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EDITED TRANSCRIPTS

EMERGING CIVIL JUSTICE ISSUES

J. Russell Jackson, Robert S. Peck
Moderator: Paige V. Butler

DANIEL POLSBY: Welcome all. I'm Dan Polsby. I'm the dean of George Mason Law School of which the Law & Economics Center is a part. Welcome to the law school.

My brief this morning is to be brief, also to be gracious to the extent that those conflict, brief dominates. So I will not detain you any longer other than to wish you a warm welcome and hope that this is a very challenging program and an important program. We're delighted to have you here, and we trust that you will have a prosperous time learning over the course of the next day and a half of programs. Thank you all again for coming.

PAIGE V. BUTLER: Thank you, Dan. I mentioned last night that this has been a very nice move here for us, and we are very happy. I am going to introduce your first panel today. We have Bob Peck and Russell Jackson. Russell is substituting for John Beisner. Bob is President of the Center for Constitutional Litigation. He argues constitutional cases in the U.S. and state supreme courts. He is adjunct law faculty at both American University and George Washington University. Bob is on the Board of Overseers for the RAND Institute, the Lawyers Committee of the National Center for State Courts, and on the First Amendment Advisory Council.

Russell Jackson is a partner at Skadden Arps in New York. He focuses on the defense of companies for their products and advertising, and handles other complex litigation at both the federal and state court level. He's a member of American Law Institute, chair of the New York City Bar Products Liability Committee, columnist for the *National Law Journal* and he hosts his own blog. So, those are brief introductions. I will turn it over to them.

ROBERT S. PECK: Thank you, Paige. It's a real pleasure to be here today. One thing that should not be overlooked as we talk about issues in the civil justice system is that, for all its faults, the civil justice system remains a remarkable achievement. It is there that an individual who is injured, neither wealthy nor well connected, can hail a powerful adversary into court on equal footing and ask the court to hold it accountable for its wrongful conduct.

Only in an American courtroom—not in legislative chambers or executive suites—can an individual seek full redress, standing at the bar on an equal basis with a powerful and influential adversary. The political and

economic advantages that one might enjoy in other arenas dissolve in the courtroom. That's something that we should not ever look to give up.

There's a story told about Hugo Black relevant to our discussion today. Before he was a U.S. Supreme Court Justice, before he was a U.S. Senator, he was a trial lawyer. In this instance, he was considered the most famous and successful trial lawyer in his vicinity. One day, according to this story, an individual went to the bar association and said, "I'm looking for your best trial lawyer. I've got a case that I want him to try for me."

They replied, "Well, that would be Hugo Black. He's trying a case down at the courthouse right now. You could see him in action." The prospective plaintiff arrived as Black was making his closing argument, describing the terrible injury that befell his client. Tears were streaming down his cheeks, as he related the injury. Black's own emotions made this a powerful, powerful closing.

Black won the case and obtained a verdict of $25,000, a princely sum in those days. He was, of course, hired by the man looking for a lawyer. Eventually, he tried that case, too. He gave a very perfunctory closing, won the $11,000 that had been claimed by the individual, and the client was happy, but still a little disappointed. He told Black, "You know, I was kind of hoping to get the tears treatment and all that." And Black's response was, "Hugo Black does not cry for less than $20,000."

Now, one of the great dangers and problems that we face in the civil justice system is that we're pricing ourselves out of reach for too many people. Many people are not going to be able to afford to use the system because their claims are too small yet still cost too much to litigate. So, the first trend I want to discuss today is the expense of litigation. This has been a standard complaint about our litigation system for nearly two centuries. It's nothing new. But still, we are seeing an increasing number of meritorious cases that are simply too expensive to bring because of the procedural fencing, the expert fees, and the protracted interlocutory appeals that make cases uneconomic to bring.

So, only if there is a large potential compensatory award is there an opportunity to seek justice and have a skilled lawyer see it through much like, as Hugo Black said, when he turned on the tears. Now, with the advent of tort reform, we have enhanced this undesirable trend by placing additional unreasonable obstacles and hurdles before the courthouse door that deter meritorious lawsuits, or with much the same effect, render them more expensive to pursue, make them more difficult to prove and diminish recoveries even when the plaintiffs prevail.

The result is that run-of-the-mill cases are going to be chased out of our system unless we find a way to deal with this, and they will end up having to find other venues or disposition, putting the judiciary much in the same position as the postal service has experienced with the kind of competition that they get from Federal Express and UPS.

The cases that are filed in court will then tend to skew to the higher end, be more complex, more contentious, and draw greater resources from the judiciary, rendering statistics about time to disposition, the number of appeals, and even the average verdict, upward.

Separately, and complementing this undesirable trend, are diminished judicial resources. The dislocating economic conditions of our times place greater demands on the judicial branch as part of the community and social fabric of our lives. Filings related to foreclosures, domestic relations and debts rise during those poor economic times as well. Yet, state budgets cut the level of funding that the courts enjoy in more flush times even as filings go up.

So, courts are facing hiring freezes, salary freezes, layoffs, pay cuts, early retirement, and increased filing fees. Eight states close their courts a certain number of days each month. Nineteen states have instituted furloughs of judicial staff. New Hampshire, for the second time in recent years, suspended jury trials in civil cases for a six-month period of time. The crisis in judicial funding is palpable, and it has broad implications for whether the courts can do the job we ask of them, as well as fulfill the promise of providing a level playing field for the resolution of judiciable disputes.

The third trend I want to mention—contributing to this seemingly perfect storm—is the new politics of judicial elections. Electing judges, which dominates the state landscape as a selection method, were originally an outgrowth of Jacksonian democracy—an attempt to overcome an elitist system that drew judges from only among the well-connected and most privileged. Yet, a selection system that relies on popular sovereignty is falling into a similar trap because of the amounts of money expended in these races continue to rise exponentially. We saw an Illinois retention election this year become the second most expensive judicial race in recent years.

This is unusual for retention, as opposed to a contested, election, and it does not portend well for the assumption that we will continue to have fair and impartial courts, if essentially the courts themselves become political footballs. Add to that development, the judicial decisions in *Citizens United*,[1] which potentially opens up the floodgates to millions in untraceable money; *Republican Party v. White*,[2] which holds that judicial candidates have First Amendment rights to take positions on issues that can come before the courts; the current challenges to the "pledges or promises" canon in the Canons of Judicial Ethics,[3] and the somewhat countering force of the *Caperton* decision,[4] holding that recusal is required as a matter of due process under an appearance of impropriety standard, when a party disproportionately aids a judge's election.

That combination of developments will create situations—and it has already occurred in several states—where candidates take positions on matters that are likely to come before their courts, are asked to recuse them-

selves, claim that they had a First Amendment right to do so, but then, because of due process, may not sit on those cases so important to their selection. If this becomes commonplace, we're going to witness a level of dislocation within the judicial branch on the issues that we really expect our courts to resolve. This is clearly not a pretty picture, but this is a picture of the civil justice system as we face it today.

The fourth trend is something that I think is potentially encouraging: the use of technology. Our civil litigation system has yet to embrace a serious use of technology as a factor that can ameliorate some of the expense in the system. I recall that in 1984, I was invited with the then-ABA president to visit a trial courtroom that was being hailed as the courtroom of the future.

We went to this courtroom, curious to see what the courtroom of the future—at least in 1984—looked like, and expected something out of a Hollywood science fiction set. The courtroom looked like any other courtroom you'd ever seen, except that there was a monitor in front of the judge and in front of each counsel on which you could get a real-time version of the transcript that the court reporter was making. That was the courtroom of the future. It didn't seem very futuristic. The future in that instance stretched no further than the lenses of my glasses from my eyes.

Now, however, we have the ability to use technology to make it less expensive to dispose of cases. For example, cars could be outfitted with black boxes much like airplanes are today. So, with GPS technology and other capabilities, given that car collision cases are still among the most frequent cases brought before courts, we could obtain real-time information about the positions of the cars when they approached, and what exactly happened—who slowed down, who didn't, and that sort of thing, which may make those cases easy enough to evaluate by simply plugging both black boxes into a computer to get the facts in a case. That's an example of how, perhaps, technology can help in certain kinds of cases that are now being priced out of the system.

The fifth trend that I want to mention this morning is the use of aggregation. Aggregation of underlying liability issues, separate and apart from the individual remedies available, remains one of the few ways that mass tort cases become affordable for both sides. Using this kind of an approach in 1991, the Judicial Conference Ad Hoc Committee on Asbestos Litigation made a recommendation about the kinds of issues that could be tried in an aggregate manner, leaving individualized issues for other parts of the litigation.

That committee was chaired by the Fifth Circuit's Judge Thomas Reavley. As a bit of full disclosure, I was the reporter for that committee. It found very little value in re-litigating the same issues of causation over, and over, and over again, for each plaintiff with disparate results. It thereby found that this was a way to narrow the dispute and make sure that it was less tedious and less expensive. Today, however, we are now witnessing a

massive attack on various systems of aggregation and on class action litigation.

If it succeeds, when combined with the other trends I've mentioned, the civil justice system may become little more than a historic artifact; a far cry from the system of justice that's equally available to all, that remains grounds for celebration. So, it is our job to find a way through this forest to make sure that promise of equal access to justice, remains true. Thank you.

J. RUSSELL JACKSON: This is my first time addressing this group. I am John Beisner's partner, and he did ask me to tell you how sorry he is that he is unable to be here. I'll admit, looking out into this sea of faces, I'm reminded of the joke about the shark family with the papa shark teaching baby shark how to eat a lawyer. There was a lawyer who had fallen off of his jet ski on vacation. Papa shark said, "There he is. You circle him first, once, with just this much of your fin showing. You circle him a second time. Slow down, and show a little bit more of your dorsal fin. The third time you circle him, you let that fin show really large and you go very slowly all the way around him. Then you eat him."

So, the son shark went out to eat the lawyer. Being an impatient kid, he ended up sneaking up on him and just gobbling him right down. He went back to papa shark who said, "Well, what did you think of the lawyer?" And the kid said, "Well, he was all right."

Papa shark said, "Well, what do you mean, 'just all right?'" And the kid said, "Well, I don't know, he tasted kind of funny." And papa shark said, "Well, did you do what I told you to do?" And the kid admitted, "No, I was in a hurry, and I just ate him. I was hungry." And papa shark said, "Don't you know? Everybody knows! Lawyers are so much better once they've had the crap scared out of them."

I actually do write a blog, and I read a lot of your decisions and on a daily basis I think, perhaps, you're attempting to do that to me. There are a lot of decisions in the class action civil justice area that leave a lot of room for debate for folks on both sides of the *v*. I come to you from the defense side of the *v*. I probably will have a few different ideas about what ought to happen in that arena than Mr. Peck, but we are friends nonetheless. But let me share with you, if I can, a few of the emerging issues that I see from my perspective, both actually litigating and in trying to report on this area for other people on my blog—consumerclassactionsmasstorts.com.

Let me begin by saying that one of the big issues, with respect to class actions generally, is how to preserve fairness for both sides. Clearly, it's important to have class actions. They've been around in one form or another for decades. It is, however, sometimes tempting to allow the desire to have a convenient procedure and to have a procedurally nice hearing, trial, and result, and allow that to get in the way of some fundamental defenses that a defendant might have.

Allow me to at least posit my belief which was, I would argue, echoed in a recent stay opinion by Justice Scalia in the Supreme Court, that there are certain fundamental rights that a litigant has that ought not to be altered just by mere procedure. So, the fact that we aggregate a lot of claims together doesn't mean that a defendant who has a right to challenge—for instance, causation or reliance—individually, with respect to each class member. It doesn't mean that that right ought to be in any way taken away just in order to facilitate a trial.

One of the themes in the arguments that you will hear coming from me this morning in these issues is that there are various ways and areas in which I would argue that it is becoming easier for folks to attempt to compromise a defendant's right to posit individual defenses in class action litigation, and in some instances, the fact that you would be unable to assert those defenses ought to mean, in my view, that there ought not to be a class at all.

But let's talk, at least in the beginning, about the pleading standards—not even for class actions generally, but just the pleading standards in general. There's been an awful lot of talk over the last few years about *Dura Pharmaceuticals*,[5] and *Twombly*,[6] and *Iqbal*,[7] and whether or not that has represented a fundamental change in the way that plaintiffs are required to plead their claims, and a fundamental change in the way courts hear claims.

From everything that we can see—first of all, the notion that *Conley*[8] was adhered to strictly, and was in fact the de facto standard that people used to evaluate motions to dismiss, is, I would argue, incorrect. Certainly, there was plenty of scholarship before *Dura* or *Twombly* or *Iqbal* that would have suggested the same. Courts, while they might have quoted *Conley*, would go on to employ some sort of their own plausibility standard, which is what—particularly *Iqbal*—enunciated and said that you have got to have some basis pled in the complaint for connecting the basic elements of the claim.

This is important not just because you need to know what it is you're trying to defend against, but it's also important because as a litigator, you understand that folks often attempt to plead claims as generically as possible so as to not hamper their ability later to make class certification arguments. And so, the more you plead about individual reliance, or individual causation, the less likely it may be later on that you would be able to get class certified, because then of course the fundamental individual character of those issues is much more obvious.

As a result of *Twombly* and *Iqbal* and the like, there's been an awful lot of movement afoot, certainly in Congress, to consider changing the standard that one would employ on motions to dismiss. Some of scholarship that we have seen so far, suggests that there's not been a huge sea change, at least in the numbers of cases that ultimately get dismissed post, what I'll call—I'll mash them together—"Twiqbal," and "pre-Twiqbal," and that in fact may be an awful lot of something to do about nothing.

At the end of the day, I think especially after the recent elections, it seems less likely that both houses of Congress would pass some sort of change in the pleading standard and so those issues may take less prominence, at least in the political sphere.

I would like to also look, if we could, at the class certification standards. There certainly had been a notion in years past that a court in considering whether or not to certify a class, shouldn't dig too deeply, shouldn't look at the merits; *Eisen*[9] frequently was cited as the reason for this. Over the course of the years, we have seen courts take kind of an opposite view and indicate that before you certify a class, you darn well better know how it's going to be tried.

You better look at the elements of the causes of action, the types of proof that are going to be offered, and give it rigorous analysis, as the courts call it, as far as how the case really will be tried, and whether it's in fact capable of being tried. Even courts that I might not have considered the most likely to have adopted this standard—such as the Ninth Circuit in the *Dukes* case[10]—have adopted this standard. There's still a debate between the Ninth Circuit and the Seventh Circuit about whether or not you hear *Daubert*[11] challenges to expert testimony on those issues and, I would argue, that perhaps may be unique in the *Dukes* case to the notion of it being a discrimination case where statistical proof is something that is frequently used to prove the elements of the claim there. I think it might be very different if you were considering, for instance, individual claims of consumer fraud or something like that.

But again, the courts generally have been focusing much more seriously on the question of, "How is this case going to be tried?" That too presents a fundamental kind of civil justice issue because it certainly makes an awful lot of difference in the outcome of the case, whether or not the claim ultimately gets certified as a class action. In fact, Judge Posner, on multiple occasions, has written about the ability of a decision on that issue to kind of force a settlement in an action because it's as if I went to Vegas and decided to put all of my money on red; that might be one decision that I would be unwilling to make, even though I might be willing to gamble individually on certain spins of the wheel—certain smaller amounts of money that might even amount to the same amount of money totally.

But at least I would be able to do it in increments and to pay attention to other factors that might be at the table. One of the issues that is currently before the U.S. Supreme Court and that is a fascinating issue, and one that's playing out as well in the Seventh Circuit, is the issue of, "What is the preclusive defect of the denial of class certification on absent members of the class?" In the case that's currently before the Supreme Court, you had folks who were absentee class members; the federal MDL court decided you can't have a class action here. And they said, "That's fine." They went to West Virginia state court, filed a class action, and proceeded to be enjoined by the MDL judge.

So, the fundamental question of whether or not absentees who did not receive notice and an opportunity to opt out at that point in the case—in fact, the court said there's not going to be a class, so there would be no notice and no opportunity to opt out—could they be bound, in essence, by the decision of the federal court in deciding that there couldn't be a class? Recently, the Seventh Circuit addressed that issue in a couple of decisions by Judge Posner. There, the court concluded, yes, the absentees could be bound.

The absentees would be parties for the purpose of challenging a decision; they could even intervene on an appeal and to the extent that all you're doing is holding them to the decision on class certification, and not adjudicating the merits of their claim or keeping them from bringing their claims individually. The Seventh Circuit said those people could be bound to a decision by a federal court on whether or not a case could proceed as a class action. This will be a fascinating decision that we'll get from the U.S. Supreme Court hopefully later this year.

Another interesting issue, and one that is constantly debated among plaintiff and defense lawyers—and it really goes, again, to the heart of the issue of, "Can you provide a forum to try all of these individual claims fairly in one courtroom?"—is the issue of statistical proof in class actions. Can you, in essence, say to a defendant where the underlying statute or law might require reliance or causation, "We're going to have an expert who comes up with a model and engages in some statistical proof, and he'll basically say 80% of the people were deceived in this case, and therefore, recovery ought to be for 80% of the people. We don't know which ones of those that might be, but it should be 80% of the people"?

The courts have been pretty clear—at least in the circuit courts, particularly in the Second Circuit—on addressing these issues, saying that statistical proof in those types of situations and consumer product cases just really doesn't cut it. That in fact, individually, the defendant is allowed the challenge the decision to purchase a product, whether that may be called reliance or causation, in a consumer fraud or misrepresentation case, and so in *Zyprexa*,[12] in the cigarette litigation, in the *McLaughlin* case,[13] the Eighth Circuit in *St. Jude Medical*[14]—all of them ended up rejecting this concept of using some form of statistical proof as a substitute for allowing the defendant to have the individual defenses that they ordinarily would have against absentee members of the class.

One of my pet issues, and one that I'll leave you with here today—that I think is important for us to consider, and often as litigants we fail to consider it, and certainly I think even courts sometimes fail to consider it—is the question of how you define a class in civil litigation. A class, while there are no written requirements in Rule 23[15] about the class definition per se, certainly the decisions and the case law suggests that a class definition must be objectively identifiable. It must be ascertainable. You must know

who's in the class and certainly be able to know that before the case is litigated.

It can't include a bunch of people who aren't injured. In other words, if you're suing for a particular kind of defect in a product that might actually manifest in 1% of the products, you can't just say, "It's everybody who bought this product," because of course, most of them don't have a claim. Most of them have not experienced any sort of problem. And then there is also the issue of a fail-safe class—that being a class where in the class definition, some of the merit issues are kind of folded into the claim: "All people who purchased a product in reliance on these misrepresentations, and thereby suffered damages." That's a classic fail-safe class that would require, in essence, a trial of the entire claim before you could decide who was even being bound by the decision.

There have been a host of decisions in the last year, both in state courts—often folks in California have written quite a lot on these issues—but also in federal courts across the country, that have recognized that unless you can actually articulate an identifiable class without including some of the elements of the causes of action to be determined, you haven't defined a class, and you can stop your analysis right there before you even get to all of the Rule 23 (a) and (b) elements if the class is not objectively identifiable.

John has a couple of pet issues that I think may work into some of what you had talked about, Robert, on the financing side: in particular, the concept of third-party financing of litigation. In fact, he did a monograph for the U.S. Chamber of Commerce which would be available on their website if the issue interests you at all. The root problem, of course, in getting investors in class actions or in civil litigation, is that it introduces a stranger to the attorney–client relationship, whose sole interest in the case is financial, and seeks to maximize the recovery regardless of the underlying merits of the claim.

One jurisdiction that has experimented with third-party litigation financing is Australia. Australia has seen, as a result of such financing, a large increase in the number of claims and attempts by investors to, in essence, exert some sort of control over the litigation that certainly would not have been allowed under what we would have known as champerty or the like. John argues in his monograph, that this type of litigation financing really has a number of problems. First, it encourages frivolous litigation because it's the ones on the margin that wouldn't ordinarily be brought by an individual or by a class action lawyer who otherwise makes decisions about cases to file, and what's strong and likely to recover and what isn't.

It's those cases on the margin that end up getting brought and financed by these third-party litigation financing mechanisms that of course raise a host of ethical concerns, because there's certainly a great danger that clients end up giving control over some portions of the litigation or perhaps even the whole decision of whether or not to settle for money, in order to obtain

financing. The funder, of course, the investor, ends up having loyalties and fiduciary duties to folks other than the litigant, such as to their own investors.

In fact, hedge funds are one of the likely investors in this type of litigation speculation. It also, of course, threatens to impair the attorney's own judgment and impartiality of judging for their client what's in the client's best interest. And because of the disclosures that have to be made to the investor at each stage of the litigation, you endanger the attorney–client privilege and work product doctrine by what it is that you may or may not have to communicate to this investor throughout the course of the litigation.

It also raises a particularly thorny problem in aggregate litigation because there you've got the whole problem of the investor. Not only does the investor not have the interest of the named plaintiff as their primary responsibility, but they also have all of the absent class members who have not assented to third-party financing of their claim but who purportedly are being represented—at least up until the time of notice and have an opportunity to opt out knowingly—are being represented by people with these litigation financing obligations.

It also, of course, increases the *in terrorem* effect, if you will, of some of these cases because again, the cases that these types of investors would want to invest in are the ones that would present a likelihood of a huge recovery. In fact, the fact that the likelihood of success may be lower is usually offset in these folks' calculus by the size of the potential recovery. They'll be willing to, in essence, take a ten-to-one shot on recovery over some threshold in order to be able to possibly get that type of return.

So anyway, third-party investing in litigation is another one of the issues that certainly affects us in the civil justice system, and I think one other that I'll raise—and then we'll probably throw the floor open for some questions—is the question of class action settlement and what you do with the stinker of a claim. We all recognize that there are some claims that are filed that just are not particularly meritorious, but somebody might need to settle them in order to get rid of them. How do you get rid of them, particularly in a post-*Catha*[16] world?

One of the ways in which some folks have attempted to extinguish such claims is through the use of site-pray recovery in settlements. And by that, I simply mean that they'll create a fund against which a class can claim, and when people don't actually make any claims against the fund, the remainder of the fund goes to the charity of the judge's choice, or the plaintiff's lawyer's choice. It might even create its own charity that gets run by the plaintiff's lawyers, which is one case that I have been brought in and dealt with in the past after it had gone awry and not hewn to its creating document and the purposes that it was created to achieve.

Site-pray settlements, and of course, if you attempt to even import that concept into litigation—litigation in order to achieve some sort of funding to some charitable purpose—is far afield of the underlying purposes of

class actions which has always been to actually compensate individuals who had claims but who might not be present in court or they might be small enough claims that they didn't want to litigate in court or couldn't afford to litigate in court.

These types of site-pray recovery—and again, we've begun to at least hear plaintiffs who espouse, in essence, fluid recovery such as Judge Weinstein had proposed in the light cigarette litigation, which ultimately was shot down by the Second Circuit[17]—this concept of, "Let's get a fund. We'll have it funded by the amount of bad that the defendant allegedly did, and then we'll give it to some charitable purpose, perhaps stopping smoking. We'll either create or there may already be a charity, and we'll give it to that."

And while these things may sound laudable in their purposes and certainly charitable, they don't necessarily sound like litigation as we understand it in the individual one-on-one context, and I would argue it is a fundamental change for the rights of the defendants when you attempt to impose that on a class-wide basis. So, those are some of the issues that I would present to you from the defense perspective. Robert, you may even want to respond to some of those. I don't know. Or we may have questions.

PAIGE V. BUTLER: Bob, if you would like to respond, and then we'll open up for questions.

ROBERT S. PECK: Well, I was amused, Russell, that one of your opening examples was Justice Scalia's stay in the *Scott* case,[18] because I'm counsel in the Supreme Court for the plaintiffs in that case. A stay is issued on the basis of an application to the Circuit Justice assigned to that Circuit. Here, Justice Scalia serves as the Circuit Justice for the Fifth Circuit. Counsel opposing the stay has a four-day period in which to respond. It was on the first of those four days that I was hired to respond to it, had to review fourteen years of litigation in the Louisiana courts, and write my brief. The complaint that justified the stay was that they did not—the tobacco companies, in this instance—did not have the opportunity to cross examine the named plaintiffs as to whether they were still in need of this remedy, which was a court-administered smoking cessation program.

The question was, after establishing essentially this form of equitable relief, having already certified the class, "Were the named plaintiffs required to continue smoking during the prolonged pendency of the class to remain "representative?" Justice Scalia ruled that there was a good chance the court would want to review that issue and granted a stay.

He also thought irreparable harm would occur if the defendants deposited $240 million into court, which would be put into an interest-bearing account and paid back to the tobacco companies if not used. The certiorari petition in the case was filed this past Thursday.

The essence of the complaint here is that state courts are not requiring individualized reliance in consumer fraud class actions. I think that the argument in the case is overblown. I know that every state consumer fraud statute says it's the fraud that is the essence of liability, and that reliance becomes a secondary issue for compensatory purposes only. So, I don't think it as major an issue, or as new a problem as Russell seems to think.

I also would like to talk about the third-party financing issue, simply because although I'm somewhat agnostic about this issue—I don't have a strong position in favor or against—it strikes me that the definition that John Beisner gives of third-party financing would equally apply to insurance companies that pay for defense costs.

It would also apply to stockholders, whose corporate investments finance corporate litigation designed to achieve a business advantage, as well as avoid liabilities. So, it strikes me that we're not talking about something very new. We're just talking about financing a side that hasn't had that advantage in the past. I also think that it's not simply helpful to cases that are weaker, but primarily cases that are going to be expensive to litigate. Perhaps one or two law firms in a state can finance this litigation already, but may not be able to finance a third case, no matter how strong it is.

The traditional way to finance such litigation is to seek fellow lawyers as co-counsel who will invest in the case. That third-party financing opens that door to non-lawyers, does not seem troubling. There is a clear trend in Europe to engage in this third-party financing, and it seems like it is probably inevitable in this country. But I don't think it's also a major change in the way that litigation is financed, at least on the defense side.

PAIGE V. BUTLER: Okay. Great, thank you. We have time for questions now.

AUDIENCE MEMBER: **[Inaudible Question—re: impact of arbitration agreements]**

ROBERT S. PECK: It's hard to say how much arbitration has effected litigation. We saw the ABA report on diminishing jury trials, but how much of that can be ascribed to the fact that arbitration takes place? Arbitration requirements are in the vast majority of credit card agreements, although credit card companies have been cutting back. You buy a new computer, the box has a little slip at the bottom that basically says you've agreed to arbitration once you turn on the computer—things like that. It's clear that for a while it was thought that arbitration was definitely cheaper and less expensive and there was a trend toward it.

More and more, both corporate counsel and plaintiffs are in agreement that it is not cheaper, and that it is taking on all the aspects of litigation in another form. Parties are frustrated by the lack of authority to appeal when an arbitrator seems to not understand the issue. And so, I think that a cer-

tain amount of displacement of trials can be ascribed to arbitration, but how much of it, I can't tell. But I also think that there is increased dissatisfaction with arbitration, and the cases that make it up to the U.S. Supreme Court, which seems to generally like arbitration, are testimony to that dissatisfaction.

I think in *AT&T v. Concepcion*,[19] recently argued at the Court, the questions that the court asked the lawyers indicated a certain amount of hesitation in staying on that arbitration bandwagon.

J. RUSSELL JACKSON: One of the interesting things about arbitration, and certainly the class issue as it relates to arbitration, is for the decisions kind of outside of California that have recognized that you can basically exclude class actions from arbitration if you do some other things like agree to pay for people's costs of prosecuting the claim and various other types of financial incentives which, again, increase the expense of it for the defendant.

You find less and less people proposing it because it gets so expensive. But the alternative is also not one that companies often are willing to bear either, so it will be very interesting to see what the Supreme Court tells us about the *Concepcion* case and see how that gets folded into a lot of these form arbitration agreements across the country.

AUDIENCE MEMBER: Some how it seems that in my federal court I'm seeing a sort of deluge of wage-and-hour cases and you when get to pre-certification discovery and you give it to the defendant and the fight starts with, "Who can contact them?" "How can they contact them?" "What can they find out, what's personal and what's not?" They sort of have to reinvent the wheel, it seems, in every case with you just fighting as soon as your feet hit the ground. Shouldn't there be some more regularity to that, don't you think, so we can at least find out what we need to find out in order to get to the Rule 23 process?

ROBERT S. PECK: I absolutely agree. There ought to be regularity and the fact—it constantly surprises me, despite more experience with litigation—how many issues seem to be unsettled and have to be individualized in that way. That's, I think, part of the challenge that we have to find a way past, because that's what makes cases unduly expensive.

J. RUSSELL JACKSON: I will tell you—and I don't do wage-and-hour cases, so I'm not intimately familiar with all of those details—I do know from representing a number of defendants in litigation, it's amazing the different ways in which documents and basic information is kept by various companies across the board, and depending upon your particular companies that may be subject to wage-and-hour claims. I'm just rattling through the number of different ways in which I can imagine my client would tell me even getting the basic information is going to be extraordinarily costly and

burdensome because we have to go through the SAP system or we have to do this, that, or the other.

The bottom line for me is that I understand absolutely; I think we would all agree that it would be nice to have a standardized answer to the question. It may not be as simple as that when it comes to how people actually keep their records in these cases.

AUDIENCE MEMBER: I'm certain you've been in my court, because that's what I hear. This is in Kansas City, that's electronic in Cerrito, California, this is in Albuquerque; gosh, we just don't keep everything together. You get kind of a little suspicious about what they're doing.

J. RUSSELL JACKSON: You may be suspicious about it. I represent a company right now, and I won't tell you who they are or really even the industry they're in, other than to say that they had a number of companies under one umbrella. They bought a competitor and took some of their little companies and they're here, there, and beyond. Everything is in historic legacy systems; none of which communicate with the other. I have no idea how they do any actual business. But when I have to tell a court, "This is really what we have to do in order to get this information, and part of it involves sending somebody on a plane to Orlando to go through file cabinets," courts look at me like, "Are you crazy?"

Unfortunately, this is really the way the company operates. And particularly, we talk about access to justice and civil justice, and often people like to think about the companies that I represent—big companies. But there are lots of much smaller companies who employ people and who do many other things, and are in fact, subject to these same kinds of suits who don't have hugely sophisticated systems for record keeping—particularly when it's not record keeping that's going to be making them money or moving product from here to there.

And so, it is frustrating, I am absolutely certain, to be the judge faced with someone who comes to you and tells you that. But I wouldn't necessarily assume that they're feeding you a line. In many instances, it really is true. Then the question becomes, "How creative can the lawyers be about trying to shortcut, 'Well what do we really need? What do you really have to have? rather than, 'I want everything!'"

AUDIENCE MEMBER: Can you talk a little bit more about the issue of e-discovery—the costs in the emerging rules related to e-discovery?

ROBERT S. PECK: Well, sitting right behind you is Judge Rosenthal who is moderating the next panel which will touch on that, so I think we're going to let them focus on it.

AUDIENCE MEMBER: Well that was my point in getting into the electronically stored information. The oldest and all of the cloud computing, the court is going to have to be much more proactive in proportionality and the other issues, or we're going to have a disaster.

AUDIENCE MEMBER: If you recognize that the third-party financing is partly due to the fact that a significant number, if not all jurisdictions, you cannot sell the claims. Have you considered why don't we create a market that allows people to buy and sell the claims? I understand that there are good ethical objections but that also means the defendant can buy claims.

J. RUSSELL JACKSON: The defendant certainly gets an opportunity to buy the claims in a settlement at any—

AUDIENCE MEMBER: Outside of litigation there would be a pure market for the purpose of sale. That lawyers come, and cut the courts out of it, and creates a market that values the claims which the defendant can buy if they want to.

ROBERT S. PECK: I think that's a very interesting notion. I don't think either of us has heard it suggested before, but it points out something else that I think is part of the inadequacy of the analogy that Russell used before when he quoted Judge Posner about going to the roulette table and choosing to spend less than all your money on a gamble. That may be true if you're treating the time that you're actually filed against and hailed into court as the moment that you've decided to take the gamble.

The fact is that you've taken the gamble when you violated the law, whether it's a wage-and-hour law or employment discrimination law. That's when you took the gamble. Therefore, the size of that gamble that you took was determined at that point, and not necessarily by the point that you've been brought to court to be accountable.

J. RUSSELL JACKSON: The assumption that you've violated the law is in fact my point exactly. Many folks don't think they took the gamble and later in the day get sued for amazing things. Your Crunchberries don't have real berries in them, and thus that's a consumer fraud claim. That's a real suit that was fortunately thrown out by a judge who had some good common sense.

ROBERT S. PECK: Usually the examples of frivolous cases are those that have been thrown out without hesitation.

AUDIENCE MEMBER: Bob you started off this discussion with the observation that access to justice, access to litigation systems, is a big concern and in some sense all the things that were discussed today can be unified

with that theme. And I wonder, as I think about lowered pleading standards, increased use of aggregation, third-party financing of litigation—it seems as though we're solving this access to justice problem, over and over and over. And so it doesn't surprise me that we get more litigation; I wonder how we get more meritorious litigation?

ROBERT S. PECK: Well, as I think I outlined, the trends are actually mostly against it. Most of the things that you've talked about—more aggregation—the trend is not right now for the courts, more aggregation. The trend is an attack on the aggregation devices that we currently have. Third-party financing is a lovely debate at the moment, but it's not something that has taken hold. But if you look at the other things that I'm talking about, the expenses in litigation and other obstacles, that's what is happening. Meritorious litigation is being deterred.

And when you up the stakes—because of the expense of the litigation, because the courts are underfunded, because of the influence of politics—what you're doing is you're forcing bigger gambles. You are forcing everyone to go all in on big cases that either pay big or pay nothing. And you're squeezing out the smaller cases, and that's the concern that I was expressing.

PAIGE V. BUTLER: Thank you very much to the panelists.

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1 *See* Citizens United v. Fed. Election Comm'n, 130 S. Ct. 876 (2010).

2 *See* Republican Party of Minn. v. White, 536 U.S. 765 (2002).

3 *See* MODEL CODE OF JUDICIAL CONDUCT (2007), *available at* www.abanet.org/judicialethics/ABA_MCJC_approved.pdf.

4 *See* Caperton v. A.T. Massey Coal Co., 129 S. Ct. 2252 (2009).

5 *See* Dura Pharms., Inc. v. Broudo, 544 U.S. 336 (2005).

6 *See* Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2007).

7 *See* Ashcroft v. Iqbal, 129 S. Ct. 1937 (2009).

8 *See* Conley v. Gibson, 355 U.S. 41 (1957).

9 *See* Eisen v. Carlisle & Jacquelin, 417 U.S. 156 (1974).

10 *See* Dukes v. Wal-Mart Stores, Inc., 603 F.3d 571 (2010).

11 *See* Daubert v. Merrell Dow Pharms., Inc., 509 U.S. 579 (1993).

12 *See In re* Zyprexa Prods. Liab. Litig., Nos. 04-MD-1596, 08-CV-5165, 2010 WL 4052813 (E.D.N.Y. Oct. 14, 2010).

13 *See* McLaughlin v. Am. Tobacco Co., 522 F.3d 215 (2d Cir. 2008).

14 *See In re* St. Jude Med., Inc., 522 F.3d 836 (2008).

15 FED. R. CIV. P. 23.

16 *See In re* Meridia Prods. Liab. Litig., 328 F.Supp.2d. 791 (N.D. Ohio 2004).

17 *See* McLaughlin v. Am. Tobacco Co., 522 F.3d 215 (2d Cir. 2008).

18 *See* Philip Morris USA, Inc. v. Scott, 131 S.Ct. 1 (2010).

19 *See* Laster v. AT&T Mobility LLC, 584 F.3d 849 (9th Cir. 2009), *cert. granted sub nom.* AT&T Mobility LLC v. Concepcion, 130 S.Ct. 3322 (May 24, 2010) (No. 09-893). Oral argument in the case took place Nov. 9, 2010 as Docket No. 09-813.

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UPDATE ON THE FEDERAL RULES ADVISORY COMMITTEE

Alexander Dimitrief, Bruce H. Kobayashi, Emery G. Lee III,
Martin H. Redish, Donald H. Slavik, John Vail
Moderator: The Honorable Lee H. Rosenthal

JUDGE ROSENTHAL: Thank you very much. It's a great pleasure to be here, and on behalf of the entire panel, I want to thank you for the opportunity to address you on what we think is just a fascinating issue. Of course, we think that a glass of red wine and the pocket part of Moores or Wright & Miller is a great Saturday night, so you may not share our sense of the joys of life. But this really is a wonderful panel because we get to ask and suggest some of the issues lurking in the question: what most needs to be done to make the civil justice system in this country work well? Not just better than it's working now, but work well. That requires, in turn, that we think about what the most pressing problems are and the most promising achievable solutions.

My focus on that is what kind of rule changes—changes to the Federal Rules of Civil Procedure in particular—are the most likely candidates to help in this work. And I come to that focus because, in addition to my work as a federal district judge sitting in Houston for the past eighteen and a half years, before that I was a trial lawyer in Houston, that in addition to that, since 1996, I have been a member of the Federal Rules work. First as a member and then as Chair of the Civil Rules Committee, and since 2007, as Chair of the Standing Rules Committee, which coordinates the work of all of the five advisory rule committees. So, I think that this is the most interesting question in the world, right up there with the meaning of life.

The other members of this panel will each bring a different perspective to this question, and the series of sub-questions that are lurking. Immediately to my left is Dr. Emery Lee. Dr. Lee is a Senior Researcher at the Federal Judicial Center in Washington. He is going to focus on some of the empirical data that the Federal Judicial Center recently gathered and studied for the benefit of the Rules Committees at a conference that you will hear about that tried to itself look at just this question. Sitting next to him is Don Slavik. Don has represented only plaintiffs in product liability actions around the country for almost thirty years. He is from Steamboat Springs, Colorado and Milwaukee, Wisconsin, and he is currently involved in litigation that includes the Toyota MVL, which gives you a sense of the level of practice that he is an expert in.

Seated next to him is Professor Marty Redish who is the Louis and Harriet Ancel Professor of Law and Public Policy at Northwestern University Law School. Marty has authored or co-authored fifteen books, over eighty scholarly articles in the areas of civil procedure, federal question,

constitutional law, and freedom of expression. He is the sixteenth most cited legal scholar of all time—that's pretty amazing. And he's Senior Counsel of the firm of Sidley Austin. Seated next to him is Dr. Bruce Kobayashi. Dr. Kobayashi is a Professor of Law at George Mason. He holds a Ph.D. in economics. He has written on law and economics in IP and antitrust and other fields. He's been here since 2000, and before that, worked for the Sentencing Commission, the Federal Trade Commission, and the Department of Justice, Antitrust Commission. His experience is also quite broad and varied. Seated next to him is John Vail. John Vail is a man of great integrity and truthfulness. He is an attorney with the Center for Constitutional Litigation, and he represents the interest of the plaintiffs in rulemaking activities.

Finally, Alex Dimitrief joined General Electric in February 2007 as its Vice President for Litigation and Legal Affairs after spending twenty years as a trial lawyer at Kirkland & Ellis. He is responsible for litigation and enforcement proceedings in the U.S. and in international jurisdictions against GE, and he also oversees the company's worldwide compliance and integrity programs. As you can see, we have a panel that represents both sides of the V and a lot of different areas in between.

So I can promise you, at the end of this panel discussion, you will get a mix of information from different perspectives on the problems that the civil justice system is grappling with. You will get some ideas for long-range approaches to address some of those problems, and I hope you will get some ideas for immediate ways action can be taken to address some of these issues. I am just going to take about two seconds to introduce the Rules Committees and its recent work. The Rules Committees for the Federal Rules of Civil Procedure have been dealing with these problems, and by these problems I want to focus on what has been described as cost and delay.

We have been hearing about these problems for a very long time. They are not new. If you go back into the 1930s debates on what became in 1938 the Federal Rules of Civil Procedure, you will find quotes of people in the committee worrying about cost and delay of this discovery business. It was not hedged around somehow. If judges did not have ways of controlling what was called in those debates, "fishing expeditions." It sounds amazingly current. The rules have been amended many times, particularly the discovery rules more than any other part of the rulebook, to try to cope with changes in discovery resulting from changes in litigation practice, in business, and most recently, from information technology, and the new challenges presented by electronically stored information.

All of those challenges and the furor that resulted from them**,** led the Civil Rules Committee last May, to hold a conference at Duke University Law School that was really thought of as something like the Pound Conference of years ago. These seminal conferences that have as the purpose to step back and take a hard and disciplined look at how the civil justice sys-

tem is operating from pleading through resolution, including importantly, electronically stored information. And the information we brought together to make sure we were disciplined and thorough in looking, included empirical information gathered by Dr. Lee and information on the actual costs of discovery in the face of the challenges posed by electronically stored information.

We also looked heavily at state practice because the state courts are enormously creative in many ways ahead of the federal system in thinking about new ways to address some of these issues. And at the end of Duke, we discovered that we had some concrete ideas to go forward with, and we had a better awareness of some of the issues, and I'm going to come back and talk about those after we hear first from our panelists. So, we are going to start with Dr. Lee who is going to give us a description of what he learned as he gathered the information necessary to help the Duke conference understand what really was going on.

EMERY G. LEE: Thank you, Judge. First, I have to state my disclaimer that everything I say represents my views only and certainly not the views of anyone else.

JUDGE ROSENTHAL: Ditto.

EMERY G. LEE: My supervisors consistently remind me that I only speak for myself, so I remind you. The other thing I want to mention real quickly is that I actually taught at George Mason for a year in the mid-1990s, but that is not actually true. I taught at a much smaller campus that is somehow buried in the middle of this monster campus that you are visiting today. This place has undergone a major transformation since I taught here. I am sure the faculty are much better too. I want to talk a little bit about the Duke conference and the research we did for it. I want to first of all say how the Duke conference is perceived, to the extent it is perceived, is largely about cost. And I am going to talk about cost, but I am going to leave that for the end, and instead, I'm going to talk about the other parts of Rule 1 very quickly.

Rule 1 of the Civil Rules has three goals for civil rules: just, speedy, and inexpensive resolution of every matter. So I am going to talk a little bit about justice first. We did an attorney survey of practitioners in recently terminated, recently closed federal cases; so these are people who are going to be in state court some of the time, but these were people in federal court. We got over 2,000 respondents to the opinion questions, and I think that is a pretty good response rate of 47%, so when I am talking about the opinion questions, these are pretty good numbers that I think you can take to the bank.

We asked two questions at least that go to the question of justice in the federal courts today. The first question we asked respondents to agree or

disagree with the statement, "The outcomes of cases in the federal courts are generally fair." This question was written really to get at attorneys' attitudes toward the substantive fairness of outcomes in federal court. What is interesting is a majority of every group of attorneys—those who represent primarily plaintiffs, those who represent primarily defendants, and those who have a mixed practice—agreed with the statement.

But there was actually some interesting variation among the different groups of attorneys. Attorneys who primarily represent defendants agreed with that statement, agreed or strongly agreed—I am just going to stipulate I always mean that when I say "agreed"—80% of the time. Only 4% of those representing primarily defendants disagreed with the statement. So, the defendant attorneys in our sample were fairly satisfied with the substantive outcomes of the cases in federal court overall. Those with a mixed practice, about 70% of them agreed with the statement.

And this is a word that gets me in trouble with my supervisors, but since I am not speaking for them, I can use it, *only* 53.9% of plaintiffs' attorneys agreed with the statement. So one thing I want to bracket here at the outset is even though a majority of each group of attorneys expressed a high degree of satisfaction with substantive outcomes, there was some variation there that has to be kept in mind. When we come to the procedural fairness of proceedings in federal court, the picture is a little different. At least two-thirds of every group of attorneys agreed with the statement, "The procedures employed in the federal courts are generally fair."

But again, there was some variation based on practice area. So, 85.5% of defendant attorneys agreed with the statement, "The procedures are generally fair." Almost 80% of those with a mixed practice, and about 70% of those who represent primarily plaintiffs. So one question to think about is, why is it that the different groups of attorneys express different views with respect to the fairness and justice of Federal proceedings? Okay, so that is justice.

Speedy. Judge Rosenthal will talk cost and delay. Never do a Westlaw search for the phrase, "cost and delay," and do not Google it either. But what is interesting is that delay is a normative term, and as an empiricist, I am very reluctant to use it. But when you look at the time to disposition in federal court, what you really have is two worlds. For the cases in our closed case sample, one-half of those cases terminated in under a year or less. Again, half of the cases are reaching termination in the district court in a year or less. Now, I cannot say what is too long, but a year to do anything substantial in this world does not seem excessive. If half the cases terminate in a year, I am not sure that is too long. What is interesting is that those cases overwhelmingly are settlement cases.

Almost 80% of those cases actually were settled by the parties in a year or less. Setting aside the question of the merits of the settlements, whether they were coerced settlements or what not, because of the fear of costs, those cases are reaching disposition fairly quickly. The other cases

that take more than a year are probably where the committee would want to focus its time. So maybe one thing we might look at going forward is trying to predict what cases are going to take longer. The way I put this as an empiricist, which no one else would agree with this, is to ask, what is different about the cases that settle in a year versus the cases that take more than a year to settle? What is it about those cases that make them take longer? And maybe we can discuss that.

Costs. I am going to say a couple of bracketing comments here. First of all, there are actually two separate discussions of cost, and we have heard both of them already this morning. They are very different discussions of cost, and I think they have to be kept separate. They are often put out together, but I think that they are actually very different. One is the access-to-justice point. Many, many people, typical families in this country, do not have the means to actually litigate their rights in court.

There was a recent *New York Times* front-page article about this, and it was about the investing in litigation issue that was also discussed this morning. That is a real problem that people face. In fact, in the *New York Times* article, and I will plug myself, in that *New York Times* article, it cited a figure from my research for the Duke conference on the cost of litigation to plaintiffs. We found the median cost that was reported by the parties—and again, this is costs reported by the parties, so these are estimates—was $15,000 to litigate a case to termination. That was the median figure.

The *New York Times* cited that as too much for a typical family of modest means to litigate in federal court. When I presented the $15,000 figure in March of this year, people told me that was way too low. So, $15,000 is too high for a lot of people, but it strikes a lot of people as way too low. And if you know a little bit about statistics, that is the median, so that is the middle number. If you take the cheapest case to the most expensive case, line it up in order, the median is just the middle one. Just like median home prices are recorded, not average, because of course, averages are distorted by really high values at the upper end.

The average costs for plaintiffs was actually almost $67,000, and that probably strikes you as closer to the ballpark than $15,000. Interestingly enough, defendants have higher costs than plaintiffs. The average costs for defendants who are non-governmental defendants is $122,000. That was the average cost to litigate the case to termination. I can see smiling in the audience. You have to remember, that includes cases that settled in less than a year. And a case that settles in less than a year is not necessarily going to have very high costs. Now, it might settle because of the fear of costs, but it does not have high costs.

