that have done so, with the exception of Colorado, have established the clear and convincing evidence standard to replace proof by a preponderance of the evidence.⁴² Colorado went further and now requires proof

36. See Jane Mallor & Barry Roberts, *Punitive Damages: Toward A Principled Approach*, 31 HASTINGS L.J. 639, 644 (1980).

37. Punitive damages are taxable as income; compensatory damages are not.

38. For example, Kansas, in medical malpractice actions, designates the money for health care and Illinois designates its Department of Rehabilitative Services as the beneficiary. KAN. STAT. ANN. § 60-3402(e) (Supp. 1992); ILL. COMP. STAT. ANN. ch. 735, art. 5, § 2-1207 (Michie 1993) (formerly ILL. REV. STAT. ch. 110, para. 2-1207 (Supp. 1990)).

39. See, e.g., UTAH CODE ANN. § 78-18-1 (1992).

40. *Kirk v. Denver Publishing Co.*, 818 P.2d 262 (Colo. 1991).

41. *Gordon v. Florida*, 608 So. 2d 800 (Fla. 1992); *Georgia v. Moseley*, 436 S.E.2d 632 (Ga. 1993). In *Kirk*, the Supreme Court of Colorado could not find that:

[a connection] between, on the one hand, any alleged governmental interest in punishing and deterring fraudulent, malicious, or willful and wanton tortious conduct and, on the other, the statutory imposition of the forced contribution on the person injured by the wrongful conduct; and the gross disproportion between the statutory forced contribution and any governmental service made available to the judgment creditor but not otherwise funded by fees and other statutory assessments imposed on civil litigants using the judicial process to resolve their disputes.

818 P.2d at 273.

Florida and Georgia had no similar difficulty. For instance, the court in *Gordon* said, "The statute under attack here bears a rational relationship to legitimate legislative objectives: to allot to the public weal a portion of damages designed to deter future harm to the public and to discourage punitive damage claims by making them less remunerative to the claimant" 608 So. 2d at 802.

42. See, e.g., CAL. CIV. CODE § 3294 (West Supp. 1994); MINN. STAT. ANN. § 549.20(1) (West 1993); MONT. CODE ANN. § 27-1-221(5) (1993). See also Appendix A.

beyond a reasonable doubt.⁴³ The logic of requiring more proof for punitive damages than for other damages is to demand that the plaintiff establish forcefully the outrageous, often malicious, conduct of which he or she complains. The effect is to reduce the instances when punitive damages are appropriate, a result desired by the tort reformers.

More states have adopted this reform than the others. Variations do exist, as noted in Appendix A, but most states follow the simple route of unconditionally increasing the burden of proof in all punitive damages cases. Moreover, the list of states adopting this approach grows longer when one includes those states that have achieved the same result through judicial decision.⁴⁴

D. Bifurcated Trials

Although not garnering the same support as the other reform measures, requiring or permitting bifurcated trials in punitive damages actions has taken hold in a few states. Generally, the notion is to try the plaintiff's entitlement to punitive damages first and hold a second hearing to set the amount of the damages.⁴⁵ The purpose is to permit the fact finder to consider the caliber of the conduct without being influenced by information about the profitability of the conduct or the defendant's financial worth.

IV. WHAT'S WRONG WITH PUNITIVE DAMAGES REFORM?

It is our assertion that most reform measures taken to date are unnecessary and misguided. We take issue with both the need for and wisdom of making many of the legislative changes to the traditional rules for awarding and computing punitive damages. First, there is insufficient evidence to demonstrate that there is, as business interests loudly contend, a crisis, or even a serious problem, in the area of punitive damages. Second, many of the legislative changes that the states are adopting clearly have the effect of eliminating or significantly diminishing the deterrence function of awarding punitive damages, an inappropriate result as long as there are people who engage in the type of conduct described in *TXO*. If business interests succeed in their efforts to prevent punitive damages from serving their historical functions, the incidence of business misconduct is likely to rise. In that case, more regulation will inevitably spring up—regulation that may be more uncertain and unpredictable than the traditional punitive damages rules about which reformers complain.

