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Punitive Damages in Developing Countries: The Argentine case

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Punitive Damages in Developing Countries: The Argentine case

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Abstract: Argentina is one of the four identified developing countries that permit punitive damages. Additionally, it is the only country in the world that has a pure continental-civil law system that allows them. Furthermore, the Argentine doctrine and jurisprudence developed a modern exegesis about the function, admission and amount of this legal remedy, which is compatible with the traditional theory of economic analysis of law. The purpose of this paper is to analyze the Argentine case, as a good model for other countries and use the traditional theory of economic analysis of law, in order to understand better the Argentine modern exegesis and its value to maximize social welfare.

Keywords: punitive damages, function, admission, amount, economic analysis of law, Argentina.

I. INTRODUCTION

David G. Owen (1994, p. 636) claims that "'P[unitive]' or 'exemplary' damages are money damages awarded to a plaintiff in a private civil action, in addition to and apart from compensatory damages, assessed against a defendant guilty of flagrantly violating the plaintiff 's rights" (footnote omitted). Only four developing countries[1] can be identified allowing punitive damages: South Africa, India, the People's Republic of China, and Argentina.

Argentina deserves special attention for three main reasons. First, it is the

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[1] Even if there is not an unanimous consensus about this kind of classification, and about the countries that should be included in it, a further discussion on this issue exceeds the purpose of this paper. For practical reasons we follow the well-known classification made by the International Monetary Fund in 2013 (pp. 142-143). In this paper, we understand that developing countries (or less developed countries) are countries that have emerging markets and developing economies. According to the IMF "The group of emerging market and developing economies (154) includes all those that are not classified as advanced economies." (p. 138).

only country in the world with a *pure* continental-civil law system[2] that successfully overcame prejudice and distrust against punitive damages, and accepted them (specifically, in its Consumer Protection Law in 2008). Second, its doctrine and jurisprudence developed a rich debate on this topic, from which we highlight a modern and valuable exegesis about the function, admission, and amount of punitive damages. Third, this modern exegesis is consistent with the postulates of the Economic Analysis of Law (EAL).

The purpose of this work is certainly modest. The article analyzes the modern Argentine interpretation of punitive damages so it can serve as a good example and guide for other countries. Additionally, the paper discusses, in some depth, the traditional EAL theory in order to understand better the Argentine modern exegesis and its importance for welfare maximization.

II. THE HISTORY AND CURRENT AVAILABILITY OF PUNITIVE DAMAGES

Legal remedies similar to punitive damages existed over forty centuries ago in the Code of Hammurabi and during the 5th century B.C. in the Law of the Twelve Tables of Rome. In 1275, the common law system of the United Kingdom allowed punishments for double damages caused to victims who were religious. Owen (1976) affirms that the precedent of the term known today as punitive damages is the case *Huckle v. Money* in 1763 (which is a case about an abuse of power against a traveler). Furthermore, punitive damages were widely accepted until the case *Rookes v. Bamard* (1964). Thereafter, the House of Lords (pp. 37-38) recognized punitive damages in only three categories of assumptions: (a) The first category is when there is "oppressive, arbitrary or unconstitutional action by the servants of the government"; (b) the second category is when "the Defendant's conduct has been calculated by him to make a profit for himself which may well exceed the compensation payable to the plaintiff"; and (c) the third category is when "exemplary damages are expressly authorised by statute".

The United States took punitive damages from British law: their major repercussion started in the 1970s. Currently, this legal remedy is allowed in forty-five of the fifty states. In the remaining five (Louisiana, Massachusetts, Nebraska, New Hampshire, and Washington), it is not allowed, unless it is specifically

[2] For example, the other three named countries have *mixed* legal systems: they are derived partly from the common law tradition and partly from the civil law tradition. Tetley (2000) explains that a *legal system* "is an operating set of legal institutions, procedures, and rules" (p. 681); a *mixed legal system* "is one in which the law in force is derived from more than one legal tradition or legal family" (p. 684); and a *legal tradition or family* "is a set of deeply rooted, historically conditioned attitudes about the nature of law, about the role of law in the society and the polity, about the proper organization and operation of a legal system, and about the way law is or should be made, applied, studied, perfected, and taught" (p. 682).

authorized by their statutes. In addition, punitive damages are also obtainable in countries whose legal systems are derived at least partly[3] from the common law tradition, such as Canada, Australia, New Zealand, Philippines, India, South Africa, and the People's Republic of China.