The costs were avoided by the settlement. Some factors that we found associated with higher costs, I am just going to go through these not quickly, but just sort of bullet form. Again, longer case processing times: time is money, and that shows very clearly that the longer a case takes to terminate, the more it costs. Stakes was the number one determining factor in costs.

If you just regress the stakes on the costs, especially for defendants, stakes explains about half of the variation in costs alone. And in a real sense, that is how it should work. The more a case is worth, the more the parties should be willing to spend to litigate it. So that makes sense.

Interestingly enough, non-monetary stakes also matter. So if the case involves non-monetary stakes, such as bad precedent, business relationships, reputation, threat of other litigation, that also increases costs separately. Factual complexity, of course, is associated with costs, and electronic discovery. Electronic discovery is an interesting topic, and we are going to talk a lot about it, I am sure. One of the strange findings of our study was that once you controlled for other factors, like stakes, type of case, type of parties, the time to disposition, different things like that, producing parties did not have higher costs than parties in cases without electronically stored information (ESI). That does not seem right.

But I have an explanation for that, and this goes along with the RAND study that was also presented at the Duke conference. It turns out that the cost of producing ESI varies greatly. So sometimes in a case where you produce ESI, it's email, it's on the server, you run a search, you produce it. I am not saying it is cheap, but it does not cost a whole lot. Other times, you have e-discovery, and you have a warehouse full of backup tapes, legacy files, all kinds of crazy stuff that people are going to talk about. Those cases are very expensive.

But see, the way the statistical model works is that something that varies a lot from case to case, even if it has a big coefficient, it is going to have a huge standard of error, and it does not reach statistical significance. But that is probably what is going on there. Producing parties do have high costs in some cases, but in other cases, the producing is not much, and that is what makes it fall out. What is really interesting is the biggest costs in the e-discovery cases are actually what I am going to call the symmetrical cases.

That is when both sides of the litigation ask for and produce information that is kept in electronic form. Those cases overwhelmingly in our study had the highest reported costs. The average costs for all the cases we had, where the defendant reported that they both asked for and produced electronically stored information, was a quarter million dollars. And the average costs for plaintiff attorneys, where the plaintiff said that they both asked for and produced electronic information, was $170,000. Sometimes people say, "Well, your research shows that electronic discovery does not affect costs," and I would say, "then you are not reading the same research that we put out because we are definitely finding there is an effect in those symmetrical cases," which do not get talked about a lot. I want to throw that out there.

Also, another important finding about electronically stored information, is that disputes over electronically stored information are extremely expensive. Well, duh, right? But even if you control for everything else—

so you control for the stakes in the case, you control for the type of case, you control for how long the case took, you control for everything I have discussed and more—each type of dispute over ESI increases costs 10%, and that is true for plaintiffs and defendants. If there is any way to change the rules to make it less disputatious about electronically stored information, that would have a huge impact on the cost of cases. Those disputes are extremely costly, and no one is going to say that they are not.

I am going to say one more thing about costs. One part of this discussion that is curious, because what the Rules Committee does is civil rules, it talks about civil rules, and it does a lot; you would not believe what this committee does. It is truly a remarkable body, and the amount of expertise blows me away every time I am there because I really do not know much about the civil rules. Judge Rosenthal knows that, and everything I know, I learned from her. But we talk about costs of civil litigation, we talk about the reasons why costs in civil litigation have increased, and we talk about that sort of in isolation; and I just want to offer this at the law and economics seminar. I am going to make maybe an economics point. But it seems to me that in lots of service sectors of the economy, we talk about skyrocketing costs.

The cause of those increases cannot really be the discovery rules, can it? I mean, here we are at an institution of higher education. Everybody knows that the costs of higher education are skyrocketing. Is that because of the discovery rules? Healthcare costs are skyrocketing. Is that because of the discovery rules? There seems to me, to be a kind of gap there when we talk only about the rules, and do not look at larger societal or economic factors that might be affecting these things, and I understand that there are actually some economic doctrines that get at this question. And that is one thing I think maybe the committee might think about going forward.

Finally, I want to talk a little bit about proportionality. That was a topic that came up this morning, and the rules authorize the judges to limit discovery to proportionality. The rules build in proportionality in all kinds of ways. We asked respondents on a scale of 1 to 7 to say how proportional the discovery in the case was to the client's stakes with 1 being too little, 7 being too much and very disproportionate, 4 being just right.

What was interesting was that more than half of the respondents, and that includes both plaintiffs and defendants in the named cases, said that the costs in the case were proportional to the stakes, just about right. Just the right amount. So, when we think about making the rules better, and I would want to do more studies like this, but there is evidence that in most cases, proportionality is not a problem. Again, the cases that settle quickly, that reach a resolution without the expenditure of a lot of costs, probably are proportional cases or even on the low side of the 4.

But there are about a quarter of the cases where it is a 5, 6, or a 7, although very few cases are a 7. But about 15% of the cases are in the 6 and 7 range, and those are probably the cases to think about going forward. And

if we could find a way to identify those cases and figure out how to apply the rules to them, that would be a real step forward. Thanks.

JUDGE ROSENTHAL: That's great. Thank you, Emery. One of the things that was striking in Emery's research is that a similar study was done in the late 1990s to try to get a feel for the costs and the satisfaction with how well the rules were working, and the pattern that emerged was very similar. Of course, what is striking about the 1990s is that it was before electronic discovery swamped the system or became ubiquitous, depending on your view of electronic discovery. But what was striking is that just as Emery's recent research revealed, most of the cases that chug along pretty well, do not require much judicial effort, and the satisfaction of the parties appears pretty high, at least as reported.

There is this stripe of cases in which the costs are high, the disputes are significant, and the perceived drain and distortion of the system are viewed as problematic. And it is fascinating that that same pattern existed before electronic discovery, although it is clear that electronic discovery is making the complaints about it louder and perhaps more pressing.

There is such a link between pleading and discovery. Indeed, the Supreme Court in both *Twombly*[1] and *Iqbal*[2] said we got to do something about the way the courts are applying the pleading standard because we are afraid that too many cases are simply moving on to full blown discovery, and these are cases that do not deserve that kind of resource being devoted to them. So next, I am going to ask Professor Redish to share with us his views on pleading and discovery.

MARTIN H. REDISH: Thanks, Lee. My research recently has been about the link between pleading and discovery, and the conclusion that I come to is basically that there's one area that needs no change by the Rules Advisory Committee and another area that needs significant changes. And to understand my perspective, let me take a minute to discuss what I refer to as the deep structure of procedure. When we decide basic procedural issues, we rarely look at the deep, underlying political, theoretical structure of the procedural system, and what it is trying to get to. I think it is essential, that in looking at both the pleading and discovery issues, we understand those different factors.

In my scholarship and the paper I wrote for this symposium, I go into some detail. But the most important, underlying, theoretical factor, is the maintenance of the substantive procedural balance. That procedure can either distort substantive rights or it can give life to substantive rights. And the delicate tightrope that has to be walked requires very careful allocation of different priorities. The danger in the pleading area is simply the lack of information that we have at that point. When we combine it with what Judge Charles Clark did in the adoption of the Federal Rules in 1938—the creation of the whole discovery process, the shift from fact pleading, the

front-loaded system to much more of a back-loaded system—we recognize what he was trying to do.

Through the creation of the discovery process, through the manipulation of procedure, he was trying to enforce substantive rights more effectively. Because often, plaintiffs could have substantive rights in name, but unless they are given access to some kind of information gathering devices, they will never be able to prove their claims, and in that sense, we will be under-enforcing the law. What Judge Clark may not have fully comprehended at the time was the danger of over-enforcing the law. That through the provision of burdensome, invasive, and often very expensive discovery devices, he may have been pushing defendants into settlements, that if we had perfect knowledge of at the pleading stage, we would not have allowed it to proceed to the discovery stage.

And in that sense, we have distorted the substantive law; those costs are passed on to the consumer, yet those are not really costs that should be borne by the consumers. So the goal is to, what I would describe as, allocate the risk of the wrong guess. At the pleading stage, we are in danger of guessing wrong. We are in danger, on the one hand, of dismissing claims that if we had perfect knowledge of, we would have known it should have been vindicated. And we, on the other hand, have the risk of allowing claims to proceed to burdensome and expensive discovery, that if we had perfect knowledge of, should not proceed.

How are we going to allocate the risk? Which of those two are we more likely to be willing to risk? Well, when the *Twombly* decision came down several years ago, it was difficult to grasp what the Court was actually trying to do. It was not an opinion I would put in Justice Souter's hall of fame. In fact, when I read the opinion, instinctively, I wrote at the top, "C-see me after class." But when one looks at it more closely, one can see that he was really on to something. It is, therefore, unfortunate that the reaction against it has been so extreme. The assumption appears to have been by many of the critics of the *Twombly*, of the so-called plausibility doctrine, that it has simply reinstated the fact pleading requirement that Judge Clark's committee in 1938 was trying to get away from.

As I tell my students: in fact pleading, facts are to co-pleading what cookies were to Cookie Monster. They can never get enough. You would have a system where you would have bills of particulars, and they would go on and on, and plaintiffs could not reasonably be expected to have those facts. The classic case of *Conley v. Gibson*,[3] where a union, long known for its racist attitudes, refused to help African-American workers who had been laid off along with white workers, but all the white workers were called back, and none of the African-American workers were.

The African-American workers brought a suit against the union alleging that they were involved in a conspiracy to discriminate racially, in violation of the labor laws. Under a fact pleading system, where you have to say who, what, where, and when, they would not have survived. But in

1957, when we had already moved to so-called notice pleading, the claim was allowed to proceed. That was a classic illustration where the old fact pleading system would have resulted in under-enforcement of the substantive law. The assumption of a lot of the critics of *Twombly* and *Iqbal* is that they take us back to the pre-*Conley* days. That is not really accurate.

The only alternative to fact pleading is not simply conclusory making an assertion and getting "open says me" to get to discovery. I think of when I was clerking on the Second Circuit, and we had in front of us Rabbi Klein, somebody who was a retired Rabbi and had lost money in the stock market. And Rabbi felt he did not lose money unless somebody was cheating him. So he brought lawsuits, both in federal and state court all over the New York area, against Goldman Sachs and Merrill Lynch. It was wonderful to see lawyers from Sullivan & Cromwell and other big firms complaining to the court that Rabbi Klein was harassing them.

In one case where a district judge imposed a bond requirement on Rabbi Klein, implying that perhaps Rabbi Klein's elevator did not stop at all floors, Rabbi Klein sued him for libel. But if we think about this case—now admittedly, this would be controlled by the PSLRA,[4] and even then it was a 9(b) case—but think about this. Is it possible that Rabbi Klein had been cheated by Goldman Sachs and Merrill Lynch? For all we know, they were saying, "How did he find us out?" But not likely. It was at least as equally explainable by the fact that people were sometimes losing money back then in the stock market. Should we have allowed him to get to discovery in the hope that maybe he would unearth something that indicated that his claim was valid? Of course not.

That would be economic and moral nonsense to let a plaintiff get by with simply conclusory assertions. And that is really all the plausibility test does. It says if you do not have detailed facts that you can allege in good faith, then the situation has to smell fishy. You are almost in a pleading analogy due to the evidentiary doctrine of race. We say that probably would not have happened unless something went wrong here. Let's find out more about it. And if you look at all of the pleading cases the Supreme Court has decided, including *Conley*, they are reconcilable with this text.

Every complaint that was allowed to proceed to the discovery stage was one where we could quite reasonably say the claim was plausible. Not that we were going to impose liability at the pleading stage, but we needed to find out more. And it seems to me that that is the appropriate standard. So those who are asking for a change in the rules have to provide some sort of statement of what their alternative is. If their alternative is simply what I refer to as a notice pleading minus standard, where you simply can make a conclusory allegation without any indication that you might have some validity to your claim, and who knows, you might get lucky in discovery, then that is not a viable alternative.

So, this is an area where I would not want the Rules Committee to change the current practice. Perhaps if any change were to be made, it

would be simply to codify the plausibility standard by name. But perhaps it is better to just not even mess with it. The discovery area, however, is one where I think change does need to be made. And a basic change on a fundamental issue that the original Rules Committee never considered, yet the practice today is unquestioned. That is the practice of, discovery costs lay where they fall. That, if a plaintiff asks a defendant to produce documents, whether electronic or not, to appear for depositions, to answer interrogatories, the costs of producing that discovery fall on the responding party.

There is nothing in logic or law that suggests that is a proper allocation. In fact, think back to the basic contract doctrine of *quantum meruit*. Put it in a modern context. You find out that one of your co-workers is going to McDonald's for lunch. You say, "Could you get me a Big Mac and a Coke. I would appreciate it." And the guy comes back with the Big Mac and a Coke. Whose cost is that? Is it his cost because he initially laid out the money? Was he not doing that for your benefit with no basis to think that there would be a favor for you other than to get it? That the cost is still yours? Well, that's what discovery is. Discovery is not for the benefit of the producing party.

It is not like all other litigation costs that a defendant bears. Those are costs to protect his or her own rights. The discovery is not for his benefit. Indeed, it is likely to hurt him. It is for the benefit of the requesting party. Therefore, those costs really belong to the requesting party. If we recognize that basic principle, we can avoid many of the problems of discovery in the kind of case Judge Rosenthal was talking about, the so-called big case where the costs of discovery are enormous. Think of it this way. If I am given an unlimited research budget at Northwestern Law School, I will not think twice about going to a conference, buying a book, or hiring a research assistant.

If I am given a budget that I have to allocate, I will ask myself is this really necessary? The danger then really is not abusive discovery. That is a relatively rare phenomenon. It is excessive discovery. We need the requesting party to avoid the economic externality of not having to pay for the discovery costs. Now, very often, plaintiffs will lack funds for those discovery costs, so I think if we understand that funding of litigation is often coming from the plaintiffs' law firms, it is not as much of a problem as it otherwise might be. Perhaps we want to subsidize particular causes of action through discovery costs.

But if so, we have to say it transparently. We do not do that now. There has been no democratic choice to subsidize the discovery costs. Simply by changing the rules to say discovery costs are deemed costs of the requesting party, I think we can avoid significant discovery problems without worrying about the transaction costs of having the court get involved and impose the very, very vague and subjective proportionality requirement.

JUDGE ROSENTHAL: With that modest suggestion, I think it is useful just to take a second and think about how really significant of a change that would be. Back in, I guess 2006, when we were working on the electronic discovery rules, we had a pitched battle all through the Rules Enabling Act process, which is multi-layer, multi-filter, transparent, with lots of public comment. And in the Judicial Conference of the United States—I think we escaped defeat by one vote on the very minor suggestion that in a particular category of electronic discovery involving information not reasonably accessible—that you might consider a judge imposing a shift of some of the costs of getting that kind of discovery to the requesting party.

We almost went down in flames, and I had really black hair before that battle erupted. But the point is, it is a sensitive and significant set of issues. So with that backdrop, and remember the first question, something that was not only a good idea to make the system work well, but also could reasonably be achieved. Think about it in those terms.

MARTIN H. REDISH: Can I make a brief, just one sentence response to that?

JUDGE ROSENTHAL: Sure.

MARTIN H. REDISH: The beauty of being a law professor is that I get to change the Federal Rules any time I want. And as an academic, that is what I am doing. I understand Judge Rosenthal's practical concern. What I do say at the end of my paper is I am not an idiot. I understand that this is not likely to be adopted. I wanted to start a debate so that judges who have the power under Rule 26(c) now to shift costs, but are extremely resistant to doing so, would at least be more willing to shift costs. I think shifting costs is a misnomer under my *quantum meruit* theory, but at least getting them to ease up on the unexplained resistance to do so, and to start a debate that really has not occurred yet. That is all I planned to do.

JUDGE ROSENTHAL: And in defense of all the judges in this room—I think I would probably not speak for us all because we do not speak for anybody but ourselves, as you have heard—but it is also remarkable that in my experience, I am almost never asked to shift or assign any part of the cost to the party requesting the discovery. So we are talking about changes in litigant and lawyer behavior and expectations, as well as judicial attitudes. I would like to now ask Don Slavik for his perspective on some of these pleading and discovery issues and comments on the challenges of litigation and the costs of discovery from the plaintiff's perspective.

DONALD H. SLAVIK: Good morning. Thank you, Judge. From a plaintiff's perspective, the challenges of litigation do significantly look at costs. And I can make a comment over my thirty years of doing products liability work

where, thirty years ago, many plaintiffs' attorneys would handle a product liability case against even an automobile manufacturer, which is a good portion of my work. That has shrunk. That has shrunk because of the cost of litigation, the cost that it takes to hire experts. The cost it takes to get through the discovery process, to the point that I must admit, it is probably to my firm's advantage that we have the ability to fund some of these cases that more of them come our way because so many plaintiffs' attorneys can't do it anymore.

The attorney in Omaha, Nebraska cannot afford it anymore, he has to call my firm, or the attorney in Bloomington, Indiana. Frequently, that happens nowadays. And it is even at a point that many of the larger firms that were doing it thirty years ago have shrunk away and gone to other business litigation and other types of litigation because of the cost associated, at least with the kind of work I do in products liability.

I was a student of Mark Tushnet and subscribe to his political theory of constitutional law, which I think has led to some of the costs that have been increased over the years as I have watched the business roundtable and others; the Chamber of Commerce, pushing for certain positions and the challenges and litigation that have arisen in that context, which have added to the costs. Let me just take, for example, preemption. Preemption goes back years, but the idea that you do not have a common law claim, as in *Guyer*, taking away the claim that there should have been an airbag in the vehicle.

And that particular case, very limited to the facts supposedly at the time, but has led to what I call, "collateral litigation" in many cases, of raising the defensive preemption in the seat belt case and many other cases. That collateral litigation is adding cost. *Daubert* has become collateral litigation.[5] *Daubert*, was supposedly at the time, easing the rules of pride as I viewed it and many others, but instead became another motion to be made, another fight to be had, whether it's in federal or state court. You think it is bad in federal court.

I practice in Texas often, and they have *Robinson*.[6] We call *Robinson*, *Daubert* on steroids. So, restricting the testimony of experts; most of the experts are on the industry side, so we have to have academics and others who go through a long fight and many battles of *Daubert*. Rule 11 was, for a short time at least, problematic. I think that has eased up. But now it's two things: e-discovery and pleading standards. From the e-discovery standpoint, again, I looked at electronic discovery as something that would make it easier, cheaper, faster to get discovery. I mean, dealing with paper, finding files, and engineers and their file drawers, their notebooks for decades trying to find the information, or even the meeting minutes of committees.

Now, it is all electronic. Well, shouldn't you be able to just pop that up pretty quickly? I have been doing electronic discovery in some form for at least twenty years. I remember going to General Motors, and they had a

laptop, and I sat with the technician and we sketched out some searches that were contained on small databases. He pulled them out, handed me a disk, I made a format, and it worked. When they took their meeting minutes and put them in electronic format, they scan them. Actually, they did not even scan them. That technology did not exist—to scan. They sent them to the Philippines.

They had them retyped, put into databases, brought them back, and we would sit there with a technician for General Motors, and they would find key words and pull up documents and print them out. And we took care of it. And it did not seem all that costly. I think the real problems with e-discovery are not so much that we are asking for things nowadays. The fact is that the world has changed. The world has changed from paper to electronics, and with that, the volume of data and the linking of the data has gone up exponentially.

So what was a haystack before—a small haystack put in the room here and find a few needles by digging through it for hours or a couple of days—now is a mountain. It's a mountain of information. And trying to dig through there to find the few needles we need to prove our case has gotten expensive for the production side, has gotten expensive for the requesting side, who has to analyze this information and find it. I can just tell you, I am in the Toyota multi-district litigation right now.[7] And it is amazing the amount of data that we have to ask for, an amazing amount of data that we have to sort through to find things.

It kind of drives me crazy because my past life, I was a professional engineer. And I think I know what I need to find technically, and I am very reluctant to turn it over to paralegals or junior associates, to try to find things and link them together unless they have the technical background. So, I end up spending a lot of time myself going through information. And it has become a veritable mountain range of information.

Let me touch on pleading standards for a moment. I do not see the problem in trying to plead facts, at least, from a plaintiff's standpoint in many cases. Yes, the standard pleading form in the Federal Rules is: the defendant was driving a car, they acted negligently, they hit me and caused the injury. You need time to get in place, we can throw that in, too. We have a police report, we can attach that.

To show you what we have been doing now on our side: the master consolidated complaint for the economic loss cases for the Toyota multi-district litigation is 725 pages long. Just the PI wrongful death master complaint is forty-two pages long, and that does not count the exhibits that are going into it. We have sixteen exhibits for the PI side, many more for the economic law side. So, just think of the time of someone reading that to try to filter out whether there's enough there.

And you know what? They made their *Iqbal* motions. Even with that. So there is the collateral litigation. There is the expense, and not just the costs of experts and things, but the cost of the time on both sides. I mean,

every minute I spend on a case is detrimental, in the sense of, I get paid a percentage so I do not want to put in thousands of hours. Hundreds of hours are fine, and I would expect the other side puts in a similar number of hours in defending their case. But now the motion practice, whether it is a preemption motion, a *Daubert* motion, an e-discovery motion, a pleading standard, an *Iqbal* motion, those are the things that are, in my view, driving us crazy in litigation, at least on the plaintiff's side.

Where is the cheapest place, the easiest place, actually most fun place for me to try a case? Oregon State Court. And why? Because there's no expert disclosure there. It is trial by ambush. And it may be a small bar but I will tell you, I do not have to do the preparation. I do not have to have the experts write reports, which then get attacked, not only in deposition, but in subsequent *Daubert* motions, for example. So if I had my way, we would go back maybe fifty years or one hundred years. But maybe not so much.

JUDGE ROSENTHAL: Can I ask for a show of hands who wants to have trial by ambush come back? You got some support here.

DONALD H. SLAVIK: I would like that. I will mention right now, I think I disagree with Professor Redish's position about shifting some of these costs on discovery. I mean, at that point, I think we might as well nail the door to the courthouse closed because we spend enough on discovery as it is. If I have to pay whatever the defendant charged for producing the information, I would have even fewer plaintiffs. I mean, we have enough right now with things like caps on recovery. Let me give you a quick example. Defect in the motor vehicle: we have had many of these cases over the years where the seat backs are not strong enough. You get rear ended at a moderate speed, the driver seat collapses backwards into the child in the back seat, injuring or killing the child. If it kills the child, if there's a cap on recovery in that state and the wrongful death laws, such as in Wisconsin, you cannot do it. Just $350,000 or $500,000 is the total recovery. The cost of prosecuting the case is about $300,000. Throw in the risk of recovery and the attorney's fees; and I am not making a significant difference in my client's life, so why do it? Whereas another state, where there are not caps like that, maybe I can do it; California, Minnesota or some other states.

But those are some of the restrictions we already face in, I call it, the "tort deformed era." Throwing in the cost of discovery on that, if you throw another $100,000 into what the defendant would charge to search their databases and produce the documents, it is driving us out of the market, so to speak. I think very valid claims cannot be brought. We are not able to enforce the law out there on defective products sometimes because of this. So, I want to applaud the FJC and the Federal Rules Advisory Committee in seeking solutions to the roadblocks that are out there. I think it is a very difficult and problematic thing.

I think they have done a good job so far in getting good data as Emery has done and others, as to what are the real costs out there. They are not that bad. Granted, it sounds like $25,000 or $15,000 for a plaintiff is a barrier to individuals seeking justice. I am looking at multiple, hundreds of thousands of dollars per product liability case. That is up from maybe $100,000 ten years ago to $200,000 or $300,000 today. But it is not all because of the cost of living. So I would ask, what could we do? I know we cannot go back to trial by ambush. But I appreciate that the judges have the ability to manage cases, and I think case management is one of the best things that is out there.

Judges who are engaged in making sure that the parties have the opportunity to have their positions heard quickly. When I make a motion, I do not want to wait four months to get a hearing. Quickly. If I make a motion, and we have a hearing in ten days, that is what we need, the ability to run through that. And to accomplish that, I think the most important thing this Administration can do right now is get those 12% or 13% vacancies filled in the federal bench to start with. I wish that was done immediately.

JUDGE ROSENTHAL: Thank you. Although, it is interesting to denote as judges that one of the motivating factors that both Justice Souter and Justice Kennedy cited repeatedly in *Iqbal* is that they had no confidence in the ability of the district judge, the trial judge to keep discovery within proportional limits. Therefore, you had to tighten up on the pleading standards because it was no answer to say you can allow limited discovery in order to be sure that the claim is worth pursuing, and then if you are satisfied that it is, you can expand the discovery. Otherwise, you would get rid of the case at that point. The Justices both said courts have proven ineffective to do this.

So we should talk about whether that is a reasonable approach or a reasonable solution if that's going to, in fact, make a difference. I would like to ask Alex now to share with us his perspective, which is the opposite end of the V, and is really perfect to highlight some of these issues because Alex lives in the world that Emery described as that stripe with troublesome cases. His client is a really big data producer and is involved repeatedly in litigation, and he sees the bills.

ALEXANDER DIMITRIEF: Thanks, Judge. I had the pleasure at Duke of presenting a survey that had been conducted by the Lawyers for Civil Justice Reform Group through Henry and the Searle Civil Center. I am happy to report that I think my invitation to come back this morning means that I was successful in not trying to oversell those results; and I was careful not to. Not only because people like Emery were listening very closely to what I had to say, but also because I think it is important to understand that the data that we presented really did not mean more than it was an emphatic exercise in the art of the possible.

When you are talking about something like litigation expenses that are incurred by American corporations, that is an enormous topic and a very hard one to get a grasp on. But what we tried to do was try to get some data to substantiate these concerns about the cost and delay that Judge Rosenthal began this morning's session with. I think that the data we presented shows that there is an issue that has to be taken pretty seriously when you think about how the rules are working. Just a highlight, I am not going to torture you with all of the pages of data, but just some reference points. We got data from thirty-six out of the Fortune 200 companies. That data showed that the outside litigation expenses for those companies had increased from $66 million per year to $114 million per year from 2000 to 2008. That is 9% a year average cost for those companies.

The total for those thirty-six in 2008, was $4.1 billion. That is a huge number. Twenty-five percent of those costs, and a growing percentage every year, are associated with the production of electronically stored information and related discovery. The proportions of that discovery that actually find their way into court are a little bit distressing. Now again, I do not know how representative this is, but for the companies and the cases that we were able to get the data for, the data suggests that one out of one hundred pages of produced information actually was marked as an exhibit that made its way into court. Now, that is an incredibly small percentage that I think goes to some of these issues of relevance and proportionality.

The thirty-six respondents said there was one case of cost shifting, I think consistent with what Marty and Judge Rosenthal have been saying today about how cost shifting just does not happen all that often, despite its availability already in the rules for certain circumstances. And the subsequent work that we did, showed that depending on how you measure it, 16% to 18% of the profits earned by American corporations go to litigation expenses. Now, some people might say, and I understand the argument, that that's an appropriate level if you want the privilege of doing business in the United States. I am proud of our legal system, and I understand where those arguments come from.

But some people would say that that percentage is very high. Whatever you think about where that number ought to eventually land, I think the fact that it is up there at 16% to 18% means it needs to be a topic that's considered by the Rules Committee and addressed thoughtfully. Here is another area where we explored some differences and where I need to add my disclaimer, is the difference between costs in the United States and costs overseas.

This is where I say, not only do I give the standard disclaimer that what you are hearing from me this morning or my opinion is not necessarily that of General Electric, but that happens to be especially true in my case because my opinions are most emphatically not shared by my increasing number of foreign colleagues who are lawyers, who work in overseas jurisdictions where more and more of our business is taking place. Who most

emphatically disagree with me about the cost effectiveness of the American legal system. And when you look at the data we presented in May, it is pretty startling. For the thirty-six companies that were surveyed, depending on the year, we spent four to nine times as much in litigation expenses per U.S. revenue than we did for overseas litigation expenses versus overseas revenue.

Now, that is a pretty shocking number. And I think that Dan Troy, the Senior Vice President and General Counsel of GlaxoSmithKline, is more emphatic about this than I am. Dan spoke at the Federal Rules Conference, and he's the general counsel of an overseas-based corporation who says that the United States legal system is an emphatic deterrent to their doing business in the United States. I will tell you that when I wrestle with this issue, and more and more of our revenue, over 50% of our revenue came from outside of the United States over the past year, and that is a trend that's going to continue.

As I interact with foreign companies and colleagues who are based overseas, they opt out of our legal system. Companies refuse to subject themselves to American jurisdiction, and it is based on perception more than it is on fact. But I will say what I said to the judges at Duke, which is most foreign companies that I do business with think we are crazy. They just do not want to take any risk of being subjected to the types of horror stories they hear about. Now, that bothers me because I will be the first person to say that as an American who was raised in the American legal system, I think we have the best legal system in the world, and I stand by it.

I am proud of the fact that at General Electric, when our conduct is vindicated by an American court, I know that it has really been vindicated because we are held to high standards, and we are proud of being held to high standards. But we are increasingly going to be subjected to litmus tests by the rest of the world as the world becomes a smaller place. And I think we have to listen to what our colleagues from other countries are saying. What I think distresses me is when I hear that companies that are subjected to much less discovery in foreign jurisdictions, do not think that they necessarily get a fairer result than the United States.

That is something that I do not think we have studied yet. I think that's something that is a fascinating new wrinkle to all the issues that we are confronting. I do not pretend to have all the answers, but as an American who is proud of our legal system, I am concerned. I think that is something that we all really need to think about. So how do I respond and where do I land on some of these issues? I think that there are four main areas where we are encouraged that there is a robust discussion going on.

The first area, begins with pleading. Look, I agree, and any general counsel of a company that gets up here and tells a body like this that access to justice is not an important issue, is kidding herself or himself. Of course it is. It has to be. That is one of the things that makes our system so great. But I think that on balance, what we are seeing is that it has to be about

more than just simple access. It has to be about reasonable access with reasonable consequences to people who are on another side of the litigation. And in that respect, our view is that plausibility is a reasonable standard is the answer when Don says he is concerned about increased costs of litigation about bad pleadings and expensive practices that are brought into place. I go back to judicial management there.

There is not a judge here in the room that cannot recognize a bad faith or frivolous motion that's brought under *Iqbal* or *Twombly*. And there ought to be consequences to defense lawyers who bring bad faith motions. But in a lot of cases, that threshold test is an important test to make sure that the system is proceeding rationally and cost effectively, and we would urge that there not be a retreat. Maybe we do not get codified within the rules, but we should not retreat from, some of what we view as, positive developments toward rational access to the system.

Second, in terms of the scope of discovery, I think that the advent and explosion of electronically stored information really requires a thoughtful revisiting of that issue. I think that Don—I tried a case when I was a young kid against your firm, against the main partner, Bob Haybush; I lived to tell about it, and in fact, I would like to think that I am one of the few defense lawyers that emerged from that case with a pretty good friend after the case. And that is because I think that he and I had a pretty good shared view of what the haystack ought to look like. That very rarely happens, and I think that the issue here is, how do you get to the right haystack, because everybody is looking for the needle in the haystack. I was struck by the comments by the plaintiffs' bar at Duke about how they only want a small set of documents.

See, but the disconnect is, that they want you to produce the entire haystack and point you to the information, but they want the right to criticize you for not having produced the entire haystack. So how do you get the haystack to be a manageable size? I think that you could do that by a change to the rule that says that instead of a document or discoverable piece of information being irrelevant to a claim or defense, it ought to be something that a party in good faith uses to support a claim or defense. That small change could be a significant difference in terms of the size of the haystacks.

Then, I think, we need to go to some of the kinds of limits that everybody thought were going to ruin the deposition process, that I think now everybody on balance thinks would actually save lawyers from themselves. And so if we could go to some sort of limit on the number of custodians for whom electronically stored information is going to be produced—say five, six, seven per case, absent showing of a need for more and maybe limit the dates to maybe two years back, absent a showing for the dates to go back farther than that—I think a lot of the problems solve themselves. And again, we save parties from themselves.

A third issue related to scope is preservation, and our belief that standards are required, again, to save lawyers and parties from themselves in a lot of respects. We are not all fortunate enough to appear before Judge Shinland or Judge Grimm and judges who have immersed themselves in the latest nuances of electronically stored information. I think that the most distressing aspect to me is the cost that the judicial system incurs and hours that judges have to devote to issues that parties really ought to have sorted out for themselves.

If anything, I think that one of the biggest shortcomings of the system is that when a court is subjected to thousands of hours of work to sort out an electronically stored information issue, why do the sanctions get paid to the other side instead of the court? So, I really think that there's something to be done there because that would really send a signal to parties that they better take these issues seriously. But to get them to take these issues seriously and plausibly, let's make the scope of the obligations reasonable. We need clear rules, not something that depends on which court you are in, and not something that is so uncertain that everybody necessarily goes toward the most strict interpretation of the obligations, but clear rules about what your preservation obligations are and what the sanctions are going to be if you fail to uphold those preservation obligations.

There is a real cost here in terms of dollars from over-preservation. There is also a psychic cost. I think I probably get a bad name within General Electric and elsewhere because I am the guy who goes to all our senior executives and says, "When you're on a layover someplace in Asia, and you're so tired that you can't even see straight, and you're using your Blackberry to keep up with the rest of the world, don't you dare forget to keep that text message or keep that outgoing email message." The psychic cost of that kind of burden of our system that says that one lost message could subject you to sanctions, is something that we really need to address. Is that really the type of system that we want to have?

And the problem, again folks, is perception becomes reality. The consequences of a case like *Coleman v. Morgan Stanley*[8] in Florida, when you look at the case itself, you understand why the judge became as upset as Judge Moss did. But again, perception leads to behavior, leads to over-preservation, and leads to a skepticism about the system, that I believe is self destructive, and could be addressed thoughtfully through some rules.

Then the fourth issue is cost allocation, and I am not really popular with a lot of my brethren when I say this, but I think that that's an idea that is going to be tough to sell. I think that when you are a company like General Electric, it comes with ill grace to say that the cost of producing information to a plaintiff in a personal injury case is somehow burdensome on us. I do not think it serves anybody for us to maintain that kind of argument. But I do think that there is a place for it, when it comes outside of a set of core custodians, core documents that are relevant to a case. And we would love to see something in the rules that essentially said that, when you

get beyond a core set of custodians or a core set of subject matters of the sort, that I think would be a good limitation within the preservation guidelines. That is, if a plaintiff or a defendant wants discovery beyond an agreed to core set of information, perhaps that is when cost shifting ought to be implicated.

But I understand the concern that we do not want to increase the cost of access to the system, so again, I think there is a lot of room to address that thoughtfully. I do think that in looking at the rules, I hope that the committee will hear us when we say that perception really is 80% of reality when it comes to assessing the cost of defending a case, assessing the cost of doing business in the United States in an increasingly competitive international world, and that we really need to listen to each other and turn down the volume a little bit because it is not just the plaintiffs against the defendants in the United States anymore.

It's all of us on both sides of the V defending our system against increasing international scrutiny. I think we ought to come out ahead in that process. But to do that, we need to continue to address these issues thoughtfully.

JUDGE ROSENTHAL: That was very provocative, and let me just ask all the members of the panel one question. We have just heard a shopping list of suggestions that the Rules Committee should consider addressing, particularly what I will call, the gap between the statement in Rule 1 and the proportionality limit that has been part of the rules since 1983, some very clear, additional limits to be imposed via rule.

The Federal Rules of Civil Procedure and lots of the state rules have within them lots of tools that judges and lawyers and litigants can use. Rule 16 and the corollary, that is in almost every state rule, says to the court, "Hey, you can limit the number of depositions. You can limit the number of interrogatories. You can limit discovery. You can set a date. You can shape the pretrial work in a way that is reasonably tailored to the needs of a particular case." And if that was done with a kind of vigor and reliability, that would seem to address a lot of the concerns that we heard today, that there is over-production and that there is no adherence to what makes sense.

Why is it not working? If the rules already provide that ability, why isn't it working? And if it's not working, what is the promise of adding these additional rules, other than the rules that are so simple, as to have inherent arbitrariness, which is not necessarily bad. I mean, you could say presumptively that you get to get information from five custodians. There has to be a specific showing of good cause to get more. You could do that. Of course, I think I can do that now. Why is it not enough to have the tools available?

ALEXANDER DIMITRIEF: I think it is not working in all cases, and in enough cases, for the very reasons that make our system so great. And that is because there is a presumption that within the parameters that are established by the rules, we are trying to err in favor of allowing the process to promote a free flow of information, of not shutting down access, of not shutting down a party's right to discover information in the possession of the other side. It is a question of baselines. And I think there are many judges who, if it were up to her or him, would limit discovery but look at the rules, look at the presumptions, look at how our system is slanted in favor of more rather than less, and say you know what? I am not comfortable doing that.

And that is why I think that concrete limits, like the ones that were put into place on depositions, do the trick and empower judges who want to exercise aggressive management to actually constrain the scope of discovery. Create a new presumption. So, it is one thing for a judge to be confronted with an argument on behalf of a litigant like me, to come in and say, "I think that you need to come up with a limitation in this case based on the circumstances of this case." It is quite another for me to come in to say, "The Federal Rules codify an expectation of a lot of smart people who have looked at this, that in most cases, you do not need more than five custodians."

And there is not enough here to overcome that presumption. So, I think changing that baseline is the magic ingredient and why I think it would make such an enormous difference.

JUDGE ROSENTHAL: Anybody else on the panel want to weigh in?

JOHN VAIL: Do you want me to disagree with that?

JUDGE ROSENTHAL: Sure. I would not be surprised to hear you disagree with that.

JOHN VAIL: You know, what is funny about it, is that I am going to disagree on the very important point about presumptions, but not necessarily about the point about outcomes, because I think you are here at Mason at a Law and Economics Conference. I think one thing to start out with, and I am certain it will go to some things that Bruce says, and it goes to a couple of things that Professor Redish said: the civil justice system has a job in our society, and it is a political job in the big sense. The goal of the civil justice system is not to arrive at Pareto optimality. The civil justice system serves our body politic first and our economy second, only because a healthy economy is, indeed, a very important component of a healthy political system.

It is just as important to keep in mind the political goals of the system. Chief Justice Marshall said in *Marbury v. Madison*,[9] one of the first duties

of any government is to provide remedies for people when they are injured. And that's the key goal of our civil justice system. That is why presumptively, it needs to stay wide open. Now, this idea of rules and where rules should be. Let's come back to some of the things that Emery said and remember that the kinds of disputes in which this stuff is important are very limited. It is a small set of the case load, and it will be a small set of the case load in your courts.

So one of the questions is, do you make rules on the basis of 15% of the case load? Or do you make rules that deal mostly with the 85% of the case load, and then have some special things you do with that other 15%? I think the answer is the second one, and that is where these protocols become important. Now, I think too, this will go to something that Professor Redish talked about with—we should have a transparent debate about why we are subsidizing people who ask for information. In most of the disputes we are talking about here, these disputes tend to be disputes between corporations. Artificial beings that we already subsidize by limiting their liability, allowing them perpetual life, indeed, allowing them to exist at all.

There are many ways in which they are not wholly analogous to humans, and I think that can become important as we think about some of these discovery disputes. But let me just stick for now with this reality that these are big cases with big parties on each side. One of the points Alex raised about disputes. There has been over eight years they looked at for the Fortune 200. Now, let me give you some idea of the size of the Fortune 200 in the year 2000. The year those numbers started, the gross revenues of the Fortune 200 were about four and a half times the gross revenues of the People's Republic of China—the gross national income of China.

They were greater than the gross national incomes of all of South America. These are big entities, and they grew. Although, their costs grew about 9% a year, they grew at a clip of at least 5% a year during that time too. So, the raw numbers overstate the percentages of what they are talking about. But come back again. These big things, how do you control them? I think there has been a lot of talk about protocols within the federal courts, and I do take this as a judicial management issue. And I think largely out of a lot of vetting, a lot of thought from a lot of people that went into the Duke conference, I think that question was largely answered that this is best addressed by managerial issues, and not by general rulemaking.

Now, what should those protocols say? I think for you, Judge Grimm, who is a Magistrate Judge in Baltimore, and who has been mentioned here several times today: you can go to the website of his court, the Federal District Court in Baltimore, and download about a twenty page document that has a lot of protocols for dealing with complex disputes about electronically stored information. Alex has mentioned a presumption of five custodians. I think actually a lot of good plaintiffs' lawyers would agree with that as a starting point. And one of these very good plaintiffs' lawyers, a guy named Steve Susman from Texas, has put out a set of protocols.

These come from him. These are Susman protocols. And I think Alex alluded to the idea of a good relationship with Bob Haybush, a noted plaintiffs' lawyer from Milwaukee, and Susman, a noted plaintiffs' lawyer from Texas; when you get these good lawyers together to address these problems, the problems tend to recede as long as they have you available to resolve the disputes they do have. So, I think as Don Slavik said, your availability to resolve disputes, your requiring in cases of this kind, that the lawyers talk, that the lawyers' technicians talk to each other, and that you have quick ways to resolve the disputes, and that you have available to you the technical expertise that you need.

I think one thing that has been talked about a lot as a protocol in these cases is having the parties agree to fund a special master who is well versed in the technology. And I think if you have some of these big cases, and I will let Alex react to this, that some good lawyers will look at each other and say, "Yeah, that is actually a good idea. We will get things done faster and more cheaply." Those are a few basic reactions. I will have many more to many of the other things later.

JUDGE ROSENTHAL: Alex, do you want to react to that, and then I'll invite that from other members of the panel, as well?

ALEXANDER DIMITRIEF: Well, you know, there's that old saying that bad facts make bad law. And what I do not think is true is, I do not think you can say, good cases handled by lawyers who get along well ought to establish a baseline for the rules. I think that, unfortunately, the types of cases where parties intelligently and thoughtfully spare the judge the pain of those types of disputes, are few and far between. I think that's shame on the lawyers, by the way, but that is what the rules are for, is to make sure that people have an appropriate baseline to work from. So again, I am not advocating hard and fast rules. I am just saying let's change the presumptions. Let's move the needles.

Let's not assume that lawyers are going to behave like responsible adults and work these issues out necessarily in every case. Let's make it impossible for them not to. Let's put those new prudent baselines into place and allow variation when a party can make a case that there needs to be an expansion beyond that certain number. But again, I do not think you can presume that every case is going to proceed with parties being able to agree that the Susman rules are the way to go. It is too bad. I was going to propose the Susman rules as the new Federal Rules of Civil Procedure, but I do not really think there are grounds for that yet.

JUDGE ROSENTHAL: Anybody else want to weigh in?

DONALD H. SLAVIK: With regard to specific limits, for example, and custodians and things, I think that is fine as long as what becomes, maybe a

presumption, does not become a ceiling in some cases. Again, the Toyota litigation, we agreed upon twenty-four subjects for preliminary depositions just to find out who knows what. Toyota agreed to produce fifteen witnesses, which we took fifteen depositions. The problem was that I think seven or eight of them were in Japanese, and I would rather have a root canal without Novocain, than do some of those depositions because of the painfulness of trying to ask a question, and waiting for a response for a long time, and the dancing that goes on.

My next motion to the court will be instead of having eleven hours for a Japanese language deposition, it should be thirty-three hours. But again, take for example, the limitation of twenty-five interrogatories. To me, it's come to such a point that I do not ask for interrogatories anymore because the limitation is now even to the ability to actually use them effectively. I would rather just do some depositions. Again, depositions do cost us as plaintiffs. Yes, it costs you to produce a witness, but you have to pay the court reporter, we typically have to travel some place. I want to pick out just a few depositions and get key depositions. I would rather call defense counsel and say, "Let's sit down over a cup of coffee on a video conference and figure out what we need to do to make this go as fast as possible."

But rule changes always alarm me, and when they start putting numbers just because what was a floor becomes a ceiling, presumption becomes another motion to make, another fight to have over whether we should do it right, or how to do it right. So I would take that. I would say that the special master route does work very well. I have done it in state court.

We are doing it in federal court now. Special masters—a good special master is worth their weight in gold; and it's worth both parties paying that hourly fee, splitting it to have a special master address this, and I wish courts would take greater intervention in appointing special masters that are agreeable with the parties to handle these discovery issues early on from the get-go.

In a recent state trial court case, the first thing the judge did was appoint a special master and relieved the court of having to deal with the issues, and that special master was available within a day or two anytime we had a dispute, or less. We took care of all those discovery disputes early on. So, I would strongly encourage that aspect of it. Put that in the rules, that special masters would be appointed upon agreement of the parties or upon the court's order.

ALEXANDER DIMITRIEF: Just one quick comment, Don, and let me just speak up on behalf of the poor Japanese witnesses who are being subjected to thirty-three hours of deposition. I do not think they probably enjoyed it very much either. And having represented a couple, I do know that from first had experience. I think a new issue for us in today's world is gauging the reactions of overseas participants in our economic system, to our system. So when a Japanese witness, who was raised in a different legal sys-

tem and has a different set of expectations is told, that for the privilege of doing business in the United States, you have to be subjected to ten, fifteen, or twenty hours of examination, they ask themselves, "Boy, does that sound right?"

I am not saying that their answer is necessarily the right one. I will be the first one to say that for the privilege of doing business in the United States, there are costs that come, and obligations that come with that. So, I am not saying that depositions should not be part of that. What I am making is a more subtle point, I hope, which is those types of reactions to our system are something that we increasingly need to take into account because, again, it is not just plaintiffs and defendants, it's how the rest of the world is interacting with the United States as well and what they think about our system.

I think that is a new lens that we are being scrutinized through now, that was not necessarily present the last few times the rules have been addressed in such a wholesale manner. And I think it is a new issue that will be fascinating to see how it works out over the next ten years.

JUDGE ROSENTHAL: Marty, did you want to weigh in on any of those points, and Bruce?

BRUCE H. KOBAYASHI: It is interesting that Donald mentioned depositions because we have Marty's alternative cost allocation rule for depositions. And he said, "When I do them, I simply do not over-depose, because I have to take into account my costs now." And that is simply Marty's rule. I teach a class on the economics of litigation, and teaching discovery is easy when you are an economist. I tell the students that the problem here, as Marty said, is that I get to externalize lots of the costs onto my adversary. I hate him too; but even if I do not hate him, I am just going to ask for information until the marginal value goes to basically close to zero.

And all that economics is telling you, is that we ought to think about giving people the right incentives. You go to my house, I have two teenagers, and there is a budget for the amount of disputes I can manage between the two teenagers. One common dispute is who gets the bigger slice of the last piece of cake. And my poor kids are the kids of two economists, and so we have incentive devices to deal with the problem, like "I cut you choose." They take really good care in splitting that cake. There are rulers involved sometimes. But the whole notion is, I do not have to deal with the disputes.

