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# Discovery of Defendant's Financial Condition in Cases Claiming Punitive Damages

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## I. Introduction

In recent years the number of cases which include a claim for punitive damages has increased. The Court of Appeals of Maryland has enlarged the scope of cases in which punitive damages may be recovered to include those negligence cases where there is evidence that the defendant was driving while intoxicated or where the defendant's negligent conduct was wanton or exhibited a reckless disregard for human life.<sup>1</sup> The facts upon which the claim for punitive damages is based are often hotly disputed. In some cases the allegations of fact and the claim for punitive damages are not well founded, but are asserted primarily to improve the plaintiff's bargaining position.

Ordinarily, information concerning a defendant's financial condition is discoverable only after judgment and in aid of execution.<sup>2</sup> In cases where punitive damages are justified, the trier of fact may consider evidence of the defendant's financial worth when determining the amount of such damages. Some procedural safeguards are necessary when punitive damages are claimed in order to balance the access to a defendant's financial information against protecting the defendant from harassment. Such safeguards are also necessary to protect the defendant when the plaintiff cannot establish the right to recover punitive damages. Safeguards are particularly important now that the right to recover punitive damages in some cases is subject to constitutional challenge.<sup>3</sup>

This issue does not appear to have been litigated recently in any reported Maryland decisions. Although it is clear that the financial condition of a defendant is relevant in cases where punitive damages are alleged, Maryland law pro-

vides that such evidence is not admissible until after a defendant is found liable and punitive damages are found to be warranted.<sup>4</sup> Because it is first necessary for a plaintiff to prove a *prima facie* case for punitive damages before being allowed to introduce evidence of a defendant's financial condition, it is probable that the Maryland courts will follow the same protective route in controlling the timing of discovery of net worth.

In Maryland, any matter not privileged is discoverable if relevant to the determination of the case or if reasonably calculated to lead to evidence admissible at trial.<sup>5</sup> Evidence of a defendant's financial condition, or net worth, is admissible at trial when considering punitive damages. Therefore, financial information falls within the scope of relevance where punitive damages are legitimately at issue in a case.<sup>6</sup>

This does not mean, however, that a defendant's financial condition may be open to discovery from the onset of the case by a mere allegation of the plaintiff's entitlement to punitive damages. Since the adoption of the new Maryland Rules in 1984, there have been no reported Maryland cases dealing with the issue of exactly when the financial condition of a defendant may be discovered. However, the issue has been discussed by commentators and courts in other jurisdictions, with varying conclusions and results.

The jurisdictions which have ruled on this issue and which permit the trier of fact to consider the financial condition of the defendant in making an award of punitive damages fall into three categories following the three leading cases in this area. The first category involves the liberal "factual allegation" rule. In *Coy v. Superior Court*,<sup>7</sup> a California appellate

court considered the issue of whether pretrial discovery of a defendant's wealth was permitted. The trial court ruled that the plaintiff must wait until after he obtained a judgment in order to discover such information. In reversing the trial court, the appellate court held that because the plaintiff sought punitive damages, the defendant's financial information was relevant and, therefore, properly discoverable. The court reasoned that because this evidence is admissible at trial for the purpose of determining the proper amount of punitive damages, the defendant must disclose the information in pretrial discovery. Other states which follow this liberal rule of discovery include Hawaii<sup>8</sup> and Tennessee.<sup>9</sup>

Since 1981, however, California appears to have become more conservative in this area. In 1981, the California legislature adopted § 3295(c) of the California Civil Code in an apparent effort to provide some procedural safeguards for this liberal financial discovery rule. This law now requires the plaintiff to first obtain an order from the court authorizing the disclosure. The court may, in its discretion, conduct a hearing on the matter. Upon a finding that there is a substantial probability that the plaintiff will prevail on the punitive damages claim, an order may be entered permitting discovery of the defendant's financial status.<sup>10</sup>

The second category of states follows a moderate rule which requires more than a mere allegation that a plaintiff is entitled to punitive damages before an order for discovery of the defendant's financial condition may be granted. This rule was enunciated in a New Jersey case, *Gierman v. Toman*,<sup>11</sup> where the court determined that the financial con-

dition of a defendant, although relevant in a case involving punitive damages, deserved some protection. Therefore, the court held that a plaintiff's right to discover a defendant's net worth was conditioned upon *prima facie* proof that the plaintiff was entitled to recover punitive damages. This rule is also followed in Colorado<sup>12</sup> and Wyoming.<sup>13</sup>

The third approach involves the more conservative rule of discovery enunciated by the New York Court of Appeals in *Rupert v. Sellers*.<sup>14</sup> The court reviewed and specifically rejected the above two rules proposed by the California and New Jersey courts, ruling that a plaintiff must first obtain a special verdict finding him entitled to punitive damages. After obtaining this verdict, it is then possible for the plaintiff to discover information regarding the defendant's financial status.

