Settlement and Litigation: Of Vices Individual and Institutional

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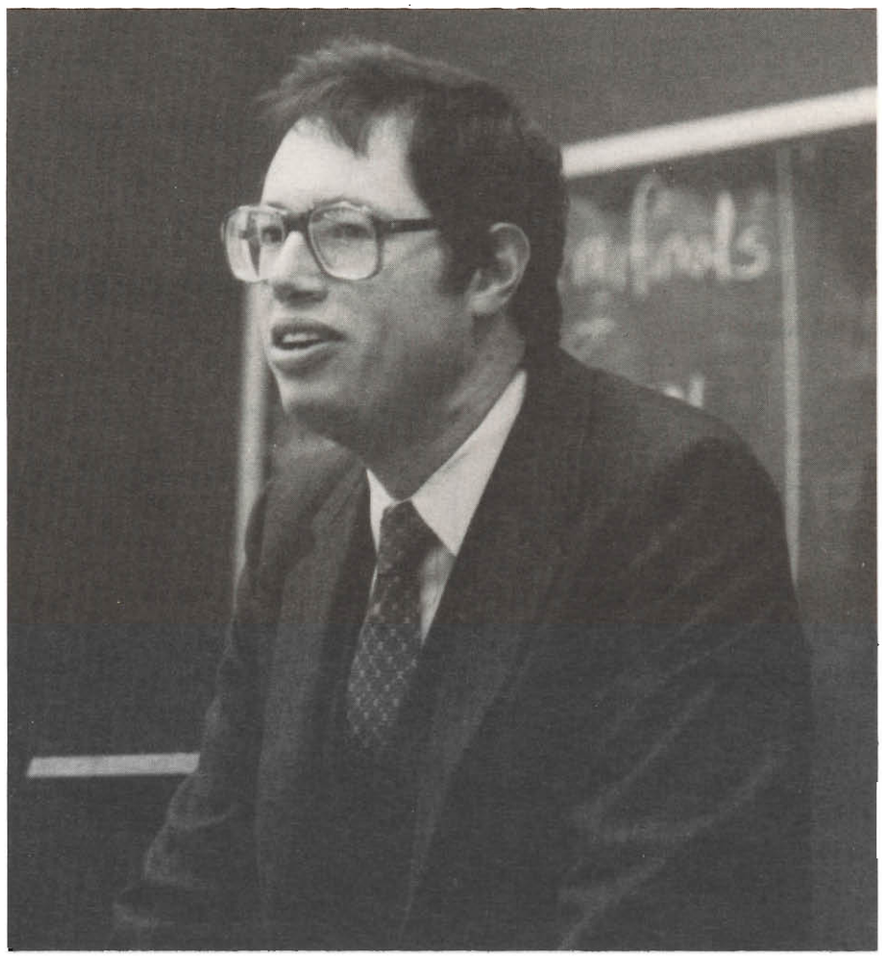
Amid the ebb and flow of intellectual fashion, one assertion steadfastly commands popular assent: people do not like lawyers. It is not that people do not like their own lawyer; he or she may be a fine citizen and a helpful counselor, nice to family and friends. Rather, lawyers as a class are regarded by the public at large as a necessary evil, as a harbinger of ill. Nowhere does the dislike for lawyers manifest itself more than in litigation. Even litigators made over into litigants share the popular dread. Their reasons are the same as everyone else's. Litigation arises when all informal means of settlement have failed. For a plaintiff it means that a stubborn defendant has left him no alternative but to sue. For the defendant it means that the plaintiff has marshalled the power of the state in aid of a cause that ought not to be pursued. For both it means that large sums of money will be spent to secure a bigger slice of a shrinking pie. One side must lose this struggle; often both do. Inject lawyers into the conflict, and normal modes of civility fail, as each party may use the other's ingratitude to justify his own



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questionable conduct. Early in teaching I received this advice from a shrewd and experienced lawyer. "You can tell the sign of a good deal—everyone leaves the room happy. You can also tell the sign of a good settlement—everyone leaves the room unhappy."

