Factors Likely to Influence Tort Litigation in the European Union

Joan T. Schmit

Department of Actuarial Science, Risk Management & Insurance, School of Business, University of Wisconsin-Madison, 5194 Grainger Hall, 975 University Avenue, Madison, WI 53706, U.S.A.
E-mail: jschmit@bus.wisc.edu

As the European Union moves towards harmonization in a variety of business, political, and regulatory settings, an opportunity exists to influence the form of tort liability found in these nations. The opportunity should not be missed, with rising concern that U.S. influences will set into motion costly litigiousness, particularly as EU member nations pull back on the level of social programmes available to cover costs typically included in tort claims. To assist policymakers in their deliberations about European Union tort directives, this paper provides discussion of the frequently cited key differences between the U.S. tort systems and what is found in most EU member nations. The discussion is focused on available evidence regarding the influences of these differences as well as important areas of future research. The most important areas seem to be (1) the need to enforce European Law when no defined regulatory body exists for this purpose; (2) the connection between government social programmes and the need for tort liability compensation; (3) and the influence of rules governing payment of legal costs and lawyer fees.

The Geneva Papers (2006) 31, 304–313. doi:10.1057/palgrave.gpp.2510075

Keywords: tort litigation; contingency fees; common and civil law

Factors Likely to Influence Tort Litigation in the European Union

As the European Union (EU) moves towards increasing harmonization in business, political, and social arenas, numerous questions and issues become relevant. One important issue is the shape of legal rules to govern tort law, including liabilities arising out of accidents involving motor vehicles, products, pollutants, and medical treatment. For purposes of developing harmonized tort liability rules that best meet policymaker objectives, cross-national comparisons of current systems become useful. Comparisons of experiences with variations in procedure, damages, and other aspects of civil (here reference is made to “tort”) liability systems allow better understanding of the influences those characteristics yield on participant behaviour and administrative costs. For example, some systems permit assessment of non-monetary compensation while others do not. The varied approach to non-monetary compensation permits consideration of how their availability affects outcomes.

While member-country experience is critical in the evaluation process, consideration of outside systems, particularly that of the U.S. which has become notorious for its tort litigation process, also is seen as informative. A further advantage of considering the U.S. experience is that far more data have been collected there and can be used for greater understanding of behavioural responses to various system characteristics. The U.S. approach, therefore, will be used as a foundation upon which analysis can be

conducted for purposes of developing proposals for an EU-harmonized tort liability system.

The purpose of this paper, therefore, will be to present comparisons and contrasts between the U.S. and EU systems, particularly focusing on qualities generally considered relevant in fuelling litigiousness in the U.S. While presenting comparisons and contrasts between EU and U.S. systems, discussion of variations across EU countries also will be provided. Member nations are in a position to influence the shape of the European Union's tort liability with the benefit of extensive experience from within their own borders but importantly also from the extensively developed U.S. system. Proactive involvement in the process appears valuable.

The United States patterns

As readers of this journal are aware, the U.S. is known worldwide as a litigious society. A recent report on product liability law by the International Academy of Comparative Law¹ refers to the United States and "The Rest of the World." The obvious point is that despite many variations across other nations, when compared with the differences between any nation and the U.S., those disparities were virtually unobservable. Data on the frequency and severity of product liability litigation offer support for this point. For instance, the number of product liability claims filed in U.S. federal courts grew from 2,393 in 1975 to 32,856 in 1997. The claiming rate has declined in recent years and now stands at approximately 15,000 per year.² Japan, in contrast, recorded a total of 200 product liability judgments for the entire period between 1945 and 1994.

The number of product liability claims in EU countries is difficult to ascertain. According to the Comparative Law Report, the number may be zero in some jurisdictions, although importantly, the authors of the report also point to procedural requirements in the U.S. that force a majority of claims to be filed. Outside of the U.S., these same procedural requirements do not exist and claims typically are not filed prior to settlement. Germans, for example, are said to make numerous claims, but due to the procedural system within which they operate, these claims generally are not recorded as legal cases. Litigation rates, therefore, are not exactly comparable. The difference between EU member country and U.S. litigation rates, however, appears to be great enough that even this variation in procedure would not account for all of it. Some evidence of litigation patterns comes from several reports requested by the European Commission on the effect of the 1985 directive calling for strict product liability. The Lovells Report³ provides survey results which indicate perceived greater levels of litigation since 1985, but no data on the trends themselves. We know that the U.K. has experienced increased litigation, given several famous pharmaceutical cases, but we cannot find any general collection of data on EU litigation rates.⁴ A European

¹ Reimann (2003).