Criticism of punitive damages has been part of the legal landscape for over a century.⁴⁶ Most recently, however, because of the alleged insurance crisis of the mid-1980s and the rise of the civil justice and tort reform movements, the debate has changed from a legal discussion about the doctrinal merits of punitive damages to a "highly politicized public policy debate about the alleged negative effects of punitive damages on American society and the economy."⁴⁷

Critics contend that punitive damages are routinely awarded, the amounts awarded are large, the frequency and size of awards has been rapidly increasing, and the

43. COLO. REV. STAT. ANN. § 13-25-127(2) (West 1989).

44. See *Linthicum v. Nationwide Life Ins. Co.*, 723 P.2d 675 (Ariz. 1986); *Travelers Indem. Co. v. Armstrong*, 442 N.E.2d 349 (Ind. 1982); *Wangen v. Ford Motor Co.*, 294 N.W.2d 437 (Wis. 1980).

45. See GA. CODE ANN. § 51-12-5.1(d) (Harrison 1990).

46. *Fay v. Parker*, 53 N.H. 342, 382 (1873).

47. *Daniels & Martin*, *supra* note 26, at 2.

problem is national in scope.⁴⁸ A number of systematic, empirical studies have been conducted on cases yielding punitive damages awards.⁴⁹ The findings of the clear majority of these studies do not support the claims made.⁵⁰ For example, an American Bar Foundation study concludes that juries do not routinely award punitive damages,⁵¹ the awards that are made are "low to modest,"⁵² there have been no dramatic trends over time in cases involving physical or financial harm (the only situations for which there are sufficient data to establish trends),⁵³ and that there is great variation among locations in terms of both the number of cases in which punitive damages are awarded and the amounts of the awards.⁵⁴ Professor Rustad concludes that, at least in product liability cases, punitive damages awards have not changed in size for twenty-five years when adjusted for inflation.⁵⁵ Moreover, when asbestos cases are removed from consideration, punitive damages awards are actually in decline.⁵⁶ Professor Saks, after reviewing other studies, asserts that the "results are far more tame than one might have expected given the impressions created in the minds of the public and policy-makers."⁵⁷ Professor Landes and Judge Posner reviewed cases awarding punitive damages and found them "generally congruent" with the formal legal standard⁵⁸ and not routinely awarded in product liability cases, except in cases of aggravation.⁵⁹

Although the issue of punitive damages is one that needs further research, the findings of the studies to date certainly suggest that the label "crisis" is inaccurate.

48. *Id.*

49. See, e.g., MARK PETERSON ET AL., PUNITIVE DAMAGES: EMPIRICAL FINDINGS (1987); GENERAL ACCOUNTING OFFICE, PRODUCT LIABILITY: VERDICTS AND CASE RESOLUTION IN FIVE STATES (1989); NAT'L CENTER FOR STATE COURTS, WHAT ARE TORT AWARDS REALLY LIKE? THE UNTOLD STORY FROM THE STATE COURTS (1992); Daniels & Martin, *supra* note 26; Michael Rustad, *In Defense of Punitive Damages in Products Liability: Testing Tort Anecdotes with Empirical Data*, 78 IOWA L. REV. 1 (1992); Michael J. Saks, *Do We Really Know Anything About the Behavior of the Tort Litigation System—And Why Not?*, 140 U. PA. L. REV. 1147 (1992).

50. See *supra* note 49. But see REPORT OF THE TORT POLICY WORKING GROUP ON THE CAUSES, EXTENT AND POLICY IMPLICATIONS OF THE CURRENT CRISIS IN INSURANCE AVAILABILITY AND AFFORDABILITY (1986), which reviewed federal court cases and determined that punitive damages awards rose from an average of \$63,000 in 1970-74 to \$489,000 in 1980-84. Because the vast majority of punitive damages cases have historically been brought in state courts, an analysis limited to federal court cases does not yield statistically significant results. TEXACO, INC., PUNITIVE DAMAGES EXPLOSION: FACT OR FICTION? (1992) shows an increase in total punitive awards in California, Texas, Illinois, and New York from \$800,000 in the 1968-71 time period to \$312 million in the 1988-91 time period. This study, conducted in part by Texaco, examines awards in a limited number of states and includes the \$3 billion punitive damages award assessed in *Pennzoil Co. v. Texaco, Inc.*, No. 84-05905 (Tex. Dist. Ct. 1985).

