

Nos. 03-2123, 03-2188

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

EDEN ELECTRICAL, LTD.,

Appellee/Cross-Appellant,

v.

AMANA COMPANY, L.P., D/B/A
AMANA APPLIANCES, INC.,

Appellant/Cross-Appellee.

**BRIEF OF THE UNITED STATES CHAMBER OF COMMERCE
AS *AMICUS CURIAE* IN SUPPORT OF APPELLANT/CROSS-APPELLEE**

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INTEREST OF THE AMICUS CURIAE

The Chamber of Commerce of the United States of America (“the Chamber”) is the nation’s largest federation of business companies and associations, with underlying membership of more than 3,000,000 businesses and professional organizations of every size and in every sector and geographic region of the country. An important function of the Chamber is to represent the interests of its members by filing amicus curiae briefs in cases involving issues of national concern to American business.

Because few issues are of more concern to American business than those pertaining to the fair administration of punitive damages, the Chamber regularly files amicus briefs in significant punitive damages cases, including each of the cases in which the Supreme Court has addressed such issues during the past 15 years. If this Court does not overturn the underlying judgment against Amana on the grounds raised in Amana’s brief, the present case promises to be among the first federal appellate decisions applying the Supreme Court’s most recent pronouncements on punitive damages in *State Farm Mutual Automobile Insurance Co. v. Campbell*, 123 S. Ct. 1513 (2003). Moreover, as a result of the reasoning employed by the district court in its excessiveness review, the Court’s decision in this case likely will be of substantial importance to the development of post-*State Farm* punitive damages doctrine. The Chamber believes that its substantial familiarity with the law of punitive damages can be of assistance to the Court in resolving the important issues in this case.

ARGUMENT

The Supreme Court has held that, when evaluating a punitive award for excessiveness, reviewing courts should consider three “guideposts”: (i) the degree of reprehensibility of the defendant’s conduct; (ii) the ratio of the punitive damages to the monetary value of the harm or potential harm to the plaintiff resulting from the punishable conduct; and (iii) any variance between the punitive damages and the legislatively established penalty for comparable misconduct. *State Farm*, 123 S. Ct. at 1520; *Cooper Indus., Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424, 435, 440, 441-43 (2001); *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 574-75 (1996).

With regard to the first guidepost, the Court has further instructed courts to consider whether:

[i] the harm caused was physical as opposed to economic; [ii] the tortious conduct evinced an indifference to or a reckless disregard of the health or safety of others; [iii] the target of the conduct had financial vulnerability; [iv] the conduct involved repeated actions or was an isolated incident; and [v] the harm was the result of intentional malice, trickery, or deceit, or mere accident.

State Farm, 123 S. Ct. at 1521. Significantly, it noted, “[t]he existence of any one of these factors weighing in favor of a plaintiff may not be sufficient to sustain a punitive damages award; and the absence of all of them renders any award suspect.” *Id.* Indeed, *State Farm* itself involved at least two of the five reprehensibility factors — a financially vulnerable victim and intentionally deceitful conduct — yet the Court strongly suggested that a 1:1 ratio of punitive to compensatory damages was the

highest that the Constitution would permit. *See id.* at 1526 (“[a]n application of the *Gore* guideposts to the facts of this case, especially in light of the substantial compensatory damages awarded (a portion of which contained a punitive element), likely would justify a punitive damages award at or near the amount of compensatory damages” — *i.e.*, \$1 million).

With respect to the second guidepost, the Court has emphasized the “long legislative history, dating back over 700 years and going forward to today, providing for sanctions of double, treble, or quadruple damages” and indicated that, although such ratios (*i.e.*, 1:1, 2:1, and 3:1, respectively) “are not binding, they are instructive.” *Id.* at 1524. Indeed, while observing that “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,” the Court made clear that “[t]he converse is also true, however. When compensatory damages are substantial, then a lesser ratio, perhaps only equal to compensatory damages, can reach the outermost limit of the due process guarantee.” *Id.* (internal quotation marks and citation omitted).