² *Ibid.*, p. 783.

³ Melzer *et al.* (2003).

⁴ Liu (2004).

Commission Green paper⁵ in which the effects of the 1985 directive imposing strict products liability were studied, reports:

There are only a few reported Court cases based on the Directive: a recent case in Ireland, 2 cases in Italy, 3 cases in the U.K., 3 or 4 cases in Belgium, Sweden and Finland, 20–25 decisions in Austria, some 30 decisions in Germany, 19 judgements in Portugal, no decision yet in France, Greece and Luxembourg.

Other frequently cited data which support the claim that the U.S. differs from the norm come from Tillinghast. Their periodic reports on “the tort tax” suggests that as a percentage of GDP, the U.S. tort expenditures exceed those in most European nations by multiples. For instance, in the 1995 study, the U.S. is shown to experience tort costs equivalent to 2.2 per cent of GDP while Denmark is low among the listed countries at 0.4, the U.K. sits in the middle at 0.8 and Belgium is high among the Europeans at 1.4. By the time of the 2000 study (reporting 1998 data), the U.S. had fallen to approximately 1.9 per cent, Denmark still stood at 0.4, the U.K. fell to 0.6, and Belgium fell to approximately 1.15 while Italy took over the dubious top honors among the Europeans at approximately 1.7. Since the 2000 study, Tillinghast has not reported relative values of other countries. As of 2003, the U.S. tort costs represent 2.3 per cent of GDP.

While it is easier to observe U.S. patterns than those of virtually any other nation because data tend to be more available, it is also true that even observing patterns in the U.S. is hampered by limited data. As a result, debate about what is really occurring (or has occurred) continues. A rich history of research exists on U.S. tort litigation, and the purpose of this paper is not to prove or disprove any theory about those patterns; hence, a full discussion of U.S. litigation patterns will not be presented. Instead, the following discussion will proceed on the assumption that the U.S. litigation rate exceeds what is found elsewhere and refer the reader to a rich literature on the U.S. tort system, patterns, and effects of tort reform, found in a variety of outlets, including the *Journal of Legal Studies*, *Journal of Law and Economics*, *Journal of Risk and Insurance*, The Rand Institute, and elsewhere.

Possible causes of differences between the United States and the European Union litigation patterns

A number of characteristics found in the U.S. tort litigation system have been highlighted over the years as significant in encouraging parties to file lawsuits. Some of these characteristics differ from the majority rule in EU member countries. The following section is a listing and discussion of the most frequently mentioned variations. The intention is to define the differences as well as present the evidence of what we know currently about their influences.

⁵ Commission of the European Communities (2001, p. 10).

Allocation of litigation costs

Loser pays rule

The “loser pays” rule is often pointed to as one major reason for relatively low litigation rates in the EU. According to the loser pays rule, whichever party loses the case pays both its own legal costs as well as those of the other party, in addition to any compensation awarded. Placing responsibility for costs on the loser contrasts with the U.S., where most parties pay their own costs regardless of the outcome of the case. Support for the use of the loser pays rule generally focuses on the deterrence of frivolous litigation. If required to pay all costs, including those of your opponent, a party is less likely to file suit unless confident of ultimate success. Furthermore, the imposition of costs on the loser encourages vigorous defense because the costs of doing so will be recouped. Sometimes the incentives are believed to be excessive.⁶ One concern with the loser pays rule is that it puts a heavy burden on lower-income claimants. The U.K. recently addressed this concern by moving away from the pure loser pays rule.

An interesting outgrowth of the loser pays rule is the development of insurance markets to cover the plaintiff's legal costs. In Germany, FORIS has emerged as a successful provider of such coverage, with competitors following close behind. The introduction of this insurance in 1998 offers a natural experiment to test the effect on litigation patterns. Reports to date indicate no detectable increase in litigation rates.⁷ A partial explanation may be that FORIS only accepts insurance for claims it expects to win, and therefore it could be acting more as a gatekeeper than a promoter of litigation.