And really, what Marty's proposal is, or the way I take it—economists Cooter and Rubinfeld have talked about this over and over again. This cost allocation rule is to get people to internalize the cost of their decisions. It is not really just a way to deter more lawsuits. And we can talk about limits. As Don suggested, we are always facing caps. Well, caps are not an economist's solution to the problem, so maybe we ought to think about what the right solutions are, and get rid of caps, and put in the right solutions, which

might be incentives. When I talk about economics, it really is thinking about marginal incentives.

MARTIN H. REDISH: I certainly do not think we should close our eyes to legal costs. In fact, I told the dean I cannot write anymore scholarships, I can afford my hourly rate. But I think we need to recognize a phenomenon that has developed. I made brief reference to this before, and it's not necessarily a bad phenomenon—do not misunderstand me—but it is one whose implications I think we have to take into account, and that is the plaintiffs' lawyer as a real party in interest. When we talk about putting the heavy costs of discovery on the poor individual plaintiff, at least in any kind of multi-party litigation, it is not likely to be borne by that poor individual plaintiff.

I think it is appropriately seen as a cost of doing business of large plaintiffs' firms. If we do want to subsidize discovery, and we may just as well in certain areas, we passed the Civil Rights Attorney's Fees Awards Act.[10] There are certain areas we believe we want to subsidize. One, I think it should be subject to transparent democratic debate. But two, why would you want the subsidy to come from a defendant who has just had no adjudication against them? There has been a unilateral complaint filed against them, and all of a sudden, there are enormous economic consequences.

Now it is true, there are going to be economic consequences just to defend oneself, but that's our system. This is qualitatively different. This is giving a benefit to the other person when there's been no due process adjudication that they were responsible or liable for anything. If there is to be a subsidy, I do not see why it is not a nationwide subsidy. Or at the very least, if it is going to come from a defendant, against whom nothing has been established legally, we should have it come legislatively after free and open debate; something that has never happened.

JUDGE ROSENTHAL: John, did you want to weigh in?

JOHN VAIL: This idea of, what you subsidize and how. Again, I come back to the idea of, you have reciprocal duties. Plaintiffs have duties in discovery. Defendants have duties in discovery. The duty burden is equal. In fact, the burden often becomes different because of information asymmetry. The plaintiff does not have access to information that the defendant does have access to that's necessary to prove a case. Marty alludes to having a free and open debate: we have a free and open debate about this. We have an interstitial common law system, and we have a rulemaking process, which is one of the most open and transparent systems that I know in the federal government. Yeah, I am sucking up.

JUDGE ROSENTHAL: It's working.

JOHN VAIL: And again, when you hear the word defendant here and you hear about these enormous costs, in your mind, do any of you picture a human defendant, or do you picture a corporate defendant?

JUDGE ROSENTHAL: I would point out to you though, John, that it is a standard part of my jury instructions when I have a corporate party, and I suspect it is in many, many courts because mine is a pattern jury instruction—I did not make this up—that a corporation and an individual are equals in a court of justice. That is part of the jury instruction.

JOHN VAIL: I agree. But Marty raised the issue of would we subsidize, and I say that is a hard question when you deal with a corporation because you create its existence to accomplish certain purposes.

MARTIN H. REDISH: Can I just say, there's no Federal Rule of Civil Procedure, nor has there ever been since 1938, that is explicitly determined that the cost of discovery are to be borne by the responding party. So I agree about the rules process. I mean, I would love to suck up, too. But there has never been such a rule. It is just established practice. We have never had this debate at any level.

JUDGE ROSENTHAL: No. We kind of tip toe around it, and it is very useful to have it brought to the forefront. But Bruce has spent much of his professional life studying how incentives play into what lawyers do, what litigants do, and what judges do. His most recent focus has been on something that Alex touched on, and that we have all been talking about, that one of the recent trends we have seen in litigation is the increase, at least perceived increase, in spoliation accusations and sanctions motions and the fear, that the fear of sanctions will in turn lead large data producers to preserve too much, which will in turn lead us all to have to conduct discovery on even more electronically stored and other information.

Bruce has actually studied this instead of simply exchanging anecdotes about it, and I would like to invite him to share the results of that scholarship.

BRUCE H. KOBAYASHI: Thanks, Judge. I do want to say one more thing about the cost allocation rule. The nice thing about going last, as my kids find out in "I cut, you choose," is that there is a last mover advantage. So most of this stuff I planned to talk about has already been talked about. But one way to deal with discovery limits, and this is really from Cooter and Rubinfeld's in their Journal of Legal Studies article,[11] is to have limits be part of the trigger at which you change the default cost allocation rule. And so you have something like ordinary and extraordinary discovery. It may not be practical or palatable to the people who are thinking about rules

amendments, but that is one way in which you can try and get some type of incentives in the system.

Don mentioned *Daubert*. I think the greatest description of the problem that we are facing here with respect to judges overseeing all this, is Judge Kozinski's order on remand in *Daubert*. He said, "I am supposed to sit in judgment of expert's science? What kind of backward world is this?" And then he basically imposed the same decision that the court reached earlier under the *Frye* standard.[12]

So one of the things that I think economics are really trying to achieve is directing the parties to have the incentives to actually figure out how to get to the right haystack, or to look at a more focused set of things. We are not trying to stop people from filing claims or tilt the playing field one way or the other. We are just trying to get the process to be a lot more rational, and to think about incentives of the parties, and not foist this problem on judges who may not be prepared to deal with this problem. I mean, it's not because they are not smart. I have to suck up a little bit. But they just do not have the information to actually manage all of this. And I think that is the basic problem here.

As far as preservation duties: I look at preservation duties and the related issue of spoliation sanctions as a system of ex post consequences designed to regulate ex ante behavior. And the only unique thing here is that this issue involves behavior that occurs prior to litigation in many cases. There is a lot of controversy over the courts' use of its inherent power and whether you can bring these things into the rules. But the perception is that the problem results from use of the common law that results in variation. People are worried about what standard should apply, when sanctions should be imposed, when are these duties triggered, and what are the scope of these duties.

So, the major problem that seems to be facing litigants is all this uncertainty related to the common law rules applied under the courts' inherent power. The solution often proposed is that we bring this into the rules, and we come up with a uniform rule. The problem is that there is lots of disagreement about what that uniform rule would be.

And so there are several lessons that economics can give you. One that I'm reminded of comes from my experience at the Federal Sentencing Commission. To talk about the Sentencing Commission and about an incredible bunch of judges is a risky proposition. But in some sense all the economists there really thought that we should have had *Booker*[13] back in the 1980s. It should have just been advisory guidelines, and it goes a lot to what Emery is doing. I think a lot of the problems of federal rulemaking are that we are trying to impose uniform solutions to a wide variety of problems that defy use of a uniform approach. A lot of the problems will have solutions that should be based on facts in the case. It is sort of similar to criminal sentencing: ten to life. And where does this judge sentence this bank robber within that broad range of ten to life?

The answer that the Sentencing Commission came up with was well, we are going to look at what judges did as a whole and then figure out through a regression analysis—I won't mention standard errors—what judges did as a whole. And it turns out, what judges did was really pretty sensible. You look at bank robbery, and there is the base offense level. And then if the guy had a gun, or he used a gun, or injured somebody or he took more money, all these things resulted in longer sentences and more time served. So what we did was just an empirical approach, because if you try to do this from scratch or just arguing through theory, it was just going to be a mess.

Instead of talking about the various reasons why we have punishment, e.g. justice, retribution, deterrence, and all that was sort of set aside in the individual guideline in favor of just figuring out empirically what the judges did in practice. And then we found out what judges did was rather sensible. The corporate guidelines were a different story because we had no past practice, and that deteriorated into arguments over theory, and that's when all the economists ended up on the street.

Adapting this to the issue of spoliation sanctions, it seems we get a similar result. If you really look at what is going on—I mean, the thing is you make a small mistake, are negligent or even grossly negligent, it is not common that a terminating sanction is imposed. That is what the case law is saying. It really has to be that there is some kind of bad faith for terminating sanctions to be imposed. And so the law on spoliation sanctions seems rather sensible. There are these really high sanctions available, but they are very rarely used. And the law guards against over-deterrence resulting from the fear of having your case dismissed, or having some kind of default judgment because of a spoliation issue because there has to be a finding of bad faith for this to happen. It is sort of like a *mens rea* requirement that prevents you from having to, out of fear, over-preserve.

So that might be certainly one thing that we could do, either through common law, or if you want to put it in the rules, to cement in this intent requirement to separate out those cases of accidental or even negligent spoliation from those which are based on bad faith. A similar issue arises in *Pension Committee*[14] and in *Rimkus*,[15] regarding whether you make the victim of the spoliation prove that there was prejudice. In the cases where there is bad faith, my approach would be—and once again I am not a lawyer, I'm an economist—you probably do not have to worry about over-deterrence from the punitive nature of the terminating sanction. You probably do not have to worry about whether or not there's a showing of harm. You can treat them as cases where we also want to punish attempts because these are intentional harms. When you get back to negligence, you probably want to scale back. So you think about *Rimkus*—I probably would have thrown the book at these guys. I would have had no problem applying the result in *Pension Committee* to this case. I have bigger problems with the *Pension Committee* approach when one is applying the sanction when there

is not bad faith, but some form of negligence. The issue of negligence gets back to what is, and when does, the duty to preserve apply?

The issue of the trigger: I think everybody thinks that there should be some kind of notice. And there's just lots of disagreement about exactly when a party has that notice. So once again, it's hard to engage in rulemaking, because there is just not a lot of evidence about what the relative costs and benefits are.

The one thing I have to say is that what the rules clearly understand is that there is nothing wrong with destroying lots and lots of evidence. And so a lot of people said this is terrible. The plaintiff could have made his case, but these emails are no longer around. Well, I mean, anybody who has a computer has Microsoft Outlook and it always asks, "Would you like to auto archive these now?" And I always click, "Yes." The most liberating recent occurrence with computers and me was when I was on a plane to a conference at USC in Los Angeles. In the middle of the plane ride, my laptop, which I used for everything, including to archive my emails, had a massive hard disk error. As a result, I switched to a Mac, which is a very liberating thing in itself, but I also lost all of this archived email that I was thinking, "Oh my gosh. What am I going to do?" And then a sense of relief came up because I was liberated from having access to all of my old emails.

But the whole notion is that there's sort of this business judgment rule with respect to ex ante management. And you have to have that because you really do not want firms managing data on the basis of the fear, it might be someday relevant to some litigation that eventually arises because that really would be inefficient. So we have a de facto business judgment rule, and as long as you have something in place that looks reasonable in order to conduct your business and manage data, you can destroy lots of data that may be relevant in some future litigation. What is not allowed is for you to deviate from that basic program under the business judgment rule.

So in *Rimkus*, you cannot ex post facto come up with a document destruction policy, or I guess they call it document retention policy. So, deviations from the business judgment rule are punished. For intentional deviations, and at some point, when litigation becomes probable, it is probably a good idea to heighten the standard for preserving data. If you look at going back to the Sentencing Commission analogy, that's really what we have. So the system, in general, seems to be fairly rational. The real issue, and I guess what everybody wants, is clarity on the margin. The problem with the centralized rulemaking process is that it often proceeds without actually much empirical data.

The Federal Judicial Center really does a lot of empirical work, but often times, it's not going to be able to answer the question of what's going to happen when we prospectively change the rules. And in that sense, the bottom line in rulemaking circles is that variation is often thought of as the enemy. On the Sentencing Commission: we wanted to reduce unwarranted

disparity. Now, why you would want to do that in a criminal law system is a good question, but in fact, there was a lot of variation, which remained after the guidelines, and it was warranted. We wanted proportionality, but you wanted like cases treated alike.

I think that is really the goal here, and the correct approach. I think we ought to sort of trust the collective decisions of the federal district courts, and rulemaking really ought to proceed on an informed basis. And way too often, for example in the Rule 26 amendments or the Rule 11 amendments in '83 and '93, there's just no actual knowledge of whether there is a problem to be solved, or whether the solution that is proposed is actually going to address the problem or make it worse. I think, what we ought to do before we go and start tinkering with the federal rules, is figure out what past practice is, and then embrace variation as a way to figure out how to proceed. Because from an empirical economists view, variation is your friend, it is not your enemy.

Without variation, there is no way to figure out whether or not a change in the cost allocation rule is going to be a good thing or a bad thing. So I think my ninety second take away is that we ought to slow down, and we ought to try and figure out; I don't know whether it's pilot programs or doing something like the Civil Justice Reform Act in 1990. Or just look at state and federal differences. But we have to find some way to increase our knowledge. For all of the craziness that surrounds the U.S. Sentencing Commission was, the one thing I think that everybody agrees is valuable, was that they actually increase knowledge; I think with *Booker*, they increase knowledge in a way that you do not actually have to pay attention to. But a lot of people still do. And that is, I think, what we have to work into the civil rules rulemaking structure.

JUDGE ROSENTHAL: Each of the panelists has given us a little bit of a wish list. I told you when we started that we would give you a mix of information about problems. I think we did that. We gave you some ideas for long-range approaches to some of those problems. You have heard some suggestions, and the good news is that we are, in fact, doing within the rules process, much of what has been described. Professor Kobayashi, we have heard you. We are committed to getting more empirical information. Emery's work has been enormously helpful. Alex's work has been enormously helpful, and we know we have only started.

I thought we would, give you some ideas for immediate ways to improve. Go to the Duke website, to the Federal Judicial Center website. You will see some of these protocols, form orders, and form agreements, that were discussed. There are forms that I use, that I have used since the conference, that I encouraged the lawyers to talk about and consider as agreements between themselves, or as orders that I enter in cases to try to manage discovery. They are enormously helpful. The Seventh Circuit has a pilot program that they are engaged in right now on better management of

electronic discovery. Their work is on their website, and it is enormously helpful.

So you can, as a take away for yourselves, take advantage immediately of some of these very useful tools that have certainly made my case management better. Maybe not as good as the Supreme Court wants me to be, but they think I can't do it anyway. I think we can all prove them significantly wrong.

AUDIENCE MEMBER: Let me start with a comment about the difference between the U.S. system and the rest of the world, and what we see as a real competitive problem. We had a speaker here last week for the American College of Business Court Judge, and he pointed out two things. The rest of the world is much more focused on regulation, which is a perspective matter. We use the common law, which is much more retrospect. And I agree with Alex that that's the best system. But our judicial systems are also more focused on conflict resolution as what their duties are. Whereas our system, to our credit, is focused on finding out what the truth is.

If that is your focus, it costs a lot more to do that. Maybe what we need is some cross pollination where we figure out what the rest of the world is doing to get conflict resolution done on a more cost effective basis. But I do not think we want to change our system that we're focusing on getting at the truth. The second point is to express a little bit of my frustration at the panel discussion this morning. I'm a state business court judge, so I have a highly specialized court. We have—and Paul Grimm has proved it—we have all of the tools that we need. If you want to know how to make it work, Paul just told the party you can pay $350,000 for discovery abuses, or you go to jail for three years.

It was a very effective rule. We have the tools to do what we need to do. What we do not have, and what the panel did not talk a lot about, is we do not have the capacity, particularly on the state level, to solve those problems. And as far as I can tell, there has been absolutely no effort in this country and nobody promoting the effort to increase the capacity of the judiciary. Until we do that, yes, the answer is judicial management. That is clearly the answer. But if you do not have the capacity, if the judges do not have the time to engage in judicial management, you can have all the rules in the world, and it won't do you any good.

We have to find ways to change the structure. And I would be interested if any of the panelists have some suggestions on how we can change the structure to create more capacity. I heard the CEO of DuPont several weeks ago say the greatest key to risk management was having the capacity to handle the unknown. We do not have the capacity in the judicial system to handle those 10% to 15% of the cases that are the real problem. Thank you.

JUDGE ROSENTHAL: Anybody want to weigh in?

JOHN VAIL: I will say a couple of things because I actually had that on my list to say. That one of the things we need more than anything else is more judges. That is not going to happen on a federal level soon. Another is that Mitch McConnell needs to give up his aspiration to be Pope, because I say that in 2,000 years, the Catholic Church has canonized approximately 10,000 saints—that's about five per year. Senator McConnell seems to think that that's a good rate for the Senate to emulate on the approval of federal judgeships, so he needs to trend away from that. And I am running for Pope anyway, so I do not want the competition.

Another thing that was on my list, I do not know how people will react, but we need to rationalize our drug laws because we are killing ourselves in our courts with what we are doing now. It takes a huge capacity in our courts, and I think a growing consensus shows that we are not getting the benefit from it for the effort that we put into it.

MARTIN H. REDISH: Okay. Can I make one comment?

JUDGE ROSENTHAL: Sure.

MARTIN H. REDISH: I thought the judge's comments were excellent. However, it comes down to this: you get what you pay for, and the state is just not taking in enough money, so it is not going to be able to allocate it. People do not want tax increases. That's fine, but if you do not raise your taxes, you are not going to get better services. And it's really just as simple as that I'm afraid.

ALEXANDER DIMITRIEF: And Judge, I'll just say, I was trying to allude to that issue when I mentioned that I think a major failing in the system right now is that people like Judge Grimm are available for free. I mean, is it really our priority that we want a talented judge like that spending as much time as he had to? I was struck in the opinion when I read about the thousands of hours that his clerks and he devoted to that dispute. So, what was produced from that was a decision that the first section or the second section with the legal analysis is a great roadmap for any practitioner. But I am not so sure that somebody should not have to pay the system for refereeing that kind of dispute.

I come to you as the legal litigation lawyer for large corporations saying, I think that part of what the system could do is when a party mucks around and causes that kind of problem, and they ought to be sanctioned for it, sanction them for it. Put in some deterrents because I do not think that Judge Grimm should be providing services like that for free.

JUDGE ROSENTHAL: When we started, I thought I said that I wanted to focus on possible solutions that were achievable. And you may have ex-

ceeded my pay grade, at least, in terms of the level of influence that we have. But you will be happy to know that Judge Grimm is a member of the Civil Rules Committee, and is helping us navigate these issues from the rules perspective. Having said that, I do not disagree with your comments.

AUDIENCE MEMBER: Sort of a different perspective than I have heard, and I want to start my question with an observation. I have probably been on three or four discovery panels, including one with Judge Rosenthal. Yet, since the Federal Rules came in, I have probably had fewer, what I consider, real e-discovery disputes than I've been on panels. So I ask myself, why is that? Is it because of the rules and how good the rules are? Or maybe—and I would pose this—is it because litigation is really a market based system? In other words, if corporate plaintiff A asks corporate defendant B for $10 million worth of e-discovery, then corporate defendant B is going to ask corporate plaintiff A for the same.

On the other hand, if small plaintiff A asks corporate defendant B for $10 million worth of discovery, then corporate defendant B is going to ask small plaintiff A for $500,000 worth, and nobody wants to get into that. Nobody wants a judge to really get involved because really, if you are in the market, if you are litigators, you do not want a market regulator. And that's what we are. Many lawyers have told me at these kind of seminars, "You judges make orders, but you just do not get the fallout, the economic and other costs of when you say okay, do A, B, C, D and you do that, and you supply that e-discovery, and it becomes unwieldy."

So is it a market system? Is that what's really making it work? Is that why I am not seeing so many e-discovery cases in a pretty sophisticated market in Los Angeles or something else?

JUDGE ROSENTHAL: Sounds like we need some more of that empirical research to answer that question.

AUDIENCE MEMBER: What only John has mentioned is the fact that all of this discovery that you are talking about is maybe 5% or 10% of what we deal with in the state court level because the kind of cases that we deal with, are cases that are real small dollar; your soft tissue car wreck case with $197 worth of body damage and $4,000 worth of chiropractic care. What no study, that I am aware of, has ever measured is how many lawsuits are not seeing the courthouse because no plaintiffs' lawyer will take the case involving $20,000 worth of medical expenses because your firm cannot afford to seek compensation.

Your company cannot afford to defend one, and if they can find any lawyer that will take that kind of a case, your company will settle it on the cheap. Our system of justice, because of the discovery rules that are applicable to all of us, has institutionalized a system where you can cheat, defraud, or injure a person, and as long as you do not injure them for $20,000

or more, no good lawyer will take the case; that is what no economics course I am familiar with, has yet studied.

How many lawsuits are no longer making it to the courthouse because lawyers' compensation has gone up, adjusted for inflation over the years, and is the contingent fee system responsible for people that are clearly injured because of clear liability, not being able to seek access to the courts anymore?

DONALD H. SLAVIK: Like I said with the example of the infant killed, clearly, and I can tell you there was a defect in the product, but we could not afford to do it, I would say that I would take—I would used to say 10%, but I think it's less than 5% on the cases I investigate with some merit that I actually end up prosecuting at some point. You make a good point.

EMERY LEE: I would love to do that. If the committee would ask me, I would love to do that. I am not sure how I would do it, but I would love to do that.

BRUCE H. KOBAYASHI: Gillian Hadfield at USC has made the more general point that in this country, legal advice is really the purview of not even the middle class. We have lots of people who are forced to deal with complex regulations like tax law or other regulatory law, and they do it basically without any legal advice. And we may want to sort of think about reforming rules against unauthorized practice or other things, which from an antitrust view are really restrictions on the supply of lawyers that make legal advice unnecessarily expensive.

I think that is part of the issue. It is not just a problem limited to plaintiffs who are injured for low amounts. We do have insurance, and there are those sorts of issues. But I think economists have thought about in fairly sophisticated and thoughtful ways, whether or not we ought to go to a different model of providing legal advice. It's not just the legal system and the rules, but in fact how our lawyer services and legal services are delivered in this country.

JUDGE ROSENTHAL: So we end where we began with Rule 1, and wondering if we really do have a system that works well to achieve it. I want to ask you to help me thank this panel, which has just been wonderful.

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1 *See* Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2007).

2 *See* Ashcroft v. Iqbal, 129 S. Ct. 1937 (2009).

3 *See* Conley v. Gibson, 355 U.S. 41 (1957).

4 Private Securities Litigation Reform Act of 1995, Pub. L. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

5 *See* Daubert v. Merrell Dow Pharm., 509 U.S. 579 (1993).

6 *See* E.I. du Pont de Nemours & Co. v. Robinson, 923 S.W.2d 549 (Tex. 1995).

[7] *See In re* Toyota Motor Corp. Unintended Acceleration Mktg. Sales Practices & Prod. Liab. Litig., No: 8:10ML02151 JVS (FMOx) (C.D. Cal. filed Apr. 9, 2010).

[8] *See* Coleman (Parent) Holdings v. Morgan Stanley & Co., 20 So. 3d 952 (Fla. Dist. Ct. App. 2009).

[9] *See* Marbury v. Madison, 5 U.S. (1 Cranch) 137 (1803).

[10] Civil Rights Attorney's Fee Awards Act of 1976, 42 U.S.C. § 1988 (2000).

[11] *See* Robert Cooter & Daniel Rubinfeld, *An Economic Model of Legal Discovery*, 21 J. LEG. STUD. 435 (1994).

[12] *See* Frye v. United States, 293 F. 1013 (D.C. Cir. 1923).

[13] *See* United States v. Booker, 543 U.S. 220 (2005).

[14] *See* Pension Comm. of Univ. of Montreal v. Banc of Am. Sec., LLC, 716 F. Supp. 2d 236 (S.D.N.Y. 2010).

[15] *See* Rimkus Consulting Grp. v. Cammarata, No. H-07-0405, 2010 WL 645253 (S.D. Tex. Feb. 19, 2010).

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EDITED TRANSCRIPTS

OBESITY LITIGATION

John F. Banzhaf III

LINDA KELLY: I want to introduce the topic of our next two sessions, and clearly someone has a good sense of humor to introduce a discussion of obesity litigation while you're eating your dessert. And that's true. We do have a sense of humor at the LEC. The growing obesity rate in America is a public health concern and statistics from the Centers for Disease Control indicate that a substantial majority of adults in the country are either obese or overweight. And it's a growing issue among children as well.

There has been a range of responses proposed to this issue from a more laissez-faire approach, to a personal responsibility approach, to education efforts such as First Lady Michelle Obama's "Let's Move Initiative." The imposition of "sin taxes" has been proposed in a number of jurisdictions. Zoning regulations have been proposed and there has also been discussion of using the litigation process to address this problem. And one of the pioneers of this approach to addressing the problem is with us here today. Professor John Banzhaf is a Professor of Public Interest Law, and the Dr. William Cahan Distinguished Professor of Law at George Washington University.

He is a well known legal activist. He teaches torts and administrative law at GW, but I think perhaps his most famous course is a course in legal activism, which I believe is a clinical course where the students actually get involved in launching public interest litigation. And he has been involved in a number of very high profile issues. He is known variously among his proponents and opponents as the Ralph Nader of the tobacco industry; one of the 100 most powerful people in Washington and my favorite—and the only reason that I would say this is because he is proud enough of it to put it on his bio—the Osama bin Laden of torts. I thought that was interesting.

So without further ado, please join me in welcoming Professor John Banzhaf.

JOHN F. BANZHAF: Thank you. May it please the court? Alright, well, in any case, please continue enjoying your lunch before I sue the Law and Economic Center for failing to disclose the calorie content of this meal. Yes, as Linda said, I've been called a legal terrorist, the Osama bin Laden of torts, a legal bomb thrower and a legal flame thrower, and not just by our host Professor Henry Butler. That's a joke. Actually, I'm honored to be here to be invited by Professor Butler to address you since his views and mine often don't coincide, as you might guess.

But I have, in fact, been called all of those names and many more, some of which we can't repeat in polite company or here, and I've also

been accused of being both a billionaire and one of the 100 most powerful people in Washington, both of which are not true. At a congressional hearing on the infamous cheeseburger bill, which was designed to stop this obesity litigation, I was accused of subverting the democratic process, trying to take away consumer freedom and fostering regulation through litigation.[1] The bill's author, former congressman Rick Heller, whose Orlando District is a fast food haven that maxed out on PAC contributions from various fast food companies like McDonald's, Wendy's and KFC, opined that I was undermining the principles of freedom of choice, common sense and personal responsibility.

Many at the congressional hearings on this bill, which fortunately died a well-deserved death, reportedly called the "fat litigation," which I helped to inspire, frivolous. Even though ten out of ten of those legal actions have already been successful, there's an eleventh one which just came down which I'll tell you about in a few minutes. In any case, the interesting thing is that they argued that big companies needed protection from frivolous lawsuits filed by law professors. I don't know.

Well, there's a brief introduction. What I would like to do now before I address you again this afternoon at the afternoon panel is to explain why public interest litigation aimed at America's obesity epidemic is not only consistent with both fundamental, economic and democratic principles, but actually a necessary component if we want the invisible hand of Adam Smith in our checks and balances form of government to deal with public health problems like obesity.

And actually, I'm going to begin by putting the issue in context alongside the public interest legal actions aimed at another big public health problem, which is smoking. Because it's my lifelong involvement with anti-smoking legal actions which led directly to this new fat litigation movement, and they have so much in common that not too long ago, Fortune Magazine in a cover story asked "Is Fat the Next Tobacco?"

Well, by way of background, when I was twenty-six years old, fresh out of Columbia Law School, and ironically while working as a gigolo on a cruise ship—that's using the word in the original sense—I brought a legal action which required TV and radio stations to make hundreds of millions of dollars worth of broadcast time available completely free for anti-smoking messages.[2] As a result, cigarette consumption fell for the first time. Something even the Surgeon General's report several years earlier wasn't able to accomplish. As a result, millions of people quit smoking, and cigarette commercials were eventually driven off the air. And all this would have been virtually impossible, probably even unconstitutional, if I had attempted to do it through legislation.

This convinced me that legal action could be a powerful and important tool against major social problems, which was a very novel idea at the time. And I went on to use legal action to start the nonsmokers rights movement by helping to get smoking initially restricted and then banned on airplanes

and in many public places, to get higher health insurance rates for smokers, to encourage the torts litigation against the tobacco companies which led, in addition to the many individual victories, to a almost quarter of a trillion dollar multi-state settlement, as well as the death of Joe Campbell and cigarette billboards. Again, things I couldn't possibly have accomplished through legislation.

Then, suddenly out of the blue, in 2002 a reporter asked me, "In view of the amazing successes which people have had using legal action as a weapon against smoking, would legal action—could legal action be effective against the newly emerging concerns of obesity?" And I said, "Yes," and that started the modern fat litigation movement with an avalanche of publicity conferences and additional legal actions, some of which you will hear about on the panel this afternoon. In making that pronouncement, or prediction, which kicked it all off, I was mindful of the role that litigation has often played in social change, both in starting entirely new movements as well as in helping to make other movements far more effective.

I think in a very real way, *Brown v. Board of Education*[3] kicked off the modern civil rights movement at a time when there wasn't sufficient public or legislative support to attack separate but equal segregation. Indeed, in a pattern, which would soon become familiar, *Brown* generated the publicity. The publicity led in turn to public support, and that in turn led to public pressure, which eventually led to modern civil rights litigation. As some of you may know, the famous PARC[4] case was brought on constitutional grounds on behalf of disabled children. That likewise sensitized the public to the plight of the disabled and the need to give statutory protection to their rights, which led in turn, of course, to the federal Rehabilitation Act and the ADA, which was subsequently passed largely, I think, as a result of that trigger.

In addition to the modern anti-smoking movement which started with *Banzhaf v. FCC*, a legal action my law students and I brought to get no-smoking sections on airplanes, first raised the public consciousness about the need to protect non-smokers from tobacco smoke pollution. That, in turn, eventually led to more and more legislation banning smoking in workplaces and public places—and, in some situations, even outdoors or in private homes. In short, litigation often breaks down barriers long before legislators are willing to act. And in doing so, generates the publicity and public support necessary to pressure legislators to act often against powerful money interests, which otherwise could easily defeat legislative attempts to reign them in.

Even when litigation doesn't start a movement, as it did with civil rights, disability rights, anti-smoking, nonsmokers' rights, and perhaps even environmental protection, it often serves as a very powerful and necessary tool for social change in areas as diverse as women's rights, our rights, safety, drunk driving, consumer product safety, gay rights and so on. The legal action has been, and will continue to be, a powerful tool for social

change—something that allows individuals like myself and small organizations to take on and often triumph over powerful interest groups, which could otherwise defeat us in the legislature as in the case of the cheeseburger bill, can no longer be doubted. But some argue that these activities are inconsistent with modern economic theory, and with our free enterprise system and philosophy. But they're wrong and here's why.

Now I'm only a former MIT engineer turned law professor and practitioner of legal activism of public interest law, and I'm not really a true economist. But my understanding is that we have and treasure a largely free enterprise system rather than a government dominated one, because we believe that millions of business people are able to make much better decisions regarding what will be produced and how it will be produced than the so called pointy headed bureaucrats and pencil pushers in Washington or state capitols. These independent businessmen and women, and not the government, are in a much better position to decide what shall be produced and how it shall be produced, because they have to balance the costs of various components of production against the increase and the expected demand for their various products. If they have accurate information, they, we believe, can do a much better job than the government.

But as many of us realize this system, making use of the invisible hand of Adam Smith, works only to the extent that the corporate decision makers actually bear those costs, and therefore, have a clear economic incentive to reduce them to the extent economically feasible. But where the company does not, in fact bear the costs, a situation in which the costs are said to be external, or externalities, it has no financial incentive to reduce them. The invisible hand of Adam Smith stops working, and some form of government intervention is appropriate, if not absolutely necessary.

The classic example, of course, is pollution. If companies generating power or making coal or refining oil don't have to pay for the cost their pollution causes, the Coase Theorem, and other forms of economic analysis, all say the government must step in to limit production—to limit pollution one way or the other. The same economic problems would naturally apply to businesses which cause great and very costly harm to the public health. For example, smoking costs the American public almost $200 billion a year, more than enough, by the way, to cover all the costs of healthcare reform or to make a significant slice in the federal deficit. And most of that is paid right now by nonsmokers in the form of higher taxes and bloated health insurance premiums. Indeed, one reason why the industry is so damned profitable is that they don't have to pay any of the costs of the injuries and deaths that they cause.

So using litigation to both encourage reform—which legislatures are reluctant, or in some cases even fearful, to impose—or simply as a step in shifting costs to the industry, and through the industry to increase prices to those who use the products, seems both fair and appropriate from an economic point of view. Indeed, failing to do so—failing to shift these costs

and making the great majority of nonsmokers bear these costs, seems grossly unfair as well as economically inefficient. Similarly, obesity is now said to cost us almost $150 billion a year, but unlike smoking, which is on the decline, obesity seems to be rising—its unnecessary medical care costs are soaring. And again, they are being paid largely by those who are not obese.

Major economic and other studies identify two major causes, culprits, if you will. The fast food industry, with its ubiquitous advertising, fat and calorie laden meals and supersizing, is said to be responsible for at least half of it; and the soft drink industry, the major totally unnecessary source of empty calories in a typical American's diet is also responsible. So it seems only fair, and logical, and economically justified to bring legal actions designed to shift some of those costs to the industry and to the consumers of their products, and to provide them with the necessary economic incentive to reduce those unnecessary costs, as they are now beginning to do so in part because of the pressure of fat litigation.

For example, looking just at McDonald's, it now has some entrees which are reasonably low in fat and calories. It also has some more healthful desserts to replace those calorie laden deep fried pies which always burn our tongues. It eliminated super-sizing, strangely, just before the movie "Super Size Me" came out. Wasn't that a coincidence? That's the first time I was ever in a movie by the way. Again, a more conspicuous disclosure of calories before it was required to do so. At least one McDonald's company actually came out and warned people, don't eat at McDonald's more than once a week, believe it or not.

Well, that was McDonald's France and once McDonald's of America found out, they shut him up. But for one brief shining moment they did. And it reformulated its Chicken McNuggets: the one dish singled out in the child obesity litigation by a federal judge who termed them a "McFrankenstein creation" with far more calories than most people are likely to imagine.[5]

Also, as you will hear this afternoon, other major companies in the food industry have also made significant changes as a result of legal action and/or the threat of legal action; including the bad publicity which can result from lawsuits, as well as the threat of disclosure through pretrial discovery of the type of embarrassing and incriminating documents which fueled the anger of jurors in the smokers suits against big tobacco.

Some people, of course, doubt that these changes were brought about by fast food litigation and the threat of fat litigation. But in many of the newspaper articles, these companies admitted that that was the cause. Many lawyers and scholars who strongly object to these legal actions, nevertheless, have publicly recognized that they're having a major legal impact. And most of the impartial reporters who wrote these stories wrote that the lawsuits were a major factor in each of these big decisions.

But as you might suspect, many, especially those on the losing side, who suffer when public health is at an advantage or protected, are com-

plaining. They call these effects "regulation by litigation" as if there is something inherently wrong with this approach. And talk about legislators subverting representative democracy. But is it? I'm not a constitutional scholar, just a humble practitioner, but it seems to me that there are three branches of our government, all of which are equal. Each is designed to play a different role in overall governance and in making law, but all of them have the power, and, perhaps in appropriate cases, the responsibility to make new law.

Legislators, of course, make law by passing statutes, but we also know that the Executive Branch, as well as the so-called independent agencies, make a tremendous amount of law by issuing regulations, adjudicating individual controversies, and by so-called "executive action." For more than 200 years we've recognized that courts and judges do not look up into the sky and proclaim preexisting common law, but rather by adjudicating cases and controversies properly brought before them, make new law; it's as important in many cases as the law made by legislative bodies, and in some cases, perhaps even more important if it's based on constitutional grounds, and cannot then be overturned by simple legislative enactment.

No one branch of government is superior to any other. I know of no requirement that new law, or even law in certain areas, must be made by the legislature rather than the executive or judicial branches. It's also well known that lawyers involved in litigation will often have a choice of judicial forums. Not just federal versus state, but sometimes different geographical locations, and quite naturally they're going to pick the one which is most likely to advantage their client and his cause. And naturally, the same is true for an attorney seeking to make law about issues involving public health, whether it's smoking, obesity or anything else.

When I was concerned about the harmful effect of ubiquitous cigarette advertising back in 1966, I would hardly turn to Congress. They just passed the law toning down the health warnings that the FTC had proposed for cigarettes and given the industry a major block of preemption immunity. Instead, I proceeded before a federal agency, where I was successful in achieving not regulation through litigation but regulation through regulation of favorable ruling, and resulting in the ban on cigarette commercials I could never have obtained from Congress or from a court.

Similarly, when McDonald's claimed that its french fries were cooked in "100% pure vegetable oil," but deliberately, and despite repeated requests, refused to disclose they were precooked in—beef fat—my law students logically did not turn to Congress. The way the food industry has so much clout, I almost succeeded in getting a cheeseburger bill against us. Instead, they brought a legal action, which I'll describe a little bit more in a minute. We went to the courts because in the courts, the wealth of one side is not supposed to buy an unfair advantage. But interestingly enough, instead of allowing a court to settle the matter in a proceeding in which neither side would be given an advantage because of wealth or potential politi-

cal influence or size, and each side would have an opportunity to present its case in a fair, open and impartial proceeding, McDonald's, which had once characterized the lawsuit as frivolous, chickened out, settled for over $12 million and agreed to provide the relief we had requested.

This in fact, has been the history of many of these so-called fat legal actions, which, by the way, are not the same as obesity lawsuits. Obesity lawsuits have as a central premise that plaintiffs became obese because they were induced to eat defendant's food through unfair or deceptive advertising or some other culpable conduct, failure to disclose material facts, whatever it might be. And that is the basis of the so-called obesity lawsuits. But a fat legal action on the other hand, is any legal action, in any form, based on any legal theory which seeks to attack fat and/or obesity. And it need not and often does not make any claims based upon the obesity of the plaintiffs. This is exactly the approach that my colleagues and I used so successfully against the problem of smoking.

While some of those lawsuits allege that smoking caused individual plaintiffs' diseases like lung cancer, the lawsuits targeted secondhand smoke, claims by states that smoking increased their medical costs, cases brought under the ADA, cases brought under the doctrine of nuisance and trespass and covenant of quiet enjoyment, and many other different legal theories and arguments. Indeed, many of the anti-smoking legal actions were brought not before courts at all, but rather before regulatory agencies: FCC, FTC, FDAC, AB, OSHA, the Department of HHS, Maryland OSH, workers compensation commissions, and many others.

The same now appears to be true regarding so-called fat legal actions, at least ten of which have now been successful. And all because the other side, frequently after assuring the public that the plaintiffs' claims were frivolous, chicken out and either settle or capitulate. It wasn't because some giant law firm or huge anti-obesity organizations were overwhelming tiny powerless little defendants—unless you think that McDonalds and KFC and Coca-Cola and Kraft and Pepsi Cola and Kellogg are tiny—largely powerless defendants unable to withstand the might of a couple law students, a Hindu attorney, a few law professors, another individual lawyer out in San Francisco, or that mighty Goliath known as CSIPI, Center for Science in the Public Interest.

Here's a quick rundown of the ten fat lawsuits which I consider to have been successful, again not because we won in court, because in each case they chickened out and gave us what we wanted. I think they were not only concerned about the possible loss, but about the adverse publicity in court and also the possibility of the discovery of documents that they would rather not have disclosed.

The first one, as I mentioned, was the suit my law students put together against McDonald's for failing to disclose that their french fries were cooked in beef fat. Settlement was $12.6 million and they made the disclosure. There were two others where companies, one Big Daddy Ice Cream,

another Pirate's Booty Diet Food, grossly misrepresented the amount of fat and calories in their food. Each one was a class action, each one was settled, and they made the proper disclosures. Another one was a suit against Kraft Oreo cookies for failing to disclose that the Oreo cookies contain dangerous transfat. The company settled out of court, and removed the transfat; resulting in cookies which certainly were healthier and probably had fewer calories.

Another was a suit against New York City School Board, who agreed to settle a suit by banning all sugary soft drinks and most fattening foods from its classrooms. There was another suit against McDonald's that involved transfat. They were sued after they announced with great fanfare that they would remove transfat, and then quietly reneged on the promise. They then agreed to make the required disclosure and paid $8 million to settle the lawsuit. Another one didn't even go to a suit. It was simply my threat to sue the individual members of the Seattle School Board for breach of their fiduciary duty if they renewed what we call a pouring rights contract. Sometimes known as a "Coke for Kickback" contract under which schools get a certain amount of money for every Coke or Pepsi or whatever it is that they sell. As a result of those threats, they grossly modified the contract, agreed to turn off the vending machine during most of the day, require healthy beverages, so on and so forth.

Number eight involved KFC. They were sued for having dangerous levels of transfat. KFC agreed to switch cooking oils to virtually eliminate it. And as far as I can tell, it will also reduce the amount of calories. Number nine involved sodas in schools again, and here there was a coordinated series of class actions, which were about to be brought against the bottlers this time for selling sugary soft drinks. But just on the eve of that being filed, the bottlers agreed to virtually ban the sale of sugary soft drinks in school, especially during school hours.

Number ten involved the Kellogg Company, who avoided a threatened lawsuit by this dreaded Center for Science in the Public Interest campaign for commercial free childhood and Massachusetts parents. Kellogg Company adopted strict nutritional standards for the foods that it advertises to young children. And the latest, number eleven, we actually won an obesity lawsuit. A Brazilian court has just ordered McDonald's to pay a former franchise manager $17,500 because he gained sixty-five pounds while working there for a dozen years. I know it's only Brazilian law and I can't translate it from the Portuguese, but think about it.

Well, in summary, to paraphrase an old tobacco industry saying, "We've come a long way, baby." And we've done it using legal and law-related actions with regard to both smoking and obesity. Indeed, many colleagues and scholars have admired what's been happening with regards to tobacco saying, "Well, if they can do that with regard to tobacco, well, why can't they do it with regard to teenage pregnancy, drug abuse, whatever?" They're throwing in whatever public health problem they can. It's also

clear that even though the use of legal action as a weapon against obesity is less than ten years old, starting in roughly 2002 as compared with the forty plus years since I first used legal action to get a blizzard of anti-smoking messages on radio and TV, it has already had a major impact far beyond the results of the individual victories which I have described above. And certainly a much bigger impact than the Surgeon General report on obesity, which had almost none.

It's just one very telling example. Every spring in Washington, there is a food policy conference. The one held in 2002 following the Surgeon General report, there was not a single panel, not a single discussion on the issue of obesity. The following year after, I had literally gotten hundreds of news items, TV broadcasts, magazine articles, and other publicity about using legal action—the issue of obesity was front and center at that conference. Indeed, the highlight was a spirited debate between me and a spokesman for the National Restaurant Association, who solemnly opined that it will be impossible to require calorie disclosures. Well, he's wrong. We're now doing it.

Also, as I noted before, legal action often leads to publicity and drawing public concern, which in turn leads to legislative action, and that's what seems to have happened with regard to fat legal actions. A few quick examples. New York was first, but now as a result of the Obama Healthcare Legislation, all fast food chain restaurants nationally will be required to disclose the calorie content of their foods, which is one of our major demands. I'm told that more than two dozen jurisdictions now have some tax on, or aimed at, sugary soft drinks. A number of jurisdictions have banned transfat. Some have banned fast food restaurants near schools, some are giving out obesity report cards. And San Francisco is about to ban kiddy meals and calorie and fat-laden Happy Meals at McDonald's.

The beat goes on as we continue to use legal action against major public health problems like smoking, and doing so, as I noted before, in all three branches of government. For example, I just helped convince the legislative branch, Congress, to permit smokers to be charged up to 50% more for health insurance, even if no wellness requirements are met. I helped persuade a number of state agencies that because they had a fiduciary duty to foster children entrusted to them, they should ban smoking in homes and cars when foster children are present. This is leading to more legislation banning smoking in cars when any children are present.

We also are increasingly turning to the courts when nonsmokers are bothered by tobacco smoke drifting or re-circulating into their apartments from adjacent buildings, or in getting court orders banning smoking in homes to protect children involved in custody disputes. Indeed, we have actually gone abroad and helped to pass, and now effectively to enforce, a new world anti-smoking and nonsmokers rights treaty. And that's why if any of you have ever had a hankering to go to a smoky Irish pub, I'm sorry, it's too late. We abolished them. And if you fly into Norway's major air-

port, you'll see a big sign out as you arrive and it says, "The only thing we smoke here is salmon."

So considering that the anti-smoking lawsuits have been going, and around much longer than the anti-obesity or fat lawsuits, I think we have made remarkable progress. And I think as with the tobacco litigation, which took a long time—and I have a very vivid memory of being on a TV show with Victor Schwartz—Schwartz on Torts for those of you who remember him—and Professor Twerski of the restatement, both laughing at me and telling me that we would never even get a tobacco lawsuit into court much less get it to a jury. Well, these things are happening. As somebody who's made a career out of bringing lawsuits which most people thought were unwinnable and probably even frivolous, I think we are going to continue to win. And I think not too long from now, a number of these private interest attorneys are going to find that as with the tobacco cases, they can not only do well, but do good by bringing anti-fat litigation. Once they learn that they can do well by doing good, indeed, fat may very well become the next tobacco.

Very certainly, this is an area of concern about the public health which is going to continue to be targeted by those of us who believe in the motto "sue the bastards." Thank you for your attention and not holding me in contempt yet.

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1 *See* H.R. 554, 109th Cong. (2005) (as passed by House, Oct. 19, 2005).

2 *See* Banzhaf v. F.C.C., 405 F.2d 1082 (D.C. Cir. 1968).

3 *See* Brown v. Bd. Of Educ., 347 U.S. 483 (1954).

4 *See* Pa. Assoc. for Retarded Children v. Pennsylvania, 334 F. Supp. 1257 (E.D. Pa. 1971).

5 *See* Pelman v. McDonald's, 237 F. Supp. 2d 512, 535 (S.D.N.Y. 2003).

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DECEMBER 5-7, 2010

EDITED TRANSCRIPTS

PROTECTING THE PUBLIC HEALTH: LITIGATION AND OBESITY

John F. Banzhaf III, Theodore H. Frank, Stephen Gardner,
Joseph M. Price, Todd J. Zywicki
Moderator: Linda E. Kelly

JOSEPH M. PRICE: Thank you. This is the largest en banc panel I have ever been on before. My name is Joe Price and I am not here today to represent the food industry, or the restaurant industry, or anybody. I am speaking on my own behalf. Listening to Professor Banzhaf before I thought I would have been introduced as Darth Vader representing the evil empire, but I'm speaking as a litigator who's trying to bring thirty-eight years of mass tort litigation experience to hand to examine this question. And in its simplest form I think the question is, "Can you solve obesity through litigation?" and I think in its simplest form the answer is, "No."

From a public policy standpoint, litigation is a blunt weapon which plaintiffs propose to use to coerce companies into making changes that the plaintiffs feel are necessary. I think many of you'll agree with me, that you can't make satisfactory policy changes with coercion. With litigation, you do not build the kind of consensus, the support for consensus that's needed to make a lasting public policy decision. Much of the food litigation to date is less designed to solve the obesity problem and more to enrich the plaintiff's bar. As you'll see, even the public interest side has a financial interest in this.

