

ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILE 8672
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incentive for the insurer to keep its rates down in hopes that the consumer advocate will not intervene.

The New Jersey statute creating such a system is attached as Exhibit L.

7. Prohibit the pass-through of lobbying expenses

Like other industries, the insurance industry engages in expensive lobbying and public relations campaigns on controversial issues. For example, since December, 1984 the industry has been engaged in a "massive effort to market the idea that there is something wrong with the civil justice system in the United States," as the Insurance Information Institute has put it. ^{14/} And in January of this year, the industry embarked on a \$6.5 million advertising campaign designed, again in the III's words, to "change the widely-held perception that there is an insurance crisis to a perception of a lawsuit crisis." ^{15/}

While insurance companies clearly have the right to seek to manipulate public opinion, whether they have the right to charge their policyholders for the cost of such manipulation is less clear. To ensure that the insurance industry does not charge its policyholders for lobbying/public relation efforts that many of those policyholders may not agree with, may be adversely affected by, and may believe to be false and misleading, states should enact legislation prohibiting the

^{14/} National Underwriter, December 21, 1984, at 2.

^{15/} Journal of Commerce, March 19, 1986, at 1, 20.

insurance commissioner from approving any rate increase to the extent that it includes expenses for public relations and lobbying. Under such statutes, insurance companies' first amendment rights to conduct expensive lobbying and public relations campaigns -- even false and misleading ones -- would be preserved; their policyholders would simply not have to pay for them.

Passing through the cost of lobbying and public relations to consumers is a particularly stark example of a larger problem: insurers blanketly passing through to policyholders all their expenses, rather than allocating those expenses by type of expense and by state. Policyholders thus end up paying for expenditures -- from charitable contributions to executive compensation -- that should more appropriately be borne by stockholders, and policyholders in low expense states end up subsidizing policyholders in high expense states.

Recently, the Supreme Court of Oklahoma ruled that insurance companies must provide "detailed evidence" of their expenses when seeking rate increases. 16/ If other states follow this decision, or legislatures codify it, rates should fall somewhat - perhaps substantially - and should more accurately reflect insurers' activities in each state.

16/ State of Oklahoma v. Oklahoma State Board for Property & Casualty Rates, No. 65,430, slip. op. at 13 (Oklahoma Supreme Court, decided July 24, 1986).

D. Require risk management

Many insurance buyers have not established risk management programs - i.e., they have not set up procedures intended to eliminate, to the greatest extent possible, dangerous aspects of their operation. Perversely, insurance companies and agents also have limited incentives to encourage insurance buyers to set up risk management programs, since the greater the risk the greater the premium, and thus the greater the profit to both the company and the agent, whose profits are calculated as a percentage of the premium.

However, states can pass laws requiring insurance purchasers and self insureds to set up risk management programs. For example, hazardous waste insurers wrote even bad risks at very low rates in the early 1980's, and refused to write even good risks - at any price - during the last year or so. However, if insurers try to control risk through careful, ongoing risk monitoring and control, rather than merely collecting and investing premiums and paying out claims, insurers can make money by writing even hazardous waste insurance.

Elevator and boiler and machinery insurance provides an instructive analogy. In their infancy, elevators and boilers were both quite dangerous, since elevator cables could break and boilers could explode. Insurers, however, insisted that those risks be managed - for example, that cables be strengthened and that boilers be monitored - before agreeing

to write elevator or boiler and machinery insurance. As a result, elevator and boiler accidents are today virtually unheard of. Insurers should spend more of their premium dollar on engineering, and insist that risks seeking hazardous waste insurance first obtain an "environmental audit" and take steps to minimize both the possibility that hazardous substances will be released and the extent of the harm should any such release occur. In that way insurers can both make money and encourage a safer environment.

A bill requiring municipalities which self-insure to set up risk management programs is attached as Exhibit M.

E. Allocate medical malpractice insurance costs more equitably

The problem with medical malpractice insurance is not its total cost -- \$3.4 billion ^{17/} or 8/10 of 1% of the \$425 billion ^{18/} spent on medical care in 1985 -- but its allocation.

The costs of the system are misallocated in four major ways. First, doctors in high-risk specialties pay for risk that should be shared by others. The medical profession may be viewed as a pyramid, with a base of thousands of general practitioners and an apex of relatively few high-risk specialists. The patient is pushed up the pyramid as his

^{17/} Best's Insurance Management Reports, Insurance Premium Distribution - 1985, Release No. 22, July 21, 1986.

^{18/} The Washington Post, July 30, 1986, at 6.

case and its treatment become more complex. As the case gets more difficult and slight error more devastating, fewer and fewer doctors are asked to bear the cost.

For example, a man may go to see his family doctor because he has blood in his urine. The G.P. may send him to a urologist, the urologist may order x-rays, on the basis of those x-rays the urologist and radiologist may determine that the man has kidney cancer, a surgeon may partially remove the cancer, and a radiation oncologist may then treat the patient with radiation. Assume that the radiation oncologist radiates the wrong kidney and the patient dies. Under the current medical malpractice insurance system radiation oncologists must bear the cost of that mistake. Were it not for the diagnosis and treatment of many other doctors at different levels of the pyramid, however, the radiation oncologist would never have treated the patient. If doctors on lower levels of the pyramid bore a small portion of the cost of a mistake by doctors on higher levels -- on the rationale that all doctors benefit economically by treating patients on whom specialists undertake high-risk procedures -- the cost of malpractice insurance for high-risk specialists would go down. In addition, such a system would give all doctors a greater incentive to exercise due care in referring patients.

Second, doctors are broken down by insurance companies into too many categories, with too few doctors in some categories. In Wisconsin, for example, the few dozen

neurosurgeons in the state traditionally have constituted one category. Thus, if an insurance company pays a major claim against one neurosurgeon it must raise rates substantially to all neurosurgeons -- there are simply too few doctors in the category among whom to spread the risk. If insurers were required to put all doctors into three or four categories rather than the dozen or so they do today, an adequate spread of risk would exist in all categories. Doctors who are today paying exorbitant premiums would pay substantially less, while doctors paying very little today would find their premiums rising slightly. The statute recently enacted in Wisconsin requiring that doctors be grouped into no more than four categories is attached as Exhibit N1. A chart showing the effect on premiums of collapsing nine doctor classifications into three is attached as Exhibit N2.

Third, today doctors pay for malpractice that could more easily be borne by hospitals. Whenever a doctor makes a mistake, whether in making a diagnosis in his office or conducting a procedure in a hospital, the doctor pays. Charging hospitals for part of the cost of malpractice occurring in hospitals would have two positive effects. Because hospitals have a very large number of beds over which to spread risk, hospitals could bear the cost of malpractice occurring in hospitals better than doctors. And requiring hospitals to pay for malpractice occurring there would encourage them to make sure that the doctors to whom they grant privileges are competent.

Fourth, doctors, unlike drivers and homeowners, are not

experience rated, so that the many doctors who are rarely if ever negligent subsidize the few doctors who are frequently negligent. If doctors were experience rated, so that those frequently involved in malpractice paid more and those with good records paid less, this subsidization would stop and most doctors would pay less. Experience rating would thus increase each doctor's incentive to exercise due care. Regulations implementing experience-rating of doctors are attached as Exhibit I2.

In addition, of course, doctors do a notoriously bad job of disciplining their own. Insurance companies should disclose all payments they make in connection with malpractice claims, and the names of doctors involved in those claims, to the Department of Insurance, and the Department of Insurance should make such information available to medical licensing boards, hospitals, professional review organizations and the public. Such disclosure would enable doctors to weed out the "bad apples," thus reducing the incidence of malpractice and consequently reducing malpractice insurance rates. Moreover, such disclosure would be invaluable to the consumer in choosing a doctor.

A bill requiring disclosure of payments in medical malpractice cases is attached as Exhibit O.

III. How to Make the Legal System More Efficient

There is a difference between "tort reform" and true legal reform. "Tort reform," in the sense in which it is

used by insurers, simply means limiting liability: making it more difficult to sue and more difficult to win, and limiting compensation -- particularly for "non-economic" injuries such as disfigurement and paralysis -- for people who do sue and win.

Limiting liability, however, does nothing to reduce the overall costs of the legal system by making it more efficient, e.g., by reducing delay, or increasing the proportion of the money flowing through the system that actually reaches the injured person. NICO's recommendations for making the legal system more efficient follow.

A. Limit lawyer's fees on both sides.

Should government limit legal fees? On the one hand, principled conservatives, including Senate Commerce Committee Chairman John Danforth (R.-MO), have forcefully argued that an administration which has sought to deregulate airlines, communications, banking and other endeavors ought not single out lawyers' fees for regulation.

On the other hand, the Reagan Administration has sought to limit plaintiff's lawyer's fees -- to 25% of the first \$100,000 recovered, 20% of the next \$100,000, 15% of the next \$100,000 and 10% of anything above \$300,000. It has not sought to limit defense lawyers fees. Because the relationship between a defense lawyer and his corporate client is a roughly equal one, whereas the relationship between a plaintiff's lawyer and his client -- a scared, unsophisticated injured individual -- is grossly unequal,

plaintiffs arguably need protection by the government that defendants do not.

The Administration's sliding scale, however, would not protect plaintiffs from overreaching plaintiff's lawyers but rather would limit the ability to sue of those people who have been seriously injured by a defective product or a negligent doctor or hospital. For example, one law firm representing several women rendered infertile by the Dalkon Shield IUD had to spend \$800,000 before recovering a penny from A. H. Robins, the manufacturer of the Shield. 19/ Under the Administration's proposal it would not be economically feasible to bring such a case, since defense fees and defense tactics -- and therefore plaintiff's lawyers' costs -- remain unlimited, while the plaintiff's lawyer's reward for winning the case is sharply limited.

If lawyers fees are to be limited, they should be limited on both sides. The fastest growing expenditure in the legal system is not plaintiff's lawyer's fees - which are typically 1/3 of the recovery if they win and nothing if they lose - but defense lawyers fees. According to the Insurance Services Office, for each dollar insurers pay to injured people they pay \$.46 to defense lawyers -- double the amount they paid to defense lawyers just ten years ago. 20/ And

19/ Robins, Zelle, Larson & Kaplan, "The Bomb in the Boardroom," Nov. 15, 1984, Minneapolis, MN (seminar) (Statement of Robins, Zelle, attorney Roger P. Brosnahan).

20/ Insurance Services Office, Inc., The Rising Costs of General Liability Legal Defense, at 3 (May 1986).

since 1956, defense lawyers' fees have risen three times as fast as claims payments. 21/

The rise in defense costs is particularly alarming because each additional dollar spent on defense lawyers means an additional dollar that must be charged directly to policyholders; increasing defense costs thus directly increases insurance rates. The amount the plaintiff spends on his lawyers, on the other hand, has no effect on premium rates, since rates are based on the amount of the jury verdict or settlement, not the percentage of that verdict or settlement that goes to the plaintiff's lawyer.

