

**THE PROBLEM OF PAIN:
APPROXIMATING DAMAGES FOR LOSS OF EARNING
CAPACITY¹**

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I. INTRODUCTION

From its beginnings, the economic analysis of tort law has traced the incentive effects of liability on potential wrongdoers who pursue their material advantage.⁴ The economic aim is to remedy the harm that does not fall under contract or property law. The idea is to make the victim “whole again”, and this is achieved through the award of damages as compensation. A *pecuniary loss* is defined as a loss of money or something of monetary value that may be acquired, while the word “indemnity” for damage to the person has been held to include compensation for everything on, about or belonging to the person, as well as all bodily injuries which are proved to be the result of the accident.⁵

The economic theory of compensatory damages relies on the concept of indifference: compensation is perfect when the victim is indifferent to having the injury and the damages, and having neither. The result of this perfect compensation is that the potential victim becomes indifferent as to whether there is no accident or

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⁴ Robert D. Cooter, *Economic Theories of Legal Liability*, 5 J. ECON. PERSP. 11 (Summer 1991); Mitchell Polinsky & Steven Shavell, *A Note On Optimal Fines when Wealth Varies Among Individuals* (National Bureau of Econ. Research Working Paper No. 3232, (1990); David D. Haddock et al., *An Ordinary Economic Rationale for Extraordinary Legal Sanctions*, 78 CAL. L. REV. 1 (1990); William Landes & Richard Posner, *An Economic Theory of Intentional Torts*, 1 INT'L REV. L. & ECON. 127 (1981)

⁵ 58 Am Jur 2d 13-14

an accident with compensation. This concept of perfect compensation may be theoretically explained in a case where injuries are suffered and in which a substitute for a lost good is available in the market. A lost good within the concept of damages litigation may refer to one's earning capacity or some other asset the victim may have lost due to the tort committed. The theory is that when a substitute is available, the market price of the substitute measures the value of the good to the plaintiff. Additionally, the plaintiff is not limited to the pecuniary losses that have occurred, but may also recover damages for future losses that will, in the court's opinion, result from the defendant's wrong.⁶ Accordingly, if potential injurers are liable for perfectly compensatory damages, they will then internalize the external harm caused by accidents, this in turn creates incentives for potential injurers to take efficient precaution. Applying the above framework in the award of actual damages, courts begin with the assumption that compensatory damages substitute (or are exchanged) for those pecuniary losses that resulted from the defendant's wrong.

The recent trend in literature involving the economic analysis of law has turned to the study of societal norms.⁷ The standard of conventional morality provides a basis for arranging and ordering wrongdoing by its seriousness but the former does not attach precise punishments to wrongs. As a result, while courts are able to gauge wrongdoing consistently according to the gravity of the offense, courts are unable to put a price tag on wrongdoing and consequently, attach inconsistent money damages to the same. The result is a steady inconsistency in the court's awards of damages that may not sufficiently approximate the pecuniary loss to the victim. Incidentally, said inconsistent awards may muddle the message conveyed by the courts concerning the seriousness of the wrong.

Our own law on damages has not escaped this same inconsistency prevalent in most jurisdictions. Our courts have more often relied on the exercise of their own discretion in awarding amounts to the victim's heirs that they might consider as "reasonable" under the factual circumstances. For example, although it has been clearly settled that the victim's net earning capacity shall form part of the compensatory damages to be awarded to the victim's heirs and beneficiaries, the determination of the amount of the victim's net earning capacity, as well as the factors to be considered, in light of present-day trends and concerns, has not been so similarly settled with much clarity. Much of the rules concerning the determination of such amount had been laid down by jurisprudence, presently and

⁶ 22 Am Jur 2d 27-28

⁷ Lawrence Lessig, *Social Meaning and Social Norms*, 144 U. Penn. L. Rev. 2181 (1996); Richard H. McAdams, *Cooperation and Conflict: The Economics of Group Status Production and Race Discrimination*, 108 HARV. L. REV. 1003 (1984); Eric A. Posner, *The Regulation of Religious Groups*, 2 LEGAL THEORY 33 (1996)

particularly, the computation proffered in the landmark case of *Villa Rey Transit Inc. v. Court of Appeals*.⁸

The doctrine laid down in *Villa Rey* has been consistently applied by the Supreme Court in determining the amount of compensatory damages, particularly for wrongful death cases.⁹ This paper questions the sufficiency of the formula for computing the loss of the earning capacity as part of the award of compensatory damages to the victim's heirs. It is argued that the current formulation for computing the net earning capacity of the victim ought to be revised as it fails to consider several other factors, which, if included in the formula, would more closely approximate the pecuniary loss to the beneficiaries of the victim. Thus, the main goal of this paper is to arrive at a more equitable computation for the actual pecuniary loss. The first part of the paper gives a brief overview of the history of the Philippine Law on Damages, including jurisprudence before and after the *Villa Rey* ruling. The second part of the paper provides a brief discussion on the economic theory of tort law and damages and concludes with an alternative to address the concerns that are not currently included in the present standards.

II. THE SIGNIFICANCE OF THE LAW ON DAMAGES

At first blush, it would seem that no aspect of the Philippine law on "damages" presents a question controversial enough to justify its use as the subject for a thesis.¹⁰ The importance of the law on damages in every legal system cannot, however be overemphasized. The measure of compensatory damages is of far-reaching importance in every legal system; upon it depends the just compensation for every wrong or breach of contract.¹¹ In fact, it is difficult to imagine litigation that would not, eventually, call for the application of the law on damages. Far from confining its operation to a particular branch of the law, it spreads out and permeates practically every sphere in the legal firmament.¹² In civil law, those who in the performance of their obligations are guilty of fraud, negligence, or delay and those who in any manner contravene the tenor of their obligations, are liable for damages.¹³ In criminal law, indemnification of consequential damages shall include

⁸ 31 SCRA 511 (1970)

⁹ *Davila v. Philippine Airlines* 49 SCRA 497 (1973); *People v. Daniel* 136 SCRA 92 (1985); *Philippine Airlines v. Court of Appeals* 185 SCRA 110 (1990); *People v. Quilaton* 205 SCRA 279 (1992); *Pestano v. Sumayang* 346 SCRA 870 (2000); *Smith Bell Dodwell Shipping Agency Corporation v. Borja* 383 SCRA 341 (2002); *Negros Navigation Co., Inc. v. Court of Appeals* 281 SCRA 534 (2005);

¹⁰ A. Melencio. *A Critical Analysis of the Philippine Law on Damages*, 23 PHIL. L.J. 481 (1948)

¹¹ Report of the Code Commission, 72.

¹² *Supra note 1*, 485

¹³ CIVIL CODE, Art. 1170

not only those caused the injured party, but also those suffered by his family or by a third person by reason of the crime.¹⁴ Even in the realm of commercial law, the owner of a registered mark may recover damages from any person who infringes his rights.¹⁵

Recognizing the importance of the law on damages, the Code Commission deemed it proper to add a separate title on damages in the present Civil Code. To say however, that the present provisions on the law on damages have sufficiently addressed gaps under the Civil Code of 1889, would be difficult to attest to, particularly, in the area of determining the award of compensatory damages.