One of the fallacies that I think we've heard from Professor Banzhaf, and that we hear from the Center for Science in the Public Interest and the Public Health Advocacy Institute, is the attempt to analogize this litigation to tobacco litigation. This is not tobacco litigation—it never has been, it never will be. Tobacco in any form over any time period is bad. Food, in almost any form over appropriate time periods and in appropriate amounts, is good. The plaintiffs try to analogize the tobacco litigation and the food litigation on the idea of addiction. Well, yes, we're all addicted to food, without food none of us would be here and it's again a question of how much you eat: calories in, calories out. There is no question that tobacco causes disease. But as I think I'll show you as we go forward here, it's not established that food causes obesity per se.

The court system is not a satisfactory vehicle for creating public policy. The legislative and executive branches are far better equipped to address these broad issues. Courts, as you all know far better than I, adjudicate a single specific dispute based on the evidence presented by the parties. Litigation, by its nature, is narrow. It is case specific. It may give a distorted view of larger issues due to the individual party's interest in the outcome.

Litigation usually revolves around money damages, not around policy considerations; and presentation by a party, either good or bad, can lead to a result which may or may not suffice for the specific dispute—but may not work as public policy. Society at large may have to deal with the ramifications of an inadequate presentation in a single court case or a slanted individual case presentation and resolution. Obviously, the influence of attorney's fees may affect counsel's decision on trial, on settlement, or appeal. And as I said, everybody has some kind of an interest in it.

This is a consultant's disclosure from Professor Daynard with the Public Health Advocacy Institute in an article he wrote several years ago, and if you look at it, even Professor Daynard, who's a "public-healther," has an interest in furtherance of the litigation. Also, lawyers for parties have ethical duties to the specific individual whom they are representing, and that interest may not necessarily be consistent with society at large. Legislators and executives are better equipped to enact broad policy goals. Input can be gained from wider numbers of sources, not just the parties to the lawsuit.

Legislatures can accumulate more information from more sources. Just recently we've seen the passage of the Child Nutrition Act.[1] We've seen the passage of the Food Safety Bill.[2] Neither of those, I submit to you, would have been possible if they had been engendered only by litigation. Litigation is uncertain, outcome is unpredictable, and the laws of the fifty states will vary on the issues. You will have multiple jury verdicts coming down, based on multiple different laws. Juries are all over the board on these types of cases, and nothing at the trial level is ever a final resolution because there's always an appeal somewhere down the road.

It's expensive; it's time consuming; and we've heard a lot this morning about the expense of litigation. These kinds of nationwide cases and frontal assaults are going to engender a vigorous defense by the defendants. There is no guarantee that the appeals will not cost more. The damages will go to the parties, not to some sort of public policy or educational initiative, and the cost of litigation will ultimately get passed onto the consumers. There are, as you will recognize, tremendous proof issues that go into this litigation.

There is no guarantee that classes will be certified, and in many of these cases where you're talking about consumer fraud issues, you are dealing with such small monetary damage amounts in an individual case, that if you do not have a class action you're not going to have a case that is even worth bringing. You're going to be confronted, if you're a plaintiff, with a variety of legal defenses. You're going to have preemption, you're going to have *Daubert* issues—you all can name them better than I can—and you're going to be confronted with the defense of personal responsibility.

And I know Professor Banzhaf. The hair just went up on the back of his neck and he's chomping at the bit to come back and talk about that. But personal responsibility is, in fact, a legitimate defense in this litigation and I will guarantee you, I have done a lot of jury research over the years, and

you all have seen juries react this way. Personal responsibility, in this country, at this time, is significant.

The idea of using litigation to fight obesity started in 2003 with the *Pelman v. McDonald's*[3] case. That case was brought by several youngsters who had eaten, I think, every day of the week at McDonald's, claiming that they became obese, then became ill. *Pelman* was ridiculed and the case gained no traction. It was the subject of late night comedy and the like, for a variety of reasons; not the least of which was, to be able to show causation, you have to be able to show a connection between the obesity, the disease, and the food. And the question is, "What causes obesity?" It's really calories in, calories out. But is it because working families are predominating today? Does that cause obesity? Because there's no time to cook healthy meals at home, and fewer family dinners mean that people go out for more fast foods? Is that why we have obesity? Is it using food stamps to purchase sodas?

Well, what about using food stamps to purchase donuts? Or what about using food stamps to purchase candy? Is it a failure to have grocery stores in low-income neighborhoods? Is it lack of exercise? This is from the Let's Move initiative that Mrs. Obama has been working on, and this was a startling figure to me: eight to eighteen-year-olds devote an average of seven and a half hours to using entertainment media including TV's, computers, video games, cell phones, and movies in a typical day. Think about that ladies and gentlemen. There are fewer physical education programs, and kids are on their computers and the video games.

There are no sandlot sports like we used to have when you would come home after school. Everybody's driven every place. There are no sidewalks for you to walk or ride your bike. These are factors that go into obesity. And then the question is, "What food causes obesity?" Was it the pizza or was it the ice cream? Was it the chips? Was it the soda? How are you going to establish, in any given case, what caused an individual to become obese? Then, here's another article that recently appeared: scientists now think that there may be a viral link to obesity, and if that's not enough scientists also believe that genetics may have a role in obesity.

All of these factors will be used to refute the argument that you can come in and say it was a McDonald's cheeseburger that caused this person to get fat. About a month ago, I was asked to speak at the Institute of Medicine here in Washington to a childhood obesity group. I looked around the room, and these were people who knew more about obesity, knew more about what causes people to become obese, understood marketing, understood restaurants, fast food—all of them understood this—and I would say about 20% to 25% of those people had a weight problem. It's not because they were snookered by the fast food companies.

Let he or she who is of a BMI of less than 25 cast the first stone. Even if you can show what causes obesity, then you have to show: did it cause a disease? Did it cause diabetes? Did it cause heart disease? Well, what

causes these things? Answer that question and you get the Nobel Prize. Some people who are skinny have these diseases; some people who are fat don't have these diseases. Many people eat badly, and, you know, some of them never get sick at all. Genetics is obviously a part of it. If science can't answer these questions, lay juries are going to have a very difficult time doing so; and the plaintiffs agree.

There is an article written by Professor Richard Daynard with the Public Health Advocacy Institute about the lessons from tobacco to obesity lawsuits—I'm sure Professor Banzhaf is familiar with this. In this article, Professor Daynard notes that there's little support for these cases because the people and the courts are critical of overweight citizens who claim restaurant food and food products made them fat. Causation issues in food litigation are complicated, and it's just what I said. And the plaintiffs recognize that. They recognize that they have an uphill battle to convince juries that food caused a disease in any given individual.

So they want to shift to consumer protection arguments. They have been talking about this now for years. Professor Daynard and I danced around this issue back in 2004. At that time, the well-honed army of lawyers was getting ready to switch from tobacco to obesity litigation, and the swat troops were getting ready. Ain't happening. And here's the esteemed Professor Banzhaf and I and Morgan Spurlock's film back in 2004.[4] The fact of the matter is that they now want to use consumer fraud instead of the direct obesity approach to try and prove indirectly what they cannot prove directly; it's a little disingenuous. It's sort of an "ends justify the means approach."

Professor Daynard admits that when you can't come up with the causal link, "Let's go try to do it through the back door." For example, you go out and see lawsuits against people who make things like Snapple. They use the term "all natural" and so somebody gets bent out of shape because they spent $1.09 and they did not think it was "all natural" because it has high fructose corn syrup, which Dr. Jacobson at CSPI agrees is the same as sugar. That was a class action in California that was denied certification.[5] There was a class action in New Jersey that was granted certification.[6] All these things are out there pending as far as whether or not this is a part of the obesity problem, but this case does not have anything to do with obesity.

Same thing with Ben & Jerry's. CSPI complained about the use of the term "all natural." Ben & Jerry's said, "Okay, we'll take it out of there." And Mike Jacobson said, "I'm glad Unilever made the right call." Next thing you know there's a suit against Ben & Jerry's over whether the ice cream is "all natural" or not. Give me a break folks—it's ice cream. This is not health food. You know what you're getting when you eat it. And then you have the settlement problems, and we'll hear about that. Kellogg's settles a $10.5 million class action: class members get three boxes of

cereal and the lawyers get $2 million in fees and expenses. So, where does it leave us?

Kelly Brownell at Yale—who's another one of the gurus of fat litigation—says that companies ought to suppress their automatic opposition to public health recommendations, and to a certain extent there's some truth to that. But I submit to you that the plaintiffs also ought to suppress their automatic, knee-jerk reaction to think that everything can be resolved by litigation. Because if we go to litigation, we're going to go to the mattresses; we're going to dig in, it's going to be costly and expensive, and there are better and easier ways to do it. Thank you.

LINDA E. KELLY: All right. Thank you Joe. Now, let's hear from Ted Frank.

THEODORE H. FRANK: Thank you. I think I'm qualified to speak about obesity class action litigation as an obese class action litigator. I would like to start with the public policy hypothetical. Let's envision the world where it's indeed the case that it's advertising that's forced me to go to fast food restaurants and buy chicken quesadillas and what not, and results in the shape that I am in today even though it's the exact same shape as my brother who has a completely different diet. What we're really looking at here is a problem of advertising. So if we have an advertising problem causing people to be obese, let's counteract it with more advertising.

As a public policy matter, we might have to really twist Hollywood's arm into this. But I think we can get to Hollywood and Madison Avenue and say, "What you need to do is, you need to go and convince the American public that what is sexy are people who are svelte—people who are thin; people who are athletically lanky; and stop glorifying the obese in your advertising. Make thin attractive. You should, when you cast roles in comedies and dramas, make sure you're not putting fat people in them, put athletic, thin, svelte people in there."

And if you are going to have somebody who's obese, make sure that you imbue them with qualities like slobbiness and obnoxiousness, maybe you can have—if you have a popular sitcom like Seinfeld—an obnoxious fat neighbor in there. Or maybe you can have some cartoons on Fox on Sunday night where the protagonists are overweight but really obnoxious. That way people will associate fat with negative qualities, and we can maybe have game shows where people lose weight and have people who epitomize sexiness and they'll be lean and they won't just be models, we'll call them supermodels.

And just in general, let's glorify thinness and make obesity unattractive. And because advertising works, once we do this and it's not just Hollywood, we can get Washington involved, maybe we can get the First Lady to do some anti-obesity campaign. But once we do this, because advertising works, fat will disappear from our nation once we have Hollywood pre-

sent the message that obesity is not socially acceptable. And okay, everybody gets the joke and we have these mixed messages from advertising and yet we have this growing obesity problem as a country. We have a growing obesity problem on this panel.

It can't all be because we're ignorant of how many calories a Big Mac has, because I didn't have the Big Mac until I was twenty-five. But it shows the problem of addressing this through litigation because there's obviously a causation issue here. It's not the advertising that's doing this. And that's what eventually doomed the *Pelman v. McDonald's* lawsuit. The class certification was denied, and in fact, if you look at the other lawsuits that Mr. Banzhaf singled out at lunch time—he calls these "fat lawsuits"—that are this marvel of public health and you look at what they're actually doing.

The results are somewhat different. For example, Kraft replaces, in their Oreo cookies, the partially hydrogenated oils with a different kind of vegetable oils. And trans fats are probably cardiologically worse for you than other kinds of fat, but at the end of the day, fat is fat. Each gram of fat still has nine calories, whether it's partially hydrogenated or not, and the difference is not going to make a difference in the obesity. It is going to transfer some money from consumers to lawyers, certainly. Maybe there will be some marginal improvement in health because Oreos no longer have the partially hydrogenated oil, but it has nothing to do with fat at the end of the day.

And it's also far from clear that—Ralph Nader has made this wonderful career of finding out that somebody was about to do something—the government or industry is about to act in a certain way, and rush out and hold a press conference and demand that they do it, and then take credit when it happened the next day.

I think that's what happens with a lot of these lawsuits over trans fats, because there's been an industry movement to move away from trans fats as people recognize the health problems related to trans fats, and they want to see other kinds of fats in their products. You begin to see across the supermarket aisles—lots of zero trans fat labels on boxes because manufacturers recognize that that's appealing to consumers. And whether or not Kraft would have gotten there without the litigation—I think they would have. Souls can differ on that, but I don't think the litigation made a big difference there.

If we look at some of the other fat lawsuits that Mr. Banzhaf has raised, one regarding Pirate's Booty, another one regarding minor ice cream brands in Florida, these are interesting class actions. What they were, were mislabeled products. Whether intentionally or mistakenly, the products said they had X number of calories and in fact they had X plus Y number of calories, and that's your basic run-of-the-mill consumer fraud. There's nothing special about that in terms of fat. These are not unique lawsuits; these are the same kind of consumer fraud lawsuits that have been brought

since the beginning of consumer fraud lawsuits. I have two points to make about them.

First of all, it's really not the case that the reason people are fat in America is because they're buying 150 calories worth of ice cream and they think it's really only 120 calories. That's not what's really happening. We're consuming more calories, we're exercising less, and it's not because we're confused about the labels. Certainly, it's not a bad thing when the consumer fraud lawsuits are brought against the bad labels. Though in both of these cases, it was not the lawyers who discovered that there was a problem, there were newspaper investigations that discovered that the labels were inaccurate and then the lawyers jumped on the bandwagon and sued after finding out about it.

But what is interesting about these lawsuits is that these lawsuits are trumpeted as examples of good public health litigation, in fact, preventing obesity. The ice cream lawsuit in Florida, you know how that settled? That settled for millions of dollars for the class action attorneys, as per usual. And the injured consumers who were grievously injured and consumed all these extra calories because of the mislabeled ice cream, they got coupons for free ice cream. And whatever that lawsuit is doing it's not preventing obesity. I think the similar thing is happening with McDonald's.

You can say litigation has caused them to offer salads that they wouldn't have otherwise. But if you look at the fast food menus across the board over the last six years, you'll see an ebb and flow of companies going back and forth on this—offering healthy options, discovering that when people go to fast food restaurants it's not for the healthy options, and taking healthy options off the menus, and then putting them back on when there's a public backlash.

Certainly, there's a consumer demand for this. Subway demonstrated this. They had a troubled young man, who did nothing but eat Subway sandwiches for a long time and lost a lot of weight doing so, and ran a whole advertising campaign around him and this encouraged other fast food restaurants to offer low calorie options. But at the end of the day, they're also offering the high calorie options. And something we've seen over the last three, four, five years is these mega-sandwiches—Carl's Jr. Thickburger or what have you—have 900 calories, 1,000 calories, 1,200 calories; all upping the ante.

Just last night, during the football game, there was a Burger King ad for a buy one get one free chicken sandwich. Two chicken sandwiches have 1,320 calories with 720 calories in fat. So, fast food restaurants do not seem to be all that scared about the litigation to the extent that they're reducing calorie options. I think it's reflecting consumer demand. Now, what can we do in terms of litigation? The whole weight issue, it's a very simple plus/minus kind of thing. More calories in versus less calories out is going to be a weight gain, and vice versa. And 3,500 calories is a pound,

and you start assigning liability on a market share basis, for who knows how much.

Do we sue George Mason for the Snickers bars in back there? It's not just the food we're eating but it's the change in our exercise patterns. A generation ago, I imagine just about everybody in this room, including me, when they were a child, when it came time to washing the dishes, you would manually wash the dishes. That burns an extra 300 calories an hour, and if you're doing that two minutes a day, that's ten calories a day. If instead of washing the dishes, you're putting them in an automatic dish washer, you're missing out on those ten calories a day. Ten calories a day over the course of a year, that's a pound a year.

Over a decade that's ten pounds a decade. What a coincidence, that's just about enough to get us where we are in terms of weight gain. Do we sue Maytag?

What we are faced with is a change in culture where a century ago our employers would pay us to perform manual labor; we have moved to a service economy where we're all lawyers sitting and typing at a computer, rather than performing manual labor. We have to go pay gymnasiums to exercise, rather than being paid to exercise, and of course we're exercising less because of it. Food is cheaper than it was before, we're eating more of it, and that's what's causing our obesity problem. That's a social issue. And it's not one that's going to be solved by litigation. Thank you.

LINDA E. KELLY: All right. Thanks Ted. And now we will hear from Stephen Gardner.

STEPHEN GARDNER: It won't be solved by litigation, but the same as having a thousand lawyers under ten feet of water, up to their necks in sand—it's a real good start. There are two arguments that people who do not like lawsuits, and would not hold food companies responsible for violating state and federal law, will use. One is the personal freedom, personal responsibility mantra; and the other (and this very odd), "Well, it will not fix the obesity crisis." Well, the tobacco litigation resulted in a significant amount of change, especially in the way cigarettes were marketed to little kids. It hasn't gotten rid of smoking, but it was a really good start. The efforts that John has been making, for longer than most of us have been alive I think, have helped.

And there's no reason that you do not approach something incrementally just because you cannot wave a magic wand at it. I think my mother was scared by a banker when I was in the womb because the only cogent thought I had in high school was that I wanted to be a consumer lawyer. The rest of the time was, "How do I get girls to talk to me?" And that's what I was able to pull off.

I was a legal services lawyer, the Student's Attorney at the University of Texas, and then I went to the New York and Texas AG's offices, work-

ing with Bob Abrams in New York and then Jim Mattox in Texas. For almost thirty years I've been bringing suits using consumer protection laws for deceptive claims made by food companies, finance companies, and all sorts of other things. It is my experience that it's completely legitimate to use consumer protection laws to have a positive effect on the marketplace. In fact, I get calls now from competitors who want me to take action against the other company because the other company is stealing their business.

That's bad capitalism. We're trying to make consumers better capitalists, better consumers, and in fact give them more freedom and more freedom of choice. Joe used the natural cases, and for reasons I honestly do not quite understand, to belittle obesity litigation. Of course the natural litigation is not obesity litigation. It's not on John's list; it's not on my list. It, again, is capitalism. HFCS, high fructose corn syrup: there's a chapter in a book on food science that lays out the process necessary, starting out with corn and then tweaking the molecular structure, to end up with high fructose corn syrup. It isn't natural, it isn't close to it.

And calling it natural so people will buy it is purely deceptive. It is absolutely right that at least based on current knowledge, it's about the same as regular sugar in causing weight gain. There's emerging science that shows that the false satiety of HFCS is not the same as sugar and therefore people will consume more of it. So developing science indicates that HFCS may be worse; but that's not the point of the lawsuits we have brought on "natural," or the lawsuits private lawyers have brought. It's just, "Tell people the truth." And no, stopping Snapple from using the word "natural" when it has high fructose corn syrup or Ben & Jerry's or anybody else, is not going to cure consumer fraud involving fraud. But it's a real good start.

I'm not going to belabor the cigarette litigation too much because John has talked about it, and I reckon he will again, and others may. But cigarette litigation is not a direct template for food litigation for a couple of very important reasons—well, one really. Food is multifarious. There are thousands of companies, there are all sorts of food, and at this point in time in the law, it is not possible to win. Courts have not bought any way to show that McDonald's made X person fat. It's certainly not going to be possible to show that McDonald's made an entire class of people fat.

But what it is possible to show is that McDonald's, or Burger King, or Kraft, misled consumers and the fact that that doesn't cure obesity does not excuse misleading people to sell food or to sell any product. You shouldn't be able to cheat to sell a product. Although food marketing is not a parallel to cigarette companies, not even the tobacco companies marketed to three-year-old children. McDonald's does, McDonald's markets—and I'll talk more about our planned McDonald's lawsuit—using toys.

Anybody who is a parent knows the toys in McDonald's and other fast food companies' products are there as an attempt to cut into parental responsibility, to cut into parental rights, by going around the parent, no mat-

ter how hard they try to prevent it, and marketing straight to the kids; and McDonald's has a toy for kids under three. So, they're marketing to three-year-olds and two-year-olds. That's something that not even—I don't think so, John might correct me—but I don't think Joe Camel was aimed at the toddler group. It works with children. Children know the golden arches and it's a problem.

I remarked to a couple of people during the break that, "All lawyers, even judges, we're all symptoms of a breakdown of decent societal function. Lawyers and judges, the whole system would not exist if we all treated each other fairly.

So it is essential in our society to have lawyers and judges and litigation to correct any number of problems. As Margo Wootan, who is the costar with John in "Super Size Me," is CSPI's Director of Nutrition Policy. When CSPI's litigation project was created and I was hired to run it, Margo was asked why CSPI got into litigation with all those sleazy lawyers. And she said, "Well, Congress hasn't done anything to address the problem. The federal agencies aren't doing anything. We are just plain out of branches of government. We've got to go judicial." And that is the choice we have to make.

We have to, when it's essential, whenever efforts of CSPI and other advocates have made to stop a problem does not work, then litigation often will work. It will not cure false advertising. It will not cure greed. It will not fix the obesity crisis. But it will stop a component of those things, and I think it's very, very important. I also think it's important to stress that we have never asked judges to make new law. We ask judges to apply existing law. And with judges who apply existing law, we're going to win. It's what I would call, the activist judges—I'm sure there are none here—who in order to make a point, will ignore what the law says because they do not like where it's going.

But that does not serve as a reason that we should not try. Most all judges in my experience apply existing law, and choose to take their oath seriously; when that happens, we by and large will win. I was somewhat—because I'm not *really* surprised by anything Joe says, but slightly offended—when he said that we're only in it for the money or words to that effect. Joe can lose and still get paid. I can lose and still get paid too because I'm on a salary. The plaintiff's lawyers lose and they don't get paid. Most class action lawsuits are not brought for the purpose of making money.

I'm going to get to, in a second, why some are, and why you should forgive us for those people. But most of them are not. But even if they were, Joe do you work for a buck a year? The defense lawyers do get paid and they get paid every month and there's nothing wrong in our society for getting paid for what you do. So, the fact that you might be motivated by money is to me a little bit misleading.

Okay, I think I'm through venting. I want to talk about our planned, announced, and much-talked-about lawsuit against McDonald's, which is based simply on the fact that young children do not understand marketing.

A lot of people say, "Well, I don't know that I believe that," and my response is, "Well, I don't care if you don't believe that the sun rises in the east. It's fact. Kids don't understand marketing." Top childhood development authorities will testify for us. Kids do not understand and thus they are deceived. We're talking about McDonald's marketing using toys directed toward children. Bypassing parents, attempting to cut out the parent's choice and the parent's responsibility to accomplish two things. One, get the kid wanting McDonald's now, and two, get the kid wanting McDonald's when the kid is no longer a kid. The lawsuit is going to be a tough one. But it is trying to address again, just one component of what is not just obesity, but the health problem that exists in this country.

One of the slides that Joe used—he didn't highlight that part, so you all may not have seen it—said that one of the problems is that there is an environment that encourages fast food. A large part of that environment is fast food companies and food companies in general, marketing junk to people. The discussion of personal responsibility, for one thing, avoids the fact that we're talking about six-year-olds. So, they really don't have much personal responsibility. They're still wetting their pants. They're not fully matured human beings, and they are the subjects of this marketing.

But even to the extent, and it's a real extent, that parents can and should control what their kids want to do and should be responsible for controlling them, the parental responsibility argument avoids the fact that the companies who are putting out the ads should be responsible for the effects of the ads too. There is a duty under state consumer protection laws, as well as under federal consumer protection law for companies not to deceive their intended victims. The argument that it's all about individual responsibility ignores the need for equal responsibility on the other side.

The only other thing I want to mention is that there are some really terrible—they are very much in the minority—but there are some terrible class action lawsuits. We call them greenmailers and copycats. I guess it's flattering, but every time CSPI files a suit or wins a decision we see copycat cases crop up. We try to persuade these people not to file, but they still do. They are the minority, they're the lazy ones, but you will see them. You will see people settling for coupons. There are some bad settlements. Most consumer class actions are not.

I do ask you all to keep in mind when you see a really cruddy class action that there are many more of them that have been resolved even before the lawsuit was filed at all. Because class action litigation is a very effective way to achieve the advocacy that I signed on to do. It's not the only way and it's not a cure-all, but it is one way to address responsibility of the companies who spend, in the case of kid's fast food meals, I think it's about

$15 billion a year trying to pull the children in. And I'm okay with that. Thanks.

LINDA E. KELLY: All right. Thanks Steve and we'll turn it over to Todd Zywicki.

TODD J. ZYWICKI: Thanks. I listened to Professor Banzhaf's lunch talk. I worked at the FTC from 2003 to 2004 and what really struck me, listening to Professor Banzhaf, was that he makes a really compelling case for, explaining quite well, why litigation is completely the wrong way to go about addressing public health issues. So, what I'm going to talk to you about is based on my experience at the Federal Trade Commission and how a regulator would look at this—a very complicated issue like this—and why thinking of it through this sort of simple minded approach of litigation on suing for things that you think you can sue, is really a counterproductive way of thinking about this.

And those who have seen me at these programs before: I've got this sort of quirky predilection where I feel obsessed to actually have to look at the data and test hypotheses about what's going on before I decide what is going on. The other thing is that I've got this quirky idea that you should actually think about the unintended consequences and the cost of the actions you take. So, while certainly, as Stephen Gardner notes, if there was an overall benefit here, even if it was small, that would be worth doing something; but if the overall benefit is exceeded by the overall cost, then I think you need to reconsider it.

What litigation is really designed to do is think about the benefits and ignore the costs, and this is an area where I think the benefits are very small, and the unintended consequences quite large. And what I'm going to focus on is advertising. Just to give you a small window of the big issue and show you how complicated that little issue is. I'm going to focus on advertising directed at children. And let me first say, obesity and weight is a big issue, so to speak. It's an important issue, and in many ways, it's actually a bigger long-term issue than smoking. The difference is obesity is a morbidity issue, which means that obesity really doesn't kill you.

What obesity does is lower your standard of life and causes you to consume a lot of health expenses for a long period of time. So it's very costly, very detrimental to people's health. Smoking is a mortality issue. So, for instance, the evidence seems pretty clear on this that in purely dollar terms—and this is a very politically incorrect thing I'm about to say but it's the first of many politically incorrect things I'm going to say in the next twelve minutes—smoking is actually a net budgetary benefit to the United States. Because smokers die earlier and they die faster, they don't consume as many medical expenses—they don't consume Medicare, they don't consume Social Security, or any of those sorts of things, right? I'm not saying that people should smoke, obviously. But obesity is a morbidity issue, it is

a net cost; smoking, from a purely financial situation, is a net benefit, which is in and of itself to give you some sense of the complexity.

So, let's talk about advertising, and what I would call hypothesis testing. If you're going to think about this, and the question you ought to think about is: "Is advertising causing kids to get fatter?" Right? Put simply. And then the question would be, even if it is: "What does the evidence show?" Then the question is whether or not we want to do something about it. So, I could think of a variety of ways in which advertising might cause kids to get fatter. Kids might watch more television and thereby see more ads, more minutes of ads. There might be more minutes of ads per hour, so there could be a change in composition.

For example, kids are seeing the same number of ads but a greater percent are junk food ads. There could be a change in the effect of advertising—it could be a change in the effectiveness of advertising. And after all that we've got to still think about what other problems there are. Let's talk about that. So, first question is, "Are kids watching more television?" How many people here think that kids watch more commercial television than they did in the '70s? It turns out kids watch less commercial television than they did in the '70s, surprising right? That does not mean that kids are out playing ball and running around the neighborhood.

What it means is they are playing video games and watching cable TV and playing on the computer and that sort of thing, but kids actually watch less commercial TV than they did in the past. They are a lot more sedentary. They are spending a lot more time on the computer and that sort of thing, but they're actually watching less television. Overall, if you look at the data, the Federal Trade Commission did a study on this a few years ago. What they found is that the fact that kids are watching less television more than anything else, kids have actually seen 9% fewer TV ads.

Kids, I'm defining, as under the age of eleven. Kids see 9% fewer television ads every year now than they did in 1977 because of that. It also turns out that food ads are a smaller percentage of ads on television. The big thing is that in 1977 when I was a kid, or an older kid, we didn't have advertisements for video games, and DVD's, and all this sort of stuff so what you've done is basically taken a whole new tranche of things, which of course, are sedentary activities, and that's competing for ad dollars with food ads.

So, kids are actually seeing—there seems to be no question when you look at TV, and TV's the big thing; we could talk about other issues—fewer food ads on television. There's also no indication that food ads have risen versus other products, as we said. And there's no change in what kind of ads you see, right? When I was a kid they advertised junk food on TV. My daughter, when she watches TV, they advertise junk food on TV. It wasn't some golden era where every ad we saw was Grape Nuts or whatever like when I was watching Hong Kong Phooey.

My daughter isn't seeing Grape Nuts ads when she watches Dora. First, there's no indication kids are seeing more ads. Second question is: have ads become more effective? Well, this is an important question to think about; the economics of advertising as it relates to consumption. Advertising has two different effects. One, it can increase market demand; this would be informational advertising. Say, when the iPod comes out, advertising tells consumers about the existence of the iPod. You would expect that advertising would cause iPod consumption to go up.

The second kind of advertising is brand advertising, which does not increase demand for the overall category of the product, it increases the demand for one product versus another; so, this would be buy Chevy versus Ford or buy Coke versus Pepsi or Nike versus Adidas. The effect there, is not to increase the overall demand for that category of product, but to increase demand for one brand versus the other. And in fact, it turns out that if what you have is brand advertising, a likely consequence is that it decreases overall demand for the category. Well, why would that be? Basically, informational advertising tends to decrease price, brand advertising tends to increase price. Why?

By making demand curves. Demand curves become more inelastic, which means you can raise prices and now there's a cost that you have put into this system that was not there previously. So, the overall effect is to increase price. Increases in price tend to cause downward sloping demand curves, which cause a decrease in consumption of that category.

We don't know whether or not what kids are eating increases market demand, like the iPod, or builds a brand, but it looks an awful lot like the second to me. That's just a hypothesis, and to the best of my knowledge, nobody's tested that hypothesis. But you would want to know it. Why? Well, I'll give you an example: cigarettes. It turns out the empirical and economic evidence on cigarettes is that cigarette advertising bans do not reduce consumption of cigarettes. That's what the economic evidence shows. Why?

Well first, almost all advertising of cigarettes is brand advertising, right? Camel's trying to steal from Marlboro or whatever. They have a shrinking market as it is. So, what happens is, if you ban advertising how do you compete? You compete on price. You reduce the price because now you can't advertise the product. So, that at least offsets the decrease in advertising because the advertising was never increasing market demand in the first place. The economic evidence shows that getting rid of advertising does not reduce consumption of cigarettes.

Third factor, maybe parents are acquiescing more to their kids? There's so much more pressure going on there. My daughter's five years old—she's precocious I admit—but she has not yet gotten into my car and driven herself to McDonald's. I wouldn't put it beyond her, but she hasn't quite figured that out, which means she has to talk me into going to McDonald's.

So, is there some evidence that maybe parents are giving in more to their kids now? Well, I don't know about that directly, but indirectly here's what we do know: kids eat what their parents eat. And the reason why kids are fat is because their parents are fat. Adults have been getting fatter faster and sooner than kids, and the problem is that the parents eat too much, they eat too unhealthy. As I said, I was guaranteeing political incorrectness so now you're getting it, right? Kids eat what their parents eat. That's what the issue is here. If you look at the data, it's quite clear that what kids eat is what their parents eat and that, if anything, the parents eat worse than the kids do. Well, what about other hypotheses? What if we could run the counter factual?

Look at societies that don't have advertising for instance, or have banned advertising to kids, or different cultures—does that make a difference? Well, you can look around the world and what you see, as it turns out, childrens' obesity is a global epidemic. You can look at places like Egypt, Ghana, Morocco, Haiti, Costa Rica and the United States; their childhood rates of obesity have maybe tripled. If you look at Ghana, rates of childhood obesity went up 3.8 times between 1988 and the mid-1990s. Morocco, went up 3 times, Brazil went up about 4 times, and Egypt went up about 4 times. Now, Al Jazeera may be awash of Cocoa Pebbles ads.

I'm not denying that it's a possibility that Al Jazeera's just jamming junk food down the throats of kids in Egypt. Color me skeptical that kids in Egypt are getting fat because of that. We've also looked at other situations. Sweden has long ago banned advertising directly to children. They have the same rates of childhood obesity as the rest of Europe. Quebec banned advertising directly to children, they have the same rates of childhood obesity and changes as everybody else in Canada. So, the effect here is that it doesn't work, and if you don't believe me, think about the final scenario, which I think of as the PBS diet.

You go to see the pediatrician and the parent says, "Well, Billy's getting a little heavy. What should we do about it?" And the pediatrician says, "Yeah, you're right he is. Does he watch TV?" "Oh, yeah, maybe four hours a day." "What channel?" "Oh, he watches a lot of Nickelodeon." The doctor says, "There's the problem. Switch him to the PBS diet. Let him keep watching four hours of TV a day but as long as it's PBS, not Nickelodeon. All that weight will just come right off." I don't know. It doesn't seem to me that the PBS diet is going to work, right?

So, we could say, I think with a high degree of certainty, that if we go after advertising directed at kids there's absolutely no indication that it's the source of the problem. The problem, if anything, is that kids are giving in too much to their parents rather than their parents giving in too much to their kids and so the question becomes, "All right, well maybe if it made a trivial, smidgen, hypothetical difference, maybe it would be worth it." Well, then we look at the cost. What are the costs? Are we willing to perhaps, get rid of Nickelodeon? Nickelodeon has a lot of food ads. Are we

willing to risk getting rid of Nickelodeon and other childrens' programming just because we have some theory that this might work, even though there's no evidence to support it? You start thinking about the unintended consequences of these things, and it starts to add up.

Let me close by then talking about one of the real problems and why this whole thing is just a side show. As I said, we're just looking at advertising; if you look at it seriously, it's not a serious part of the problem and it could have unintended consequences if we did it.

So, what are the real problems? Food is incredibly cheap now. We used to live in a society, up until a few decades ago, where starvation was the biggest problem that we had. Now, obesity's the biggest problem we have. Most of the problems that you have with obesity are simply a side effect of having solved much more pressing and important social problems. And unless we address that—if we're going to just fiddle with these gimmicks and stuff and think it's going to make a difference—we're not going to focus on the real thing. Food's incredibly inexpensive, and we've become incredibly wealthy, so food costs less. Activity levels are much, much lower. As Ted said, it used to be, "Your boss would pay you to work."

Most people were engaged in very physically demanding work. Now, you have to pay to exercise. All right, I'm sorry, your boss used to pay you to exercise, just as a byproduct of your work. Now, you have to pay to exercise. Suburbanization makes a difference. Longer commutes. Kids don't walk to school. Family changes. I promised political incorrectness so here you have it. A clear risk factor is that two parents working is a contributor to rising obesity, for exactly the reasons that Joe alluded to, which is there's less time to eat at home.

You eat out more, and when you eat out more, you tend to eat bigger meals. Finally, I'll give the most politically incorrect reason. This is not for kids, but for adults: smoking. Reducing smoking, which is a very good thing, has led to an increase in obesity. So, I look forward to the situation when Professor Banzhaf sues himself for the rising obesity epidemic. Thanks.

LINDA E. KELLY: Thanks Todd. We certainly have a diversity of views on the table here, and at this point, I would like to turn back to Professor Banzhaf to respond.

JOHN F. BANZHAF: My simple answer is déjà vu: I've heard all of this over, and over, and over again. I heard it twenty years ago when we started suing tobacco companies. There is no one simple solution to smoking or obesity. There is no one simple approach. That is why in my presentation, I pointed out that as an advocate, I have only certain choices. I can't wave a magic wand and make parents do this or that.

I can go to the legislature when it is the most effective, and I can go to the courts when it is the most effective; and I do, and I will continue to do so because we have proven over, and over again, that this stuff works—whether or not all these naysayers believe it. Joe talked about courts making bad decisions. Yes, occasionally courts make bad decisions; but I think it's likely that legislatures make worse ones because they are directly influenced by big food companies and other companies like that.

At least the hope is that most judges are reasonably impartial and, of course, if a judge makes a decision that is bad and is incorrect, it can be modified through the appellate process; unless he somehow does it on constitutional grounds, which nobody is talking about. The legislature can overturn it, but at least it will force the legislature to finally address the situation of obesity, which most of them are not doing. And I have heard personal responsibility, that's a good one. It goes back at least twenty years.

They told us we would never be able to win a cigarette suit because of personal responsibility. Bear in mind, there, we are talking about adults, and here, we are talking about children. And the answer is, "Yes, personal responsibility can play a role." Although, for a six-year-old or a ten-year-old, I'm not sure it's a very big role. As you know, it's brought up as a product liability action; personal responsibility diminishes, even if it's brought on a negligence basis. How much assumption of risk and contributory negligence are you really going to blame on a ten or twelve-year-old child?

Yes, maybe the parents are somewhat responsible, but where does that fit into the equation when the child is the plaintiff and he's suing a company? We are asking which one is responsible, and the answer is not, "Neither one is responsible," but, "Both are responsible to a certain extent." That in fact, is how we continue winning a lot of these tobacco lawsuits despite the same silly argument of personal responsibility. The *Pelman* case—everybody seems to dump on it. The fact is, that it's alive and well. Five out of five federal judges have upheld it. Judge Sweet upheld three of the major theories in his first decision and the suit goes on, even though everybody calls it frivolous.

And, as I think Joe pointed out in one of his articles, the Second Circuit has basically given us a road map: they say, "All you need is bare bones pleading," so anybody in the Second Circuit can file a very similar suit on the same grounds. The big problem everybody seems to be worried about is causation. Again, that is the same thing I have heard for twenty years with lung cancer in smokers, or lung cancer in non-smokers, and so on. But despite that, we continue winning.

Let's just take a hypothetical case; let's take little Jimmy who's ten years old. He and his mother are homeless. They do not have much opportunity for home cooked meals. Joey eats about 40% of his meals at McDonald's. Joey is morbidly obese and has, what we used to call adult

onset diabetes because it never happened in kids, now because it's increasingly happening in kids, we call it type two diabetes. If he eats 40% of his meals at McDonald's, roughly 40% of his calories are coming from McDonald's. Actually, we've done some studies. It turns out the meals he eats at McDonald's have more calories than the ones elsewhere, so maybe it's up to 45%.

Can we show that McDonald's is a substantial factor in causing his obesity? Sure. Is exercise the problem? No. I did some calculations not too long ago, pointing out that sending Ronald McDonald into schools arguing that the answer to obesity is just more physical activity, is a little bit like sending Joe Camel into schools arguing the answer to smoke, is just don't inhale as much. If a kid eats a typical Happy Meal, he has to play volleyball for about seven and a half hours to work off those calories from one single meal. I'm a volleyball fanatic, but I would never play seven and a half straight hours. Now, Todd, I have to tell you that dishwashers are not the problem of obesity.

Counter advertising does work, and the way we know that is I proved it can work. Give us one out of three ads: every time there's a fast food ad or a soft drink ad, give us one out of those three spots and we will reduce consumption by coming up with strong anti-obesity ads, the same way we did with smoking. I proved it. We know it works. Dishwashers are not the culprit. We know, for example, that although Europe has much the same society as we do, they have a much lower level of adult obesity; and we know that when people come over from Europe to here, they tend to gain weight. It's not because their genes change on the flight over. Maybe it's because we have a toxic environment.

Steve talked about the differences between the issue of tobacco and obesity. There are many differences and we acknowledge them, but some of them work in our favor. For example, unlike the tobacco industry, the fast food industry is very worried about its reputation. Therefore, they are risk averse. They are very worried about discovery. They learned from the tobacco industry. And unlike the tobacco industry, which can not really make a safer cigarette, they can. McDonald's, Wendy's, Burger King, can make changes, and I did not have time to go into it, but all of them have made it as a result of this. Do we want bureaucrats like what's-his-name over here working at the FTC? The FTC has never been a powerhouse of consumer protection.

We call the little old lady of Pennsylvania Avenue, and if I had to have somebody working on my behalf, I would much rather have somebody working on a contingency fee. There is that old saying, "Never underestimate the power of a lawyer on a contingency fee." In closing, let me remind the judges of what Prosser said with regard to torts. He said it was the business of the courts to make precedent where wrongs call for redress, even if lawsuits must be multiplied.

And if there is a wrong here, where one out of every three kids in school today will come down with diabetes—which is a dangerous and very costly disease—then I think you have to look at the common law, apply it with reason to changed circumstances, and that—as this happened in the past with regard to tobacco and some of our anti-fat suits—judges will begin making changes. I also go by the motto that Cardozo came out with for litigators. He said, "All found, however, in the end, that there was a principle in the legal armory, which when taken down from the wall where it was rusting, was capable of furnishing a weapon for the fight and hewing a path to justice."

That is basically what I do and what many of my colleagues do. We look out and we see a major wrong, whether that's smoking, whether that's obesity, or something else. We look to see not what is the single one ideal solution, because there is none, and I can not wave a magic wand and get Congress to pass a statute. Whichever one is going to be most effective, I take that weapon down from the wall and I hew it. And the bottom line is that despite all these naysayers, we keep winning. Thank you.

LINDA E. KELLY: If you have an additional point you want to add, and then we will throw it to the judges for questions.

JOSEPH M. PRICE: Just a couple points. Steve, I have nothing against anybody making a buck, and I am as for it as the next person. My point with regard to the money motivation is that when lawyers have a financial motivation in connection with a lawsuit, that shapes how they handle the lawsuit. It shapes the outcomes and that is not the optimal way to shape public policy. And just on this whole thing of obesity of kids: don't misunderstand me, Your Honors. We have a terrible problem here with obesity in this country. I don't think anybody up here would deny that. It is an epidemic.

JOHN F. BANZHAF: Well, what have you done about it? What have you, Joe Price, done about the problem of obesity?

JOSEPH M. PRICE: Well, what I have done about it is talked about the fact that there are ways to approach the obesity problem—legislative ways, administrative ways—and as I said before, we would not have things like the Child Nutrition Act or the Food Safety Bill if it had been left to the hands of litigation. Those were the results of the legislative process. So, it is not as though we are all ignoring this. Nobody is in favor of obesity.

What we are talking about here is, what is the best way to solve a very thorny problem; I think it's a legitimate basis to have a difference of opinion. As far as the best way to go about doing it: what you heard from me is exactly what I think you heard from Professor Zywicki. This isn't the most effective way to do it. Childhood obesity—you can mock personal respon-

sibility, but at some point, parents have to say to their three-year-olds, "No, you can't have a Happy Meal."

LINDA E. KELLY: Ted, any additional points to add briefly?

THEODORE H. FRANK: Certainly. I think Professor Banzhaf proves my point about Europe and dishwashers; the reason Europe is thinner than America is because, for one thing, they exercise more than we do. They have a pedestrian society; we have a pedestrian and biking society, and we have a driving society. New York City for example, which is less car oriented, has a much lower obesity rate. Also, Europe has much fewer dishwashers than we do.

Second, if you're taking this hypothetical example of the homeless family that's eating 40% of their meals at McDonald's, I suggest the solution there is that child services needs to get involved and take the kid away from the mother, who is spending her food budget on McDonald's instead of on housing. And if you think that is cruel and rights-violating, well how is it that the mother—the parent—is less responsible than McDonald's in that scenario? Third, not a single one of Professor Banzhaf's lawsuits on obesity has done anything for consumers.

It's certainly helped the lawyers, it's certainly helped some third parties, it's certainly helped some defense lawyers. He can call them victories, but they have not done anything for consumers. And Mr. Gardner suggests that he is against these bad lawsuits that do not do anything for consumers, so I ask him to put his money where his mouth is. I have a case right now in the District of New Jersey against Breyers.

It's a settlement where consumers get $0 and the attorneys get 100% of the proceeds. It's called *Ercoline v. Unilever*.[7]

And finally, Professor Banzhaf challenged us to come up with a solution. I think it is beyond the scope of this panel because we are talking about obesity litigation, and we were just asked to debate that issue. But I'll be happy to give a solution. In his lunch talk, he talked about the problem of externalities; people imposing costs upon others, that they are not realizing themselves. Right now, our greatest externality in the field of obesity is that people do not pay their own health costs.

So, when they overeat and when they have health problems because they overeat, those health costs are passed onto third parties because they are not realizing it themselves. If we change our economy so that people are bearing their own health expenses rather than third party insurers or the government, that would have a big difference on our obesity rates.

LINDA E. KELLY: I'm going to turn it over to Steve Gardner. Steve?

STEPHEN GARDNER: Two quickies. To respond to Joe—I agree with you Joe about the financial motivation of lawyers shaping the conditions of liti-

gation—but another area where I have seen abuse is defense lawyers who spend hours and hours arguing over why they should not have to produce relevant documents. I would pose the question: "When you're in a discovery fight, who's making money off that?" The guy who's going to bill on a contingency later, or the guy who's going to bill monthly and get paid for it? There are financial motivations, but it is not just on the side of plaintiffs' lawyers. And Todd, you said obesity does not kill you? I wrote that down, but seriously, did I get that right?

TODD J. ZYWICKI: I've said it was morbidity, not a mortality issue generally, yes.

STEPHEN GARDNER: Okay, well obesity does not kill you anymore than a bullet kills you. The bullet causes your internal organs to shut down and that's exactly what obesity does. It is not the immediate shutdown, but they both do the same thing. It's just that a bullet is a little quicker and more direct.

TODD J. ZYWICKI: Well, let me clarify that. Basically, the point is that obesity does not substantially shorten your lifespan in the way smoking does. That's what I meant by the distinction between morbidity and mortality; because of modern medicine, you can stay alive for a very long time even if you are highly overweight. And so, that was the distinction I was drawing. Smoking kills you earlier, obesity keeps you at a lower level of capacity; they are both obviously problems, they are just different problems, and the obesity problem is a much more expensive problem.

Let me just make a couple points then. First, I'm not going to say these cases are frivolous. As far as I can tell, there is no case in the world that is too frivolous to be brought and survive summary judgment somewhere. So, trying to figure out whether something is frivolous or not, is not a game that I think we can play anymore. What I do think we want to focus on is whether or not the benefits of a particular action exceed the cost. I think it is very clear here: if you just focus on the advertising component and you look at the fact that other countries have in fact tried this with no effect.

There will not be any effect from this and there will be a cost. The question about litigation is, can judges do that sort of cost–benefit analysis to figure out exactly what the benefit is going to be and what the cost is? I think a third question, that's a larger question: is that a cost?

LINDA E. KELLY: Well, we've put some very controversial thoughts on the table. Please join me in thanking our panelists.

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1 *See* Healthy, Hunger-Free Kids Act of 2010, Pub. L. No. 111-296, 124 Stat. 3183 (2010).

2 *See* FDA Food Safety Modernization Act, S. 510, 111th Cong. (2010).

