

# Punitive Damages

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## How Juries Decide

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By Rudolph Houck

*Wherever German businessmen gather and their talk turns to doing business in the United States, the topics of greatest concern are – in order of increasing concern – the U.S. legal system, jury awards and punitive damages. The recent book, Punitive Damages – How Juries Decide, University of Chicago Press (2002), should be of interest to all businessmen, but especially to Germans. This article is not a true book review, but rather a summary of the authors' findings, with some unscientific suggestions for reducing the risks of punitive damages.*



**A**s background, two University of Chicago Law School professors, Harry Kalven Jr. and Hans Zeisel (a German), conducted the first study of jury behavior, in 1966. The subject book builds on that tradition. The Chicago School is synonymous with economics and the role of economics in the law. As we will see, the behavior of juries is not consistent with the best outcome for society, at least from an economic standpoint. (For ease of reading, please note that the rules set forth in this article are all subject to exceptions and qualifications. No article intended for the businessman can cover this topic without such a disclaimer. To insert them wherever appropriate would make the article unwieldy and unreadable.)

In what situations are juries likely to award punitive damages? In negotiated, commercial transactions between businesses, the parties may protect themselves by agreeing to waive trial by jury or to submit disputes to arbitration. However, in claims by consumers or passers by injured by a product or by defendant's behavior, no such contractual arrangement is possible and

anyway public policy would not enforce it. Employees, too, may also have claims – for sexual harassment or age discrimination, for example – that cannot be foreclosed by agreement. This article will focus on situations where punitive damages cannot be excluded by contract.

To collect compensatory (in contrast to punitive) damages, the plaintiff must present evidence showing that (1) the plaintiff has suffered some harm; (2) the defendant caused the harm; and (3) in causing the harm, the defendant violated some legal standard controlling the conduct. Compensatory damages may be readily determined, such as the cost of repair or replace-

ment of a damaged or destroyed car or house, actual and estimated future medical bills, and lost income. If the case involves serious personal

injury to the plaintiff, the law allows the plaintiff to recover “pain-and-suffering damages.” The plaintiff’s attorney describes how the injury has devastated the plaintiff’s life and asks the jury for “compensation” for this loss.

The question of punitive damages does not come up until the jury has first decided that the defendant is liable for the plaintiff’s harm and has determined the amount of damages that will fully compensate the plaintiff. The the-

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ory of punitive damages is not to compensate the plaintiff but rather to deter the defendant, to teach it a lesson.

The bases most commonly used for a punitive damages award are “recklessness,” “reckless disregard,” “maliciousness,” “oppression,” “reprehensibility,” or “egregious or outrageous behavior.” “Reckless” conduct requires a conscious choice of action, either with knowledge of serious danger to others or with knowledge of facts that would disclose the danger to any reasonable person. It is highly unlikely that a corporate defendant would do something “malicious” or intending to cause harm. Therefore this article focuses on recklessness. A judge’s typical instruction to a jury would require it to find four factors in order to award punitive damages:

1. The defendant must be conscious of a particular grave danger or risk of harm and the danger or risk must be a foreseeable and probable effect of the defendant’s conduct.
  2. The particular danger or risks of which the defendant was conscious must in fact have eventuated.
  3. The defendant must have disregarded the risk in deciding how to act.
  4. The defendant’s conduct in ignoring the danger or risks must have involved a gross deviation from the level of care which an ordinary person would use, having due regard to all circumstances.
- In contrast, “negligence” is the failure to use the care that a

reasonable, prudent and careful person would use under similar circumstances. In some instances, the mere fact of injury is enough to justify the award of compensatory damages. The 4-part jury instruction described above appears to be a difficult standard for the plaintiff to meet. But the book explains in detail how human psychology works to both (a) lower that standard and (b) raise the amount of punitive damages awards.

The studies reported show areas of consistent and inconsistent jury behavior. (In the studies, the “juries” were not

actual juries but rather individuals selected by testing companies to play the roles of juries.) An area of great consistency and predictability is the relative level of outrage felt by the test subjects in response to reckless action of defendants. Faced with 10 scenarios, mock juries will consistently rank them in the same order of recklessness and resulting outrage. This predictability breaks down when the juries are asked to determine (a) when simple negligence crossed over into recklessness and (b) the dollar amount the defendant should pay by reason of its behavior.

