

HOW TO PUT THE RIGHT CAP ON PUNITIVE DAMAGES

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In an important but split decision, *State Farm v. Campbell*, the U.S. Supreme Court in April held that "the Due Process Clause [of the 14th Amendment] prohibits the imposition of grossly excessive or arbitrary punishments on defendants in tort cases. This was the second High Court ruling in the past few years that rightly objected to steep punitive damage awards.

Punitive damages are often added to compensatory damages awarded to victims of drunk drivers, medical malpractice, defective goods, and others who suffer because of careless or irresponsible behavior. There is no controversy about the fact that incompetent doctors, intoxicated or reckless drivers, and companies that produce dangerous and shoddy products should have to pay for the harm they cause.

But compensatory damages alone may not be enough to deter harmful actions. It is not always possible for victims to detect careless medical practices, dangerous goods, and other behavior. Moreover, some victims may be unwilling to file lawsuits because of the sizable expense in time and money, the discomfort of having to testify in court, and the uncertainty that they will win even legitimate cases. So punitive damages are often valuable; they help encourage such lawsuits and deter dangerous behavior.

Given that punitive damages are desirable, how big should they be? In his dissent in the *State Farm* case, Justice Antonin Scalia argued that the determination of punitive damages should continue to be left to individual judges and juries because the Supreme Court cannot devise a "principled application" that determines what these damages should be in different circumstances.

Unfortunately, under the present system, the principle that juries sometimes use is the depth of defendants' pockets. The Utah jury in the *State Farm* case awarded the Campbells \$2.6 million in compensatory damages and \$145 million in punitive damages. On appeal, the Utah Supreme Court reduced compensatory damages to \$1 million but allowed the punitive ones. Punitive damages, therefore, amounted to 145 times compensatory -- a ratio that is far too high.

State Farm may have misled the Campbells, but its behavior was not especially reprehensible. It assured the Campbells they had no liability and no need to hire counsel to defend Curtis Campbell against charges he caused a serious auto accident. When the jury returned a large judgment against him, *State Farm* at first refused to pay but eventually relented and paid.

Excessive punitive damage awards are not harmless transfers of wealth: They damage the functioning of the U.S. economy and judicial system. Companies pass these costs on to consumers via higher prices. In addition, large punitive damages encourage expensive

class-action law firms, driven by the prospect of big contingency fees, to pursue unwarranted suits.

The challenge is to find rules to set punitive damages that are neither too weak nor clearly excessive. The Supreme Court indicated in the State Farm case that the ratio of punitive to compensatory damages should generally be in the single digits. Antitrust laws have established this ratio at 3 to 1 in private suits against companies engaged in monopolistic business practices. Although trebling damages is a rigid rule, it can be administered consistently and is a reasonable standard to apply in tort cases as well.

Some states have already acted to limit punitive damages in different classes of lawsuits. However, they generally have imposed maximum dollar limits, as when the Florida legislature recently voted to cap physician payments in malpractice suits for noneconomic damages at \$500,000. Yet to deter harmful behavior, punitive damages should not be capped. They should rise with the size of compensatory damages. It makes little sense to impose similar punitive damages for behavior that causes harm of \$50,000 and \$20 million.

Strict limits on the ratio of punitive to compensatory damages would elevate the importance of accurate measurement of compensatory harm. For example, loss of life in automobile accidents caused by drunk drivers, or wrong statements by producers of drugs that cause severe harm or death to inappropriate users, damage victims and their heirs in ways that go far beyond the loss of future earnings. Although economists have developed techniques to gauge the monetary value to individuals of the loss of future activities due to wrongful deaths, juries have been reluctant to rely on them.

One might agree either with the majority of justices in the State Farm case that the 14th Amendment implies restrictions on punitive damages, or with Justice Ruth Bader Ginsburg, who argued in her dissent that federal courts should defer to state legislators in the setting of punitive damages. But unless more is done at the judiciary or legislative levels to limit these damages, the American tort system will continue to be costly and arbitrary.