51. Daniels & Martin, *supra* note 26, at 17 (the punitive damages rate "never exceeded one-quarter of all successful cases or one-fifth of all cases.").

52. "Fifteen of the twenty [research] sites have median punitive damage awards below \$40,000, thirteen of the sites have median punitive damages awards below \$30,000." *Id.* at 23.

53. *Id.* at 28 (the data show "relatively low, stable rates . . . generally below 10%").

54. *Id.* at 15 ("This . . . finding suggests that sweeping statements about national trends used to instigate reform should be viewed with a great deal of skepticism.").

55. Rustad, *supra* note 49, at 49.

56. *Id.* at 37.

57. Saks, *supra* note 49, at 1262.

58. WILLIAM M. LANDES & RICHARD A. POSNER, THE ECONOMIC STRUCTURE OF TORT LAW 185 (1987).

59. *Id.* at 302. The authors also reject the notion that punitive damages are being overused in product liability law. *Id.* Furthermore, they find them neither "frequent nor crushing in any absolute sense . . ." William M. Landes and Richard A. Posner, *New Light on Punitive Damages*, REG. 33, 54 (September/October 1986).

One wonders whether the characterization by tort reformers of the punitive damages system as out of control is anything more than self-serving hyperbole. Whether a crisis does or does not exist, it is premature to act on the changes demanded by business interests and tort reformers until it is clear that there is in fact a problem and until the character and dimension of the problem are much more clearly defined.

Absent convincing evidence of the necessity for limiting punitive damages, it would be extremely unwise to do so.⁶⁰ Punitive damages have historically served the critical function of deterring misconduct.⁶¹ But, the deterrence function is significantly compromised, and in many cases eliminated, if it is possible for a potential defendant to calculate *ex ante* her or his potential exposure to liability. Imagine, for example, the executives of TXO deciding whether to attempt to coerce Alliance into renegotiating the royalty arrangement, knowing that the scheme they were about to undertake was clearly wrongful. They believe that the profits to be made from convincing Alliance to reduce its share of the royalties will be substantial. They could, as economically rational actors, decide that going forward with the scheme is worth the risk of having to pay some amount of punitive damages if they are "caught." How differently the decision-making process may proceed from there if they are in Virginia, where their absolute exposure is \$350,000, or if they are in West Virginia, where their exposure is not limited. Indeed, TXO's claim on appeal that they were not on notice that the jury could return as large a punitive damages award as it did suggests that they undertook some form of cost/benefit analysis. A company may well decide, in economic terms, to risk \$350,000 for the sake of making a multimillion dollar profit; it is much less likely to take that risk when the penalty is unknown and could potentially create a substantial loss. It is precisely the uncertainty that makes one think again. Indeed, creating predictability in punitive damages may lead to exactly the type of cost/benefit analysis imagined above. It is a type of business decision-making that society should wish to discourage.⁶²

Business interests and tort reformers would be well advised to be careful what they wish for. In a number of jurisdictions, they have been successful in convincing legislatures to pass statutes limiting punitive liability. Yet, what will happen when future instances of horribly egregious business misconduct go essentially unpunished, or if decreasing levels of deterrence cause an increase in misconduct? There will undoubtedly be frenzied calls for more reform directed at clamping down on businesses that are "out of control," and the overreaction may be as distasteful to businesses as the crisis they claim to be facing now. In addition, a significant number of punitive damages awards come in business on business cases.⁶³ Business interests should consider that the reforms they are seeking also will limit their own ability to sanction

60. We are mindful of Michael Saks's warning that when the models lacking empirical validation form the basis of reform efforts, the effects may be contrary to the intentions of policy makers. Saks, *supra* note 49, at 1288-89.

