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Recent Application Of State Farm v. Campbell In Bad-Faith Cases

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Commentary

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I. Introduction

The last decade of jurisprudence has seen significant changes regarding the amount of punitive damage awards – begging the question, how much is too much? The United States Supreme Court decided *State Farm Mutual Automobile Insurance Co. v. Campbell*[1] in 2003 – discussing three guideposts for determining whether punitive damages awards were excessive under a due process analysis.[2] The reasoning in *Campbell* remains critical in bad-faith cases where plaintiffs often seek an award of punitive damages. Numerous courts have applied the constitutional "guidance" provided in *Campbell* since 2003 and these decisions reveal the nuances in how the three guideposts are interpreted and applied in different scenarios. But did *Campbell* really provide as much guidance as practitioners had hoped?

Some eight years after *Campbell*, however, it is difficult to predict how a court will rule as to the excessiveness of a punitive damages award. The purpose of punitive damages is to "punish and deter" reprehensible conduct.[3] Recent decisions on this issue illustrate how each guidepost is being applied in practice and considerations to keep in mind when evaluating the possibility of punitive damages.

II. Application Of The Guideposts Since *Campbell*

In *Campbell*, the Supreme Court reviewed an award of punitive damages of $145 million in a third-party bad-faith case against State Farm where the compensatory damages awarded were $2.6 million.[4] *Campbell* arose out of a car accident in which the insured, Campbell, caused a serious accident (leaving one person dead and another permanently disabled).[5] State Farm contested liability for this accident, declined to settle the claims for the $50,000 policy limits, ignored its own investigator's advice, and took the case to trial (assuring Campbell and his wife that they had no liability for the accident, that State Farm would represent their interests, and that they did not need separate counsel).[6] The jury returned a verdict of three times the policy limits. Campbell then retained his own counsel to appeal the verdict. When Utah's highest court denied Campbell's appeal, State Farm paid the entire excess judgment. The Campbells then initiated the bad-faith action against State Farm.

The Supreme Court based its analysis of the punitive damages award (and whether it really was "too much") on consideration and application of the following three "guideposts":

(1) The degree of reprehensibility of the defendant's misconduct;

(2) The disparity between the actual or potential harm suffered by the plaintiff and the punitive damages award; and

(3) The difference between the punitive damages awarded and the civil penalties authorized or imposed in comparable cases.[7]

The Supreme Court noted that the most important "indicium of the reasonableness of a punitive damages award is the degree of reprehensibility of the defendant's conduct."[8] The Court held that few awards exceeding a single-digit ratio between punitive and compensatory damages, to a significant degree, will satisfy due process.[9] *Campbell* did not lay out a specific mathematical formula for calculating a punitive damages award, but rather, gave insight and guidance on how to evaluate whether the amount awarded was reasonable in light of the harm caused. The Court stated "because there are no rigid benchmarks that a punitive damages award may not surpass, ratios greater than those we have previously upheld may comport with due process where 'a particularly egregious act has resulted in only a small amount of economic damages.' "[10]

Campbell attempted to reign in punitive damage awards while remaining flexible. That flexibility leaves discretion to the courts reviewing punitive damage awards when analyzing and applying the three guideposts. Notably, the highest ratios that are upheld (for example of 16:1) often appear outside the context of bad-faith litigation in mass tort cases.[11]

A. Reprehensibility

Reprehensibility, the key guidepost when evaluating a punitive damages award, comes down to the conduct of the insurer and how the court views that conduct. The court will consider the following factors when it determines the "reprehensibility" of the conduct:

(1) whether the harm caused was physical as opposed to economic;

(2) whether the tortious conduct evinced an indifference to or a reckless disregard for the health or safety of others;

(3) whether the target of the conduct has financial vulnerability;

(4) whether the conduct involved repeated actions or was an isolated incident; and

(5) whether the harm was the result of intentional malice, trickery, or deceit, or merely accident.[12]

The first "sub-factor," considering whether physical harm was caused, can be used to justify a higher level of reprehensibility. In *Moore v. American Family Mutual Insurance Company*,[13] the insured purchased a duplex that had to be moved because it was located in a flood plain.[14] Five weeks before the deadline to move the duplex a fire destroyed the structure.[15] American Family claimed that the fire was a result of arson and alleged that the insured was responsible for the arson, and denied the claim.[16] Mr. Moore brought suit against American Family for breach of the insurance contract and bad faith in denying his claim.[17]