3 *See Pelman v. McDonald's Corp.*, 237 F. Supp. 2d 512 (S.D.N.Y. 2003).

[4] SUPER SIZE ME (2004).

[5] *See* Von Koenig v. Snapple Beverage Corp., No. 2:09-cv-00606 FCD EFB, 2011 WL 43577 (E.D. Cal. Jan. 6, 2011) (granting defendant's motion to dismiss).

[6] *See* Holk v. Snapple Beverage Corp., No. 07-3018, 2010 WL 4065390 (D.N.J. Oct. 15, 2010) (granting plaintiff's motion to reopen class action suit).

[7] *See* Ercoline v. Unilever, No. 2:10-cv-01747 (SRC-MAS) (D.N.J. filed Apr. 6, 2010).

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EDITED TRANSCRIPTS

ASBESTOS BANKRUPTCY TRUSTS AND THEIR IMPACT ON THE TORT SYSTEM

The Honorable Mark Davidson, Lloyd Dixon, Nathan D. Finch, James L. Stengel
Moderator: Henry N. Butler

HENRY N. BUTLER: This session is on asbestos bankruptcy trust with the bigger policy question about their impact on the tort system, and we have a great lineup of folks to explain how this works.

Lloyd Dixon from the RAND Institute for Civil Justice is going to kick things off for us by sharing some empirical results on the use of bankruptcy trusts. And then Nathan Finch from Motley Rice, is going to talk about the plaintiff's perspective in some of these cases. He will be followed by James Stengel, who represents defendants in a lot of these cases.

Then we have Judge Mark Davidson who handles the asbestos MDL in Harris County, which is Houston. Mark and I met many years ago when he came to one of our programs at the University of Kansas, and he has served several terms on our judicial advisory board.

LLOYD DIXON: Good afternoon, a pleasure to be here today. I'm just going to give you a little background on the work we've been doing, and just a background on this issue in general. First let me start by saying the Institute for Civil Justice is located in Santa Monica, California. We're a nonprofit and we've been looking at asbestos issues for many years. Back in 1983, we were the first to examine and collect empirical information on asbestos claims. We did a series of studies in the 1990s looking at national administrative solutions to asbestos, and then a 2005 report updated the data on litigation dynamics and number of claimants.

Through 2002, we found that there were roughly 730,000 asbestos claimants, about 8,400 defendants, and about $50 billion had been spent on compensation. Well, much has changed in asbestos claiming since then. In different areas, there have been numerous actions in courts and legislatures that have reduced the number of unimpaired claims. There have been tort reforms in various states that have changed where filings occur.

Most importantly for what we're talking about today, many of the major defendants responsible for exposure have filed for bankruptcy and bankruptcy trusts—the trusts are set up for those insolvent firms, and are now paying substantial amounts. Well, what's the problem from the defendant's point of view, what's the problem? Well, the peripheral—what are called peripheral defendants—didn't pay much in the 1990s. The primary defendants went bankrupt, and payments by once peripheral defendants, increased.

Then the trust came online—the trust set up for those insolvent parties came online—and what the remaining defendants see, is that payments by the once peripheral defendants did not fall much. So what the defendants argue is that they're not receiving setoffs for trust payments, or they're concerned that they're not receiving enough setoffs for trust payments, and are concerned that insolvent parties are not being sent appropriate share of liability in states with acceptable liability. On the other hand, plaintiff's attorneys don't see these same problems. They assert that remaining defendants are receiving setoffs for trust payments.

They also point out that trusts pay only a fraction of the liability of the bankrupt firms. Trusts, because of assets—their assets aren't adequate to cover the full costs that were projected for their claims—only pay twenty to twenty-five percent of the liquidated value of a claim. Then the plaintiffs point out, when liability is joint and several, the remaining defendants appropriately pick-up the unpaid share of bankrupt defendants in states with joint and several liability. They also point out that it's really up to the defendants to establish the liability share of the bankrupt parties, not the plaintiffs. So that by way of background of what's setting up the issue here.

We have a study underway that's first trying to provide more information on what's going on with the bankruptcy trust, how many there are, how much they're paying, what their performance is. We're trying to provide information to understand better what that linkage between the trusts and the tort system is, and finally to collect some data to update what compensation is for asbestos victims, both from the trusts and from the defendants. We produced a first report last summer and it's available on our website, www.rand.org. Also, if you give me your card, I'd be happy to send people a copy.

It provides some overview of trust governance and procedures, and summary statistics, and has a detailed appendix on the operations of twenty-six of the largest trusts. This graph shows what's going on with the number of bankruptcies for asbestos. Bankruptcies where asbestos liability has been involved—that's the red line—and it shows that from the late 90s through 2002, 2003 there was a big jump in the number of bankruptcies involving some asbestos liability.

You can see from the yellow line: that's the number of asbestos bankruptcy trusts that have been set up. There's something on an average of a four-year lag between the date of bankruptcy and the date a trust is set up. You can see on this chart, between 2003 and 2007, the number of asbestos bankruptcy trusts jumped from roughly twenty to around fifty. So a big jump, and there are a good number of trusts in the pipeline. These trusts hold a substantial amount of assets. At the end of 2008, the largest trust held about $18 billion in total assets. Now here's just a little background on asbestos litigation, and where we are in that litigation.

This line shows estimates that were produced many years ago actually, but many people think that these numbers have held up over time. It shows

the number of excess mesothelioma deaths in the United States, and it peaked at roughly 3,000 in the first part of 2000, 2002, and 2003. It's starting to gradually taper off, but as you can see there's many years of asbestos litigation ahead because even in 2016 you have 20,000 excess deaths a year. These two lines show the estimates or data—the red line is the amount paid by the trusts, and you can see the rapid jump increase in the amount paid by the asbestos trust to asbestos claimants.

This is not just mesothelioma, this is all asbestos related injuries. It was $4 billion in 2008. Now, that may well come down because there are a lot of new trusts that came online, and they're going through a backlog of claims, so I wouldn't necessarily assume that that will stay up at $4 billion. It may drop. On the other hand, there are new trusts coming online that will keep or tend to push that number up. The yellow line is the estimates from our 2005 study on the total payouts for asbestos compensation, and it was over $8 billion in 2002.

That number may have come down as well because of the reduction of unimpaired claims, and so we're hoping to update that number in future work. Okay, so that's the second part of our study—that's just a brief overview of some work in the study that came out in the summer. The second part that we're working on now is to better understand the linkages between the torts, and the tort cases and the trusts. We're working with this kind of conceptual framework for the claiming process for plaintiffs with asbestos related injuries. So from a plaintiff's point of view, what are their sources of compensation?

They can approach firms prior to the filing of a case in what are often called matrix deals or administrative settlements, pre-suit settlements. They can file tort claims, and that's a familiar process of trial; if there's a plaintiff verdict it is some type of verdict molding that considers the setoffs or payments that have already been received. Or a plaintiff can submit a trust claim, and the trust uses different evaluation criteria than the tort system does, and there's payment or no payment on those claims.

One way that these two systems—no, I don't really think of them as separate systems—the trust and tort sources of compensation interact, is through the evidence that is shared or not shared in the claim evaluation process: the data that's submitted with trusts, or the evidence that's submitted in a trial. There's a lot of back and forth, and we'll hear about what evidence and what information is shared from a trust claim versus the information submitted in trial.

A second way that these different sources of compensation interact is through the setup process and the verdict. During the verdict molding, payments through the matrix deals or payments from the trusts are considered or not considered as it may be in the verdict molding stage of a case. And finally, post-verdict. A verdict defendant may or may not be able to file an indirect claim with the trust, and recover payments that the plaintiff would otherwise have been due from that trust. So what we're doing is

looking at six separate states and we're finding that situations are very different in the states. Here's an example of one example of what we're seeing in West Virginia.

West Virginia is a state where they seem to have a pretty full integration of the trust and the tort modes of compensation. In West Virginia, liability is joint and several, and because of that the verdict defendants pick up the liability of insolvent parties that's not paid by the trusts. In West Virginia, there are full setups for past trust payments, payments made before verdict, regardless of whether trusts are on the verdict sheet. So if there's any kind of trust payment, those trust payments are set off from the verdict amount. And then in West Virginia, the verdict defendants are assigned the rights to recover from the trusts, post-verdict.

According to the case management order in West Virginia, the plaintiffs are supposed to assist the defendants in making those recoveries, although what exactly that entails is not specified. But the point is that if there are any post-verdict trust recoveries, they go to the defendants, and as a result plaintiffs don't receive more with the trusts than without the trusts in West Virginia.

West Virginia seems to have addressed this issue about the interaction of the trust and the tort, and I would say the area most open is how are defendants really going to be able to recover from the trusts post-verdict? That's the issue there. Now in Pennsylvania it's very different. Pennsylvania is also a joint and several liability state. In Pennsylvania, insolvents do not appear on the verdict sheet, and there are no setoffs for parties not found liable. So in Pennsylvania, you can have a situation where if a plaintiff settles, receives a settlement from the trust prior to the verdict, the verdict amount is not reduced by the amount of that payment.

There you get an issue where there are not full setoffs. As a result, plaintiffs can recover more with the trust than without the trust, and solvent defendants may not be receiving credit for all trust payments. We're going through this for all the other four states; that's just a part of what we're reporting out for those two states. Just to summarize, these are the issues that we're seeing concerning how the trust and the torts interact. The first one is that defendants see limited ability to assign fault to insolvent parties in states with several liability. Defendants are concerned that they are not able to get the information they need to assign fault to the insolvent parties.

We also see that in some states, setoffs for pre-verdict trust payments are incomplete, and that's an issue in some states for these two sources of compensation. And then finally, I didn't go into it a great deal, but there's a large amount of uncertainty, and confusion, I would say, about the circumstances under which verdict defendant files indirect claims with the trusts. You'll talk to some trust officials, people who work at the trusts, and they'll say that the verdict extinguishes the right of a plaintiff to bring a direct claim.

And you'll talk to another trust official, and they'll say there's nothing in our trust distribution procedures that extinguishes the right of a plaintiff to bring a claim post-verdict. Because the plaintiff still has the right to bring that claim, the verdict defendant does not. So these are three different areas that we're focusing on that need to be addressed moving forward in this area.

HENRY N. BUTLER: Well, thank you Lloyd for setting up this issue. This is an interesting one, it's been nine years now since we had a program where Dickie Scruggs attended. One of the judges asked him a question about that—at that point I think we were probably dealing with our second or third wave of asbestos litigation. Someone asked him what he thought of that, and Dickie said, "Well, I don't have a dog in that hunt, but to me it appears that it's the never ending pursuit of a solvent bystander."

NATHAN D. FINCH: Right.

HENRY N. BUTLER: All right, we'll turn it over to Nate.

NATHAN D. FINCH: Good afternoon, may it please the courts. My name is Nate Finch. Some of you may see in your program that the speaker for this, the plaintiff's perspective, was supposed to be Elihu Iselbuch. He sends his regrets—he's had some recent health issues. He and I were law partners for the past ten years until I recently moved to Motley Rice. Motley Rice is a firm that is been known to do asbestos litigation from time to time, Caplin & Drysdale is a firm that is known to do asbestos bankruptcy litigation and the creation of a lot of these trusts from time to time.

I think that I'm probably one of the only people in the country that's both tried a case in front of a federal district court that lead to the creation of a bankruptcy trust, and tried an individual mesothelioma case. I didn't know until 4:00 p.m. Friday afternoon whether I would be here in front of you all, or in Virginia picking a jury in a mesothelioma trial. Just so I can get a little bit of a feel for my audience, I'm going to do some voir dire very briefly. How many of you have either tried an asbestos case or overseen a docket of asbestos cases, either as a judge or in the private practice? So it's a fairly small percentage of the audience.

I think there are some basics about asbestos litigation that might—and maybe Mr. Stengel might disagree with me, but probably not by much—be helpful here. Unlike in the food litigation we heard about earlier today, there is no personal responsibility defense in asbestos litigation. Every one of my clients who get sick and die, all they ever did was go to work. They worked around products that contained asbestos, and those products contained asbestos because companies back in the 60s and 70s continued to make choices to put asbestos in the products without warning them.

On the science and the medical side—outside the great state of Texas, and this includes in federal courts as well, pretty much any place you are—any nontrivial exposure to asbestos can cause mesothelioma, or it can be a substantial contributing factor in causing mesothelioma, and that's both under a *Daubert* standard,[1] or under state substantive law standards. The federal district courts that have—the federal MDL that hear all the asbestos cases—recently denied *Daubert* motions on that ground, and in front of juries, oftentimes it comes in the causation context.

If this is all the asbestos exposure that the client had from multiple companies, including bankrupt companies, this is the asbestos exposure from Union Carbide, then what caused mesothelioma? What was the last straw that broke the camel's back? In most places, not everywhere, but in most places most of the time, you get to a jury on a case like that.

Asbestos litigation is often different from other types of tort litigation in that there are legitimately ten to twenty to thirty companies that made asbestos, companies that emitted fibers that my clients and other people breathed, which caused or contributed to causing mesothelioma. My clients didn't do anything wrong, and the juries oftentimes get to decide complicated medical and factual questions about who got who, who caused this man's mesothelioma, this woman's mesothelioma, and who caused this exposure. But like most civil litigation, most cases get resolved short of trial.

A lot of asbestos cases get tried just by the sheer number of cases, and just by the fact that if a case starts out with twenty defendants and you settle with eighteen of them, you go to trial with the last three or four. So I have that big pie up there to sort of represent, graphically speaking, how asbestos cases typically get resolved; you have multiple defendants, you have multiple responsible parties.

Some of those responsible parties went into bankruptcy long ago. Some of those responsible parties went into bankruptcy a few years ago. Some of those responsible parties are still at the table, they're still solvent defendants. Some of the responsible parties start the trial and settle during the course of the trial. Some of the responsible parties are in the trial all the way through. And sometimes plaintiffs win, and sometimes defendants win if it goes all the way to a verdict. But generally speaking, the 524(g) trust system is a creation of Congress.[2]

It creates a special statute that allows companies to shed themselves of their asbestos responsibilities by putting an amount of money into a trust that's effectively equal to the equity value of the company, to pay the claims going forward for the next thirty or forty years, so that the company can reorganize and continue doing business and doesn't have to deal with asbestos liabilities or asbestos claims—the trust has to deal with that.

The first example of that, the biggest, well-known example of that was the Johns Manville Company.[3] After Manville went into and came out of bankruptcy, it had some problems with the stock market believing that it

had actually resolved its asbestos liability. Congress went and passed the statute in 1994 that effectively codified what the federal judges had done in the Manville case. The main point, from the plaintiff's perspective is the 524(g) trust system isn't designed to change anything about basic common law rules as they relate to discovery, or setoffs.

It's just in the way it's applied in asbestos litigation—it's by nature of the litigation it's somehow different than maybe other types of litigation you might be used to. As I was saying, the vast majority of cases are resolved before a verdict. The trust systems and the trust rules are not designed to change state law; either the state law relating to discovery or the state law relating to setoffs. I think there are some basic principles that apply to asbestos litigation just as they apply to all kinds of litigation. The first is if the plaintiff gets to choose who he or she sues. The plaintiff can sue all the potentially responsible parties, some of the potential responsible parties, or none of them.

Believe it or not, there are mesothelioma victims in the United States today who do not sue anybody because they decide they would rather spend what little time they have left on this planet doing something else, not very many, but there are some. The general rule is that bankrupt entities or companies that went into bankruptcy can't be sued. That's not just an asbestos rule, that's bankruptcy 101. You can't go out and sue Johns Manville anymore; you can't sue Owens Corning anymore. What has stepped into their shoes are these bankruptcy trusts. I don't think anybody would dispute that the facts that what a plaintiff did, what he worked with, where he worked, that is discoverable.

That is discoverable from the plaintiff himself. You can take the plaintiff's deposition. You can get a list of the places where the plaintiff worked. You can take depositions of the plaintiff's coworkers. You can do document discovery from the premises owners of the places that he worked. You can go out and hire expert witnesses, and I'll get to that in a little bit. In a case I just tried—we had some experience dealing with expert witnesses working for one of the defendants who researched the various types of asbestos containing materials that were on the ship that my client was on. There are lots of ways you can discover the evidence of what the plaintiff was exposed to.

Where I think the dispute or the rub is, and you'll hear about this more from Mr. Stengel, is this—can the defendants get access to the materials that the plaintiffs provide to the asbestos bankruptcy trusts in the context of settlement negotiations with those trusts. And at what stage in the proceedings is that material discoverable? And are the defendants entitled to know how much money the plaintiffs collect from the trust, and at what stage in the litigation?

I would argue that in general, the defendants already know, or have a pretty good idea of what plaintiffs either can recover or are likely to recover from asbestos bankruptcy trusts; and they can use that information both in

settlement negotiations with plaintiff's counsel and in trial. The final sort of basic principle is that—and generally speaking in litigation, not always but most of the time—settlements are confidential in that the terms and the amount of settlement are confidential, unless and until a judge needs to know it to mold a verdict or calculate a setoff. One thing I think is absolutely crystal clear is that a settlement agreement is not the same thing as tort liability.

The fact that someone can obtain money from either a solvent defendant or a bankruptcy trust by providing a certain set of documents or providing a release, doesn't mean that the defendant has agreed that its product was defective; or, that it caused the plaintiff's mesothelioma or any other asbestos related disease. It doesn't mean the plaintiff says that that particular entity is not liable. But generally speaking, almost every settlement agreement I've ever seen or negotiated says that the defendant does not accept or admit responsibility for whatever it is the lawsuit was about.

The settlement contract may well be a contractual liability. It may well create a liability in a financial sense. It may well create a liability that you should have to measure if you're trying to estimate the total cost of asbestos claims that some company might be faced with in the future; maybe a liability for 10K reporting purposes or insurance coverage purposes—but it's not a tort liability. At least in the federal system, and most states have similar rules. Evidence of settlements is not admissible in a trial to prove liability on a claim or lack thereof.

I don't know how many of you have tried cases where there are multiple defendants at the start of a case. If some of them settle out during the course of that trial, is the jury told that there was a settlement, and that defendant "X" paid "Y" amount of dollars to resolve its differences with the plaintiffs? I don't know of any court in the country where a jury is told that. There are evidence rules that prevent that. So what we're really talking about here, I think, and I guess Mr. Stengel can correct me if I'm wrong, is at what point is the bankruptcy trust submission discoverable, and how is it to be used in the context of solvent defendant litigation?

I would argue that a lot of the information that is sort of disputed or that the defendants would like to see more of, is already either available to them or, the type of information that they want to see discoverable, or want to get is exactly the type of information that they don't want to give plaintiffs or courts.

Bankruptcy trusts, particularly the newer ones—and those would be the vast majority of them, the ones that my old firm did a lot of litigation to create over the past ten years—create these trusts, and the corpus of the trust has assets with the duty to pay asbestos claims that would've belonged to Johns Manville, or Owens Corning, or some other company that is no longer available in the tort system because they use the bankruptcy code to resolve their asbestos problem.

These trusts have what's called trust distribution procedures, which are effectively standing settlement grids that say if you provide us with certain information, if you can prove that you worked at such and such a site, or if you can prove through an affidavit that a coworker provides that you worked with such and such a product, we'll make a standing settlement offer to you of "X" amount of dollars. The trusts publish those settlement offers; the standing offers in something called a trust distribution process which is available online—it's freely available.

The standards for receiving a settlement from a trust are very different from the standards that you would have to meet to prove up a case to get all the way to jury and judgment in the tort system. It may be similar to the standards that the predecessor company used to settle cases. Generally speaking, a lot of companies figured out that if a plaintiff could prove that he worked at a place where their product was probably used, then more likely than not the plaintiff would probably be able to put on admissible evidence to prove that he breathed the asbestos fibers from that product. But proving that you worked at a place is not nearly the same thing as proving up liability of that company.

Judge Davidson has a very famous order out of Texas and I'll let him describe it himself, which I call the "What's sauce for the goose is sauce for the gander" rule: effectively, the defendants have the same sort of burden that the plaintiffs do to show that other people are responsible. Any good defense lawyer worth his or her salt, I would argue, already knows what plaintiffs are likely to get from asbestos bankruptcy trusts—they know where the guy worked, they know what kind of jobs he had, they have thousands of depositions taken in these cases where they can look to see what products are at what place. So what this really boils down to is what I call, "who has to pay the cost of trying the empty chair."

I put an empty chair underneath the screen there because trying the empty chair is a time honored way that defense lawyers—and believe it or not I have done some defense work in my career—use to defend themselves. As one brief case study in this federal MDL case tried last month, I was on the losing side of a defense verdict. We started the case with four solvent defendants. Our client had done an affidavit of exposure to multiple companies for products, including many bankrupt companies.

The federal district court judge denied a *Daubert* motion based on each and every exposure. The defendants argued that the exposures from their products were trivial, the last little bit in the glass so to speak. We tried the case for two weeks, we settled with two of the defendants along the way, went to verdict with the last one. The solvent defendant we went to verdict with did a very good job with trying the empty chair—using the types of information which they say is not available, but actually was, and they got a defense verdict.

So I would just argue that, I don't see the interplay between the trusts and the solvent defendants as a big problem in asbestos legislation. 524(g)

trusts are not designed to, and do not really change the way state settlement, verdict setoff, or discovery rules work.

HENRY N. BUTLER: Thank you very much Nate. Jim, are you ready?

JAMES L. STENGEL: Sure. Good afternoon everybody, my name is Jim Stengel. The more astute of you reading Nate's materials may have inferred that I represent Union Carbide, which is true. I have past experience, though for most of the 90s I was outside council to Manville Trust. So I'm reasonably familiar with what the trusts do and how they operate. None of us so far have said why any of this matters to you. Many of you are probably in that fortunate position of having states where there is a dedicated asbestos bench, and you're not it, in which case you may think you're not at all worried about this. But I think that there are some broader policy implications for how we as a justice system work.

Some of what Lloyd talked about highlights that the money at stake here is staggering. To quote Senator Dirksen from Illinois, "A billion here, a billion there, eventually you're talking real money." This is a huge amount of money. We're not covering ourselves with glory in terms of how we process these claims through the system, the amount of transactions cost involved, and the fairness to the outcomes. From a solvent defendant perspective, there is an inherent unfairness in the way these cases are tried. Lloyd put up the slide, which is a preliminary assessment of West Virginia versus Pennsylvania.

What wasn't perhaps as clear as it should be, is that in West Virginia there is a case management order specifically addressing discovery and disclosure from the trusts. In West Virginia, the plaintiffs were required within a fairly short period of time to disclose all claims that have been made and all claims that will be made, so that the defendants are given a full disclosure of what trust claims will exist. It also includes penalties, such as loss of trial dates, if that information is not provided. It also deals with judgment molding or setoffs. As I think Nate would suggest, we don't get that information until late.

There are a couple of things that Nate described, and generally I agree with his description of the system—there are some areas where I think, frankly, red herrings were raised. I candidly don't care, until I have a judgment, what a plaintiff is getting from a trust. That's not the crux of what we as solvent defendants are looking for. To understand what we're looking for, I think I need to take you through what modern asbestos litigation and trust claims look like, at least in brief.

At the dawn of asbestos litigation, the claimants or plaintiffs were largely insulators. They worked directly with thermal insulation products containing asbestos. They knew they worked with Manville Asbestos, they knew they worked with Kaylo; they knew they were spraying limpet. There was not really a big question in their minds if they became ill, and

they were also the members of certain unions that did a very good job about informing their membership about where their health problems were coming from. But we are several generations removed from having a plaintiff population that is largely made of people who have a reason to know what they were exposed to and how is contributed to their illness.

One of the values of the plaintiff's bar gives to their clients is with today's claimants: if you're a seventy-eight year old gentleman with mesothelioma, you probably know where you worked, and you have some surmise as to who may be responsible there. But frankly, it's the plaintiff's bar who can help educate them as to what products they've been exposed to, and which of those products contain asbestos. There's a whole store of intellectual property at the plaintiff's bar level that's not immediately apparent, and those claimants may not know that they have a claim, say against Union Carbide, my client, until they actually talk to a plaintiff's lawyer.

Unless in that consultation, that educational process goes forward, that claimant may proceed in blissful ignorance that he's had that exposure. Which is why the timing here is very critical. Because the disconnect which we fight against, because we think these systems should, as in West Virginia act as an integrated system, we try today primarily in malignancy docket. The waves of the unimpaired claim which were the bane of the early 2000s, have largely passed away because of case management orders, legislation in some states, or the economics of the process.

We're dealing with a population of people who are seriously ill, largely mesothelioma, although there are lung cancers and other cancers in the mix. Because of that, in most jurisdictions we are going to trial from twelve months to as short as four months. We are going to trial right here, right now. That puts in a tremendous burden on the defendants to be able to gather the evidence we need to defend these cases. Now, Nate has said, and I'm from another context, "Well wait a minute, this isn't the plaintiff's problem, you guys do your job."

As you heard earlier, we get paid by the hour as opposed to on a contingent basis, so we should be happy out there, churning away doing discovery on all the trust exposures. The problem is that's ineffectual and its inefficient, and to the extent recollection has not been refreshed by a claimant's own lawyer, it will be very difficult for us to do that discovery in the time allowed. The corresponding development here within the last several weeks, a motion that has been filed to amend the standing order in Madison County, Illinois that will strip the duration of evidentiary depositions of the plaintiff to three hours in total, with an hour and a half available to the thirty to forty defendants in each case, and an hour and a half available to the plaintiff.

So we get put in a box where it's impossible for us to adequately discover the exposures. If we get a complaint obviously, we can go through the list, we see who is in the case, we know that, since it's disclosed by the plaintiff. There's typically no statute of limitations in the trust world, and

here I'm not accusing plaintiff's lawyers of misconduct. There are some notorious examples of bad conduct in the trust context.

But here they are probably doing their job by their ethical obligations—which if I'm the plaintiff's lawyer and I don't have an affirmative obligation to help produce information about trust predecessor exposures, and I can sit back and file that claim in a year and a half or two years, and get my money from the Manville trust and from Owens Corning and all the other dead entities, and I can go to trial against Union Carbide and other solvent defendants—I'm probably doing the right thing from that lawyer's and that claimant's perspective. Now, you're not doing the right thing when they're knowingly helping obscure the fact that there may be other claims.

What is it that we're really looking for? Nate talked a lot about settlement amounts, the fact that settlements don't prove liability—absolutely right. The trust claim process is very streamlined right now. I think other than *Celotex*,[4] all the trusts take e-filing. A very detailed proof of claim form will be filed with the trust, and with that claim form will go medical information and records. But from our perspective as a solvent defendant still in the tort system, what's critical is not the amount the trust may pay that person; if we have a verdict that will matter a great deal, but unless and until that happens, what we really care about are the assertions of exposure to somebody else's products or premises.

Because that's really the critical evidence, and from our perspective, those are essentially admissions by the plaintiff that they've been exposed to somebody else's asbestos. That matters a great deal because the level of exposure may vary; there are different kinds of asbestos with different capacities to cause disease. So if I find that I have a plaintiff in a case against me who claims that he was working around a Manville product, that's really a very critical piece of information that I have to have to fairly evaluate the case, and if I have to, try it under fair conditions.

That's really what we're looking for, and it's easy to do because they've made this submission; if the plaintiff's lawyers know they need to marshal the evidence they will do so. Now think about pre-Manville bankruptcy filing: no competent plaintiff's lawyer would have said, "I'm going to sue some of the responsible parties, but not all of them. I've got five or six defendants I don't really care about, so I'm going to leave them off the complaint, and just let things unfold." Malpractice? Clearly. In today's environment there's no need, there's no reason for them to put them in the complaint. What does that mean from a defendant's perspective?

It'll vary by jurisdiction, and it still matters in joint and several jurisdictions because we can prove intervening cause; we can disprove causation on the part of our clients because it may be there were massive exposures to Manville or some other bankrupt entities' asbestos. But if we were in joint and several liability, or any other jurisdiction where we are allocating fault, we don't get to put the bankrupts on a verdict for them because we say so.

We can't say, "Your honor, here's my list, I'd like all these entities there." We have to come forward with proof that there's an evidentiary basis to list those entities. As Judge Davidson has observed, we have to prove other exposures.

And we can use the trust information, the assertions of exposure, as a very efficient way to prove that exposure. It's not that we're creating something, or that we're distorting something—it is a submission to receive compensation made by or on behalf of a claimant that says, "I was exposed in the following ways to this asbestos." As we get to increasingly peripheral levels of defendants in this drama, it is harder and harder for those defendants to know what other exposures may have taken place.

So this is really critical, it matters a great deal. When you take the hyperbole out of the discussion, what defendants see is nothing more than a true return of what the tort system looked like, by reintegrating the trusts and their evidentiary processes into the tort system, so we have full transparency. Again, if we were looking for dollar amounts, that was our primary concern pre-verdict, if we wanted to go into court and say, "Your honor, we need prove no more about the Manville exposure because they've gotten paid by the trust." That's definitive. It's on the record. We get a directed verdict in essence on that causation. But that's not what we're looking for.

We just want the evidence that we can go to a jury, so we can prove the other thirty-five exposures, and that's not an outsized number given where we are—and we operate in a world with a level playing field, with fairness to all litigators. Thank you.

HENRY N. BUTLER: Mark Davidson.

JUDGE DAVIDSON: Judge to judges: let me tell you what a court of general jurisdiction needs to know about asbestos and then what you need to know about asbestos trusts in the rest of my time. You've already heard there are three kinds of asbestos disease. Asbestosis consists of an internal scarring of the lung. None of you will probably ever have to have one of those cases come to your court because for the most part, they're out of business nationwide—a few states will still pick up a few.

Cancer cases. There are a number of cancers that have an association with asbestos inhalation. It's not just lung cancer. I've seen esophageal cancer. I've seen testicular cancer allegedly associated, if not caused by asbestos. Finally, there's mesothelioma. Those are the ones that you may have seen in your courts. You may see advertisements on television by lawyers—a person that is diagnosed with mesothelioma typically has a year to live, and essentially over the course of the year, they suffocate to death. I have seen day-in-the-life films ad nauseum on mesothelioma cases, and I have nightmares from having seen those day-in-the-life films.

Okay, those are the three kinds of asbestos related diseases that you will see. By the way, Henry was gracious enough to say that I'm the MDL

asbestos judge for Harris County. Not true: I'm the asbestos judge for the State of Texas, all 254 counties; all 85,000 asbestos cases is what I live with—that's all I'm doing right now, it's one heck of a job. You heard that any exposure, however slight, can cause mesothelioma. Maybe that's true, maybe it's not.

If a person smoked thirty different packs, thirty different brands of cigarettes over their lifetime, and came down with lung cancer, say, and we knew that the lung cancer was caused by cigarette smoking, which one of the cigarette companies would be liable? The answer, for purposes of your state's courts, depend upon what state you're in. If you're from California you're probably familiar with the *Rutherford* case, which requires you to show frequency, proximity and duration of exposure to asbestos.[5] If you're from Maryland you're probably familiar with the *Lohrmann*[6] case. A number of states have adopted *Lohrmnan*, a number of states have adopted the *Rutherford* test. Texas had the loosest standard. Texas had adopted the "one fiber" test.

And my favorite case was the guy that worked in the auto parts department of a dealer—a car dealership in Marshall, Texas. Three buildings over, they did brake drum repairs, and the argument was that the asbestos that flowed out of the brake drum department through two different buildings, into the door of the parts department, caused mesothelioma. By the way, he also spent thirty years as an attic insulator blowing asbestos insulation, but they settled with those people; they didn't settle with the car dealer—that case went to trial. They poured him out, but he got a trial.

Texas had a one fiber theory that in June 8, 2007, our supreme court promulgated in the *Flores v. Borg-Warner*[7] case, which took Texas from the loosest state proving causation on asbestos disease, to by far the strictest state. In Texas, you must prove how much—that is, the quantum of asbestos fibers that the plaintiff was exposed to from each defendant. There's a recent case out of the Dallas court of appeals, which indicates you have to prove which defendants' asbestos started the tumor that led to the mesothelioma.

To turn Professor Posner's comments on its head, that's the case where science has to follow law, and not law following science—that one can't be done.

Now, let me get to asbestos trusts, and what you need to know. You had all these companies that filed a bankruptcy, and you had all these companies that set up asbestos trusts. You already heard that you can file an application with the bankruptcy trusts, and the plaintiff will get some money. First of all, there's no statute of limitations on an obligation of the plaintiff to file with a bankruptcy trust.

Some plaintiff's lawyers therefore don't file with a bankruptcy trust until after their litigation with solvent defendants is over. In states where you have dollar-for-dollar credit for trusts therefore attempt to prevent the solvent defendants from being able to get a credit from those bankruptcy

trusts. I heard for the first time today—did you say that in Pennsylvania—a defendant gets the benefit of post-litigation bankruptcy trust distributions. I was unfamiliar with that because in Texas, you do not because we have a finality of judgment rule.

If you have a final judgment against a bankrupt asbestos entity or a final settlement that ends everything, the defendant who paid money can't come back and seek compensation from an asbestos trust. The more interesting consequence of that is—I've heard from the Johns Manville director that his job is to spend all of the billions of dollars that is in the Johns Manville trust.

Now, they're paying to current applicants the amount of money that they've allocated; they will have enough money for it but at some point that curve will end, and there will be no more making claims against the Johns Manville trust, but there will still be money. And at that point, he says, he's going to go back and distribute money to everybody who's ever made a claim. How we're going to find those people in twenty or thirty years is an interesting question. How the defendants are going to be able to come make a claim against that—how are the plaintiff's lawyers going to find their clients?

How are you going to be able to find some of the plaintiff's lawyers, is a set of interesting questions that I don't want to have anything to do with; but those of you in a state that give a defendant who paid money in settlement or verdict, a right to seek a distribution from a plaintiff's bankruptcy trust distribution, are going to have an interesting time come fifteen, twenty, thirty or thirty-five years from now. I will no longer be a part of this litigation then. The issue however, has come to me several times is: whether a trial judge can order an asbestos plaintiff's lawyer and plaintiff to seek a bankruptcy trust application before a verdict.

I have ruled that under Texas law, our statutes do not authorize me to compel an asbestos plaintiff to make a pre-lawsuit or pre-verdict application with the bankruptcy trust. I'm familiar with maybe one state that has held otherwise, and I think that was as a result of a statute.

NATHAN D. FINCH: West Virginia, right?

JUDGE DAVIDSON: Pardon me?

NATHAN D. FINCH: I think that was West Virginia?

JUDGE DAVIDSON: Okay, whatever state it was, I believe this to be a legislative policy matter and that is better taken up with legislatures. I feel that judges should follow statutory law to the letter, and can sort of adjust the common law as I believe the appellate courts would do so. The one final thing you do, if you have an asbestos case in your court and there were

bankruptcy trusts filed—you have two implications. One relates to discovery, and one relates to admissibility.

Discovery. You've heard that the applications paid by a bankruptcy trust and the applications made to bankruptcy trusts are confidential unless there's a court order. If you're in a state that requires dollar-for-dollar credit, the defendant is probably entitled to the amount of money paid by the bankruptcy trust to the plaintiff, so that you can apply dollar for dollar credits.

If you're in a state that has either a proportionate responsibility, a comparative negligence standard, or better yet, a responsible third party standard, the statement made by a plaintiff in his application to the bankruptcy trust that he was exposed to the product of one of the bankrupts, in my opinion, is admissible to attempt to prove that exposure. In Texas, that's not enough because you have to prove a causative link, and I ruled that if the plaintiffs in Texas have to prove dose, the defendants have to prove dose as to alleged responsible third parties or settling parties under the doctrine of poultry equivalence.

Everybody know about the doctrine of poultry equivalence? What's good for the goose is good for the gander. One final thing, can a plaintiff deny causation as to a bankruptcy trust after they've alleged exposure from the entity behind the bankruptcy trust? Interesting question and I think I've ruled that they are not, but only because of the unique Texas *Borg-Warner* standard.

Do any of you have a so-called "innocent retailer statute" in your state other than Judge Moye, who I know does? Well, if you don't, then I'm not going to talk about it—Ohio did—but if you don't, then I'm not going to talk about it because it's unique to Texas.

HENRY N. BUTLER: Sure, so why don't we run back through the group and see if there are any comments, additions that people would like to add, Lloyd?

LLOYD DIXON: Oh, just in West Virginia, there is a requirement for the plaintiffs to declare what trust they could conceivably, or might be able to recover from, but not actually a file.

JUDGE DAVIDSON: Statutory or Rule based?

LLOYD DIXON: Case management order. And now in New York, my understanding is that there is a requirement to file with all trusts that you would be eligible for prior to verdict. However, when I've talked to plaintiff's attorneys that practice in New York, they don't really think that's enforceable and don't do it—is my understanding. Just clear that up.

HENRY N. BUTLER: Okay, Nate would you like to add here?

NATHAN D. FINCH: Yes, two points about the bankruptcy trust issue. The full transparency argument. A lot of bankruptcy trusts, particularly the newer ones for mesothelioma claims, all they say that there has to be meaningful and credible evidence of exposure; but that can be just a site list. That can be working at a site where somebody is; it could be the equivalent of the guy who was at the place where the auto parts were three buildings over. I would argue that doesn't prove causation, and while that may be admissible to prove something, it's not the same thing as the type of proof that would get you to a jury, or get you past a directed verdict motion on the defense's cross claim against another defendant.

If after a verdict, if you're in a joint and several state, the defendant takes a verdict and it can show that it's extinguished the liability not only of itself but also of the bankrupt companies to the plaintiff. Depending on whatever the state law is, defendants can go and make applications to these bankruptcy trusts. The bankruptcy trust system doesn't change underlying state law. In fact, there's a special provision in the bankruptcy trust distribution procedure to deal with exactly that issue. If a defendant extinguishes a liability of some other entity, i.e. an insolvent bankrupt trust, they step into the shoes of the plaintiff so to speak, and they can make an application to the trust.

So the argument that the trust system somehow tilts the playing field in favor of the plaintiffs is not what it was intended to do, and I don't think it does. I do think that there are lots of ways to get the discovery of the facts of exposure beyond getting the settlement communications. What my view of what the defendants want, is they want to tilt the field in their favor by saying, "Look we want evidence of your settlement communications with these bankruptcy trusts."

Well, how is that any different than Mr. Stengel who represents Union Carbide going to Georgia Pacific, which is another solvent defendant in asbestos litigation, and saying, "I want the evidence of what the plaintiff said to you to settle the case"? I was in trial last month, where two different solvent defendants settled out, two solvent defendants stayed in. The ones that stayed in went all the way to verdict. They didn't have any more right to go after the settlement communications between me or my co-council and the solvent defendants. What they really want is the ability to get that from the trusts, but not be able to have their own settlement negotiations or statements made to them by plaintiff's discoverer.

HENRY N. BUTLER: Jim, do you have anything to add?

JAMES L. STENGEL: Sure, a couple things. One on West Virginia: I think some of the limitations the case made were reflected in this concern about jurisdiction and power. The claimants there are all required to disclose the claims that they may have or have made; they aren't forced to file anything.

Post-verdict there's provision where claims have not been either made or they're still in process. They will be assigned to the defendants. So there is a mechanism, I think, that avoids some of the sort of overt coercion aspects. This is probably true in a broader basis about asbestos litigation.

The federal trust fund legislation[8] was a very good idea, and that would have made all this irrelevant, but it didn't pass. There are legislative proposals; the American Legislative Exchange Council has a fairly comprehensive proposal that's been out for a couple of years now.[9] It's been considered in some states, most notably West Virginia where it was very close to passage, which I think the skeptical among us may presume that's probably why there's a consented amendment[10] to CMO[11] in that state.

As to Nate's point, we're not looking for settlement information. I don't care about what somebody says to a trust officer about his or her claim, but I do care about the factual submission made, and we don't need that from co-defendants because they're in the case with us. We know by virtue of the complaint what the plaintiff thinks about their responsibility for this injury.

JUDGE DAVIDSON:I've tried hard to stay neutral in discussions at every forum I've ever been in between plaintiffs and defendants but I want to slightly disagree with you on one thing. In my view, an application made online by a plaintiff to a bankruptcy trust is not settlement discussions. It's an application for proceeds from a bankruptcy trust. In my experience, there's no negotiation: you file your application, often online, and often get money back, well, reasonably quickly.

In Texas where we not only allow, but we've been trying referral fees—there are lawyers who do heavy advertising, and will bring in plaintiffs, file the asbestos bankruptcy applications online, take forty percent of the money they get back within a month or two, and then refer a case to somebody that can actually try a case, that can actually take a deposition. And sometimes when they refer the case, they don't bother telling the plaintiff's lawyer that they've already skimmed $100,000 or $150,000 or whatever they get off the top.

My point in saying all this is, sometimes discovery is going to be necessary by the bankruptcy trusts. Something else that nobody has told you today and I've just remembered to tell you: do you know who's running the asbestos bankruptcy trusts set up by these bankrupt companies? For the most part, plaintiffs' lawyers are the board of directors; true?

NATHAN D. FINCH: No, not true. Independent trustees; the trustees are court approved by the federal bankruptcy court of federal district court judge. They typically are retired judges—a lot of them. There are plaintiff's lawyers that are on something called the Trust Advisory Committee. Which has the right to give comments to the trustees, but the trustees—for example the trustees of the Manville trust—none of them are plaintiff's

lawyers. The trustees of the USG trust include a former retired judge who used to have the asbestos docket in Cook County.

The trustees run the trust. Anything that the trustees do that is challenged by the plaintiff's lawyers in Trust Advisory Committee ultimately gets decided by the federal bankruptcy court judge, who oversees the trust. So it's sort of a myth that the plaintiff's lawyers run these trusts.

JUDGE DAVIDSON: A plaintiff lawyer in Dallas has told me he's on the board of trustees of three different trusts.

NATHAN D. FINCH: He's on the Trust Advisory Committee—he's not a trustee of any of them.

JUDGE DAVIDSON: I only know what he told me. In any event, it is not easy for defendants to get the applications or the amount of settlements, and yes, is does often require an order. Handling all the cases statewide in Texas, I sign those orders any time I'm asked and people have stopped fighting. Because it's something I think defendants legitimately need. But remember that under the Texas system because we require a dose, alleging that you were exposed to a product does not prove a dose. In other states where any exposure is enough—

NATHAN D. FINCH: Probably would.

JUDGE DAVIDSON:—and allegation of an exposure to a bankruptcy trust's product probably would get you to the jury.

NATHAN D. FINCH: Yes, absolutely, and it absolutely does. In the case I just tried in the federal district court, in the MDL, my causation expert was asked on cross by one of the defendants, "Isn't it true that one day of exposure to Unibestos," which is an amosite product that was on the ship, "contributed to causing his mesothelioma?" And my expert said, "Yes, of course it did." That was enough—I don't know exactly why the jury poured us out, but that may have had something to do with it.

JUDGE DAVIDSON:In any event, if any of you ever draw the black thing and have a bankruptcy case—sorry, asbestos case fall in your court, give me a call because asbestos litigation is my life. That tells you just how low my life has descended [inaudible]. No, it's challenging, it's rewarding. I have wonderful lawyers every week, and it's not the same old, same old. They continually challenge me with new questions that I never thought they would before. I mean it's a judge's dream to have no home foreclosures, no tax suits, no slip and falls, no car wrecks, and only have million dollar cases with million dollar lawyers. That's what I'm doing right now with my

docket. Having said that, I'm called by my colleges, a dust judge. So that's where it is.

HENRY N. BUTLER: Any other comments or reactions on the panel here? Okay, any questions out there?

JUDGE STEVE BRICK: Well, let me observe that I raised my hand as one of the few judges in the room who's tried a few asbestos cases to verdict or statement of decision judgment, and settled or watched settle several others. So here's my observation and question: I've observed that most of the cases that go away without a verdict do so after several days, sometimes weeks of *in limine* motion hearings, and several days and sometimes a week of jury selection.

I'd love to get a perspective of what's going on through national council behind the scenes to settle these cases, and why it takes swearing in the first witness or sometimes during jury selection to get the defendants to drop out, and is there anything that we as trial judges can do to move that process up two months?

JUDGE DAVIDSON:Let me answer your last question first. Is there anything you can do? No, I'm sorry. Mediation won't help, maybe a .357 magnum pointed at somebody's head might—but remember, I'm from Texas.

JAMES L. STENGEL: That's acceptable judicial procedure.

JUDGE DAVIDSON:Yeah, yeah we do it all the time. The answer to that last question there, I'm afraid to tell you, is no. Asbestos is a mature tort; for the most part the same group of experts go nationwide. To a large and growing extent, the same group of lawyers go nationwide, and without regard to what state they practice in, try cases nationwide. You know it's funny, I hear you must be from California?

JUDGE STEVE BRICK: Right.

JUDGE DAVIDSON: I heard judges from California say two weeks or more of motions *in limine*. I usually blow through motions *in limine* in Texas in about forty-five minutes, both sides.

JUDGE STEVE BRICK: 250 in one month.

JUDGE DAVIDSON:271 from the defendants, usually about 117 from the plaintiffs, but I've ruled on all of them before, and under the Texas system my rulings are binding on the trial judge. I don't try the case, I only do the motions *in limine*, the exhibits, the video deposition excerpts, and I've now convinced the lawyers that the ruling I made on their 271 defendants and

113 plaintiffs motions *in limine* last week are the same ones I'm going to make this month. If you could find one judge in California to make those rulings, and have it stick with all of your judges, I think you'd find that those two and three weeks in voir dire would whittle down to about fifteen or twenty minutes.

That is, which of those motions *in limine* is unique on this case? To me there's only two states, Texas and Delaware, that have a statewide system. But I know there are counties in California—San Francisco and Los Angeles come to mind; Philadelphia and Allegany County in Pittsburg, and of course Madison County, Illinois, have one judge that handles all pre-trial cases in asbestos cases. So the solution to three weeks of voir dire, which I'm sympathetic to, or motions *in limine*, is uniform rulings. If you do that, it won't happen again.

I'm also told by lawyers out in California that some of the motions *in limine* that you spend a day or two in pre-trial relate to motions for summary judgment that have already been ruled upon. If that's the case, then the trial judge should say, "No, my ruling on all summary judgments will carry forward to motions *in limine*," and I've been told that would trim two weeks from your three-week motion *in limine* experience. Just that one statement, I've ruled before, I'm going to rule the same way again. Now, I can't tell you for sure that's the case, but that's what I've been told. In terms of voir dire, it is a mature tort, but sometimes the amount paid depends upon who's on the jury.

It may not surprise you that there are some juries that are thought to skew plaintiff and some juries that are thought to skew defendant. Having said all that, there are some firms that refuse to discuss settlement until a week before trial on both sides of the docket, and there are some firms that encourage settlement discussions a month or two months after. Have I answered your question?

