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CAPS ON DAMAGES: THE "LAY OF THE LAND"

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Your company manufactures, assembles, designs, distributes, leases and/or sells products used throughout the United States. You are a key player in the company's legal or risk management department. While the vast majority of your fellow employees spend their workdays contributing to the very purpose of the company, *i.e.,* making profit, you are charged with doing your best to retain as much of that profit as is reasonably possible – or at least be able to accurately predict the ultimate cost of that most recent personal injury lawsuit to the company's bottom line.

Indeed, the evaluation of liability exposure and litigation costs attendant to any particular personal injury claim can be fraught with peril, and is anything but an exact science. Of course, it does not help you that this is the last thing management and engineers want to hear from you. In recent history, however, a modicum of assistance with this daunting task has come from what some might consider an unlikely source: various state governments. Under the banner of "tort reform," many states have enacted legislation that limits the amount of various types of damages recoverable in personal injury actions. Granted, none of these caps on damages truly "cap" the damages you might have to pay in any given lawsuit – at least not to the extent that you can define a maximum judgment in any given case. The limitations invariably apply to only *some* of the blanks on the jury verdict form, such as punitive or non-economic damages. Many of them are riddled with exceptions that will void or mitigate the cap depending upon the degree of the defendant's misconduct or the severity of the plaintiff's injuries; the applicability of these exceptions is often left to the highly unpredictable discretion of the jury. They are typically subject to annual increases to account for inflation. Generally speaking, the caps are so high that they only become a real factor in cases of significant exposure.

So, it is fair to say that "caps" legislation is not exactly a panacea. It should come as no surprise, however, that attorneys who make their living on the plaintiff's side of the bar have not been particularly fond of tort reform legislation in general, and damages caps, in particular. After all, a fair percentage of every dollar saved by a defendant as a result of the "caps" would have otherwise wound up in a plaintiff attorney's pocket. Consequently, it was predictable that we would ultimately see challenges to this legislation.

Caps and Constitutional Challenges

To date, almost half of the fifty states have enacted "caps" legislation that could potentially limit recovery of certain types of damages in a personal injury action filed against a product manufacturer or seller. A couple of other states have introduced bills that could lead to caps. The reality is that the absence, existence and/or preservation of tort reform legislation in any particular state is often a factor of the political climate in that state. Our research indicates that, to date, constitutional challenges have worked their way through the to the highest appellate court in at least eleven states that have passed damages cap legislation. In all but two of those states (Illinois and Ohio), the constitutionality of the legislation was ultimately upheld, which would seem to bode well for this type of legislation. More importantly, this success rate would seem to provide us with enough information to formulate some reasonable conclusions

– or, at least, educated guesses – about the continued viability of caps that can be relied upon to limit certain areas of exposure faced by product manufacturers and sellers in future personal injury actions.

A Recent Case Study

By way of example, in Michigan, sweeping products liability reform legislation was enacted in 1996. With a conservative, pro-business, Republican governor in office for three terms, and a solid Republican majority in both chambers of the Legislature, not to mention the concomitant "packing" of the appellate courts with like-minded jurists, the conditions were ripe for tort reform that would withstand the foreseeable challenges. The legislation took effect on March 28, 1996. Among other "reform" provisions, the new law provided that the total amount of damages that could be awarded in a products liability action for noneconomic loss could not exceed $280,000, unless either of the following situations were found to exist: (1) the product defect caused either death or permanent loss of a vital bodily function, in which case the amount of damages awarded for noneconomic loss shall not exceed $500,000;[1] or (2) at the time of manufacture or distribution, the defendant had actual knowledge that the product was defective and that there was a substantial likelihood that the defect would cause the injury that was the basis of the action, and the defendant willfully disregarded that knowledge in the manufacture or distribution of the product.[2] It was further provided that the amount of the caps would be adjusted by the state treasurer on an annual basis "to reflect the cumulative annual percentage change in the consumer price index."[3] As a result of these annual adjustments, these "caps" are presently $366,000 and $653,500, respectively.