States could limit defense fees by disapproving any rate that included within it more than a certain percentage -- say 25% -- for defense costs. Under such a plan, the amount spent on defense costs is limited, but the insurer has the ability to determine how best to allocate that amount. With lawyers fees limited, a greater percentage of the money flowing through the system would wind up in the hands of the injured person.

A bill taking an extremely modest first step toward controlling lawyers fees on both sides is attached as Exhibit P.

B. Penalize frivolous actions on both sides

Just as insurers have sought to limit plaintiff's but

21/ Insurance Services Office, Inc., and National Association of Independent Insurers, "1985: A Critical Year" (May 1985).

not defense lawyers' fees, they have sought to penalize frivolous actions by plaintiffs - frivolous suits -- but not frivolous actions by defendants - frivolous motions and objections.

In fact, however, much greater incentives exist for the latter than for the former: because they charge by the hour, defense lawyers have an incentive to "keep their meter running" by raising defenses, filing motions, interposing objections and briefing and rebriefing the same issue -- no matter how untenable their position -- even if settling the case quickly would actually be cheaper for their clients. Plaintiff's lawyers, in contrast, have no incentive to delay, since they work on a contingency fee basis, getting paid only if and when they win.

States should enact legislation establishing severe sanctions, or encouraging judges to impose such sanctions, for delaying tactics or actions taken in bad faith, whether by plaintiff or defense lawyers. Possibilities include:

1. The judge could order that the party found to be acting in bad faith pay the attorney's fees involved in opposing the action found to be in bad faith, perhaps with an additional penalty;
2. The judge could direct a verdict on the issue or issues dealt with in bad faith against the party found to be acting in bad faith;
3. The judge could direct a verdict in the entire case against the party acting in bad faith;

4. Lawyers found to be acting in bad faith could be suspended;

5. Lawyers found to be continually acting in bad faith could be disbarred.

Bills imposing modest penalties for frivolous actions are attached as Exhibits Q1, Q2 and Q3.

C. Prohibit secrecy agreements

What does a lawyer do when a defendant offers to settle his client's case for a generous amount, but only on condition that the settlement agreement remain sealed and that all material discovered during the case be returned or destroyed? The settlement is clearly in the individual client's best interest, but equally clearly can be contrary to the public interest: it may allow the manufacturer to continue to market a product it knows is defective, it causes more people to be killed and injured by that product, and it makes it more difficult for other people injured by the product, or the families of those killed by the product, to receive compensation.

Perhaps the most sordid and well-known example of a corporation insisting on secrecy agreements is that of A. H. Robins in Dalkon Shield cases; 22/ today, Honda and the other

22/ See Remarks of Miles Lord, Chief Judge, District Court for the District of Minnesota, to Messrs. Robins, Forrest and Lunsford of A.H. Robins Co., Feb. 29, 1984 ("In order that no group of plaintiffs might assert a sustained assault upon your system of evasion and avoidance, you time after time demand that able lawyers who have knowledge of the facts must, as a price of getting their cases, agree to never again take a Dalkon Shield case nor help any less experienced lawyers with their cases against your company.")

manufacturers of 3-wheel All Terrain Vehicles (ATV's), which have already been responsible for almost 200 deaths, are insisting on similar agreements.

To eliminate the conflict between the individual client's interest and the public interest, to reduce costs and to save lives, states should prohibit secrecy agreements.

A draft bill prohibiting such agreements and accompanying explanations are attached as Exhibit R.

D. Encourage offensive collateral estoppel

Under the doctrine of collateral estoppel, a party that has had a full and fair opportunity to litigate a fact at issue is not permitted to relitigate that issue in case after case; rather, the fact is established and can be used in future cases.

Judges have been hesitant to allow the use of collateral estoppel by plaintiffs, even though allowing such use would substantially speed up the resolution of cases. Taking the Dalkon Shield example again, in case after case A. H. Robins argued that the Dalkon Shield was not defective, even as court after court found that it was defective; had the defectiveness of the product been deemed established early in the litigation, with liability then depending on whether or not there was causation in each individual case, costs on all sides would have been substantially reduced. 23/

23/ See M. Mintz, At Any Cost: Corporate Greed, Women and the Dalkon Shield (1985).

E. Pass back collateral source benefits

Under current law in the majority of states, the jury is not permitted to hear evidence of any payments the plaintiff may receive for his injury from sources other than the defendant, e.g., workmen's compensation benefits, health insurance benefits, or social security benefits. In some states the jury may consider such evidence, and in a few states the jury verdict is automatically reduced by the amount of benefits from these "collateral sources."

The majority rule -- the so-called "collateral source rule" -- presents a difficult issue. On the one hand, a defendant who has negligently caused an injury certainly does not deserve a windfall because the plaintiff happens to have insurance or is eligible for other benefits. On the other hand, a plaintiff who receives compensation for medical expenses from both a jury verdict and another source receives double recovery to the extent medical expenses paid by the other source exceed the payment he has made to that source, such as premiums for health insurance.

To prevent both windfalls to defendants and double recovery for plaintiffs, the fairest solution is probably to require the defendant to pay the full amount of the verdict, but to excuse the source of the collateral benefits from paying such benefits to the extent that they are already included in the jury verdict. With the money thereby saved, the source of the collateral benefits would be required to reduce the cost of those benefits across the board. For

example, if the jury verdict included compensation for lost wages, and the plaintiff was eligible for workmen's compensation benefits, the defendant would pay the full amount of the verdict to the plaintiff and the plaintiff's workmen's compensation carrier would be excused from paying the plaintiff, but would be required to pass through the savings by reducing its rates across the board.

Under this rule, the cost of health insurance and workmen's compensation insurance should fall by 10-15%, and transaction costs would be reduced. And taxpayers, workers and purchasers of health insurance would not subsidize liability insurers, as they would if jury verdicts were reduced by collateral source benefits.

F. Create incentives to settle.

Because they're paid by the hour, defense lawyers have an incentive to keep their meters running by delaying the resolution of cases -- even those where liability is clear -- to the greatest extent possible.

Penalizing defendants for refusing to make reasonable offers, and penalizing plaintiffs for making unreasonable demands, would encourage both sides to be more reasonable more quickly in negotiating and thus to resolve cases more quickly.

A bill penalizing both the failure to accept a reasonable offer and the making of an unreasonable demand is attached as Exhibit S.

G. Establish alternatives to the tort system - including

no-fault systems, arbitration, mediation, mini-trials,
and other alternative dispute resolution systems

The tort system serves three important functions: compensation, deterrence and disclosure. Because no effective criminal penalties exist to deter corporations from acting irresponsibly, the tort system provides the only meaningful deterrent to such actions. And because government regulators can not be depended on to ferret out information that corporate defendants do not wish to disclose, the tort system is the only means to force disclosure of such information. The stories of A. H. Robins and the Dalkon Shield, 24/ Ford and the Pinto gas tank, 25/ Richardson-Merrell and MER-29, 26/ and Johns- Manville 27/ and asbestos are just a few of the scandals unearthed as a result of tort litigation. And it was only the fear of more litigation, and of large awards for both compensatory and punitive damages, which finally forced these and other dangerous products off the market and encouraged the development of less dangerous substitutes.

It is therefore essential that the common law continues to develop and that no limits be placed on either

24/ See id.

25/ See Grimshaw v. Ford Motor Co., 174 Cal. Rptr. 348 (1981)

26/ See Toole v. Richardson-Merrell, 251 Cal.App. 2 689 (1967).

27/ See P. Brodeur, Outrageous Misconduct: The Asbestos Industry on Trial (1985).

compensatory or punitive damages in cases involving defective products.

In other types of cases, on the other hand, factors other than the tort system may deter irresponsible conduct or force disclosure - or deterrence and disclosure may be less important - and another type of system might compensate people more efficiently than does the tort system. The classic example is no-fault auto insurance. Both criminal penalties and self-interest deter people from driving recklessly, and when the police arrive at the scene of an auto accident it becomes a matter of public record. A no-fault insurance system which neither deters reckless conduct nor forces disclosure but does compensate people more efficiently than does the tort system therefore makes sense for auto accidents. Up to 95% of each dollar flowing through such systems reaches the injured person, compared to less than 50 % of each dollar in the tort system.

For other types of uncomplicated cases involving relatively minor injuries, such as many slip-and-fall cases, no-fault systems may also be worth trying. For example, states may wish to consider a no-fault system with an add-on penalty for deterrence for all cases not involving death, disfigurement or permanent disability in which the plaintiff's economic loss was less than a certain amount. Under such a system, if the injured person sought payment of his economic loss from a defendant causing the injury, and the defendant failed to pay such economic losses within 30 days, the defendant would automatically be penalized heavily,

e.g., by being required to pay treble damages. Such a system might well provide a sufficient deterrent to run-of-the-mill negligence causing relatively minor injury, although it would not force any disclosure.

In addition, for parties with roughly equal bargaining power -- such as an asbestos manufacturer and its insurer or two major manufacturers -- other less costly alternatives to the tort system may make sense. Corporations that have frequent business dealings with each other, for example, can provide by contract that any disputes between them be resolved by binding arbitration, or by "mini-trials" that are much less formal and expensive than full blown trials.

Finally, in certain cases the tort system has worked exactly as it is supposed to: litigation and substantial damage judgments have not only compensated injured people but have also stopped irresponsible actions, or forced responsible ones, and have enabled the public to learn the truth about outrageous corporate misconduct. After the corporation and its officers are punished adequately, many still-uncompensated victims of the product might be more quickly and adequately compensated through an alternative dispute resolution system than through the tort system.

Bills establishing various types of alternative dispute resolution systems are attached as Exhibits T1, T2 and T3.

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RAND "THREE LEVEL" STUDY AND OTHER REPORTS

- 1) Report: Trends in Tort Litigation, 1987
- 2) Report: Costs and Compensation; Paid in Tort 1986 Litigation
- 3) Report: Contingent Fees for Personal Injury Litigation - 1980
- 4) Report: Medical Malpractice Liability Study - 1989

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CORRECTION

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The Institute for Civil Justice, established within The RAND Corporation in 1979, performs independent, objective analysis and research on the American civil justice system. The Institute's purpose is to help make the civil justice system more efficient and more equitable by supplying policymakers with the results of empirically based, analytic research.