61. "Extreme power discrepancies breed arrogant and highhanded conduct. The doctrine of punitive damages is one of the few remedies that can constrain a giant corporation that is willing and able to take advantage of its less powerful 'adversaries.'" Michael Rustad & Thomas Koenig, *The Historical Continuity of Punitive Damages Awards: Reforming the Tort Reformers*, 42 AM. U. L. REV. 1269, 1277 (1993).

62. See Appendix A for an analysis of what damages would have been assessed against TXO in each state with punitive damages legislation that employs a cap or multiplier.

63. See PETERSON ET AL., *supra* note 49, at 19.

egregious conduct when it is directed at them.

V. A PROPOSED APPROACH TO PUNITIVE DAMAGES LEGISLATION

It may well be too late in the day to argue against the statutory reform to punitive damages that have already taken place. The fact is that a majority of states have undertaken some reform, albeit at different levels of intensity, and it is unlikely that they will turn back the clock. Although we do suggest that those states that have passed reform legislation reconsider the wisdom of limiting the effectiveness of punitive damages, our proposal is directed primarily at those states that are contemplating a change. The data and policies underlying punitive damages do not support many of the reforms undertaken thus far. It is therefore important that future attempts be measured and that they be undertaken with a clear understanding of the data and with the traditional policies supporting the award of punitive damages in mind.

A. Caps

It defies logic to impose a cap on punitive damages. An arbitrary cap set at a fixed dollar amount suggests that we can put a price *ex ante* on outrageous behavior. Caps do lend predictability, as argued by their proponents. However, the quest for predictability hides the deterrent function of punitive damages.⁶⁴ In the extreme, a cap provides an incentive for really outrageous behavior. A cap could incite the rational actor to undertake a scheme or fraud that would net substantially more than the amount of the cap. Indeed, it is precisely the lack of predictability that gives punitive damages their deterrent effect. If an actor is contemplating insurance fraud or a scheme to engage in insider trading and is put off of the deed by the unknowability of the costs, then the law has performed its function elegantly. Thus, we conclude that caps are inappropriate vehicles for controlling punitive damages and should be avoided.

B. Multipliers

Similarly, we assert that setting punitive damages as a multiple of compensatory damages is equally inappropriate. Punitive damages have nothing to do with the claimant's actual damages and confusing the two works great mischief. Compensatory damages compensate and punitive damages punish and deter. The former focuses on the claimant and the latter focus on the defendant's conduct. To create mathematical formulae that tie one to the other ignores the punishment and deterrence function.⁶⁵ Once again, the desire to predict and calculate has overcome the original purpose of punitive damages. Using the *TXO* facts as an example, because *TXO* was unsuccessful in its attempt to shake down Alliance for a smaller royalty payment, Alliance's actual damages were very modest. However, the trier of fact clearly wished to send a message to *TXO* and others similarly inclined that this conduct is intolerable. The message is worth sending, whether or not the plaintiff has suffered great harm.

TXO talks about a reasonable relationship between the punitive award and the harm.⁶⁶ The harm to which the Court refers is both the harm that would have occurred had the defendants succeeded in their scheme and the harm that could occur in

64. See Mallor & Roberts, *supra* note 36, at 666.

65. "Lopsided ratios between punitive and compensatory damages awards are often necessary for the punishment and deterrence of powerful corporations." Rustad & Koenig, *supra* note 61, at 1277.

66. 113 S. Ct. at 2721.

the future if similar conduct is not deterred. That is not to be confused with a relationship between punitive and compensatory damages. TXO's conduct had great potential to do harm; it is merely fortuitous that extensive harm did not occur. The trier of fact must be free to consider what might have happened as a consequence of the defendant's behavior, not only what did happen, and punish accordingly.

Procedural safeguards such as remittitur, judgment notwithstanding the verdict, and appeal exist to assure that fact finders do not go to extremes. Legislation that duplicates existing safeguards is unnecessary and produces confusion about the law's policies. We propose that future legislation, to permit punitive damages to fulfill their traditional role, decouple the compensatory/punitive damages link that has been forged in some states.

