PUNITIVE DAMAGES AND THE RULE OF LAW: THE ROLE OF DEFENDANT'S WEALTH

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UNTIL recently, the rules governing punitive damages occupied a dark corner of the law. With the upsurge in product liability and other mass tort litigation, and increased "bad-faith" claims against insurance companies, these rules have been exposed to the brighter light of legal controversy. Yet one feature of the law of punitive damages remains unexamined: the long-standing rule that the defendant's wealth is relevant in determining punitive awards. In this article, we examine this position and the arguments that support it. We find them unpersuasive. In our view, the defendant's wealth is irrelevant to the goal of deterring socially undesirable conduct and is an improper consideration in assessing the basis for retribution. The law should be changed, and evidence of the defendant's wealth should be made inadmissible in private actions for punitive damages.[1]

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[1] How often the introduction of evidence of defendant's wealth into evidence actually results in abuses is difficult to ascertain, but there are many cases suggestive of such abuse. For example, in Spaeth v. Union Oil Company of California, 762 F.2d 865 (10th Cir. 1985), a jury awarded the plaintiff $22,807 compensatory and $3,000,000 punitive damages for breach of an implied covenant in an oil and gas lease to protect against drainage. There was evidence in the case that the defendant's net worth was approximately three-and-one-third billion dollars. (After a first appeal, the plaintiff remitted $1,000,000 of the punitive award, and the remainder was upheld on a second appeal.) Similarly, in Robinson v. Winn-Dixie Stores, Inc., 447 So.2d 1003 (Fla. Dist. Ct. App. 1984), the court upheld an award of $750,000 in punitive damages for false imprisonment and malicious prosecution for shoplifting, stating that the "defendant is a multimillion dollar corporation so economic castigation is not an issue." *Id.* at 1004. It seems highly probable that the juries in these cases considered the defendants' wealth in assessing punitive damages. Many other decisions provoke similar suspicions. See also Hatrock v. Edward D. Jones & Co., 750 F.2d 767 (9th Cir. 1984) ($200,000 punitive award not excessive because it "represents only one-third of one percent of [defendant's] gross revenues"); Roy Export, Etc. v. Columbia Broadcasting System, Inc., 503 F. Supp. 1137 (S.D.N.Y. 1980) ($410,000 punitive award not excessive in light of

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Underlying our arguments on both deterrence and retribution is our belief that evidence of the defendant's wealth threatens norms linked to the rule of law. Most obviously, it invites punishment based on status—on who the defendant is, rather than on what the defendant has done. Considerations of that sort may be impossible to squeeze out of the system entirely, but that is no reason to tolerate them unnecessarily. More subtly, and more dangerously, evidence of the defendant's wealth invites the jury to speculate about conduct not proved in court. For a wealthy defendant with recurrent business affairs, the assumption too easily can be made that this instance is only the tip of the iceberg. The jury that is satisfied with the proof of one specific instance of misconduct too readily may conclude that similar, undetected incidents have occurred as well. Punishment may then be based on undisciplined speculation about what lies below the surface. Admitting evidence of the defendant's wealth invites conjecture of this sort, as well as judgments based on mere status, and is for that reason doubly objectionable.

I. Compensatory Damages: A Comparison

The two major purposes for awarding compensatory tort damages are deterrence of socially undesirable conduct and compensation of the victims of such misconduct. Other purposes that might be specified include the victim's dignitary interest in bringing a grievance before an impartial decisionmaker and the encouragement of suits that will inform other agencies of government of problems calling for their attention.

None of these concerns is thought to justify inquiry into the defendant's wealth. Evidence of defendant's wealth is irrelevant to the purposes of compensatory damages and, hence, irrelevant to the issues that arise in an ordinary tort suit. Consequently, evidence of defendant's wealth is not admissible in a suit for compensatory damages. Indeed, such evidence is not only inadmissible but also prejudicial. Mere mention of defendant's wealth is likely grounds for a mistrial, as is mention of the related issue of defendant's liability insurance. Examining these points in more detail will set the stage for considering the role of defendant's wealth in suits for punitive damages.