Similar types of coverage are available in other European nations as well, including the United Kingdom, where the availability of legal aid has been reduced tremendously in the past decade.⁸ By providing both the insurance against liability as well as insurance for the plaintiff's legal costs, the insurance industry in the U.K. controls nearly every aspect of personal injury disputes. According to Lewis,⁹ insurers deny payment in only 14 per cent of the personal injury claims made against them (the vast majority of which are motor vehicle and workplace accidents). Recently, reports have indicated that liability insurers are also providing medical care clinics to some claimants against their insureds' policies.¹⁰

⁶ Some examples of excessive defense and continued litigation once begun also have been noted, given the opportunity to recover costs. The costs incurred in litigation between Naomi Campbell and the *Daily Mirror* in which the model claimed invasion of privacy, for instance, exceeded £1,000,000. Her initial costs were £250,000, which were to be paid by the *Mirror*, according to the trial judge. Upon appeal, Campbell was to pay the *Mirror* \$350,000. Following a decision in Campbell's favor, the newspaper was ordered to pay an additional £350,000 in costs. The actual damages were valued at £3,500 (Kritzer, 2005).

⁷ Coester and Nitzsche (2005).

⁸ See the website for DAS Legal Expenses Insurance at <https://www.das.co.uk> for an example of marketing this insurance.

⁹ Lewis (2005).

¹⁰ Fleming (2005).

Contingency fees

Closely related to the loser pays rule is the general standard in many EU countries that legal representatives are compensated according to a set process regardless of case outcome. In contrast, plaintiff attorneys in the U.S. tend to be paid a fee contingent upon winning the case, and set as a percentage of those winnings. Lawyers under such contingent fee systems in the U.S. are believed to have incentive to pursue large-valued claims, even if the probability of success is low. Although numerous economists have suggested that contingency fees can align the lawyer's incentives well with the client's objectives,¹¹ many other commentators believe that contingency fees are a major, perhaps the major, driver of U.S. litigiousness.¹²

Kritzer is one of the few to collect specific data on contingency fee lawyer compensation. The results of his work suggest that contingency fee lawyers tend to accept a variety of cases.¹³ Kritzer's surveys also indicate that for the vast majority (approximately 90 per cent) of cases, contingency fees translate into hourly rates approximately 25–30 per cent higher than standard hourly fees charged on a non-contingent basis, which he considers a reasonable risk premium, given the likelihood of no payment at all for the contingency fee lawyers. Kritzer further reports that the majority of high-end contingency fee cases are argued by an elite group of lawyers rather than randomly spread among the profession generally. Kritzer concludes that a few well-known contingency fee lawyers obtain very large fees while the remainder are compensated similarly to those on an hourly fee arrangement.

Kritzer also reminds us that fees conditional on winning, and even associated with ultimate compensation levels, are not exclusive to the U.S. Kritzer lists the following examples of payment contingent on winning, sometimes with a percentage fee attached to it, other times with fees unrelated to the claim payment:

- All Canadian provinces except Ontario; some of these are percentages of recovery costs, some not;
- Scotland, where lawyers are permitted to enter into arrangements for payment dependent on winning;
- Northern Ireland and the Irish Republic, same as Scotland;
- New Zealand, where both barristers and solicitors may charge on a “speculative basis;”
- Australia, where the practice of “no win no pay” goes back to 1960, but only to 1994 on a routine basis;
- France and Belgium are moving toward conditional fees;
- Japan, for motor vehicle, where litigation generally is paid on a contingency basis;
- Since 1995 conditional fees have been accepted in the United Kingdom, sometimes contingency;
- Greece, but no more than 20 per cent of the fee is related to the award;
- Dominican Republic, but not more than 30 per cent;
- Some aspects in Italy, Luxembourg, Portugal and Brazil.

¹¹ Polinsky and Rubinfeld (2003); Rickman (1999); Danzon (1983), among others.

¹² For example, Brickman (1996).

¹³ Kritzer (2002).