In reviewing the jury’s \$17,875,000 punitive award, the court below expressly found that four of the five reprehensibility considerations identified in *State Farm* are absent here: the harm was economic, not physical; there was no reckless disregard of health or safety; the plaintiff was not financially vulnerable; and Amana’s tort was an

isolated incident. Mem. Op. 18, 22. Only the fifth subfactor — whether the harm was the result of intentional malice or deceit — was found to be present. *Id.*¹ Because it found only one reprehensibility subfactor to be present, the court concluded that a ratio in the high single digits cannot be squared with *State Farm*. *Id.* at 23-24. While that conclusion was certainly correct as far as it went, the court nevertheless erred in two significant respects in approving a \$10 million punishment that is almost five times the compensatory damages. First, seriously misreading *State Farm*, the court treated Amana’s financial condition as an aggravating factor justifying a higher ratio than would have been permissible for a defendant of more modest means. Second, the court failed adequately to account for the extraordinarily high award of compensatory damages in determining the maximum permissible punitive/compensatory ratio.

A. The District Court Erred In Invoking Amana’s Financial Condition As Justification For Allowing A \$10 Million Punishment.

In determining the maximum constitutionally permissible punishment, the district court deemed it both necessary and permissible to consider Amana’s

¹ We agree with Amana that, in upholding the finding of punitive liability and then conducting its excessiveness analysis, the district court erroneously considered conduct that took place after the parties entered into the contract and hence had nothing to do with the alleged fraud in the inducement that was the sole basis for liability. Nevertheless, for purposes of this brief we accept the trial court’s conclusion that Amana’s conduct fell “at the more reprehensible end of the business fraud category” (Mem. Op. 18). As we discuss in Section B of this brief, even an egregious “business-on-business” fraud does not warrant a punitive award in excess of the compensatory award when, as the trial court found here, the compensatory damages are “substantial” (*id.* at 20).

substantial net worth, stating in no uncertain terms: “The Court concludes that it must throw into the balance and otherwise take into account Amana’s net worth when considering the maximum punitive damages amount the Due Process Clause will permit.” Mem. Op. 25. *See also id.* at 24 (“If the punitive damages sanction is to continue to meet its twin aims, must not a court consider who is to be punished or deterred when ascertaining whether an award is constitutionally permissible?”). That ruling — without which the \$10 million punitive award cannot stand — is utterly irreconcilable with the Supreme Court’s decisions in *BMW*, *Cooper Industries*, and now *State Farm*. Moreover, the district court’s underlying assumption that the deterrence objective requires consideration of corporate financial condition is fundamentally wrong.

1. Corporate Financial Condition Is Not A Permissible Consideration In The Determination Of The Maximum Constitutional Punishment.

The district court’s belief that corporate financial condition must be “throw[n] into the balance” when considering the maximum constitutionally permissible punitive award is flatly inconsistent with the Supreme Court’s recent punitive damages decisions.

As noted, the *BMW* Court identified three guideposts for evaluating the permissible size of a punitive damages award. Significantly, the Court did not include corporate financial condition as a factor — even though the respondent had argued that the \$2 million punishment in that case should be sustained on the basis of BMW’s

substantial financial condition. See Brief of Respondent at 39, *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559 (1996) (94-896), 1995 WL 330613, at *37-*39. To the contrary, the Court observed that “[t]he fact that BMW is a large corporation rather than an impecunious individual does not diminish its entitlement to fair notice of the demands that the several States impose on the conduct of its business.” 517 U.S. at 585.

In *Cooper Industries*, the Court again embraced the three *BMW* guideposts (532 U.S. at 435, 440, 441-43) and again elected to omit corporate financial condition as a relevant consideration — even though the lower courts had relied on the defendant’s finances as the primary basis for upholding the \$4.5 million punitive verdict. See *Leatherman Tool Group, Inc. v. Cooper Indus., Inc.*, 1999 WL 1216844, at *1 (9th Cir. Dec. 17, 1999) (“The district court specifically found that the punitive damage award was proportional and fair, given the nature of the conduct, the evidence of intentional passing off, and the size of an award necessary to create deterrence **to an entity of Cooper’s size and assets**. Those findings were supported by the evidence, such that the award did not violate Cooper’s due process rights.”) (emphasis added), vacated by 532 U.S. 424 (2001).

