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Stephen Carroll

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For information about the Institute for Civil Justice, contact

Dr. Deborah Hensler, Director
Institute for Civil Justice
RAND
1700 Main Street
P.O. Box 2138
Santa Monica, CA 90407-2138
310.393-0411, x6916
Internet: Deborah_Hensler@rand.org

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PREFACE

This publication contains the written statement of Stephen Carroll delivered on June 24, 1997 to the Judiciary Committee of the United States Senate. The statement is based on a RAND Institute for Civil Justice study of punitive damages in financial injury cases, but it does not necessarily reflect the views of the Institute, or RAND, or of the Institute's Board or research sponsors.

The author summarizes RAND estimates of the frequency and size of punitive damage awards in financial injury cases. He also presents estimates of what percentage of the financial injury punitive awards in the database would have been affected by caps of various sizes and how the caps would have affected the total amount of punitive damages awarded in such cases.

Punitive Damages in Financial Injury Jury Verdicts

Statement submitted to the Judiciary Committee of the United States Senate

by

Stephen Carroll

Institute for Civil Justice, RAND[1]

Mr. Chairman and Members of the Committee, thank you for inviting me to participate in your hearings on punitive damages. My name is Stephen Carroll; I am a Senior Economist in the Institute for Civil Justice at RAND. My testimony today is based on an Institute study of punitive damages we have just completed. The views and conclusions presented in my testimony are my own and should not be interpreted as representing the views of RAND, of the Institute for Civil Justice, or of the Institute's Board or research sponsors.

INTRODUCTION

Policy debates over punitive damages have generally focused on personal injury disputes, particularly in the areas of product liability and medical malpractice. However, ICJ research has established that almost half of all punitive damage awards were made in cases in which the damages were financial, rather than personal in nature. Moreover, these verdicts, which we call *financial injury verdicts* to distinguish them from personal injury verdicts, are far more likely to include an award of punitive damages. While punitive damages are awarded in less than four percent of all civil jury verdicts, there is a 1 in 7 chance of a punitive award in disputes arising from contractual or commercial relationships including, for example, disputes arising from insurance or employment contracts or from unfair business practices.

Little detailed information has been available about *financial injury* cases. To provide an empirical basis for the ongoing debate about punitive damages, we draw on the ICJ's jury verdict database to describe trends and patterns in punitive damage awards in financial injury cases in selected jurisdictions during the period 1985 to 1994. We provide a separate analysis of punitive damage awards in financial injury verdicts reached in Alabama between 1992 and 1997. Because caps on punitive damages are a prominent feature of many reform proposals, we also estimate what percentage of the financial injury punitive awards in our database would have been affected

[1]Stephen Carroll is a senior economist at RAND. RAND is a nonprofit institution that helps improve public policy through research and analysis.

by caps of various sizes and how the caps would have affected the total amount of punitive damages awarded in such cases.

THE DATA USED IN THIS STUDY

This study uses data collected from 1985 to 1994 in all state trial courts of general jurisdiction in the states of California and New York; Cook County, Illinois (Chicago); the St. Louis, Missouri, metropolitan area; and Harris County, Texas (Houston).[2] We supplement data from these jurisdictions with information obtained from the Administrative Office of the Alabama Courts for verdicts reached in that state's trial courts of general jurisdiction during the period 1992 to 1997. Because these data differ in important ways from the data in the ICJ database, we report the Alabama data separately.

Collectively, these jurisdictions account for about one-quarter of the U.S. population (1995).

For all financial injury verdicts in which punitive damages were awarded, we identified the particular type of dispute that led to the punitive damage award and added information about the parties, their relationship to each other, and the industrial sector in which the dispute arose.

It is important to keep the following in mind when interpreting jury verdict data:

- Cases tried to verdict may not be representative of all claims filed. Many claims are settled before reaching trial.
- The pattern of civil jury outcomes in any year or jurisdiction reflects the mix of cases tried to verdict in that year or jurisdiction, as well as jury decisions. The mix of cases may reflect changes in court jurisdiction, legal rules, and system user behavior.
- A substantial fraction of jury awards are reduced after verdict by trial or appellate court action or by settlement.
- We cannot assume that the patterns observed in one jurisdiction will be replicated in any other jurisdiction.

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[2]We omitted one very large financial injury verdict from Harris County—an award of more than 13 billion dollars, more than 3 billion of which was punitive—because it would have strongly affected many descriptions of the data. The next largest verdict in our database was less than one-thirtieth the size of this verdict.