The present standards for valuing compensatory damages currently adopted by courts offer very little guidance and thus do not always reflect the true costs that the victim incurred and should be compensated for. As society advances into more exacting methods of determining and expanding the scope of protected and compensable interests, so does the need for a legal recognition of an economically sound standard to guide the courts.

III. A BRIEF HISTORY ON THE PHILIPPINE LAW ON DAMAGES

The term “damage” is the loss caused by one person to another, or to his property, either with the design of injuring him, or with negligence and carelessness, or by inevitable accident.¹⁶ The term “damages”, on the other hand, signify the compensation in money for the loss or the damage.¹⁷ The theory upon which the law allows damages for the violation of a civil right is based upon the doctrine that where a civil injury has been sustained, the remedy provided by the law should be commensurate to the injury done.¹⁸ Thus, whether the action be *ex contractu* or *ex delicto*, the end view is the same - that the plaintiff be made whole.¹⁹

The Spanish Civil Code grants this remedy under its Article 1902, which states that *any person who by an act or omission causes damage to another by his fault or negligence shall be liable for damages so done*. In order to give rise to the obligation imposed by this article of the Civil Code, the concurrence of two distinct requisites is necessary:

¹⁴ REV. PEN. CODE, art. 107

¹⁵ INTELLECTUAL PROP. CODE, sec. 154

¹⁶ F. Natividad. *A Comparative Study of the Law of Damages Under the Spanish and the Common Law Systems*. 2 PHIL. L.J. 227 (1916)

¹⁷ 15 Am. Jur., sec. 2, p 388

¹⁸ *Supra* note 8

¹⁹ R. Villaflores. *Deficiencies of the Philippine Law on the Subject of Damages* 7 PHIL. L.J. 331 (1928)

(1) That there exist an injury or damage not originating in acts or omissions of the prejudiced person himself, and its existence be duly proven by the person demanding indemnification therefore; and

(2) That said injury or damage be caused by the fault or negligence of a person other than the sufferer.²⁰

Although the defendant may be made liable for damages for injury caused by his fault or negligence, a limit is placed on his liability in that he may only be made liable for *all actual pecuniary loss or personal injury directly resulting from the wrongful act or omission and which are the natural result of the said act or omission.*²¹ Thus, an injurer may not be held liable for the remote consequences of his act.²² In the same vein, and except when brought under the Employer's Liability Act (Act No. 1874) and the Libel Law (Act No. 277), a defendant may not be held liable for non-pecuniary damages such as those sustained for mental suffering and anguish, mental pride, sense of shame and humiliation and the like.²³

The Spanish Civil Code provisions on damages have been largely criticized as deficient, especially when juxtaposed with common Law principles of damages.²⁴ In *Algarra v. Sandejas*²⁵, the Supreme Court therein had occasion to comment on the status of the law on damages under the Spanish Civil Code:

We are of the opinion that as the Code is so indefinite (even though from necessity) on the subject of damages arising from fault or negligence, *the bench and bar should have access to and avail themselves of those great, underlying principles which have been gradually and conservatively developed and thoroughly tested in Anglo-Saxon courts. A careful and intelligent application of these principles should have a tendency to prevent mistakes in the rulings of the court on the evidence offered, and should assist in determining damages, generally, with some degree of uniformity.* (emphasis supplied)

This deficiency was in fact, recognized in the Report of the Code Commission where it was admitted that *the present Code has but few general principles on the measure of damages.... Moreover, practically the only damages in the present Code are compensatory ones and those agreed upon in a penal clause.*²⁶ The Commission has, therefore, deemed it advisable to include in the revision a Title on "Damages"

²⁰ *Manzanares v. Moreta* 38 SCRA 821 (1918)

²¹ CIVIL CODE (1889), Art. 1101

²² *Supra* note 8, 232

²³ *Supra* note 10.

²⁴ A. Melencio. *A Critical Analysis of the Philippine Law on Damages*, 23 PHIL. L.J. (1948); F. Natividad. *A Comparative Study of the Law of Damages Under the Spanish and the Common Law Systems*. 2 PHIL. L.J. (1916); R. Villaflor. *Deficiencies of the Philippine Law on the Subject of Damages* 7 PHIL. L.J. (1928)

²⁵ 27 Phil. 284 (1914)

²⁶ Report of the Code Commission 72.

which embodies some principles of the American law on the subject.²⁷ Thus, as early as the enactment of the present Civil Code, our jurists have acknowledged the benefit of integrating common law principles into our civil law system owing to the more developed rules in the adjudication of damages in the former.

Under the present Civil Code, *Damages may be: (1) actual or compensatory, (2) moral, (3) nominal, (4) temperate or moderate, (5) liquidated or, (6) exemplary or corrective.*²⁸ The Civil Code further provides that the principles of the general law on damages are hereby adopted insofar as they are not inconsistent with this Code.²⁹

IV. COMPENSATORY DAMAGES UNDER THE NEW CIVIL CODE

Actual or compensatory damages are those awarded in satisfaction of, or in recompense for, loss or injury sustained.³⁰ They proceed from a sense of natural justice and are designed to repair the wrong that has been done, to compensate for the injury inflicted, and not to impose a penalty.³¹ Embodied in Article 2199 of the Civil Code is the general rule that *one is entitled to an adequate compensation only for such pecuniary loss suffered by him as he has duly proved.* Thus, to seek recovery of actual damages, it is necessary to prove the actual amount of loss with a reasonable degree of certainty, premised upon competent proof and on the best evidence obtainable.³² Such evidence may be in the form of receipts,³³ evidencing the actual expenses of the victim's heirs, the victim's income tax return,³⁴ or financial statements of the victim's employer.³⁵

The New Civil Code expressly allows the award of actual damages in any action involving any source of obligation,³⁶ provided the general rule on proof is complied with. In contracts and quasi-contracts, *the damages for which the obligor who acted in good faith is liable for shall be those that are the natural and probable consequences of the breach of the obligation, and which the parties have foreseen or could have reasonably foreseen at the time the obligation was constituted.*³⁷ In *Cariaga v. Laguna Tayabas Bus Co.*,³⁸ the Supreme

²⁷ *Ibid.*

²⁸ CIVIL CODE, Art. 2197

²⁹ CIVIL CODE, Art. 2198

³⁰ A. TOLENTINO, COMMENTS AND JURISPRUDENCE ON THE CIVIL CODE OF THE PHILIPPINES (2002)

³¹ *Ibid.*

³² *People v. Lab-co* 373 SCRA 461 (2002)

³³ *People v. Magalona* 406 SCRA 546 (2003)

³⁴ *People v. Singh* 360 SCRA 404 (2001)

³⁵ *Alcantara v. Surro* 93 SCRA 472 (1953)

³⁶ T. Aquino *Loss of Earning Capacity* 42 SAN BEDA L.J. 28 (2005)

³⁷ CIVIL CODE, Art. 2201

³⁸ 110 Phil 346 (1960)

Court included in the award of compensatory damages, the income that the victim would have earned had he not met with a tragic accident and continued on with his medical studies to become a doctor. Rejecting the defendant's contention that only medical, hospital and other expenses are within the category of "foreseeable or reasonably foreseeable consequences", the Supreme Court held that the income which the victim could earn if he should finish the medical course and pass the board examinations must be deemed to be reasonably foreseeable since, at the time of the accident, the victim was already a 4th year medical student in a reputable university. His scholastic record, which was presented at the trial, justified an assumption that he would have been able to finish his course and pass the board in due time.