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FOREWORD

During the last two years, the issue of tort reform has been vigorously debated in virtually every state legislature and in the U.S. Congress. Because the tort system directly affects the interests of the various parties to this debate, it is not surprising that the proponents and opponents of reform have sharply differing ideological positions. The more striking feature of the debate is the sharply differing perceptions of the underlying reality—perceptions buttressed by a bewildering array of seemingly contradictory statistics.

Proponents of reform cite numbers showing an explosion of lawsuits, jury verdicts that are "out of control," and a system where legal fees and expenses rival the amounts paid in compensation. Opponents marshal other data to show that the explosion of suits is a myth, that jury awards have been remarkably stable, and that the transactions costs of the system are reasonable given its objectives.

This report takes on the task of sorting out these conflicting claims and statistics. The task is a natural one for the Institute for Civil Justice—and not simply because both sides have used ICJ research to support their positions. The Institute has played a leading role in shifting the grounds for the debate from an exchange of anecdotes to presentation of empirical data to support assertions.

The central message of the report is that much of the confusion results from the implicit notion of a single, homogeneous tort liability system. This misperception is shared by policymakers and by proponents and opponents of reform who operate under the assumption that indicators of change along one dimension of the system reflect changes in the system as a whole. In fact, the tort liability system appears to consist of three separate systems. The report delineates these systems and suggests why they appear to be evolving in different directions. It proposes an explanation for why diverse statistical data have characterized the policy debate and provides an important framework for understanding the conflicting claims resulting from that debate.



Most ICJ publications present the findings of a single empirical study. However, as our research inventory has grown, we have frequently been asked to synthesize and interpret our findings. Until now, we have responded to these requests in legislative testimony or in professional journal articles—forums designed for relatively specialized audiences. With this report, the ICJ initiates a new series of publications, intended for a wider audience, that will synthesize the results of previous ICJ studies and place them in a broad policy context.

Kevin F. McCarthy
Director, The Institute for Civil Justice

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INTRODUCTION

Over the past two years, insurers, manufacturers, physicians, consumer advocates, and trial attorneys have vigorously debated the costs and benefits of the tort system as a mechanism for compensating and deterring injuries. The debate began with a perceived "insurance crisis." Liability insurance premiums, particularly for medical malpractice and commercial lines, increased sharply, and insurance for some kinds of activities became unavailable at any price.

While there was broad consensus that obtaining and paying for insurance was a pressing problem, there was little agreement about the cause or its solution. On the one hand, insurers linked rising rates and unavailability to trends in tort litigation, thus focusing attention on the legal system. In many states and at the federal level, insurers, manufacturers, health care professionals, and local government officials formed coalitions to support substantive changes in tort law. On the other hand, trial attorneys and consumer groups generally opposed these changes, arguing that what needed reform was not tort law, but poor management practices in the insurance industry.

It is hardly surprising that the proponents and opponents of what became known as "tort reform" held sharply differing positions. However, they also appeared to hold sharply differing views of reality.

Proponents of change argued that there has been an explosion of liability lawsuits in the past five years, that recent verdicts demonstrate that civil juries are "out of control," and that the monetary benefits delivered by the tort system to injured parties are overshadowed by the enormous costs of administering the system. Tort reform was needed to counteract these trends.

*The policy debate
over tort reform*

Opponents of tort reform argued that the litigation explosion is a myth, that jury awards have been basically stable for 25 years, and that the transactions costs of the system are acceptable, given the system's twin objectives of compensation and deterrence. Tort reform was not only unnecessary—it might be harmful to those whom the system is intended to serve.

*The statistical
debate . . .*

Each side presented statistical data that appeared to support its position. But the differences in the data cited were puzzling even to those wise in the ways of lying with statistics. Each side claimed to be accurately describing the tort litigation system, yet the two sides seemed to be talking about different worlds. A sample:

*. . . on the
litigation
explosion*

- Between 1977 and 1981, the number of civil lawsuits in state courts grew four times faster than the total U.S. population (*Time*, March 24, 1986, p. 20).
- The annual number of tort filings in 17 states rose 9 percent between 1978 and 1984; meanwhile, population in those states rose 8 percent (*"The Manufactured Crisis,"* Medical Economics, November 10, 1986, p. 69).

*. . . on the
growth in amount
awarded*

- The average award in product liability and medical malpractice cases is now over a million dollars (*Time*, March 24, 1986).
- Between 1975 and 1984, the growth in the median medical malpractice award has been less than the rise in inflation. In product liability cases, the growth rate for median awards has exceeded the inflation rate, but not by much (*"The Manufactured Crisis,"* p. 68).

Where does the truth lie?

*The worlds of
tort litigation*

Recent research on trends in tort litigation, conducted by The Institute for Civil Justice (ICJ)¹ at The RAND Corporation, suggests an explanation for the apparent discrepancies among the statistics: There is no longer, if there ever was, a single tort system. Instead, there are at least three types of tort litigation, each with its own distinct class of litigants, attorneys, and legal dynamics.

- The first is the world of routine personal injury torts, exemplified by auto suits. They occur frequently and usually involve modest injuries and relatively low

¹The Institute for Civil Justice was founded at RAND in 1979 to conduct independent, objective policy analysis and research on civil justice issues. RAND is a nonprofit institution; the ICJ is supported by pooled grants from corporations, including insurance and noninsurance organizations, private foundations, trade and professional associations, and individuals.

financial stakes. Settled law and routine procedures lend an air of stability to this world.

- The second is the world of high-stakes personal injury suits, such as product liability, malpractice, and business torts. Here the litigation itself is newer, the law is still evolving, and the stakes per case are larger and increasingly uncertain.
- The third is the world of mass latent injury cases, such as asbestos litigation, Dalkon Shield cases, and other suits arising from mass exposure to drugs, chemicals, or toxic substances. The lack of "fit" between traditional tort law and the facts of these cases leads many to view them as problematic.

Each of these worlds is characterized by a different litigation growth rate, jury verdict trend, and cost profile. Treating the three types of litigation together—as is done whenever overall statistics for tort litigation are reported—produces a distorted picture of tort litigation that does not accurately reflect the reality of any of these worlds. Inferences about trends in one area of litigation based on data drawn from another are also likely to be wrong. Just as the blind men who tried to identify an elephant by feeling different parts of it each perceived different realities—none of them an elephant!—statistical views of any one part of the litigation system are necessarily distorted. And the resulting controversy over whose statistics were *right* has diverted attention from the story behind the statistics: the changes taking place in different areas of litigation—changes that may well merit different types of policy responses.

In this report, we will review and explain the statistical evidence as we sketch a comprehensive picture of the three worlds of tort litigation, drawing on seven years of ICJ research. We will use this research to answer three questions that are at the heart of the recent debate on trends in tort litigation:

- How much litigation is there?
- Are jury awards stable or out of control?
- How much does litigation cost, and who gets the money?

*Treating three
worlds as one
invites distortion*

*Key questions to
be answered*

We will show how the answers to these questions differ depending on which world of litigation one examines. And we will suggest why litigation trends and outcomes in these worlds are increasingly divergent.

LITIGATION: HOW MUCH IS THERE?

It would be hard to find a wider range of opinions than those held, and strongly asserted, about the amount of litigation nationwide. Some observers claim the United States is witnessing a litigation explosion reflecting litigiousness unmatched anywhere in the world.¹ Others claim that recent statistics on court filings indicate stable, or very slowly increasing, litigation rates.² Yet others argue that many Americans with legitimate grievances do not pursue them in court because they lack the financial and social resources necessary to do so.³

The controversy

Why is there so much uncertainty and controversy about this basic question? Three reasons: (1) not enough good data; (2) confusion between litigiousness and amount of litigation; (3) description of different types of tort litigation. In this section, we will attempt to avoid these sources of confusion by examining the amount of litigation in each of the three worlds.

Three organizations are the source of the most commonly cited data in the debate over litigation rates: (1) the Administrative Office of the U.S. Courts, which yearly collects information about filings in the federal district courts; (2) the National Center for State Courts (NCSC), a private, nonprofit, court-supported organization that has been monitoring the amount of litigation in state courts across the country since the late 1970s; and (3) The Institute for Civil Justice, which does not itself collect or publish caseload statistics, but has reviewed and interpreted the available data in the course of its studies.

Data sources . . .

¹For example, see Elaine S. Knapp, "Who's to Blame? Insurers or Courts?" *State Government News*, Vol. 29, No. 3, March/April 1986; or "There Is a Litigation Explosion," *The National Law Journal*, May 19, 1986.

²David Burrow and John E. Collins, "Insurance Crisis—Texas Style: The Case for Insurance Reform," *St. Mary's Law Journal*, Vol. 18, No. 3, Winter 1987, pp. 760-761.

³"The Manufactured Crisis," *Medical Economics*, November 10, 1986, p. 61.

*... and data
problems*

The growth rate for federal filings is straightforward. The data from the Administrative Office of the Courts are complete and show that tort filings in federal courts grew at an average annual rate of 4 percent between 1981 and 1984. Unfortunately, however, federal filings are a very small part of total tort action. About 95 percent of the tort cases are filed in the state court system,⁴ but these data are incomplete. The NCSC is hampered in its recordkeeping because not all state courts distinguish tort litigation from other civil cases such as commercial and contract suits. Therefore, both the NCSC and all other users must extrapolate from the data available. The NCSC estimates an average annual growth of 2.3 percent in tort filings in state courts between 1981 and 1984; the comparable ICJ estimate is 3.9 percent.⁵

*Total amount of
tort litigation
nationwide is
growing slowly*

Whatever the slight differences among estimates, it is clear that the amount of tort litigation nationwide is growing relatively slowly. Indeed, when the rate is adjusted for population growth, it sinks (according to estimates by ICJ researchers) to a modest 3 percent. This number is not, by itself, a good measure of litigiousness. Such a measure would have to include other kinds of information—for example, whether the number of claims or grievances that could be litigated was growing. But it is a good measure of overall litigation activity.

*But growth
differs for
different case
types*

But the total amount of tort litigation nationwide is not the relevant statistic for policymakers. When we examine how much litigation occurs in different types of cases, we see significant differences. Figure 2.1 illustrates this point. It shows changes from 1975 to 1985 in the amount of tort litigation in the federal courts and in California state courts, one of the few state courts that tracks the personal injury caseload. The data for the federal caseload let us show separate results for auto, marine, and air cases, other nonproduct personal injury cases, and product liability. For California, we can distinguish only auto and other personal injury, a category that includes product liability,

⁴For further discussion, see James S. Kakalik and Nicholas M. Pace, *Costs and Compensation Paid in Tort Litigation*, The RAND Corporation, R-3391-ICJ, 1986, Chapter II.

⁵The ICJ estimation method is discussed in detail in Kakalik and Pace, 1986.