On the other hand, scholars from pure continental-civil law countries (with the exception of Argentina) often view punitive damages with suspicion and distrust because they usually consider this legal tool belongs in particular to the common law tradition (Salvador Coderch, 2001). Consequently, they believe that it should not be allowed by their countries that have a different legal tradition (one with a Roman origin). They think that in these countries where the focus of the tort system is on full compensation of the harm inflicted (i.e., where compensation is based on actual loss, but no more), the availability of this legal remedy would defeat their legal institutions and tradition (Bustamante Alsina, 1994a, 1994b).

III. PUNITIVE DAMAGES IN ARGENTINA

III. a) First step: Admitting punitive damages

In general, the statement that punitive damages are alien to the continental-civil law tradition is irrelevant in Argentina, since the majority of scholars believe that they should analyzed legal remedies (traditional or not) in terms of the advantages and disadvantages associated with their adoption, rather than closing a priori the marketplace of new ideas on legal policy (Salvador Coderch & Castiñeira Paul, 1997).[4]

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[3] See the former footnote. For example, in general in Canada and in particular in Quebec there is a mixed legal system (Tetley, 2000). In fact, whereas the common law system has prevailed in Canada, the French Civil Code of 1804 has been the main influence in Quebec's private law. Nevertheless, even though the French continental-civil law system does not admit punitive damages, the Quebec Civil Code of 1992 provides them (see Articles 1610, 1899, 1902, 1968, and, especially, 1621). Among others, the People's Republic of China (PRC) is another example of a mixed legal system. It has, officially, the socialist legal system with Chinese characteristics, and it has been influenced by different legal traditions. There are independent legal systems in Hong Kong, Macau and Mainland China. Hong Kong has the common law system adopted from the United Kingdom, Macau has the continental-civil law system inherited from the Portuguese civil law system, and Mainland China also has this latter system but influenced mainly by the German civil law system (among other European civil law systems). In the PRC, for instance, Article 47 of its Tort Law of 2010 allows victims to be required to pay punitive damages (or punitive compensation as are denominated in the PRC).

[4] For example, the Argentine Civil Code was enacted by Law 340 on September 25, 1869, and took effect on January 1, 1871. Its drafter, Dalmacio Vélez Sarsfield, and the vast majority of the Argentine legal experts at that time agreed that the civil code should base its liability system on negligence rules (e.g., see Articles 509, 520, 521, 903-906, 1067, 1072, 1109). The reform of the civil code made by the Law 17711 of 1968 was inspired by new social requirements that were clearly non-traditional ones. For instance—beyond some isolated cases that the majority doctrine

The idea of admitting punitive damages in Argentina began in 1993 with the published paper written by Daniel Pizarro; he studied this legal remedy and openly advocated for its Argentine reception. This work provoked a rich debate: some scholars supported Pizarro's position (e.g., Trigo Represas, 1995), others opposed it (e.g., Bustamante Alsina, 1994a, 1994b), and others adopted an eclectic viewpoint (e.g., Kemelmajer de Carlucci, 1993). All in all, since 1994, the vast majority of Argentine doctrine has agreed that punitive damages should be accepted in the country (according to the conclusions of the National Conference on Private Law, Corrientes, 1994, the Fifteenth National Conference on Civil Law, Mar del Plata, 1995, and the Seventeenth National Conference of Civil Law, Santa Fe, 1999; see Sobrino, 1996; Alterini, Ameal & López Cabana, 1998; Ghersi, 1998; Zavala de González, 1999; Galdós, 1999).

Finally, in 2008, the Amendment Bill to the Law 24240 (2008), Argentine Consumer Protection Law (*Ley de Defensa del Consumidor*, 1993), was approved and incorporated the Article 52 bis. It provides the following:

> Punitive Damages. If a supplier does not meet his legal or contractual obligations to a consumer, at the request of an injured party, the judge may impose on the supplier a civil fine in favor of the consumer, which is graduated according to the gravity of the offense and other circumstances, beyond compensatory damages. When more than one supplier is responsible for the failure, they are jointly and severally liable to the consumer, without prejudice to any contribution action in their favor. The civil fine that is imposed may not exceed the maximum monetary punishment of the fine provided in Article 47, inc. b of this law. [Article 47, inc. b establishes a maximum of 5 million Argentine pesos.]