On the other hand, in crimes and quasi-delicts, the necessity that such damages have been foreseen or could have been reasonably foreseen by the defendant is dispensed with. Art. 2202 *makes the defendant liable for all damages which are the natural and probable consequences of the act or omission complained of, regardless of whether or not the same could have been reasonably foreseen.* Damages resulting from a tort are measured in the same manner as those due from a contractual debtor in bad faith, since he must answer for such damages whether he had foreseen them or not.³⁹ Additionally, in crimes, the damages to be adjudicated may be respectively increased or lessened according to the aggravating or mitigating circumstances.⁴⁰ However, the law counterbalances the burden of liability upon the defendant by providing that *the contributory negligence of the plaintiff shall reduce the damages he may recover.*⁴¹ Furthermore, the law imposes an obligation on the party suffering loss or injury to exercise the diligence of a good father of a family to minimize the damages resulting from the act or omission in question.⁴²

V. NET EARNING CAPACITY AS A PART OF COMPENSATORY DAMAGES

The Civil Code provides for two instances when the victim's earning capacity is considered in the determination of the award of compensatory damages: (1) in cases of temporary or permanent personal injury⁴³; and (2) in cases of death caused by a crime or quasi-delict.⁴⁴ Although the law clearly mandates that the defendant shall be liable for the loss of the earning capacity of the deceased, the law however is silent on the *manner* of determination of the said award and the *factors* to

³⁹ A. TOLENTINO, COMMENTS AND JURISPRUDENCE ON THE CIVIL CODE OF THE PHILIPPINES (2002)

⁴⁰ CIVIL CODE, Art. 2204

⁴¹ CIVIL CODE, Art. 2214

⁴² CIVIL CODE, Art. 2203 NCC

⁴³ CIVIL CODE, Art. 2205 par. 1

⁴⁴ CIVIL CODE, Art. 2206

be considered in arriving at a precise value. It often happens therefore that apart from questioning the adjudication of the actual merits of a case, the amount of damages awarded by a trial court has always been included as one of the assignments of error by either party-litigant. The debate on the amount of lost earning capacity is largely due to the reality that neither statute nor case law lays down an exacting formula from which the amount may be computed from.

In the early case of *Alcantara v. Surro*,⁴⁵ the salary to which the deceased would have been entitled had he survived the years 1946, 1947, 1948 and 1949 was used to determine the indemnity to be awarded to the heirs of the deceased. The reason for picking out the salary for these particular years as the determinative basis of the award was however not elucidated by the Court. While the Supreme Court therein cited the American Experience Table of Mortality in assessing the remaining life expectancy of the deceased, pegging it at 28.90 years, Supreme Court deigned to use this mortality table and opted to pick an arbitrary figure with which to multiply the base salary with, ratiocinating simply that such course of action was “fair and reasonable”. The Supreme Court even laid down the rule that the *introduction of mortality tables is not absolutely essential to prove the life expectancy of a deceased or his beneficiary, and if introduced they are not conclusive, and the jury are not bound by them*. This reasoning by the Court can in fact be said to have laid the basis for its proclamation that *the determination of the indemnity to be awarded to the heirs of a deceased person has therefore no fixed basis and that much is left to the discretion of the court*.⁴⁶

Subsequent claims for damages brought before the courts followed the same arbitrary manner of determining the value of lost earning capacity. In the aforementioned case of *Cariaga v. Laguna Tayabas Bus Co.*⁴⁷, reference to a monthly salary of P300.00 was made by the Court, but awarded P25,000.00 as compensatory damages, which amount was already inclusive of both medical expenses and loss of earning capacity. In that case, the medical expenses of the victim was in the total sum of P17,719.75, leaving therefore, an amount of P7,280.25 or, the equivalent of only 2 years salary, to stand for damages in the concept of lost earning capacity. In *Mercado v. Lira*⁴⁸, the trial court awarded P18,000.00 for the loss of the earning capacity of the deceased, said award being computed at the rate of P1,800.00 per annum multiplied by 10 years. The same award was reduced by the Court of Appeals, and affirmed by the Supreme Court, to P2,000.00. Again, the reason for the arbitrary figures as well as the decrease in the award for lost earning capacity was not contained in the decision. In *Heirs of Castro v. Bustos*⁴⁹, the loss of the victim’s earning capacity was set at P13,380.00 where the victim was found to have an annual salary of P2,676.00. Said amount would be equivalent to roughly 4 years of the future earnings of the deceased, similar to what the court used in *Alcantara v.*

⁴⁵ 93 Phil. 472 (1953)

⁴⁶ *Ibid.*

⁴⁷ *Supra.* note 35

⁴⁸ 3 SCRA 124 (1961)

⁴⁹ 27 SCRA 327 (1969)

*Surro*⁵⁰. In all these cases, no reason was offered by the courts to support its determination that the remaining life expectancy of the deceased ought to be set at either 2 or 10 years.

The courts cannot be faulted for exercising its discretion and producing estimates of lost earning capacity from out of thin air; the law does not, anyway, impose such a burden upon judges to create standards and factors from which the award may be based. *Much is left to the discretion of the court considering the moral and material damages involved, and so it has been said that 'there can be no exact or uniform rule for measuring the value of a human life and the measure of damages cannot be arrived at by precise mathematical calculation, but the amount recoverable depends on the particular facts and circumstances of each case.'*⁵¹ The wisdom of advertent to the "court's discretion" in determining the amount of lost earning capacity is however put to doubt especially in light of the legal fact that, under the law, the courts are tasked to *assess* the value of the loss of earning capacity, and not to exercise its discretion in arriving at this amount.

VI. AN ATTEMPT AT PRECISION: THE *VILLA REY* TRANSIT FORMULATION

It was not until the early 1970s when the Supreme Court stepped up to lay down an objective formula for determining the loss of earning capacity. In *Villa Rey Transit, Inc. v. Court of Appeals*,⁵² Chief Justice Concepcion set in stone the mathematical formula that would henceforth, guide the bench and bar in arriving at the amount of compensatory damages for the loss of earning capacity. *The determination of such amount depends, mainly upon two (2) factors, namely: (1) the number of years on the basis of which the damages shall be computed and (2) the rate at which the losses sustained by said respondents should be fixed.* In that case, 29-year old Policronio Quintos, Jr. met with a fatal vehicular accident, prompting his only surviving heirs to press for damages against the public transportation company. Included in such claim was an amount for the loss of the victim's earning capacity, which amount is recoverable in favor of the heirs of the deceased. The Supreme Court adverted to two empirical data to formulate the victim's lost earning capacity: (1) computation for remaining life expectancy, which can be determined by applying the formula $[2/3 \times (80 - \text{Age at time of death})]$;⁵³ and (2) computation for the rate of loss to the victim's heirs,

⁵⁰ *Supra* note 42

⁵¹ *Alcantara v. Surro* 93 Phil. 472 (1953)

⁵² *Supra* Note 5

⁵³ Sourced from the American Expectancy Table of Mortality or the Actual Combined Experience Table of Mortality. A table published in 1868 of expected mortality rates, based on data accumulated from twenty American insurance companies. This table was widely used by life insurers until the 1950s to establish rates. The table was superseded by the Commissioners' Standard Ordinary Table.

which can be determined by taking the annual gross salary of the victim and deducting from said salary a reasonable amount for the cost of living expenses of the victim. It was in this case, that the value of a human life, which was once conceded to be incapable of any “uniform rule of determination” in Philippine jurisprudence, was abridged to a simplistic mathematical formula: *life expectancy multiplied by net earnings*.