My purpose here is not, however, to belabor the known truth that litigation is not the road to contentment, but rather to pursue two lines of inquiry: first to seek an explanation for the rapid rise in the frequency of litigation, second to ask what, if anything, can be done about it. In discussing these issues some commentators have attempted to identify some larger change either in the social fabric or in personal mores that could in turn be translated into an increased propensity to litigate. The massive increase in litigation, and the bitterness it spawns, have been attributed to an emerging claims consciousness in the American public who now reject informal dispute resolution in favor of litigation; to the rise of sensationalist journalism; to an increased level of greed fed by the profit system; or inversely to the decline of religion and the loss of faith. Alternatively, Chief Justice Burger has fastened a large portion of the blame upon lawyers themselves, for their failure to act as "healers" in civil litigation. The illness having been diagnosed, the remedy remains uncertain. Who can restructure society at large in order to control the excesses of litigation? And who can remove from lawyers the aggressive instincts that are part and parcel of their craft?

I do not want to deny that the enormous increase in the level of litigation over the past generation has social causes as well as social consequences. Nor do I want to deny, as President Derek Bok of Harvard University has suggested in a well publicized report, that this upturn in legal business has diverted far too great a proportion of national wealth and talent to legal pursuits, to the exclusion of science, arts and business (I will not add government to the list). But I do want to argue that the phenomenon is often misunderstood. Bok is wrong to see the increase in litigation as a symptom of an irreversible social decline. The Chief Justice is wrong to locate the heart of the problem in the aggressive instincts of lawyers.

The sources and the cure of the present problem may have something to do with culture in the round and the character of the legal profession in particular. But the more powerful reasons have more modest and prosaic origins. The current situation is the regrettable but predictable outcome of a large set of discrete social choices about the substantive and procedural rules governing litigation. These choices are often made by courts or legislatures. The net effect of the current rules has been to drive a wedge between private gain and the social good derived from litigation. As the rules are now structured, individual plaintiffs may gain from suit while the society at large will lose. As they can initiate the process unilaterally, defendants must then take whatever private steps will minimize their losses from suit. The repeated application of the current legal rules will leave most people (save lawyers) worse off than they otherwise would have been. If the rules were restructured to remove the wedge between private and social gains, private parties would face higher costs and realize smaller gains from litigation. The social problem of excessive litigation would shrink in size, even if the instincts of lawyers remained as aggressive as they are today.

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The central question of governance has always been: what institutional arrangements harness the best that individual self-interest has to offer while at the same time curbing its excesses? The common law rules of procedure were not built on the assumption that private litigants acted with a disinterested benevolence toward the opposition. On the contrary, the concern was that clever lawyers could prevail not on the merits of the litigation but on technical points, surprise, or even perjured testimony. Indeed, many of the old rules, like those forbidding parties to testify on their own behalf, are largely explicable against a backdrop of pervasive perjury in testimonial evidence, far beyond the capacity of cross-examination to reveal. The old story of the experienced English barrister tells a good deal about the foibles of litigation: "In my youth," the barrister said, "I lost some cases that I should have won. Now that I am an experienced hand, I win some cases that I should lose. Which goes to show that justice is done in the long run." Self-interest, legal intrigue and worse have long been with us. How could anyone expect otherwise? The Romans had a rule that any litigation between partners automatically terminated the partnership. Once the bonds of trust are gone, a relationship predicated upon trust cannot survive. Litigation occurs because informal methods of compromise and adjustment have broken down between parties unconcerned about maintaining long-term relationships. Litigation is a slice of life in which self-interest is the norm. The legal system must answer the perennial question of the political philosophers: How can that self-interest be harnessed and controlled?

The answer here surely does not lie either in praise or condemnation of the adversary system. Every lawsuit is adversarial if it is not collusive. The question is how to modify the incentive structures in which the adversaries operate. In this country the rules as they are now fashioned guarantee high expenditures in litigation. Once parties are involved in litigation, they do not act irrationally. Quite the opposite is true. There may be individual cases of self-destruction, but most cases settle short of litigation precisely because both parties can gain by reducing their litigation costs and eliminating the uncertainty of all-or-nothing judgments. Indeed, every serious study of which I am aware indicates that once the rules are taken as a given, the behavior of the

parties conforms in the aggregate to the predictions of classical economics.[1] The central tendency is for litigants to maximize their private gain, net of their private costs.

