

## SOUTHERN DISTRICT CIVIL PRACTICE ROUNDUP

BY EDWARD M. SPIRO AND JUDITH L. MOGUL

### *Procedural Aspects of Challenging Punitive Damages*

In our last column, we discussed the constitutional limitations on the size of punitive damages awards as illustrated by three recent decisions from the U.S. District Court for the Southern District of New York that dramatically reduced punitive damages verdicts in employment discrimination cases.<sup>1</sup> But post-trial litigation over the size of a punitive damages award is only the last stage in a process that often sees requests for punitive damages eliminated before trial or subjected to limiting jury instructions. Separate and apart from the constitutional limitations on the amount of punitive damages that can be awarded, demands for punitive damages raise numerous procedural issues from the pleading and motion stages, through discovery and into trial. This article examines some of those procedural questions, again in the context of recent decisions from the Southern District.

#### Threshold Motions

Defendants frequently seek early dismissal of requests for punitive damages on the ground that the plaintiff is not entitled to punitive damages as a matter of law. These motions are variously styled as motions to dismiss or motions to strike, without distinction by the parties or the courts, and are designed to limit potential punitive damages exposure as early in the case as possible. One area of recurring litigation is where plaintiffs seek to cast their claims as sounding in tort as well as contract in order to expand the scope of recovery to include punitive damages. Under New York law, the general rule is that “[p]unitive damages are not recoverable for an ordinary breach of contract, as their purpose is not to remedy private wrongs but to vindicate public rights.”<sup>2</sup> However, punitive damages will be available in connection with a breach of contract claim where a defendant’s conduct (i) is actionable as an independent tort; (ii) involves a “a high degree of moral turpitude...demonstrating such wanton dishonesty as to imply a criminal indifference to civil obligations;” (iii) is directed to plaintiff; and (iv) is part of a pattern directed at the public generally.<sup>3</sup>

Three recent cases highlight the difficulty of meeting this standard. In *M’Baye v. World Boxing Association*,<sup>4</sup> Judge Denny Chin granted the defendant’s motion to strike the punitive damages demand in a



Edward Spiro

Judith Mogul

complaint by a professional boxer against the World Boxing Association (WBA), finding that plaintiff’s claim that the WBA had improperly bypassed him for championship bouts, sounded in contract and was not actionable as an independent tort.

Similarly, in *AD Rendon Communications Inc. v. Lumina Americas Inc.*,<sup>5</sup> the plaintiff asserted claims for breach of contract as well as for conversion against a company that had contracted to provide various financial services to the plaintiff, and had allegedly misappropriated plaintiff’s funds. In addition to compensatory damages on both claims, plaintiff sought punitive damages in connection with its conversion claim. Judge Kenneth M. Karas granted defendant’s motion to dismiss the conversion claim on the ground that it was duplicative of plaintiff’s contract claim. He then went on to hold that plaintiff could not recover punitive damages because it had not alleged an independent tort, and because it had failed to allege sufficiently that defendant’s conduct was egregious and part of a pattern of conduct directed at the public generally.

Finally, in *Cerveceria Modelo, S.A. de C.V. v. USPA Accessories LLC*,<sup>6</sup> Judge Harold Baer Jr. granted plaintiffs’ motion to strike the punitive damages demand associated with a counterclaim for tortious interference with contract. He held that plaintiffs’ alleged conduct did not reflect a high degree of moral culpability and was not directed at the public, as required when there is a “close nexus” between tortious conduct and the contract from which it arises.<sup>7</sup>

#### Subject Matter Jurisdiction

On occasion, whether a plaintiff is entitled to punitive damages will determine if the court can hear the case at all. Amounts claimed as punitive damages may be included in determining whether the \$75,000 amount in controversy required by 28 U.S.C. §1332(a) for diversity jurisdiction has been satisfied.<sup>8</sup> However, when a punitive damages demand boosts

a complaint that would otherwise fail to satisfy the amount in controversy requirement over the \$75,000 threshold, courts will subject the punitive damages demand to greater scrutiny than a demand for actual damages, which is considered presumptively (albeit rebuttably) valid. The punitive damages demands in two recently decided cases failed to withstand that scrutiny, resulting in dismissal of both cases for lack of subject matter jurisdiction.