A. COMPUTING FOR THE REMAINING LIFE EXPECTANCY

The ruling in *Villa Rey* set the standard to be followed for subsequent claims for actual damages brought before the courts. The Supreme Court has however found freedom in reducing or increasing the figures to be used in the formula, depending upon the particular facts and circumstances relating to other factors such as, the victim’s health,⁵⁴ lifestyle,⁵⁵ and as well *as* advances in medical science, improved nutrition, food supply, diet consciousness and health maintenance.⁵⁶ In *Davila v. Philippine Air Lines*,⁵⁷ the Supreme Court reduced the remaining life expectancy of the deceased from 33 years to 25 years, owing to the victim’s medical history of backaches, chest pains and occasional feelings of tiredness. From these set of circumstances, the Supreme Court therein concluded that the victim could not have lived to the ripe old age of 80 because of said health ailments. Similarly, in *People v. Daniel*,⁵⁸ the remaining life expectancy of the victim, a driver of a passenger jeepney, was reduced to 25 years by taking into account the fact that drivers of passenger jeepneys cannot continue the back-breaking pace and unmering nature of their work for those many years, and so concluding that it was reasonable for the remaining life expectancy of the deceased to be less than the ordinary man not engaged in such risk-prone occupation. The case of *People v. Quilaton*⁵⁹ is significant as this was the first time the Supreme Court updated the basis for computing a person’s life expectancy. The Supreme Court therein took notice of the fact that *the formula used in Villa Rey Transit was based on a table derived from actuarial experience prior to 1970 and that actuarial experience subsequent to 1970 has changed, indicating a longer life expectancy in the Philippines due to certain other conditions such as better health maintenance. Said improved conditions was reflected in the 1980 Commissioner’s Standard Ordinary Mortality Table (1980 CSO),⁶⁰ which table was*

⁵⁴ *Davila v. Philippine Airlines* 49 SCRA 497 (1973)

⁵⁵ *Rodriguez-Luna v. Intermediate Appellate Court* 135 SCRA 242 (1985); *People v. Daniel* 136 SCRA 92 (1985)

⁵⁶ *People v. Quilaton* 205 SCRA 279 (1992)

⁵⁷ *Supra* note 44

⁵⁸ 136 SCRA 92 (1985)

⁵⁹ *Supra* note 46

⁶⁰ the generally accepted formula in computing for life expectancy, based on the 1980 CSO table is:

used by the court in arriving at an initial value of 46 years as the remaining life expectancy of the victim. This initial determination of remaining life expectancy was however, similarly reduced to 39 years taking into consideration that the victim was a government employee who is expected to retire at age 65 and reasonably presuming that a man would not normally continue working to earn money up to the final month or year of his life.

From the foregoing cases which were promulgated immediately after the ruling in *Villa Rey* was laid down, it can be seen that the trend with respect to determining the remaining life expectancy is to use an objective table of values in order to arrive at the victim's remaining life expectancy *and then decreasing the said value to make allowance for circumstances which are "deemed reasonable" to the Court.* Thus, although some semblance of objectivity is injected in determining the remaining life expectancy of the deceased, such objectivity is diluted when the court exercises its discretion to vary the figure arrived at for the remaining life expectancy.

The present trend however, is to set a person's life span definitively at eighty (80) years. *A person's demise earlier than the estimated life span is of no moment for purposes of determining loss of earning capacity, life expectancy remains at 80.*⁶¹ Similarly, the age of retirement is no longer factored in to decrease the life expectancy of the victim as *it is assumed that the deceased would have earned income even after retirement from a particular job.*⁶² Life expectancy therefore, should not be based on the retirement age of government employees, which is pegged at 65.⁶³

B. COMPUTING FOR THE RATE OF LOSS

The rate of loss to the victim's heirs has been consistently computed by, determining the gross annual salary of the victim and deducting from the said value *the expenses necessary in the creation of such earnings or income and other living and other incidental expenses.*⁶⁴ The determination of that percentage of the gross income, which is said to form part of the amount necessary to maintain the living expenses of the

$$\frac{S (L_x + 1, L_x + 2, \dots, L_x + n),}{L_x}$$

Where, $n = 100 - x$

$x =$ age upon death

$L =$ number of people in sample surviving after x number of years

⁶¹ *Smith Bell Dodwell Shipping Agency Corporation v. Borja* 383 SCRA 341 (2002)

⁶² *Negros Navigation Co., Inc. v. Court of Appeals*. 281 SCRA 534 (1997)

⁶³ *Supra* note 51

⁶⁴ *People v. Daniel* 136 SCRA 92 (1985)

victim, has however, gone through several variations but has eventually settled at 50% of the gross annual income of the deceased. In the case of *Villa Rey*, an amount of P1,184.00 was deducted from the gross annual salary of the victim of P2,184.00, which amount is roughly at 54.2% of the victim's gross annual salary. In *People v. Teehankee, Jr.*,⁶⁵ the court allowed a deduction of P19,800.00, roughly 42.4% of the deceased's gross annual salary of P46,659.21. In *People v. Myco*,⁶⁶ where the deceased was employed as a farm laborer and earning a monthly salary of P1,600.00, a deduction of P15,360.00 was made from the victim's gross annual salary of P19,200.00, which deduction amounted to almost 80% of the gross annual salary of the victim. The Supreme Court therein however, did not provide any objective basis for pegging the victim's living expenses way over and above the usual 50% value.

C. PRESENT TRENDS IN COMPUTING LOSS OF EARNING CAPACITY

At present, not much departure has been made from the formula laid down in *Villa Rey*. Thirty-six years after the said decision was promulgated, our courts have still relied on the two-factor formula of life expectancy and net earning capacity, with but minor, if not, insignificant changes. Thus, the civil indemnity for death has now been increased from the statutory value of P3,000.00⁶⁷ to P50,000.00⁶⁸. While damages in the form of lost earning capacity of the deceased is a mandatory award, the same is now considered as in the nature of actual damages which must therefore comply with the general rule under Article 2199, subject only to very limited exceptions. Thus, in *Nueva Espana v. People of the Philippines*,⁶⁹ the Supreme Court denied the claims of P2,997,000.00 and P1,728,000.00 by the heirs of the victims, Reynard So and Nilo Castro, respectively, for lost of earning capacity on the ground that the values claimed were not substantiated by documentary evidence but were merely proved through the testimonies of the respective heirs. Citing *People v. Mallari*⁷⁰, the Supreme Court held that *the rule is that documentary evidence should be presented to substantiate a claim for loss of earning capacity*. The Supreme Court has however, excepted to this rule of documentary proof, instances where there is testimony that the victim was either (1) self-employed, earning less than the minimum wage under current labor laws, and judicial notice is taken of the fact that in the victim's line of work, no documentary evidence is available; or (2) employed as a daily-wage worker earning less than the minimum wage under current labor

⁶⁵ 249 SCRA 54 (1995)

⁶⁶ 331 SCRA 192 (2000)

⁶⁷ Civil Code, art. 2206

⁶⁸ *Pestano v. Sumayang* 346 SCRA 870 (2000)

⁶⁹ 460 SCRA 547 (2005)

⁷⁰ 404 SCRA170 (2000)

laws.⁷¹ Thus, in *People v. Perreras*,⁷² the Supreme Court allowed the heirs of the deceased to recover damages for loss of earning capacity notwithstanding the fact that the prosecution did not present documentary evidence to support this claim. The Court therein relied on the un rebutted testimony of the deceased's widow who established that her husband died at the age of 50 and earned a basic salary of P130.00 a day.