JUDGE STEVE BRICK: It won't hurt to hear the other discussions.

JUDGE DAVIDSON:Take it away.

JAMES L. STENGEL: Yes, from my perspective, Judge Brick, it's a quandary that we've always faced. Now, part of it is that we've developed this very specialized asbestos forum. People are lurching from trial to trial, and it's hard to get clients to attend to cases where they're literally there. The jury configuration does matter, because it will skew perceived value in a case pretty substantially, particularly if we're in San Francisco or Alameda—places where we generally expect the jury not to be in love with large chemical companies.

Sometimes you get a jury picked that's pretty good, and that will impact your value. The bigger problem, I think is just the multiplicity of parties and I would be interested to hear Nate's perspective on this. We'll be

in cases where we think we should be able to get out with either no payment or very low payment, and we're so far down the food chain—at least as the plaintiffs have configured the case—that they won't even talk to us.

We're sort of ahead in a case, but we're forced to spend time and money defending the case because you don't want to not prepare and then find yourself the last standing defendant. Some claimant's lawyers are obviously much better than others; there are some firms where we resolve our cases fairly early, I think on a full exchange of information, but we just know they'll talk to us, when they file. Other plaintiff's firms I know, that until we've got at least a couple jurors in the box, it's a waste of time to even try.

Now, there's another element here which I hesitate to disclose in front of this group as a defense lawyer, but back to who gets paid by the hour, I think there are defense lawyers who keep cases alive long after they should be. There's a lot of file churning that goes on in the asbestos world on the defense side. People have tried to squeeze it out of the system, but it's proved to be very intractable; clients give dire warnings to their outside council about what will happen if they discover it, and then little or nothing happens. One of the things that a judge can do is to make sure there isn't unnecessary delay.

The one thing that I don't know if it would work, I mean if you had the equivalent of Federal Rule 16 conferences—remember we're talking about malignancy cases—these are million dollar plus cases—they're serious cases; we've washed all the unimpaired cases out. The cases probably merit that kind of judicial attention. And I don't know, but I suspect if judges hauled litigants in fairly early and said, "What's this case about? What did this person do? What were the exposures?" and maybe require lead council to attend, or somebody with authority, you might clear at least some of your cases. But judges in Judge Davidson's position are probably better equipped to see what the pattern by firm is because I think there's a real personality issue there.

NATHAN D. FINCH: My perspective is basically in agreement with Judge Davidson and Jim Stengel, although people always refer to me as the War Department, not the State Department. I almost never get involved with settlement negotiations, but I give advice or comments to people who are doing that. Without getting into the specifics of anything, a lot of times I and people like me will move from case to case, and a lot of the defendants will have gone away earlier in the process on motions for summary judgment, or if there's settlements. Or if there'll be, I think Lloyd referred to them as matrix deals; sometimes there are defendants who will just settle up an entire docket just because they want to get rid of that docket with that particular law firm.

Oftentimes in the last week or two before trial, like the case I was supposed to be picking a jury in today. I didn't get put on that case until about

ten days ago, when we had settled out with most of the defendants. We were down to the last two, did the causation experts deposition, my client's expert got deposed, and really focused on, what's left, what do we have to do? There's an old saying—one of my mentors taught me long ago—that in trial work, particular jury trial work, you can have 100% of the facts on your side, 100 percent of the law on your side, Abe Lincoln as your lawyer and still have only about an 85% chance of winning.

That really hits home in jury trials because until you know exactly who's in the box, it can definitely swing the dynamics one way or another. There are good plaintiff jurisdictions and there are good defendant jurisdictions, but there are good defense juries in good plaintiff jurisdictions and there are sometimes good plaintiff juries in good defense jurisdictions. And until you go through the voir dire process, you may not know exactly how to value the case properly.

JUDGE DAVIDSON: There's one more thing you need to know, and all of you need to know this if you have an asbestos case: asbestos to me is the only form of litigation anywhere in America where trial counsel has no role in settlement discussions. Let me repeat that. There's national council, which is a different firm most of the time, then the defense firm representing the defendant, and there are settlement lawyers with the firm that are totally separate and are not in the courthouse when the trial lawyers are doing their thing.

Both sides are getting a report from their teams at the courthouse, but they negotiate with each other sometimes on one case, sometimes on teams of cases. I've literally seen it happen—you've probably seen it happen—where voir dire will be going on, and all of a sudden everybody's Blackberry will go off, and everybody will look at their Blackberry at the same time and say, "Golly, this case just settled."

Well, that's what they say in North Carolina; in Texas they say something else, but it's an obscene word, so I won't—in any event, they'll say, "Golly the case just settled," they'll approach the bench and discharge the jury. Did that happen in your cases?

JUDGE STEVE BRICK: It happened during jury selection, and in one case we had.

JUDGE DAVIDSON: Okay, but trust me when I tell you the trial lawyers didn't know what settlement discussions were, weren't told, and had no role in the process. I think that asbestos litigation is unique in this regard. You can hammer the lawyers in front of you all you want, and it will do no good because they have no role in settlement discussions.

NATHAN D. FINCH: Advisory, limited advisory capacity. I mean we report accurately what's going on from our perspective, we want to be as ac-

curate as possible, but do I engage in settlement negotiations? No, I try cases that's what I do.

HENRY N. BUTLER: Any more questions?

AUDIENCE MEMBER: Let me ask you: are you aware as you got away from the low-hanging fruit to the upper-tier fruit, that what happened in a lot of the trusts is the trusts actually own the reorganized entity? And what are you doing in that context in your numbers on the dollar that are flowing out, and on yours, on the setoff issues—because the structure on the companies that are not viable with big-dollar payments to supposed claimants, is that the trust earns all the equity, it is the reorganized entity which actually frequently gets the setoff rights?

[Inaudible]

MALE SPEAKER: The original one was done by Ness Motley.

NATHAN D. FINCH: Yes, I know that. The companies, the whole point of 524(g) is to separate the liabilities from the companies, and while initially the trusts owned the stock of the company, the Manville trust owned the stock of Johns Manville; like any trustee, they don't want to put all their eggs in one basket, so they typically try to sell off the companies at some point in the process. I think of the asbestos bankruptcy trusts, there's only a handful that actually own the majority of the stock of the reorganized company. I think the Owens Corning trust still owns a big chunk of Owens Corning. I can't remember what that state of Armstrong is.

I know in the USG case we basically did a deal with Warren Buffett where he bought the company back from us and put cash in there. So it's not always the case that the trust owns the company, but even if it does own the company, the entity that is potentially liable is not the company; unless the United States Supreme Court says that 524(g) is unconstitutional, the setoff goes to whatever that entity that held the liability.

The Owens Corning trust is Owens Corning for purposes of asbestos litigation, and whether you call it Owens Corning or the Owens Corning trust, I don't think really matters from his perspective. It's just which box made something, or which box his predecessor made something a long time ago that had asbestos that gives right to a cause of action against that entity. And because the entity is protected by a channeling injunction, you can't go after Owens Corning or the trust.

HENRY N. BUTLER: Let's declare victory on this one. Please join me in thanking the panelists.

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[1] *See* Daubert v. Merrell Dow Pharm., Inc., 509 U.S. 579 (1993).

[2] 11 U.S.C. § 524(g) (2005).

[3] *See In re* Johns-Manville Corp., 68 B.R. 618 (Bankr. S.D.N.Y. 1986).

[4] *See* Celotex Corp. v. Catrett, 477 U.S. 317 (1986).

[5] *See* Rutherford v. Owens-Illinois, Inc., 16 Cal.4th 953 (1997).

[6] *See* Lohrmann v. Pittsburgh Corning Corp., 782 F.2d 1156 (4th Cir. 1986).

[7] *See* Borg-Warner Corp. v. Flores, 232 S.W.3d 765 (2007).

[8] The Fairness in Asbestos Injury Resolution Act, S. 3274, 109th Cong. (2006).

[9] Asbestos Claims Transparency Act, §2(b), American Legislative Exchange Council (2007).

[10] Case Management Order at Paragraph 22, *In re* Asbestos Personal Injury Litigation, No. 03-C-9600 (W. Va. Mar. 3, 2010).

[11] Asbestos Litigation Case Management Order.

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Daniel F.C. Crowley, J.W. Verret, Todd J. Zywicki
Moderator: Geoffrey J. Lysaught

PAIGE V. BUTLER: Let me introduce our moderator for this session, Geoff Lysaught. He is from the group who moved with us from Northwestern, and he is in charge of the Searle Civil Justice Institute, our long-term research arm. So, I will turn it over to Geoff and let him introduce everybody.

GEOFFREY J. LYSAUGHT: Great, thank you Paige. Well, today's last session is sort of some emerging perspectives on the Dodd-Frank Wall Street Reform and Consumer Protection Act.[1] I suspect this is a topic that you will be hearing a lot about, not only over the course of today but over the course of the next several years. I think we are just beginning to scratch the surface on what will probably be a very deep pool of litigation activities that will ultimately make their way in front of you. So, we have a great panel here.

One of the members of the panel will be here shortly; that's Dan Crowley. He is a partner at K&L Gates, but we also have with us, two distinguished gentlemen: an Assistant Professor of Law, J.W. Verret, from George Mason University and Professor Todd Zywicki who you are also already familiar with. He promised that he will not encourage any more Jerry Springer moments on any future panels. So, J.W., take it over.

J.W. VERRET: Well, thank you and thank you, Henry, Paige, Geoff, Karen, all the rest of the LEC, and everyone else for putting this great event together and for allowing me to join you here. I am a connoisseur of political cartoons. Let me describe two of my favorites to you; although, I can't surely do them justice. One of them shows a road up on a cliff that has a very small shoulder and a sharp drop on a cliff, and Barney Frank and Chris Dodd are in a road construction truck, and they're going along putting down fences and each post alternatively says, "Dodd," "Frank," "Dodd," "Frank."

One of them says to the other one, "Thank goodness that we're able to put this fence up to keep investors from going off the cliff in the future," and Barney says, "Well, hey, what about the fencing in between the post? Shouldn't we put that up?" And Chris says, "No, no, no, don't worry the regulators and the lobbyists are going to come along in the next few years and put those up for us. So, it should be okay."

There's another one where it shows one scene of a Capitol Hill security guard all in a panic saying, "There's an earthquake! There's an earthquake!" And the next scene shows a hallway with a giant stack of papers on the floor, and in front of it is an intern that's fallen on the floor in front of the three-foot-tall stack of papers. And Barney Frank is leaning out of his office and he says, "Hey, haven't I told you don't run in the hall while you're carrying the Dodd-Frank bill because it's going to cause a ruckus?"

So, a very big bill, a very expansive set of new rules to govern financial regulation. In fact, the specific set of rules I'm going to talk about, the corporate governance area, in its own right would have been sweeping, right? But it was housed in such a huge omnibus bill, such a death star of a bill, that it largely went unnoticed as all the other provisions went through. So, I'll focus specifically on the securities law and corporate governance aspects and mention briefly as one area that I think is particularly controversial in which I have specialized.

First, one of the requirements that Dodd-Frank includes will be to require a so-called "say on pay" advisory vote at publicly traded companies. Now, this will mean that between every one and three years, shareholders will get to vote on the pay packages of the companies in which they own investments. The vote will be advisory. It will not be a binding vote, but a very specific set of executive compensation policies, including the triggers for bonuses, all that will need to be voted on by the shareholders. The United Kingdom has had say on pay for quite a while. It's been a fairly sleepy affair over in the U.K., but the type of shareholders the U.K. has is very different from the United States. The United States has a set of very politically powerful shareholders in union pension funds and in state government pension funds; the corporate defense community will say they are the boogey man and they are going to abuse their powers.

They will say, "No, we're solely interested in maximizing shareholder wealth. It's not about political conflicts for us." Though, they are run either by union managers or state-elected officials. I think the truth is probably somewhere in the middle, and certainly, the political conflicts of these institutions are going to inform their votes and inform the bargaining that they use these votes to accomplish. It will also require a say on pay vote on golden parachutes. These are change-of-control bonuses that really facilitate the market for corporate control. Firms will have to put those say on pay, those golden parachutes to an advisory vote as well.

The big kahuna here is proxy access. This is the most heavily argued over, most fought over corporate governance provision in Dodd-Frank. Now, this will give the shareholders who have at least 3% of the shares, either individually or as a group, and who have held those shares for three years, the right to put nominees on the corporate ballot that the company pays for. This will make it a lot easier to institute proxy fights for a minority representation on the board for up to a quarter of the board directors.

So, that means the AFL-CIO and the California pension fund, who by the way, were two of the most vocal proponents of this provision, will be able to put AFL-CIO and California pension fund representatives on the board of directors of publicly traded companies. This is a very contentious issue that the Chamber of Commerce and the Business Roundtable have filed suit under various provisions, including a First Amendment challenge, and the litigation is ongoing. The D.C. Circuit is looking into this. The SEC had a rule implementing proxy access, but they stayed implementation of the rule while litigation is ongoing.

So, we'll see what happens with proxy access, but it is probably the most controversial and the provision I think most likely to be litigated over and over in the future at particular contests. So, we will keep an eye on that and after finishing this overview, I want to go back to proxy access for just a moment to talk about some of the work I have done in that area.

Compensation committees: each board of directors has a compensation committee that sets the compensation for the executives. There's an added disclosure required. There's a new requirement that the compensation committee be independent, and, also, some new provisions requiring disclosure of the consultants that work for these committees and the types of arrangements that these consultants have with the compensation committees of the board. Clawbacks are also going to be required.

So now, as a result of Sarbanes-Oxley[2] we have clawbacks in certain instances. In other words, if an executive gets a bonus, as a result of some accounting irregularities that later required a restatement, and that executive did not really deserve that bonus, and they are the reason why the accounting was wrong in the first place, it does not seem fair to give them a bonus.

Sarbanes-Oxley in 2003 already gave us some new laws requiring they pay that bonus back, or the company claw that bonus back. Well, the new Dodd-Frank provision extends clawbacks much more widely to any executive who gets a bonus, who did not participate in the accounting irregularities at all, but they just got a bonus because some earnings target was hit, that was not really hit, but was the result of some accounting irregularities. Even if the executive did not participate in the accounting problems, in the wrongdoing that led to the misstatement, and did not fail to oversee people—in other words, did nothing wrong—they will still get their bonus clawed back.

That will make it difficult to have people feel secure in their bonuses. So, for three years after they get a bonus they will have to worry, "Maybe my bonus will get clawed back sometime in the future for something I had nothing to do with." So, that's a really controversial provision. There are some enhanced disclosures about executive compensation, particularly about internal pay equity.

Companies are going to have to show ratios of the highest paid workers to the average paid worker. This is going to be particularly difficult to implement for companies that have a lot of international employees, all

around the world, for whom a lot of compensation is not direct cash compensation, but is instead, indirect compensation; this is also particularly difficult for a lot of outside contractors and part-time employees. There will also be enhanced disclosure of employee and director hedging, whether or not a company allows an employee to hedge positions in the firm.

We want employees to hold—particularly high level executives—to hold options in a company so that they get a piece of the upside if the company does well. But, of course, there are lots of different financial instruments you can use to hedge positions that you take. So, the SEC under Dodd-Frank is going to implement new rules to enhance disclosure about employee hedging. That is going to be tricky, of course, because even if you just buy treasury bonds, that in some way hedges interest rate risk at a particular company. So, the SEC will have to think about what is a hedge and what is not a hedge.

Those are two types of animals that are very similar but have slightly different feathers. Also, new disclosure will be required about separation of the chairman and the CEO positions. Now, this is a bugaboo that has been coming up for the last fifteen or twenty years. And finally, now the rule is, rather than mandating separation of CEO and the chairman position, Dodd-Frank requires disclosure about it. Now, there's no evidence to suggest whatsoever that there's a change in earnings between companies that have the same CEO and chairman and those that have a separate CEO and chairman; but there will be disclosure about it nevertheless.

So, with respect to proxy access, I want to talk a little bit about where I see the future of proxy access going. The litigation that the Chamber of Commerce will bring against proxy access is uncertain. I am not sure what will happen or not, but I do know that even if the Chamber wins the SEC does have the authority to issue a proxy access rule even if it does not have the authority to issue the one it did. So, we'll see on proxy access. It's just a matter of what form it will take; and the next step that boards of directors will take is to defend against proxy access.

In instances where they feel like the conflicts are overwhelming, and the conflicts are going to damage the value of the company, and they are going to hurt other shareholders, boards of directors are going to feel obligated to defend against a hostile nomination. There are a couple mechanisms that could be used and a couple mechanisms that I've invented to defend against hostile proxy fights. And so, I'll just talk about a few of them.

Number one, you can put into the bylaws of your company, qualifications for service on the board. The SEC gets to say who goes on your proxy statement or not, but state law still controls qualifications for service on the board. So, even if the SEC makes you put someone on the corporate proxy, and even if they win the election, if they do not meet the standards for qualification for service on the board, then they do not get to sit on the board; and I think that it's all in the how you draft those qualifications.

Members of the board of directors are very interested in getting directors and officers insurance against personal liability under the securities law and state and corporate law. They are also very interested in being indemnified by the board. I see no reason why the board of directors should feel obligated to indemnify or insure members of the board whose election it did not support. Boards work by committee, issues are delegated to committee, and the boards get to decide who serves on the committee. I see no reason, if you feel like a conflicted director is going to damage your firm, why you should not keep those conflicted directors off the key committees and why you should not delegate more decision making to those committees.

And finally, there are a number of other types of mechanisms that we have already seen in a hostile takeover context used from time to time: poison pills, proxy puts, mechanisms that simply limit the ability of a challenger to make a hostile tender offer. Those mechanisms can also be adapted, I think, to proxy fights. And so, I think the design is useful. I think under state law, most of these will be upheld, and I think that the proponents of proxy access are going to be hopping mad about these provisions; at least if their response to my papers about it is any indication, they are already hopping mad.

They do not like me very much and have issued corporate governance alerts to all the union pension funds in the country. So, I see the potential for litigation about this in both federal and state courts, not just the SEC's right to issue proxy access, but all the variety of defenses the boys are going to come up with including, hopefully, a few of the ones that I have invented. So, I see for all the members of the judiciary here, I think there will be plenty of other things for you to do.

Members of the board, I think there will be plenty of things for you to implement in response to that particular provision of Dodd-Frank, which I think is the most far reaching corporate governance provision of Dodd-Frank. I'll turn it over now to my colleague.

GEOFFREY J. LYSAUGHT: We are going to go to Dan next.

DANIEL F.C. CROWLEY: The Dodd-Frank Act embodies a fundamental shift in policies with respect to capital markets generally. And I always like to use pictures wherever possible. This is a picture of the fall of the Berlin Wall, which really symbolizes the era of free market capitalism that came in the post-Reagan years.

In the Emergency Economic Stabilization Act of 2008,[3] TARP, and all of the other policy responses to the credit crisis, we have essentially entered an era of government-managed capitalism, and that's true globally. I am going quickly give you some context, at least from my perspective, on implementation of Dodd-Frank; from the standpoint of a financial services lobbyist that spends most of his time up on Capitol Hill. This is the con-

text. If you recall in October of 2008, most of the discussion was about systemic risk. In my opinion, that is a red herring.

When I was in business school, it was called systematic risk and it was the kind of thing you tried to diversify away from, but now, the government, in its infinite wisdom, has concluded that it can manage systemic risk, and that really is the overarching focus of Dodd-Frank. There were concerns about gaps and redundancies. Our financial services laws have evolved since the 1860s with the National Bank Act piecemeal. In the '20s and '30s we had enactment of the '33 Securities Act, the '34 Exchange Act, the 1940 Investment Company Act, and so forth, and so on, all were discrete efforts to deal with financial services.

This is the first time in historic that Congress has taken a look at all of it at the same time and revisited it, simultaneously, with an eye toward filling the gaps. Remember Bernie Madoff and the fact that the SEC missed it, FINRA missed it, and there were also redundancies or overlapping jurisdictions, particularly in the banking agencies. So, the orientation and the policy response, predictably, was comprehensive legislation. The headlines say it all—July 21, 2010 ushered in the era of Dodd-Frank. And it set in motion an unprecedented amount of rulemaking. We have never seen anything like this. The last major financial services law before Dodd-Frank was Sarbanes-Oxley a decade ago.

That had, I'm trying to recall, fifteen to twenty rulemakings. Dodd-Frank has 315 rulemakings by our count, and, by the way, this is just the substantive rulemaking. Other law firms count it differently. These are both the mandatory and permissive substantive rulemaking and there are another 145 study requirements. Notice that 140 of these rulemakings are in the area of OTC derivatives and swaps. Title VII creates a whole new regulatory regime for swaps, largely in response to the credit default swaps that were the fundamental issue at AIG.

With respect to timeframe, some of it had to be done immediately. The Federal Reserve, for example, had to issue interim final regulations—if that is not an oxymoron—within ninety days of enactment, with no due process, and no notice or opportunity to comment. The Fed, to its credit, did reach out conscientiously to members of the regulated community and essentially created their own due process. But that was a very interesting provision in which the independent appraisers managed to get a requirement that the Fed promulgate rules on customary and reasonable appraisal fees without regard to whatever appraisal management companies might now be charging.

So, Congress carved out 70% of the industry and mandated that the Fed establish customary and reasonable fees with respect to what is essentially an archaic business model—but that's what you get in Dodd-Frank across the board. One of my favorite expressions is that a camel is a horse designed by Congress. There is no better example than Dodd-Frank. And the judiciary, frankly, is going to be busy for years with this one.

This is one of the most fundamental aspects of Dodd-Frank that, in my opinion, has not received proper attention, which is the creation of a super regulator in the form of a Financial Stability Oversight Council (FSOC). The Secretary of the Treasury is depicted here as King Arthur and the FSOC as the Knights of the Roundtable for the very simple reason that the FSOC, as it's now being called, requires two-thirds vote to do anything, and one of those votes has to be the Secretary of the Treasury. So now, de facto, he is the most influential regulator in Washington with respect to financial services, and I have yet to see a single press story making that point.

This is a depiction of what I believe is in the offering in terms of the implementation of Dodd-Frank. There are so many ambiguous provisions or provisions left to the discretion of the regulators, that everyone who is represented by lobbyists is going to be engaged in many cases in a zero-sum game in terms of how the regulations are written. These are the key reform issues. This roughly tracks Dodd-Frank—there are about fourteen, I guess sixteen titles. These are basically the issues by title in Dodd-Frank.

Some of the notable ones, in addition to OTC derivatives, which is my favorite, far and away of the whole bill, and we have already heard a very good presentation on the executive compensation and corporate governance provisions. Municipal securities is another area that an entirely new regulatory regime is being created for advisors to municipal securities and to municipalities who issue securities because of what happened in Jefferson County, Alabama. Insurance is sort of the sleeper issue here. Congress could not achieve consensus on what to do about federal regulation of insurance.

So, they have laid a number of pieces of the foundation for federal regulation including creation of an office of insurance at the Treasury, which has subpoena authority but no real mission other than to gather information. That is clearly foundation laying for rethinking insurance going forward. Preemption—we could spend an hour talking about the preemption issue alone. I won't. Let me move on to what I believe are the implications of Dodd-Frank so far.

We historically, have had two competing schools of regulatory thought with respect to the financial markets: the capital markets approach, which is based on transparency and allowing investors to make informed investment decisions for the efficient allocation of capital, on the one hand, versus the banking model of safety and soundness, on the other hand. I would suggest to you that what we have in Dodd-Frank is the triumph of safety and soundness over the capital markets model. That is most obviously reflected in the FSOC where the SEC and the CFTC are now outnumbered by banking regulators in a sort of co-equal body.

The focus of policy in the new era is on harnessing the wealth that markets create, as opposed to the focus in the free market system, which is creation of individual wealth, and the implications for that are littered throughout Dodd-Frank. The focus on executive compensation is one, em-

powering the Fed to basically engage in utility rate making with respect to debit card interchange fees, without consideration of the cost to the plant and equipment, which is probably unconstitutional, and at least very controversial. Customary and reasonable appraisal fees I have already mentioned.

Concentration limits for financial institutions to make sure that nobody gets too big—arbitrarily, by the way—that is 10% of the size of all financial deposits. And then, consolidated supervision by the Federal Reserve. The idea here, is that once the FSOC designates an institution as large enough and integrated enough to warrant supervision by the Federal Reserve as essentially a holding company; it means that the Fed will now have authority to police all of your activities, even in subsidiaries that formerly had been regulated by, say, the SEC.

Take for example, an insurance company that has a mutual fund subsidiary. If it is big enough to be designated for supervision by the Fed, the Fed will now have the ability to supervise the mutual funds.

I'll go through very quickly the implications of the election. Not a single House Republican voted for Dodd-Frank, and only three Republicans in the Senate. And of course, we had an election which means that now Republicans will have the oversight gavel. There really is no real legislative history on Dodd-Frank. There is no committee report on Dodd-Frank.

There is a Senate Banking Committee report on an earlier bill, but nothing authoritative to help with the Congressional intent on any of these ambiguous provisions. What that suggests is that the Congressional intent is essentially whatever the person holding the gavel of the oversight committee says it is. So, we are going to most likely have Spencer Bachus; Edward Royce is challenging him. We will find out this week who chairs the committee. The subcommittee chairs are all going to have considerable influence over the regulators during implementation. Scott Garrett, probably the most important, as Paul Kanjorski's successor at the Capital Market Subcommittee.

Jeb Hensarling will not only chair the Financial Institutions Subcommittee, but he's already been elected House Republican Conference Chairman: the fourth highest ranking position in House. And, of course, he was also on the Congressional Oversight Panel with Elizabeth Warren, who chaired it, and is now at the Treasury helping to implement CFPB; Jeb has told me that Tuesdays are reserved for CFPB oversight. In addition, the oversight committee, will have Darrell Issa as Chairman. He has asked each of his subcommittee chairs to hold no fewer than two hearings a week. If you do the math in the next year, that is about 240 hearings that the Administration can look forward to.

On the Senate side, Tim Johnson will most likely be Senate Banking Committee Chairman; Richard Shelby will be a strong ranking member who also very strongly opposed Dodd-Frank. Here are the takeaways: I think, looking at it at a macro level, Dodd-Frank really is a function of the

ratchet effect of government involvement in business for all financial services participants. Government is now effectively a partner, and I think a necessary facet on every strategic business plan going forward. The fundamental aspect of GOP oversight is going to be a requirement that all regulations have a cost–benefit analysis, which is not required in any way by Dodd-Frank.

And then you will see, I think, more nationalism and increasing protectionism. We are already seeing that in the fight over currency exchange rates. In Europe, they have basically said, "If you want to run a hedge fund in Europe, you have to have a European presence if you want to sell to European customers." Sovereign wealth funds—you can think through the implications of the politicized markets when governments have their own money at stake. I am giving you this as a resource.

The firm, K&L Gates, is a global financial services firm, and what we have done with any of the issues that have come up through Dodd-Frank, is to have our experts prepare alerts that are publically available on our blog, which is www.globalfinancialmarketwatch.com. I hope that has been helpful.

GEOFFREY J. LYSAUGHT: Todd?

TODD J. ZYWICKI: I am going to primarily talk about the Consumer Financial Protection Bureau (CFPB) and the Durbin Amendment, which becomes part of that. And my story is that there was a lost opportunity to do something useful, and some of the things I'm going to talk about today I am also going to talk about at a more conceptual level tomorrow.

I think there is a real need to improve our consumer protections system when it comes to dealing with consumer credit. I think that simplicity is a real need; streamlining and one integrated consumer protection regulator, I think was a good goal. Certainly, one mortgage disclosure form was a good goal, and it would be great if the CFPB going into effect would do that, but unfortunately, I do not think it is. I think that what they have created is a monster that's going to be contrary to the goals that we would have liked to have seen, which would be more simplicity, more competition and the like, for consumers.

So, I'm going to talk about what I see as the three major defects in the CFPB, which I hope will eventually be rectified, because I think they are laying the inevitable foundation for a train wreck down the road. The first one is the structure of the CFPB. Now, if you had sat down and tried to create a model of a bureaucratic monster that would be subject to every bureaucratic pathology that scholars and regulators have identified over the past thirty years, it would look exactly like the CFPB does.

It is as if the people who created this went to sleep during the Nixon Administration and woke up and basically kept doing the exact same thing we were doing thirty-five or forty years ago, without any recognition of

what we know about regulation and the regulatory process that we knew then. The way the CFPB works is it creates a one person director, appointed for a fixed five-year term, removable only for cause. The provisions affecting the deputy director are probably unconstitutional, at least as it will play out under the PCAOB Act. But it creates a one person director, and so, it basically is driven by whatever that one particular person decides to do.

It is housed inside the Federal Reserve, but is basically independent of the Federal Reserve. So, what they have done, is they have created an independent agency inside of another independent agency, which is relatively unprecedented, I think. It is very difficult to get oversight—it has a guaranteed budget. Basically, every year, the director of the Bureau simply sends a budget demand to the Federal Reserve Board, and the Federal Reserve Board must grant the budget demand as long as it is no more than 12% of the revenues of the Federal Reserve—no questions asked. It has a narrowly-focused parochial mission just on consumer protection related factors.

Finally, any regulation or decisions made by the CFPB can only be overruled or prevented by a two-thirds vote of the Regulator Council, and only if a decision of the CFPB would threaten the safety and soundness of the American financial system or the stability of the financial system. Two-thirds is a very high standard. Now, what they have done is created a perfect storm of conditions for the worst of bureaucratic pathologies as we have come to understand—they will have almost a tunnel vision focus on the Agency's regulatory mission at the expense of all other missions. Excessive risk aversion will be likely, in terms of the impact it will have on dampening innovation and that sort of thing. And there is a real threat here of agency overreach to try to expand into other worlds, in addition to a real threat of capture by interested parties, such as big banks and the like.

What all that adds up to, is the big problem that this agency simply is not set up to do the most important thing that should be done by a consumer protection bureau, which is they should be able to balance the trade offs involved in consumer protection; which is balancing consumer protection goals, against other goals such as access to credit, competition in markets, and price for consumers.

I'll give you an example: think about professional licensing under lawyers or doctors. What you can think about there is, yes, higher standards for becoming a lawyer might protect consumers. The evidence is not clear. At least it does not seem to be, but you can imagine how higher licensing could protect consumers, right? But at the same time, if you have higher licensing requirements, you have a lower supply of lawyers, and you increase the price for lawyers. There is some trade off there between consumers getting a lower price and more choice in lawyers, versus perhaps, consumer protection of licensing.

That is riddled throughout here, but the Agency is not set up in order to do that when it comes to, say, mortgage brokers, what kind of mortgages

will be sold, and that sort of thing. Now, this especially jumps out at me because as I said earlier today, I worked at the Federal Trade Commission. The Federal Trade Commission, up until now, has been the sort of main consumer protection agency of the Federal Government. The Federal Trade Commission is set up completely differently from how this is set up and it is set up specifically to process these sorts of trade offs. So, the FTC is set up with a five member bipartisan commission, so it brings different perspectives on these sorts of things.

It has an institutional balance internally between the Bureau of Competition, the Bureau of Consumer Protection, and the Bureau of Economics. And so, basically what you get is a sort of rivalry within the Agency at the Commission. Colloquially, if you were to take an alumnus of the Bureau of Consumer Protection and make them an independent agency with the authority to sue anybody they want to, pass any regulation they want to, impose fines, very high fines, do you think that would be a good idea? I think almost anybody who has worked at the FTC would think you had lost your mind. If the Consumer Protection Bureau could just run around suing anybody and passing regulations, soon, they would be out of control. And so, it works better with a five member bipartisan commission in line. But that is exactly what they have done here. They have created that farcical consumer protection agency that I described.

A second problem is the vagueness of a lot of these regulations to be filled in later. "Abusive" is a good example. The regulation gives the CFPB the power to go after unfair, deceptive, and abusive problems. "Unfair and deceptive," although they seem vaguely defined, actually are just taken from the Federal Trade Commission definitions, and they have gotten cabined over time. Abusive is much more problematic; it is not clear what abusive means. As Dan noted, there is no legislative issue. Nobody has any idea where the concept of abusive came from. It just springs into the bill. If you look at the language, it is kind of hard to tell, but what it seems to suggest is that it would now give the government the power—obviously it means something other than unfair and deceptive, right? So, it is not just a matter of disclosure and making sure you are not defrauding people.

What abusive seems to mean in the regulation is some substantive level of understanding by consumers. That consumers actually substantively understand things, not just that you have disclosed it, but give them an opportunity to shop around, and that sort of thing. That is a real sea change in the way we think about consumer protection, number one. And number two, what it seems to suggest is that there are certain populations—for instance, who we should think of as being too stupid to be able to protect themselves—and these guys would get some sort of special protections under this, which of course means that these people will see less access to credit. It again, is not clear who would fit within that category.

Third, is the problem of preemption and arbitration, and Dan alluded to this. The idea here, is that it used to be that the federal banking regula-

tors could preempt state laws that they thought threatened the safety and soundness of the banking system. This law, Dodd-Frank and the CFPB, makes it much more difficult to preempt laws of consumer protection. Now, the logic here was that there was other enforcement of consumer protection laws. So now, the reason we were going to get rid of preemption is because we thought there was under-enforcement on consumer protection laws.

So, we needed to be able to turn the attorney generals and the state agencies loose on the banks in order to do it, right? The catch with that, is what? Well, we have gotten rid of that. We have created this new super regulator. Thus, it seems like we have gotten rid of the reason for getting rid of preemption, right? Because now, we have got this massive consumer protection agency that was the whole justification for getting rid of preemption in the first place. Instead, what we have now is both the new regulator and basically elimination of preemption.

And so, what we are getting is a piling-on effect where the idea of doing a coherent cost–benefit analysis of regulation, as this agency is set up to do very well; that problem is going to be exacerbated even more when you add on the fact that now state attorney generals are going to be able to pile on top of that as well. We see how this works in practice. The Searle Center has published work on so-called little FTC acts, which mirror the Federal Trade Commission Act,[4] but what we see is states apply that very differently in a much more heavy-handed manner than the Federal Government does. So, we have gotten rid of the reasons why we did not want to preempt, and then, decided not to preempt anyway.

There are also provisions in here that would restrict arbitration. It gets rid of arbitration for mortgages and home equity loans when you enter into a mortgage. It also provides a provision for a study of arbitration in consumer credit contracts generally. How this can best be understood is really just a shop to class action lawyers—this basically is a way of giving them a new vehicle to pile on, still more, by getting rid of arbitration with respect to mortgages and the like.

Fourth, the big problem here is it really does nothing at all about the incentives that lay at the root here. But the underlying problem here really was not a problem of consumer protection, but the alignment of incentives that we saw here. Things like state anti-deficiency laws, cash-out refinances, that caused people not to have equity in their home and that sort of thing. And in fact, what this actually does is exacerbates that problem. For instance, it requires a special notification if the consumer were to refinance their mortgage and thereby lose their protection of their state non-recourse or anti-deficiency law.

It eliminates prepayment penalties in a lot of mortgages and caps them in others, which, of course, makes it easier for consumers to refinance when their house goes up in value; which allows them to strip out their equity so that when their house price falls, they are going to more readily fall into

negative equity territory. The whole structure of the agency is set up on a particular theory about the financial crisis, which I think is only slightly correct, if at all, and is primarily wrong. What this illustrates is that they have failed to understand the moral hazard problems and the kind of problems that they are setting up. With some of these, they are just helping lay the foundation for the next financial crisis and exacerbating the things we saw over the past few years.

Final thing I want to talk about is the Durbin Amendment parts. Moving from the CFPB to the Durbin Amendment on credit cards and debit cards, which is the interchange fee regulation that Dan referred to. The interchange fee, you may recall, is the fee that the merchant pays when you swipe your credit or debit card.

The Durbin Amendment reduces interchange fees from 1.3% on the transaction, to 0.2% of the transaction. At this time**,** I've got to say two words to finish that up. First, the unintended consequences of this are obvious, which is they cap debit card interchange fees to now credit card interchange fees. Credit card interchange fees are higher than debit card interchange fees. All they are going to do, is they are going to cause people to move from debit to credit cards.

Finally, the last thing to talk about, to echo what Dan said, was this whole idea of this agency; the whole purpose is to redistribute wealth to merchants from issuers, and eventually from consumers. All of you now are going to have to pay for your debit cards instead. And it's ingrained in this legislation, picking winners and losers by politics rather than by market processes, which I think is a really frustrating development.

GEOFFREY J. LYSAUGHT: Thank you very much. Why don't we recirculate through the group. Any thoughts that were triggered J.W., as you listened to Todd and Dan speak?

J.W. VERRET: Sure. There were too many to mention when I listened to my colleagues, particularly Professor Zywicki, speak, and I think we often end up getting partnered on things. I think one of the thoughts that Professor Zywicki's presentation triggered to me was the benefits of federalism and questions about preemption. He discussed the problems with the bill and that they do not permit federal preemption, and I want to draw out that distinction from my own side of things.

I'm generally a corporate federalism guy, right? I generally come at things from the point of view, that I support states as entities that charter companies and that govern the relationship between companies and shareholders. But at the same time, I tend to also support when the Fed, and the SEC at times, preempt state regulation. So, I want to make sure that schizophrenia has some kind of an intellectual basis.

And I think it's simply this: when states charter institutions and states can internalize the cost of over-regulating those institutions, then, I trust the

states as sources of law in that respect; whereas, if states can bring an enforcement action or regulate an institution it did not charter, then I question the ability of states to internalize the costs of over-regulation and over-enforcement. I think that maybe adds some consistency to supporting the rule of states in chartering corporations, and even in chartering banks and regulating those banks that it does charter. But at the same time, it also speaks to the benefits of federal preemptions of state overregulation.

I will just call it the Eliot Spitzer effect. Essentially, the ability of a state attorney general to go after institutions with only the upside of bringing enforcement actions. I think if I was a Louisiana attorney general, and I saw a Texas bank that made a good target—and boy, whether or not they did anything wrong—I could go after them in court and say something about a complex banking regulation anyway. Why not bring a large expensive action against that Texas bank?

So, that might be one of those principles that I think ought to inform our thinking here, and I think regrettably, was something where Dodd-Frank took the opposite approach. Where preemption was good, it didn't allow preemption. Where preemption is bad, it went full speed ahead with all-out preemption of state law.

GEOFFREY J. LYSAUGHT: Thank you. Dan?

DANIEL F.C. CROWLEY: Well, I was thinking as Todd was speaking, that this is a unique regulator process. Typically, Congress passes a law, and the regulators go off, and interpret it, implement it with rulemaking in a linear fashion. I think this time, what we are going to see is much more circular.

Because of the absence of legislative history, because of the election, and people holding the oversight gavel who really do not like the law, you are going to see an unprecedented number of hearings, attempts to channel decisions by the regulators by calling them up and asking embarrassing or tough questions on the record, by little rifle shot amendments in various ways to try to clarify the legislative intent, by letter or colloquy on the floor. My favorite is withholding funding for agencies that do not quite get the intent of Congress, reflected by people passing appropriations bills.

But one example of this, I think, is the CFPB, because of the dynamic that Todd discussed with a single appointee who has all this power, not subject to review. The reason, by the way, why the CFPB is buried inside the Fed for funding is precisely to insulate it from annual Congressional scrutiny in the appropriations process. What has happened though, is that the President and his advisors concluded that Elizabeth Warren was not confirmable by the Senate, so he's now appointed her to positions in Treasury and the White House, both of which are subject to annual funding pressures.

So, they set up an almost inevitable dynamic here where the Republicans not only are going to go after the funding for her position, but will block any effort to appoint a permanent director until they are able to make structural changes. So, I am going to go way out on a limb here and predict that as a condition for getting confirmation of who the President finally does nominate, it will be an effort by Republicans to revisit the composition of the CFPB along the lines of what Todd described by the five member bipartisan panel.

GEOFFREY J. LYSAUGHT: Questions from the group? Sir?

AUDIENCE MEMBER: Gentlemen, you certainly persuaded me that this is the same as the Bankruptcy Bill, which was so garbled after five years of study. Since you find nothing good in it, you imply that there was nothing wrong with our financial system, which required repair. And thus, could you tell me why our financial system collapsed, since it was so good before this bill was passed?

DANIEL F.C. CROWLEY: Fannie Mae, Freddie Mac, and mortgage interest deductions—I think we start there. Fannie Mae and Freddie Mac were not included in this bill. And frankly, it is a bit of a live wire. Republicans like to complain about it, but when they have the gavels and the White House, they find it's a politically sticky wicket to undo that Gordian Knot, as much as the Democrats do. But Fannie Mae and Freddie Mac were not included in the bill at all, and I think it begins and ends at their doorstep.

TODD J. ZYWICKI: Well, some people here have seen me talk about this for at least an hour, but I will give the short version, as it relates to this. Basically the idea is, I don't think everything was good with the financial system. Certainly, I do not think everything was good with the way consumer protection laws were written, as I said. But fundamentally, what drove this was misaligned incentives, and what we have ended up doing is diagnosing a safety and soundness problem as a consumer protection problem.

So, for instance, if I take out an interest only mortgage with no down payment in a state that has anti-deficiency laws, you can not collect against me when I walk away from my house. Then, my house goes down in value and I decide to walk away from the house. When I rationally respond to those incentives, that is not a consumer protection problem. We probably do not want to allow banks to make those loans. It is a safety and soundness problem. Why do we not want to allow banks to make those loans? Precisely because of the structured incentives that they set up.

What I think we needed to do is go in here, understand the structured incentives—whether it was Fannie and Freddie, whether it was Federal Reserve monetary policy—all these sorts of things created a system of in-

centives combined with moral hazard problems that these banks knew they were probably going to get bailed out. They have been getting bailed out for twenty years, going back to Continental, Illinois.

California today, knows it does not need to fix its budget because we are going to bail out California because it's too big to fail. So, we have created this environment where banks rationally respond to doing incentives, consumers rationally respond to doing incentives, and this bill misdiagnoses almost all of that.

DANIEL F.C. CROWLEY: It's funny. The causes of the credit crisis, is sort of like a Rorschach test. People see different things in it. I do not disagree that the GSEs and the incentives were part of the problem. But from my standpoint, I think the fundamental problem was that banks did not appreciate the nature of the risks that they were assuming across the board. It was a lack of transparency on investor choices. There's no doubt that there was a problem that needed correction, but it is interesting to me, the extent to which all of the previous work that had gone into trying to address capital market issues was ignored; there were a whole series of reports. The Treasury had a blueprint.

Hal Scott at Harvard had a whitepaper. Bloomberg and Schumer did one. It was about five of them. The last one was the G30 chaired by Paul Volcker that all said the same thing, which is, move to a more prudential model of regulation, streamline regulation, consolidate the banking regulators, merge the SEC and the CFTC. And the interesting thing to me about Dodd-Frank is that it does none of that.

GEOFFREY J. LYSAUGHT: I would be interested in your thoughts on this; sort of throwing rotten fruit at the actual legislation, and the process by which the legislation was created. We have teed up a huge fight for a future regulator process. When you think about investors or consumers of financial products, what, if anything, good can be attributed to this Act?

J.W. VERRET: I would suggest the one good thing about proxy access is that it gives companies an opportunity to implement the defenses that I have designed. It gives people a chance to read my new paper on this in the *Journal of Corporation Law* coming out next month defending against proxy access and company defenses in the era of Dodd-Frank.[5]

TODD J. ZYWICKI: It's hard for me to think of good things. When it comes to consumer protection, everybody agrees. I do not think I have seen a defender of the law question this. There's no question that the impact that CFPB is going to have is to raise the price of credit and reduce access to credit. Defenders of the law do not question that. And, in fact, many defenders of the law say that is the point, to reduce access to credit. There was too much access to credit, right? So really, the only question then is

whether or not there is reason to raise the price of credit and reduce access to credit, a lot, or do it a little in places where the discretion lies in this.

There is a cycle of consumer protection in consumer credit over time that this fits into very nicely. The Durbin Amendment is an unmitigated disaster. Economically, it is utterly absurd. Everybody is going to pay more for debit cards. If you are lucky enough to consume other bank services, you might not notice it as much, but a lot of people are going to lose free checking. A lot of people are going to be forced to drop out of the banking system. It's terrible economics, as I said.

It's great politics because, as I said, it caps the interchange fees on debit cards but not credit cards, which means people are going to switch to credit cards, which have higher interchange fees. Well, within three months of this law going into effect, all the merchant groups are going to be back here spending millions of dollars trying to persuade Congress to extend price gaps to credit cards. And so, it's beautifully phased in process for political purposes. Since I'm on the topic, I'll just note how we ended up with debit cards higher than credit cards. So, they started with the economic engineering problem as to which would be easier to calculate, and then reversed engineered to put price caps on debit cards and not on credit cards. That is the only explanation I have been able to hear. As Dan noted, this is actually being challenged. The lawsuit has been filed, challenging the constitutionality of the Durbin Amendment in the Federal District Court of South Dakota.

I can see one good thing: there will be an integrated mortgage disclosure form that'll make it easier for people to figure out what their costs are in mortgages. It's easier for me to tell you what's the worst provision in Dodd-Frank: I think it has to be in the investor protection provision—the whistleblower provisions which create a bounty for people to report securities law violations to the SEC. They can get somewhere between 10% and 30% of any recovery over a million dollars. And if that was not bad enough, we have added an anti-retaliation provision for employees. So, what we have done is created an incentive for your worst employees to not bring problems to the attention of the internal compliance department, but instead, to go to the SEC and file a complaint, where after their jobs are protected.

GEOFFREY J. LYSAUGHT: Any other questions? Well, given that we have discovered there will be less credit available, there will be more expenses, home prices are still propped up. We have a regulatory disaster awaiting us, I think it's time to drink on somebody else's dollar. Thank you.

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[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[2] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745, §§ 101, 105, 203 (2002) (codified as amended in scattered sections of 11, 15, 18, 28, and 29 U.S.C.).

[3] The Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, § 128, 122 Stat. 3765, 3796 (to be codified at 12 U.S.C. § 461).

[4] *See e.g.*, Henry N. Butler & Joshua D. Wright, *Are State Consumer Protection Acts Really Little-FTC Acts?*, 63 FLA. L. REV. 163 (2011).

[5] J.W. Verret, *Defending Against Shareholder Proxy Access: Delaware's Future Reviewing Company Defenses in the Era of Dodd-Frank*, 36 J. CORP L. (Forthcoming).