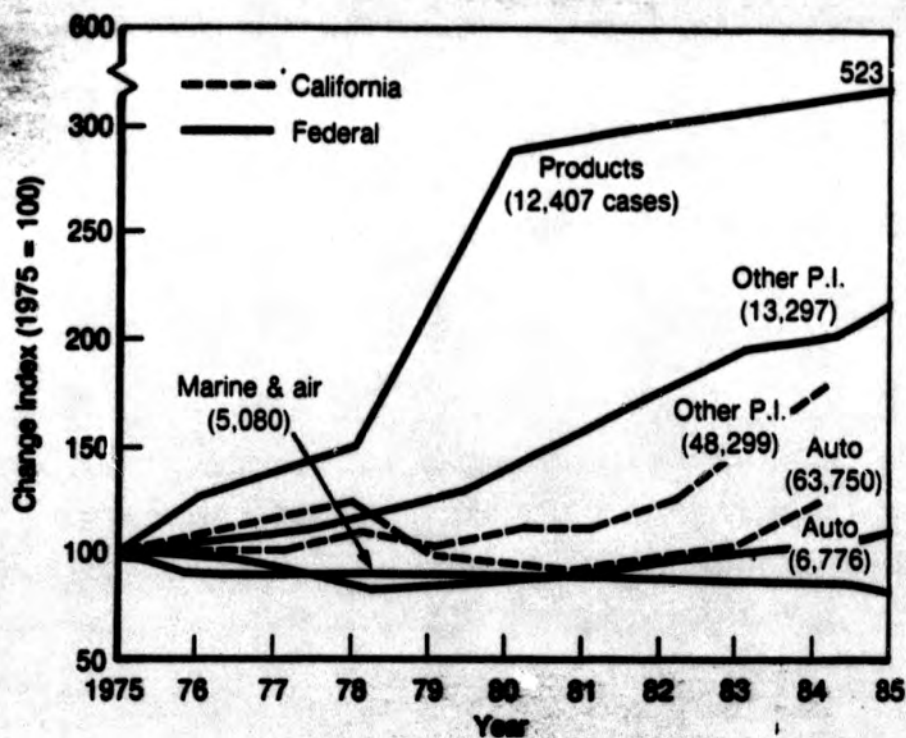


Fig. 2.1—Growth differs for different case types

medical malpractice, and a variety of other personal injury torts. We have used 1975 as the base year and calculated deviation from it.

Because there are only two categories, the California pattern is the simpler. The data for auto cases show a slight increase, which roughly mirrors population growth during this period; in other words, litigation in this area remained basically stable. However, the increase in other personal injury suits is much sharper and far outpaces population increases.⁶

*High-stakes
personal injury
suits are growing
faster*

⁶See Deborah R. Hensler, *Trends in California Tort Liability Litigation*, The RAND Corporation, P-7287-1CJ, March 1987.

Although the data from the federal courts are more diverse, the basic pattern is the same. The number of auto and marine and air cases was very stable over the entire period. However, other nonproduct personal injury cases grew rapidly and product liability cases have soared. It is the precipitousness of this last increase that has attracted so much media attention. It is unclear whether this quantum jump is because the federal courts are now getting a portion of these cases that used to be filed in state courts, or because asbestos cases and other mass latent injury suits are swelling the caseload. Probably both factors are operating, but we are unable to tease out their separate effects from these data.

A different measure of changing caseload is the composition of the caseload. Table 2.1 shows the shift in caseload for federal courts, California courts, and NCSC data for a group of state courts (California, Hawaii, Maryland, Michigan, and Texas) that report more detailed information about filings.

Table 2.1

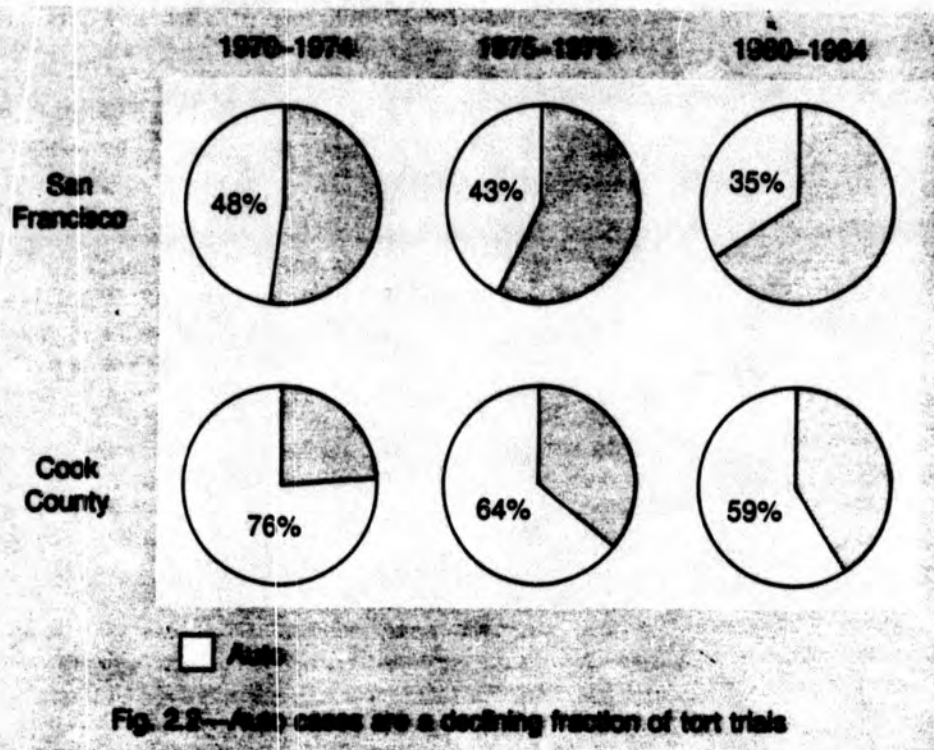
**AUTO CASES ARE A DECLINING
FRACTION OF TORT FILINGS**

	Percentage of Case Filings	
	1975	1985
Federal courts		
Auto	25	16
Non-auto	75	84
California	1975-1976	1984-1985
Auto	65	43
Non-auto	35	57
Five state courts ^a	1980	1984
Auto	61	55
Non-auto	39	45

^aCalifornia, Hawaii, Maryland, Michigan, and Texas (NCSC).

Although the periods covered are not identical because some data are unavailable, we observe similar patterns. In every category, auto cases are a declining percentage of case filings.

For most courts, we are fortunate just to have data on filings. But the ICJ has been able to assemble data on tort trials in San Francisco and in Cook County, Illinois, for 1960-1984. These data allow us to analyze the composition of trial caseloads, as shown in Fig. 2.2.⁷ Throughout the period 1970-1984, Cook County tried a much larger percentage of auto cases than did San Francisco. However, in both jurisdictions, auto accident cases constitute a steadily declining slice of the caseload pie, falling from 48 percent to 35 percent in San Francisco, and from 76 percent to 59 percent in Cook County.



⁷Based on data from Mark A. Peterson, *Civil Juries in the 1980s: Trends in Jury Trials and Verdicts in California and Cook County, Illinois*, The RAND Corporation, R-3466-ICJ, 1987.

**Where the
explosion may
occur**

There is little ambiguity about the trends in the third category of cases—mass latent injuries. Data from asbestos and Dalkon Shield claims demonstrate truly explosive growth for these types of cases. For example, most experts estimate that there were about 16,000 asbestos worker injury claims in 1981; five years later, there were more than 30,000 asbestos cases in state and federal courts. In 1981, there were an estimated 7,500 lawsuits pending over injuries from Dalkon Shields. By 1986, after A. H. Robins, the manufacturer, had sought protection under Chapter 11, more than 325,000 claims had been submitted to the bankruptcy court.

Mass latent injury suits have this explosive quality for two reasons. First, some toxic substance litigation is concentrated in particular areas where that substance may have been used. For example, asbestos was widely used in certain industries—in shipbuilding on the east and west coasts and on the Gulf and in the petrochemical industry on the Gulf. Because of this geographical concentration, asbestos claims may flood the courts in some cities even though they might not constitute a very large percentage of the national caseload.

We have estimated the contribution of asbestos claims to judges' civil caseloads in a number of federal and state courts.⁸ For 1984, the percentages ranged from a low of about 7 percent in Northern California to highs of approximately 25 percent in Massachusetts and New Jersey.

Second, the statute of limitations defines a time window within which claims must be brought. If newly discovered evidence or a new legal ruling provides a new basis for claims, then a large number of people must file expeditiously. The system may well experience the results as an explosion.

As the metaphor suggests, this explosion of tort filings may be temporary—a bulge that the system slowly absorbs. But because these cases appear on the legal scene suddenly and in very large numbers, they contribute to a

⁸For details, see Deborah R. Hensler, William L.F. Felstiner, Molly Selvin, and Patricia A. Ebener, *Asbestos in the Courts: The Challenge of Mass Toxic Torts*, The RAND Corporation, R-3324-ICJ, 1985, p. 27.

general impression of hectic court activity and may well overwhelm courts in certain locations.

The answer to the question of how much tort litigation there really is depends critically on which world of litigation the data describe.

So how much tort litigation is there?

- *Auto accident cases are a steady or declining percentage of court action.*
- *Non-auto personal injury cases such as malpractice and product liability are growing moderately in state courts and more dramatically in federal courts.*
- *Mass latent injury cases have the potential for explosive growth as new evidence of harms is developed.*

JURY AWARDS: STABLE OR OUT OF CONTROL?

More statistical confusion

Some of the most memorable salvos of the insurance crisis war have been aimed at the amounts that juries award injured plaintiffs. And nowhere is the bewildering discrepancy between statistics so dramatic:

The average verdict in both product liability cases and medical malpractice cases is now more than \$1 million, and the number of million-dollar awards has been growing quickly. Between 1980 and 1984, it jumped nearly 200 percent to 401 (*The Wall Street Journal*, May 16, 1986).

The increase in awards is necessary to keep up with climbing health care costs. . . . The cost of inpatient, outpatient, and physician care has risen an average of almost 16 percent between 1978 and 1984. During that same period, verdict amounts rose only about 13 percent (*The Wall Street Journal*, April 8, 1987).

Is there a way to reconcile these viewpoints?

Which yardstick to use

The debate about jury awards has been further complicated by argument over the proper statistics to use in describing trends. The most frequently cited statistics are *medians* and *means*.

Median awards

The *median award* is the midpoint of the distribution of jury awards to the plaintiff. To compute the median, one simply lists all the awards in the jurisdiction under study in order of their dollar value and locates the award at the midpoint of the list. Medians are not affected by either extreme high or low values. Although it is possible for many of the values in a distribution to diverge significantly from the median, in the absence of other information, it is reasonable to guess that most of the values are not too much higher or lower than the median. For this reason, it has become popular to think of the median as indicating the "typical" jury award.¹ Trends in median awards indi-

¹A more accurate statistical indicator of the typical award would be the *mode*, which is the value that occurs most frequently.

cate whether the behavior of juries, in general, has changed.