CBS's size; "award must be 'of sufficient substance to smart . . . the offender' "), aff'd, 672 F.2d 1095 (2d Cir.), cert. denied, 459 U.S. 826 (1982); Maxey v. Freightliner Corp., 450 F. Supp. 955 (N.D. Tex. 1978) (in justifying $10 million punitive award: "The larger the company, the larger the award of punitive damages must be in order to bring this message [of punishment and deterrence] home"), aff'd, 665 F.2d 1367 (5th Cir. 1982); Tetuan v. A. H. Robins Co., Inc., 738 P.2d 1210 (Kan. 1987) ($7.5 million punitive award not excessive in view of evidence of defendant's $563.5 million net sales and $58 million net earnings); Palmer v. A. H. Robins Co., 684 P.2d 187 (Colo. 1984 en banc) ($6.2 million punitive award affirmed in light of "the financial ability of the offender to pay").

First, and most importantly, the defendant's wealth is irrelevant to deterrence. Whether the defendant is rich or not simply has no logical bearing on the inhibitory role of the threat of tort liability. Deterrence theory is based on the (usually and to one or another extent plausible) assumption that actors weigh the expected costs and benefits of their future actions. Specifically, a potentially liable defendant will compare the benefits it will derive from an action that risks tort liability against the discounted present expected value of the liability that will be imposed if the risk occurs. Whether a defendant is wealthy or poor, this cost-benefit calculation is the same. If, as is likely, a wealthy defendant derives no greater benefit from a given action than a poor defendant, then both will be equally deterred (or equally undeterred) by the threat of tort liability. A defendant's existing assets do not increase the expected value of a given future action. Therefore they do not require any adjustment in the level of sanction needed to offset that expected value. The defendant's wealth or lack of it is thus irrelevant to the deterrence of socially undesirable conduct, and evidence on the subject is inadmissible in the typical tort action claiming compensatory damages.

Of course, this is not to say that admitting evidence of a defendant's wealth would have no deterrent effect. Other things being equal, juries do seem to impose greater liability on defendants whom they suspect of having substantial assets,[2] and this phenomenon may tend to increase the deterrence of wealthy defendants. But greater liability for poorer defendants would also increase deterrence. Generally speaking, any increase in liability would increase deterrence.[3] If maximum deterrence were the object, then any increase in tort liability could be justified on that ground. But, of course, tort law's goal is not maximum deterrence, but optimal deterrence, and in these terms, augmenting liability for wealthy defendants is illogical. If the rules of tort law create optimal deterrence in the absence of evidence of the defendant's wealth, then admitting such evidence would overdeter wealthy defendants. If, on the other hand, the rules of tort law create inadequate deterrence in the absence of evidence

[2] For example, analyses conducted by the Institute for Civil Justice of the Rand Corporation show that juries are likely to award substantially more in a product liability, malpractice, or work injury case than in an auto accident case for injury of the same severity. See Audrey Chin & Mark Peterson, Deep Pockets, Empty Pockets: Who Wins in Cook County Jury Trials 52–56 (1985).

[3] The limiting case is the potential defendant whose assets are exceeded by the expected value of the risk it takes. It might make sense to threaten such a defendant with liability for punitive damages up to the value of its assets in cases where the damages such risk-taking actually causes are exceeded by those assets. Conceivably, evidence of the defendant's wealth would aid in achieving this purpose. But the necessary calculations would be extraordinarily complex (Was the expected value of a risk taken but not realized greater than the defendant's assets?) and, in any event, this odd case lies very far from the usual situations where evidence of the defendant's wealth is admitted.

of defendant's wealth, then the cure is to raise the expected costs to all defendants, not just to those with great wealth. Either way, there is no deterrence justification for considering the defendant's wealth.