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Moreover, that tendency is not upset by the occasional account of self-destructive behavior. The larger institutional agenda is set by institutional and not anecdotal evidence.[2] The critical questions are systematic, not personal.

Let us start by examining one procedural rule: under the American rules of voir dire parties are allowed to dismiss potential jurors for cause. They are also allowed to question potential jurors extensively to see if cause exists. Any responsible lawyer can tell his client that a thorough voir dire could pay large dividends if it skews the jury in his favor. The catch is that the same point is true for both sides. Each will examine at length in order to remove the jurors it dislikes most, carefully preserving peremptory challenges for the right moment. In the end their efforts largely cancel out. One could get a jury with about the same degree of partiality with far lower costs under the traditional English system (itself now under attack) in which the judge conducts voir dire and confines his attention to relations by blood, marriage and financial interest. The occasional question by counsel may be put to the prospective juror through the judge. Neither side can spend enormous sums of money even if it has them. The level of jury bias will be no greater than under the American rules, and perhaps less where skill of counsel or financial resources are unequal. Here the shape of the legal rules has increased the costs of the American legal system.

Consider next an even more fundamental point of procedure: the American rules of cost providing that each person should bear his own expenses in litigation, except under rare circumstances when the principal claim or defense is wholly frivolous. The rule in question contrasts sharply with the English and Continental procedures in which the party who wins is reimbursed his costs. Indeed, a feature of German practice carries the basic principle to its sensible conclusion. Suppose that a plaintiff claims $10,000 and receives judgment for only $1,000. The plaintiff has won, but only 10 percent of the case. He is then required to reimburse the defendant for 90 percent of the costs, receiving in exchange only 10 percent. The net effect is that the defendant gets 80 percent of his costs from the plaintiff, who of course bears his own in full. The fabulous *ad damnums* of American complaints cannot long survive a rule that exacts its heavy toll for an erroneous estimation of either claim or defense. There is no question that strict rules of cost will influence behavior. Under the present system any run-of-the-mill lawsuit may in principle yield an enormous verdict, as in the famous $125,000,000 jury verdict entered against the Ford Motor Company for its Pinto in a routine crashworthiness case, later reduced to a still very substantial $3,500,000.[3] Once the *ad damnum* gives the outer limit of the loss there is no reason for a defendant to commit millions of dollars in order to save thousands. But the effects of sound rules on cost go deeper. Since most private parties are averse to risk and fear uncertainty, a rule which makes the costs of litigation follow the outcome of litigation will reduce the level of litigation, and encourage quicker settlement of the litigation that does take place.

The incentives under the American system are quite the opposite of those at work in the Continental systems. Now the costs in litigation that are inflicted on the other side cannot as a practical matter be brought back upon the party who imposes them. Every good trial lawyer knows the proper way in which to handle discovery. It is to make a set of perfectly routine and inexpensive requests that impose intolerable burdens on the other side. Discovery is a way to punish the other side for resistance, to wear the opposition down until settlement becomes a form of surrender. But the catch again is that the aggressor with the first round of interrogatories is the victim of the second. Let the extent of damage awards increase, and there is more for both sides to gain from strategic behavior, and the creative use of the legal imagination. In order to quell this abuse one might think that some efforts to place limits on discovery would seem appropriate. But since the 1938 adoption of the Federal Rules of Civil Procedure, the American system has gone in quite the opposite direction. Discovery is routinely done on service of notice to the opposite party and outside of the direct supervision of the court. The scope of the examination is exceedingly broad because the formal rules of evidence, and the general requirement of relevance, do not bind the parties at this stage of the proceedings. Discovery can be conducted on any issue calculated to lead to admissible evidence. The efforts to control abuse against frivolous

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[1] *See, e.g.,* Patricia Munch Danzon & Lee A. Lillard, *Settlement out of Court: The Disposition of Medical Malpractice Claims,* 12 J. Legal Stud. 345 (1983); William M. Landes, *An Economic Analysis of the Courts,* 14 J. Law & Econ. 61 (1971); John P. Gould, *The Economics of Legal Conflicts,* 2 J. Legal Stud. 279 (1973); George L. Priest and Benjamin Klein, *The Selection of Disputes for Litigation,* 13 J. Legal Stud. 1 (1984).