The *mean award* is the statistical average of all jury awards. To compute it, one sums the dollar value of all awards to the plaintiff in the jurisdiction under study and divides by the number of these awards. A few very high or very low awards will skew the mean award; therefore, it may not be a good measure of what the typical jury is doing. However, it does provide the single most accurate estimate of the amount awarded to successful plaintiffs.

Mean awards

Both medians and means usually describe points in the distribution of dollar amounts in the cases that the plaintiffs have won. However, plaintiffs do not always win. A better estimate of *expected award* includes cases that they lose. We can calculate the expected award by multiplying the *average award* by the *probability of winning*, which is less than one. This expected award is the best available indicator of what plaintiffs can expect to win or defendants expect to lose in the relevant jurisdiction.

Expected awards

Since 1979, the ICJ has conducted a series of studies about the decisions of civil juries. We examined detailed data for more than 14,000 civil cases tried by juries in Cook County, Illinois, and San Francisco, California, between 1960 and 1984. Data were obtained by creating computer records of information published in periodic jury verdict reporters for each jurisdiction.² Each record identifies the court and judge, relevant dates, type of case, liability issues involved, number of plaintiffs and defendants, and offers and demands; it also provides data about a wide variety of characteristics of the trial, including information about each defendant, each plaintiff, the nature of the claim, the plaintiff's possible negligence, and the outcome of the trial. ICJ researchers have used this rich database to study:

ICJ jury verdict studies

²The *Jury Verdict Reporter*, published by Max Sonderby, is a private, weekly subscription newsletter for lawyers and insurance companies in the Chicago area. *Jury Verdicts Weekly*, published by Kenneth Raymond, is a similar newsletter describing civil cases reaching verdict in California.

Key issues studied

- kinds of cases tried and trends in outcomes³
- how juries compensated various types of personal injuries and how compensation changed over time⁴
- how jury verdicts are related to the characteristics of litigants⁵

We draw on these analyses in the following discussion of trends in jury awards. The data are specific to San Francisco and Cook County, and we would not expect to observe the same medians and means in all the jurisdictions in the country. Indeed, San Francisco and Cook County differ on some dimensions, as we discuss below. However, the data are valuable because they are currently the only data available in the United States that allow us to discuss long-term trends in trial outcomes. And the similarity of trends between the two jurisdictions leads us to believe that the trends we are observing may hold nationwide. Moreover, the difference—discussed below—between verdict amounts for automobile accident and other routine tort cases, on the one hand, and product liability and medical malpractice cases, on the other, are repeated in more than three-fourths of the 44 jurisdictions nationally for which *short-term* jury verdict data have been assembled.⁶

Overall, median awards haven't changed much . . .

Figure 3.1 shows that median tort awards, when adjusted for inflation, remained remarkably stable in both jurisdictions during the period 1960–1975. The median was virtually constant in Cook County. In San Francisco, there is

³Mark A. Peterson and George L. Priest, *The Civil Jury: Trends in Trials and Verdicts, Cook County, Illinois, 1960–1979*, The RAND Corporation, R-2881-ICJ, 1982; Michael G. Shanley and Mark A. Peterson, *Comparative Justice: Civil Jury Verdicts in San Francisco and Cook Counties, 1959–1980*, The RAND Corporation, R-3006-ICJ, 1983; Mark A. Peterson, *Civil Juries in the 1980s: Trends in Jury Trials and Verdicts in California and Cook County, Illinois*, The RAND Corporation, R-3466-ICJ, 1987.

⁴Mark A. Peterson, *Compensation of Injuries: Civil Jury Verdicts in Cook County*, The RAND Corporation, R-3011-ICJ, 1984.

⁵Audrey Chin and Mark A. Peterson, *Deep Pockets, Empty Pockets: Who Wins in Cook County Jury Trials?* The RAND Corporation, R-3249-ICJ, 1985.

⁶Stephen Daniels and Joanne Martin, "Jury Verdicts and the 'Crisis' in Civil Justice," *Justice System Journal*, Vol. 11, No. 3, Winter 1986. Daniels and Martin make a practice of reporting medians and interquartile ranges only.

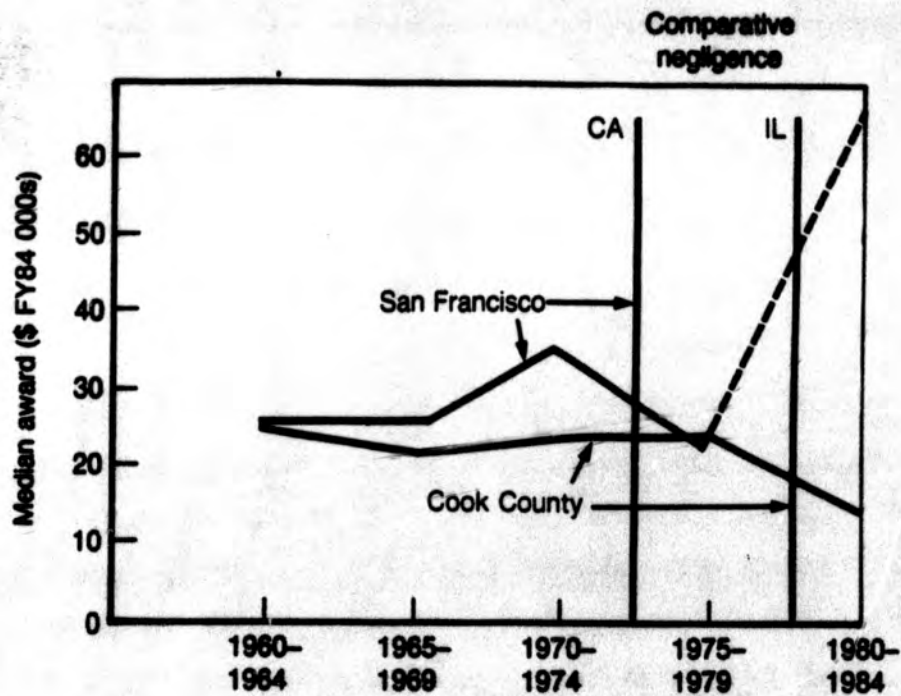


Fig. 3.1—Median tort awards are quite stable over time

more variation; nevertheless, in the period 1975-1979, the median award was slightly lower than it was in 1960.

In the 1980s, the median tort award (in constant dollars) changed in both jurisdictions. In Cook County it actually fell, but in San Francisco it rose dramatically. We believe that a change in the law—the substitution of a comparative negligence standard for contributory negligence—may be responsible for the decline in the median award in Cook County. More plaintiffs were winning awards, but the awards tended to be smaller, perhaps because they were reduced to reflect the plaintiffs' negligence. In San Francisco, changes in the composition of the trial caseload probably account for the change. The establishment of mandatory arbitration for smaller-value cases and an increase in the jurisdictional level of the lower

... but some recent changes are evident

court drove smaller-value cases out of the superior courts and caused a higher-value caseload overall.⁷

If our explanation of post-1980 trends in these jurisdictions is correct, then median awards have been strikingly stable over a 25-year period. As with the amount of litigation, however, this aggregate pattern changes when we examine the separate trends for auto vs. product liability cases (Fig. 3.2). The stable trend in medians persists for auto cases. However, the median for product cases has risen very sharply. The trend for medical malpractice suits (not shown in Fig. 3.2) is equally steep.

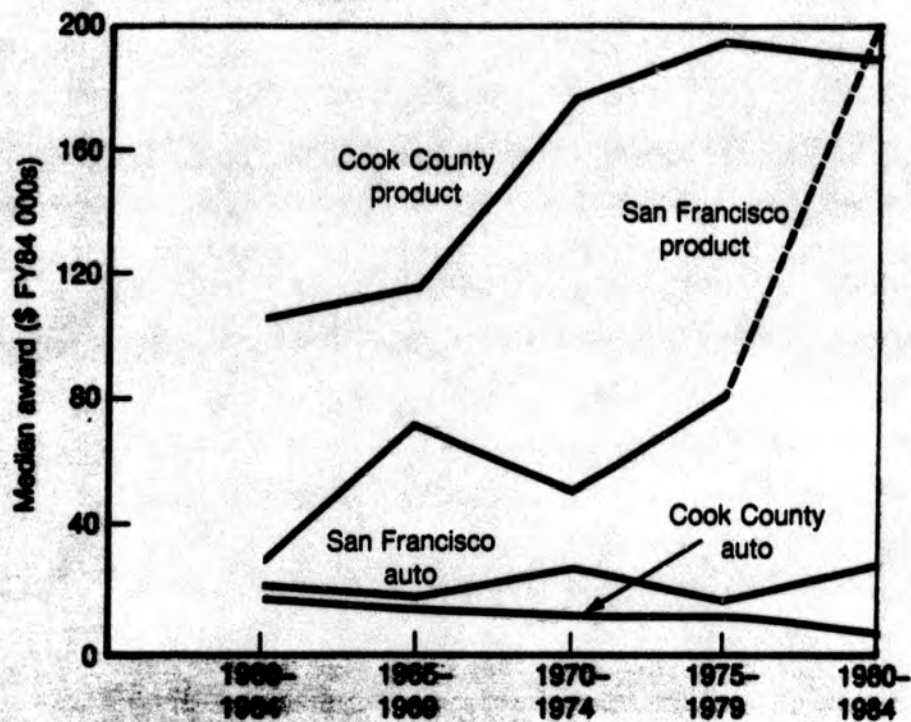


Fig. 3.2—Overall median for tort awards masks sharp differences

⁷These data are discussed in detail in Peterson, *Civil Juries in the 1980s*, 1987.

When we focus on the alternative yardstick—the mean—we find that average tort awards, adjusted for inflation, have increased sharply in both jurisdictions; the mean rose steadily in Cook County from \$59,000 during 1960–1964 to \$187,000 during 1980–1984 and in San Francisco from \$66,000 at the beginning of the period to \$302,000 during 1980–1984.