It is currently unclear which, if any, of the above three rules adopted by other jurisdictions will be followed by Maryland courts. In two cases decided by trial courts prior to the enactment of the revised Maryland Rules, the courts refused to allow the plaintiffs to obtain pretrial discovery from the defendant regarding his financial status prior to obtaining a judgment. In the first case, *Whiteley v. Lockner*,<sup>15</sup> the court ruled on whether a defendant was required to answer interrogatories of a plaintiff suing to recover money allegedly loaned to the defendant. In pretrial interrogatories, the plaintiff requested information regarding the financial condition of the defendant which the defendant refused to answer. The court held that these interrogatories were premature and might be proper if and when the plaintiff obtains a judgment.<sup>16</sup> While this case is not directly on point, it shows the court's tendency to prevent the disclosure of a defendant's financial status before the plaintiff proves his entitlement to such information.

The second case, *Miller v. Crook*,<sup>17</sup> is directly on point because the plaintiff actually made a claim for punitive damages. In *Miller*, the plaintiff attempted to obtain information regarding the defendant's financial condition through pretrial discovery. The court held that unless there is a specific showing of good cause why a defendant must disclose his financial affairs in advance of trial, the issue of

defendant's financial condition is considered severable from the issue of liability, and pretrial discovery of such information is not permitted. However, the court ordered the defendant to prepare the information requested and to have it available at trial to submit to the jury after a determination of the plaintiff's entitlement to punitive damages.<sup>18</sup>

There does not appear to be any other reported decisions regarding this matter in Maryland. Despite this lack of authority, it has been written that Maryland courts have traditionally controlled the timing of the discovery of net worth and required its production only after demonstration by the plaintiff of a *prima facie* case for punitive damages.<sup>19</sup> Before such a showing, the defendant may properly refuse production of net worth data.<sup>20</sup>

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***"[T]he outrage . . . is that a defendant's financial condition, while relevant, . . . is highly confidential and personal."***

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## II. Public Policy Considerations

The major consideration motivating the outrage and debate by courts and commentators alike is that a defendant's financial condition, while relevant to a determination of the amount of an award for punitive damages, is highly confidential and personal. The divulging of such information, while a great incentive for effectuating settlements, may actually coerce a defendant to settle unmeritorious claims. This concern was discussed in *Miller v. Crook*<sup>21</sup> where the court stated the following:

[indiscriminate discovery] could bring about irreparable and unjust harm to litigants. A person with an unfounded claim could seriously embarrass another. A man could ruin a business competitor by alleging a case for punitive damages, discover his opponent's business secrets and then dismiss the suit.

The discovery rules could of themselves become an instrument of malice.<sup>22</sup>

An article discussing the discovery and admissibility of a defendant's financial condition addressed the public policy reasons why a rule allowing unfettered, pre-trial access to such financial information is injudicious, stating the following:

[T]he vexations aspect of this free-wheeling discovery is two-fold. First, there is a concern that every case will be pled as a punitive damage case in order to engage in pre-judgment asset discovery and to apply settlement pressure. Second, there is a concern for legitimate privacy and proprietary interests which might be unduly compromised.<sup>23</sup>

If the Maryland courts adopted a rule making such discovery immediately available upon a factual allegation supporting punitive damages, defendants would be "essentially defenseless against the pretrial discovery motions of a plaintiff in cases where the alleged conduct could support punitive damages."<sup>24</sup>

California, one of the first states to adopt the "factual allegation" rule, made the following observations after two decades of that rule's use:

It soon became obvious . . . that such discovery had enhanced rather than removed the 'game element' by creating a situation in which a plaintiff, merely by alleging a claim for punitive damages, could pressure a defendant into a settlement because of a desire to protect his financial privacy.<sup>25</sup>

Another court cautioned:

If plaintiffs were allowed unlimited discovery of defendants' financial resources in cases where there is no actual factual basis for an award of punitive damages, the personal and private financial affairs of defendants would be unnecessarily exposed and, in some cases, the threat of such exposure might be used by unscrupulous plaintiffs to coerce settlements from innocent defendants.<sup>26</sup>

As can be seen from these cases, a defendant's right to privacy is held to rank higher on a societal hierarchy of values than a plaintiff's discovery needs.<sup>27</sup>

Therefore, there must be some sort of protective measures in place to protect such a vital interest.