C. Burden of Proof

Many states have increased the burden of proving punitive damages beyond the typical standard of proof by a preponderance of the evidence, either judicially or by legislation. This reform does less violence to the original concept of punitive damages than the others discussed. The conduct complained of in the usual punitive damages case is nearly criminal in nature, as are the sanctioning purposes of punishment and deterrence. Although it is not necessary to step up the proof to match that required in criminal cases,⁶⁷ inasmuch as the action is civil, it can be argued that the unusual nature of a punitive damages case justifies a heightened scrutiny of a plaintiff's allegations.⁶⁸ If successfully asserted, the defendant will be penalized financially for her or his conduct, above and beyond any harm caused to the plaintiff. The stakes can be very high; it is therefore appropriate to put the plaintiff to an extra measure of proof.

Likewise, the movement toward clear and convincing evidence does not wreak a significant hardship on the plaintiff. A plaintiff must establish that the defendant has engaged in willful or wanton conduct, or maliciousness, or oppression, or fraud in order to make a claim. If the conduct is truly egregious⁶⁹ and worthy of being punished, it is imperative that the proof demonstrate that convincingly. Furthermore, it is likely that the plaintiff with a legitimate claim can satisfy the requirement without incurring much more of an onus than proof by a preponderance of the evidence imposes. Once the plaintiff can demonstrate a scheme of defalcation and trickery, the scheme unravels and the proof easily meets the heightened standard. Therefore, we recommend that those states that undertake reform in this area consider increasing the burden of proof. It assures that punitive damages are limited to the extreme forms of behavior they were designed to sanction.

D. Payment to the State

State extraction of a portion of a punitive damages award is a novel approach

67. *But see* COLO. REV. STAT. ANN. § 13-25-127(2) (West 1989), which adopts proof beyond a reasonable doubt.

68. *See* William H. Volz & Michael C. Fayz, *McBride v. General Motors: Judicial Response To Constitutional Challenges In a Products Liability Punitive Damage Limitation Statute*, 29 AM. BUS. L.J. 367, 408-09 (1991).

69. Consider the "really stupid" and "really mean" characterization by the West Virginia Supreme Court of Appeals in *TXO*. 419 S.E.2d 870, 887-88 (W. Va. 1991). *See supra* note 24 for court's language.

taken by ten⁷⁰ states. Because the tactic does nothing to respond to concerns about the amount of or occasions for making the award, it is obviously designed to answer complaints about the windfall punitive damages supply to plaintiffs. Unlike most of the other criticisms leveled at punitive damages, the windfall argument is legitimate and worthy of response. We see value in returning a portion of the award to the state as a reasonable reaction to the windfall criticism. Therefore, we recommend that states adopt laws requiring that seventy-five percent of any punitive damages award, after deducting reasonable costs and attorney fees incurred by the plaintiff, be paid into the state coffers. Rather than going to the general treasury, the state's portion of the award should be earmarked for a special fund bearing a relationship to the harm. For example, a product liability judgment could be earmarked for public health, and an award in a consumer fraud case could be earmarked for consumer protection. If no suitable fund exists, the amount could be applied to court administration.

The figure of seventy-five percent is the upward limit of statutes passed to date. Although high, our recommendation of that figure is based on our attempt to respond to the reality that punitive damages do not compensate—some would say overcompensate—the plaintiff while, at the same time, preserving the incentive for plaintiffs to pursue legitimate claims.

We are mindful of the constitutional implications of this proposal. Different responses from Colorado,⁷¹ on the one hand, and Florida⁷² and Georgia⁷³ on the other, create confusion about the fate of this plan. Future appeals of the cases and the initiation of others will provide more guidance. Obviously, attempts to construct a statute along the lines we have proposed requires careful drafting to survive a constitutional challenge.

E. Multiple Claims

A difficult question of the appropriateness of punitive damages arises when one defendant is assessed over and over for harm arising out of the same conduct as different plaintiffs bring their claims.⁷⁴ Asbestos litigation provides a convenient example. Asbestos producers argue, with justification, that they should not be held liable for punitive damages in multiple suits for failure to warn about the harmful effects of asbestos. If the purpose of punitive damages truly is to deter and punish, then the first suit, if it properly takes into account the nature of the conduct, the potential for harm, and the amount necessary to discourage similar actions, adequately makes the point.