*Average awards
have risen sharply*

Figures 3.3 and 3.4 illustrate why the overall average award has risen so substantially. The average has increased even for routine, usually low-stakes cases such

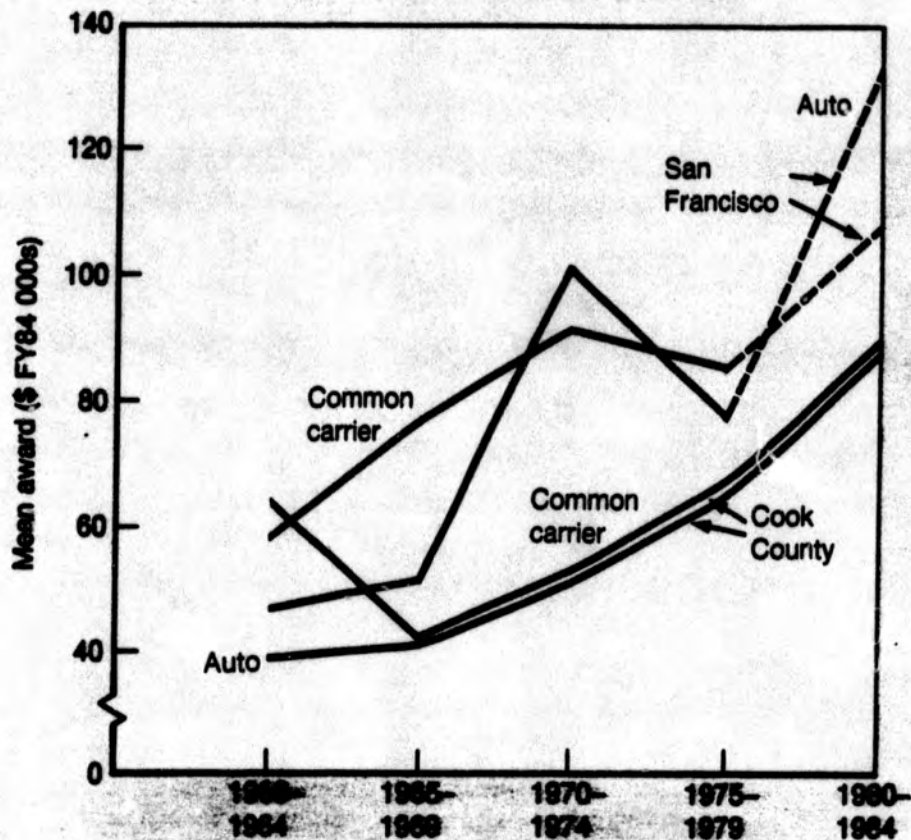


Fig. 3.3—Average auto and common carrier awards have risen for routine cases

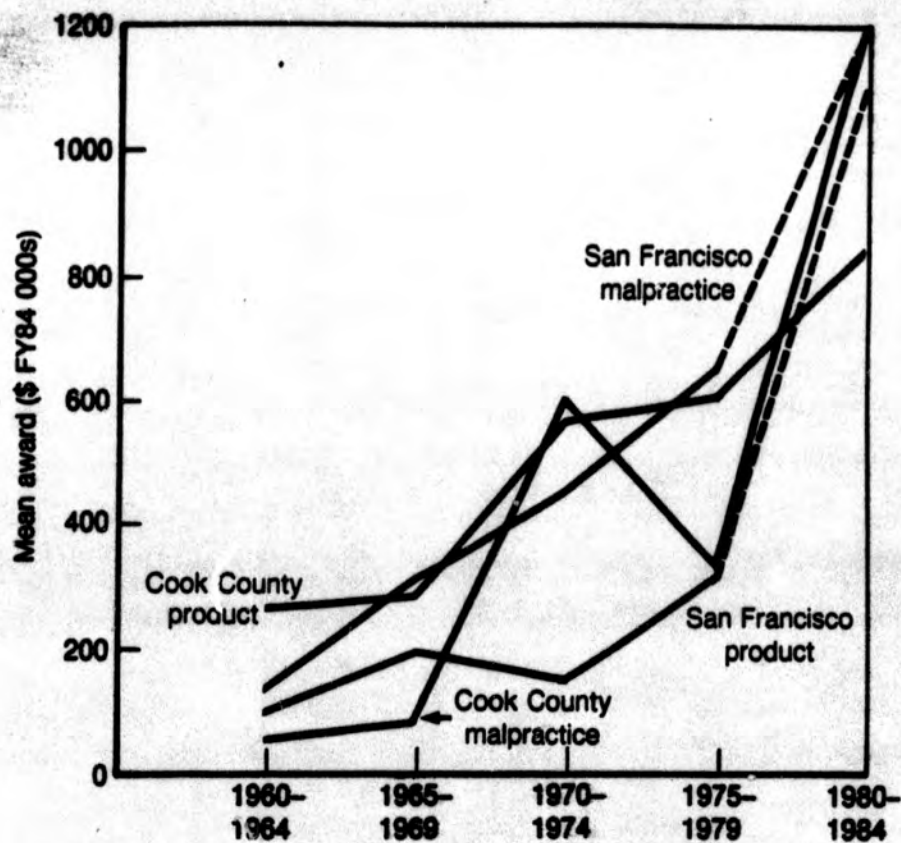


Fig. 3.4—Average award has risen sharply in malpractice and product liability cases

The chances of winning have increased

as auto. And in the case of high-stakes suits such as product liability and malpractice, the growth in the average award has been truly explosive, reflecting increases ranging from 200 to more than 1,000 percent.

The expected award is the product of the average award and the probability of winning. We have just examined two indicators of the trends in jury awards and seen substantial growth in the median award in all but the most routine cases and an increase in average awards across all types of cases. But plaintiffs do not always win. Has the probability of their doing so changed over time?

In the two jurisdictions that we studied, the answer is clearly "yes."⁶ For every type of liability case, Cook County plaintiffs were far more successful in the early 1980s than were plaintiffs twenty years earlier. For example, in the 1960s, plaintiffs won about one-fourth of product liability and malpractice cases. In the late 1970s, they won about one-third of such cases. By the 1980s, they were winning almost one-half of them. Plaintiffs in San Francisco also won more often in the 1980s, but the increase in their success rate is not as dramatic across all case types. In the 1970s, they won about one-third of all malpractice trials. Ten years later, they were winning more than one-half of them. For product liability cases, their success rate actually declined slightly over the period, but in the 1980s they were still winning more than one-half of these cases.

The increased probability of winning, coupled with the increase in average awards, results in higher expected awards. Figure 3.5 illustrates this increase as well as the differences among case types. The expected award for auto cases has risen from about \$25,000 to \$60,000-90,000 at the end of the period, but this move is dwarfed by the rocketing awards in product liability cases, which grew 400-900 percent between 1960 and 1984.

Judging from these data, there is little question that average jury awards are increasing in San Francisco and Cook County and that awards have increased more in high-stakes cases than in routine litigation. But are juries, or the jury system more generally, "out of control?" To answer that question we need more information because several other explanations also fit the data. For example:

Are juries "out of control?"

- *Jury awards might be changing because the cases coming before them are changing.*
- *Jury awards might be changing because juries are doing a better job of calculating the amounts necessary to compensate plaintiffs and deter defendants' negligent behavior.*
- *The jury trial system might be "correcting" any unreasonable or untoward awards through posttrial processes.*

⁶See Peterson, *Civil Juries in the 1980s*, 1987.

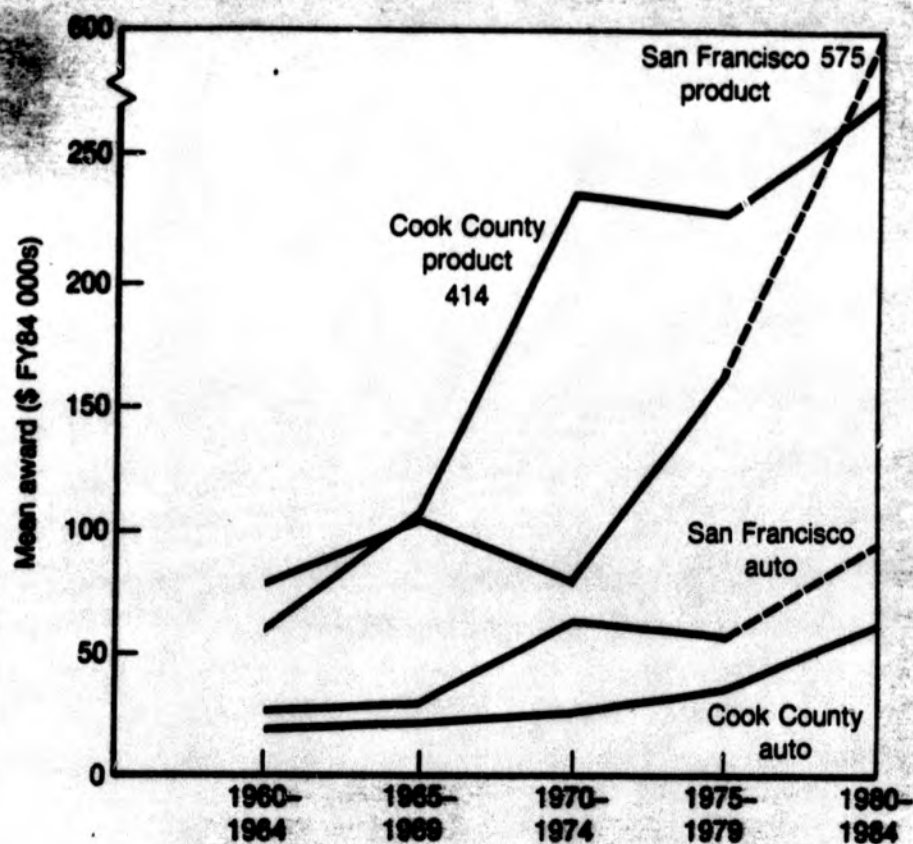


Fig. 3.5—Expected awards have risen

If any or all of these hypotheses hold true, we might conclude that whatever changes we observe in outcomes, juries are not "out of control."

Explaining jury behavior . . .

One way to figure out *why* jury awards are increasing is to perform multivariate statistical analysis that measures how awards vary in relation to characteristics of cases, plaintiffs, and defendants. The database the ICJ has assembled for San Francisco and Cook County is uniquely suited for such analysis. Here's what we have found so far:

Juries are now seeing cases that involve more serious injuries and larger medical expenses than cases tried at the beginning of the period. To the extent that this is true, juries are not necessarily behaving differently—they are being confronted with different circumstances.⁹

*... trying
different kinds of
cases*

After we take into account the increase in both the seriousness of the injuries and the size of medical expenses, juries are still awarding more money for serious injuries than they did 25 years ago.¹⁰

*... awarding
more dollars for
serious injuries*

Our analyses show that juries are likely to award substantially more money in a product liability, malpractice, or work injury case than in an auto accident case for an injury of the same degree of severity. And the "premium" awarded to these kinds of cases has been increasing over time. Juries also award more money when the defendants are institutions or organizations rather than individuals—the "deep-pocket" effect. Since many, if not all, product liability cases and malpractice cases involve institutional defendants, the "premium" effect and the "deep-pocket" effect are often confounded. Nevertheless, we can detect a separate, statistically independent effect for deep-pocket defendants, even in cases that do not involve products or malpractice.¹¹

*... responding
differently to
cases from
different "worlds"
of litigation*

Do juries respond to cases differently because they are "irrational" or "capricious?" The answer is: We don't know. Juries might have "irrational" sympathies for people who are hurt on the job or "irrational" prejudices against corporate defendants. Or it may be that juries presented with product liability, malpractice, or work injury cases feel that the defendant had a special kind of public duty or care that should have been exercised, and that the "premium" awarded is a kind of deterrent signal.