In *Rodriguez v. Kulcsar*,<sup>9</sup> the plaintiff sued his criminal defense attorney for the return of a \$5,000 retainer paid in connection with the attorney’s representation of the plaintiff on an unsuccessful motion for reduction of sentence under Federal Rule of Criminal Procedure 35. Plaintiff alleged that he was fraudulently induced to pay the retainer by the attorney’s false representations concerning the likelihood of success on the Rule 35 motion. He sought compensatory damages of \$500,000 and punitive damages of \$1 million. In assessing, *sua sponte*, whether the court had diversity jurisdiction, Judge Denise L. Cote noted that although the plaintiff bears the burden of showing a “reasonable probability” that the amount in controversy is satisfied,<sup>10</sup> that burden is “hardly onerous” in light of the rebuttable presumption that “the face of the complaint is a good faith representation of the actual amount in controversy.”<sup>11</sup> In order to rebut this presumption, the defendant opposing jurisdiction “must show to a legal certainty that the amount recoverable does not meet the jurisdictional threshold.”<sup>12</sup>

Judge Cote quickly dispatched plaintiff’s claim for \$500,000 in compensatory damages, finding that although he had properly pled a claim for his out-of-pocket expenses of \$5,000, it was legally impossible for him to recover the remaining \$495,000. Turning to his claim for punitive damages, she noted that although punitive damages may be counted toward the jurisdictional amount, given the more speculative nature of such damages, the court is “plainly not compelled to accept” the amount claimed and may subject a claim for punitive damages to “closer scrutiny” than a claim for actual damages when determining subject matter jurisdiction.<sup>13</sup>

Invoking the limitation that punitive damages may be recovered in a breach of contract case under New York law only when the defendant’s conduct is aimed at the public generally and involves a high degree of moral turpitude, Judge Cote characterized the plaintiff’s claim as “manifestly a private dispute predicated on a disagreement about his attorney’s performance” that would not support an award of punitive damages. Specifically, she noted that although plaintiff alluded to a loss of public confidence in the judicial system, he made no allegation that defendant engaged in any

**Edward M. Spiro** is a principal of, and **Judith L. Mogul** is counsel to Morvillo, Abramowitz, Grand, Iason, Anello & Bohrer, both concentrating in commercial litigation. Mr. Spiro is the co-author of “Civil Practice in the Southern District of New York,” 2d ed. (Thomson West 2007).

systematic abuse of clients, or that his conduct was wanton or malicious.

Finally, Judge Cote observed that even if punitive damages were legally permissible, the amount of punitive damages that would satisfy the jurisdictional threshold for diversity jurisdiction, relative to the actual harm plaintiff allegedly suffered, would be unconstitutionally excessive under *State Farm Mutual Automobile Insurance Co. v. Campbell*.<sup>14</sup> Accordingly, she dismissed the case for lack of subject matter jurisdiction.

In *Howard v. Municipal Credit Union*,<sup>15</sup> Judge Lewis A. Kaplan adopted the report and recommendation of Magistrate Judge Debra Freeman that similarly found that plaintiff could not use punitive damages to meet the requisite \$75,000 amount in controversy for diversity jurisdiction. The plaintiff had sued his credit union for reporting and then allegedly failing to correct false information about him to credit reporting agencies and for alleged improper charges on auto and life insurance policies. The court dismissed plaintiff's federal claims under the Fair Credit Reporting Act, and held that absent the dismissed federal claims, it lacked subject matter jurisdiction over his remaining state law claims for fraud and breach of contract because even the strongest arguments suggested by his pleadings did not show a reasonable probability that those claims would exceed \$75,000.<sup>16</sup>