Defendant's wealth is also irrelevant to the compensation aims of conventional tort liability. The successful tort plaintiff is entitled to recover in full for all losses proximately resulting from the action for which the defendant is held liable. The wealth available to the defendant to satisfy this obligation may be an important practical concern in settlement negotiations, but it is irrelevant to plaintiff's right of recovery. If evidence of the defendant's wealth were admissible, and if the jury took such considerations into account, the plaintiff's right to recover and the magnitude of the defendant's liability would depend on the identity of the defendant, rather than on the nature of the defendant's action and the extent of the plaintiff's loss. Although juries sometimes act as if they knew the extent of the defendant's wealth—to the point that commentators have coined the term "deep pocket" to explain the phenomenon—the law governing recovery of compensatory damages excludes such considerations as best it can.

II. Punitive Damages and Deterrence

The conclusion to be drawn from the preceding discussion is obvious but important: given that defendant's wealth is irrelevant to compensatory tort liability, any justification for considering defendant's wealth in actions for punitive damages must be specific to that context. Contrary to the assumptions of many, there is no general argument from deterrence to support admitting evidence of defendant's wealth. If there were, it would apply as well to compensatory tort liability. The question then becomes: Is there something special about deterrence in punitive tort liability that would justify a different rule?

The obvious, and ultimately the correct, answer is no. Indeed, we have not seen focused argument to the contrary. One possible argument for considering a defendant's wealth in assessing punitive damages may actually help to explain the origin of the practice. Some individuals may be willing to pay compensatory damages in order to obtain the satisfaction of inflicting the harm they intend. The sting of a punitive award is necessary to deter these individuals, who cause harm out of spite or malice. On this view, the wealth of such individuals is relevant to the sting that they can be expected to suffer from a punitive award.

As applied to those individuals who derive gratification from harming others, this argument may be plausible. But it is not plausible outside that context. Today, the most frequent and economically disruptive punitive awards are levied against organizations, not against individuals. Yet, organizations typically do not and usually cannot act out of spite or malice. In addition, the degree of misconduct necessary to support imposing liability for punitive damages has now declined to the point where proof of spite or malice usually is not required. Consequently, whatever strength this original justification for admitting evidence of a defendant's wealth may once have possessed has now largely disappeared.

Perhaps the most nearly plausible deterrence argument begins with the premise that liability for punitive damages can neutralize the effects of underenforcement of compensatory tort liability.[4] The premise is not implausible. For example, in cases of mass exposure to toxic substances, some people may contract diseases without being able to trace the causal connection between exposure and their illnesses; or persons may suffer losses too small to warrant suit for compensatory relief. Similarly, if an insurance company wrongly denies claims by many policyholders, few may actually bring suit.

For these, and perhaps other, reasons, traditional compensatory tort liability may yield inadequate deterrence.[5] Additionally, it might be true that punitive damages work, in a rough and ready way, to correct that shortfall. But it does not follow that the deterrence argument for augmenting compensatory liability with the threat of punitive damages justifies evidence of the defendant's wealth. That assumption is flawed for at least two reasons.

First, there is no logical, necessary, or even plausible connection between the extent of the defendant's wealth and the amount of underenforcement. The amount of underenforcement in mass tort cases, for example, is likely to depend on factors completely unrelated to the extent of the defendant's wealth. They include whether the plaintiffs' losses are minor or severe; whether the action causing plaintiffs' injuries is easy or difficult to prove; whether that action was sudden and violent or gradual and insidious; and whether the injuries or diseases suffered by the plain-

[4] See, for example, Dorsey D. Ellis, Jr., Fairness and Efficiency in the Law of Punitive Damages, 56 S. Cal. L. Rev. 1, 26–33 (1982).

[5] Traditional compensatory tort liability, however, may also yield excessive deterrence. Even successful defendants must pay their lawyers and bear their own litigation expenses. Some potential defendants may therefore conclude that a given risk is not worth taking because of the cost of defending suits brought when that risk materializes, regardless of whether, on balance, the risk would be worth taking were it not for this cost. Similarly, a series of new doctrines that relax plaintiffs' burden of proof regarding causation may generate liability in cases where the harm in question was not caused by the defendant. This approach may also produce overdeterrence. See Kenneth Abraham, Individual Action and Collective Responsibility: The Dilemma of Mass Tort Reform, 73 Va. L. Rev. 845, 859–68 (1987).

tiffs are commonly caused by a variety of actions or substances, or instead can be caused only by a unique action or substance for which the defendant is responsible.