**Other factors which affected jury awards:**

- Other factors which affected jury awards of punitive damages included the following:**
- **If the jury spent little time discussing the judge’s instructions, the award was likely to be higher. Juries generally spent little time considering the judge’s instructions and decided based on its “gut” feelings.**
  - **The farther away the plaintiff lives from the jury, the lower the award; the more distant the defendant, the higher the award.**
  - **If the defendant did an internal cost-benefit analysis in determining whether to take a particular safety precaution, the award was likely to be higher.**
  - **If the value put on life in such a study was high (thereby making it more likely that the defendant would act responsibly), the defendant was punished!**
  - **Jury deliberation does not result in an average of the awards the individual jurors were likely to grant pre-deliberation. The actual award was likely to be higher than any of the pre-deliberation awards. So the process of deliberating drove the award up.**
  - **Not surprisingly, the wealthier the defendant, the higher the award.**
  - **A corporate defendant will be punished more than an individual.**
  - **The amount of compensatory damages has little effect on the size of the punitive award. If compensatory damages have already been paid, the jury is less likely to award punitive damages.**

Juries cannot predictably translate their outrage into dollar amounts. The ranking function involved a limited number (10) of scenarios. In contrast, the dollar awards were (and in real life are) set on an unlimited scale.

Perhaps the key factor in predicting punitive damages awards is the amount asked for by the plaintiff's attorney, obviously an unscientific, uncontrolled factor. This is viewed as an "anchor" in the process of setting the punitive damages award. Otherwise the juror has no range or even starting place for determining the amount. Indeed, setting a cap on punitive damages also served as an

anchor, increasing the amount of some awards.

Another dangerous aspect of jury behavior was "hindsight bias." If an accident was described in theoretical terms to a jury, it was seen as being unlikely to occur. But if the jury was told that the accident did indeed happen, then the jury found it likely to occur, i.e. "I knew it all along." The next step in this false line of thinking is, "if I knew it, then the defendant must have known it. Therefore the defendant decided to ignore a likely risk and acted recklessly." So this

"hindsight bias" makes a defendant seem more reckless than it was, lowering the requirements for awarding punitive damages. Hindsight bias is not, however,

increased by the extent of the damages caused by the accident.

The amount of actual damages suffered by the plaintiff had little effect on the punitive damages award.

Although punitive damages are theoretically directed at deterring the defendant from engaging in reckless

**A significant number of jurors thought that no amount of money was too great to spend to avoid a risk, no matter how small.**

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behavior, in fact juries use punitive damages to punish the defendant, to “teach it a lesson.” The legal concept and purpose of punitive damages do not readily correlate with everyday layman’s concepts. A trial and a judge’s rather complex instructions at the end of the trial are simply not adequate to educate a jury to the subtleties of the law. As a result, more intelligent, higher educated juries are less likely to award punitive damages.

**Juries cannot predictably translate their outrage into dollar amounts**

The risk management aspect of punitive damages (given special importance by the

injured people may not know the cause of their injury, may not know their rights or may not have access to the court system. Punitive damages should be awarded to make up for these inefficiencies in the legal system. To award punitive damages in amounts that are too large will create economic inefficiencies, by forcing potential defendants to spend more money on risk avoidance than is economically efficient. Such awards deter innovation and progress.

This is where the logic of cost

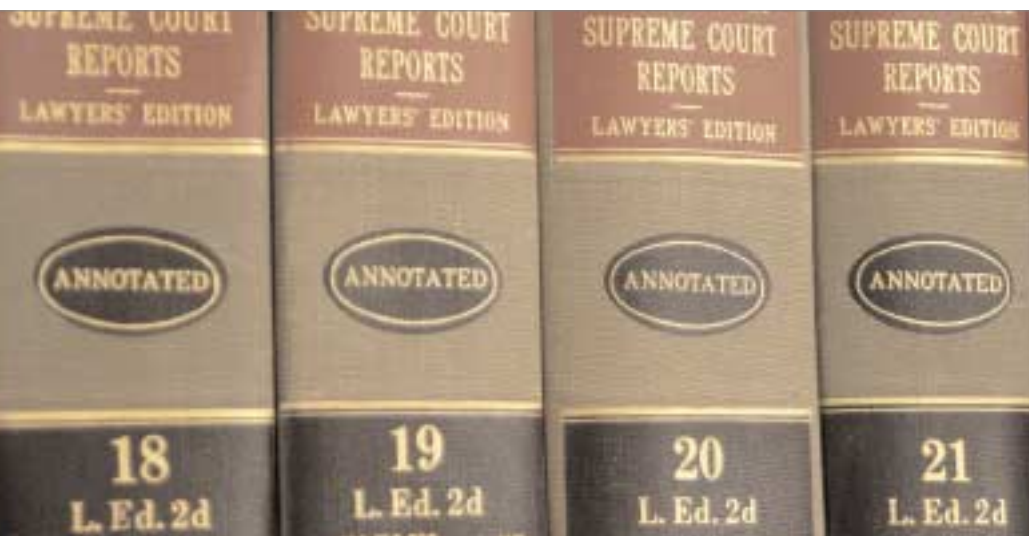
value of life” factor in the calculus of risk. Also, jurors do not factor in the likelihood of detection. The test jurors did not increase punitive damages awards based on the defendant’s efforts to avoid detection. A logical, risk deterrence calculus would mean the greater the likelihood of detection, the lower the punitive damages. Jurors focus on the plaintiff’s injuries and not on the possible benefits or logic of the defendant’s actions. Jurors punished corporations more than individuals. Apart from their distance and impersonal nature, corporations were assumed to have more resources to spend on reducing risks.