The rule on requiring documentary evidence to prove loss of earning capacity has been criticized to misinterpret "loss of earning capacity" to mean "loss of earnings"⁷³ *The insistence on documentary evidence is a manifestation of adherence to the theory that only lost earnings can be recovered; if proof of the amount of actual income is deemed indispensable, then the other face of the damage [the power to earn] is being disregarded.*⁷⁴ Nevertheless, the Supreme Court has held that in cases where the heirs of the victim failed to prove their claim for actual damages, but have shown that they have suffered pecuniary loss by reason of the death of victim, an award of P25,000.00 by way of temperate damages is justified in lieu of an award of actual or compensatory damages.⁷⁵

The award for lost earnings as part of damages is also computed on the basis of the life expectancy of the deceased and not those of the heirs or the deceased's beneficiaries. In *Pestano v. Sumayang*,⁷⁶ the petitioner therein assigned as error for the lower court to have used, as basis for the computation of the loss of earning capacity of the deceased, the life expectancy of the deceased instead of that of the respondent-beneficiaries, which value was shorter than the life expectancy of the deceased. The Supreme Court however, rejected this argument reasoning that the life expectancy variable in computing for lost earning capacity has been consistently computed based on the life expectancy of the deceased and not on that of the heir.

VII. AN ECONOMIC THEORY OF DAMAGES: THE GOAL OF PERFECT COMPENSATION

In economic models of liability, "perfect compensation" leaves the victim indifferent between no harm and harm with compensation.⁷⁷ In other words,

⁷¹ *People v. Oco* 412 SCRA 190 (2003)

⁷² 362 SCRA 202 (2001)

⁷³ T. Aquino. *Loss of Earning Capacity* 42 San Beda L.J. (2005)

⁷⁴ *Ibid.*

⁷⁵ *People v. Duban* 412 SCRA 131 (2003); *People v. Quimzon* 427 SCRA 261 (2004); *Nueva Espana v. People of the Philippines* 460 SCRA 547 (2005)

⁷⁶ 346 SCRA 870 (2000)

⁷⁷ ROBERT COOTER & THOMAS ULEN, *LAW AND ECONOMICS*, 297-298, 363-65, 444-48 (1996).

perfect compensation restores the victim to the same indifference curve as if no injury had occurred. A liability system with perfect compensation would make victims indifferent about the behavior of injurers. If victims are indifferent, then injurers should be free to decide how to act.

There are however important theoretical reasons why fully informed persons in a voluntary market might wish to limit the total amount of damages that are recoverable after an occurrence of any accident. The fact is that bodily injury makes the victim worse off in two ways. First, it lowers his effective income by reducing his earning power and imposing costs. Second, it lowers the value to him of any given income by eliminating the ways in which he can spend it⁷⁸. Death is the extreme case; not only does it lower the victim's income to zero, it simultaneously reduces to zero the benefit he can get by spending any form of income—including damage payments. One thing this argument suggests is that “full compensation” — a level of payment for damages that restores the victim to the level of welfare he had before the injury, is in a sense inefficient.⁷⁹ The inefficiency arises because, if given a choice, the injured party would rather have received money prior to an accident that he could have spent on other consumer items in his uninjured state.⁸⁰ Accordingly, the suggestion is that the law should permit any person to sell insurance on his life, that is, to receive payments for today in exchange for selling to other persons the right to collect damages in the event of death at some future time.⁸¹ The sale of the insurance provides the seller with income at the time when its value is greatest. Simultaneously, placing the tort claim in the hands of the buyer preserves the deterrent effect of the tort law on the injurer. The typical majority of cases involve the specification of an award that is designed to make some allowance for pain and suffering, medical care, and lost earnings, yet there is no pretense of the possibility that the victim can be left with as “rich” and “full” a life after injury as was enjoyed before it.

A. THE HAND RULE

The economic objective of a tort system is to maximize total social utility with the most efficient allocation of resources, and the condition for achieving this optimally efficient state is for the expected marginal costs of an accident to equal the marginal cost of the care taken to avoid an accident. Given a case of simple

⁷⁸ Posner, Richard, *A Theory of Negligence*, 1 J. LEGAL STUD. 29 (1979)

⁷⁹ Thomas Friedman, *What is 'Fair Compensation' For Death or Injury?* 2 INT'L REV. OF L. & ECON. 81, 82 (1982)

⁸⁰ Epstein, R., *Causation and Corrective Justice, A Reply to Two Critics* 8 J. LEGAL STUD. 477 (1979) 570

⁸¹ Calabresi and Hirschoff, *Toward a Test of Strict Liability in Torts*, 81 YALE L.J. 1055 91972) 706

negligence where only one party is at fault, the traditional approach in setting up incentives for precaution is to measure the loss borne by the injured party (plaintiff) and to allocate this amount to the injurer (defendant)⁸². The solution is to have the injurer internalize the cost and remove the distortions to economic efficiency that result from the true social cost not being used in the allocation of resources⁸³.

This legal standard for precaution was enshrined in the case of *United States v. Carroll Towing Co.*⁸⁴ where Justice Learned Hand found the barge owner negligent in not having his attendant on board, the presence of whom could have avoided the sinking of the barge. As the cost of having the attendant was less than the probability of the accident happening *multiplied* by the value of the risk, the barge owner should have taken more precaution, and in failing to do so, should consequently shoulder the cost of the damage.

In terms of neoclassical economics, the marginal Hand Rule states that the injurer is *negligent* if the marginal cost of his or her precaution (*Burden = B*) is less than the resulting marginal benefit (*Probability × Liability = PL*).

$$B < PL$$

The injurer is held liable under the Hand Rule *when further precaution is cost-justified*. The necessity for further precaution is justified when the given precaution falls short of the efficient level. To escape liability under Hand's rule, the injurer must increase precaution until the inequality becomes an equality.

$$B = PL$$

$$\text{marginal social cost} = \text{marginal social benefit}$$

In an ideal system where social welfare is maximized, the total of all individual's utility together will be as large as possible. Under this setting, economic efficiency requires that all the incentives together produce the amount of precautionary behavior. It appears therefore that under the Hand Rule, it is more straightforward to deal with only the *costs* (or what other economists would label as the "wealth" factor) and the resulting linear utility of cost (wealth) function is *assumed* to be the same (linear) for *both* the injurer and victim. The only task left under these assumptions is to consistently and accurately measure the costs borne by the victim (or his loss of wealth).