Interestingly, early evidence suggests that the introduction of conditional fees in the U.K. has led to a reduction in availability of legal representation.¹⁴ Attorneys appear to be risk averse, concerned that they will not be paid sufficiently, given that compensation is dependent upon winning the case. If this pattern bears out to be true in the long run, the result is opposite the claims that contingent fees fuel litigation in the U.S. Because the contingent fees introduced in the U.K. coincided with other changes, such as reduced legal aid, however, a clear determination of the effect of any single change is muddled. Furthermore, the results could suggest that the contingent nature of the fees is not nearly as important as the link between the size of the award won and the legal fee paid. The change is also too recent to be able to draw firm conclusions. A great deal of additional research is warranted on this and the other topics mentioned here.

Judge vs. jury decisions

For the most part, jurisdictions other than the U.S. rely on judges or tribunals outside of the jury system to resolve legal disputes. Japan recently passed legislation that will institute jury trials for tort cases, but they do not go into effect until 2009. The U.S. allows for both jury and judicial forums in tort, with either party able to request a jury trial, a request that cannot be vetoed by the other party. The right to a jury trial is provided in the Bill of Rights of the U.S. Constitution, now more than 200-years old. This difference between the U.S. and “The Rest of the World” offers another source of discussion about what fuels litigation rates in the U.S. The public perception is that juries are far more lenient, awarding larger damages more often than do judges.

The empirical evidence, however, is somewhat mixed. As Hersch¹⁵ indicates, most empirical evidence to date is based solely on case verdicts without consideration of differences in settlement probabilities across forums. Given this caveat, however, most of the studies show limited differences between judges and juries in their decisions. Some evidence indicates that juries are less favourable toward plaintiffs, but most of these differences could reflect disparities in case characteristics. Regarding the more common (though none are common) punitive damage awards, Hersch and Viscusi¹⁶ find generally similar punitive damage incidence and values among jury-tried cases as judge-tried cases; however, they also observe that juries tend to be involved in the extreme-value cases, awarding them more often and at higher levels than do judges.

Although evidence indicates, at least somewhat, that juries are more lenient in tort case outcomes than are judges, the differences appear small enough that this factor seems unlikely to drive a significant amount of the U.S. litigation. An exception might be the existence of what proponents of tort reform refer to as “tort hell holes.” These are jurisdictions considered especially unfavourable to defendants, and therefore as jurisdictions sought after by plaintiffs. Interesting real-life experiments on the effect of

¹⁴ See Lewis *op.cit.*, p. 67.

¹⁵ Hersch (2003).

¹⁶ Hersch and Viscusi (2004).

judges versus juries in claim outcomes will be available as Japan alters its system in 2009. Perhaps other jurisdictions will consider similar actions. Worth noting as well is the fact that even in a judge-based system, variations in legal interpretations are likely.

An important aspect of the U.S.-type jury system is the extensive discovery allowed. The EU civil code, in contrast, tends to limit plaintiff discovery, which may be more important than the actual decision-making powers of judges versus juries. Being forced to provide financial and other data in a legal dispute could provide significant behavioural incentives. Recent examples for Merck in the Vioxx trials and the tobacco industry in the U.S. state attorneys general cases are informative. These are, of course, the counter-examples. Decisions by firms to alter their behaviour because of concerns over discovery possibilities are undetectable precisely because their behaviour has been altered and resulting injuries prevented.

Damages

Compensation for harms typically involves three types of harms: economic, non-economic, and punitive. Within the EU, non-economic damages often are categorized as either personal injuries (mostly human rights violations) or non-material harms (including pain and suffering, although this concept is limited in appreciation throughout the EU). Furthermore, within the EU, punitive damages are virtually absent. Reports from Italy suggest that judges might have punishment in mind as they set awards,¹⁷ and recent decisions in other EU nations indicate some similar notions elsewhere for situations involving human rights violations.¹⁸ However, in general, commentators on EU tort systems indicate that punitive damages are unknown among their jurisdictions.