Finally, jurors were unable to judge the probability of events. They regularly overestimated the probability of improbable events and underestimated the probability of probable events. They also focus on the worst-case scenario, giving little attention to the most likely level of damages resulting from an accident. In contrast, judges who were tested did a better job of valuing human life and were less prone to hindsight bias. But their judgment too was flawed, seen from an economic standpoint. Judges sometimes awarded punitive damages in situations where economic analysis would fully justify the risk taken by the defendant.

In summary, despite the high stated standards for finding recklessness and awarding punitive damages, human nature works to lower those requirements. Hindsight, faulty

“Chicago School”) is basically as follows: The defendant should be deterred from conscious, overly risky behavior. This can be done most efficiently by taking away any reward the defendant might get from such behavior. If all plaintiffs injured by the risky behavior could recover their damages, this would be sufficient to deter the defendant. But the legal system is not so efficient. Many

benefit analysis, even using high values for human life and suffering – which results in spending more money on safety – runs into the illogic of the jury system. Apparently jurors find the conscious trade off of money for lives to be abhorrent. A significant number of jurors thought that no amount of money was too great to spend to avoid a risk, no matter how small. This is the “infinite



risk analysis, inability (or unwillingness) to understand and carry out the judge's instructions, sympathy for an injured plaintiff, lack of identification with a distant corporate defendant and a desire to teach it a lesson all increase the likelihood that punitive damages will be awarded. The amount of the award itself is increased by totally illogical factors including an absence of dollar standards, the dynamics of jury deliberation and a distaste for valuing lives in dollars.

Obviously the current system of punitive damages is illogical and economically destructive and in need of reform. The Chicago studies did not, however, result in a clear solution, even if it could be implemented. What can be done to reduce the risk until a solution is found?

The following suggestions and observations are based on the Chicago studies but not advocated by them. They are focused on U.S. subsidiaries of German companies. U.S. companies face these problems, but they are worse for German companies.

- Try to become a "small, local good citizen." Establish a local headquarters and staff it with local employees. Become active in local affairs. Sponsor local civic events. Hold an annual open house.
- "German-ness" is a double-edged sword. German precision makes it less likely that products will malfunction and less likely that they will cause damage. At the same time, perceived German cold-

ness and haughtiness increase the likelihood that the producer will be punished.

- As stated above, in commercial contracts, select a favorable jurisdiction as the exclusive site for trials. Obtain a waiver of jury trial. Consider arbitration as an exclusive remedy.
- In judging safety and responsibility, apply U.S. standards, not German ones. Americans are less likely to be familiar with how to use complicated products. Join a U.S. trade group. Read U.S. style instruction manuals and warning labels. Be sure any translation has been checked by a native English (U.S.) speaker.

- Similarly, learn U.S. standards of dealing with employees. Failure to understand and implement U.S. standards of political correctness and respect for diversity – gender, sexual preference, race, age, handicaps – can be very expensive. "How we do it in Germany" is no defense.
- Note that the use of cost-benefit studies will be punished. Of course this makes no sense, at least as long as life is given a relatively high value. Note that U.S. discovery procedures will require disclosure of any such studies.
- Pay compensatory damages fully and promptly.
- Indications of wealth will be

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punished. The life styles of top executives or wealthy German owners may increase punitive damages awards.

- Try to have the trial held in a favorable jurisdiction. White, male, well-educated juries are less likely to award punitive damages. Empanelling such a jury or getting a trial moved to a jurisdiction more likely to produce such a jury may not be simply a legal matter. Non-legal consultants may be required.
- Prepare economic information for the jury to counter the plaintiff's attorney's dollar request for punitive damages.
- Deal with the history of the German parent company. The

plaintiff's attorney will certainly describe the role of the company during World War II.

- In considering settlement negotiations, recognize that defendant's attorneys' estimates cannot be very reliable. The range of possible awards is quite wide.
- The length of time a jury takes to decide punitive damages can indicate at least two, contradictory dynamics. The more time a jury spends discussing the judge's instructions, the less likely it will award punitive damages. Once agreed to award punitive damages, the deliberations drive the award up, not down.

• The amount a defendant spent on safety devices may not have much effect on the result.

- In judging the likely outcome, ignore the judge's instructions. The jury will pay little attention to it. Focus on common sense as to liability, but focus on bad judgment and the plaintiff's request in predicting the amount.
- Ironically, reading this article and implementing its suggestions may be viewed by a jury as a sort of cost-benefit manipulation of the jury's informal legal system and thereby increase the likelihood and size of punitive damages awards.



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