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# CONTRACTS—The Supreme Court Speaks Where The Legislature Was Silent: Torrance County Mental Health Program, Inc. v. New Mexico Health & Environment Department

## I. INTRODUCTION

In *Torrance County Mental Health Program, Inc. v. New Mexico Health & Environment Department*,<sup>1</sup> the New Mexico Supreme Court ruled, on public policy grounds, that a plaintiff cannot recover punitive damages in a breach-of-contract claim against the state.<sup>2</sup> Striking down the hefty \$1.5 million punitive damages award in this case of first impression, the unanimous supreme court settled a question of law that stemmed from a disparity between two governmental immunity statutes. With an express statutory prohibition against tort-based punitive damages already in place,<sup>3</sup> this case likely represents the last word on the question of whether punitive damages can be recovered from the state. This article examines the propriety of punitive damages in a suit for breach of contract against the state.

## II. STATEMENT OF THE CASE

The plaintiff, Torrance County Mental Health Program, Inc. (“Torrance”), initiated an action in 1982 against the New Mexico Health and Environment Department (“HED”) and three of its employees. Torrance provided community mental health counseling services for the state from July, 1978, until the termination of its contract in December of 1981. According to Torrance’s version of the facts,<sup>4</sup> Torrance had been the victim of a conspiracy between HED officials and an ambitious Torrance employee named Vigil. Torrance alleged that, pursuant to a secret agreement with Vigil, HED officials staged a phoney inspection. This inspection, the validity of which was hotly contested at trial, disclosed “serious misuse of funds” by Torrance’s directors. HED terminated the contract pursuant to a contract provision that permitted rescission for misuse of funds. Shortly thereafter, HED awarded the contract to a rival corporation, Valencia Counseling Services, that had been quickly formed by Vigil.<sup>5</sup> Valencia Counseling Services continues to provide mental health services in Torrance and Valencia Counties to the present day.

Alleging that it had received a prearranged “hatchet job” from HED, Torrance and its former employees filed suit against HED and three of its officers. The initial complaint included claims under theories of breach

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1. 113 N.M. 593, 830 P.2d 145 (1992).

2. *Id.* at 601, 830 P.2d at 153.

3. See N.M. STAT. ANN. § 41-4-19(B) (Repl. Pamph. 1989).

4. For the purposes of the appeal, the court viewed the plaintiff’s version of the facts “in the light most favorable to support the jury’s verdict . . .” *Torrance County*, 113 N.M. at 594, 830 P.2d at 146.

5. *Id.* at 595, 830 P.2d at 147.

of contract, civil rights violations, and fraud. By the time the case actually came to trial in 1990, Torrance remained as the sole plaintiff, and the breach of contract claim remained as the sole cause of action. A pretrial order dismissed the claims against individual defendants so that, going into trial, HED remained as the only defendant.<sup>6</sup>

On the first day of trial, Torrance sought to amend the pretrial order to permit a claim for punitive damages "of approximately \$100,000." Torrance maintained that its earlier omission of the punitive damages claim had been the result of an oversight on the part of its former counsel. The trial court acceded and amended the pretrial order.<sup>7</sup>

After a four-day trial, the jury returned a verdict in favor of plaintiff for \$1.77 million compensatory and punitive damages. The compensatory damages consisted of awards of \$27,000 for employee expenses and \$250,000 for loss of corporate value; the judgment also included \$1.5 million in punitive damages. On appeal, HED sought to overturn the decision on three grounds: 1) the trial court erred when it amended the pretrial order and permitted the punitive damages claim; 2) there was insufficient evidence to support the award of compensatory damages; and 3) the award of punitive damages is improper in a breach of contract claim against the state. The New Mexico Trial Lawyers Association ("Trial Lawyers") submitted an amicus brief urging affirmance of the punitive damages award.<sup>8</sup>

In an opinion authored by Justice Montgomery, the New Mexico Supreme Court affirmed in part and reversed in part. The court affirmed the trial court's award of \$27,000 to compensate former employees for out-of-pocket costs occasioned by HED's breach. The supreme court struck down an award of \$250,000 which the trial court awarded for Torrance's loss of corporate value on the grounds that this award was "completely unsupported." Finally, the court reversed the award of \$1.5 million punitive damages after holding that public policy did not permit such an award.<sup>9</sup>

### III. HISTORY OF SOVEREIGN IMMUNITY AND PUNITIVE DAMAGES

On appeal, both plaintiff and defendant relied heavily on statutory construction and legislative intent arguments. The court, however, was not particularly persuaded by either interpretation of history and instead resolved the case on policy grounds.<sup>10</sup> Nonetheless, an understanding of the historical development of both sovereign immunity and punitive damages in New Mexico is essential to an analysis of the arguments.

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6. *Torrance County*, 113 N.M. at 595-96, 830 P.2d at 147-48.

7. *Id.* at 595, 830 P.2d at 147.

8. *Id.* at 596-97, 830 P.2d at 148-49.

9. *Id.* at 601-04, 830 P.2d at 153-56.