As with the windfall argument, we believe the overdeterrence argument has some merit. In response, we propose that states limit punitive damages awards arising from a single event to the first lawsuit and cut off subsequent claims. Inasmuch as punitive damages do not compensate the plaintiff and only punish the defendant, it does not do violence to plaintiffs' rights to limit awards to one.⁷⁵ Furthermore, the proposal en-

70. Colorado's has been overturned. See Appendix A.

71. *Kirk v. Denver Publishing Co.*, 818 P.2d 262 (Colo. 1991).

72. *Gordon v. Florida*, 608 So. 2d 800 (1992). The law now requires that 60% be paid to the state.

73. *Georgia v. Moseley*, 436 S.E.2d 632 (1993), cert. denied, 114 S. Ct. 2101 (1994).

74. See Mallor & Roberts, *supra* note 36, at 645; Victor E. Schwartz & Liberty Magarian, *Challenging the Constitutionality of Punitive Damages: Putting Rules of Reason on an Unbounded Legal Remedy*, 28 AM. BUS. L.J. 485, 490 (1990). See also *Dunn v. HOVIC*, 1 F.3d 1371, 1387 (3d Cir. 1993) (holding that multiple awards do not violate substantive due process).

75. Missouri permits sums previously paid as punitive damages to be credited to an award arising

courages a full hearing in the first suit to consider all the relevant criteria and set an award that adequately performs the punishment and deterrence functions.

We recognize that this proposal, without more, does not adequately treat the occurrence of multiple cases seeking punitive damages being prosecuted in different states. Naturally, one state cannot legislate against actions being brought in other states. The recommendation can succeed only if the plan achieves nearly universal adoption. Therefore, as with all situations in which state variability allows for differing results and, consequently, forum shopping, consensus among the states must be achieved to assure consistency in implementing legislation. Alternatively, states could refuse to entertain punitive damages claims if any other state has awarded them for the same event (i.e., against a different plaintiff), so long as the first proceeding provided a full hearing on the question of the adequacy of the damages. Obviously, a damage award that was limited by a statutory cap or a multiplier would not satisfy the requirement, nor would an amount paid in settlement. The approach is drastic, but gives states a chance to sort out the issue of multiple claims until uniformity is achieved.

In summary, future statutory reforms in punitive damages should be more circumscribed than those that have occurred. Earlier attempts have ignored the reasons for punitive damages and have, in our judgment, been driven by incorrect assumptions. It is time to put the data to good use. In this way, logical solutions can be crafted that are not driven by rhetoric and anecdote. The future use of caps and multipliers should be discouraged. Instead, reform efforts should be directed at increasing the burden of proving punitive damages, devising ways to support and encourage socially responsible behavior with the proceeds of such awards, and prohibiting multiple awards.

VI. CONCLUSION

States that have restricted defendants' exposure to punitive damages have acted in response to the hysteria generated by business interests and tort reformers rather than to any valid data about the business impact of punitive damages awards. The data that do exist does not support critics' claims that punitive damages are routinely awarded, awards are large, the size and frequency of the awards are increasing rapidly, and the problem is a national one. State legislatures have, therefore, "solved" a problem that may not exist at all and certainly does not exist at the level of magnitude charged by reformers. The statutes that they have passed have substantially limited or eliminated an important and powerful weapon to deter business misconduct.

One of the primary purposes of exposing business to the risk of punitive damages has traditionally been to deter, both individually and collectively, conduct by business that transcends the bounds of propriety. An essential element of the deterrent function is the unpredictability of the risk: If a business cannot determine *ex ante* the cost of engaging in misconduct, it cannot use a cost/benefit analysis to decide whether it will be profitable to so act. Another important purpose of punitive damages is to punish bad actors. If punitive damages are restricted to amounts that may be no more than an annoyance to a business with deep pockets, they will barely merit the attention of, let alone punish, the wrongdoer. In limiting business exposure to punitive damages,

out of the same conduct. MO. ANN. STAT. § 510.263(4) (Vernon Supp. 1993). See David G. Owen, *Punitive Damages in Products Liability Litigation*, 74 MICH. L. REV. 1258, 1325 (1976) for the proposition that the first plaintiffs to bring their claims deserve disproportionate awards for their cost and trouble.

the state reform legislation passed to date largely ignores the goals of imposing such damages.