Finally, in *State Farm* the Court not only declined to add financial condition to the guideposts but went substantially farther, holding that the lower court’s reliance on “State Farm’s enormous wealth” constituted “a departure from well-established

constraints on punitive damages.” 123 S. Ct. at 1525. Accordingly, it stated unequivocally that “[t]he wealth of a defendant cannot justify an otherwise unconstitutional punitive damages award.” *Id.*

That the Court has repeatedly rejected exhortations to include financial condition as a guidepost is not surprising because the use of financial condition to justify a high punitive award (as the district court did here) is affirmatively inconsistent with the three guideposts it has embraced. With regard to the first guidepost, varying punishment with the defendant’s wealth conflicts with the well-established, constitutionally-based principle that punishment should fit the offense.² Put simply, the fact that a defendant has a high net worth does not make its conduct more egregious.³ As to the second guidepost, the Supreme Court has expressly observed that the defendant’s financial condition “bear[s] no relation to the award’s reasonableness or proportionality to the harm.” *State Farm*, 123 S. Ct. at 1525.

² *BMW*, 559 U.S. at 575; *Solem v. Helm*, 463 U.S. 277, 284 (1983) (“The principle that a punishment should be proportionate to the crime is deeply rooted and frequently repeated in common-law jurisprudence.”); *Weems v. United States*, 217 U.S. 349, 366-367 (1910) (it is “a precept of the fundamental law” as well as “a precept of justice that punishment for crime should be graduated and proportioned to offense”); see also *Massachusetts Bonding & Ins. Co. v. United States*, 352 U.S. 128, 133 (1956) (“[b]y definition, punitive damages are based upon the degree of the defendant’s culpability”).

³ See *Zazu Designs v. L’Oreal, S.A.*, 979 F.2d 499, 508 (7th Cir. 1992) (Easterbrook, J.) (“having a large net worth” is not “the wrong to be deterred”); *Lane v. Hughes Aircraft Co.*, 993 P.2d 388, 402 (Cal. 2000) (Brown, J., concurring) (“Many of the wealthiest defendants are corporations, and the size of a corporate defendant is not an additional evil that in itself warrants an enhanced penalty.”).

Finally, consideration of net worth is even more inconsistent with the comparative fines guidepost because neither the fines considered in *State Farm* and *BMW* nor most other criminal or administrative fines vary with the wealth of the defendant.⁴

In short, corporate financial condition is not a fourth guidepost, and the district court plainly erred in treating it as one by relying upon Amana's finances to set an otherwise indefensible award.

2. Corporate Financial Condition Is Not Relevant To The Deterrent Function Of Punitive Damages.

Although the issue already has been resolved by the Supreme Court and it therefore should not be necessary to consider as a matter of first principles whether corporate financial condition *should* have a role to play in setting punitive awards or reviewing them for excessiveness, it is also true that the district court's reason for including Amana's financial condition in its constitutional calculus reflects an instinct that is fundamentally fallacious. Citing Finnish income-based traffic fines and the homespun wisdom of Andy Griffith, the district court reasoned:

[A]n award that would effectively punish and deter General Motors or Bill Gates would have to be many, many, many times greater than an award which would adequately punish and deter, say, the local one-store druggist. Otherwise, the potential punitive damages sanction might risk becoming merely an insignificant additional cost of doing business to some wealthy entities.

Mem. Op. 24.

⁴ See *Kemezy v. Peters*, 79 F.3d 33, 36 (7th Cir. 1996) (Posner, C.J.) (“[t]he usual practice with respect to fines is not to proportion the fine to the defendant's wealth”).