Courts in states following the "factual allegation" rule have begun relying upon protective orders as a means for relief for defendants. As a Tennessee court noted, "a protective order can be fashioned which protects defendants' legitimate privacy rights while preserving the discovery rights of plaintiffs."<sup>28</sup> The problem with protective orders is that they merely prevent public disclosure of this private information. Forcing a defendant to disclose personal financial information to the plaintiff or the plaintiff's attorney may coerce a defendant to settle the case rather than comply with a discovery order.<sup>29</sup>

To require the pretrial disclosure of a defendant's assets to the plaintiff, even as an aid to settlement and subject to a protective order against disclosure to others, would be a serious invasion of privacy. The threat of having to place a dollar value on one's assets and to disclose that valuation to strangers may well serve as a powerful weapon to coerce a settlement which is not warranted by the facts of the case.<sup>30</sup>

Other commentators agree that complete "unfettered access" to a defendant's financial net worth by a simple allegation of entitlement to punitive damages would cause unreasonable harassment and irreparable harm to a defendant's right to privacy. One author argues that the question of discovery of a defendant's net worth should not be resolved until after the conclusion of discovery on the merits.<sup>31</sup> After this conclusion, the plaintiff must prove a *prima facie* case of a triable issue on the defendant's liability for punitive damages in a "mini-trial" before such discovery is allowed. This technique properly balances the defendant's interest in privacy, the plaintiff's need to discover relevant information in time to either settle the case or prepare for trial and the interest in judicial economy.<sup>32</sup>

Another suggestion is that a defendant would be required to file with the court a form containing net worth information by the date the trial commences.<sup>33</sup> The information would remain sealed until the jury rendered a special

verdict of liability for punitive damages. At that time, a recess would be called in order to allow the plaintiff the opportunity to inspect and challenge the net worth representation. The trial could then resume with the presentation of net worth evidence.<sup>34</sup>

### III. Conclusion

It is premature to conclude that Maryland courts will adopt the New York rule requiring the plaintiff to first receive a special verdict on liability and a finding that plaintiff is entitled to punitive damages before he may discover information regarding the defendant's financial status. It is clear, however, that there is a tendency in Maryland, prior to the enactment of section 10-913(c) of Maryland's Courts and Judicial Proceedings Article and the current Maryland discovery rules, to protect the defendant

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from unreasonable intrusion and harassment by limiting the availability of discovery of a defendant's financial status prior to the point where it is shown that the plaintiff is entitled to such information.

It is more probable that the Maryland courts will require the plaintiff to show a *prima facie* case for punitive damages before discovery of the defendant's financial status is permitted. As indicated above, there are strong public policy reasons for a procedure requiring that financial information be disclosed only

after the plaintiff has proved a *prima facie* case at trial or in a separate hearing. These same considerations also support a procedure which mandates such information remain sealed until after the trier of fact has determined that punitive damages should be awarded or the plaintiff has satisfied the court that a *prima facie* case exists.

### Endnotes

<sup>1</sup>*Smith v. Gray Concrete Pipe Co.*, 267 Md. 149, 297 A.2d 721 (1972); *Potomac Electric Power Co. v. Smith*, 79 Md. App. 591, 558 A.2d 768 (1989); *Nast v. Lockett*, 312 Md. 343, 539 A.2d 1113 (1988).

<sup>2</sup>*Whiteley v. Lockner*, 1 Md. Rules Decisions 296 (1966).

<sup>3</sup>*Aetna Life Ins. Co. v. Lavoie*, 475 U.S. 813 (1986); *Bankers Life & Casualty Co. v. Crenshaw*, 486 U.S. 71 (1988); *Pacific Mut. Life Ins. Co. v. Haslip*, \_\_\_\_\_ U.S. \_\_\_\_\_, 59 U.S.L.W. 4157 (1991).