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GEORGE MASON JUDICIAL EDUCATION PROGRAM
DECEMBER 5-7, 2010

EDITED TRANSCRIPTS

CLIMATE CHANGE LITIGATION

Richard O. Faulk, Eric Mayer, Joseph F. Speelman, Jason S. Johnston
Moderator: Henry N. Butler

HENRY N. BUTLER: Today, I think we have a very interesting set of panelists for you. I would characterize some of these as big picture type of issues that we're going to be looking at. The first panel is on climate change litigation. It's kind of hard to get bigger than the world. The next one is a panel on the balancing of markets litigation, regulation, and some broad public policy issues as to what's the proper role of the courts, the legislature, and so forth. We have a great line up of scholars to talk to you on that one. Then, Larry Ribstein is going to talk about the death of big law at lunch, which I think is something you'll find interesting. The final panel, "The Role of the Civil Justice System and Allocating Societal Risk," is another big picture type of question.

These issues are things that are very much in our mind. There is policy relevance with this panel. The other panels relate to issues in terms of the changes that have been going on in Washington and the way we think about the relative merits of different parts of our legal system in terms of addressing challenges. The first panel is a distinguished group of folks that we have put together here. All of them have participated in some of our programs in the past, and they passed that test, so we are thrilled to have them back here. To my immediate left is Rich Faulk from Gardere in Houston. Rich is an accomplished litigator in a lot of environmental law areas.

He's been very much involved in the climate change litigation, and public nuisance lawsuits. Rich is going to take on a professorial role and give us an overview of the leading cases that are covered here. To his left is Eric Mayer from Susman Godfrey in Houston. Eric is substituting for Steve Susman, and Eric has participated in our programs in the past. Steve had some litigation that he couldn't get away from, so I'm sure that Eric will fill in ably because I've seen him in action before. Then, we have following up is Joe Speelman who is from the Houston office of Blank Rome.

Joe has spent many years in the corporate counsel office, most recently with LyondellBasell, and he is very much involved from a corporate perspective in how you deal with threats of these large lawsuits dealing with public nuisance and climate change issues. Following that is Professor Jason Johnston from the University of Virginia. Jason is going to give us a policy perspective on a number of these issues. Now, the perspectives I would characterize is that Eric Mayer is going to be pro-public nuisance, climate change litigation cases, and the other three are basically going to express some skepticism about those types of cases.

This may seem unbalanced, but Eric is not daunted by this challenge at all. In fact, he welcomes it. He thinks we should have more people up here on the other side; so balance is in the eye of the beholder, and I think that you will see we've got a good fight going on up here. We'll turn it over to Professor Rich Faulk.

RICHARD O. FAULK: Good morning. I'm supposed to be a neutral professor.

HENRY N. BUTLER: For the first few minutes.

RICHARD O. FAULK: For the first few minutes in any event, so Eric has a bit of a respite here as I go forward. I'm going to set the stage for what this litigation is all about. We can't get anymore topical or newsworthy than climate change litigation. Yesterday, the Supreme Court of the United States granted certiorari in a big case called *Connecticut v. American Electric Power*[1]—a case in which we have filed a brief—on whether climate change litigation will be allowed to proceed in this country. The case is a public nuisance case under federal law involving emissions of greenhouse gases by public utility companies up in the Northeast. It will probably have a major impact not only in that particular area, but also upon other cases that are pending elsewhere.

There's another case involving the exacerbation of Hurricane Katrina by greenhouse gases that is also in front of the Supreme Court on a writ of mandamus application. And there is another case that is being prosecuted by my friend Eric Mayer in the Ninth Circuit, which involves, as he will tell you, a native village in Alaska whose coastline has been eroded. They claim that their village is in danger because global warming has melted the ice pack that normally protects their coast from wave action. Those three cases are the big cases currently pending.

These cases are framed under federal common law as a general rule under a tort called public nuisance. I suspect all of you have had or have had to deal with public nuisance cases at one point or another. The question here is whether the vessel of public nuisance can hold a universal tort based upon climate change issues. Many advocates, such as Eric here, will argue that the issue isn't one of the tort's vitality—it's really a question of scale. Others, including me, think that size matters, and that the unmanageability and lack of standards governing greenhouse gas emissions makes the cases non-justiciable.

Public nuisance consists of a few elements, and they're not very complicated. First of all, a public right must be involved—a right common to the general public that they have a legal right to enjoy. Second, there must be a substantial interference with that right that causes some sort of damage, or threatens to cause some sort of damage. Two remedies are available in public nuisance litigation. The first is an equitable remedy known as

abatement, where a court can, upon finding a public nuisance, order the defendant to stop or to change its activities. The court can also order the defendant to remediate the problems caused by it. Under some circumstances, damages may be awarded. Costs of remediation and other compensatory awards may be available.

Let's look at a couple of examples. I live in Houston. Let's say that during Hurricane Ike a tree fell from my property and crashed into my neighbor's house and damaged his roof. Under those circumstances, no public right is involved. Under those circumstances, it's simply a private dispute between landowners.

It may be *private* nuisance that he has a tree in his living room, but it's a matter between us as private land owners, and a public nuisance does not arise.

But let's say that the tree falls the other way and it blocks the street in front of my house. Under those circumstances, the public has a clear right to go down that road, to navigate it, to deal with whatever errands it needs to run. Since the fallen tree invades a right that's common to everyone, it's a public nuisance. The remedy is to order me to remove the tree.

Now, that's a simple illustration. Let's look at global warming. Let's say, for example, that several utility companies in the Northeast burn coal in their plants. Those plants, through their smokestacks, release greenhouse gases—all kinds of things like carbon dioxide, methane, various other things as a result of the combustion of the coal. Let's say that, for the purposes of argument, science has established that those types of emissions cause or contribute to cause global warming, which is a deleterious thing to human beings.

I don't think anyone would doubt that the air we breathe is a common resource. So, there probably is a public right involved in these circumstances. But there are other issues. One of them is whether the emissions of these particular defendants are, in fact, substantially contributing or causing the climate change.

Generally in tort cases involving public nuisance, there is a term, which we all know from negligence cases and other torts, called proximate causation. In proximate causation, there is a "but for" test: but for the defendant's activity, would the injury have happened? Can we say that climate change would not have happened if these power plants, these isolated five power plants, were not emitting greenhouse gases? If they completely stopped, would we still have global warming? If you shut them down completely and have them completely dismantled, would we still have global warming? Is it really *their* emissions that are causing this, or is it the other billions and billions of things on the planet that caused global warming—such as volcanoes? Such as gases being naturally released through earth actions, through off-gassing? Is it the refinery down in Texas instead?

Is it the elephant on the grasses in Africa? Is it my cows on my ranch in Texas who emit methane every day from their digestive systems? How

can we characterize the public utilities' actions as "but for" causes or "substantial contributions?" So far, the courts haven't even reached these issues on the merits.

But there's another issue that we have to consider. What kind of order can a court of equity render in a climate change case? As judges, you all know that, in equity, any order you render needs to solve the problem, right?

You don't want your order to just be a symbolic act. As a matter of fact, there's the maxim of equity—which we've all heard since law school—that "equity does not do a vain thing." Equity does not engage in idle gestures. Let's say we shut down the plants or regulate the emissions from the electrical plants in the Northeast. Does that solve the problem of global warming? Can a truly efficacious order be rendered in those circumstances? Or is that something from which equity simply must abstain? And that's an issue that comes up.

So in climate change cases, these concerns translate into two threshold issues. The first issue concerns standing. In order to bring a lawsuit into your courts, a plaintiff must have standing to sue, and usually that's pretty obvious. They have been hurt and allege that their damage is caused by this particular defendant. But what if they can't trace their injury to the actions of any particular defendant that they have sued? And what if they admit that they can't prove that the defendant who owns this particular power plant caused the injury that they are suffering from? That raises the issue of constitutional standing. That's one of the issues that the Supreme Court of the United States granted certiorari to review yesterday in our case.

The other issue concerns the "political question" doctrine. That issue asks whether courts have any business being involved in this sort of a dispute. If courts can't render orders that solve the entire problem, if courts can't identify traceable injuries caused by global emissions, isn't this a controversy that should best be dealt with by an international body? By an international treaty? Isn't this an issue of international relations? After all, the only judge I know that has universal jurisdiction doesn't really sit on any court that I practice in front of—I see him every Sunday at church.

Under those circumstances, is this a "political" question? Is this something that Congress and the EPA should handle—instead of the courts? That's an issue that the Supreme Court has agreed to review in our case.

And lastly, we have to consider the impact of the EPA's recent decision to regulate greenhouse gases—regardless of whether the courts take action.[2] EPA has now decided to regulate certain facilities, and they're in the process of promulgating hundreds and thousands of regulations. What's left for courts to do? Hasn't the EPA displaced all the tort suits? That's exactly what President Obama, through the Solicitor General, told the Supreme Court in a brief that he filed in our case.

He said, "Let the EPA regulate. We're regulating. Step aside. We don't want lawsuits in this particular issue. We have displaced the field.

We're regulating these gases on our own and we should be allowed to continue without any interference b the courts."

So that's your primer. I realize I have downloaded a lot of information, and I have tried to be neutral in this presentation.

Now, I will just ask one question of Eric, and I know he's going to answer this in his presentation because he's told me so.

Assuming all of this falls apart, and the Supreme Court says, "Yes, you can proceed with your climate change lawsuits"—I would really like to know how they are going to be tried. If this gigantic global situation is coming soon to your courts, I think each of you judges should have an idea of what to expect. Eric should tell you how he's going to try these cases and make sense out of them in front of you and in front of juries. So with that question asked, I will sit down.

ERIC MAYER: I can proceed without him. The slides are only pictures. They're just pictures of the native village of Kivalina, and I think I can convey to all of you a little bit about this plaintiff and why this litigation was something that we became involved in. My name is Eric Mayer. I'm with the Susman Godfrey firm. We are commercial litigators that have offices in a variety of cities: Houston, Dallas, New York, Los Angeles, and Seattle. We are a commercial litigation firm, but we do some climate change litigation, and we do some litigation in the environmental arena on a pro bono basis.

All of the work that we have done in this area has been without charge. Our single largest client is a coalition of Texas cities, including Houston and Dallas, that hired us after we offered our time pro bono to begin litigating the permitting of coal fired power plants around the state of Texas. We've done a couple of those proceedings. The reason I raise that is because I think as trial judges, you should be aware that the global climate change issues are getting more traction at traditional law firms. Law firms, like mine, that do civil litigation have become involved in some of this litigation. I don't think anyone believes that this is a money-making venture.

We became involved because of our obligation to do a significant amount of pro bono work, and we have done that for the last five years. The case that I wanted to talk about—and I did mention that I would speak about when we win in the Ninth Circuit—how we will try our case. I'm going to proceed and begin with that. But let me just tell you first a little bit about Kivalina, and why we took the case and why we got involved. Kivalina is a village that sits north of the Arctic Circle; if you imagine Alaska, you have got to go to the northern portions of Alaska. It is a settlement that has been there for generations, and it's a federally recognized Indian tribe.

That has some significance, which I will get to in a moment. It's also a city that's recognized under the State of Alaska, and that has some significance because what's happening in Kivalina is that the area that the tribe inhabits is at the end of a long peninsula. The peninsula sits out into the

ocean. Previously, ice has surrounded the peninsula most of the year—naturally forming ice sits there virtually all year. But several years ago, the tribal leaders noticed the ice was melting, and the ice was establishing itself later in the year. The ice was forming much later in the fall and breaking up much earlier in the spring.

They noticed that because the ice wasn't forming and lasting as long as it was, that the land that they sit on was subject to terrific winter storms. Those terrific winter storms began to erode the land that the tribe has sovereignty over. There's a treaty. This is their land. It's recognized by the U.S. Government as a separate, independent sovereign. The tribal leaders had to make a decision what to do, so they contacted the Army Corps of Engineers, and they contacted the U.S. Government Accountability Office, and they said, "Please come in and help us. We have 400 or so people that live here and have lived here for generations, but our land is now being eroded."

They got two reports. The reports from the Army Corps of Engineers and of the Government Accountability Office said, "You're going to have to move. You can't stay here any longer. The erosion is so significant and dangerous that the land that you and your forefathers have inhabited is eroding away, and the buildings that you have constructed have to be moved. The cost of that is going to be between $95 and $400 million." And they went on.

Both organizations said the property is being damaged because of global warming. The Indian tribe leaders had to decide what to do. They don't have the $400 million to move. So they began to seek legal advice—not originally from my firm, but from a bunch of public interest law firms. The lawyers that were working at those firms decided to start looking at the law of federal public nuisance because they have a report that says climate change and global warming is resulting in the erosion of the property. This is property that this Indian tribe owns. The tribal leaders—if you stop and step back a moment—the tribal leaders have an obligation to their constituents.

They're charged with maintaining the tribal lands. If they do nothing, that's really not consistent with exercising their right to make sure the property is there not only for themselves, but also for the future generations. So, with a bunch of law firms, a lawsuit was filed on Kivalina's behalf in federal court in California, against Exxon Mobil and fifteen of the nation's largest oil and gas coal companies.[3] Now, many people have said, including members on our panel, that climate change lawsuits like ours are going to fail in the courts because they pose really significant challenges to the whole concept of torts, duty, and causation.

Some commentators have said that although our lawsuits are destined to fail, they are doing wonderful things by forcing the attention of the community on these issues, and bringing about change that is needed in order for the society to continue. Because what we're really talking about

is what does a sovereign do when the sovereign feels that his or her property is being invaded and damaged by another entity? If you stop for a moment and think about what did the United States do before we had pollution laws?

If you look at the cases that came before the United States Supreme Court, they are public nuisance pollution cases: State of Illinois suing another state and a bunch of cities for polluting some of the Great Lakes,[4] State of Georgia suing other states for what is a precursor to acid rain.[5] One of the questions was, is the tort vessel sufficient to hold it? The short answer is: yes, of course it is, because that's exactly what we did prior to the time we had pollution laws in this country. The reason the sovereign is important is because in a federation—such as the United States of America—if a state is unhappy with what someone else is doing, they cannot stop those emissions through an aggressive act.

As part of membership in the United States, the sovereign—such as my state, Texas—has given up its ability to go to war with Oklahoma for polluting Texas property. They can't do it. The Supreme Court has said in *Massachusetts v. EPA*,[6] which was decided several years ago, that states have standing. Sovereigns have standing to challenge pollution because the only way they can challenge it is in court. They don't have the ability to do anything else. That's part of what this great United States of America is all about.

That's why those cases originally began in the courts in the first place—because states were unhappy with what other states were doing that impacted their constituents. If you build a large plant right across the border in Oklahoma, and then I have people in Texas that can no longer farm their land because sulfur emissions fall on and kill the alfalfa, do you have a remedy? Yes, you do have a remedy, and the remedy is public nuisance. Now, there are some restrictions on it. The law in this country is that if the area is regulated by the federal government, then the federal common law nuisance doesn't exist because the theory is, "Hey, the government has stepped in and regulated it."

We don't need federal common law for this issue. That becomes important with what we just learned because under the Bush Administration, greenhouse gases were not regulated. The EPA refused to regulate them. That resulted in a lawsuit by Massachusetts and several other states to demand that the EPA start regulating greenhouse gases, because the failure to regulate greenhouse gases was causing global warming, which was impacting Massachusetts's property—its coastline. That went all the way to the U.S. Supreme Court in a 5–4 decision. The United States Supreme Court said, "You're right, Massachusetts."

Carbon dioxide and greenhouse gas emissions are pollutants under the Clean Air Act. The EPA has no excuse for not regulating them. Congress has said they have to regulate them. The Bush Administration has refused. We, as the highest court in this land, order the EPA to begin regulating

greenhouse gases. Now, from a litigator's standpoint, that was very helpful for me because it indicated clearly that there was a total absence of regulation. The Supreme Court had to step in and order it done. Hence, that permitted the lawsuit of public nuisance to proceed. The law of nuisance is complex. It is multifaceted, but in general, our lawsuit is fairly simple.

Under the law of public nuisance, federal common law, a nuisance is unreasonable if the harm to the public outweighs the social utility of the conduct that's causing the nuisance. The common law has helped us develop shortcuts for determining when something is unreasonable. For example, if an actor is intentionally invading the interests of another's land, and the harm to the land is severe, then that is an unreasonable interference for nuisance purposes regardless of the utility of the actor's conduct. So, if you're invading someone's land, that invasion is serious. The Restatement of Torts section 829(a)[7] states, regardless of the utility of the conduct, that's an unreasonable interference.

That doesn't mean the actor has to stop what they're doing. I mean, a misconception here is that every nuisance suit is an abatement—it's not. Our suit, the Kivalina suit, is not an injunctive request. We're simply saying it's $400 million to move this Indian tribe. The invasion is significant. It doesn't matter that the defendants, the emitters of almost 4% of global greenhouse gases worldwide, may be doing something that is socially beneficial. The question is: who will pay for the move? Under public nuisance law, section 829(a) of the second restatement, that is an unreasonable interference.

The actor only stops what he or she is doing if an injunction is requested. The injunction—I posit to you as trial judges—the injunction is where you have to weigh the utility. You have to decide whether you're going to stop somebody from doing something. We're not seeking that, and I would concede those are much more difficult cases to prove on the plaintiff's side. The injunctive cases you typically see that are successful in this area, are brought by states, not by private litigants. We have not asked for injunctive relief, and under restatement section 829(a), once an intentional invasion that causes severe harm to another's land occurs, the actor has to pay for the harm they have caused.

They can still continue the conduct; they just have to pay for it through the mechanism of damages. Here's an example. The case is *Jost v. Dairyland Power Cooperative*[8]—it's a Wisconsin Supreme Court decision—State of Wisconsin. A power plant in the City of Wisconsin is emitting sulfur fumes that are causing alfalfa crops in the city to wither and die. Screen doors and windows in the houses are rusting through. You cannot grow flowers in your yard because of the chemicals in the air. The farmers sue. They say the sulfur fumes constitute a public nuisance.

The defendant says, "Wait a minute. We're providing a great social utility here. We're generating power for the city. How can this be a problem? You can't call us a nuisance unless you weigh and tell us that what

we're doing is wrong." The Wisconsin Supreme Court says no. In its holding, it's a common law precursor to section 829(a). It says the air pollution is still unreasonable, even if the activity causing the pollution has great social utility because it causes a severe harm to the land of the property owners adjacent to the power plant—and that's the same situation we have here in Kivalina.

We alleged that the defendants have emitted collectively, hundreds of millions of tons of greenhouse gases over the last few decades, and those emissions have contributed to climate change, which is why the ice pack is no longer forming. Now, the defendants have argued that the court cannot possibly adjudicate the case because it would have to weigh the social utility of power production versus the harm to the Indian village. It's simply wrong as a matter of black letter nuisance law. That's not what the Supreme Court of Wisconsin held in *Jost*, and it's the opposite of the rule in section 829(a).

The defendants have also made another argument: there's no principled way of how you could decide among the millions of actors who contributed to climate change, who should bear the cost of moving the Indian village. Why should Exxon have to pay? Why shouldn't you go sue the power plants in China? That is not an unusual question. Of course, it's a good question. But the law in this country has dealt with that question, too; it arises in every multiple polluter case that exists. There's litigation right now between the State of Oklahoma and Tyson Foods.[9] There is a huge litigation about the placement of poultry waste on land in the Illinois River Water Shed.

Oklahoma has sought an injunction, which was denied. But there's a lawsuit by Oklahoma against Tyson, among others, but against Tyson for pollution under public nuisance and state pollution laws. Tyson's response was, "Well, wait a minute. You're suing me but this pollution is caused by everybody that has cattle farms, and it's caused by everybody that has septic tanks. So we're going to sue in a third party action; we're going to sue everybody else that's polluting in the State of Oklahoma, and guess what trial judge, this case is totally unmanageable—we can't have a case with 10,000 defendants."

The law in this country is that you can sue those defendants that you think are responsible, and there are mechanisms within the law to deal with this issue of whether others should be joined to the lawsuit. That's typically in the pleading stages of the lawsuit. This issue has come up—what Oklahoma said is, "Listen, we're going to let you third party in some other people who you claim are the major polluters beside you, the chicken polluters. That's fine. We're going to sever those claims. Let's deal with you in the State of Oklahoma because there's a lot of issues here we have to deal with."

For example, is the chicken waste causing the pollution? If it is, then we'll deal with the claims we have severed, and you can try to assert your

claims for apportionment or contribution. So in every multiple polluter case, you're going to hear the argument that there are other polluters who should be before the court. Let me say, in *Massachusetts v. EPA*, one of the arguments the EPA made to the U.S. Supreme Court was as follows: we are not wasting our time regulating greenhouse gases because we only represent the United States of America, and most of the greenhouse gases are in China or in India.

The U.S. Supreme Court said, "That's not a good reason. The fact that others may be doing it doesn't relieve you of the responsibility to get out and start regulating." Now, courts have developed four ways to deal with multiple polluter cases. The first is an implicit recognition of plaintiff's right to select the defendants who they claim are responsible. The fact that there may be other defendants who are responsible does not mean that these defendants who the plaintiff has sued are not responsible—and that was the district court holding in *Illinois v. Milwaukee*,[10] which was a multi-state polluter case.

The State of Illinois sued Milwaukee and other jurisdictions that surrounded one of the Great Lakes for polluting. The second way they deal with multiple causation is the common law rule, which you'll see in Prosser and Keaton on torts.

I'm going to read you a quote now from Judge Posner in the Seventh Circuit, "Even if the amount of pollution caused by each party would be too slight to warrant a finding that any one of them have created a nuisance, pollution to the stream, even to a slight extent, becomes unreasonable and, therefore, a nuisance when similar pollution by others makes the condition of the stream approach the danger point. The single act itself becomes wrongful because it is done in the context of what others are doing. If each defendant bears a like relationship to the event, and each seeks to escape liability for a reason that, if recognized, would likewise protect every other defendant in the group, leaving the plaintiff without a remedy, the attempt to escape fails and each defendant is liable." That's a quote from Judge Posner—summary of the common law and pollution cases from an en banc decision of the Seventh Circuit in *Boim v. Holy Land*,[11] a recent decision of the Seventh Circuit. The key point here is the knowledge point.

In our lawsuit, we claim through a conspiracy allegation that each of the major defendants in our case knew that the emission of greenhouse gases was, in fact, causing global warming. We also have an allegation that the defendants conspired together to create doubt among the public about whether greenhouse gas emissions were causing climate change. Now, there's also an exception under the tort restatements third for liability for physical and emotional harm for trivial contributors.[12] One of the arguments these defendants have made is, "Wait a minute. If you're suing all of us, don't we have the right to sue every resident of California for driving their cars because each one of those residents is contributing greenhouse gases?"

We don't believe the law permits that type of—there's a trivial exception. We don't believe that's a legitimate defense, but we also believe that, if there are other contributors that they believe are providing pollution, that they believe should be before the court, they can implead them as was done in the *Tyson* litigation—the trial judge can then decide. The third way that Courts have dealt with multiple polluters is the notion that the injury is indivisible. When there's no way to know how much damage Exxon caused versus BP, the law in this country has been that each is responsible, and there's apportionment.

For example, if the defendants could argue successfully that they only contribute 4% of the emissions in the world toward global warming, therefore, we should only recover 4% of our 400 from them, that would be a legitimate defense. They could certainly assert it, and it may be something that the trial judge would accept. But none of this has happened because obviously, we haven't even briefed this issue of apportionment; the apportionment issue also answers joinder, impleader, and contribution issues. Defendants have raised the "specter of potentially unlimited joinder," as they put it.

The idea that everyone on earth will end up in this lawsuit—there are two problems with that. The first is the limiting principles of knowledge and triviality, which I mentioned. The defendants may or may not be able to show that unused joint tortfeasors had the requisite level of knowledge. Besides this triviality problem of each individual driving a car in California, you have the question of knowledge. The defendants are very different in terms of knowledge. They each have scientific staffs that have been studying this issue, and we contend, obviously, that certain defendants engaged in a pattern of misinformation to the public.

Let's say that for the sake of argument, the harm cannot be apportioned, and the defendants have a valid impleader action against some unjoined third parties. The fourth way courts have dealt with multiple polluters situations is denying or severing a claim for impleaded parties—and that's what happened in *Tyson Food*. Let me skip to the end—how are we going to try our case? When we get back to the trial court, we're going to call a representative from the village of Kivalina to explain the problem of melting sea ice, and what the storms are doing to their land. We're going to show how this 400-person village hardly emits any greenhouse gases.

The last thing we're going to do—to obviously guard against some claim of comparative responsibility—is we'll call a damages expert and probably introduce ourselves, the reports from the government, the Government Accountability Office and the Army Corps of Engineers. They are U.S. Government reports—they are self-authenticating. They are going to come into evidence. We'll read in the record interrogatory responses that we will have asked each one of the defendants tell us over the last twenty years, what their greenhouse gas emissions have been.

We'll call some experts on our side to make the point that the greenhouse gas emissions mix in the atmosphere to cause climate change—although I think that's how Justice Stevens began his decision in *Massachusetts v. EPA*, and I don't think we'll have a problem establishing from a scientific standpoint, that's what happened. We will call some of the defendants, executives, and scientists, and cross examine the defendants' experts on why they believe the greenhouse gases don't result in the change in climate that has effected Kivalina. And then we will probably rest.

At the end of the day, we believe that the evidence will support the public nuisance claim that we have filed, and we'll get some compensation for the move for the village of Kivalina. With that, I'm going to end, and I welcome any questions that some of you may have following this presentation.

HENRY N. BUTLER: Thank you very much, Eric. I can't help but ask about the damages calculation and the $400 million figure for the 400 people. Can I join the tribe right now?

ERIC MAYER: Well, it's $95 million to $400 million—the cost of the actual move could be as low as $95 million.

HENRY N. BUTLER: It seems to me that Ted Stevens has not been doing a very good job with his port. Why didn't he just build a big old sea wall right there?

ERIC MAYER: Well, the pictures that I didn't get to—you can see, they have actually tried to build walls. There's a lot of protective work that has been done at great cost, up until this point; but the experts have finally told them, "There's no more protection you can do. You've got to move."

HENRY N. BUTLER: Okay, and are they going to pick up the buildings and move the buildings?

ERIC MAYER: Yes. They're going to have to move the property.

HENRY BUTLER: Why do they have to do that? Why don't they just abandon it?

ERIC MAYER: Because there is a fair amount of property that they have constructed there.

HENRY N. BUTLER: Okay—all right. There's so much, before we have to get to damages, on the question—but I just couldn't help but ask those questions. Now, we'll turn it over to Joe Speelman, who is going to talk about the corporate perspective of dealing with these types of litigations.

JOSEPH F. SPEELMAN: Good morning. I have spent thirty-one years in-house, representing large manufacturing corporations in the United States; including nineteen years as Chief of Litigation at the third largest chemical manufacturer in the world. I have a perspective that's different than what you have heard this morning. Let me first address one thing that my friend and colleague, Mr. Mayer, said. He said, "It's not a money making venture." That's baloney. This is all about money. We just heard the exchange. This whole thing is about money. I'm going to talk to you in the next few minutes about two of the largest transfers of wealth ever in our country's history. Then, I'm going to finish by talking about what is the issue today, which is the largest transfer of wealth proposed in the entire world, ever.

It's about the money. Twenty years ago, Stuart Altschuler wrote an article that was entitled, *Usurping Regulatory Power Through Mass Tort Litigation*.[13] In that visionary article written twenty years ago, everything that has happened was predicted by Mr. Altschuler. The idea expressed by the National Resources Defense Counsel and other NGOs was that they didn't like democracy because it didn't get them what they wanted, and so they were going to use the courts to run the American political process—fundamentally anti-democratic philosophy that they have consistently maintained—and might I add—relatively successfully.

Now, during my nineteen years as Chief of Litigation, it has been my privilege to retain both Eric and Steve Susman from the Susman firm to represent my client, and Rich Faulk. I have no greater admiration and respect for both those firms than anybody. That having been said, the real title of my program could be—since this is about climate change and it's in December—we could say, "Baby it's cold outside." That's a catchy phrase. But really, it's more about the following: from those people who brought you asbestos and tobacco, we're on the cusp of the largest proposed transfer of wealth in the entire world, and you as judges, are being asked to do it.

I would ask you to step back, talk to your colleagues, and let's have a second—a quiet, rational second thought about this process. I have been quoted in the past as saying the American tort system is broken, and it is. We have commoditized the law in the process to the point that we have the following absurd results. In tobacco, we had the largest transfer of wealth in this country. It's still going on, and what did we accomplish? More young girls smoke cigarettes now than ever before. Cigarettes are not gone and, in fact, they are guaranteed they are going to be around for a long time. Why?

Because the annuities created in favor of the American plaintiff's bar require funding from non-bankrupt tobacco companies. Therefore, the cost of tobacco and cigarettes has gone up ridiculously. They're still around. They're making money, and they're paying their annuities to the American plaintiff's bar. We still have smoking, and we still have cancer deaths. As

I've said before, more young girls smoke now than ever before. Is that the way this is supposed to work? What did we accomplish as a society? Nothing. But we did transfer wealth to a few people. What did they do with that wealth? Well, there's always asbestos.

I recently had the opportunity to watch a Chapter 11 bankruptcy proceeding in New York City. In that proceeding, a lawyer from Texas filed 285,000 proofs of claim for asbestos liability against the debtor; 285,000 claimants asserting that that lawyer represented all 285,000 of them and that they were all injured. The bankruptcy judge, being a good judge and a judge that's been around a while, granted the defendant's motion to seek some more clarification about it. Do you really represent all these people? Are they really injured? Did the debtor cause that injury? Seven days after that order was entered, which was a fair order, all 285,000 claims were withdrawn.

Subsequent to that, several letters came in from a number of those 285,000 people that said, "I saw my name listed, and some lawyer in Texas said that he represents me. Can you tell me how I can get a hold of this person because I don't know?" The commoditization of the law and the abuse is unbelievable. Who pays for that? Well, one of the things that businesses try to do is make money. If you watch television at all, you know that companies are being exhorted to hire people. We need to reduce unemployment. Why aren't you guys hiring people? For twenty years, I've watched business leaders—most of whom are engineers, by the way.

I always used to tell young lawyers or law students, "If you're going to go into the law, and you're going to go in-house, understand that you live in a nest of engineers because engineers are wonderful people who make things, and they end up being business leaders." Engineers have a very rational and direct thought process. To try to explain the law and the consequences to them the way it used to be, was a challenge because they didn't understand it. The typical comment was, "But we didn't do anything wrong. Didn't we abide by the law?" "Yes." "Why are we being sued? Why is this liability before us?" What is the answer to that?

The answer is: about every two or three years, the people that brought you asbestos and tobacco come up with new ideas; predatory ideas. They're designed to separate money from people that have it and take it somewhere else. So it is about the money. Now, try to explain that to your client. Put yourself in my posture. The only way I can safely advise a client to avoid liability in this environment is to not make, buy, sell, or insure anything—but that would make it really hard for us to do what the administration asks business to do, which is to hire people.

Is it the American business's responsibility? Is it our responsibility to deal with the change in the climate in this world? Well, let me talk about that for a minute. The theory is public nuisance, and it's a novel theory, but I want to give you some comments from people who had a lot to do with creating that theory. Professor Jim Henderson, from Cornell University,

he's a co-reporter for the Restatement Third on Products Liability which includes the language that all rely upon for public nuisance. There has been litigation for almost thirty years now on lead, and involving people who are responsible for lead in paint.

That was legally, in fact, compelled, fifty years ago; but now somebody says, "Oh, this is a horrible thing. We need money." So litigation ensues. Before the Rhode Island Supreme Court, Professor Henderson in an amicus brief termed the theory of public nuisance the way it's being utilized now, as simply lawlessness—nothing less than pure lawlessness. This is the man that wrote the language on public nuisance, but never intended it to be used the way it is being used. It's being used to try to change society. Is that the law's job? Or is the law's job to try to set standards so that people like me can advise clients on how they can obey the law? It's so much fun to say, "Do the right thing." What is the right thing?

If you keep changing what is right, and then seek damages for what was right then, but it's not right now—how long can that go on? How many jobs can business create when they're constantly having to look at their books and figure out how much liability they have to reserve for? There's another case I want to refer you to. It's *North Carolina v. TVA*,[14] in the Fourth Circuit. It's very similar. It's on this public nuisance theory. While the Supreme Court hasn't said they are going to look at that, there might be a reason why they have said they're not going to, because that decision stated there is not a public nuisance cause of action in this sort of situation—this being climate change and damage.

The circuit court deemed the theory of public nuisance, as it's being utilized, standardless liability—no standards. No ability for Joe Speelman to advise his client on how to do the right thing to avoid liability. There are no standards. I can't tell you how to do it. And if I can't do that, then the entire process by which business operates and makes things and sells things in this country, ultimately comes down—we get to what we really have, which is a casino mentality. So, as I said when I started—from those folks that brought you asbestos, lead litigation, and tobacco—we now have climate change.

Well, that's interesting. Let's talk about that for a minute. What should the defense be? Well, the defense needs to respond to this. The response needs to be principled, and it needs to be consistent. You need to hear what it is, but here are some points that underpin it. First, we insist in this country on rule of law, and not the rule of politics in law. That's important. Now, we also have to understand that we have an industrial base in this country that everybody is happy with in the sense that they like employment, and they like that process; so we have to be mindful of that.

Let me go on and make a really ripe statement. I think we have to defend American jobs and American industry, and we have to balance the legal issues and understand that there's a political debate going on here that is the essence of democracy. The law shouldn't be used to undermine that

debate. Well, let's start with the defense. First, legitimate science: I want all of you to go to Google when you get a chance—or, if you're like me, ask your seventeen-and-a-half year-old son to go to Google for you, because I'm not that capable. I want you to Google "Wall Street Journal Climate Gate." That's all. Type that in.

You're going to find the most fascinating set of articles, and it goes like this—I'm going to shorthand it because I'm from Kansas, and we speak in monosyllables as often as we can. Look, third division university in England gets the opportunity to do research from a grant, the source of which they still won't talk about. They conclude from this research that people, that industrialized society is causing global warming. Upon further review, it may not be true. The people involved attempted to hide this, attempted to intimidate scientists who disagreed or who raised questions.

All of this is documented. If you were a judge, how would you rule on evidence that's undermined like that? Would you allow that in? A number of scientists now say there's no consensus that people cause global warming. But let's go beyond that, and let's talk about the rational legal thought process here. I want to mention four words to you, and you're going to recognize all four of them: China, Russia, India, Japan. They all met in Copenhagen with great fan fare last year, and all four of them flipped America off on the concept of responsibility. And every one of those, with the possible exception of Russia, generate more greenhouse gas than this country does.

China is the largest greenhouse gas producer in the world by far, and getting worse. Neil Cavuto—I'm a fan of his. He has a way of putting it straight when he sees a ridiculous argument. He says, "Give me a break." Well, give me a break. This is not about American law, and American law can't fix this issue. What is the impact on our economy? Well, I think we have to think about how we're going to impact our economy if we're going to transfer—based on flawed science from a third division university in England—more wealth than has ever been transferred in the world before.

Is that what we should be doing, and should the law be used as a device or a weapon to accomplish this? Or should the law step back and take a calm second view? What is the impact of a volcano erupting anywhere in the world? Does anybody know? Anybody know how many volcanoes are active? Well, I can tell you. Again, my seventeen-and-a-half year old looked this up for me: 1,500 active volcanoes in this world. Do you know that one volcano erupting—all the things we do like recycling—wipes all of that out because of the greenhouse gas it emits? We have 1,500 volcanoes that are belching periodically in this world.

One last question I want to leave you with: does anybody know why Greenland is called Greenland? Fifteen hundred years ago, when the Vikings landed there to start farms, it was the greenest, most beautiful country they had ever seen. You can take tours now to Greenland and visit those ruins. They're still there. Why did they leave? Because it turned white.

Why did it do that? It wasn't General Motors's fault. General Motors wasn't even in existence, nor was Exxon Mobil. Folks, every 1,500 years, climates change in this world, and it's nobody's fault, unless you want to blame the Almighty.

And I don't advise it because you don't have personal jurisdiction. Look, let's be rational about this. This is goofy. It would be funny if it weren't for the amount of money involved. So Eric, with all due respect—it is about the money. Climate change is bigger than American law. It's bigger than American courts, and it's bigger than decisions arbitrarily made; it needs to be discussed in that context before anybody writes a check. In order to write a check, of course, you have to have money in the bank. In order to have money in the bank, you have to make money. In order to hire people, you have to make money. Thank you.

HENRY N. BUTLER: All right, Jason, you have two minutes. You try to stop these guys. You have three minutes now, Jason.

JASON S. JOHNSTON: I'm going to not talk too much—I have three basic points: these interstate public nuisance actions are inefficient, they're anti-democratic, and they're counterproductive, ironically, for advocates of greenhouse gas emission reduction. There's a lot I could say about the science. I could maybe direct you later to a long monograph that I have online that attempts to cross examine the climate change science, and that monograph is cited in some of the ongoing litigation challenging EPA's endangerment finding. But I think what I'm going to do today is—given the thorough and expansive coverage of all the previous talks—I'll try to be brief and focus on a couple of points.

Really, the point that this litigation is anti-democratic, counterproductive, and not justified by the foundations of interstate public nuisance law: I want to clarify that at the outset. We are talking about a limited set of cases here. These are all interstate public nuisance cases. There are plaintiffs in some states suing defendants who, for the most part, are in other states. There is some overlap in some of the cases such as *Comer*[15] and *Kivalina*,[16] but generally, the interstate character of these public nuisance actions is very, very important. Why?

Just imagine this: an attorney general brings a public nuisance action—not interstate—against whom? Oil companies and other companies located only in that attorney general's state? We haven't seen that litigation, and I ask you, do you think we're going to see that litigation? You don't sue anybody else. You just bring an ordinary public nuisance action against emitters of greenhouse gases located only in your state, so the interstate character of these things is very important. There are a set of cases articulated by the Supreme Court a long, long time ago—not recently, or fairly recently that apply to interstate public nuisance. The point is, most of these cases involve an extensive amount of externalization of cost to "pol-

luters" that are located in states other than the states where the victims are located.

A great example is *Connecticut v. AEC*. The Supreme Court granted certiorari, as Rich mentioned, on that case yesterday. The defendants are a group of power companies; they provide power to states located in the South and the Midwest. The plaintiffs are a group of states. There is no overlap between the plaintiff states and the people served by the defendant power companies. That's perfect externalization. "Global warming," the plaintiff attorney general will say, "is a problem, but we're not going to sue our guys. We're going to sue people who provide coal based electricity in other states. So we're going to externalize all the costs of reducing greenhouse gas emissions to the people located in states other than ours."

Now, what's the problem with externalization across states? One: it's very likely that this is going to be an inefficient externalization. That is to say you come up with some award from the court, and the basic idea of economics is we use the liability system, to what? To internalize costs. If people bear the costs of their actions, they have an incentive then to take precautions or take various steps to lower the cost to other people of the actions that they take. The inefficiency of the externalization here is very, very likely. Why? Among other things, there are very real benefits from global warming that can be expected to benefit lots of states and lots of cities.

This is not fanciful. Matt Cohn—who is an economist at UCLA, is the gold standard basically of applied environmental economics—just published a book talking about how American cities are going to be gigantic beneficiaries in a global warming environment. Matt Cohn is as mainstream as it gets when it comes to environmental economics. North Dakota, South Dakota, Minnesota—all kinds of places—could expect increases in agricultural productivity. Any time there are beneficiaries, they're not at the table.

States that think they're going to be beneficiaries, or think that they're going to be real net losers from greenhouse gas emission reduction—because they're states where a lot of electricity comes from burning coal and/or they mine and produce coal in those states—those states are not at the table in these litigations either. There are a lot of benefits and costs that are not included in this dyadic interstate public nuisance litigation. They're almost sure to generate inefficient results. Another reason why they're sure to generate inefficient results is because the benefit of any litigation depends upon the remedy affecting behavior, and behavior affecting the harm that people suffer.

It's simply a fact that by 2020, China is going to be responsible—forget about India and Brazil—for about 45% of the world's greenhouse gas emission reduction. So, there's no remedy in any of these cases that will provide any relief to any of the plaintiffs—except if you think, as in *Comer* and *Kivalina*, that these are appropriate situations for what, for a

damage remedy. Give damages to people for the harm that they allegedly have already suffered due to global warming; and the defendants being sued, of course, have been to some extent, contributors allegedly to the greenhouse gas emission build up in the atmosphere that's caused this global warming problem.

So the problem with *Kivalina* and *Comer*: you could say, "Gosh, they're the plaintiffs that are going to get a remedy. They're going to get money if they're successful." There are a bunch of defendants in *Kivalina*, for example, but one of them is not China National Petroleum. They didn't sue China National Petroleum. What are we going to get out of *Kivalina* and *Comer*? This is to pick up on a theme that Joe just articulated. We're going to get cost imposition, if these cases are successful: the imposition of some kind of costs and damages on not entirely American companies. I believe BP was also sued and Kivalina and Shell.

But we're going to primarily concentrate costs on American companies, which is a great thing to do in terms of what, international competitiveness? We are now—in my opinion, and I'm trying to show this empirically—beginning to see the effects of twenty to thirty years of the explosion in American tort liability in a very real sense, which is we don't compete. It's affected American companies' costs. We do not compete any longer, effectively, on the international stage. The tort system in its position of liability on American firms is a reason for that. If you impose costs on American firms, but not on Chinese firms, you exacerbate a problem that is basically a catastrophic problem for the United States.

You can't have a situation in which we import more, and more, and more from a low-cost country, which is China, and then borrow from it—this is not sustainable. The tort system has made a profound contribution, a significant contribution in my opinion, to this. But you could say to yourself, "Who cares if this is efficient or not efficient—the kind of externalization, the kind of cost shifting that you get out of these interstate public nuisance cases." Well, maybe you don't care about efficiency. I think you should care about democracy. We live in a democracy. China is not a democracy. This is an incredibly important point, of course, for Americans to realize, which they don't seem to usually realize.

Does the efficiency of interstate cross externalization even matter? You might say, "No, I don't care." Well, the problem with these cases is worse in a sense. How are we supposed to deal in a democracy with the problem of alleged harm caused by greenhouse gas emissions through the democratic process in Congress? How would that process work? I don't know exactly. Nobody knows exactly. There's no political scientist even, who can give you an exact answer to that; but it would surely be the outcome of a bargaining process in which members of Congress more or less represent the preferences of the median voters in their states or jurisdictions.

Some states think they're going to be big winners from greenhouse gas emission reduction. California, for example, where they've almost bet the state vote on greenhouse gas emission reduction, and it's a sinking boat. And there are states—West Virginia, Wyoming, probably Indiana, maybe a large number of other states—who think, "Well, we don't think that we would gain that much from greenhouse gas emission reduction, unless we get a lot of other stuff thrown into any bill that would allegedly accomplish greenhouse gas emission reduction." So what is it? It's a bargain. It probably wouldn't be an efficient result. There's nothing that says that the deals that emerge from Congress are efficient.

But they're democratic. The important point for present purposes, is the deal that you would expect that would emerge from Congress; if you look at Waxman, for example, a bill that now will never be reintroduced again for a very, very long time, maybe never. But that gives you an example of what emerges from Congress. It's a lot different than what you get from these interstate public nuisance cases that are cooking along. So in that sense, it's profoundly antidemocratic. You're going to get courts, federal courts, issuing injunctions or assessing damages. Either way, they're generating outcomes, which are going to be very different than anything you would ever expect to emerge from a democratically elected Congress.

I'll conclude with a couple of points. None of this is actually consistent with the doctrine. That these cases exist in the first place or would end up in plaintiff victories only occur through a very ahistorical and blinded reading of the interstate public nuisances cases. Generally, the Supreme Court has said that this is a matter of federal common law, by the way. Interstate nuisance is federal common law. There is not a lot of federal common law. Why is there not a lot of federal common law? Because the Court said things like this: you have a question of federal common law emerge only when the Court is compelled to consider this, and the question cannot be answered from federal statute alone.

It's compelled. The Court has to act. Well, there was a time when the Supreme Court thought they had to act in these intestate public nuisance cases 100 years ago; these two most important cases, *Georgia v. Tennessee Copper Company*[17] and *Missouri v. Illinois*.[18] Those cases are over 100 years old. That's forty years after the Civil War. Justice Holmes wrote those opinions. In both of those opinions, he talks about the states relinquishing some aspects of sovereignty, and he also says we have to step in here and resolve these interstate public nuisance disputes because we don't want what? We don't want the states to go to war with one another. People today tend to think this was just what, metaphorical? It wasn't metaphorical.

He was wounded seven times in the Civil War; Justice Holmes was. The Civil War was a reality. Also, what was true 100 years ago about the perceived extent of potential constitutional authority of the federal government to regulate—very, very limited compared to today, right? Holmes

himself in one of these opinions stated, it's a very real question about whether the federal government could—that is to say Congress could—do anything in this area, so we have to act. That is to say the Supreme Court is saying they've got to get involved in this dispute between Missouri and Illinois over what the City of Chicago is doing with its sewage because there's nobody else.

That's not true today. As you all know, Congress's power is generally understood to be very, very broad, perhaps not unlimited, but very broad. So Congress can act, and Congress has acted. I could say more about these cases, but I'm going to try to stay within my time limit. The other thing Justice Holmes said very quickly is he said a precondition of interstate nuisance liability is what? Symmetry. No state gets to sue another state unless they're not doing the same thing, if they complain about what the defendant state is doing. In all of these cases involving interstate public nuisance where you have state attorney generals as plaintiffs, that simple test would basically doom all these lawsuits.

Finally, what's going to happen? Who knows what's going to happen at the Supreme Court level. But these are likely to be very ineffective and counterproductive. Remember, for a lot of environmental groups, the reason for bringing these interstate public nuisance cases is they thought they were going to force Congress to act. Well, Congress didn't act. There's not going to be any federal greenhouse gas cap and trade legislation at least for the next two years—most people I know in the environmental community would say for the next six years. So that didn't happen.

It just didn't work if that was the goal. What has happened? Well, we got this regulatory program under the Clean Air Act, which the Supreme Court in *Massachusetts v. EPA*, in one of Justice Stevens's final departing acts, decided that they had to do. So we have regulation. The EPA is proposing to regulate all big stationary sources of greenhouse gas emissions. The EPA has already done what? Regulating greenhouse gas tailpipe emissions from automobiles by promulgating new, tougher cap based standard. We've got a pretty comprehensive regulatory program; even though, in my opinion and the opinion of other people, I think there are aspects of the Clean Air Act Regulatory Program that are illegal.

But we have it. Given that, it doesn't seem like however you interpret the law of interstate public nuisance, there can be an argument that this is an area where the Supreme Court is compelled to articulate federal common law. So that's that.

HENRY N. BUTLER: Thank you, Jason. We're going to jump to Eric right now who I imagine has a little bit of response to this. Then we'll go with Rich Faulk who has got a professorial hat response, he says, here for a moment.