10. *Id.* at 599, 830 P.2d at 151.

### A. Governmental Immunity in New Mexico

The New Mexico territorial legislature adopted sovereign immunity when, in an 1876 statute, it received "the common law as recognized in the United States . . ."<sup>11</sup> Sovereign immunity had its roots in the medieval belief in the infallibility of the sovereign.<sup>12</sup> Common law sovereign immunity did not apply different rules to different causes of action. All claims against the state, whether based in tort, contract, or unjust enrichment, were invalid in the absence of an express statute authorizing such a claim.<sup>13</sup>

Prior to the supreme court's abolition of common law sovereign immunity in *Hicks v. State*<sup>14</sup> in 1975, the legislature enacted several specific waivers to the doctrine. The first waiver, a 1941 statute, permitted state liability for automobile accidents involving government employees.<sup>15</sup> Between 1941 and 1975, the legislature passed several other limited immunity waivers.<sup>16</sup>

A 1963 law waived sovereign immunity for breach of contract claims against the state.<sup>17</sup> Entitled "An Act Relinquishing the Sovereign Immunity of the State in Actions Based on Written Contracts," this law provided that "[a]ctions not otherwise provided by law may be maintained and any judgment enforced against the state and any of its agencies when based on a written contract."<sup>18</sup> During the thirteen-year period that the 1963 law remained on the statute books, the question of whether it authorized punitive damages never arose. Pre-*Hicks* sovereign immunity prohibited government liability for punitive damages "in the absence of a statute so authorizing."<sup>19</sup>

In a 1975 decision, *Hicks v. State*,<sup>20</sup> the New Mexico Supreme Court followed the lead of several other states and abolished common law sovereign immunity.<sup>21</sup> Two years earlier, the supreme court had foreshadowed this development by warning that the doctrine of sovereign immunity was "headed for a deserved repose."<sup>22</sup> Whether *Hicks* abolished sovereign immunity in all its forms or merely for tort actions was not entirely clear from the *Hicks* opinion. Although the *Torrance County* court adopted Torrance's position that *Hicks* had abolished sovereign immunity "in all its ramifications," the *Hicks* opinion itself had certainly

11. 1875-1876 N.M. Laws, ch. 2, § 2 (codified as N.M. STAT. ANN. § 38-1-3).

12. Jamie McAlister, Note, *The New Mexico Tort Claims Act: The King Can Do "Little" Wrong*, 21 N.M. L. REV. 441, 442 (1991).

13. See *id.* at 442.

14. 88 N.M. 588, 590, 544 P.2d 1153, 1155 (1975).

15. Ruth L. Kovnat, *Torts: Sovereign and Governmental Immunity in New Mexico*, 6 N.M. L. REV. 249, 252 (1976).

16. *Id.*

17. 1963 N.M. Laws, ch. 152 (codified as N.M. STAT. ANN. § 22-23-1 (1953)).

18. *Id.*

19. *Brown v. Village of Deming*, 56 N.M. 302, 311, 243 P.2d 609, 618 (1952).

20. 88 N.M. 588, 544 P.2d 1153 (1975).

21. *Id.* at 590, 544 P.2d at 1155-57. *Hicks* involved a wrongful death tort claim in which the plaintiff asserted that the state had negligently maintained a public bridge.

22. *City of Albuquerque v. Garcia*, 84 N.M. 776, 778, 508 P.2d 585, 587 (1973).

left ample room for the argument that it abolished sovereign immunity only for tort claims.<sup>23</sup>

The *Hicks* court recognized that it "would work an . . . injustice to deny defendant and other units of government a defense on which they have a right to rely."<sup>24</sup> Accordingly, the supreme court ordered that the abolition of sovereign immunity would be effective only for torts occurring after July 1, 1976.<sup>25</sup> The supreme court provided this respite to permit the legislature to take measures to protect the state from liability.<sup>26</sup> The New Mexico legislature quickly seized this opportunity and passed the Tort Claims Act, which became effective on July 1, 1976.<sup>27</sup> This act reinstated governmental immunity from suit and enumerated a number of specific exceptions to this immunity.<sup>28</sup> The Tort Claims Act specifically prohibited the recovery of punitive damages from the state: "No judgment against a governmental entity or public employee for any tort for which immunity has been waived under the Tort Claims Act shall include an award for exemplary or punitive damages or for interest prior to judgment."<sup>29</sup> As its name implies, the Tort Claims Act addressed only tort claims.<sup>30</sup>

Prior to the *Hicks* decision, the waiver of common law sovereign immunity required affirmative legislative action.<sup>31</sup> After *Hicks*, immunity would only exist when it was specifically imposed by the legislature.<sup>32</sup> This alteration in the fundamental theory underlying governmental immunity mandated a new legislative approach.<sup>33</sup> Accordingly, the same legislature that enacted the Tort Claims Act also repealed the 1963 statute which authorized contract claims against the state.<sup>34</sup> In its place, the legislature enacted a statute that accomplished the same end with different language. While the old law had "Relinquish[ed the] Sovereign Immunity of the State in Actions Based on Written Contracts," the new law "granted