We need to conduct research on *how* and *why* jurors reach their decisions—based on interviewing real jurors or individuals who hear and decide "mock jury" cases—before we can decide which of these explanations (or some other) is

⁹See Peterson, *Compensation of Injuries*, 1984.

¹⁰See Peterson, *Compensation of Injuries*, 1984.

¹¹See Chin and Peterson, *Deep Pockets, Empty Pockets*, 1985.

*What happens
after trial?*

correct. The ICJ is currently exploring the possibilities for such research.¹²

The civil justice system has a number of mechanisms for reducing jury awards, including trial judge adjustments in awards, retrials, and reversals on appeal. A recent ICJ study compared jury awards and ultimate payments in a sample of recently tried cases to see whether these mechanisms were having their intended effect of "correcting" untoward awards. The study involved 900 cases, tried between 1982 and 1984 in Cook County, in San Francisco, and in a group of smaller California cities, including urban, suburban, and rural communities. The sample included a full range of verdicts, from million-dollar awards to defense verdicts.¹³

About 80 percent of the trial verdicts remain unchanged; however, the verdicts that were reduced involved some of the largest rewards, and the reductions were substantial. As Fig. 3.6 shows, the reduced cases had awards more than three times the size of the sample average, and involved reductions of almost half the original award.

The reductions increased with the size of the award. Table 3.1 shows the average award and the ratio of the amount paid to the award for four different case categories. For cases less than \$100,000, the average reduction was only 7 percent. However, the percentage reduction increases steadily with award size, and, for cases over \$1 million, it amounts to almost 40 percent.

This suggests that awards most likely to be viewed as "excessive" by critics are most likely to be cut substantially. However, trials involving deep-pocket defendants and/or product liability suits had smaller reductions.

¹²Molly Selvin and Larry Picus, *The Debate over Jury Performance: Observations from a Recent Asbestos Case*, The RAND Corporation, R-3479-ICJ, 1987.

¹³Michael G. Shanley and Mark A. Peterson, *Posttrial Adjustments to Jury Awards*, The RAND Corporation, R-3511-ICJ, 1987. See also Peterson, *Civil Juries in the 1980s*, 1987.

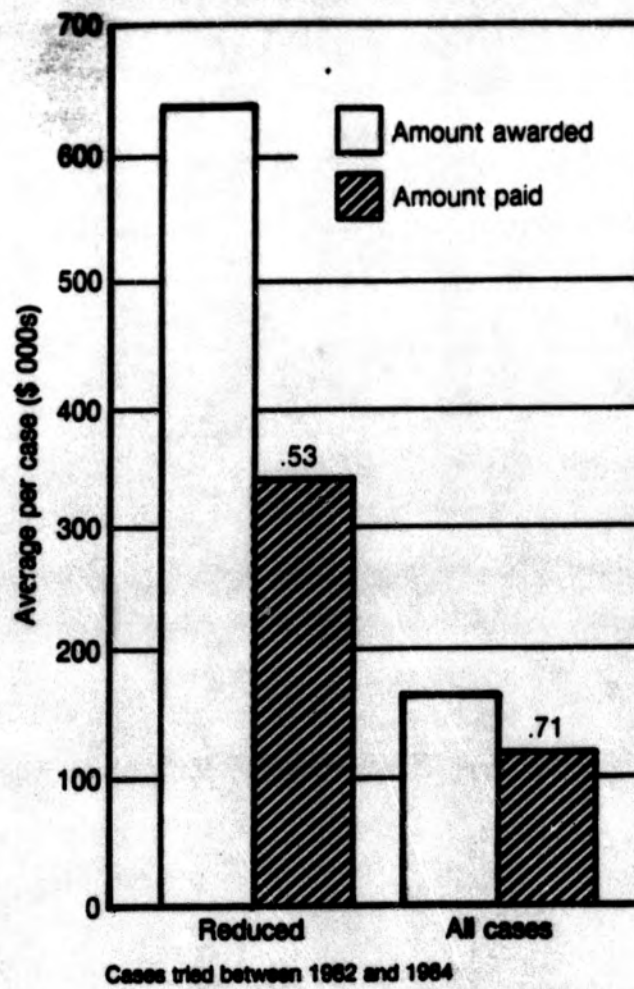


Fig. 3.6—Reduced cases involve large awards and significant reductions

Table 3.1

REDUCTIONS INCREASE WITH AWARD SIZE

Size of Award (\$)	Average Jury Award (\$000s)	Ratio Paid/Award
1-99 thousand	23	.93
100-999 thousand	314	.82
1-10 million	2,673	.68
10+ million	27,220	.57
All trials	161	.71

The bottom line

The answer to our initial question, Are jury awards stable or out of control? turns out to be complicated. It depends both on which world of litigation you look at and whether you are focusing on bottom-line results—jury awards—or the behavior behind them—jury decisionmaking processes.

- *Plaintiffs in auto cases involving modest injuries and expense continue to obtain modest awards and, at least in recent years, these awards generally hold after trial.*
- *Plaintiffs in product liability and malpractice cases are winning more frequently and obtaining higher awards.*
- *And deep-pocket defendants in product liability cases ultimately pay much, if not all of the awards against them, even after posttrial adjustments.*
- *Jury behavior seems more unpredictable, but this may simply be because we do not have a very good sense of why juries make the decisions they do.*

LITIGATION COSTS: HOW MUCH, TO WHOM?

"Litigation," says former Chief Justice Warren Burger, has become "too costly, too destructive and too inefficient."¹ Proponents of tort reform claim that the transactions costs of the system exceed the benefits provided in compensation to plaintiffs.

Perhaps the aspect of tort litigation that draws the most fire is the contingency fee. Critics complain that contingency fees, typically one-third of the award, are too high and encourage lawyers to take frivolous suits to court. Lawyers retort that contingency fees provide access to the courts for plaintiffs who cannot afford to pay hourly fees, and that the contingency arrangement is an appropriate way to cover the risks and expenses of lawyers, who receive nothing for their time when they do not obtain payment for their clients.

Although plaintiff attorneys get the most bad press, defense costs also draw their share of criticism. Defense attorneys charge by the hour, and there are no standards to suggest how many hours are appropriate for a case unless the defendants provide limits.

Unfortunately, there is no ready measure of the inherent reasonableness of the system's transactions costs. Especially when we focus on the tort system's goal of deterrence, we might encounter circumstances in which we find very high transactions costs acceptable. However, when we view the tort system as a compensation system, we would generally argue for costs that are lower, relative to compensation.

In any case, a first order of business is to determine how high the transactions costs really are and who is getting them. As with other basic issues in this area, the data are not readily available. Over the last five years, the ICJ has conducted a number of studies on the costs of litigation

*Transactions
costs—complaints
and rebuttals*

*Where the dollars
go*

¹The Wall Street Journal, May 18, 1986.

and the division of the payments.² Here are some aggregate numbers based on these studies.

- In 1985, the total expenditure nationwide for tort litigation terminated in state and federal courts of general jurisdiction was between \$29 and \$36 billion.³ This accounts for approximately 92 percent of all compensation paid in tort litigation.
- Of that total, \$16 to \$19 billion was spent for the various costs of the tort litigation system, not including the net compensation paid to plaintiffs.
- Plaintiffs were paid \$21 to \$25 billion in total compensation. After deducting their legal fees and expenses, which on average amount to about 30 percent of the total compensation, and the value of their time, they netted \$14 to \$16 billion in compensation.
- Defendants' legal fees and expenses totaled about \$4.7 to \$5.7 billion.

Figures 4.1, 4.2, and 4.3 disaggregate litigation costs for the three categories of cases that we have been examining: routine torts such as auto, higher-stakes cases such as product liability and malpractice, and asbestos cases as an example of mass latent injury torts.⁴

²James S. Kakalik and Abby Robyn, *Costs of the Civil Justice System: Court Expenditures for Processing Tort Cases*, The RAND Corporation, R-2888-ICJ, 1982; James S. Kakalik, Patricia A. Ebener, William L.F. Felstiner, and Michael G. Shanley, *Costs of Asbestos Litigation*, The RAND Corporation, R-3042-ICJ, 1983; J. S. Kakalik and R. L. Ross, *Costs of the Civil Justice System: Court Expenditures for Various Types of Civil Cases*, The RAND Corporation, R-2985-ICJ, 1983; James S. Kakalik, Patricia A. Ebener, William L.F. Felstiner, Gus W. Haggstrom, and Michael G. Shanley, *Variation in Asbestos Litigation Compensation and Expenses*, The RAND Corporation, R-3132-ICJ, 1984; Kakalik and Pace, *Costs and Compensation Paid in Tort Litigation*, 1986.

³We give a range of costs because we made two estimates. The first was top down, starting with the insurance industry's aggregate data on direct losses and expenses paid in 1985, adding self-insurance, and then deleting payments for claims that were not lawsuits. The second estimate was bottom up, starting with data from surveys of individual tort lawsuits, projecting the numbers to 1985, and deriving a national estimate by multiplying by the number of tort lawsuits terminated in 1985.

⁴Asbestos cost estimates are drawn from two reports dealing specifically with those cases: Kakalik et al., *Costs of Asbestos Litigation*, 1983, and Kakalik et al., *Variation in Asbestos Litigation Compensation and Expenses*, 1984.