In July 2004, the Michigan Supreme Court issued an opinion in a "caps case" handled on appeal by a partner at Plunkett & Cooney, Ernest Bazzana. While the case, *Phillips v. Mirac, Inc.*,[4] involved constitutional challenges to a statute which limited the amount of a lessor's statutory vicarious liability in rental car agreements, the court's opinion upholding the statute as constitutional will be controlling in any future challenge to the constitutionality of Michigan's product liability caps on damages.

As is common in such challenges, the plaintiff in *Phillips* argued that the Michigan legislation was unconstitutional because it violated her rights to (1) a jury trial, (2) equal protection and (3) due process. The supreme court first concluded that the subject statute did not violate the plaintiff's right to a jury trial for two reasons. First, the court explained that, while the finder of fact may decide that "a defendant acted negligently and the amount of damages occasioned thereby,"[5] it is ultimately left to the court to decide the legal consequences of these findings. For instance, the court may rule that a defendant is not liable for its negligence and the damages proximately caused to the plaintiff because of governmental immunity statutes. On the other hand, the court may enter a post-trial judgment which doubles or trebles the damages found by the jury, in accordance with a variety of different statutes. Consequently, the court reasoned that the amount actually received by a plaintiff, as opposed to the amount that the plaintiff has been found to suffer, "was never within those things a jury can decide."[6] Second, the court explained that if the legislature can create or abolish causes of action, even those based on common law, it must be able to take the "less drastic step" of modifying a cause of action by limiting the amount of damages recoverable from a particular defendant.[7]

The equal protection challenge in *Phillips* was based on the argument that the plaintiff, unlike litigants pursuing other types of claims, was being prevented from recovering an amount decided by a jury to be her damages.[8] After first pointing out that legislatures are in the business of drawing lines and enacting laws that inherently treat individuals differently, the court determined that Ms. Phillips' equal protection claim would be properly analyzed by applying the rational basis test, because the statute "does not result in discrimination by race, national origin, or ethnicity, nor affect an interest that is fundamental" (which would invoke the strict scrutiny test), nor did the statute discriminate on the basis of gender or illegitimacy (which would invoke the heightened scrutiny test).[9] The court concluded that the legislation satisfied the rational basis test because it is rationally related to a legitimate governmental interest, i.e., reduced insurance costs for automobile lessors would increase the number of providers available to Michigan consumers.[10] Since the plaintiff's substantive due process claim invoked the same rational basis test, it met with the same result. [11]

Withstanding Scrutiny in Other States

The Alaska Supreme Court explained that in a substantive due process challenge to a "cap" on noneconomic and punitive damages, where only economic interests are at stake, only a "fair and substantial relationship" between the statute and a legitimate state objective was required, i.e., a limited rational basis test.[12] In its earlier discussion of its basis for rejecting a plaintiff's equal protection challenge, the Alaska Supreme Court recognized discouragement of frivolous litigation to decrease the cost of litigation and liability insurance as a legitimate state objective.[13] Similarly, the North Carolina Supreme Court identified the state's need to preserve its economic development, public confidence in the judicial system and the importance of clear notice to defendants of possible penalty as legitimate state objectives justifying a "cap" on punitive damages.[14]

It's Not All Good News

Other courts have rejected constitutional challenges to caps based on theories of taking of property without just compensation,[15] vagueness,[16] guarantees to open courts,[17] separation of powers,[18] and prohibitions on special legislation.[19] Lest any products liability defendant become too comfortable with the continued viability of such tort reform legislation, there remains "the other side of the coin." In *State ex rel. Ohio Academy of Trial Lawyers v. Sheward*,[20] the Ohio Supreme Court struck down a statute capping punitive damages in tort actions, including product liability claims, to the lesser of $100,000 ($250,000 for "large employers") or three times the amount of the compensatory damages awarded, as an unconstitutional violation of the right to jury trial. The court observed that Ohio's tort reform legislation created the "illusion" of constitutional compliance by allowing juries to assess punitive damages, but requiring the court to reduce any such award if it exceeded the cap, which it concluded was no more constitutionally appropriate than precluding the jury from making the determination in the first place.[21] Interestingly, the Ohio "caps" legislation included a provision that precluded a defendant from being assessed punitive damages more than once. The Ohio Supreme Court found this to be "egregious" in that it effectively instituted a "lottery" whereby the first victim of that company's negligence to collect was rewarded, with all others simply losing their constitutional right to a jury trial as to punitive damages.[22]