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23. In what appeared to be the holding in *Hicks*, the court stated that "[c]ommon law sovereign immunity may no longer be interposed as a defense by the State, or any of its political subdivisions, in tort actions." *Hicks*, 88 N.M. at 590, 544 P.2d at 1155 (emphasis added). In contrast, another passage in the same paragraph did not confine its criticism to tort-based sovereign immunity: "[Sovereign immunity] can no longer be justified by existing circumstances and has long been devoid of any valid justification." *Id.* HED took the position that *Hicks*' abolition of sovereign immunity was limited to tort-based actions and left undisturbed the state's sovereign immunity from contract based claims. Appellant's Reply Brief at 16, *Torrance County Mental Health Program, Inc. v. New Mexico Health & Environment Dep't*, 113 N.M. 593, 830 P.2d 145 (1992) (No. 19-272). HED's position failed to take into consideration the reasoning of *Hydro Conduit Corp. v. Kemble*, 110 N.M. 173, 177, 793 P.2d 855, 859 (1990). See *infra* text accompanying notes 73-76.

24. *Hicks*, 88 N.M. at 594, 544 P.2d at 1159 (quoting *Spaniel v. Mounds View School*, 118 N.W.2d 795 (Minn. 1962)).

25. *Id.* at 593, 544 P.2d at 1158.

26. *Id.* at 594, 544 P.2d at 1159.

27. *Id.*

28. 1976 N.M. Laws, ch. 58, §§ 1 to 31 (codified as N.M. STAT. ANN. §§ 41-4-1 to -19 (Repl. Pamp. 1989)).

29. N.M. STAT. ANN. § 41-4-19(B) (Repl. Pamp. 1989).

30. *Id.* § 41-4-4.

31. See *Hicks*, 88 N.M. at 589, 544 P.2d at 1154.

32. See *Torrance County*, 113 N.M. at 597, 830 P.2d at 149.

33. See *Hydro Conduit Corp. v. Kemble*, 110 N.M. 173, 177, 793 P.2d 855, 859 (1990).

34. See *id.*

immunity from actions based on contract," and then waived this immunity for written contracts.<sup>35</sup>

Unlike the Tort Claims Act, the 1976 contract claims statute was silent on the issue of punitive damages.<sup>36</sup> The supreme court was unable to discern from this silence any legislative intent "one way or the other."<sup>37</sup> Thus, in ruling on the propriety of punitive damages against the state, the *Torrance County* court had to decide what significance, if any, to attribute to the disparity between these two statutes.<sup>38</sup>

### B. Punitive Damages

New Mexico courts have permitted recovery of contract-based punitive damages since the 1940 case of *Stewart v. Potter*.<sup>39</sup> The *Stewart* court said that "[s]uch damages are allowable where the wrong is aggravated, wanton, or maliciously intentional."<sup>40</sup> This standard has remained consistent during the half century that has elapsed since *Stewart*.<sup>41</sup> Although many jurisdictions require that the defendant's breach of contract must constitute an independent tort in order for punitive damages to be proper, New Mexico has declined to adopt this requirement.<sup>42</sup>

There are at least two published pre-*Hicks* New Mexico cases which involve punitive damage claims against governmental entities.<sup>43</sup> The courts disposed of both of these cases on sovereign immunity grounds.<sup>44</sup> Until *Torrance County*, a published New Mexico appellate opinion has not addressed the propriety of recovering punitive damages from a governmental entity under post-*Hicks* law.

## IV. LEGISLATIVE INTENT

Both *Torrance* and the Trial Lawyers relied heavily upon statutory construction arguments to support the contention that the legislature intended to permit recovery of punitive damages in contract-based claims against the state.<sup>45</sup> These arguments focused upon the fact that the 1976 post-*Hicks* contract claims statute made no mention of punitive damages.<sup>46</sup> This law stands in marked contrast to the 1976 Tort Claims Act which

35. See *id.*

36. See 1976 N.M. Laws, ch. 58, § 24 (codified as N.M. STAT. ANN. § 37-1-23 (Repl. Pamp. 1990)).

37. *Torrance County*, 113 N.M. at 598, 830 P.2d at 150.

38. *Id.*

39. 44 N.M. 460, 104 P.2d 736 (1940).

40. *Id.* at 464, 104 P.2d at 740.

41. See, e.g., *Romero v. Mervyn's*, 109 N.M. 249, 784 P.2d 992 (1989); *Hood v. Fulkerson*, 102 N.M. 677, 699 P.2d 608 (1985).

42. See *Romero*, 109 N.M. at 257, 784 P.2d at 1000.

43. *Rascoe v. Town of Farmington*, 62 N.M. 51, 304 P.2d 575 (1956); *Brown v. Village of Deming*, 56 N.M. 302, 243 P.2d 609 (1952).

