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SCHIFF'S

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The Horror of 'Excessive Lawsuits'

Legal Reform

You've heard it before. The legal system is out of control. The plaintiff's bar is ruining America. If we don't get legal reform, terrible things will happen: businesses will go bust or go elsewhere; jobs will be lost.

Insurers have railed against the current system. Recently, the CEO of a colossal international insurance-and-financial-services company called the plaintiff's bar a group of "terrorists." This CEO's company is deeply involved with the U.S. Chamber of Commerce in a campaign to change state laws and elect business-friendly judges.

Before proceeding, let's ask a question: Is the legal system out of control?

Certainly there are abusive and stupid lawsuits and ridiculous verdicts. There are also corporate criminals—armed with big law firms—that are never held accountable for their actions. Nevertheless, a review of statistics and papers put out by opposing sides of the legal-reform issue does not lead one to the inexorable conclusion that the whole system is a one-sided mess.

The Institute for Legal Reform, an affiliate of the U.S. Chamber of Commerce, disagrees. Since 2000 it has spent $100 million on lobbyists, "voter education," and advertising in an effort to influence legislators and elect judges who are unlikely to rule in favor of plaintiffs. This year, the Institute's annual budget is more than $40 million.

On Tuesday the Institute rolled out its new national advertising campaign. The hard-hitting ad, shown on this page, is being run in *The New York Times*, *The Wall Street Journal*, *The Washington Post*, *The Washington Times*, and other publications.

"It destroys your jobs. It raises your taxes. It takes your money. And it's all legal," declares the ad, which ranks state legal systems from best to worst. The ad delivers a message that's supposed to scare the bejesus out of you: "Excessive lawsuits cost every American $809* a year," (the asterisk after $809 refers the reader to fine print citing a Tillinghast-Towers Perrin study).

Tillinghast's 29-page study, "U.S. Tort Costs: 2003 Update–Trends and Findings on The Costs of the U.S. Tort System," can be found on Tillinghast's website. It does *not* conclude that the cost of lawsuits or the tort system is excessive.

The study—written by Russ Sutter, a principal at Tillinghast—provides estimated figures for the cost of the U.S. tort system each year since 1950. The study, which was first published in 1985 and has been updated five times, compares estimated tort costs with various economic indicators over time.

Tillinghast estimates that the total cost of the U.S. tort system in 2002 was $233 billion, or $809 per citizen. This figure is derived by multiplying insurance-industry "earned" liability premiums by the "combined ratio" for these lines. Thus, the "cost" includes insurance-company expenses for commissions, advertising, general and administrative, underwriting, claims handling, paid and *incurred* claims, and the cost of defense. The 2002 figures are $166 billion for liability, $25 billion for medical malpractice, and an estimated $43 billion for self-insured tort costs. Sutter does not in-

Don't believe this insurance-industry sponsored ad.

clude costs for no-fault or workers' comp.

Because the study's annual tort "cost" is based heavily on insurance companies' estimates for *incurred* losses, the cost for any given year—or change in cost from year-to-year—should not be considered a precise figure. (Sutter concurs.)

Incurred losses include insurance companies' estimates of claims that will be paid in the future as well as reserve adjustments for previous years' losses. If the insurance industry takes a $25-billion reserve charge in 2004, would it be fair to say that the cost of the tort system increased by $25 billion in 2004? We think not. On the other hand, a look at Sutter's figures for tort costs over a long period—since 1950—provides a useful perspective.

Tillinghast's study is not definitive. One can make a good case that earned premiums—instead of incurred losses—provide a more accurate representation of the long-term cost of the tort system. The total of earned premiums is a precise figure rather than an estimate. Insurance companies are, presumably, charging premiums that over time not only cover their costs but provide some profit. Because the insurance-industry hasn't reported an underwriting profit in the relevant liability lines since 1979, using the "combined ratio" as a multiplier (Tillinghast's method) produces a cost that's 17% higher than earned premiums.

The Institute for Legal Reform refers to Tillinghast's study when it asserts that "excessive lawsuits cost every American $809 per year." We asked Sean McBride, the Institute's vice president for communications, how his organization determined that tort costs are "excessive." (The Tillinghast study does *not* say that lawsuits or tort costs are excessive.)

"It's our belief that the vast majority of tort costs are for frivolous and excessive lawsuits," McBride said.

Tillinghast's study estimated the *total* cost of the tort system. It includes auto-liability claims, products liability, general liability, awards for economic loss and for non-economic loss (i.e. pain and suffering), claimants' attorney fees, defense costs, insurance-company sales-and-administrative costs, and a profit factor that's built into insurance pricing. How did the Institute for Legal Reform conclude that every dollar spent was "excessive"?

It turns out that the Institute does not have any calculations or statistics to back up its assertion. McBride reiterated that tort costs were "excessive" because of "the number of meritless or frivolous lawsuits." That number, according to his organization, is 100% of lawsuits. "It's our belief that Tillinghast's study represents the best available data," McBride said.

It is reckless for the Institute for Legal Reform to cite Tillinghast as the basis for its contention that "excessive lawsuits cost every American $809 a year."

"They've mischaracterized" our study, says Tillinghast's Sutter. "The total cost of the *system* is $809 per citizen. We don’t make a value judgment; we’re just trying to keep score.”

The Institute for Legal Reform, which is supported by big business and insurance companies, has no basis for its figures. Furthermore, there are those who strongly disagree with some of Tillinghast’s methods. Robert Hunter, director of insurance for the Consumer Federation of America and former Texas insurance commissioner of insurance, believes that Tillinghast has calculated inflation-adjusted per-citizen tort costs incorrectly. Tillinghast states that per-citizen tort costs (adjusted for the change in the CPI) increased from $716 in 1990 to $809 in 2002.

An analysis by Americans for Insurance Reform criticizes Tillinghast for using the general rate of inflation (changes in CPI) rather than the rate of *medical* inflation, which has been higher. “The bulk of tort claim payouts are to cover injuries to people through recompensing them for their medical expenses,” states the analysis. If Tillinghast had adjusted its figures accordingly, contends Americans for Insurance Reform, inflation-adjusted per-citizen tort costs would have declined from $914 in 1990 to $809 in 2002.

“We have the greatest system in the world,” says Hunter, who’s an actuary, “and it’s really inexpensive. Sure it could be improved, but you don’t throw it away, and attack it in ways that are unrealistic. The big corporations and the insurance companies are getting their way with government. The only thing that stands in their way is lawsuits. They see it as the last remaining obstacle.”

Jason Adkins, of the law firm Adkins, Kelston & Zavez, does not see a system filled with frivolous lawsuits. “The world according to the Chamber of Commerce is one where victims have no rights,” he says. “It takes real gall to advocate against victims at a time when stories of corporate abuse at the highest levels are now on the front pages of our daily newspapers.”

For its part, *Schiff’s* is against frivolous lawsuits and for compensating those who have been injured, wronged, or abused.

The Institute for Legal Reform will have spent close to $150 million by the end of this year in its battle against “excessive lawsuits,” which its backers contend are threatening the very foundation of the American economy. Yet it can’t provide statistics to support its thesis.

Insurance companies that align themselves with the Institute’s unsupported, scare-tactic misinformation should be ashamed of themselves. ■

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