The Illinois Supreme Court was a bit more creative in finding that state's "caps" legislation unconstitutional. The Illinois legislation limited non-economic damages to $500,000 in all tort and products liability actions, regardless of whether the court or the jury awarded a larger amount. The Supreme Court, however, concluded that the statute violated the special legislation clause of the Illinois Constitution because the damages cap was arbitrary and not rationally related to a legitimate governmental interest in reducing systemic costs of tort liability.[23] In fact, the court observed that, even if the suggested savings were realized, it ran afoul of the special legislation prohibition to allow the entire burden of same to rest on one class of injured plaintiffs.[24] The court further held that the statute violated the separation of powers doctrine by undercutting the power of the judiciary to reduce excessive verdicts by functioning as a legislative remittitur without regard to the specific circumstances of individual awards.[25]

Where Are We Headed?

"Can't we have some uniformity," you ask? Well, no. While the drumbeat of "federal tort reform" seems to get louder in advance of each presidential election, the reality is that, for the most part, tort law is a matter of state law. Even when tort actions are filed in federal court, based upon diversity of citizenship, the court applies state law to the substantive issues.

To the extent that a "bottom line" can be drawn on this issue for a products liability defendant who can be sued in multiple jurisdictions throughout the United States, it would simply be that there may be a degree of occasional certainty as to the "worst-case scenario" which management can assess. While the issue is jurisdictional-dependent, there is an increasing chance that a given new lawsuit will come with the benefit of a cap, and that, far more often than not, these caps will withstand constitutional scrutiny.

The good news, of course, is that, no matter what state you are sued in, counsel can steer you through "the lay of the land" in their jurisdiction, so that you can be prepared for those tough questions from management about the company's exposure in its next products liability lawsuit.

If you have any questions or comments on these issues, the authors can be contacted at (313) 983-4919 or ehiggins@plunkettcooney.com.

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[1] MICH. COMP. LAWS § 600.2946a(1). However, if death or permanent loss of a vital bodily function was the result of the defendant's gross negligence, there is no limitation on noneconomic damages. *Id.* at § 600.2946a(3).
[2] *Id.* at § 600.2949a.
[3] *Id.* at § 600.1483.
[4] 685 N.W.2d 174 (Mich. 2004).
[5] *Id.* at 182.
[6] *Id.* at 183.
[7] *Id.*
[8] *Id.* at 183-84.
[9] *Id.* at 185.
[10] *Id.* at 185-86.
[11] *Id.* at 186.
[12] *Evans ex rel. Kutch v. Alaska*, 56 P.3d 1046, 1055 (Alaska 2002).
[13] *Id.* at 1053.
[14] *Rhyne v. K-Mart Corporation,* 594 S.E.2d 1, 45 (2003).
[15] *See, e.g., id.* at 179.
[16] *See, e.g., id.* at 187.
[17] *Evans*, *supra,* at 1056-57.
[18] *See, e.g.*, *Smith v. Dep't of Insurance*, 507 So. 2d 1080, 1092 (Fla. 1987).
[19] *Evans*, *supra,* at 1057.
[20] 715 N.E.2d 1062 (1999).
[21] *Id.* at 1091.
[22] *Id.*
[23] *Best v. Taylor Machine Works*, 689 N.E.2d 1057, 1076-77 (Ill. 1997).
[24] *Id.* at 1077.
[25] *Id.* at 1080-81.

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Editors' Note: As the authors point out in their article, plaintiffs' attorneys are not keen on damages caps. If you are interested in viewing a counter-position, which discusses purported impediments to caps in medical malpractice cases, review the October 8, 2004 edition of *The Wall Street Journal* or e-mail the *Perspectives* editors.