At trial there was evidence presented that the insurer reported to the Property Insurance Loss Register that Mr. Moore's claim had been denied for arson and fraud.[18] There was also testimony that once information is submitted to this database it can never be removed and that insurance companies do not insure arsonists.[19]

The jury found in favor of Mr. Moore and awarded him $48,414.97 on his breach of contract claim, $1.15 million in actual damages (the court refers to this amount as "actual damages," however, it seems to really refer to the amount awarded on the claim for bad faith), and $1.15 million in punitive damages.[20] Considering reprehensibility, the Eighth Circuit noted that the injuries were not merely financial because in the insurer's allegation that the insured was an arsonist caused the insured emotional distress, chest pain, trouble sleeping, and caused him to smoke more. Also, since accusing someone of being an arsonist implies a serious felony, the court found that this act constituted an indifference to or disregard of the insured's financial, emotional, and physical well-being.[21] There was also evidence that the insured was financially vulnerable and that the treatment of this claim was typical. Thus, the court held that there was sufficient evidence of "reprehensibility" to support the award.

In another recent decision, the Third Circuit (in *Jurinko v. Medical Protective Co.*) discussed and applied the factors for reprehensibility and found that the harm caused in that case was not actually physical harm (and ultimately reduced a punitive damages award).[22] This action arose out of a medical malpractice claim that the Jurinkos had against Dr. Marcincin, an insured of Medical Protective.[23] A jury found the doctor liable for medical malpractice and awarded the Jurinkos $2.5 million in damages ($1.3 million over the coverage of his policy).[24] The doctor then assigned his bad-faith claim

against Medical Protective to the Jurinkos.[25] During the negotiations of the underlying actions there had been recommendations at a pre-trial settlement conference to settle the case between $1.5 million and $2 million.[26] The doctor wanted to settle the action at that time but it proceeded to trial.[27] Then during the trial the plaintiff offered to settle the case for $1.1 million, but Medical Protective never offered more than $50,000 (even though their notes indicate they valued the case at between $750,000 and $1 million).[28] The claims adjuster's testimony was the most damaging in the bad-faith action – he testified that he acted unreasonably and irresponsibly in the negotiations and denied the doctor an effective defense by appointing the same attorney to represent both physicians involved.[29]

In the bad-faith action, the jury found that Medical Protective acted in bad faith and awarded $1,658,345 in compensatory damages (for the bad faith) and $6,350,000 in punitive damages. The Third Circuit reviewed the award of punitive damages to determine if the award was excessive. This court reviewed the three guideposts and in particular discussed the sub-factors for determining "reprehensibility." The court held that causing the insured to undergo a lengthy trial and be embarrassed in the community does not constitute "physical harm" for purposes of the reprehensibility analysis.[30] This court also found that the actions of Medical Protective did not evince "an indifference to or a reckless disregard for the health or safety of others."[31] Ultimately, this court reduced the award and found that the doctor only suffered economic harm that was easily measured – the amount of the excess judgment.[32] The court stated that "Medical Protective's acts were egregious, but not likely 'particularly' egregious."[33]

The most common factors for reprehensibility that courts find and rely on in bad-faith cases are that the target of the conduct was financially vulnerable, that the conduct involved repeated actions, and that the conduct was intentional. Regarding the financial status of the target of the conduct, there is no clear guidance on what is and is not "financial vulnerability." It seems that the vast majority of all plaintiffs could in some way argue that they were financially vulnerable.

Discussion of the repeated actions is also commonly implicated because plaintiffs will seek to show that the actions taken were common and part of the insurer's regular business practices.

III. Ratio Between Harm And The Punitive Damages Award

Campbell attempted to set some limits and certainly attempted to provide a more clear guideline for what ratios are presumptively excessive (as well as ratios that are presumptively acceptable). However, *Campbell* was very careful not to require any rigid formula – particularly egregious conduct could justify a higher ratio.[34] Thus, the reprehensibility and the ratio guideposts are intertwined. Courts then will often justify a higher ratio by the conduct based on this language. For this guidepost a court will compare the compensatory damages at issue (for the bad faith) and compare that number to the amount awarded in punitive damages. *Campbell* stated that "the Court has been reluctant to identify concrete constitutional limits on the ratio between harm, or potential harm, to the plaintiff and the punitive damages award," but that "in practice, few awards exceeding a single-digit ratio between punitive damages and compensatory damages will satisfy due process."[35]