These factors do not correlate with defendant's wealth. For example, while there may be underenforcement of tort liability for certain forms of exposure to toxic substances, there is no reason to suppose that there is any underenforcement of tort liability for airplane crashes, yet both kinds of actions typically involve large corporate defendants. Insofar as we can assess, the relation between underenforcement of compensatory tort liability and defendant's wealth is nothing more than random.

Second, even if the wealth of the defendant were related to the probability of underenforcement of its tort liabilities, no additional liability should be imposed absent specific proof of underenforcement in the case at hand. Otherwise, the defendant would be held liable for punitive damages, in potentially ruinous amounts, without the opportunity to disprove the facts on which such liability is based.

The only rational deterrence explanation for taking defendant's wealth into account is one that is rarely voiced. It is the speculation that a wealthy defendant, usually a large corporation, may have engaged in a *pattern* of misconduct, of which any given case is merely illustrative. Thus, the insurance company shown to have denied one claim in bad faith may be assumed to have a corporate policy or practice of denying covered claims. On this assumption, exaggerating the punishment for wealthy defendants would not be illogical. It could be seen as a corrective for the systematic underdeterrence that results from underenforcement of compensatory tort liability. If only a few cases of corporate wrongdoing are brought to light, those instances might be punished all the more severely in order to offset corporate gain from the undiscovered cases. All this is plausible *if* one assumes that the defendant's size or wealth is a marker for a pattern of repetitive (and significantly undiscovered) misbehavior.

This assumption may not be altogether irrational, but it is surely wrong. Of course, it is descriptively wrong in many cases, but more than that, it is normatively wrong. Punishment cannot fairly be based on unaided speculation about what the defendant might or might not have done in various unspecified circumstances not then before the court. Yet that is exactly what evidence of the defendant's wealth invites—unaided speculation about the defendant's conduct in other cases. Of course, if a pattern of repetitive misbehavior is actually proved in court, that is another matter. In that case, the entire course of misconduct rightly may be considered. But where no such pattern is proved, inviting the jury simply to assume its existence is plainly unfair. Whether that unfairness rises to the level of a constitutional violation is a question we do not pause to discuss. We think it sufficient to say that calculating deterrence based on wholly speculative inferences that might be drawn from evidence of the defendant's wealth falls grossly short of the standards of fairness and accuracy to which our system of civil justice aspires.

III. Punitive Damages and Retribution

Similar concerns arise when the focus shifts to retribution. In our view, retribution is the only plausible justification for considering the defendant's wealth in awarding punitive damages. The idea is that it takes a big slap to hurt a big defendant. If, in fact, wealthy defendants are indifferent to small sanctions, it may seem sensible to consider the defendant's wealth in fixing penalties. Some such notion underlies the appeal to juries that plaintiffs' lawyers make and defense counsel fear: "Look at the such-and-so corporation. Its net worth is measured in *billions* of dollars. Anything less than a million-dollar fine won't even get its attention."

This kind of reasoning does have a modest plausibility. At least at first viewing, the retributive justification for considering the defendant's wealth seems to make sense. In our view, however, this argument is subject to very substantial objections. Those objections are both factual and normative. First, the retributive justification for considering the defendant's wealth is factually shaky, because it rests on certain assumptions that cannot be proved. Second, taking the defendant's wealth into account in assessing the need for retribution threatens commonly accepted normative values associated with the phrase "the rule of law."

The factual weakness of the retributive justification for considering defendant's wealth is that it rests on interpersonal comparisons of utility. Even as between individuals, such comparisons are fraught with difficulty. Liability for $10,000 is likely to hurt a given defendant more than liability for $1,000, but whether liability for $10,000 will hurt defendant A more than defendant B is anybody's guess. That one defendant may have a greater net worth than the other does not resolve the problem. The wealthier defendant may value his or her money more than the less wealthy defendant. The assumption that larger penalties are needed to inflict a given pain on wealthy defendants is speculative or, at the very least, unsubstantiated.