As with the plaintiff in *Rodriguez v. Kulcsar*, plaintiff's out-of-pocket damages were well below the threshold amount, and his complaint did not allege the type of conduct that would support an award of punitive damages under state law. The court found that although plaintiff alleged in his prayer for relief that defendants were scamming the minority community, without any supporting factual allegations, this "conclusory remark" was "insufficient to transform an otherwise private transaction...into the type of gross and wanton fraud against the general public that might support a punitive damages claim."<sup>17</sup>

### Appropriate Vehicle

Attorneys seeking to dispose of punitive damages demands later in a case may do so through a motion for summary judgment or a motion in limine, although there is some disagreement within the Southern District of New York as to which of these vehicles is the most appropriate. In a decision last year in *In re Methyl Tertiary Butyl Ether ("MTBE") Products Liability Litigation*,<sup>18</sup> Judge Shira A. Scheindlin found that summary judgment was an "ill-suited procedural vehicle" for seeking to foreclose a punitive damages request, because punitive damages are a "remedy" rather than a claim. Reasoning that the court can only render judgment on a claim, and that judgments as to particular remedies are outside the contemplation of the Federal Rules of Civil Procedure, she opted to treat the motion as one in limine "to exclude from trial all arguments and evidence that are relevant solely to punitive damages..."<sup>19</sup>

Judge Gerard E. Lynch reached the opposite procedural conclusion in *George v. Ford Motor Co.*,<sup>20</sup> a suit for injuries arising from the allegedly defective manufacture of an automobile. He found that defendant's motion directed at plaintiffs' request for punitive damages was not a proper motion in limine, but was instead a "covert motion for partial summary

judgment," which he declined to grant. He noted that the motion did not comply with Local Civil Rule 56.1 (requiring submission of a statement setting forth the undisputed material facts that entitle the moving party to judgment in its favor). He also found that however unlikely it was that the plaintiffs would be entitled to an award of punitive damages, the issue was so intensely factual that it would be better addressed at or after trial, following presentation of the evidence.<sup>21</sup>

### Jury Instructions

Judge Robert W. Sweet's decision in *Scherer v. City of New York*,<sup>22</sup> focuses on a jury instruction concerning punitive damages, but illustrates the importance of developing issues relating to punitive damages well before that stage, during discovery and trial. Plaintiffs moved to set aside a jury verdict of \$500 in compensatory and \$1,000 in punitive damages in a case against the City of New York for civil rights violations surrounding anti-war demonstrations.

They claimed that in submissions relating to the jury charge, the city had misinformed the court of its policy concerning indemnification of its police officers so that the jury was charged that it could consider the officers' individual ability to pay a punitive damages award, without also hearing that the city had a practice of indemnifying its officers. The city had persuaded the court to remove language from the proposed charge informing the jury that the city had the legal authority to indemnify the defendant police officers for an award of punitive damages by citing a state law establishing that it had no legal duty to do so.

After the trial, the city revealed, in response to interrogatories served in a different case, that despite the lack of any legal duty to indemnify police officers for punitive damages, it had done so in a number of specific cases (including *Scherer*), and that in every case over the past decade in which it had represented an individual officer it had indemnified the officer for both compensatory and punitive damages where such damages were awarded.

Judge Sweet rejected the *Scherer* plaintiffs' argument for a new trial under Federal Rule of Civil Procedure 60(b)(2) on the theory that the information about indemnification obtained in the subsequent action constituted "newly discovered evidence." He stressed that the plaintiffs could not show that they were "justifiably ignorant" of the city's indemnification practices, having referenced those practices and offered to prove them at an evidentiary hearing in a footnote in their request to charge. He further noted that the plaintiffs had not exercised due diligence in obtaining the facts ultimately learned through discovery in the subsequent action, because they never sought that information in their own case.