Additionally, many EU countries base payment for non-economic damages on a set scale, similar to the caps on damages found in some U.S. jurisdictions, but even more specific with set amounts under various circumstances. As discussed by Wagner,¹⁹ the scale may be formally adopted (e.g., Italy) or informally and generally applied by insurers (e.g., Sweden). Wild fluctuations in award values, therefore, are uncommon. Interestingly, EU insurance requirements tend to be much higher than those found in the U.S. With greater fluctuation in award values in the U.S., and inclusion of more types of harms, higher U.S. limits would seem to make sense.²⁰ Yet even with lower amounts of insurance required, the percentage of motorists who drive without insurance is higher in the U.S. (on average) than in most EU countries.

While commentators seem not to expect expanded use of non-economic damages generally in the EU, one area is receiving attention: enforcement of European Law.

¹⁷ Iudica and Scarso (2005).

¹⁸ Wagner (2005).

¹⁹ *Ibid.*

²⁰ Insurance company data indicate that non-economic damages in the U.S. account for one-third the total claim value, on average (Kritzer (2004)). Kritzer cites data from the Insurance Research Council, over several survey periods beginning in 1977 and ending in 2002. At the high in 1977, non-economic damages represented more than half of all payments. The low value was reported in 2002, at approximately one-third (p. 492).

With increasing harmonization, new European Law initiatives are being created, often without regulatory bodies available to enforce those laws. Private actions, therefore, are needed to impose the stated requirements. An important example is the current rise of anti-discrimination litigation. An interesting area of research along these lines is to investigate the extent to which litigation rates track regulatory controls, that is, are greater levels of litigation observed in jurisdictions perceived as providing insufficient levels of governmental controls to enforce desired regulations?

Another question becoming more common in recent years is how much influence is being exerted by extensive social programmes found in most EU member countries. Social programmes tend to provide compensation for the same harms associated with tort litigation, including provision of medical care and payment of lost income. Kagan,²¹ among others, has suggested that social programmes represent substitutes for liability, leaving little incentive to litigate. A study currently in process suggests the existence of a negative statistical relationship between liability insurance premiums and government outlays for social programmes.²² Various commentators, however, disagree with the idea that any such association exists.²³ The question is becoming more important as EU countries reduce the level of their social programmes.

Common vs. civil law

In some ways the loser pays rule, use of judges, and set standards for awarding damages reflect the civil law system in many EU countries. Among EU members, the U.K. is the sole common law nation. The U.S. also follows a common law system. At its extreme, the civil law specifies in its statutes precisely what outcome will result for any given dispute, and therefore, the need to litigate is eliminated. At the other extreme, under common law, it would involve the absence of legislative rules altogether. Instead, rules would develop solely through case law as courts (judges) make decisions about particular issues. The reality for civil and common law systems is somewhere in between with gradations toward legislative and case-based rules.

The form of civil law used in EU member nations varies quite a bit from country to country. Even the genesis differs, with Scandinavian, German, and French systems all growing out of different histories. Several papers in the finance area have observed effects of differences across these forms of legal systems in promoting economic development.²⁴ Effects in general tort litigation likely also exist and warrant additional research. Initial evidence of such effects was found in Kerr *et al.*²⁵ It may be, in fact, that civil law itself accounts for the majority of differences between U.S. and EU litigation patterns. While the United Kingdom employs a common law approach, a more pronounced sense of liability also exists there compared to other EU countries. Furthermore, the common law effect in the U.K. might be dampened by extensive social programmes not found in the U.S.

²¹ Kagan (2001).

²² Kerr *et al.* (2004).

²³ Wagner, *op. cit.*

²⁴ Laporta *et al.* (1998).

²⁵ Kerr *et al.*, *op. cit.*

Concluding remarks and future research directions

The United States has long been regarded as an excessively litigious society. Despite recent rises in European litigation, it remains calm relative to the U.S. Yet, concern exists that U.S. influences will find their way to the EU and cause negative economic effects. Furthermore, the EU is in the process of developing harmonized systems including those associated with tort litigation, offering an opportunity to design one that best achieves system objectives. As a result, investigation of various tort liability characteristics and their apparent effects is useful.

In this paper, four general characteristics that distinguish U.S. from EU tort liability systems were discussed: rules allocating costs; employment of judges versus juries; assessment of damages; and civil versus common law systems. Within these categories, several areas deserving future research were identified. Most significant may be the effect of civil versus common law rules, but also to observe the effects of using juries, contingent fees, and providing insurance for legal costs. Another avenue that deserves attention is the increasing use of litigation to enforce European Law, particularly anti-discrimination suits and similar actions. Several commentators have suggested that the significant social programmes found in EU countries provide further deterrents to litigation. As EU member countries pull back their social programmes, close observation of effects on liability patterns is warranted.