III. b) Second step: Interpreting punitive damages

Because of the ostensible vagueness of this article and the doctrine's[5] and jurisprudence's[6] crucial role in Argentina, scholars and judges have seriously

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considered cases of presumed negligence (e.g. harm caused by animals, Arts. 1124 *et seq.*) and that the minority doctrine argued were cases related to strict liability— the truth is that the reform of 1968 introduced non-traditional rules different from the negligence liability: strict liability for damages arising from the risk or defect of things (Art. 1113), the abuse of rights (Art. 1071), compensation for reasons of equality (Art. 907), and so forth.

[5] Comparative law scholars Tetley (2000), David and Brierley (1985) explain that the doctrine in continental-civil law countries has a very important function, even more than in common law countries. Its function is to "clarify and purge the subject of impure elements, and thus provide both the practice and the courts with a guide for the solution of particular cases in the future" (David & Brierley, 1985, p. 94). In addition, it is worthwhile to stress that the Argentine doctrine is not an exception in this regard.

[6] The Argentine doctrine concluded unanimously in both the *XXII National Conference on Civil Law* (Córdoba, 2009) and the *XII Bonaerense Conference on Civil, Commercial, Procedure, and Labor Law* (Junín, 2009) that punitive damages under the "Art. 52 bis of Law 24240 (as

analyzed this legal remedy to provide precise legal guidance. We underline and explicate in this section the Argentine modern exegesis about the function, requirements and proper calculation of this legal remedy, consistent to the traditional EAL theory.

As explained in a previous paper (Irigoyen-Testa, 2009), the function or purpose of punitive damages in Argentina can be divided into: a principal function (deterrence); and an accessory function (sanction). The former, the main function, is the deterrence of harm conforming to the socially desirable level of care. The latter, the accessory function, is the sanction of the defendant; this accessory function (sanction for the factual circumstance of being a monetary award that goes beyond compensatory damages) follows the fortunes of the principal function (deterrence). That is, the defendant should only be imposed with punitive damages (sanction function) when society needs to deter him (principal function of deterrence), in an extra way, with an additional monetary award beyond compensatory damages, in line with his reprehensible behavior.[7] Both functions can be justified by the goal of welfare maximization (in aggregate terms). The main function (deterrence) tends to prevent the number and severity of socially intolerable damages, and, consequently, to raise average population well-being. The accessory function (sanction) has a teleological foundation, considering the effects of punishment on human behavior and the desirability of these effects in accordance with welfare maximization.[8]

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amended by Law 26361) have significant technical deficiencies, but these can be corrected by a prudent and rational application of them by the judges."

[7] These ideas have been accepted by Argentine jurisprudence. Thus, among others, the National Civil Court of Appeals, Chamber F (Cámara Nacional de Apelaciones en lo Civil, sala F), in the case *Cañadas Pérez María v. Bank Boston NA* (2010), said: "The principal function [of punitive damages] is the deterrence of harm according to the socially desirable level of care (...) The accessory function of punitive damages would be the sanction of the offender, because any civil fine, by definition, has a sanction function for the factual circumstance of being a money award that goes beyond compensatory damages—civil fines are to sanction defendants as compensatory damage are to compensate victims— (in accordance with Irigoyen-Testa, Matías, ¿Cuándo el juez puede y cuándo debe condenar por daños punitivos?, published in Revista de Responsabilidad civil y seguros, La Ley, no. X, October 2009)." The same ideas are also explained in decisions of the Superior Courts of Argentine provinces (e.g., *Borquez Juana Francisca v. Cía. de Teléfonos del Interior S.A. CTI Móvil*, 2011), Courts of Appels of other Argentine provinces (such as, *Suhs, Javier Alejandro v. Armorique Motors S.A.*, 2012), and, National Courts of First Instance of Argentina (e.g., *Pinillos, Pablo Daniel v. Supermercados Mayoristas Yaguar S.A.*, unpublished).