44. See *Rascoe*, 62 N.M. at 55, 304 P.2d at 577; see also *Brown*, 56 N.M. at 316, 243 P.2d at 616-17.

45. See *Torrance County*, 113 N.M. at 597-99, 830 P.2d at 149-51.

46. *Id.*

specifically prohibits punitive damages in tort-based actions.<sup>47</sup> Torrance theorized that by silence, the legislature expressed its intent to permit punitive damages in contract claims.<sup>48</sup> HED's counter-argument was that the Tort Claims Act's prohibition served to immunize the state from punitive damages completely, regardless of the form of the claim.<sup>49</sup>

The New Mexico Supreme Court has recognized that, in applying a statute, its primary goal is to uphold legislative intent.<sup>50</sup> In determining legislative intent, the court looks primarily to the plain language of the statute: "When the words of the statute are free from ambiguity and doubt, resort should not be undertaken to any other means of interpretation."<sup>51</sup> If the statute's meaning is not apparent from the text, the court may consider the historical context of the statute's enactment.<sup>52</sup> Although New Mexico courts refuse to read into a statute that which is not there, they have been willing to "read the act in its entirety and construe each part in connection with every other part to produce a harmonious whole."<sup>53</sup> Applying these principles of statutory construction, the *Torrance County* court was unable to discern any legislative intent to permit punitive damages in contract claims against the state.<sup>54</sup> Instead, the court recognized the desirability of construing the two statutes to achieve a harmonious result:

What sense would it make to have one rule disallowing punitive damages for say, malicious conduct in committing a tort, and the opposite rule for the same or similar conduct in breaching a contract? We think that such a juxtaposition of the operative legal rule would be nonsensical, and we decline the invitation to adopt it.<sup>55</sup>

Disposing of Torrance's legislative silence argument, the *Torrance County* court said:

[O]ur legislature's silence on punitive damages in Section 37-1-23 cannot be read as expressing an intention to waive immunity for punitive damages in contract actions, even though in the same act (1976 N.M. Laws, Chapter 58 (2d Session)) the legislature, dealing with the major subject of the legislation (tort claims against the state), expressly granted immunity for punitive damages in tort cases.<sup>56</sup>

The court did not see a need to account for or explain the disparity between the two statutes: "We find no intent one way or the other on

47. *Id.* at 597, 830 P.2d at 149.

48. *Id.* at 597-98, 830 P.2d at 149-50.

49. Brief-in-Chief for Appellant at 31, *Torrance County Mental Health Program, Inc. v. New Mexico Health & Environment Dep't*, 113 N.M. 593, 830 P.2d 145 (1992) (No. 19-272).

50. See *First Nat'l Bank of Santa Fe v. Southwest Yacht & Marine Supply Corp.*, 101 N.M. 431, 435, 684 P.2d 517, 521 (1984).

51. *State ex rel. Stratton v. Roswell Indep. Schools*, 111 N.M. 495, 500, 806 P.2d 1085, 1090 (Ct. App. 1991).

52. See *State ex rel. Kline v. Blackhurst*, 106 N.M. 732, 735, 749 P.2d 1111, 1114 (1988).

53. *Id.*

54. *Torrance County*, 113 N.M. at 598, 830 P.2d at 150.

55. *Id.* at 601, 830 P.2d at 153.

56. *Id.* at 598, 830 P.2d at 150.

the subject of punitive damages in contract actions. Whether by legislative oversight or otherwise, the legislature simply failed to express its will on the subject."<sup>57</sup>

Even if the *Torrance County* court had attempted to divine meaning from the legislature's silence, it is doubtful that the court would have adopted Torrance's legislative silence theory. If one assumes arguendo that the New Mexico legislature's silence did reflect an intention to permit punitive damages in contract claims against the state, one faces two difficult questions: 1) Why would the legislature want to permit punitive damages for contract-based claims, but not for tort-based claims? and 2) Why did the legislature not explicitly state its intention?

In their appellate briefs, both Torrance and the Trial Lawyers argued that punitive damages would promote important social policies by deterring government officials from malicious conduct.<sup>58</sup> Yet, neither brief attempted to explain why, if the legislature intended to deter state agents from maliciously breaching contracts, the legislature refused to provide the same safeguard against malicious torts. Furthermore, neither brief attempted to explain why the legislature failed to state this intent explicitly. The absence of a credible rationale renders Torrance's legislative silence theory untenable.

The *Torrance County* court did not attempt to account for the disparity between the tort and contract claim statutes, except to say that the difference may have been the result of "legislative drafting or oversight."<sup>59</sup> An examination of the position occupied by punitive damages in the law of contracts supports the inference that the difference between the two statutes was merely the result of legislative oversight. In virtually all United States jurisdictions, punitive damage claims are far more prevalent in tort cases than in contract cases.<sup>60</sup> In *Romero v. Mervyn's*,<sup>61</sup> the supreme court expounded New Mexico's law of punitive damages in contract cases. The court held that punitive damages are appropriate when the breach of contract is accompanied by "malicious, fraudulent, oppressive, or . . . reckless[]" conduct.<sup>62</sup> In dicta, however, the *Romero* court also recognized that punitive damages are the exception rather than the rule in contract cases: "Notwithstanding the *general exclusion* of punitive damages from contract cases, however, exceptions long have been recognized."<sup>63</sup>

Most treatise writers agree that punitive damages are exceptional in contract law.<sup>64</sup> It is reasonable to assume that the drafters of the 1976

57. *Id.*

58. See Brief for Appellee at 46-52, and Brief of the New Mexico Trial Lawyers Association, Amicus Curiae, at 18-25, *Torrance County Mental Health Program, Inc. v. New Mexico Health & Environment Dep't*, 113 N.M. 593, 830 P.2d 145 (1992) (No. 19-272).