As applied to the computation of actual compensatory damages:

⁸² *Supra* Note 75, p. 201 ; *See* ANNEX

⁸³ *Supra* Note 5, p. 357

⁸⁴ 159 F. 2d 169 (2d Cir. 1947)

- When a substitute is available, the market price of the substitute measures the value of the good to the plaintiff.
- In cases where there are no substitutes, the assumption is that if the expenditures on precaution are rational, then the reduction in the probability of a fatal incident, multiplied by the value of the fatal risk equals the marginal cost of care:

$$(\text{probability of accident})(\text{value of fatal risk}) = \text{amount spent on precaution}$$

or

Value of Fatal Risk	=	Amount spent on precaution
		Probability of accident

The computation assumes that the regulator/court takes actual market purchases as guide to how much the purchaser values safety. Efficiency requires taking additional precaution until the burden (B) equals the change in probability (p) multiplied by the loss (L), or $B = pL$. Forensic economists argue that repeated application of the Hand Rule enables adjudicators to discover the efficient level of cause.⁸⁵ In trying a case, the court should determine whether further precaution was cost-justified. If the answer is yes, then the injurer has not satisfied the legal standard and the injurer is liable to pay damages. The presumption is that injurers will respond to this decision by increasing their level of precaution, and eventually, a case will reach the courts in which further precaution is not cost justified.

B. ANALYSIS OF THE *VILLA REY* FORMULATION

In the case of *Villa Rey*, the Supreme Court determined probably net earning capacity in accordance with the following formula:

⁸⁵ W. LANDES AND R. POSNER, *THE ECONOMIC STRUCTURE OF TORT LAW* (1987), p. 204

$$\textit{Probable Earning Capacity} = \frac{\textit{Remaining Life Expectancy}}{\textit{Life Expectancy}} \times \textit{(Projected Gross Annual Income)} - \textit{(Estimated Yearly Expenses)}$$

In the above formulation, the remaining life expectancy is equivalent to 2/3 multiplied by the difference of 80 and the age of the victim at the time of his/her death. In recent years, the Court has set estimated yearly living expenses to be 50% of annual income.⁸⁶ It is argued that above formulation however may not always lead to a realistic approximation of the lost income stream of the victim, considering the following factors:

1. The possibility that the lump sum amount to be paid by the plaintiff may in fact result to overcompensation.
2. The possibility of increases in victim's projected gross income.
3. The current formula does not take into account inflation and income taxes.
4. There are actuarial probabilities that the victim will still be able to work beyond his retirement age if the accident did not happen or may cease working even before he reaches his retirement age.

1. Lump-sum Award may result to Overcompensation

It is quite ironic that in the very same case where the mathematical formula for computing loss of earning capacity was first laid down, we also find one of the first few arguments against the inadequacy of the said computation. In the case of *Villa Rey*, the counsel for the petitioner bus company appealed rate at which the damages to be computed was set, arguing that the damages to be awarded would have to be paid *now* (i.e. upon finality of the decision) *whereas most of those sought to be indemnified will be suffered years later*. The counsel for the bus company was apparently arguing for the allowance of computing the present value of the future loss, which is defined as that amount which, if invested safely, would eventually grow into an amount equal to the lost income stream of the victim.⁸⁷ This argument by the

⁸⁶ Metro Manila Transit Corporation v. Court of Appeals GR 11617, November 1999).

⁸⁷ POSNER, RICHARD. ECONOMIC ANALYSIS OF LAW (1986)

counsel for the bus company seem to be economically sound especially when we consider the fact that the current method of computation may overcompensate the victim or his heirs, because if they invest the lump-sum awarded to them, they would, in addition thereto, derive interest income thereon, which would not be the case had the amount been received periodically in the form of salaries.

In rejecting this argument, the Supreme Court held that, although payment of the award will have to take place upon finality of the decision, the liability of defendant bus company is offset by the fact that the potentiality and capacity to increase one's earning capacity was not taken into consideration in arriving at the loss earning capacity, unlike in the case of *Alcantara v. Surro* where such potentiality was given due consideration. The Supreme Court however failed to realize that one did not necessarily offset the other as, in fact, both factors ought to be taken into consideration in arriving at the amount of lost earning capacity, if said amount is desired to be as proximate as possible to the actual earning capacity of the deceased. It is also noteworthy to add that although Commonwealth Act 284 was already repealed by our present law on damages, it was then provided that the *civil liability for the death of a person shall be fixed by the competent court at a reasonable sum, upon consideration of the pecuniary situation of the party liable*. The policy for the law then may just as well stand true at present, where the law endeavors to balance the conflicting claims of the parties, with the end goal of giving what is just and equitable to the claimants and preventing the economic hemorrhaging of the party liable.

Furthermore, since a decedent's future earnings would have been subject to income taxes if he had lived, it is argued that the amount available for those entitled to support from him would have been *after taxes*. Therefore unless the awards of compensatory damages take income taxes into consideration, the beneficiaries would accordingly be receiving *more* than they would have, had the deceased lived.

2. Increases in Projected Net Earnings

It is important to take into account possible changes in the projected gross annual income of the victim, as it serves as the basis of determining the major stages of his career. Individuals' incomes tend to increase for two reasons: either the monetary value changes because price levels change or real growth occurs due primarily to changes in productivity of the individual⁸⁸. These changes should be

⁸⁸ Leigh, J. Paul, "Compensating Wages, Value of a Statistical Life, and Inter-Industry Differentials", J. ECON. & MGMT. 28(1), p. 83

accounted for in any estimate, since for most people, lifetime real income first increases, then decreases at retirement.⁸⁹

In nearly all occupations, a worker can expect to receive salary increases from time to time, whether due to his individual characteristics or because of societal factors. Income reported is not the sole consideration as there are additions and deductions that must be first made to the prospective earning figures. Some of these include fringe benefits that are lost to the remaining family members and should be added to the loss suffered by that family⁹⁰.

The path of future earnings may be estimated with a much greater precision by using *age earnings profiles* as it trends national earnings growth, with respect to a group of individuals who are similarly situated⁹¹. A forecast of profiles will show that earnings over the course of time will continue to rise until earnings reach a plateau towards the end of the working life. The adoption of an age earnings profile is economically sound as it reflects the positive effect of additional training and experience on productivity, and therefore earnings, and the fact that training is concentrated relatively early in the work life-cycle.