[8] These arguments are rooted in utilitarian positions, whose classical exponents were Jeremy Bentham (*An Introduction to the Principles of Morals and Legislation*, 1789), and John Stuart MILL (*Utilitarianism, Liberty, and Representative Government*, 1863). Notice that, according to EAL theory, the accessory function (sanction) is not to inflict a pain (through a monetary award) on someone who intentionally harmed the victim (theory of private retribution) or the victim's society (theory of social retribution), injuring freedom and the equality of rights (for an in-depth

With respect to the requirements for the admission of punitive damage, the majority of the Argentine doctrine and jurisprudence requires two *sine quo non* conditions: (a) The defendant's behavior is considered a seriously reprehensible conduct (it involves *dolo* [malice or recklessness] or *culpa grave* [gross negligence]),[9] and (b) the sanction (the accessory function) is "necessary" to address the main function (deterrence). In Argentina, from the EAL point of view we claim that, in cases of seriously reprehensible conduct, it is "necessary" to sanction the wrongdoer, when there is a probability less than one hundred percent that the wrongdoer is sentenced to compensate the total value of the damage caused or expected (Irigoyen-Testa, 2006, 2011, 2012).[10]

Finally, regarding the socially desirable amount of punitive damages, the basics of the passed Amendment Bill to the Law 24240 state that: "Punitive damages are intended to disrupt the perverse equation that encourages an injury to occur because it is cheaper to compensate it, in individual cases, than prevent it for general cases."[11] In order to disrupt this perverse equation (deterrence

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analysis on the function of punitive damages, see OWEN, 1989; WRIGHT, 1995, 1999; SUNSTEIN, KAHNEMAN & SCHKADE, 1998; GEISTFELD, 2005; COLBY, 2003, 2008; SEBOCK, 2007; ACCIARRI & IRIGOYEN-TESTA, 2015).

[9] Firstly, we believe that this requirement could also be justified by the EAL theory. The explanation of this statement exceeds the objective of this paper (see COOTER, 1999, p. 24-29). Secondly, in Argentina, the legal term *dolo* can be classified, mainly, as the following: (a) *dolo directo* (direct or actual malice), (b) *dolo indirecto* (indirect malice), and (c) *dolo eventual* (recklessness).

[10] At the *Third Euro-American Conference on Consumer Protection Law* (Buenos Aires, 2010), the following *lege lata* motion passed unanimously (commission no. 5): "Punitive damages should only be admitted when the supplier acted at least with gross negligence " and "the monetary punitive damage award should not be less than or exceed the amount necessary to fulfill its function of deterrence." Additionally, the Argentine jurisprudence said: "arguing that a lawyer is entitled to require and a judge should admit punitive damages based on the mere circumstance that the supplier has not fulfilled his legal or contractual obligations is contrary to the essence of punitive damages and more than 200 years of their history. Judges need something else in order to be able to admit punitive damages: the evidence of the defendant's malice or gross negligence" López Herrera, Edgardo, "Daños punitivos en el Derecho argentino, Article 52 bis, Ley de Defensa del Consumidor", JA, 2008-II, 1201." (See *La Cruz, Mariano Ramón v. Renault Argentina S.A. and other*, 2010; also see *Ríos, Juan Carlos v. Lemano S.R.L. Altas Cumbres,* 2010.) In addition, the Argentine jurisprudence quoted that punitive damages are "closely associated with the idea of prevention of certain injuries, and also the sanction of wrongdoers and the full dismantling of illicit effects; because of the severity of the wrong or the illicit consequences, more is required than the mere compensation of harm caused (Stiglitz, Rubén S. and Pizarro, Ramón D., "Reformas a la ley de defensa del consumidor", LL 2009-B, 949)" (*Machinandiarena Hernández, Nicolás v. Telefónica de Argentina,* 2009).