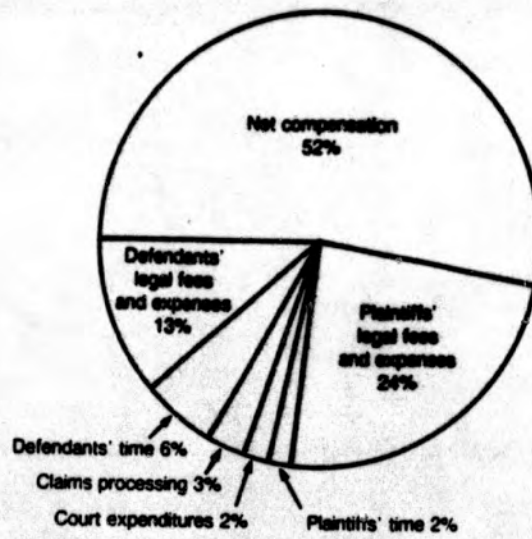


Fig. 4.1—Allocation of total auto tort litigation expenditures, 1985

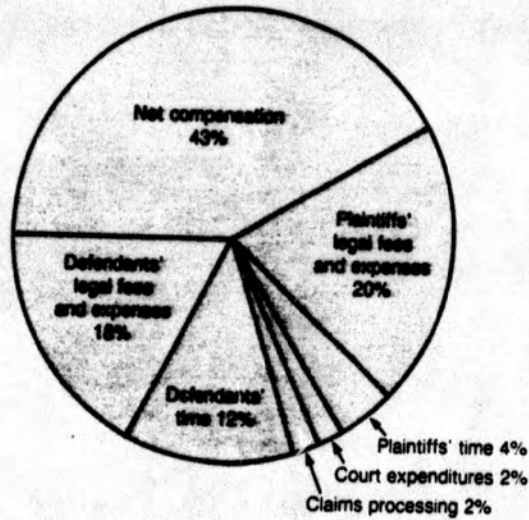


Fig. 4.2—Allocation of total non-auto tort litigation expenditures, 1985

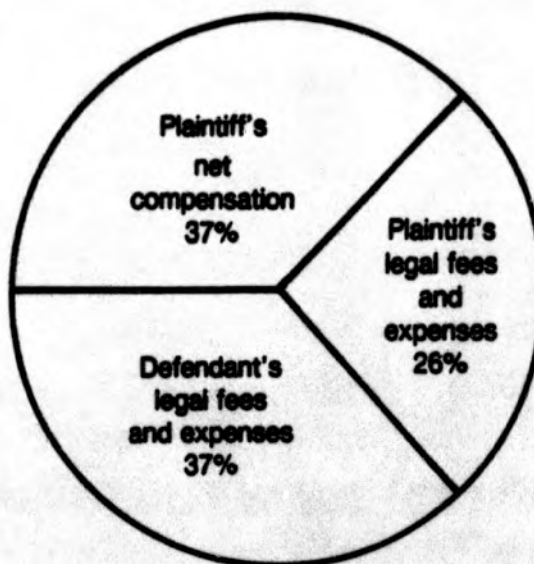


Fig. 4.3—Allocation of per-claim expenditures for asbestos claims closed before 8/82

Effect of case complexity

As we might expect, as the complexity of the case increases, plaintiffs net less and less in compensation. As the summary in Table 4.1 shows, plaintiffs' legal fees and expenses are a relatively stable proportion of expenditures, but defendants' legal fees and expenses increase in more complex cases.

Growth rate for transactions costs

Earlier we noted that the annual growth rate for the amount of tort litigation was approximately 3-4 percent. However, the growth rate in expenditures for the tort system has been higher. Between 1980 and 1985, the average growth rate in insured defendants' average legal fees and expenses paid per claim was about 6 percent for auto (i.e., less than the rate of inflation) and 15 percent for other tort claims.

Table 4.1

ALLOCATION OF LITIGATION EXPENDITURES: SUMMARY
(In percentage of totals)

Type of Case	Defendant Legal Fees	Plaintiff Legal Fees	Net Compensation to Plaintiff
Auto	19	26	52
Non-auto	30	24	43
Asbestos	37	26	37

Our snapshot of litigation in 1985 shows that the costs of litigation consumed about half of the \$29 to \$36 billion dollars that were spent on litigation. When we disaggregate these costs, we see that in more complex cases (non-auto torts) the costs of litigation were higher. In the case of asbestos claims, the only mass latent injury cases for which these data have been assembled, litigation costs constituted almost two-thirds of the total per-claim expenditures.

In sum . . .

THE STORY BEHIND THE STATISTICS

The emerging worlds of tort litigation

We now understand why the statistics bandied about in the insurance crisis debate generate more confusion than enlightenment. The characteristics we want to examine—for example, growth rates or award amounts—trend up in one kind of case, down in another. Aggregate statistics make it impossible to detect sources of change or stability. In many cases, statistic-bandiers on both sides of the crisis are right—they are just describing different parts of the system.

When we disaggregate the numbers, we can detect clear differences:

- Routine personal injury torts such as auto cases are growing slowly in frequency and costs, and their outcomes—inflation adjusted—have not changed much over the last 25 years.
- Higher-stakes torts such as malpractice and product liability are growing faster in frequency and costs, and their outcomes have increased dramatically over the past 25 years in the jurisdictions we have observed intensively, and substantially in the shorter five-year period for which we have national data.
- Mass latent injury torts, once identified, tend to explode in number, carry high transaction costs, and have highly uncertain outcomes.

We believe that these differences point to an important evolutionary process in the tort system that merits close policymaker attention. In Table 5.1, we characterize the three worlds of litigation that constitute important states in this evolution. Below we discuss these characteristics in more detail, drawing on our previous research and recent discussions with participants in the tort litigation process.

Routine personal injury torts

Auto accident cases epitomize this category. There is a huge volume of such cases, about half a million filed annually nationwide. Perhaps because they have been with us so long, there has been little recent change in the substantive law related to them since the adoption of no

Table 5.1

THE EVOLVING WORLDS OF TORT LITIGATION: CASE PROFILES

Auto and Other Ordinary Lawsuits	Product Liability, Malpractice, Business Torts	Mass Latent Injury Cases
• High volume • Stable law • Routinized • Increasing ADR • Modest stakes • Little deterrence potential • Slow growth in frequency, outcomes, costs	• Lower volume • Evolving law • Increasingly specialized • Heavy pretrial procedure • Little ADR • Large \$ potential per case • Deterrence is factor • Faster growth in frequency, outcomes, costs	• Concentrated in time and place • Problematic law • Small, highly specialized bar • Discovery critical • Procedural innovation • Enormous \$ stakes for parties • Deterrence is key issue • Highly uncertain in number, outcome, and costs

fault insurance provisions. Because of their high volume and the stability of law, it has been possible to routinize their processing and resolution. As a result, we have seen an increasing reliance on alternative dispute resolution procedures, particularly court arbitration programs, for these cases.¹

Most of these cases involve relatively modest injuries and small amounts of money, and the parties to the dispute are ordinary citizens rather than institutions. Except in cases of very serious injury, there is little basis for large awards,

¹For further discussion, see Deborah R. Hensler, "What We Know and Don't Know about Court-Administered Arbitration," *Judicature*, Vol. 69, No. 5, February-March 1986.

and the attorneys who handle them are not generally high-stakes litigators. Although the application of tort law to these cases is intended in principle to deter bad drivers, concerns about deterrence do not appear to motivate the attorneys who specialize in this area.

Because of these characteristics, auto lawsuits are not growing significantly. Increasingly, it appears, they are being settled elsewhere, in forums that produce stable, predictable outcomes. The use of alternative procedures and settlement mechanisms produces lower transaction costs than we observe in other tort litigation areas.

In sum, this world of tort litigation is the least problematic by most standards. It also remains the world in which the average citizen is mostly likely to become a participant.

*Higher-stakes
personal injury
torts*

Although these kinds of cases have received the lion's share of the attention in the recent tort debate, they are still relatively low volume by comparison with the auto cases.

But these cases differ from routine torts along many dimensions. The law with regard to product liability in particular has changed dramatically since the early 1960s with the adoption of strict liability—a principle that holds that manufacturers may be held liable for any injury that their products might cause. This expansion of the principle of liability has enabled more plaintiffs to bring suits. It has also provided the opportunity for the development of a highly specialized, well-capitalized corps of litigators on both the plaintiff and defense sides.

The stakes in these cases are usually higher than in auto torts, and because the law is perceived as volatile, the outcomes are often uncertain. To many scholars, attorneys, and litigants, deterrence is a central concern: The system has a clearly stated interest in trying to deter manufacturers from making bad products; to deter doctors from practicing bad medicine; to deter businesses from trying inappropriate practices. Plaintiff attorneys may be spurred by these concerns to invest substantial resources in developing cases. And because defendants—particularly manufacturers—may have an incentive to deter further suits over the same product, defending against these cases, rather

than settling them, is particularly attractive. As a result, pretrial discovery—with its associated costs in dollars and time—is a prominent feature of these cases. Alternative dispute resolution is not.

Because the evolution of the law in this area has expanded the grounds for bringing suits, it is not surprising that more suits are being brought. By their nature, these suits involve larger and more uncertain stakes than routine cases such as auto—the injuries are more serious, the defendants have more money, the plaintiff attorneys have invested more and stand to earn more. As a result, we observe higher and less predictable outcomes and higher transaction costs.

Mass latent injury torts are a special case of product liability torts, with special characteristics that justify treating them separately. Both substantive and procedural law in this area is evolving rapidly, and attorneys on both sides view the litigation process as problematic.² Pretrial maneuvering is extensive in these cases because the latency of the injuries produces knotty legal issues; discovery is usually prolonged and costly because attorneys must collect data over extended periods to substantiate charges that the manufacturer's product caused the injury. Because of the large number of claims, the rapid influx of cases into courts after the harm has been identified, and the characteristic geographical concentration of the cases, courts frequently experience overload problems that may lead to further delay and costs.

*Mass latent
injury torts*

Deterrence is seen as a critical issue in these torts. Indeed, concerns about deterrence have evoked missionary zeal on the part of some plaintiff attorneys. Defendants have been willing to invest huge amounts of resources because the trials may decide the future of their corporations.

Despite the fact that alternative dispute resolution procedures have not been widely adopted for ordinary product liability and malpractice suits, there has been considerable interest in innovative procedures for dealing with mass latent injury torts. We believe this interest stems

²See Hensler et al., *Asbestos in the Courts*, 1985.

from general agreement that the cost of processing these cases under the current system is excessive.

Mass latent injury torts are the most volatile world of tort litigation. Costs, dynamic legal environment, and the uncomfortable fit between these cases and the tort system conspire to make the number, outcome, and future costs of these suits highly uncertain.

*What the tort
evolution implies
for policy*

Unlike some of the statistical arguments used in the tort reform debate, the central policy implication of our discussion is clear: We need to know what part of the elephant we are patting. If we want to diagnose the system's ills and prescribe effective remedies, we must disaggregate the system. Researchers must ask sharper questions, target their inquiries, and look for appropriate data so that they do not make assumptions about one part of the system based on trends observed in another. Opinion leaders must be willing to consider the possibility that complex realities generate seemingly inconsistent data and ask what these data mean rather than rejecting them out of hand. And policymakers may need to consider more seriously specialized solutions tailored to special problems that characterize some torts, but not others. Most of all, we need to bring the perspective provided by the "three worlds" framework to bear on the current tort reform debate in the hopes of generating a little more light and a little less heat.

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