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International Review of Law and Economics 20 (2000) 383–394

International
Review of
Law and
Economics

Deterrence, litigation costs, and the statute of limitations for tort suits

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Received May 1999; received in revised form October 1999

1. Introduction

The conventional justification for a statute of limitations on tort suits (or any other legal claim) is that evidence deteriorates over time, thereby increasing the likelihood of legal error.¹ The optimal statute balances this cost of a longer statute length against the dilution in deterrence that results from a shorter length. In this paper I develop a formal model to show that a finite statute length is optimal even in a world without the possibility of legal error. The trade-off involves only litigation costs and deterrence: while a shorter statute reduces deterrence, it also saves on litigation costs by limiting the number of suits that can be filed.

I examine this trade-off under both strict liability and under negligence, and show that the optimal statute length is (probably) shorter under strict liability than under negligence. Intuitively, the marginal benefit of lengthening the statute is higher under a negligence rule because, by increasing the length of time over which victims can file suit, deterrence is enhanced, which in turn reduces the likelihood that a given injurer will be found negligent. Thus, fewer victims file suits at each point in time because their chances of winning are reduced. As a result, litigation costs fall, which partially offsets the extra litigation costs when the statute is lengthened.

The paper is organized as follows. Section 2 sets up the basic model, Section 3 derives the

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¹ See, e.g., Cooter and Ulen (1988: p. 155), Landes and Posner (1987: p. 307), and Epstein (1986). Despite (or possibly because of) the wide acceptance of this argument, there has been almost no formal analyses of statutes of limitations in the law and economics literature. An exception is Baker and Miceli (2000).

optimal statute of limitations for a strict liability rule, and Section 4 repeats the analysis for a negligence rule. Section 5 then offers some informal evidence in support of the theory based on the enactment of statutes of repose for products liability cases, the emergence of the rule of discovery under negligence law, and differences in the statute of limitations for trespass versus nuisance cases. Finally, Section 6 concludes.

2. The model

The model is based on the one developed by Hylton (1990). Injurers and victims are both risk-neutral, and injurers alone can take care to reduce the likelihood of an accident (i.e., the model is one of unilateral care). For simplicity, the injurer's care choice is dichotomous: either take care or no care. Let q be the probability of an accident if the injurer takes care, and p be the probability if he does not, where $p > q > 0$.

The cost of care for injurers is denoted x , which varies across the population of injurers according to the distribution function $H(x)$. Injurers know their own cost of care, but victims do not observe the costs of individual injurers (though they know the distribution function), nor do they know if an injurer actually took care in a given case. However, I assume that the court can observe whether or not an injurer took care as well as the injurer's cost of care (for purposes of applying a negligence rule) if a case goes to trial.

Victims vary in their (fixed) damages in the event of an accident, denoted D . The distribution function of victims' damages is $F(D)$. At the time they make their care choice, injurers do not know the damage that an individual victim will suffer, but they know the distribution of victim damages. However, the court can observe D after the fact when determining a damage award.

When an accident occurs, if the victim files suit, she incurs litigation costs of c_v , while the injurer incurs litigation costs of c_i . In Hylton's (1990) static model, all victims who find a suit profitable file immediately. Here I allow the possibility that some victims will delay filing suit. For example, some injuries might not be immediately evident or some injurers might avoid immediate detection or identification. To keep the model simple, I abstract from the specific reason for delay and simply treat the length of time after an accident that a victim files suit, denoted t , as a random variable with distribution function $G(t)$. Thus, for example, if the statute of limitations is set at L , then $G(L)$ is the probability that a randomly chosen victim will file suit by time L .²

3. Strict liability

Under strict liability, all victims for whom $D \geq c_v$ and $t \leq L$ will file suit. Thus, if an accident occurs, the probability of a lawsuit is $g(t)[1 - F(c_v)]$ at any t up to L (where

² Alternatively, $G(L)$ can be interpreted as the number of suits filed by L . I assume that t is independent of the victim's damages, D .

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