References

- Brickman, L. (1996) 'ABA regulation of contingency fees: Money talks, ethics walks', *Fordham Law Review* **65**: 247–298.
- Coester, M. and Nitzsche, D. (2005) 'Alternative ways to finance a lawsuit in Germany', *Civil Justice Quarterly* **24**: 83–102.
- Commission of the European Communities (2001) *Report from The Commission on The Application of Directive 85/374 on Liability for Defective Products*, COM(2000) 893 final, Belgium: Brussels.
- Danzon, P. (1983) 'Contingent fees for personal injury litigation', *Bell Journal of Economics* **14**: 213–224.
- Fleming, C. (2005) 'Car insurer has medical clinic to cut costs', *The Wall Street Journal* (December 28, 2005), pp. B1, B2.
- Hersch, J. (2003) *Jury demands and trials*, Harvard Law School Public Research Paper Series, No. 92, November 2003.
- Hersch, J. and Viscusi, W. (2004) 'Punitive damages: How judges and juries perform', *Journal of Legal Studies* **33**: 1–36.
- Iudica, G. and Scarso, A.P. (2005) 'Tort liability and insurance: Italy', in G. Wagner (ed) *Tort Law and Liability Insurance*, Wien: Springer.
- Kagan, R.A. (2001) *Adversarial Legalism: The American Way of Law*, Boston: Harvard University Press.
- Kerr, D., Ma, Y.L. and Schmit, J.T. (2004) *Is liability a substitute for social insurance?*, Proceedings of the International Insurance Society, New York.
- Kritzer, H.M. (2002) 'Seven dogged myths concerning contingency fees', *Washington University Law Quarterly* **80**: 739–794.
- Kritzer, H.M. (2004) 'Advocacy and rhetoric vs. scholarship and evidence in the debate over contingency fees: A reply to Professor Brickman', *Washington University Law Quarterly* **82**: 477–507.
- Kritzer, H.M. (2005) 'Loser pays doesn't', *Legal Affairs* (November/December): 24–25.
- LaPorta, R., Lopez-de-Silanes, F., Shleifer, A. and Vishny, R.W. (1998) 'Law and finance', *Journal of Political Economy* **106**: 1113–1155.
- Lewis, R. (2005) 'The relationship between tort law and insurance in England and Wales', in G. Wagner (ed) *Tort Law and Liability Insurance*, Wien: Springer.

- Liu, J. (2004) 'Two roads diverged in a yellow wood: The European community stays on the path to strict liability', *Fordham International Law Journal* **27**: 1940–2005.
- Melzer, J., Freeman, R. and Thompson, S. (2003) *Product Liability in the European Union: A Report for the European Commissions*, MARKT/2001/11/D.
- Polinsky, A.M. and Rubinfeld, D. (2003) 'Aligning the interests of lawyers and clients', *American Law and Economics Review* **5**: 165–188.
- Reimann, M. (2003) 'Liability for defective products at the beginning of the twenty-first century: Emergence of a worldwide standard?', *American Journal of Comparative Law* **51**: 751–867.
- Rickman, N. (1999) 'Contingent fees and litigation settlement', *International Review of Law and Economics* **19**: 295–317.
- Wagner, G. (2005) 'Tort liability and insurance: Comparative report and final conclusions, in Gerhard Wagner (ed) *Tort Law and Liability Insurance*, Wien: Springer.

About the Author

Joan T. Schmit is holder of the American Family Insurance Chair in Risk Management and Insurance at the University of Wisconsin-Madison. She conducted this research in part while a visiting scholar at St. Gallen University in the Institute of Insurance and Risk Management under the directorship of Professor Hato Schmeiser. She is grateful to her colleague, Dan R. Anderson, for insightful comments, and to participants in the Second Annual Liability Regimes Conference, October 2005 in Munich Germany. Professor Schmit is a past president of the American Risk and Insurance Society as well as of the Risk Theory Society. She has written extensively on issues related to tort reform and liability claiming patterns.