PUNITIVE DAMAGE AWARDS IN FINANCIAL INJURY VERDICTS IN CALIFORNIA, COOK COUNTY, HARRIS COUNTY, THE ST. LOUIS METROPOLITAN AREA, AND NEW YORK: 1985 TO 1994

There are differing perspectives about which features of punitive damage awards are most important. Accordingly, we report multiple measures of punitive damage awards. The *fraction of cases in which punitive damages are awarded* indicates the probability that punitive damages will be awarded in a case. The *proportion of total awards that are punitive damages* indicates the fraction of all the moneys awarded by juries that are punitive. The *mean award* is, in a statistical sense, the amount a defendant could expect to pay if a jury made a punitive award. The *median award* indicates the typical amount of punitive damages awarded in the sense that if all punitive awards are ranked by amount, the median award is the one at the center; half of all punitive awards are larger than the median, and half are smaller. The *90th percentile award* captures the worst-case scenario; 90 percent of punitive awards are for amounts less than the 90th percentile award while only 10 percent of awards are larger. The *amount of punitive damages awarded in a case divided by the amount of compensatory damages awarded in that case* indicates how the punitive award compares to the harm suffered by the plaintiff, as measured by the amount required to compensate the plaintiff for his or her financial injury. For example, a 1.4 ratio of punitive damages to compensatory damages indicates that the punitive award was 1.4 times, or 40 percent greater than, the compensatory award.

Variation by Case Type

We categorized the financial injury cases in our database to reflect case types frequently mentioned in the policy debate, including: insurance,[3] employment,[4] securities,[5] real property,[6] other contract,[7] and other commercial.[8]

Table 1 summarizes the punitive damages awarded in all financial injury verdicts in the jurisdictions studied.

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[3]Disputes involving the existence, interpretation, or performance of an insurance contract.

[4]Disputes arising out of an employee-employer relationship.

[5]Disputes arising out of the existence of a security instrument, including stocks, bonds, and other instruments of finance or ownership. Includes shareholder derivative suits.

[6]Disputes arising out of the sale, lease, or improvement of real property.

[7]An aggregate of many types of contractual disputes other than those identified above.

[8]Financial injury cases arising out of non-contractual relationships between the parties. Largely antitrust and unfair business practice.

Table 1

PUNITIVE AWARDS IN FINANCIAL INJURY CASE TYPES: 1985 TO 1994

Type of Dispute	Number of Punitive Awards	Punitive Awards as % of No. of Verdicts	Punitive Awards as % of Total Amount Awarded	Punitive Damage Awards ($1992 millions) Mean	Punitive Damage Awards ($1992 millions) Median	Punitive Damage Awards ($1992 millions) 90th Percentile	Median Ratio of Punitive to Compensatory Award
Insurance	134	13	71	7.9	0.7	13.6	3.9
Employment	125	17	60	2.7	0.2	2.1	1.2
Securities	6	21	90	30.3	1.2	174.3	1.5
Real property	113	12	46	2.1	0.1	2.0	0.9
Other contracts	258	15	43	6.2	0.3	8.4	1.2
Other commercial	11	36	54	1.7	1.0	3.4	2.9
Overall	647	14	53	5.3	0.3	6.2	1.4

Excluding *securities* and *other commercial* cases in which we have few observations, punitive damages were awarded in about 14 percent of all financial injury cases tried to a jury verdict. Punitive award amounts were often high. The mean punitive awards varied from $2.1 million to $7.9 million, with an overall mean of $5.2 million. The overall 90th percentile award amount was $6.2 million.

Punitive damages represented a large portion of the total amount of damages awarded in these case types. Overall, punitive damages represented more than half of all the damages awarded, including those cases in which there was no punitive award, and more than 60 percent in insurance and securities cases.

Overall, the median ratio of punitive damages to compensatory damages was 1.4; thus, punitive awards were typically about 40 percent larger than the compensatory award. The highest median ratio was in insurance verdicts, where punitive awards were typically almost four times compensatory awards. The median ratio of punitive damages to compensatory damages was just under three for other commercial cases and ranged between 0.9 and 1.5 in the other case types.

Variation by Jurisdiction

Among the jurisdictions studied, punitive damages awards were most common in California (punitive damages were awarded in about 20 percent of all financial injury verdicts in California.) and in Harris County, Texas (14 percent of all financial injury verdicts). Punitive damages were awarded in about 7 percent of financial injury cases in the St. Louis metropolitan area and in about 4 percent of these cases in both Cook County and New York state.

Award amounts varied across jurisdictions. The mean punitive damage award was considerably higher in California ($5.8 million), Cook County ($3.2 million), or Harris County ($6.7 million) than in New York ($570,000) or the St. Louis metropolitan area ($360,000). And in the former three jurisdictions, punitive damages represented more than half of total damages awarded.

The ratio of punitive award to compensatory award also varied across jurisdictions. This ratio was much larger in Cook County (2.5) and the St. Louis metropolitan area(2.3) than in California (1.5), Harris County (1.0), or New York (0.5).