Although it is probably too late to turn back the legislative clock, we encourage those states that have acted to reconsider and propose that no caps or rules that set punitive damages as multipliers of compensatory damages be set in those states that have not already done so. We recognize, however, that there are legitimate criticisms of the traditional punitive damages rules. These include that the preponderance of the evidence standard is too lenient, that punitive damages are a windfall to the plaintiff, and that permitting multiple awards for the same conduct is unfair and excessive punishment. To address these criticisms, we propose that the burden of proof be set at clear and convincing evidence, that states extract seventy-five percent of the punitive damages award, and that multiple awards be prohibited.

APPENDIX A

STATUTORY MEASURES RELATING TO PUNITIVE DAMAGES

State	Cap	Exceptions to the Cap	Clear & Convincing Evidence	Money to State	Bifurcated Trial	TXO Outcome
Alabama	\$250,000 Ala. Code § 6-11-21	Pattern or practice of wrongful conduct, actual malice, libel, slander, defamation	Ala. Code § 6-11-20(a)			Cap won't apply b/c of pattern or practice exception
Alaska			Alaska Stat. § 09.17.020			
California			Cal. Civil Code § 3294(a)		Cal. Civil Code § 3295	
Colorado	1:1 Colo. Rev. Stat. Ann. § 13-21-102	Ct. may increase or decrease under certain conditions but not beyond 3X actual damages	Beyond a reasonable doubt Colo. Rev. Stat. Ann. § 13-25-127(2)	Colo. Rev. Stat. Ann. § 13-21-102(4)		\$19,000 to \$57,000, depending on circumstances

State	Cap	Excep- tions to the Cap	Clear & Convinc- ing Evidence	Money to State	Bifurcat- ed Trial	<i>TXO</i> Outcome
Connect- icut	In product liability cases, pun. dam- ages can not ex- ceed 2X comps. Conn. Gen. Stat. Ann. § 52-240b					N/A
Florida	3:1 Fla. Stat. Ann. § 768.73	Class actions or if P is awarded more than 3X actual dams., it is pre- sumed excessive and P must show by C&C evidence that it is not	Fla. Stat. Ann. § 768.73 Adopting C&C only for awards above presump- tive cap of 3X comps.	35% Fla. Stat. Ann. § 768.73(2) [if pers. injury or wrongful death, money pd. to Public Med. Assis- tance Fund]		\$57,000, unless Alliance can show by C&C evidence that pun. award was not excessive

State	Cap	Excep- tions to the Cap	Clear & Convinc- ing Evidence	Money to State	Bifurcat- ed Trial	TXO Outcome
Georgia	\$250,000 Ga. Code Ann. § 51-12- 5.1(g)	Product liability actions and tort cases where it is found D acted with specific intent to cause harm. Ga. Code Ann. § 51-12-5.1 (e) & (f)	Ga. Code Ann. § 51-12- 5.1(b)	75% (product liability verdicts only) Ga. Code Ann. § 51-12- 5.1(e)(2)	Ga. Code Ann. § 51-12- 5.1(d)	
Idaho			No. Pre- ponderanc e of evid. by statute Idaho Code § 6- 1604(1)			

State	Cap	Excep- tions to the Cap	Clear & Convinc- ing Evidence	Money to State	Bifurcat- ed Trial	TXO Outcome
Illinois				At ct.'s discretion; funds pd. to Dept. of Rehabilita- -tive Ser- vices. Ill. Comp. Stat. Ann., ch. 735, art. 5, § 2- 1207 [formerly Ill. Rev. Stat. ch. 110, para .2-1207]		
Indiana			Ind. Code Ann. § 34-4-34-2			
Iowa			Iowa Code § 668A.1 (1)(a)	75% to Civil Repara- tions Trust Fund Iowa Code § 668A.1 (2)(b)		