3. Inflation

Another factor which, is not included in computing for the loss of earning capacity of the deceased, is that of interest, that should be awarded in view of the reality of inflation. In common law jurisdictions, the rule is now well settled that a court, in determining whether an award of damages for personal injuries is proper, can consider the changes in the cost of living or, in its alternative expression, in the purchasing power of money.⁹² The basis of this rule is that compensation means compensation in money, and the value of money lies not in its intrinsic worth but in what it will buy.⁹³

Article 2211 of the Civil Code provides that *in crimes and quasi-delicts, interest as a part of the damages may, in a proper case, be adjudicated in the discretion of the court.* Although the law expressly provides for the award of interest, said provision

⁸⁹ Ziliak, James P. "Does the Choice of Consumption Measure Matter? An Application to the Permanent-Income Hypothesis," J. MONETARY ECON., February 1998, 41(1), pp. 201-216

⁹⁰ *Supra* note 27, p. 97

⁹¹ Kniesner, Thomas J., W. Kip Viscusi, W. Kip, and James P. Ziliak, *Life-Cycle Consumption and the Age-Adjusted Value of Life*, National Bureau of Economic Research (Cambridge, MA), Working Paper No. 10266, January 2004

⁹² 22 Am. Jur. *Damages*, 125 (1965)

⁹³ *Ibid.*

however, appears to suffer from a “triple uncertainty”⁹⁴ whereas inflation, as represented by an award of interest, is an absolute reality especially in a jurisdiction where litigation extends to an indefinite period of time. Thus, on top of being merely a permissive award, interest, as part of actual damages may further be diluted at the court’s discretion and even altogether, disallowed, if not found to be a proper case. In *Philippine Airlines Inc v. Court of Appeals*, the Supreme Court acknowledged the effect of inflation in depleting the value of the judgment in favor of the claimant, where litigation has dragged on for thirty years. In this case, the court allowed payment of interest at the legal rate from the date of judgment until fully paid.⁹⁵ However, in the later case of *Negros Navigation v. Court of Appeals*⁹⁶, where litigation of the claim of respondent’s damages spanned a total of seventeen years, the Supreme Court disallowed the award for interest on the judgment award without explanation.

4. The Effect of Taxes

The 1997 National Internal Revenue Code of the Philippines excludes from gross income damage awards received in compensation for personal injuries, even when they are substitutes for loss income⁹⁷. Hence damages for violation of personal or family rights, damages for slander and libel, award for loss of life, and damages for injuries are not taxable⁹⁸. The theory is that recoupment on account of such loss is not income, since it is not derived from capital, from labor or from both combined and, the fact that the payment of such loss was voluntary does not change its exempt status.⁹⁹ However, in the litigation of cases involving wrongful death, other jurisdictions have supported the view that in the fixing of damages, income taxes should be factored in the formula because a decedent would have never received the amount withheld as income taxes if he had survived¹⁰⁰. The

⁹⁴ “triple uncertainty” embodied in the fact that interest may be awarded in the proper case upon the court’s discretion.

⁹⁵ 185 SCRA 110 (1990)

⁹⁶ 281 SCRA 534 (1997)

⁹⁷ Exclusions from Gross Income - Section 32(B)(4) Compensation for Injuries or Sickness - *Amounts received, through Accidental or Health Insurance or under Workmen’s Compensation Acts, as compensation for personal injuries or sickness, plus the amounts of any damages received, whether by suit or agreement, on account of such injuries or sickness.*

⁹⁸ McDonald, Lyde 9 BTA 1340; *Farmers and Merchant’s Bank of Carlettsburg v. Commissioner*, 59 Fed. (2d) 912

⁹⁹ MAMALATEO, VICTORINO C. PHILIPPINE INCOME TAX FIRST EDITION (2004)

¹⁰⁰ O’Connor v United States (1959, CA2 NY) 269 F2d 578, Huddell v Levin (1975, DC NJ) 395 F Supp 64, where the US courts held that in computing damages for wrongful death under the Federal Tort Claims Act, which limits compensation to recovery of losses sustained, income taxes should be deducted from the decedent’s total salary before computing that part of his earnings which would reasonably be expected to go to his beneficiaries.

victim's heirs would thus be overcompensated should taxes on the income of the deceased not be factored in the computation of his net earning capacity.

Arguably, future taxes have been held to be too uncertain to admit of advanced computation, it would be unrealistic to suppose that at any time within the life expectancy of the victim, either the discontinuance or substantial reduction of income taxes would occur, such that any estimate based on *current rates* should prove to be unreliable¹⁰¹. The incidence of future income taxes is no more guesswork and no more difficult of exact calculation than possible future advancement, wage increases, and inflation that are taken into account in calculating future income.

5. Life Expectancy vis-à-vis Employment

It is uncertain whether the victim would be able to continue his employment until retirement assuming that the mishap did not occur. For example, he might be killed or disabled as a result of other causes and not be able to work even before he reaches his age of retirement. Similarly, there likewise exists an actuarial probability that the victim would still be able to work constantly even beyond his day of retirement. Given the complexity of trying to make an exact calculation, litigants frequently follow the relatively simple course of assuming that the victim would have continued to work up to a specific fate certain.

It is argued however that the stream of future earnings should be adjusted to take into account of the changing probability of employment over a claimant's working life as the number of years a person would have worked if the injury had not occurred must be measured in relation to the *industry* where he belonged and the *nature* of his work¹⁰². The resulting value is not simply the number of years until the victim would have reached statutory retirement ages since - some individuals leave and re-enter the labor market, some individuals leave before, or work beyond, the statutory retirement age and some people die before their retirement¹⁰³.

The foregoing economic factors call for a re-evaluation of the formula, as the court should adopt a method for calculating the amount of compensation for loss of earning capacity other than by simply multiplying the remaining life expectancy of the victim with his hypothetical net yearly earnings. It is suggested

¹⁰¹ Mosley v United States (1976, CA4 NC) 538 F2d 555

¹⁰² Sunstein, Cass R. *Are Poor People Worth Less Than Rich People? Disaggregating the Value of Statistical Lives*, AEI Brookings Joint Center for Regulatory Studies (Washington, DC), Working Paper No. 04-05, January 2004

¹⁰³ Frank, Robert H., and Cass R. Sunstein, "Cost-Benefit Analysis and Relative Position," U. CHICAGO L. REV., Spring 2001, 68(2), pp. 323-374

that the Supreme Court is aware of such additional factors, which may be considered to be reasonably necessary in order to arrive at a precise and proximate value for lost earning capacity. The reluctance and/or inconsistency of the courts in applying these factors, despite the proven reality of the same, denies, not only the just compensation due to the victim's heirs but also the rightful amount that should be shouldered by the party liable. The next section presents an alternative to address this concern.

C. PROPOSED REVISION OF THE VILLA REY FORMULA

A common practice in tort actions involving wrongful death is to reduce the amount of the decedent's lost earnings by the amount of his personal consumption. Additionally, from an economic perspective, part of the loss experienced by society from an individual's death is the loss of utility derived from *all* items purchased with the decedent's earnings.¹⁰⁴ The process of discounting future income streams can be justified by a single proposition – a peso today is more than a peso next year. If a person is in possession of the peso at the present time, he will be able at the end of the year, to enjoy both the peso and the interest earned on it. If he gets the peso at the year, the interest on it will benefit the person who has had the use of the peso in the intermediate period. The value of that one year's use of the peso is a function of the going rate of interest for the use of money. As interest rate increases, the demand for immediate cash, relative to future payments, increases as well.

The Villa Rey formulation may be revised to arrive at a realistic approximation of the lost income stream of the victim. One formula, addresses the concern for overcompensation,¹⁰⁵ to wit:

$$D = \sum_{n=1}^N d_n \quad \text{Where } d_n = \text{the present value of } p_n e_n$$

• **D** is the amount of damages for loss of earning capacity that should be awarded to the victim or his heirs. Considering the factor of increases in projected

¹⁰⁴ Posner, Richard, *Epstein's Tort Theory: A Critique*, J. LEGAL STUD. 457 (1979), 569

¹⁰⁵ Goco, J. *Damages for Loss of Earning Capacity*, THE LAWYERS REVIEW, November 30, 1999, p. 8-11

income, D will be taken as the *sum* of the compensation for loss of earning capacity of the victim for each major stage of his employable life as determined by substantial increases in his salary for each year thereof.