Variation Over Time

We examined the entire population of financial injury verdicts in our database for the five-year periods 1985–1989 and 1990–1994. The number of punitive awards decreased between these periods, both in absolute numbers and as a percentage of the overall number of verdicts. Punitive damages were awarded in about 16 percent of all financial injury verdicts in the 1985–1989 period and in about 13 percent of all financial injury verdicts in the 1990–1994 period. This change reflects the facts that plaintiffs are winning at a slightly lower rate, and given that they have won the case, plaintiffs are being awarded punitive damages at a slightly lower rate as well.[9]

However, the mean award amount increased from $3.4 million to $7.6 million between these two periods. In addition, punitive damages represented a larger portion of all damages awarded, rising from about 44 percent of all damages awarded in the 1985–1989 period to slightly less than 60 percent in the 1990–1994 period.

In contrast, the median ratio of punitive damages to compensatory damages fell over the two periods from 1.5 to 1.2. Given that the size of punitive awards, on average, grew from the late 1980s to the early 1990s, the decline in the median ratio of punitive to compensatory damages suggests that compensatory awards were climbing even faster.

ESTIMATED EFFECT OF CAPS ON PUNITIVE DAMAGE AWARDS

Many states have already approved caps on punitive damage awards, and similar measures are being considered in other states and at the federal level. To provide some context for the policy debate, we estimated what the effects would have been of imposing caps on the existing financial injury punitive awards in our database from California, Cook County, Harris

[9]The question of whether these changes reflect changed jury behavior or changes in plaintiffs' and defendants' litigation strategies, which, in turn, changed the mix of cases going to verdict, is beyond the scope of this analysis.

County, metropolitan St. Louis, and New York.[10] The caps we analyzed are different multiples of the compensatory damages awarded in the case. (Resource and time limitations precluded extending the analysis to the effects of absolute dollar caps, in addition to or instead of, multiples of compensatory damages, on punitive damages; we will explore that issue in future research.) We chose multiples of one through five and ten—an array of proposals that spans legislative efforts in many states.

If punitive damages had been capped at the amount of compensatory damages in each case, 60 percent of all punitive awards would have been affected, and the total amount of punitive damages awarded in these cases would have been reduced by roughly 65 percent. If caps had been imposed at higher levels, fewer awards and a smaller percentage of the damages awarded would have been affected. A cap of three times compensatory damages would have affected about one-third of all the financial injury punitive awards and decreased the total amount of punitive damages awarded by 40 percent. A cap of five times compensatory damages would have affected about one-quarter of all the financial injury punitive awards and decreased the total amount of punitive damages awarded by 27 percent.

PUNITIVE DAMAGE AWARDS IN ALABAMA: 1992 TO 1997

We analyzed data describing verdicts reached in Alabama's trial courts of general jurisdiction from 1992 to 1997. We estimated that the percentage of all financial injury verdicts in which punitive damages were awarded in Alabama was between 17 and 32 percent during the period 1992 to 1997.[11] The mean punitive damage award was between $540,000 and $945,000; the 90th percentile award was between $947,000 and $1.9 million. In Alabama, punitive damages represented between 80 and 86 percent of all damages awarded in all financial injury verdicts.

The median ratio of punitive damages to compensatory damages in Alabama was somewhat over 5; this suggests that in Alabama punitive damages are awarded more often and are higher in any given case relative to compensatory damages than in the other jurisdictions in our database.

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[10] Since 1987, Harris County has capped punitive damages at the greater of four times compensatory damages or $200,000 except in cases of malice or intentional tort. Consequently, for Harris County our estimate is the effect of imposing caps beyond the cap already in place.

[11] We present our results for Alabama as a range because some "general awards" are reported as a lump sum, without distinguishing what portion, if any, is a punitive award. The lower number in our estimated range of 17 to 32 percent assumes that the awards are entirely compensatory; the upper number assumes that they are entirely punitive.

We also estimated the effects of a range of caps on punitive damage awards in the Alabama data.[12] We estimated that a cap at the level of compensatory damages would have affected approximately 80 percent of the punitive awards in Alabama and would have reduced the total amount of punitive damages awarded by about 90 percent. A cap at three times compensatory damages would have affected the punitive damages awarded in 60 percent of the punitive damage awards in financial injury cases in Alabama and reduced the total amount of punitive damages awarded in these cases by 82 percent. A cap at five times compensatory damages would have affected the punitive damages awarded in half of the punitive damage awards in financial injury cases in Alabama and reduced the total amount of punitive damages awarded in these cases by 77 percent. In our estimates, we assumed that all general awards were compensatory. Had we assumed that they were in part or entirely punitive in nature, the effect of caps would have been larger.

Mr. Chairman, this completes my testimony. I submit prepublication copies of the study on which my testimony is based for the record. I will be pleased to answer any questions.

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[12]Alabama law limits punitive damages to $250,000, unless the defendant has exhibited a pattern or practice of intentional wrongful conduct involving actual malice or libel, slander or defamation.