In *Haberman v. Hartford Ins. Group*,[36] the court reviewed an award of $548,000 for breach of contract, $5,000 for the bad-faith claim and $100,000 in punitive damages on the bad-faith claim.[37] The Hartford argued that the punitive damages award of $100,000 is grossly excessive (in comparison to the $5,000 award for the bad faith), violating its due process rights.[38] Hartford argued that the ratio between the compensatory award for the "bad faith" claim and the award for the punitive damages is 20:1 and thus does not comport with due process. The *Haberman* court cited to *Campbell* for the proposition that there are no rigid benchmarks and that greater ratios may comport with due process where a particularly egregious act has resulted in only a small amount of economic damages.[39] Thus, the ratio guidepost essentially referred the court back to a reprehensibility analysis to determine if the conduct was egregious.[40]

While analyzing the ratio, it is also crucial to determine which amount the punitive damages award will be compared to. Courts will look to the amount awarded for the bad faith (and also attorney's fees awarded for pursuing bad faith, not the damage resulting from the breach of contract). Where $48,000 was awarded for

breach of contract and $1.15 million was awarded for the bad-faith claim, the amount awarded for the bad faith applied and a punitive damages award of $1.15 million constituted a 1:1 ratio (not a 20:1 ratio as argued by the insurer).[41] Another court found that the proper number to compare with the punitive award included not only the $2,000 awarded on the contract claim but also another $135,000 is attorneys' fees and costs that were awarded as part of their bad-faith claim. Thus, the court found the ratio to be 1:1 and acceptable.[42]

The ratio guidepost provides the most definitive limit on a punitive damages award. While the courts are not bound to any specific ratio, when faced with a disproportionately high ratio, the *Campbell* decision will force the courts to analyze the ratio and the conduct to determine if the award was excessive and, at the least, justify why this high award is reasonable under the particular circumstances.

IV. Punitive Damages And Civil Penalties

The third guidepost – consideration for civil penalties – is the black sheep of the excessiveness analysis. Often you will find very little analysis of this guidepost in an opinion (usually following a lengthy discussion of reprehensibility and the ratio). This guidepost intends to give some deference to the legislature[43] – *e.g.*, what punishment does the legislature believe is appropriate for specific conduct.[44] It seems logical that if the purpose of punitive damages is to punish and deter specific conduct, then the punishments for that conduct proscribed by the law of the state would be relevant to the consideration. However, in practice the third guidepost rarely will limit a high punitive damages award and is hardly discussed at all.

For example, in *Moore v. American Family Mutual Insurance Company,*[45] the Eighth Circuit discussed "reprehensibility" in considerable detail while only three short sentences were devoted to the third guidepost.[46] The *Moore* court stated that the insurer could face suspension or revocation of its license if it knew or should have known that it was violating North Dakota's unfair insurance practices act and reasoned that such a suspension or revocation of its insurance license "might well prove more costly than a punitive damages award of $1,150,000."[47]

Another court noticed its confusion in applying the third guidepost. The court agreed that the penalty for a violation of the Unfair Insurance Practices Act includes a penalty of up to $5,000 and could involve suspension or revocation of licenses. The court stated, "We are similarly unsure as to how to properly apply this guidepost, and we are reluctant to overturn the punitive damages award on this basis alone."[48] This court then went ahead to affirm a $150,000 punitive damages award.[49]

The trend as far as the third guidepost seems to be that the reviewing courts can breeze through this guidepost by always considering the possibility that an insurer's license being suspended or revoked could prove to be costly – courts have held that this factor helps to justify a higher award of punitive damages. Interestingly though, it seems that in every case involving allegations of insurer bad faith, the argument could (and likely will) be made that the insurer's actions were a violation of the applicable state unfair insurance practices act and thus could result in suspension or revocation of their license. Therefore, this guidepost could conceivably be used to satisfy any punitive damage amount.

V. How Can We Use *Campbell*?

Campbell is significant in its requiring of rational limitations on awards of punitive damages. The holding also, however, left great discretion and requires that this determination be made on a case-by-case basis.

Each case will undoubtedly have its own set of facts that will affect the guideposts and how they are applied. While this leaves uncertainty as to any specific amount to be awarded, it also allows for an individualized determination. The awards will always vary – there are many other factors to consider including the state laws implicated.

Reprehensibility of the conduct is the most important guidepost in the analysis. Even the second guidepost (the ratio) can be adjusted based on how egregious the conduct. The highest awards are upheld where there was some physical harm and where the conduct was intentional (and in some cases, repeated).

Endnotes

1. 538 U.S. 408 (2003).