The district court's assumption that it takes a higher penalty to deter a wealthy defendant than it takes to deter a defendant of modest means does have merit when applied to *individuals* who have committed *non-economically motivated* torts — *e.g.*, assaults, defamations, hate crimes, or even traffic violations. In such instances, it is necessary to “monetarize” the subjective value of the misconduct to the wrongdoer, and that value will depend to a material degree on his or her wealth. But this rationale loses its validity when applied to institutional defendants accused of economically motivated torts. As Judge Easterbrook has explained for the Seventh Circuit:

For natural persons the marginal utility of money decreases as wealth increases, so that higher fines may be needed to deter those possessing great wealth. * * * Corporate assets finance ongoing operations and are unrelated to either the injury done to the victim or the size of the award needed to cause corporate managers to obey the law. Net worth is a measure of profits that have not yet been distributed to the investors. Why should damages increase because the firm reinvested its earnings?

Zazu Designs v. L'Oreal, S.A., 979 F.2d 499, 508 (7th Cir. 1992). Scholars who have considered the subject generally agree with the Seventh Circuit. As one pair of commentators explains it:

[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. * * * The defendant's wealth or lack of it is thus irrelevant to the deterrence of socially undesirable conduct * * *.

Kenneth S. Abraham & John C. Jeffries, Jr., *Punitive Damages and the Rule of Law: The Role of the Defendant's Wealth*, 18 J. Legal Stud. 415, 417 (1989); *accord* 2

American Law Institute, Reporters' Study, Enterprise Responsibility for Personal Injury 254-55 (1991); Bruce Chapman & Michael Trebilcock, *Punitive Damages: Divergence in Search of a Rationale*, 40 Ala. L. Rev. 741, 824-26 (1989); Robert D. Cooter, *Punitive Damages for Deterrence: When and How Much?*, 40 Ala. L. Rev. 1143, 1176-77 (1989); A. Mitchell Polinsky & Steven Shavell, *Punitive Damages: An Economic Analysis*, 111 Harv. L. Rev. 869, 910-14 (1998); Malcolm E. Wheeler, *A Proposal for Further Common Law Development of the Use of Punitive Damages in Modern Product Liability Litigation*, 40 Ala. L. Rev. 919, 950-52 (1989); Malcolm E. Wheeler & Jack Carr, Comments, *Symposium Discussion, Punitive Damages*, 56 S. Cal. L. Rev. 155, 190-91 (1982).

Because businesses are economic actors, punishment should be sufficient if it is calibrated to the expected profitability of wrongful behavior. Large and small companies alike are interested in avoiding losses, and the overall size of a business has little bearing on the way its employees behave. Because there is little or no difference in the motivation of large and small businesses to increase the company's profits, a profit-removing punishment should be equally effective regardless of the company's size. As Judge Easterbrook has explained:

General Motors is much larger than Chrysler, and so makes more defective cars, but the goals of compensation and deterrence are achieved for both firms by awarding as damages the injury produced per defective car. Corporate size is a reason to magnify damages only when the wrongs of larger firms are less likely to be punished; yet judges rarely have any reason to suppose this * * *.

Zazu, 979 F.2d at 509.

Moreover, the district court's equation of Amana with Bill Gates, the fictional New York entertainer on the Andy Griffith show, and Finnish traffic scofflaws is mistaken in one other respect that is pertinent here:

Corporations * * * are not wealthy in the sense that persons are. Corporations are abstractions; investors own the net worth of the business. These investors pay any punitive awards (the value of their shares decreases), and they may be of average wealth. Pension trusts and mutual funds, aggregating the investments of millions of average persons, own the bulk of many large corporations. ***Seeing the corporation as wealthy is an illusion, which like other mirages frequently leads people astray.***

Id. at 508 (emphasis added).