[2] *See, e.g.,* Timothy J. Muris, *Rules Without Reason—the Case of the FTC,* Regulation Sept/Oct 1982 at 20, on the need for systematic evidence in agency rulemaking. The same point applies to any effort to understand institutional behavior. Reliance on anecdote guarantees biased information.

[3] Grimshaw v. Ford Motor Co., 119 Cal. App. 3d 757, 174 Cal. Rptr. 348 (1981). For critical commentary, *see* David G. Owen, *Problems in Assessing Punitive Damages Against Manufacturers of Defective Products,* 49 U. Chi. L. Rev. 1 (1982).

requests depend upon protective orders sought by the deponents, which are obtainable only at the discretion of the trial judges that is only rarely exercised on a case-by-case basis.

Those who support the modern discovery procedure claim that it allows persons to develop legal theories based upon the facts. Yet no amount of data will develop a theory of a case unless the applicable substantive principles are themselves independently understood. Discovery is also supposed to allow each side to probe the strengths and weaknesses of the adversary's case. Unfortunately, this benefit comes at a very high cost, for while it may yield useful information, it is also fraught with dangers. Each side can ransack the files of the opposition, or tie down its key personnel in depositions, all as a lever to secure a more attractive settlement. These costs may not have been apparent at the formation of the federal rules, which were drafted to cover the ordinary personal injury suit arising out of an intersection collision, rather than the complex business and statutory litigation that has become standard fare today. The cost of unsupervised discovery activities depends heavily on the nature of the underlying dispute. Though it may be attractive to let the facts speak for themselves in automobile cases, a bit of structure is more welcome when litigation examines, say, the hiring practices of a firm for a period of decades, when none of the Aristotelian unities of time, place, and action define the subject matter of suit.

The relationship between procedure and subject matter in litigation deserves greater emphasis than it generally receives. The shift in procedural laws alone antedates much of the recent growth in litigation and cannot therefore solely account for it. But these procedural reforms provided a fertile ground for the onslaught of substantive innovations. One of those changes, undramatic but critical, has already been mentioned: the level of damages awards has increased far more rapidly than inflation. As the stakes of the game get larger, the resources devoted to playing it have increased as well. However, two other points are worth some analysis here. The first change concerns the relative decline of *per se* rules based on overt behavior with the parallel rise of substantive tests that turn either on the reasonableness of conduct or the motive of the parties. The second involves a change in the number of parties to the litigation. I shall discuss the points briefly in turn.

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One characteristic feature of many common law rules was that they gave to private parties "bright lines" around which they could organize their behavior, both before and after litigation. A bright line for primary conduct indicated what conduct could be undertaken without fear of legal suit, and what conduct necessarily brought legal action in its train. The party who trespassed could be liable for entry; the party that did not trespass could not. A single fact was often sufficient to determine legal liability in the routine cases. The uncertainty generated elsewhere (as in killing or wounding trespassers in defense of property) occurred with sufficient infrequency as not to overwhelm the legal system as a whole. As most ligitation involved routine cases, the scope of discovery was thereby reduced while the certainty of outcomes was increased.

In sharp contrast, modern rules tend in quite the opposite direction since they ordain complex balancing acts to determine liability. In part this tendency is justified by the belief that this fine tuning is necessary in order to eliminate individual acts of injustice that are not caught by the general rules. But that hope is often delusive. Any refinement in legal rules will increase their error in application as well as their costs of administration; at some point the benefits of precision are overwhelmed by their costs. Perfect justice can only be done at an infinite price—which is another way of saying that it cannot be done at all. A willingness to entertain some tradeoff between simplicity and aspiration is not only the counsel of prudence, it is also a precondition for justice in the broad run of cases. Nonetheless, the judicial taste for fine tuning has lately proved irresistable. Let me give three examples drawn from different areas of the law.[4]