59. *Torrance County*, 113 N.M. at 598, 830 P.2d at 150.

60. See DAN B. DOBBS, HANDBOOK ON THE LAW OF REMEDIES § 12.4, at 818 (1973); see also Stephanie E. Pochop, Note, *Hoffman v. Louis Dreyfus Corp.: Punitive Damages on the Borderland of Tort and Contract*, 35 S.D. L. REV. 118, 124 (1990).

61. 109 N.M. 249, 784 P.2d 992 (1989).

62. *Id.* at 255, 784 P.2d at 998.

63. *Id.* at 257, 784 P.2d at 1000 (emphasis added).

64. See DOBBS, *supra* note 61, § 12.4, at 818; 5 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 1077, at 438-39 (1964).

contract claims statute were cognizant of this "general exclusion."<sup>65</sup> If these drafters had desired to go against the grain of a widespread legal norm, by permitting punitives in contract while denying them in tort, it seems that the drafters would have explicitly stated this intent. But, as the *Torrance County* court pointed out, it is unlikely that the drafters intended such a result.<sup>66</sup> A more plausible explanation is that the drafters of the contract claims statute, if they considered the matter, saw no need to exclude that which was already generally excluded in the contract law of New Mexico and the nation.<sup>67</sup>

As an alternative to the legislative intent argument, Torrance and the Trial Lawyers argued that *Hicks's* sweeping abolition of sovereign immunity in all its forms left in its aftermath only the common law.<sup>68</sup> The common law, as recognized in New Mexico, permits recovery of punitive damages in breach of contract claims.<sup>69</sup> Torrance and the Trial Lawyers argued that therefore, after *Hicks*, the common law doctrine which permits punitive damages in contract cases, unmodified by the legislature, equally applies to claims against the state.<sup>70</sup>

In contrast, HED adopted the position that the *Hicks* decision's abolition of sovereign immunity applied only to *tort* claims.<sup>71</sup> The uncertain language of the *Hicks* opinion left room for HED's argument that *Hicks* did not abolish the state's sovereign immunity to contract claims.<sup>72</sup> Nevertheless, in a 1990 case, *Hydro Conduit Corp. v. Kemble*,<sup>73</sup> the supreme court cleared up this ambiguity and ruled that *Hicks's* abolition of sovereign immunity applied to actions based in contract and quasi-contract as well as tort.<sup>74</sup> Thus, HED's position that sovereign immunity from contract claims remained intact after *Hicks* is irreconcilable with the *Hydro Conduit* decision.<sup>75</sup>

Taking the same position that it had taken in the *Hydro Conduit* decision, the supreme court agreed with Torrance that *Hicks* "generally abolished the common law doctrine of sovereign immunity in all its ramifications, whether in tort or contract or otherwise, except as implemented by statute . . . ."<sup>76</sup> Nonetheless, the supreme court refused to be bound by a "common law mandate that the state may be assessed punitive

65. Cf. *New Mexico ex rel. Bird v. State*, 91 N.M. 279, 284, 573 P.2d 213, 218 (1978) (legislature presumed to know existing common law).

66. See *Torrance County*, 113 N.M. at 598, 830 P.2d at 150.

67. See *supra* notes 61-64 and accompanying text.

68. *Torrance County*, 113 N.M. at 598, 830 P.2d at 150.

69. *Romero v. Mervyn's*, 109 N.M. 249, 255, 784 P.2d 992, 998 (1989).

70. *Torrance County*, 113 N.M. at 598, 830 P.2d at 150.

71. Appellant's Reply Brief at 16, *Torrance County Mental Health Program, Inc. v. New Mexico Health & Environment Dep't*, 113 N.M. 593, 830 P.2d 145 (1992) (No. 19-272).

72. See *supra* note 24.

73. 110 N.M. 173, 793 P.2d 855 (1990).

74. *Id.* at 173-74, 793 P.2d at 859-60. The *Hydro Conduit* court ruled that, although the *Hicks* opinion's abolition of sovereign immunity applied to quasi-contract, the contract claims statute, N.M. Stat. Ann. § 37-1-23 (Repl. Pamp. 1990), effectively prohibits quasi-contract claims against the state. Section 37-1-23 provides that the state shall only be liable for written contracts. Quasi-contracts are, by definition, implied and not written. Hence, a quasi-contract claim will not lie against the state.