Finally, just as it is unnecessary to hold a meeting of the Joint Chiefs to stop enlisted troops from stealing candy bars from the PX, it is not necessary to “send a message” to the top management of a large company by pegging punitive damages to corporate net worth. Large companies, more than small ones, must operate by delegating power and responsibility to lower levels of the company, and managers at those levels will feel the consequences if their actions bring down upon the company liabilities that undercut the profitability of the operations they supervise. *See Johansen v. Combustion Eng'g, Inc.*, 170 F.3d 1320, 1338-39 (11th Cir. 1999) (observing that punitive award need not be large enough to “make the company newsletter” because a far smaller award “would, no doubt, bear heavily upon regional or local managers where failures to regard consequences would be expected to subject

their employer to loss”). For that reason, apportioning punitive awards to the economics of the particular transactions that give rise to liability is all that is necessary to satisfy the goal of deterrence and hence all that is constitutionally permissible. *See State Farm*, 123 S. Ct. at 1521 (“a more modest punishment for this reprehensible conduct could have satisfied the State’s legitimate objectives, **and the Utah courts should have gone no further**”) (emphasis added); *BMW*, 517 U.S. at 584 (question is “whether a lesser deterrent would have adequately protected the interests of Alabama consumers”); *Continental Trend Res., Inc. v. OXY USA Inc.*, 101 F.3d 634, 641 (10th Cir. 1996) (“[t]he Supreme Court’s opinion [in *BMW*] seems to ask for the least punishment that will change future behavior”).

In sum, the core assumption underlying the district court’s heavy reliance on Amana’s financial condition is false. Hence, even if reliance on corporate financial condition were not already precluded under *State Farm* and its progenitors, it should be as a matter of rational administration of the goal of appropriate, but non-excessive, deterrence.

B. The District Court Erred In Failing To Take Into Account The High Compensatory Award When Determining The Constitutional Maximum Amount Of Punitive Damages.

As previously noted, in applying the second *BMW* guidepost the Supreme Court has deemed “instructive” the double (1:1), treble (2:1), and quadruple (3:1) damages remedies that have been a hallmark of Anglo-American jurisprudence for 700 years,

reiterated that a ratio of 4:1 may be “close to the line of constitutional impropriety,” and admonished that, when compensatory damages are substantial, a punitive award that is no greater than the plaintiff’s actual damages may be the maximum constitutionally permissible. *State Farm*, 123 S. Ct. at 1524. The district court acknowledged these pronouncements (Mem. Op. 23) but then proceeded to ignore them, concluding that Amana’s substantial net worth necessitated a \$10 million punishment and hence a ratio of close to 5:1 notwithstanding the absence of all but one of the reprehensibility subfactors.

Although the Supreme Court has declined “to impose a bright-line ratio which a punitive damages award cannot exceed” (*State Farm*, 123 S. Ct. at 1524), its discussion of the second guidepost in *State Farm* suggests a framework that appellate courts profitably can use in providing further guidance to trial courts.

First, ratios in excess of 9:1 are presumptively unconstitutional. 123 S. Ct. at 1524. Such ratios generally will be permissible only if (i) the compensatory damages are small and/or (ii) the conduct is especially likely to escape detection (such as dumping toxic materials in a remote area under cover of night). *Id.* Although there may be room for debate as to the meaning of “small,” it surely is the case that, once compensatory damages reach beyond five figures, ratios of double digits (or higher) become highly suspect.

Second, when the conduct is highly reprehensible — characterized by several of the aggravating factors identified in *State Farm* — and the compensatory damages are relatively modest, a ratio between 4:1 and 9:1 may be constitutionally permissible.

Third, when compensatory damages are substantial and the conduct involves only one or two aggravating factors (and hence is barely sufficient to cross the threshold for punitive liability), ratios of 2:1 to 4:1 generally will be the outside limit, depending on the circumstances.

Finally, when, as here, the conduct is a business-on-business tort that implicates few if any of the reprehensibility subfactors, and the compensatory damages are substantial, lower ratios — 1:1 or lower — will be the most that is constitutionally permissible. Indeed, the Third Circuit presciently reached this precise conclusion several years before *State Farm* was decided, reducing a \$50 million punitive award that was roughly equal to the \$48 million compensatory award to \$1 million and explaining that “high, easily calculable compensatory damages may more appropriately be accompanied by a lower punitive damages ratio.” *Inter Med. Supplies, Ltd. v. EBI Med. Sys., Inc.*, 181 F.3d 446, 467-68 (3d Cir. 1999). Like the present case, *Inter Med.* involved a dispute between a manufacturer and a distributor — one that degenerated into a “war” in which the defendant’s ultimate objective was “to destroy [the plaintiff].” *Id.* at 461 (internal quotation marks omitted). Nevertheless, finding it significant that the injury was purely economic, the plaintiff