[11] In this regard, the Argentine Supreme Court of Justice in the case *Banco Central de la República Argentina v. Banco Patricios S.A.* (2006) said: "this Court has repeatedly stated that the general context and the informed legal purposes must be taken into account in the task of interpreting the law ... The application of this interpretative guideline imposes an inquiry into the

function) scholars concluded unanimously, in the *XI International Conference of Tort Law, AABA* (Buenos Aires, 2011), the following: "To calculate a punitive damage award that is neither higher nor lower than the amount needed to fulfill its deterrence function, it would be valuable to use math formulas, among other tools, to fulfill this function."[12]

Because the traditional EAL theory of punitive damages helps to understand better the Argentine exegesis and its value to maximize social welfare, we address it in some detail in next section.

IV. THE TRADITIONAL ECONOMIC ANALYSIS OF LAW THEORY OF PUNITIVE DAMAGES

According to the traditional EAL theory (Cooter, 1982, 1989; Posner, 1992; Polinsky & Shavell, 1997; Cooter & Ulen, 2000), punitive damages collaborate with the tort system to achieve the adequate level of care. In principle, the tort system does not need them to deter correctly civil wrongs. In general, compensatory damages are sufficient to achieve this goal.

As explained in previous papers (Irigoyen-Testa, 2012; Acciarri & Irigoyen-Testa, 2015), the latter statement may be clarified by the so-called Hand formula (which arises from the ruling of judge Hand in the case *United States v. Carrol Towing*, 1947). According to the formula, people should be considered guilty when they do not prevent injuries with expected values greater than the amount required to avoid these injuries; or more precisely, when they cause inefficient harm without investing in the optimal amount necessary to prevent it.[13] The Hand formula can be written as follows:

[1]

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purpose of the lawmakers in the parliamentary debate (Fallos: 182:486; 296:253; 306:1047)." (p. 4)

[12] Also see motion passing unanimously at the Euro-American Congress on Legal Protection of Consumers quoted in footnote 10. Additionally, the Argentine judge Falco (2011, p. 14) of the Civil and Commercial Court of First Instance, 9th Judicial District, Province of Córdoba (*Juzgado de Primera Instancia, 9ª Nominación, Civil y Comercial*, Córdoba) explains that "The proposed formulas or calculations are another tool *in order to provide fairness and proper foundation to calculate the 'civil penalty' [punitive damage]* [italics added], but they are not the only one."

[13] An expected ham is inefficient or efficient when its economic valuation is, respectively, higher or lower than the amount needed to prevent it. The EAL theory states that the law should create incentives to prevent inefficient harm. In this paper, we address the optimal term as used generally in the EAL literature, according to the Kaldor-Hicks efficiency criterion (Kaldor, 1939; Hicks, 1940): we face an optimal situation when there is no room for improvement since, if a change takes place, winners would get less than the losses that others would endure (the social welfare would decline). For further information on these topics, see Acciarri, 2009; Cooter & Acciarri, 2012.

$$L < p_h H$$

Where L represents the level of care that is socially desirable to prevent the expected harm, and $p_h H$ is the expected harm (H is the value of the harm if it occurs, and p_h is the probability of its occurrence).[14]

For example, if tortfeasors do not invest \$ 9 (L) to prevent an expected harm of \$ 10 ($p_h H$) (i.e., there is a probability of 10%, p_h, that the harm of \$ 100, H, occurs), then they should be considered guilty.

$$\$9 < 10\%\$100 = \$10 \qquad [2]$$

Rational and risk-neutral people with perfect information will always prefer to invest \$9 in the desired level of care instead of accepting a higher expected payment for compensation, \$10. In these cases, in principle, compensatory damages are sufficient to induce them to invest \$9 in precaution. (So, an extra award as punitive damages is not necessary.)

However, in many instances some individuals have a probability of being sentenced to pay for the total harm caused and/or expected (\$10) less than one hundred percent ($p_c < 100\%$). Suppose, for example, that some suppliers realize that only 50% ($p_c = 50\%$) of the injured consumers are able to prove in court that the suppliers are guilty (or that only 50% of the victims who suffered micro-damages are willing to sue). In these cases, the suppliers who act based on their low probability (of being made to compensate the total injury caused) do not have proper incentives to invest \$9 in the level of care, since (although the expected harm is still \$10; $p_h H = 10\%\ \$100 = \$10$) their own expected payment for compensation is only \$5 ($p_c p_h H = 50\%\ 10\%\ \$100 = \$5$). Therefore, the following happens:

$$p_c p_h H < L < p_h H$$

$$50\%10\%\$100 = \$5 < \$9 < 10\%\$100 = \$10$$

Since \$5 is less than \$9, the expected amount for compensation would be insufficient to deter potential offenders. Where suppliers know that probability is less than 100% (in our example, $p_c = 50\%$) and they choose to deviate from the desirable level of care (L = \$9), they must compensate the harm caused (H = \$100), and pay an extra amount as punitive damages, to dissuade adequately this type of behavior. Taking this purpose into consideration, we should calculate a

[14] For simplicity of exposition, we analyze the formula as was exposed originally by Judge Lenard Hand. However, it is necessary to interpret it in marginal terms to be consistent with efficiency objectives (among others, see Salvador Coderch & Castiñeira Paul, 1997).

punitive damage award that makes the *expected total liability* equal to the *expected harm* ($10). So, in our example, the punitive damage award should be $100.

$$\$9 < 50\%10\%(\$100 + \$100) = \$10$$

To determine this magnitude of punitive damages, the traditional EAL theory proclaims that, in these situations, tortfeasors must pay for *the value of the harm caused* (compensatory damages, *C*) multiplied by the *inverse of the probability of being awarded for it* ($1/p_c$).

$$L^* < p_c p_h C \frac{1}{p_c} = p_h H$$

Replacing the variables in the previous mathematical expression with the values of our example, we obtain

$$\$9 < 0{,}50x0{,}10\$100 \frac{1}{0{,}5} = \$10$$

Once the harm ($ 100) occurs, the total responsibility (R_t) that must be effectively paid is the sum of compensatory damages (*C*) and punitive damages (*D*).

$$R_t = \frac{C}{p_c} = C + D$$

$$R_t = \frac{\$100}{0.5} = \$100 + D = \$200$$

In other terms, we obtain the amount of punitive damages (*D*) by subtracting the quantity of the monetary compensation (*C*) from the total responsibility (R_t). That is, in symbols,

$$D = \frac{C}{p_c} - C$$

Taking out the common factor *C*, we get the traditional formula for calculating the amount of punitive damages (*D*) (Cooter, 1982, 1989; Posner, 1992; Polinsky & Shavell, 1997; Cooter & Ulen, 2000).

$$D = C\frac{1-p_c}{p_c} \quad [3]$$

Again, substituting the variables in this equation [3] with the values of our example, we calculate *D* ($100).

$$D = \$100\frac{1-0{,}5}{0{,}5} = \$100$$

Finally, proponents of this traditional EAL theory argue that with this approach the wrongdoers' incentives would be restored properly. This is stated because when replacing the variables of [4] for the values of our example, according to this view, the desired equality would be achieved between the *expected total liability* of the wrongdoers and the *expected harm caused* by them (p_hH): $ 10. This basic traditional formula, however, can be refined to capture other relevant possibilities.[15]

$$L^* < p_c p_h\left(C + C\frac{1-p_c}{p_c}\right) = p_h H \quad [4]$$

$$\$9 < 0{,}50x0{,}10(\$100+\$100) = 0{,}10x\$100 = \$10$$

V. CONCLUSION

Argentina, a developing country in Latin America, is the first and only country with a pure continental-civil law system that successfully overcame the prejudice and suspicion against punitive damages, and that admitted them. Despite the vagueness of the article that incorporates them in the Argentine Consumer Protection Law, the doctrine and jurisprudence have developed a fruitful analysis about this topic, from which we highlight a modern exegesis of the function, admission, and amount of punitive damages. We believe that the Argentine case is a good model for other countries, and studying the traditional EAL theory is useful to understand better the Argentine exegesis and its value to maximize social welfare.

[15] In a previous work, we proposed some improvements in this approach. That research project won the award for the best paper presented at the *Fifteenth Annual Meeting of the Latin American and Iberian Law and Economics Association (ALACDE)* held at the Universidad Pontificia Javeriana, Bogotá, 2011 (IRIGOYEN-TESTA, 2012).

CONFLICT OF INTEREST

The author confirms that this article content has no conflicts of interest.

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