75. See *supra* note 24.

76. *Torrance County*, 113 N.M. at 597, 830 P.2d at 149.

damages in contract actions.’<sup>77</sup> Instead, the supreme court adopted the position that the legislature’s silence left the issue “open for decision by this Court, applying what we believe to be the relevant policy considerations . . . .”<sup>78</sup>

## V. POLICY

In language that was reminiscent of such landmark cases as *Scott v. Rizzo*<sup>79</sup> and *Lopez v. Maez*,<sup>80</sup> the supreme court asserted its authority to shape the common law on the basis of policy in the absence of legislative action.<sup>81</sup> The court stated that “[r]esolution of that [punitive damages] issue is not dictated by anything the legislature has said, nor by any judicial precedents decided before or after our decision in *Hicks*.”<sup>82</sup> After setting this stage, the court went on to discuss what it saw as the relevant policy issues.<sup>83</sup>

The *Torrance County* court acknowledged that Torrance had raised a persuasive policy argument in favor of permitting punitive damages.<sup>84</sup> The court agreed that punitive damages would provide a strong disincentive against the abuse of government power and “‘send a message’ to the legislature.”<sup>85</sup> Nonetheless, the court determined that the public policy of deterrence was subordinate to two overriding policy considerations: 1) the irrationality of punishing taxpayers; and 2) the need to conserve tax dollars.<sup>86</sup>

### A. Punishment

The *Torrance County* court recognized that because punitive damages serve to punish the wrongdoer, an award of punitive damages against the state is, in effect, punishment of the taxpayers.<sup>87</sup> The court adopted the reasoning that the United States Supreme Court used when it rejected an award of punitive damages against a municipality in *City of Newport v. Fact Concerts, Inc.*:<sup>88</sup>

Punitive damages by definition are not intended to compensate the injured party, but rather to punish the tortfeasor whose wrongful action was intentional or malicious, and to deter him and others from similar extreme conduct . . . . Regarding retribution, it remains true that an award of punitive damages against a municipality ‘punishes’

77. *Id.* at 598, 830 P.2d at 150.

78. *Id.*

79. 96 N.M. 682, 634 P.2d 1234 (1981) (judicial adoption of comparative negligence).

80. 98 N.M. 625, 651 P.2d 1269 (1982) (judicial imposition of dram shop liability).

81. See *Torrance County*, 113 N.M. at 599, 830 P.2d at 151.

82. *Id.*

83. *Id.* at 599-601, 830 P.2d at 151-53.

84. *Id.* at 599, 830 P.2d at 151.

85. *Id.*

86. *Id.* at 600, 830 P.2d at 152.

87. *Id.*

88. 453 U.S. 247 (1981).

only the taxpayers, who took no part in the commission of the tort.<sup>89</sup>

A large number of jurisdictions have adopted positions virtually identical to that taken by the *City of Newport* Court.<sup>90</sup>

That the imposition of punitive damages upon government entities irrationally punishes innocent taxpayers is a widespread criticism.<sup>91</sup> Nonetheless, one can make the same criticism of the state's liability for compensatory damages. In its appellate brief, Torrance pointed out that "[the] argument that the taxpayers will ultimately pay punitive damages is equally applicable to compensatory damages against the state . . . ."<sup>92</sup> In New Mexico, as in most states, governmental entities can be liable for compensatory damages in certain types of tort and contract actions.<sup>93</sup> When a court holds the state liable for compensatory damages as a result of the act of a government agent, the innocent taxpayer bears the burden just as he would if the state paid punitive damages.

Whether the distinction between punitive and compensatory damages claims is valid may depend upon the proper function of these two different remedies. Under the law of New Mexico, the stated purposes of punitive damages are punishment and deterrence.<sup>94</sup> Arguably, punishment and deterrence are indistinct and punishment is merely the means by which deterrence is achieved. The court of appeals adopted this position in *State Farm Mutual Automobile Insurance Co. v. Maidment*<sup>95</sup> when it said that "[t]he deterrent effect of punitive damages on others, however, is inextricably tied to the punishment of the tort-feasor. If the tort-feasor cannot be punished, it follows that there can be no general deterrence."<sup>96</sup>

New Mexico courts have held that, in contract law, compensatory damages function primarily to compensate the plaintiff for the loss caused

89. *Id.* at 267. The *City of Newport* Court pointed out that holding the government official personally liable for punitive damages would best serve the aims of deterrence and punishment. *Id.* at 269. This is not a viable alternative under New Mexico law, however, because the Tort Claims Act prohibits the assessment of punitive damages against the government agent who commits a tort while acting within the scope of his employment. See N.M. STAT. ANN. §§ 41-4-4 to -19 (Repl. Pamp. 1989). In contrast, the New Mexico contract claims statute does not immunize a government official from liability. *Id.* § 37-1-23 (Repl. Pamp. 1990). Nonetheless, a breach of contract suit will not lie against a public employee when the employee's conduct is the cause of the state's breach because the official is not a party to the contract. Furthermore, the Tort Claims Act will not permit a suit against the government agent (individually) for the tort of interference with contractual relations if the agent was acting within the scope of his official duties. See *id.* §§ 41-4-1 to -19.