was not financially vulnerable, and the injury arose out of a contractual arrangement, the Third Circuit concluded that the conduct was not sufficiently egregious to warrant a multimillion dollar punishment. *Id.* at 467. Accordingly, it reduced the punitive damages to \$1 million (*i.e.*, 1/48th the compensatory damages), concluding that any more than that would be “greater than reasonably necessary to punish and deter” and hence unconstitutional *Id.* at 469 (internal quotation marks and citation omitted).

State Farm confirms the soundness of the Third Circuit’s approach. As the Supreme Court pointed out, the historical tradition of double, treble, and quadruple damages remedies is “instructive.” Many of those multiple damages statutes were designed to deter conduct far more serious than a business-on-business tort. For example, Congress deemed a treble damages remedy (*i.e.*, a ratio of 2:1) adequate to deter price fixing (15 U.S.C. §§ 1, 15); racketeering (18 U.S.C. § 1964); and tying arrangements in the provision of credit and other banking services (12 U.S.C. §§ 1464(q)(3), 1975). And it regarded double damages to be adequate to deter lenders from charging excessive interest (15 U.S.C. § 1831d(b)) and from violating the Truth in Lending Act (15 U.S.C. § 1640(a)(2)(A)(i)). Similarly, early English statutes deemed double and treble damages sufficient to deter theft of livestock, deprivation of property under color of office, bribery, and malicious prosecution. *E.g.*, 3 Edw. 1, cc. 1, 17, 24-27, 30 (1275) (Eng.); 13 Edw. 1, c. 36 (1285) (Eng.).

Given the long tradition of limiting recovery to double and treble damages even for conduct directed at vulnerable victims, it makes sense to set double damages (*i.e.*, a 1:1 ratio) as the presumptive outside limit when the case involves a business-on-business tort and the compensatory award is substantial. And when, as here and in *Inter Med.*, the compensatory damages are in the millions of dollars, even a 1:1 ratio is likely to be excessive in relation to the state's deterrence interest. After all, a punishment of even \$2 million is "tantamount to a severe criminal penalty" (*BMW*, 517 U.S. at 585) and hence is justifiable only when the defendant's conduct is "egregiously improper" (*id.* at 580). That will almost never be the case in the business-on-business context and certainly not when, as here, the plaintiff is a sophisticated entity that could have protected itself through the contractual process. *See Inter Med.*, 181 F.3d at 467.

CONCLUSION

The district court went seriously off the rails in concluding that Amana's financial condition trumps the Supreme Court's pronouncement that a ratio of 1:1 may be the constitutional maximum when the compensatory damages are substantial and the conduct is not extraordinarily reprehensible. If the Court does not reverse the judgment in its entirety, it should reduce the punitive damages to no more than \$2.1 million, the amount of Eden's already ample compensatory award.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE WITH FRAP 32(a)(7)

Pursuant to Federal Rule of Appellate Procedure 32(a)(7)(C), I hereby certify that – according to the word-count facility of WordPerfect 9.0, the program used to draft this brief – the foregoing brief contains 4,138 words (excluding those portions excluded under Rule 32(a)(7)(B)(iii)), and therefore complies with the type-volume limitation contained in Rule 29(d).

Evan M. Tager

CERTIFICATE OF COMPLIANCE WITH 8TH CIRCUIT RULE 28A(d)(2)

I hereby certify that the PDF of this brief included on the CD-ROM that accompanied this brief has been scanned for viruses and is virus-free.

Evan M. Tager

CERTIFICATE OF SERVICE

I hereby certify that I caused two copies of the foregoing Brief Of The United States Chamber Of Commerce As *Amicus Curiae* In Support Of Appellant/Cross-Appellee, along with one virus-free copy of the brief in PDF format, to be served by overnight delivery on the following counsel:

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