<sup>4</sup>Md. Cts. & Jud. Proc. Code Ann. §10-913(a) (1989 rep. vol.).

<sup>5</sup>Md. Rule 2-402(a) (1990).

<sup>6</sup>Note, *Pretrial Discovery of Net Worth in Punitive Damages Cases*, 54 S. Cal. L. Rev. 1141, 1142-47 (1981) (hereinafter Note, *Pretrial Discovery*).

<sup>7</sup>58 Cal. 210, 373 P.2d 472, 23 Cal. Rptr. 393 (1962).

<sup>8</sup>*Vollert v. Summa Corp.*, 389 F. Supp. 1348 (D. Haw. 1975).

<sup>9</sup>*Breault v. Friedli*, 610 S.W.2d 134 (Tenn. Ct. App. 1980).

<sup>10</sup>Cal. Civ. Code § 3295(c) (Supp. 1991); see also Schlueter & Redding, *Punitive Damages*, § 4.3(c)(2) (2d ed. 1987).

<sup>11</sup>77 N.J. Super. 18, 185 A.2d 241 (1962).

<sup>12</sup>*Leidholt v. District Court of Denver*, 619 P.2d 768 (Colo. 1980).

<sup>13</sup>*Campden v. Stone*, 635 P.2d 1121 (Wyo. 1981).

<sup>14</sup>48 A.D.2d 265, 368 N.Y.S.2d 904 (1975).

<sup>15</sup>*Whitley*, 1 Md. Rules Decisions 296.

<sup>16</sup>*Id.*

<sup>17</sup>*Miller v. Cook*, 1 Md. Rules Decisions 330 (1969).

<sup>18</sup>It is also important to the determination of this issue to note that the threshold question of whether a plaintiff is entitled to have the trier of fact consider an award of punitive damages is a question of law for the court to decide. See, *supra* Note 1, *Nast*, 312 Md. 343, 539 A.2d 1113.

<sup>19</sup>P. Niemeyer & L. Richards, *Maryland Rules Commentary* §§2-402 to 2-403 (1984).

<sup>20</sup>*Id.*

<sup>21</sup>*Whitley*, 1 Md. Rules Decisions 296.

<sup>22</sup>*Id.*

<sup>23</sup>Powell and Leiferman, *Results Most Embarrassing: Discovery and Admissibility of Net Worth of the Defendant*, 40 Baylor L. Rev. 527, 538-39 (1988).

<sup>24</sup>*Id.* at 539.

<sup>25</sup>*Rawnsley v. Superior Court*, 183 Cal. App. 3d 86, 227 Cal. Rptr. 806, 808 (1986).

<sup>26</sup>*Tennant v. Charlton*, 377 So. 2d 1169, 1170 (Fla. 1979).

<sup>27</sup>See also *Gierman* supra Note 11, 77 N.J. Super. at 25, 185 A.2d at 244.

<sup>28</sup>*Breault*, 610 S.W.2d at 139.

<sup>29</sup>Powell and Leiferman, *supra* note 22, at 540-42.

<sup>30</sup>*Doak v. Superior Court*, 257 Cal. App. 2d 825, 65 Cal. Rptr. 193, 198 (1968) (emphasis added).

<sup>31</sup>S. Woodbury, *Limiting Discovery of a Defendant's Wealth When Punitive Damages are Alleged*, 34 Def. L.J. 675, 679 (1985).

<sup>32</sup>*Id.* at 679. Woodbury states that the proper standard for whether the plaintiff has shown a *prima facie* case for punitive damages should be whether there is "a real possibility that punitive damages will be at issue at trial." *Id.* at 684 (citing *Chenoweth v. Schaaf*, 98 F.R.D. 587 (W.D.Pa. 1983)). This standard is significant in light of the pervasive federal influence on the Maryland Rules.

<sup>33</sup>Note, *Pretrial Discovery*, *supra* note 6, at 1141.

<sup>34</sup>*Id.* at 1165.

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This article was written and submitted prior to the decision of the Court of Appeals of Maryland in *Owens-Illinois, Inc. v. Zenobia*, 325 Md. 420, 601 A.2d 633 (1992).

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