90. See, e.g., *Fisher v. Miami*, 172 So. 2d 455 (Fla. 1965); *Gary v. Falcone*, 348 N.E.2d 41 (Ind. Ct. App. 1976); *Foss v. Maine Turnpike Auth.*, 309 A.2d 339 (Me. 1973); *Chappell v. Springfield*, 423 S.W.2d 810 (Mo. 1968); *Sharapata v. Town of Islip*, 437 N.E.2d 1104 (N.Y. 1982); *Ranells v. City of Cleveland*, 321 N.E.2d 885 (Ohio 1975); *Nixon v. Oklahoma*, 555 P.2d 1283 (Okla. 1976). But see *Hennigan v. Atlantic Refining Co.*, 282 F. Supp. 667 (E.D. Pa. 1967), *aff'd* 400 F.2d 857 (2d Cir. 1968), *cert. denied* 395 U.S. 904 (1969) (applying Pennsylvania law); *Young v. City of Des Moines*, 262 N.W.2d 612 (Iowa 1978), *overruled by Parks v. City of Marshalltown*, 440 N.W.2d 377 (Iowa 1989).

91. See *supra* notes 90-91 and accompanying text.

92. Brief for Appellee at 50, *Torrance County Mental Health Program, Inc. v. New Mexico Health & Environment Dep't*, 113 N.M. 593, 830 P.2d 145 (1992) (No. 19-272).

93. See *supra* notes 33-39 and accompanying text.

94. N.M. UNIF. JURY INSTRUCTION CIV. 13-1827.

95. 107 N.M. 568, 761 P.2d 446 (Ct. App. 1988).

96. *Id.* at 570, 761 P.2d at 449.

by the defendant's breach.<sup>97</sup> Thus, the different goals between compensatory and punitive damages (compensation vs. deterrence) may provide a theoretical basis for the disparate treatment given these two remedies. In contrast, Judge Posner, the foremost Law and Economics theorist, asserts that the primary function of compensatory damages is not to compensate for the plaintiff's loss, but to deter uneconomical breaches.<sup>98</sup> If one accepts the premise that deterrence is the objective of both punitive and compensatory remedies, then there seems to be no theoretical justification for permitting one remedy and denying the other when the defendant is a government entity.

The rule that a government can be liable for compensatory but not punitive damages may also be justified on the ground that retribution is an element of punitive damages. If punishment for punishment's sake is a goal distinct from deterrence, then the disparate treatment given compensatory and punitive remedies is defensible. Prosser indicates that punitive damages include elements of both deterrence and retribution:

In one rather anomalous respect, however, the ideas underlying the criminal law have invaded the field of torts. Where the defendant's wrongdoing has been intentional and deliberate, and has the character of outrage frequently associated with crime, all but a few courts have permitted the jury to award in the tort action "punitive" or "exemplary" damages . . . . Such damages are given to the plaintiff over and above the full compensation for the injuries, for the purpose of punishing the defendant, of teaching the defendant not to do it again, and of deterring others from following the defendant's example.<sup>99</sup>

Ultimately, the question of whether there is any theoretical basis for treating punitive and compensatory damage claims differently may hinge on the question of whether retribution, the expression of society's outrage, can be the basis for the civil remedy of punitive damages. The debate which focuses on the question of whether retribution is a legitimate goal of criminal law<sup>100</sup> seems equally relevant to civil punitive damages. If retribution, by itself, can support an award of punitive damages, then the widespread objection to taxpayers paying such damages is theoretically sound. If, however, deterrence is the only legitimate aim of exemplary remedies, then the prohibition against government liability for punitive damages may be a mere line-drawing process by which tax dollars are safeguarded.<sup>101</sup>

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97. *Allen v. Allen Title Co.*, 77 N.M. 796, 798, 427 P.2d 673, 675 (1967).

98. See RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* § 4.1, at 91 (4th ed. 1992).

99. W. PAGE KEETON ET AL., *THE LAW OF TORTS* § 2, at 9 (5th ed. 1984). In contrast to Professor Prosser, Professor Posner questions the legitimacy of retribution, even as an objective of criminal law. Rather, Professor Posner argues that deterrence, not retribution, is the legitimate basis for both civil and criminal sanctions. See RICHARD A. POSNER, *THE ECONOMICS OF JUSTICE* 207-27 (1981).