Plaintiffs also unsuccessfully sought a new trial under Rule 60(b)(3), asserting that the city had misinformed the court of its practices concerning indemnification. Although Judge Sweet questioned the city's intent in selectively informing the court only of its legal duty to indemnify rather than of its actual practices, observing that defense counsel could have been more candid and that the process would have been better served had the city been more forthcoming, he concluded that the city's reticence did not "constitute a fraud upon the Court" or "substantially interfere" with plaintiffs' ability to present their case.

### Conclusion

As these cases demonstrate, issues surrounding punitive damages can permeate a litigation from the pleading stage, through discovery and dispositive motions, and into and following trial. While there may be some in terrorem benefit for plaintiffs in including demands for punitive damages, plaintiffs must also understand that procedural and substantive issues, including the constitutional limitations on excessive awards, make punitive damages fertile grounds for litigation delay and expense.



1. Edward M. Spiro, *Constitutional Limitations on Punitive Damages Awards*, NYLJ, Vol. 239, No. 64 (April 3, 2008).

2. *Rocanova v. Equitable Life Assurance Soc'y of the U.S.*, 83 N.Y.2d 603, 613 (1994) (citation omitted).

3. *New York Univ. v. Continental Ins. Co.*, 87 N.Y.2d 308, 315-16 (1995) (citing *Rocanova*, 83 N.Y.2d at 613-14; *Walker v. Sheldon*, 10 N.Y.2d 401, 404-05 (1961)).

4. 2007 WL 844552 (S.D.N.Y. March 21, 2007).

5. 2007 WL 2962591 (S.D.N.Y. Oct. 10, 2007).

6. 2008 WL 1710910 (S.D.N.Y. April 10, 2008).

7. *Id.*, at \*6-7 (quoting *MacQuesten Gen. Contracting Inc. v. HCE Inc.*, 296 F. Supp. 2d 437, 446-47 (S.D.N.Y. 2003) (Francis, M.J.)).

8. *A.F.A. Tours Inc. v. Whitchurch*, 937 F.2d 82, 87 (2d Cir. 1991).

9. 2007 WL 3120906 (S.D.N.Y. Oct. 24, 2007).

10. *Id.*, at \*1 (citing *Colavito v. N.Y. Organ Donor Network Inc.*, 438 F.3d 214, 221 (2d Cir. 2006)).

11. *Id.* (quoting *Scherer v. Equitable Life Assur. Soc'y of the U.S.*, 347 F.3d 394, 397 (2d Cir. 2003)).

12. *Id.*, at \*2.

13. *Id.*, (quoting *Zahn v. Int'l Paper Co.*, 469 F.2d 1033, 1033 n.1 (2d Cir. 1972)).

14. 538 U.S. 408 (2003) (where ratio between punitive and compensatory damages exceeds single digits, punitive damages award likely to be unconstitutionally excessive). See generally Spiro, *Constitutional Limitations on Punitive Damages Awards*, NYLJ, April 3, 2008.

15. 2008 WL 782760 (S.D.N.Y. March 25, 2008).

16. Judge Kaplan adopted Magistrate Judge Freeman's recommendation that the court leave open the possibility of exercising supplemental jurisdiction over the state law claims if the plaintiff successfully repudiated his federal claims.

17. *Id.*, at \*10, n.11.

18. 517 F. Supp. 2d 662 (S.D.N.Y. 2007).

19. *Id.* at 666-67. On the merits, Judge Scheindlin granted the defendants' motion, ruling that a jury should not be able to award punitive damages where, as in the case before her, plaintiffs intend to rely on market share liability rather than proving which defendant or defendants actually caused their harm.

20. 2007 WL 2398806 (S.D.N.Y. Aug. 17, 2007).

21. See also *Clinton v. Brown & Williamson Holdings Inc.*, 498 F. Supp. 2d 639 (S.D.N.Y. 2007) (Briant, J.) (punitive damages treated as a "claim" capable of preclusion under the doctrine of res judicata).

22. 2007 WL 2710100 (S.D.N.Y. Sept. 7, 2007).