2. The Campbell opinion discussing excessive punitive damages awards came after the Supreme Court

decided BMW of North America, Inc. v. Gore, 517 U.S. 559 (1996) and Cooper Industries, Inc. v. Leatherman Tool Group, Inc., 532 U.S. 424 (2001) (holding that a review of substantive due process is a legal question and thus entitled to de novo review), which provided more flexible guideposts for evaluating punitive damages awards. These cases, however, are often viewed as the first in a series of cases where the Supreme Court attempted to limit extreme punitive damages awards.

3. *See* Gertz v. Robert Welch, Inc., 418 U.S. 323, 350 (1974) (stating that punitive damages are "private fines levied by civil juries to punish reprehensible conduct and to deter its future occurrence.").

4. *Supra.* n.1, at 415.

5. *Id.* at 408.

6. *Id.* at 408.

7. *Id.* at 418.

8. *Id.* at 419 (citing Gore, 517 U.S. at 575).

9. *Id.* at 425.

10. *Id.* (citing Gore, 517 U.S. at 582).

11. *See*, *e.g.*, Bullock v. Phillip Morris USA, Inc., 2011 WL 3599605 (Cal. App. 2 Dist. 2011) (holding that the punitive damages award with ratio of 16:1 was not unconstitutionally excessive). The court found that the conduct of Philip Morris was extremely reprehensible and that the $13.8 million in punitive damages while exceeding a single digit ratio was reasonable based on this extreme level of reprehensibility. *Id.* at **15-16.

12. *Supra* n. 1, at 419. The Supreme Court found that the lower court had erred in its reprehensibility analysis by considering conduct of State Farm that occurred outside of Utah. *Id.* at 420-421. This would allow the case to not focus on the harm caused to the plaintiffs but instead would focus on nationwide condemnation of State Farm's practices. *Id.* at 420-421.

13. 576 F.3d 781 (8th Cir. 2009).

14. *Id.* at 784.

15. *Id.*

16. *Id.*

17. *Id.*

18. *Id.* at 788.

19. This evidence was submitted at the underlying trial in support of Mr. Moore's claim of uninsurability since he was a farmer with multiple vehicles that needed to be insured in order for him to earn income and a loss of insurance could cause him "ruinous economic injury." *Id.*

20. *Id.* at 784.

21. *Id.* at 790.

22. Jurinko v. Medical Protective Co., 305 F. App'x. 13 (3d Cir. 2008).

23. *Id.* at 15.

24. *Id.*

25. *Id.*

26. *Id.* at 16.

27. *Id.*

28. *Id.* at 17.

29. *Id.* at 18.

30. *Id.* at 26.

31. *Id.*

32. *Id.* at 28.

33. *Id.*

34. *Supra*, n.1, at 425 (citing Gore, 517 U.S. at 582).

35. *Id.* at 410 (citing Gore, 517 U.S. at 581).

36. 443 F. 3d 1257 (10th Cir. 2006).

37. *Id*. at 1263.

38. *Id*. at 1272.

39. *Id*. (citing Campbell, *supra* n. 1, at 425).

40. The court at this point stated that the conduct that it found to be "egregious" consisted of the Hartford denying the insured's claims for uninsured motorist and medical payment benefits, delaying payments of medical payments coverage until just weeks before the trial, not evaluating his claim until the third day of trial, and not offering any amount of money for her uninsured motorist claim, and not checking to see if state law permitted tying the policy's uninsured motorist coverage for an individually named insured to specific vehicles. *Id*. at 1272.

41. *Supra* n. 13, at 791. In Myers v. Workmen's Auto Ins. Co., 95 P.3d 977 (Idaho 2004), the court did not conduct a ratio analysis and instead held that "ratios of compensatory damages and punitive damages are of no real assistance in this case where only nominal damages are sought. The court upheld an award of $300,000 in punitive damages in an action where $735 in nominal damages were awarded. *Id*. at 992.

42. Willow Inn, Inc. v. Public Service Mut. Ins. Co., 399 F.3d 224 (3d Cir. 2005).

43. Gore, 517 U.S. at 583.

44. *Supra* n. 1, at 428 (citing Gore, 517 U.S. at 575). In Campbell, the Supreme Court stated that the third guidepost in determining whether a punitive damages award was unconstitutional is the disparity between the punitive damages awarded and the "civil penalties authorized or imposed in comparable cases." *Id.*

45. 576 F.3d 781 (8th Cir. 2009).

46. *Id*. at 790-791.

47. *Id*. at 791.

48. Willow Inn, 399 F.3d at 238.

49. *Id*. ■

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