100. See Jeffrie G. Murphy, *Marxism and Retribution*, 2 *PHILOSOPHY & PUB. AFF.* 217 (1973).

101. One could argue that the court has drawn the line in the wrong place. Under the provisions of the Tort Claims Act, a damage cap limits the state's liability to \$300,000 per person per incident. N.M. STAT. ANN. § 41-4-19 (Repl. Pamp. 1989). Thus, there is a viable argument that the legislature

### B. Conservation of Public Revenues

The *Torrance County* court identified the need to "protect public revenues" as the second policy justification for denying the recovery of punitive damages from government entities:

Revenues for the operation of state and local government programs are notoriously thin these days, and diversion of those revenues to punish a recalcitrant or abusive governmental agency may diminish funds available to carry out other programs that are of equal importance to the chastised program and merit it no reduction in funding because of another agency's derelictions.<sup>102</sup>

The court saw this need to conserve tax dollars as "especially compelling given the legislature's determination that public revenues shall not be diverted to payment of punitive damages in tort cases."<sup>103</sup>

One New Mexico court has pointed out that "the need to protect the public treasuries" is the foremost justification for governmental immunity.<sup>104</sup> Likewise, the high courts in a number of jurisdictions have recognized that there is a compelling need to limit government liability and to protect public revenues.<sup>105</sup> As the United States Supreme Court noted, the wealth of governments makes them particularly attractive and vulnerable:

Because evidence of a tortfeasor's wealth is traditionally admissible as a measure of the amount of punitive damages that should be awarded, the unlimited taxing power of a municipality may have a prejudicial impact on the jury, in effect encouraging it to impose a sizable award. The impact of such a windfall recovery is likely to be both unpredictable and, at times, substantial, and we are sensitive to the possible strain on local treasuries and therefore on services available to the public at large.<sup>106</sup>

Proponents of government liability for punitive damages argue that the danger to public revenues is minimal because judicial scrutiny will serve as a safeguard against huge, unjustified awards.<sup>107</sup> Even if this is true, punitive damage claims would likely impose a "strain on local treasuries" extending beyond the monetary judgment itself. The court of appeals has pointed out that governmental immunity "enables the gov-

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has already drawn the line, and therefore a plaintiff should be able to recover compensatory and punitive damages totalling \$300,000 in a contract-based claim against the state. Of course, the rejoinder to this argument is that the legislature's decree that punitive damages are not recoverable in tort actions against the state expresses the legislature's aversion to the concept of state liability for punitive damages. This is the position which HED argued and which the *Torrance County* court adopted. See *supra* notes 46-61 and accompanying text.

102. *Torrance County*, 113 N.M. at 600, 830 P.2d at 152.

103. *Id.*

104. See *Garcia v. Albuquerque Pub. Schools*, 95 N.M. 391, 394, 622 P.2d 699, 702 (Ct. App. 1980); see also *Hydro Conduit*, 110 N.M. at 173, 793 P.2d at 856.

105. See, e.g., *City of Newport*, 453 U.S. at 266; *Brown v. Wichita State Univ.*, 547 P.2d 1015, 1027 (Kan. 1976).

106. *City of Newport*, 453 U.S. at 270 (footnotes omitted).

107. See *Young v. City of Des Moines*, 262 N.W.2d 612, 622 (Iowa 1978), *overruled by Parks v. City of Marshalltown*, 440 N.W.2d 377 (Iowa 1989).

ernment and its various subdivisions to function unhampered by the threat of time and energy consuming legal actions which would inhibit the administration of traditional state activities."<sup>108</sup> If a state were to permit the recovery of punitive damages from itself and its subsidiaries, it would need to defend against potential plaintiffs attempting to get at the "ultimate deep pocket."<sup>109</sup> Longer court dockets and greater legal costs would impose additional drains on public revenues.<sup>110</sup> The potentially large size and versatility of punitive damage claims would be attractive to prospective plaintiffs,<sup>111</sup> and defense costs would probably burden governmental entities considerably.

## VI. CONCLUSION

By holding for policy reasons that the state cannot be liable for punitive damages, the *Torrance County* court essentially engaged in a line-drawing process. This legal dichotomy affords a powerful remedy to one plaintiff while denying it to another plaintiff who has the misfortune of suffering injury at the hands of the state. Some have criticized this as an arbitrary and unjust result.<sup>112</sup>

In *Torrance County*, the injured plaintiff argued that punitive damages, when awarded against the state, would promote important social policies by deterring public employees from future wrongful conduct.<sup>113</sup> Whether punishment and deterrence are distinct goals or punishment is merely the means by which deterrence is achieved, the innocent taxpayer ultimately bears the cost.<sup>114</sup> Had the *Torrance County* court affirmed the trial court's award of punitive damages, the taxpayers would have borne the brunt of the punitive sanction. The actual wrongdoers would have escaped punishment, and the fully-compensated plaintiff would have received a windfall. The supreme court reached a just result.

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108. *Garcia*, 95 N.M. at 394, 622 P.2d at 702.

109. See Ronald A. Cass & Clayton P. Gillette, *The Government Contractor Defense: Contractual Allocation of Public Risk*, 77 VA. L. REV. 257, 284 (1991).

110. Cf. *Brown v. Wichita State Univ.*, 547 P.2d 1015, 1027 (Kan. 1976) (governmental immunity is necessary because knowledge of government's vast resources encourages lawsuits).

111. See *City of Newport*, 453 U.S. at 270.

112. See David H. Hines, Note, *Municipal Liability for Exemplary Damages*, 15 CLEV.-MAR. L. REV. 304, 312 (1966).

113. See *supra* note 59.

114. See *supra* notes 88-102 and accompanying text.