The traditional body of property law adopted a powerful version of the *ad coelum* rule. So long as the conduct of one person did not invade (directly or by its physical consequences) the land of another, no cause of action followed.[5] Applied to the question of light, the uniform rule was that it was never tortious to block the light of a neighbor, even if (as happened in the famous dispute between the Fontainebleau and Eden Roc hotels) it blocked the sunlight on a neighbor's swimming pool.[6] More recently, however, the preoccupation with solar energy has led some courts to rethink this old position and to adopt a legal standard (the word is too flattering) to determine when it is reasonable for one neighbor to block the light of another.[7] The reasons announced for the change stress that light is now used for

[4]There are also less important illustrations of an earlier vintage. A 1944 study of recovery for psychic injury concluded after a detailed examination of the medical evidence in the reported cases showed that "Taking all cases decided between 1850 and 1944, the net balance of justice would have been greater had all courts denied damages for injury imputed to psychic stimuli alone," given the rate of error in favor of plaintiffs. *See* Smith, *Relation of Emotions to Injury and Disease: Legal Liability of Psychic Stimuli,* 30 Va. L. Rev. 193, 284-85 (1944).

[5]*See, e.g.,* Edwards v. Sims, 232 Ky. 791, 24 S.W.2d 619 (1929).

[6]Fontainebleau Hotel Corp., v. Forty-Five Twenty-Five, Inc., 114 So. 2d 357 (Fla. App. 1959).

[7]Prah v. Maretti, 108 Wis. 2d 223, 321 N.W.2d 182 (1982).

energy purposes and not aesthetics, or that the social demands for land development are not as pressing as they once were. Whatever one thinks of these reasons, however, it seems very clear that a great deal more is left to the legal imagination under the modern formulation of the easement of light than under the old view, for virtually everything that touches on the relevant gains and losses to both sides is now fair game for discovery in litigation. A clean, certain rule is displaced by a confused and uncertain one. The costs and frequency of litigation can only increase, while the gains to the one litigant are more than offset by the losses to the other.

The point may seem small, but in fact it influences the relationships between neighbors in subdivisions across the country. Of greater importance, however, the retreat from fixed rules occurs everywhere throughout the system. Consider the recent developments in the law of wrongful discharge. At common law most agreements could be terminated at will by either side.[8] Again the delineation of rights was clear, and the scope for litigation minor: who wants to litigate the question of whether the employee was fired? Today this rule is limited in every direction. By statutory command it is undercut in cases where workers are dismissed for union activities or because of racial or sexual discrimination. And at common law it increasingly has been hedged in by rules that insist that all contracts may be terminated only for cause, no matter what the private understandings.[9] One consequence of this shift is that scope of litigation necessarily increases. Rights and duties turn less on overt conduct, and more on motive. Motive itself can only be established by indirect evidence, and this in turn invites discovery on every aspect of individual and firm behavior. Personnel records for the aggrieved worker are the obvious place to begin. But any resourceful lawyer can show the relevance of general firm policy; the treatment of comparable cases within the firm; the practices in other firms; the testimony of supervisors and employers; and the level of profitability of the firm, and of the industry at large. Thousands of pages of relevant information can be collected and motive may turn in the end on whether a supervisor provided the dismissed employee with a Christmas turkey. The social costs are enormous, for in addition to the costs of litigation, retaining one employee at the very least forecloses the hiring of a replacement. Where are the social gains that justify the pursuit?

One final example: today, actions for damages by automobile passengers against manufacturers who produced uncrashworthy vehicles are commonplace, even though they were virtually unknown before about 1968.[10] But what are the standards? Simple compliance with statute and custom will not exonerate the supplier, so reasonableness tests again become relevant to examine every stage of the design and the production process. It is difficult to attribute any improvement in product design to a set of legal doctrines that are so amorphous and indeterminate as to be utterly useless in the planning process. Indeed, much the same can be said about most of products liability law. Shortly after its well publicized bankruptcy, Manville Corporation published an advertisement in which it noted that it had tried the issue of liability in five asbestos cases in the same court room before five different juries.[11] The verdicts, all on the same evidence, varied from no liability to punitive damages. How does anyone respond to such conflicting signals? When this lack of clear substantive rules is linked to the modern procedural devices, the result is inescapable: an increase in the frequency and severity of litigation.