Where the defendant is a corporation, the pain-infliction problem becomes even more perplexing.[6] The corporation does not and cannot "suf-

[6] Ironically, large, wealthy firms may have more valuable reputations and, therefore, more to lose by disclosure that they engaged in deliberately risky activity than smaller, poorer firms. If the reputations of wealthy firms function as a bond for future performance, then there may actually be a negative correlation between a defendant's wealth and the probability that it has engaged in other unproved, but highly risky, activities.

fer.'' Its operations can be impeded and its productive capacity can be reduced, but both these reductions in operating strength are equal to the amount of money it loses. The value of the corporation's assets prior to the imposition of liability does not affect the size of the reduction in operations that results from the liability. This is a function of the size of the liability, not the size of the defendant. Of course, by reducing a corporation's profitability, punitive liability imposes pain on the corporation's shareholders. But if one could suppose that these shareholders somehow deserve retribution—as distinguished from the need to enhance their incentive to assure that corporate management does not engage in excessively dangerous activities—one is led back into the difficulty of ascertaining how much ''pain'' an individual will feel if a given amount of liability is assessed. Yet here the problem is greatly magnified, given the need to determine the aggregate ''pain level'' of the community of shareholders.

Conceivably one could argue that, in the corporate context, differences in interpersonal utilities among shareholders cancel each other out. All corporations with a given net worth could therefore be assumed to suffer the same amount of pain from a given punitive damages award. But if one is serious in attempting to impose pain on corporate shareholders and serious in the belief that a party's wealth is relevant to the amount of pain he suffers from a given liability, then the cancel-out theory will not hold. For even if the shareholders of different corporations have similar utility functions and pain thresholds, they do not necessarily have similar wealth levels. Consequently, in the corporate context, the wealth theory also would seem to require that the wealth of shareholders be admitted into evidence in an action for punitive damages. That would obviously be a practical nightmare. The lengths to which one would have to go to begin to make sensible distinctions are a kind of symptom of the unwisdom, as well as the futility, of the enterprise.

Even apart from these concerns, defining ''the'' corporation whose wealth is to be measured can be an exercise in arbitrariness. What if one corporation uses a wholly owned but adequately capitalized subsidiary, and another uses an internal subdivision? What if the earnings of the former are positive, but the subsidiary itself is not profitable? The possibilities are many since any corporation consists of an elaborate network of contracts. Yet there are no obviously fair or even coherent criteria for deciding how sensitive punitive damages law should be to the structure and form of these contracts.

More important, basing retribution on the defendant's wealth is normatively objectionable. Ordinarily, retribution is geared to the nature of the wrongful act and/or to the harmful consequences that flow from it.[7] Punishment based on the characteristics of the actor must be viewed with suspicion. The reasons are obvious. At the extreme, punishment based on the characteristics of the actor, rather than on specific misconduct, threatens fundamental notions of freedom from government constraint.[8] The traditional criminal-law requirement of an actus reus works to constrain criminal liability within a tolerable sphere and to mark off a boundary of individual accountability to the collective will.[9] To put the same point less grandly, punishment based on the characteristics of the actor invites judgment based on prejudice, on caprice, on unaccountable ad hoc reactions. The worst case, of course, is backdoor reliance on illicit motivation—racial animosity, religious prejudice, class bias, or refracted political opinion. Even where no such motive arises, punishment based on the characteristics of the actor invites erratic and random responses to concerns that have nothing to do with specific misconduct.