- N is the number of each of these major phases. d_n is the present value of $p_n e_n$ ¹⁰⁶

- P_n is the actuarial probability that the victim would still be able to work for the n^{th} major stage following the accident.

- E_n is the victim's corresponding projected net earnings for that major phase, which is equal to his gross annual income (less personal exemptions), less income taxes and yearly living expenses multiplied by the number of years in such major stage.

To test our hypothesis, we present the following problem:

Suppose a young male lawyer, an associate working in a large prestigious law firm with a prospect of becoming a partner, dies as a result of an accident. At the time of his death, he was only 26, single and had gross annual income of about six hundred thousand pesos (P600000). The table below summarizes the respective positions and salary grade of the firm in which he belongs to.

Age	Position	Gross Annual Income
25-30	Associate	600000
31-39	Senior Associate	896245
40-65	Partner	2500000

Solution 1: Applying the formula given in the case of *Villa Rey*:

$$[2/3 (80-26)] \times [600000-0.5(600000)]$$

$$36 \times 300000 = \mathbf{10,800,000}$$

¹⁰⁶ $A = S / (1 + i)^n$ where A is the principal amount, S is the accumulated amount and i is the interest rate

Under the present standard, he should receive **P10,800,000** as actual damages for loss of earning capacity.

Solution 2: Alternative Formula – Discounting to Present Value

Given the proposed formulation, we first determine the corresponding income tax that is to be paid by the individual at the different stages of his career.

Position	Gross Annual Income¹⁰⁷	Income Tax¹⁰⁸	Gross Annual Income after Tax
Associate	580000	150600	429400
Senior Associate	876245	245398	630847
Partner	2480000	758600	1721400

We next determine the **Hypothetical Net Yearly Earnings** of the victim. Unlike the Villa Rey formulation that pegs the value of expenses at 50% of Gross Annual Expenses, we assume that the counsel for the victim's heirs is given the opportunity (and is in fact able) to prove that his expenses are in fact 40% of his Gross Income After Tax.

$$\text{Hypothetical Net Year Earnings} = 60\% \text{ of } (\text{Gross Income After Tax})$$

ge	Gross Annual Income after Tax	Hypothetical Net Year Earnings
-----------	--------------------------------------	---------------------------------------

¹⁰⁷ Less Personal Exemption of P20,000

¹⁰⁸ P125,000 + 32% of the amount over P500000

5-30	429400	171760
1-39	630847	252339
0-65	1721400	688560

We then multiply the Hypothetical Net Year Earnings by the number of years spent in a position (career level) to obtain his Projected Net Earnings for Each Major Phase of his career (E_n). In the lawyer's case, from an Associate, to Senior Associate and finally, as a Partner. Note that we use this ability-to-work probability instead of the probability that the individual would be in the labor force because the former more closely matches the legal definition of earning capacity.

Age	Position	No. of years	Hypothetical Net Year Earnings	Projected Earnings for Each Major Phase
25-30	Associate	5	171760	858800
31-39	Senior Associate	10	252339	2523386
40-65	Partner	25	688560	17214000

The Projected Earnings for Each Major Phase is then multiplied by the victim's corresponding probability of survival (P_n) based on the Commissioner's Standard Ordinary Table of Mortality¹⁰⁹.

Position	Projected Earnings for Each Major Phase	Probability of Survival	$P_n E_n$
Associate	858800	.99	808948

¹⁰⁹ *Supra* Note 56

Senior Associate	2523386	.98	2352897
Partner	17214000	.88	11812182

Finally, we find summation of the Present Values of $p_n e_n$ to arrive at the amount to be awarded (**D**). In finding the present value of the lost income stream, the interest to be chosen should only reflect the *opportunity cost* of the use of money which is between 1% and 3%¹¹⁰. For this example, we use the conservative estimate of 1%.

Age	$p_n e_n$	Form ula	Prese nt Values
Associate	8 08948	$A=S/(1+0.01)^5$	769686
Senior Associate	2 352897	$A=S/(1+0.01)^{10}$	213004 7
Partner	1 1812182	$A=S/(1+0.01)^{25}$	921076 7
TOTAL			P12,110,500

Under the revised formula, the victim should receive **P12,110,500** for the loss of his earning capacity

As can be observed, the amount to be awarded under the present formulation is *larger* than that arrived at using the formulation in Villa Rey. This may not always be the case as there are differences in variables and underlying assumptions. It is argued however that the above formula and resulting value more closely approximate the pecuniary loss to the beneficiaries of the victim – as the factors of tax, allowance for proving the amount of fixed expenses, increases in

¹¹⁰ *Supra* Note 84, p. 180

projected income and present value of the award is taken into consideration. By applying the above formula, the undeniable obsolescence of the Villa Rey computation becomes even more striking. The inevitability of the revision of the formula laid down in Villa Rey thus becomes imperative upon the courts if actual pecuniary compensation is sought to be achieved.

VIII. CONCLUSION

One must concede that unlimited judicial discretion in the fixing of damages may invite extreme results that may jar one's statutory sensibilities. We need not, and indeed cannot, draw mathematical bright lines between the statutorily acceptable and the statutorily unacceptable that would fit every case. We can say however that general concerns of reasonableness and adequate guidelines should direct the court when engaging in any computation.

The alternative formula for computing lost earning capacity is undeniably, of common law origin. The rise of a new discipline in forensic economics in most common law jurisdictions has aided courts in more accurately computing for the actual pecuniary loss to those left behind by the unfortunate victim and has in fact, created much progress in the law on damages in their jurisdiction. The adoption of such a formulation cannot immediately be said to be anathema to our own law on damages that is in fact, of civil law origin. As early as the enactment of the present Civil Code, our jurists have admitted to the more advanced state of the law on damages in American jurisdictions and has not hesitated to incorporate some American principles into our own law on damages. A similar adoption of their formula for computing lost earning capacity for purposes of determining the award of compensatory damages may prove to be beneficial to the development of our own system of awarding damages.

Theories on efficiency seem like they could work as comprehensive theories of tort law. The idea of mathematical precision suggests the availability of a correct economic answer for each tort case. The problem however is that this "precision" is somewhat deceptive. An efficiency theory will actually be precise only if it assigns a specific monetary value to each element of the cost benefit calculus. The theory must be able to say in each case how much human time, human attention, human suffering and human life are worth. Such valuations can be quite controversial. While most might agree that there is a limit to the amount that the court should award to compensate for a human life, it is unlikely that society can reach any agreement as to what, in monetary terms, that amount might be. So long as the cost benefit formula cannot be turned into a *real* mathematical calculus, theorists can only speculate as to what efficiency requires, and so long as there remain ambiguities in the worth of human time, attention and injury, no calculation will be possible in the vast majority of cases. This limitation must not however,

deter the courts from continuously seeking and adopting the most efficient computation that will best approximate the victim's heirs' actual pecuniary loss. For as long as there exists a better means to mathematically ascertain the accurate value of a human life, our courts must not shy away from incorporating societal and economic factors in the determination of the award of actual damages.