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The second major shift in substantive rules concerns the number of parties that may be joined in a single lawsuit. In principle, the minimum number of parties is two. Two is also the ideal number because the complexity of litigation increases exponentially with the number of parties. In many cases, as with suretyship litigation, multiple party suits may be unavoidable. But today the changes in underlying substantive theories positively invite a proliferation of parties. Modern rules on joint and several liability allow free suits between codefendants where the jury has broad discretion in determining the percentage of loss borne by each. Furthermore, theories of market share liability accepted in some states now allow an injured party who cannot identify the supplier of a given drug to sue all the firms that produced it.[12] The

[8] *See, e.g.,* Payne v. Western & Atl. R.R. Co., 81 Tenn. 507 (1884).

[9] *See, e.g.,* Monge v. Beebe Rubber Co., 114 N.H. 130, 316 A.2d 549 (1974).

[10] The seminal case in the line is Larsen v. General Motors, 391 F.2d 495 (8th Cir. 1968), where the defendant's Corvair was said to be defective in that head-on collision directed the steering column into the plaintiff's head. On remand at trial the defendant won the case, contending that the plaintiff would have sustained a much more serious injury had the steering column struck him in the chest. See Bowman, *Defense of An Auto Design Negligence Case,* 10 For the Defense No. 5 (1969).

[11] N.Y. Times, Aug. 27, 1982., § D, at 3.

[12] *See, e.g.,* Sindell v. Abbott Laboratories, 26 Cal. 3d 588, 607 P.2d 924, 163 Cal. Rptr. 132 (1980). Since then even more exotic forms of liability have been adopted. *See, e.g.,* Collins v. Eli Lilly Co., 342 Wis. N.W.2d.37 (1984). adopting what looks like a theory of "risk creation" in which any company in the market can be held liable for DES injuries because of its alleged overall responsibility in bringing the product to market, wholly without regard to its market share. Liability between producers in the injury is again a function of an elaborate and indeterminate set of principles of apportionment. The decision reads as if administrative costs were a free good.

relaxation of the rules for class actions, permissive joinder, and other procedural devices increase the likelihood that any given lawsuit will be a multi-party affair. Perhaps the best illustration of this is the current litigation over the proper construction of the insurance policy language in the asbestos coverage dispute. The relevant text of the policy is only several paragraphs long.[13] Yet the current litigation in California has produced discovery orders against every insurance carrier in the litigation, costing millions of dollars to answer.[14] Simultaneous depositions now take place daily in the elusive search for the original contractual intention, when every piece of past conduct by every party may lead to relevant or admissible evidence. The attractions of the parol evidence rule, and the constraints it places on extrinsic intent evidence, have never seemed greater. A close reading of the document is much cheaper and probably more accurate.[15]

The result of all this seems clear. Substantive rules first allow the number of relevant parties to proliferate; thereafter they make the liability of each rest upon uncertain standards. The impact on litigation is as expected: these rules create incentives for its increase. In some of these cases added to the system, the costs in litigation may be justified by the superior social outcomes that they produce. But as the costs of litigation are in themselves deadweight social losses, the improvement they make in the human condition must be very large to justify their expense. Here the path of reform is to undo much of the needless complexity of modern litigation. Yet this can only be done by the legal profession that itself is the major beneficiary of the modern changes, each of which may have appeared commendable standing alone, but which are oppressive in combination. Good procedural rules can serve as a welcome break on complex substantive legal theories. Sound substantive rules can reduce strains on unsound procedural rules. The elimination of personal vices is quite beyond our power. But complex substance and cumbersome procedure are institutional vices for which cures are both necessary and possible. ■

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[13]The key provision states: "[The insurer] will pay on behalf of the insured all sums which the insured shall be legally obligated to pay as damages because of bodily injury or property damage to which this policy applies, caused by an occurrence." " 'Bodily injury' means bodily injury, sickness or disease, sustained by any person which occurs during the policy period, including death at any time result therefrom."

[14]The case, still mired at the trial level, is styled "Judicial Counsel Coordination Proceeding: Asbestos Insurance Coverage Cases no. 1072." It involves about 100 insurers and 75 manufacturers.

[15]It does not augur well, however, to note that to date there are five separate opinions on the proper meaning of the standard clause, each of which has adapted a different construction. The details of which are not relevant to the central point.