State	Cap	Excep- tions to the Cap	Clear & Convinc- ing Evidence	Money to State	Bifurcat- ed Trial	TXO Outcome
Kansas	Lesser of \$5 million or D's highest gross w/i last 5 yrs. Kan. Stat. Ann. § 60-3701(e)	If ct. finds D expected to make profit in excess of cap, set dams. at 1.5 X D's expected profit Kan. Stat. Ann. 60-3701(f).	Kan. Stat. Ann. § 60-3702(c)	50% of awards made in med. mal. cases. Kan. Stat. Ann. § 60-3402(e) [to state health care]	Kan. Stat. Ann. § 60-3702(a)	Undetermined, either \$5 mill. or \$7.5 to \$12.5 mill., based on Alliance's figures
Ken- tucky			Ky. Rev. Stat. Ann. § 411.184(2)		Ky. Rev. Stat. Ann. § 411.186	
Mary- land					Md. Cts. & Jud. Proc. Code Ann. § 10-913(a)	
Minneso- ta			Minn. Stat. Ann. § 549.20 subd. 1(a)		Minn. Stat. Ann. § 549.20 subd. 4, upon request	
Missouri				50% Mo. Rev. Stat. § 537.675(2)	Mo. Rev. Stat. § 510.263, upon request	
Montana			Mont. Code Ann. § 27-1-221(5)		Mont. Code Ann. § 27-1-221(7)(a)	

State	Cap	Excep- tions to the Cap	Clear & Convinc- ing Evidence	Money to State	Bifurcat- ed Trial	TXO Outcome
Nevada	<p>≥\$100,000 then 3:1; <\$100,000 then max.</p> <p>= \$300,000 Nev. Rev. Stat. Ann. § 42.005(1)</p>	<p>Prod. liability Housing discrim. Toxic spills Defama- tion Bad Faith re. Insur- ance Coverage</p>	<p>Nev. Rev. Stat. Ann. § 42.005(1)</p>		<p>Nev. Rev. Stat. Ann. § 42.005 (3)</p>	\$300,000
New Jersey					<p>For product liabil- ity only. N.J. Stat. Ann. § 2A:58C-5</p>	
North Dakota	<p>Greater of 2:1 or \$250,000 (N.D. Cent. Code § 32-03.2- 11(4)</p>		<p>N.D. Cent. Code § 32-03.2- 11(1) & (5)</p>		<p>N.D. Cent. Code § 32-03.2- 11(2), upon request</p>	
Ohio			<p>Ohio Rev. Code Ann. § 2315. 21(C)(3)</p>		<p>Ohio Rev. Code Ann. § 2315.21 (C)(2) [damages deter- mined by ct.]</p>	

State	Cap	Exceptions to the Cap	Clear & Convincing Evidence	Money to State	Bifurcated Trial	TXO Outcome
Oklahoma	1:1 Okla. Stat. Ann. tit. 23, § 9(A)	Ct. finds C&C evidence of fraud, oppression, etc. Okla. Stat. Ann. tit. 23, Section 9(A).	Okla. Stat. Ann. tit. 23, § 9(A). Adopting C&C for exceptions to cap			Cap won't apply if C&C evidence found; otherwise \$19,000
Oregon			Or. Rev. Stat. § 41.315(1)	50%, after fees Or. Rev. Stat. § 18.540 [funds go to Crim. Injuries Compen. Account]		
South Carolina			S.C. Code Ann. § 15-33-135			
Texas	Greater of \$200,000 or 4:1 Tex. Civ. Prac. & Rem. Code Ann. § 41.007	Malice or intent'l tort Tex. Civ. Prac. & Rem. Code Ann. § 41.008				Cap won't apply b/c of intentional tort

State	Cap	Excep- tions to the Cap	Clear & Convinc- ing Evidence	Money to State	Bifurcat- ed Trial	TXO Outcome
Utah			Utah Code Ann. § 78-18- 1(1)(a)	50% in excess of \$20,000 to gen. fund Utah Code Ann. § 78-18- 1(3)	Utah Code Ann. § 78-18- 1(2)	
Virginia	\$350,000 Va. Code Ann. § 8.01- 38.1	No excep- tions				\$350,000