These concerns lie just below the surface in punitive damages litigation. Defendants are subjected to punishment over and above any compensatory obligation. This punishment is administered without the protections

[7] The potential divergence between these two criteria is usually unimportant. Ordinarily, the consequences that flow from a wrongful act are closely related to, and not substantially divergent from, the nature of the risk that made the act wrongful. In such circumstances, there is only a theoretical interest in distinguishing the magnitude of the wrong from the magnitude of the resulting harm. In some cases of inadvertent risk creation, however, a disparity may arise. Consider drunk driving. Driving under the influence creates a small but significant risk of causing the death of another. Should the magnitude of the sanction depend on whether that risk is realized? In Anglo-American criminal law, the traditional answer has been "yes," but modern reforms (in the content and penalty structure of inchoate offenses and in the definition of substantive crimes of risk creation) have tended consistently to lessen that emphasis. The issue is plainly open to debate, but we incline toward the view that the theoretically correct answer is that the nature of the wrong, not the magnitude of the resulting consequences, should set the retributive basis for punishment. Departures from this position are in part concessions to history, and in part they reflect the generally sensible intuition that resulting harm is evidence of the nature of the risk. Thus, in drunk driving cases, we may believe that not all instances of drunk driving (or drunk drivers) are the same and that causing the death of another is not merely bad luck but is indicative of some additional risk creation (for example, speeding) beyond the mere fact of driving under the influence. In any event, for present purposes we assume either that risk creation and resulting harm are not significantly different or that, if they are, both may be taken into account. This rather relaxed view of the matter serves to isolate the unusual and inappropriate emphasis on defendant's status.

[8] See Robinson v. California, 370 U.S. 660 (1962).

[9] Other reasons for the act requirement in criminal law are an evidentiary function in corroborating other proof of evil intent and an equally important function in differentiating daydreams from fixed intentions. See John Calvin Jeffries & Paul B. Stephan, Defenses, Presumptions, and Burden of Proof in the Criminal Law, 88 Yale L. J. 1325, 1371 n.130 (1979).

that guard against unwarranted criminal conviction. In many jurisdictions, juries are told that they can punish the defendant where it is merely more likely than not that the defendant deserves punishment.[10] Moreover, the substantive criteria for imposing punitive liability are notoriously unconstraining.[11] And juries are allowed to hear evidence on punitive damages before determining compensatory liability. The prospect of prejudice is obvious.[12]

Into this loose and flabby proceeding comes evidence of the defendant's wealth. The admission of this evidence threatens to bring the politics of resentment into the courtroom. Particularly where a large corporation is involved, juries are tempted to ad hoc redistribution of wealth. Of course, some such instinct might arise in any case, but admitting evidence of the defendant's wealth encourages and legitimates the Robin Hood reaction. It validates an extralegal approach to civil punishment and in doing so offends the values of fairness and regularity conventionally captured by the phrase "the rule of law."

This analysis suggests that the retributive purposes of the imposition of punitive damages cannot be consistently and fairly served by admitting evidence of the defendant's wealth. Such evidence has no bearing on the gravity of the defendant's wrong; admitting such evidence risks allowing the finder of fact to speculate that the defendant has committed other, unproved wrongs; and evidence of the extent of the defendant's wealth cannot assist any effort to impose consistent degrees of punishment on defendants. In short, the admission of evidence of the defendant's wealth violates a principal feature of the rule of law in our system—the right of either party, plaintiff or defendant, to have his or her case adjudicated on the basis of the evidence before the court.

IV. Conclusion

In our view, the admission of evidence of the defendant's wealth in punitive damages cases is unwise. The practice fails to achieve any legiti-

[10] See James Ghiardi & John Kircher, Punitive Damages § 9.12 (Supp. 1987).

[11] Courts use a variety of vague terms to describe the quality of behavior required to support awards of punitive damages. As one treatise summarized, "There must be circumstances of aggravation or outrage, such as spite or 'malice,' or a fraudulent or evil motive on the part of the defendant, or such a conscious and deliberate disregard of the interests of others that the conduct may be called wilful or wanton." W. Page Keeton *et al.*, Prosser and Keeton on Torts 9–10 (5th ed. 1984).

[12] One need only imagine what would happen if a prosecutor tried to introduce evidence of past crimes or arrests or police suspicions to aid its case in chief in a criminal prosecution. The defense counsel would rightly scream bloody murder.

mate purpose, and it threatens important systemic values of the rule of law. No doubt there are other settings in which those values should be more zealously guarded. But small reforms should not be dismissed simply because they do not solve large problems. We believe that restricting admission of evidence of the defendant's wealth is a sensible small reform in the law of punitive damages.