ERIC MAYER: I'll say a couple of things. Obviously, I have some disagreement. The thing I think that is something that we ought to stop and talk about is this: most of you are judges. There's a comment that several of the speakers have made that this is undemocratic. That I disagree with because the highest decision of the courts in this country is part of the democracy. When we have disputes in this society, we turn to judges to help resolve them. Now, he may not like what Justice Stevens wrote in a 5–4 majority opinion, but he should not lose sight of the fact that there are five U.S. Supreme Court justices that signed that opinion. That is democracy.

I think it's impugning the system to suggest that. That is why society today is so adversarial, because while I disagree, I may not like the fact they took the certiorari petition in the case that they did on Monday. But whatever decision comes out of that Court is democracy. It is democracy. The fact that Exxon may not like that the cost of creating greenhouse gases is going to be more spread about in this country because concepts of tort law say that somebody who is not responsible for the damage, who has a remedy under public nuisance law, can collect some of that, is democratic.

That's what this country was founded on. I do find it improper to suggest that any ruling by the Supreme Court is undemocratic. It may not make economic sense, and the speaker may feel that it's not justified under his view of economics, but it is the essence of democracy in this country. What separates this country from other countries is that somebody like Kivalina can use the Court system to address inequities that it perceives exist and do so within the framework of democracy. So, I do think it is an incorrect assumption to say that the evolution of tort law is undemocratic.

The cases that we cite are old. Some of them are more recent. But they are dealing with societal issues of how we balance the rights of one group of people versus another. That's what this is all about. Should the companies that generate greenhouse gases and their shareholders have the money without bearing any of the burdens? Should they be required to share some of the burdens? Is that fair? Now, economically, it may not be fair, and there are problems with assessing blame and holding people responsible and figuring out a rational form of damages. But I would submit to you that as judges, that is precisely why you are in the positions you are, because we as a society need that type of resolution.

HENRY N. BUTLER: Okay. Eric. Why don't you stay there. Jason, you want to respond to that?

JASON S. JOHNSTON: Just to clarify, I was not criticizing *Massachusetts v. EPA* as undemocratic or anti-democratic. That was a case in which the Supreme Court interpreted the Clean Air Act, which is clearly what the job of the Court is to do. I disagree with the decision. I think it's wrong, but I didn't mean to say it's anti-democratic. The conflict between outcomes in court and outcomes in Congress that I did call antidemocratic is between

the outcome and a lawsuit articulating federal common law where you have appointed, unelected, federal judges determining the outcome of global warming policy, and I compared that with the outcome that you would get in Congress.

There, it does seem to me it's fair to say that there's a conflict between democracy and the outcome of a democratic legislative body and what a federal court might come up with under the federal common law of interstate public nuisance. I think, when you look at—we don't have very many, as Mr. Mayer said of these interstate public nuisance cases—but when you look at some of the more recent ones, Justice Rehnquist's opinion in the second *Illinois v. Milwaukee*[19] opinion, you see a very profound concern on his part with precisely the relationship between the courts and Congress and great, great, deference and great recognition to the fact that if Congress has authority to regulate in an area and has regulated, the Court really, really has to respect that and has told the regulatory agency that. So that's just to clarify.

ERIC MAYER: The last point is the China point because the China point was made by the EPA. The EPA said the same thing in *Massachusetts v. EPA*. They said, "Why should we regulate greenhouse gases? I mean, it's so insignificant. The U.S. has nothing." China is really the ones that are doing the pollution, and it comes up in the question of redressability because you can't have standing to pursue a claim if there's no redressing. In other words, if the Court acts, and it doesn't address your problem, then that's a standing issue. The Supreme Court said on this very issue, "While it may be true that regulating motor vehicle emissions will not by itself reverse global warming, it by no means follows that we lack jurisdiction to decide whether the EPA has the duty to take the steps to slow or to reduce it."

Plaintiffs satisfy the redressability requirement when he shows that a favorable decision will relieve a discreet injury to himself. He need not show that a favorable decision will relieve his every injury. Because of the enormity of the potential consequences associated with manmade climate change, the fact that the effectiveness of the remedy might be delayed during a relatively short time it takes for the new motor vehicle fleet to replace an older one is irrelevant. Now, here's the part about China: nor is it dispositive that developing countries such as China and India are poised to increase greenhouse gas emissions substantially over the next century.

A reduction in domestic emissions would slow the pace of global emission increases no matter what else happens elsewhere. The point being that it's not sufficient to argue that it would be completely irrelevant, and we should do nothing because other countries are doing things that may end up resulting in more harm. The Supreme Court's point—and I admit; this was a case dealing with the EPA's refusal to regulate, not a public damages lawsuit. But the point I think the Supreme Court is making is that the fact

that it may only be a baby step or the fact that others maybe doing things—yes, that's significant, but it's not a reason for not acting.

I would submit to you that in the great mix of judicial decisions, that's one aspect the judges will be weighing. But, it has to go to maybe apportionment of damages or how much you would be entitled to recover from the actor you did sue.

HENRY N. BUTLER: Thank you, Eric. We're going to turn it over to Rich for a little bit, and then we'll have time for a question or two.

RICHARD O. FAULK: When I got out of law school, I went to work for a court as a law clerk. I know a bunch of people have done that. In my youth, I was always eager for the court to decide every great issue that came before it. I used to get into arguments with the judges about, "Why don't you reach out and decide this question. It's right here in front of you."

The Chief Justice—who had been a judge longer than I've been a lawyer now—used to look at me, and then he would say: "Rich, one of the things you learn when you sit on the bench is that you don't decide anything that you don't have to decide. You get into trouble when you start answering questions that you don't have to decide, that aren't truly presented to you—questions that you really don't have to reach on the merits." I suspect that all of you, one way or another, have had a little bit of that wisdom creep into your experience.

Now, why did I say that? Well, it dovetails into what I told the Supreme Court in the brief that we filed. This issue, in my view, is a question of jurisprudence. There's "juris," which is law, and "prudence," which is what is the right and prudent thing to do.

So as a matter of jurisprudence, I believe we should recall a statement that Justice Cardozo wrote way back at the turn of the twentieth century.

He wrote that the common law moves in a "molar and molecular" fashion. What in the world is he talking about? Well, he's saying that the common law chews on things for a while. It thinks about things for a while. It savors issues for a while before it really swallows them whole. The issue that we have here is just that. When we talk about "political" questions, or "standing" questions, we're really asking, as a matter of prudence, whether courts should decide these issues. Should you weigh into this controversy? Even though courts are a part of our democratic institutions, is this something that a court should prudently do?

That's the argument here. I think it's really common judicial sense, if I can be so bold. I've learned that the greatest candor an advocate owes a judge is to honestly tell a judge when a case should be decided and when an issue should not be decided. The issue of climate change litigation requires that kind of candor.

So, I guess if I have to sum it up in a professorial sort of way, I still talk as an advocate, and I say you don't have to swallow it. You can chew on it for a while, but you don't have to swallow it.

HENRY N. BUTLER: Thank you. And Eric is going to close with a prediction for us.

ERIC MAYER: My prediction is that the Supreme Court will probably do an end to the public nuisance arena because the Obama Administration is now interested in having this area regulated. I think if you look at the cases, you'll see that if there's regulation, then the law seems to suggest there's no place for a public common law nuisance, but we'll see.

HENRY N. BUTLER: Well, please join me in thanking the panel.

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1 *See* Am. Elec. Power Co. v. Connecticut, 582 F.3d 309 (2d Cir. 2009), *cert. granted*, 79 U.S.L.W. 3092 (U.S. Dec. 6, 2010) (No. 10-174).

2 Regulating Greenhouse Gases Under the Clean Air Act, 73 Fed. Reg. 44354 (proposed July 30, 2008) (ANPR).

3 *See* Native Village of Kivalina v. ExxonMobile Corp., 663 F. Supp. 2d 863 (N.D. Cal. 2009).

4 *See* Missouri v. Illinois, 180 U.S. 208 (1901); Illinois v. Milwaukee, 406 U.S. 91 (1972).

5 *See* Georgia v. Tenn. Copper Co., 206 U.S. 230 (1907).

6 *See* Massachusetts v. EPA, 549 U.S. 497 (2007).

7 RESTATEMENT (SECOND) OF TORTS §829(a) (1979).

8 *See* Jost v. Dairyland Power Coop., 172 N.W.2d 647 (Wis. 1970).

9 *See* Oklahoma v. Tyson Foods, Inc., 237 F.R.D. 679 (N.D. Okla. 2006).

10 *See* Illinois v Milwaukee, 406 U.S. 91 (1972).

11 Boim v. Holy Land Found. For Relief & Dev., 549 F.3d 685, 696-97 (2008).

12 RESTATEMENT (THIRD) OF TORTS, Liability for Physical and Emotional Harm, §36 (2005).

13 Stuart Altschuler, *Government by 'Privateer' – Usurping Regulatory Power Through Mass Tort Litigation*, 42 FOR THE DEF. 9, Sept. 2000 at 37.

14 *See* North Carolina v. Tenn. Valley Auth., 615 F.3d 291 (2010).

15 *See* Comer v. Murphy Oil USA, Inc., No. 1:05-CV-436-LG-RHW, 2007 WL 6942285 (S.D. Miss. Aug. 30, 2007), *rev'd*, 585 F.3d 855 (5th Cir. 2009), *appeal dismissed*, 607 F.3d 1049 (5th Cir. 2010).

16 *See* Kivalina v. ExxonMobil Corp., 663 F. Supp. 2d 863 (N.D. Cal. 2009).

17 *See* Georgia v. Tenn. Copper Co., 206 U.S. 230 (1907).

18 *See* Missouri v. Illinois, 200 U.S. 496 (1906).

19 *See* Milwaukee v. Illinois & Michigan, 451 U.S. 304 (1981).

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5TH ANNUAL JUDICIAL SYMPOSIUM ON CIVIL JUSTICE ISSUES
GEORGE MASON JUDICIAL EDUCATION PROGRAM
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EDITED TRANSCRIPTS

THE BALANCING OF MARKETS, LITIGATION AND REGULATION

Keith N. Hylton, Larry E. Ribstein, Paul H. Rubin, Todd J. Zywicki
Moderator: Geoffrey J. Lysaught

GEOFFREY J. LYSAUGHT: Good morning, as I am sure most of you are probably aware, in addition to judicial education programs that the Law and Economics Center conducts, we also have a division that focuses on public policy research, known as the Searle Civil Justice Institute. In November, we held a public policy roundtable where we commissioned a variety of research and brought together a group of experts, both academic and practitioner experts, to discuss the issue of balancing the appropriate roles of markets, litigation, and regulation. And the notion there is that each one—markets, litigation, and regulation—can and probably should play a role in addressing various consumer harms.

You might expect that as institutions, they have various strengths and weaknesses in pursing that mission of addressing particular consumer harms. So, the question is: what are the appropriate roles of markets, litigation, and regulation? If they do have institutional competencies, should we have an expectation that they would work in a somewhat coordinated fashion, in an efficient and effective manner together? And if that were a reasonable hypothesis, why is it that at least observationally it looks like there is overlap, contradiction, and confusion produced by our litigation, regulation, and market systems?

Each of the individuals on this panel were participants in that public policy roundtable. We thought that this would be an interesting dialogue to share with all of you in your practices. So, on our panel today, we have Paul Rubin, who is a Professor of Economics at Emory University, Larry Ribstein, who is a Professor of Law from the University of Illinois, Keith Hylton, who is a Professor of Law from Boston University, and Todd Zywicki, who is a Professor of Law at George Mason University. Without further ado, I will hand it over to Paul Rubin.

PAUL H. RUBIN: I am an economist. So, I start with markets, by looking at safety and looking at various ways of achieving it. And of course, the three ways that is addressed are regulation, both common and tort law litigation, and markets. And two of them are very visible; tort law and regulation are very visible. Markets are less visible, but in fact, markets are probably the strongest force for safety that we actually have in an economy such as ours. People want safety, and as people get richer, they want more safety, and markets are in the business of providing what people want.

So, as people get richer and want more safety, lo and behold, markets provide more safety independently of any of the other forces. As long as

markets work well, they provide a good deal of safety. I provide some evidence in my paper. For example, if we look at the relation between income and safety—safety measured by accidental death rates—we find that both for the U.S. over time and across the world, as incomes go up, accidental death rates go down. A robust relationship, both statistically significant and economically significant, which leads to a substantial reduction—an increase in incomes leads to a substantial reduction in accidental death rates. There is more direct evidence.

Many people look at what is called a statistical value of life, and the way that economists measure that is to look at various jobs, look at the risks associated with that job, and see what happens to wages as the risk of injury or death goes up. It is universally found that as risks go up, wages go up. People demand compensation for accepting risks. The numbers are in the $3 million to $5 million range. In fact, I was chief economist at the Consumer Product Safety Commission a while ago; that agency and many other agencies use those numbers routinely in deciding on levels of safety.

But the point I want to make now is that there is a market there. As risks go up, people demand higher pay, which of course creates incentives for employers to make workplaces safer, and that is what we observe over time. Workplaces have become safer because people demand more safety. Products have become safer. Cars have become safer. Again, mostly because people demand more safety, and many studies have looked at things like accidental death rates over time, and they have thrown in creation of agencies such as the National Highway Traffic Safety Administration (NHTSA), and the Consumer Product Safety Commission (CPSC), and you really do not see any breaking point in the data from those agencies. Death rates go down as incomes go up, and it has been that way for as long as we can measure.

Then in the paper I provide a little anecdotal evidence about particular products. But again, the point about markets is we do not see them. They work subtly, but they work all the time. I mentioned something called ground fault circuit interrupters (GFCI). You probably know them as those little boxes in your bathroom that occasionally you have to push the button or your toothbrush will not work; but those are an important safety device. They have been around for about thirty or forty years, now. Over time, they have continually been modified, and continually been changed.

Originally, they were used for swimming pools. Now, they are used for almost all places where water and electricity are near each other; just recently, for wet bars in homes. This has happened almost entirely through a market process, one you do not see. Many of the GFCIs are hidden; you can see the one in your bathroom, but you do not see the other ones that may be somewhere else in your house, but they have been increased. The sophistication has been increased through a market process, through a function of the market, adopted into the National Electric Code, which then, is often mandated by law in states.

But the point is that the actual improvement has happened through the market, not obviously, but in a way that is not seen by the very important group I work with, the CPSC; a good part of what that agency does is deal with voluntary standards organizations, which are mainly made up of representatives of industry, and continually looking for new ways to improve safety. As I say, a subtle process, one that is not seen, but one that is very important. So, markets are very important. We see them when they fail.

When there is a market failure—when cars roll over when they should not or when there is a dangerous drug—then we see that markets are not working, and we have a tendency to say, "Let's do something about it. We have to regulate this. We have to control it." But most of the time, markets do work, and they work subtly, and we do not see them. It is only when they stop working that we may see them. Now, there are some times when markets will not work, and there are two basic conditions when markets will not provide the optimal amount of safety.

One of them is when there are third party effects: when my decision affects your risk. In the modern U.S. economy, an important example is automobiles. If I have a safe car, you are safer. If I have an unsafe car, in certain ways, if I don't have a good braking system or a good lighting system, I can impose risks on third parties, but I do not have any incentive to take account of those risks. So, when I am deciding how safe a car to buy, I consider myself and my family and people maybe in the car with me, but I do not consider fully the effects of safety on others. And that is where the role for some non-market system comes in.

The most important non-market system, of course, is the tort system, which regulates—along with traffic laws, and insurance, and so forth—but the tort system also has an important role in regulating third-party safety events between strangers, between people with no contractual relations. We also regulate more directly through NHTSA. NHTSA regulates both third-party effects and non-third party effects. They do not seem to differentiate, as they regulate internal car safety as well as external safety. But that is a case where you need something besides a market where there are third-party effects.

You need something besides a market. At CPSC where I used to work, most of the products we dealt with were individual risk, but some were third-party risks; things like fires can affect third parties. So, there is a stronger case for regulating fire safety, perhaps more so for other things that CPSC regulates. But not much regulation is involved with third-party risks. Much of tort law, as we will see, is not involved with third-party events.

The other case where markets may not work is information. If people do not know about risks, then the market may not provide the optimal level of safety. The way the markets are effective is that people are less likely to know about risks because many, many risks we face in today's world are very, very small. CPSC has regulated very small risks. Some big risks too: automobiles were risky, cigarettes of course, and swimming pools. But

most of the risks were quite small and because they are small, people may not learn about them.

So, there may be a case for some sort of third-party regulation, but again, whether that is beneficial or not beneficial is a question I will try to address. But we start with markets. They are a good first step for creating safety. We will mainly do something else when markets may not work, and they may not work for third-party effects or because of information. On the other hand, information is a tricky thing. The example that has been most carefully studied by economists and others is the Food and Drug Administration (FDA), which regulates the safety of new drugs. And the consensus among scholars who have studied the FDA is that it overregulates in the sense that it creates too much safety.

Now, how can there be too much safety? Well, think of some new drug that can cure a disease. If the drug takes five years to get to market instead of taking three years, then those extra two years, people suffer from the disease. So, there is a trade-off between the risk of the drug and the risk of the disease. I do not know of any studies where it was not invariably found that the FDA errs on the side of too much safety. Our life expectancy is probably a little bit shorter because the FDA does not allow quite enough new drugs to be sold. Why does it do that? Well, the politics is very clear.

If a drug would save your life, but it is not sold, you probably do not know about it, and so no one has any reason to complain. If a drug is sold that harms someone, there are Congressional hearings, the FDA is blamed, people ask, "Why did you allow that drug? Why didn't you provide more safety?" The result is a very clear political pressure for the FDA to overregulate, and I think that is also due to an information failure. On the one side, you think, "Well, if drugs were sold that were not regulated, people would not have information about them, and too many would be sold." On the other side though, people do not have information about drugs that are not sold.

So, the FDA does not worry about the effects of not selling a drug. Rather, they worry about the effects of selling too many drugs, and so they tend to overregulate with respect to safety. That is probably most severe at the FDA. Among other things, the FDA has more prior approval authority. Mostly CPSC dealt with stuff after it was sold, but at the FDA for example, you have to have a drug approved, and there is a good deal of evidence that it does overregulate. I am always amazed, if you talk to the FDA, and you say, "Well, my grandmother took this medicine and it really cured her. Why don't you approve it?" They will say, "That is an anecdote. There is no data there. We rely on science. We are a scientific agency. We do not care about anecdotes." If you turn it around and say, "What good have you done?" They immediately talk anecdotes. They talk about, "Well, we kept this drug off the market. We kept that drug off the market."

I have never seen any FDA publication that actually looked at the evidence of the effectiveness of the FDA itself. Even though there is lots of

research on it, the FDA seems to ignore that and only talk anecdotally about the good they have done.

Let me get to tort law, which is probably of more interest to you than the others. Again, tort law with the respect to strangers and automobile accidents, makes good sense. Much of modern American tort law, as you know, deals with non-stranger situations: product liability, medical malpractice, or both; situations where people are not strangers, where conceivably, they could contract with each other, they could arrange what terms would govern in the event of an accident. In particular, for malpractice and product liability with respect to drugs, are two things I have written about. For both of these there is a trade-off—better care versus more care—because malpractice and liability for malpractice increases the cost of medical care.

The result is some people buy less of it. Similarly with drugs, you increase the price, some people buy fewer drugs. Fewer drugs are developed. There is a real trade-off between more drugs and safer drugs, more medical care and safer medical care. In the paper I wrote a couple of years ago with a colleague, we found that on the margin, in the U.S., we probably erred too far in the direction of liability.

We looked at all the states over a twenty-five year period, and we looked at accident rates and accidental death rates as a function of tort reform, and we found that tort reform—which is to say, reduction of damage payments, damage caps, things like that—actually led to fewer accidental deaths. In other words, by reforming the tort system, by cutting back on the scope of liability, fewer people were killed probably because more doctors were available in emergency rooms, and the result was better treatment and fewer deaths.

In terms of the relationship, one issue that was just litigated in two cases before the Supreme Court, is preemption: whether FDA approval preempts state tort law in the case of medical products. The Supreme Court ruled that there *was* preemption in the case of medical devices. They ruled there was *not* preemption for drugs in a recent case.

In my view, since both the tort system and the regulatory system have an incentive to overregulate if we put the two of them together, we are going to get even more overregulation, fewer new drugs, more expensive new drugs, and probably on net, make consumers less healthy than they would be if there were preemption, if the FDA did preempt state tort law.

GEOFFREY J. LYSAUGHT: That is very interesting. Larry?

LARRY E. RIBSTEIN: I am going to talk about preemption. This is based on an article that I am doing with Erin O'Hara at Vanderbilt University. It comes out of our book that we published about a year and a half ago, which I highly recommend to all of you, called, "The Law Market." In it we envision law as being virtually traded, in a kind of market. The federal courts

and Congress act as a kind of umpire or referee in this market. This is where we get to preemption.

Sometimes it seems like the court system is making ad hoc decisions. Yesterday, J.W. Verret was talking about Dodd-Frank, and he made some judgments that I happen to agree with about Dodd-Frank, which is that Dodd-Frank preempted when it should not have, and it did not preempt when it should have. I sense that that is true, but I would like to come up with some kind of theory about when the courts should preempt and when they should not.

To some extent, this obviously depends on Congressional intent. You are going to be looking at Congress for some expression of when a law should be preempted. That expression is not always there, so we need a gap-filler. The gap-filler that I am talking about here is based on Constitutional norms about what Congress should be doing. We may not know what Congress explicitly intended to do in a given case. So, maybe we could fill in the gap by asking what Congress should have been doing under the Constitution when it enacted the law.

The answer is that Congress serves a coordinating role in the law market. I see two kinds of coordination problems: horizontal coordination, and vertical coordination.

Horizontal coordination is coordination among the states. You can see two kinds of horizontal coordination problems. One deals with what I would call positive spillovers: when a state enacts a law that has effects in other states. So, a state enacts or decides a tort case in a way that has implications for the manufacturer and sale of that product all over the country.

State laws also theoretically can have negative spillover effects, which comes about because of choice of law rules. A choice of law rule makes a state law effective in another state in a way that causes deregulation in the other state. Corporate law is an example of this because of the internal affairs doctrine, which causes Delaware law to apply to corporations all over the country. I am not going to worry about that kind of negative spillover effect because whether any state's law applies in another state is up to that other state.

Then, you have a vertical coordination problem, the other kind of coordination problem that I am talking about, which is state versus federal. The federal government wants to limit the positive spillover problems among the states. On the other hand, if the federal government goes too far and shuts down the law market too much, then it is imposing a top-down solution that reduces the benefits that we get from having multiple states. Multiple states give parties the opportunity to escape bad laws and make it possible for different states to have different laws that are appropriate for different parts of the country. So, we have to coordinate states versus the federal government.

Our point with respect to preemption is that it addresses both kinds of coordination problems. In other words, it helps achieve horizontal coordi-

nation of the states getting too unruly and without getting into a vertical coordination problem of the federal government oppressing state variation. That is what we are trying to achieve with our preemption rule.

Again, Congress can decide whether to give the law a particular kind of preemptive effect. The problem is that Congress does not usually focus on the exact preemptive effect that its laws are supposed to have. So there are gaps in the law about what Congress intends in terms of the scope of preemption. When you look at the preemption cases, as I have done to some extent, you see a mess because the question is, when are the courts actually applying Congressional intent and when are they filling in the gaps with policy arguments? If they are filling in the gaps with policy arguments, is this an appropriate role for the courts, or should they be deciding preemption strictly on Congressional intent? Then again, you have the gaps there that somebody has to fill. So how do you fill these gaps?

I am going to Constitutional norms to figure out what Congress should have been doing when it adopted the law. Erin and I think that what Congress should have been doing is playing a coordination role. That is what the Commerce Clause is all about, which is one of the key Constitutional provisions that Congress is acting under in preemption cases, along with, rarely, Full Faith and Credit. These Constitutional provisions, under which Congress is enacting the laws that are being given preemptive effect, involve some kind of coordination function.

Again, the question is, how do we help Congress achieve this coordination function by deciding to what extent the laws have preemptive effect? Our basic approach is that preemption decisions should reflect the need for coordination. But we are not excluding other policies.

We also take several considerations into account in deciding when coordination needs to be achieved. One factor the court should be looking at is, do we need to coordinate the states? Maybe the states have already coordinated. Maybe they have adopted a uniform law.

But sometimes we are going to preempt even when the states have already coordinated when it is a bad kind of coordination. For example, all of the state attorneys general can get together and decide the states are all going to adopt a similar policy, and maybe that policy has perverse or adverse public policy consequences that Congress was concerned about.

One other consideration here is that the amount of coordination we want under the federal law depends on the type of federal law. So, if we are talking about the federal law imposing federal policy on the states, we are going to demand less evidence that coordination is necessary because that is a bottom-up and not a top-down solution. We are not talking about necessarily imposing federal policy if the federal policy we are talking about is something like arbitration or choice of law.

Let me give you two examples, which are really drawn from the kind of issues we were talking about yesterday on the Dodd-Frank panel. Corporate law is a situation which the states have already coordinated and they

have done a pretty good job of coordinating. We do not get the positive spillovers that I was talking about. By deciding which corporations they are going to charter, states are not interfering with other states. So, that situation, we do not need the federal government to step in and impose a solution on the states. We would say be careful about preempting there and only preempt when Congress has made it explicit that it wants to preempt state law.

On the other hand, where the states have been unruly is in cases involving consumer and tort law. There are several preemption cases on the Supreme Court this term particularly involving national standards and tort law. Those are situations for which we really need national coordination. So we would say, "Presume in favor of preemption in those situations."

In summary, presume against preemption where the states have already coordinated, as through a choice of law or arbitration rule. But presume in favor of preemption in situations where the states have not coordinated, where they refuse to impose national standards, where the states are imposing their own rules on other states. Thank you.

GEOFFREY J. LYSAUGHT: Mr. Hylton.

KEITH N. HYLTON: Thanks. Following up on what Larry said, I am not as confident that I could articulate a general theory of preemption. I think Larry is dealing with a different set of cases than I am dealing with, so maybe it is possible to do it for his set of cases. I would rather think of preemption in terms of specific problems that come before courts. And so, the specific area that I want to take a look at is product liability litigation.

Maybe it is the most important area of preemption because you have so much money invested into designing products and into the regulatory process. So, here is an area of preemption where certainly the decisions matter a lot and there is a whole lot at stake. What I want to do in this talk is try to accomplish two things. One is to provide an economic theory of preemption as a choice between regulatory regimes trying to choose the best regulatory regime. And the second is to extrapolate from this regulatory choice model to look at implications for some of the broader controversies about preemption.

Preemption is a topic that begins with fairly concrete problems, especially the products liability area, and then, expands from there into all sorts of questions about the relationship between state and federal power. And there is a large amount of literature now that looks at general preemption issues in terms of these conflicts between state and federal power. And what I want to suggest is that the practical work of the preemption doctrine can be done sort of independently of this whole business about the relationship between state and federal power. So, I wanted to make some reflections on that before I wrap it up.

The concrete problem that I am thinking about is, say, something like a medical product whose design is challenged in a products liability lawsuit. What typically happens is the manufacturer comes in and says, "Well, the design of this product has been approved by the FDA under the medical devices act, so the plaintiff's lawsuit is preempted. There is no point in considering this question." The court's choice in these cases is, in essence, a choice between two regulatory regimes, two regulators.

Either the FDA regulates the design, or the court gets to regulate the design, or common law courts get to regulate the design, and gets to decide independently on the design of the product or at least reconsider these design questions in addition to the FDA's choices. So, how do you choose? How do you decide between two regulatory regimes? What's the best regulator? Well, you have to figure out what you are getting out of regulation. What are you getting out of the design regulation? Well one, you are hopefully getting some reduction in the injuries to consumers of this product.

But it is not just that, that you are worried about, because if you choose a safer design, you are also foregoing the utility of this relatively risky design, assuming that it has some additional utility. And so, products liability law has generated a risk utility test to trade off these two, weigh these different trade offs in any product design case. In a sense, the risk utility test is an effort to look at the net consumer welfare impact of a regulatory standard governing design.

The second question is the cost of compliance. How much does it cost to comply with this regulatory order? Because the net benefits of regulation would be the benefits from the change in design, then subtract away the compliance cost on the regulator firms, and then the third component would be the administrative costs of the regulatory regime and the risk connected to the regulatory regime. So, you could have a regulator that is very good in terms of the design issues, in terms of minimizing compliance cost, but the administrative costs of running this regulatory regime are so high that it swamps all of the benefits that you get out of regulation, or the risk is so great that it swamps the benefits.

There is an objective function that goes behind the choice between regulatory regimes. It is looking at the net benefit to consumers minus compliance cost or net benefits to society, if you want to, minus the compliance cost, minus the administrative costs, minus the risk that is imposed by the regulatory regime. So, in a sense, if you wanted to think about the economics of choosing regulatory regimes, those are the fundamental components in that choice.

The most important one is the net benefit, which I have described as the consumer welfare differential. The consumer welfare differential that results from regulation: to what extent does the regulation lead to a reduction in risk which completely offsets any reduction in utility? To what extent does the risk utility test come out in favor of regulation? So, there are a bunch of factors that go into looking at the first component. One is the ex-

pertise of the two regulators, whether it is the court or the FDA, and here, it is often an obvious choice in those cases.

Very often, the regulator, the FDA for example, has experts who are in a much better position to examine and to evaluate this consumer welfare differential than a court, which consists of having a jury look at these things. So, the expertise factor often weighs in favor of preemption; that is, in favor of winning the regulatory regime, the federal regulator makes the decision on product design. But then, there are other factors as well. One is the extent to which local information is important in deciding the optimal design choice or what's best for society, and there are some cases in which local information is important.

Take for example, a nuisance case, in which some federal regulatory regime has asserted that it can preempt certain kinds of nuisance claims. Well nuisance claims are, at least in the common law, very heavily influenced by local factors, and it is highly unlikely that any regulatory regime in D.C. can make a general decision on local factors on how a court should weigh or consider local factors. So, that will cut against preemption.

The third factor is political independence, or the degree to which the regulatory regime is vulnerable to capture bias from pressure groups. This is something in which courts are in a pretty unique position, as they are able to look over the shoulders of the regulatory regime and say whether it seems to be vulnerable to bias or distorted decision making. We have seen examples of that in certain cases, in *Wyeth v. Levine*,[1] the court looked at the FDA's own statements about the preemptive effects of its regulation and said, "Well, we do not think we are going to trust those statements because they do not appear to be objective and reliable." And then, you have other cases.

One famous one is *Wilson v. Bradlees*[2] in the First Circuit in 1996, where Judge Boudin looked at the regulatory process in that case and said, "Well, it seems to me that the industry is written the relevant regulations, and they were written independently by the regulatory agency and that was the basis on which they chose not to preempt in that case." So, there are cases out there in which courts are in a position to examine the regulatory process itself, in terms of its independence, or in terms of its vulnerability to bias.

The compliance cost factor. It is a little more complicated in the products liability case because, in looking at this consumer welfare differential, you are actually taking compliance cost into account. And so, the only other compliance cost to consider would be the loss in profits from being forced to choose a safer design; that is not explicitly part of the legal standard, nor is it explicitly part of the regulatory process. In theory, it ought to be, but there are many reasons why maybe it should not be in practice: one is a difficulty of actually getting objective information on this factor.

Another point to add is that in a competitive industry, that profit differential would not matter much—in the long run at least—because those

profits are competed away by the entry of other firms. The third factor is administrative cost and risk and usually the administrative cost factor will point toward preemption, point toward leaving this matter to the agency. Why? Because the agency typically moves first, and so, if courts are considering these things, that simply adds to the administrative cost. But that is not always the case. There may be other cases in which a different answer should be reached.

The risk factor often points in favor of the agency as well because the agency is one regulator among multiple regulators with different objectives and subject to different kinds of distortion in their decision making. So, there is an optimal rule on preemption that is suggested by this. I have referred to it as something I call the congruence theory. And it runs roughly as follows: if the agency's regulatory process is rigorous and independent, a common law claim should be preempted if the regulatory standard and the common law standard are congruent in the sense that the agency standard incorporates all of the factors that would be examined under the common law standard.

In other words, if the regulatory process exhausts all of the issues that would be considered in the plaintiff's tort lawsuit, then that is a strong case for preemption, and if it does so in a way that is independent and rigorous. And again, I pointed to these three factors that are part of the standard. One is the expertise of the agency, another is the degree of local information, and a third is the extent to which the agency is independent and not vulnerable to bias. So, this congruence theory leads to a whole bunch of variables that go into the preemption decision.

One is the extent to which local information is important in deciding the issue of consumer welfare or risk utility; to the extent that local information is important, then that goes against preemption. To the extent that it is a case in which expertise is important, that cuts in favor of preemption. For example, a pacemaker is a product which the expertise of the agency would matter a lot and certainly would be greater than what you find in a court, and local information is relatively unimportant. So, that is a case in which you are more likely to find preemption.

I have used this theory to try to explain the preemption cases that have come out of courts and I have an earlier paper that was published in the Supreme Court Economic Review in 2008 that looks at a sample of 243 federal court opinions and 118 state court decisions.[3] And I created a bunch of variables to try to test the theory. So, I found evidence supporting this congruence theory in that sample of cases, and if you run through some of the better known Supreme Court cases, I think they line up with the theory in general.

For example, in *Medtronic v. Lohr*[4] in 1996, the design that was attacked had been approved under the FDA substantial equivalence test. Under that test, the FDA does not really examine the risk utility issues. It just

asks, "Well, is this product equivalent to something that was on the market before 1976? If so, that is okay. We will just give you a free pass."

When the plaintiff comes to court with a design claim, that design claim is going to look into all sorts of issues that the FDA did not look into at all. So, there is no congruence there. There is no sense in which there is congruence between the regulatory process and the common law process. The theory predicts that in a case like that, a court should not find preemption, and that is what the court found in the *Lohr* case.

On the back end of that is the *Riegal*[5] case where the design had been through the premarket approval process, which is much more involved and rigorous and looks into all the risk utility issues. There, the court found preemption, of course, because there is congruence.

The last thing I will say, is if courts could move away from the fundamental issue in this area—the case law, and the issue basing preemption on the Supremacy Clause, and the conflict between federal and state law—it seems to me that a common law court is in the position to take the decision of a regulatory agency to improve a product as just a piece of evidence in favor of regulatory compliance, and use that evidence in conjunction with all of the other factors that I have been laying out, as courts actually seem to be doing under the surface to establish a pattern for preemption decisions. One that, in a sense, divorces this whole preemption case law from all of the business about the Supremacy Clause in federal–state power, because that is an unstable basis for the preemption case law.

The courts' opinions are changing on these issues, and it gets us into a whole lot of problems about determining whether you have to decide these cases on the basis of some notion of Congressional intent. Then, you open the legislative process to gaming by industries that bargain with Congress, and they are going to make a real effort to try to fashion that legislative intent.

So, we would be better off if the whole preemption case law—which for the most part I think has done a good job of choosing the right regulatory regimes—were articulated clearly and were moved away from this whole issue of state and federal power, which is an uncertain and shifting area of the law. That is all.

GEOFFREY J. LYSAUGHT: Thank you.

TODD J. ZYWICKI: Yesterday, I talked about the CFPB and other sorts of things. Now, everybody is thinking, "All right, smart guy, how would you think about these questions?" So, that is what I am going to spend the next few minutes talking about. Thinking about primarily the area of consumer protection generally, my example is going to primarily be drawn from consumer credit, but the lessons are going to be, I think, pretty applicable to all areas of consumer protection: whether it is commercial advertising, perhaps

pharmaceuticals, some of the obesity issues we were talking about yesterday, and that sort of thing.

And the way I want to frame this—the way I think about it, and the way we thought about it when I was at the FTC, and I want to urge you to think about it—is think about two different types of regulation. To sort of overgeneralize: market reinforcing regulation versus market replacing regulation. Market reinforcing regulation, on one hand, and market replacing regulation on the other hand. Now, what do I mean by those?

Well, building on what particularly Professor Rubin has said and what the other members of the panel have said, is market reinforcing regulation is basically the idea that we start with the market as our primary ordering system. We try to think about the ways in which we can make markets work better for consumers, to harness the power of competition and consumer choice, and everything that goes along with that. And provide a prompt for that to work better for consumers and use the invisible hand of the market as a form of regulation that will lead to higher quality products and lower prices for consumers.

Versus market replacing regulation, which would be basically substantive regulation where a regulator, a legislator, or oftentimes a judge, basically dictates what the attributes of a product should be, and basically takes it out of the market process. If we look at consumer credit, we see over the history in the United States, that these two different forms of regulations move in cycles.

If you go back to the beginning of the 20th Century, what you see was a period—or even going back before that—we had very strict substantive regulation, market replacing regulation on consumer credit, very strict interest rates, usury ceilings on credit is what they called them, for instance. As we moved from an agriculture society to a more urban society, labor based society, in the beginning of the 20th Century, we saw this great migration to the cities, where people were moving off of the farms and into the cities and a lot of immigrants were coming in, and what we found was that the very low interest rates that were allowed by law, did not enable the making of small loans to wage earners.

So, people would have periodic disruptions in their labor just because of the business cycle, because of seasonal output, in factories. What you had was more and more people who needed access to short-term credit in order to pay their bills, to deal with medical bills, to deal with the rent, to deal with utility bills and everything that came about. What we found at the beginning of the 20th Century was a great flourishing of illegal lending because legal lending was not economical, so we saw was a huge amount of illegal lending. You can look at the beginning of the 20th Century in the cities and you could see this was a real problem.

So, what consumer reform advocates of the day said was, "Alright. We can't wish away the need of these wage earners for credit." And everything that goes along with illegal lending went along with that, right? So,

people basically said, "Alright, let's not pretend like these people don't need credit and let's not pretend like we're going to get rid of credit by having ill-designed regulations. Let's free up the markets and come up with mechanisms for allowing higher priced short-term loans to consumers." And so, that is what they did, and that was how, in a variety of ways, we started making access to credit available to people.

And it is expensive, right? It is expensive to make a short-term small dollar loan with a high risk of default. Well, what happened was—in a curious way—if you look back in history, what you see is that many people blame the Great Depression on too much consumer credit. Sounds like something we have heard recently? So, the response to the Great Depression was that they came in and they re-imposed substantive limitations on lending, and I could go into the details, but it is not that important.

But the effect was, beginning in the '40s and '50s, we brought back many of these old-style regulations such as usury regulations, and that sort of thing, such that by the 1960s, what we saw was that illegal lending and loan sharking was the second biggest revenue source of the mafia. Gambling was the only bigger revenue source than illegal lending for the mafia in the 1960s. Again, what we saw was a coalition of economists, and this is one of those issues that economists always agree on 100%; every economist understands the implications of interest rates ceilings, and that they lead to reductions in access to credit and proliferation of illegal lending.

We saw beginning finally in the 1960s and '70s, was in the effort to fight organized crime as well as to just make credit available to consumers, we saw an erosion of usury ceiling, substantive limitations, and that sort of thing. Basically, what we got was a proliferation of different sorts of credit markets that a lot of people find aesthetically unpleasing like payday lending and that sort of thing. Now, what we are seeing with the CFPB and the Dodd-Frank bill, I think, is a resurgence of this old view of re-imposing substantive regulation on the issuance of credit.

In my view, it is inevitable that we are going to get a lot of the same effects that we had in the past as a result of this. But unfortunately, as I think we saw in the past, what has happened and the way in which the CFPB has been crafted and will probably be implemented, is a desire to just wish away the unintended consequences that come along with this. So, to briefly give you a sense then, of why substantive regulation and market replacing regulation is dangerous, is that basically what you get is three effects.

You get term re-pricing; so for instance, when they restricted interest rates on credit cards, what happened is that credit card issuers just imposed annual fees on credit cards. When they got rid of restrictions on interest rates, annual fees disappeared for most credit cards. You get product substitution. For instance, Arkansas, which had the strictest usury regulations in the 1970s, was also the pawn shop capital of America. People could not get a small loan. People could not get a credit card in Arkansas. So, as a

result, the only way people could get credit in order to fix a transmission or to pay utility bills, was to go to a pawn shop. And this is how these creatures like layaway and all these other crazy things came into effect.

The other big factor was most credit was tied to a particular department store or retailer. The reason was because what a retailer could do—they could not charge a market rate of interest for credit—but what they could do, would be to just tie it to the price of goods and hide the real price of credit in the price of goods. So, empirical studies found for instance, that in Arkansas, a refrigerator cost about 8% or 10% more than a refrigerator cost in Texas. The reason was because Arkansas retailers were burying the price of credit in the price of the goods.

This gave retailers a comparative advantage in evading usury laws by just tying those things together and regular banks could not do that. And the final effect was rationing. This is basically the leg breakers I was talking about. Either people would have no credit at all, or they would basically have to go to Tony Soprano in order to get the money that they wanted.

I think that is the logic of the CFPB, which if you look at the logic of the CFPB, it has got a lot of substantive regulation. It has things like bans on prepayment penalties, bans on arbitration clauses, strict restrictions on mortgage brokers, and various other terms of loans, which I think are going to have all these offsetting effects, which nobody has really thought about. Prepayment penalties, for instance: it's very clear that a prepayment penalty in a mortgage, is traded off with the lower interest rates. So, getting rid of prepayment penalties, on average, increases interest rates by about forty to sixty basis points on the loan. Now, the biggest problems are the unintended consequences of substantive regulation.

What I want to address is market reinforcing regulation and talk about why Dodd-Frank came about, and the CFPB, and why I think of it as a lost opportunity to fix things that have gone wrong in the way regulatory structure handles consumer protection. A good example is the Truth in Lending Act (TILA).[6] When the Truth in Lending Act was originally introduced, it was three pages long. The idea behind the Truth in Lending Act was to try to create standardized disclosures so that consumers could easily compare among different loan offerings and decide which one was the best.

It did not tell consumers what they should choose, it just helped the market process, and competition, and dynamism to work on their own. Now over time, Reg Z—associated with TILA and being reauthorized by the Federal Reserve—is now thousands and thousands of pages long. And the reason is that over time, what we have gotten are these accretions to the Truth in Lending Act, first by piecemeal regulatory add-ons and litigation add-ons. The problem with taking a sort of piecemeal, or regulatory, or litigation approach to this, is that what it does is just adds on more things here and there, without integrating the overall effect.

We see this, whether it is warnings, or credit disclosures, or whatever. You get the problem of information overload for consumers, because once

you add on, you lose track of the central animating purpose. I heard a story over the weekend. Apparently, in the 1970s or '80s sometime, Ford Motor Company actually designed and built a car that was consistent with every tort judgment that had ever been leveled against Ford Automotive Company; they had to have thicker walls by the gas tank, and they had to have this, and they had to have that, and that sort of thing. What they discovered was that by the time they were done, the car cost thousands of dollars more, weighed thousands of pounds more, and could not move because once you took each different piece and tried to put it on the car, it would not work anymore.

There is a regulatory confusion that I think is also in the CFPB, which is the effort to try to do substantive regulation through the backdoor of disclosure regulation. What they end up doing is messing up both. It is what I call normative disclosure, and I will give you my favorite example, which is the one we have all seen now. We have all seen our credit card statements, right? On the front page of our credit card statement, a quarter of the page is a little box that tells you how long it is going to take you to pay off your credit card balance if you only make the minimum payment. It also tells you that if you only make the minimum payment, that your credit card balance will keep going up. They put that in there, it is on your statement, right? Not in your terms, it is actually on your statement. Now, the question is: how many people in this room would do the following?

Would you, number one, want to know how long it would take you to pay off your minimum balance if you only made the minimum payment? And number two, would you be willing to stop using your card? Because if you keep using your card, you keep adding to that, so it becomes useless, right? So, how many people find it useful to know every single month how long it would take you to pay off your credit card balance by only making minimum payments, and would consider stop using that card and paying off the balance only by making the minimum payment?

Now this is an unrepresentative study, but the Federal Reserve found that about 4% of Americans would actually find that useful. Why is that there then? It is obviously not because it is helping consumers to make decisions in the disclosure sense, to shop among the products they want. Obviously, what it is trying to do is use disclosure to change consumer behavior. What does it actually do? It clutters up the statement.

First, what we have to do is identify the market value of disclosure; that is useful to deal with market values in the market for information, not for substantive problems. So, what we are trying to do is use disclosure to solve substantive problems, or what some people think are substantive problems, like over-indebtedness, not disclosure. We have to understand what the problem is.

Second, we have to appreciate that people do not choose perfectly, but by and large, people choose better than their regulators. People focus on the factors that matter to them. People who revolve their balances know

what their interest rate is. I know I do not know what my interest rate is on my credit card. I would wager that many of you do not know what your interest rate is on your credit card. That is perfectly rational if you are not revolving balances, right? If you are not revolving a balance, it does not matter what your interest rate is. You care about benefits, annual fees, those sorts of things. People who revolve actually know what their interest rates are.

Finally, we get the problem if we do come in with substantive regulation and impose it, that it sets it in amber and it is very hard to change regulations or change case law after they have been rendered. Whereas market-based mechanisms can be much more dynamic and adjust for innovation and that sort of thing. So I think, by and large, what we want to think about is what can we do with market reinforcing regulation? What can we do with disclosure laws, and what can we not do and keep that more in mind?

GEOFFREY J. LYSAUGHT: Before we open it up to questions, why don't we take a few minutes to go back through the panel and see if there are any additional thoughts that have occurred and we will start with Professor Rubin.

PAUL H. RUBIN: I more or less agree with Keith. I think we may disagree on how to implement some of Keith's tests in particular cases, but I think looking at overall utility of the regulation, is the right way to go. The problem I have is that sometimes the regulation does not accomplish the goal that we think it would accomplish, and I guess there I would disagree with him.

We do not really have a choice in the FDA case, for example, between FDA and state. We have a choice between FDA plus state, or only FDA. We are not going to replace FDA regulation with state tort law, or rather add on a separate system. So, the question is, do we gain by adding on that separate system or are we better off just with the FDA?

GEOFFREY J. LYSAUGHT: Professor Ribstein?

LARRY E. RIBSTEIN: Yes, another comment about Keith. And that is, the problem that I think you have to confront with preemption is that we are fundamentally getting back to Congressional intent. These cases do not involve something like the dormant Commerce Clause where you are invalidating legislation because it has some inherent problem. This involves a Congressional decision to act and that is the only reason the preemption decision arises in the first place. So, since we are linking the preemption decision with the Congressional decision to act, the preemption rule has to relate to what Congress decides to do.

This idea of comparative regulatory competence, while it is a very attractive notion from an efficiency standpoint, raises the question: did Con-

gress really care about regulatory competence? When you think about all the political factors and so forth that go into a Congressional decision, it can be unclear. So that is why Erin and I, in our paper, talk about this inherent—although less satisfying—idea of coordination. It is very complex. It does not have the ring of satisfaction that you get from something like efficiency or comparative regulatory competence, but it ties into Congress's constitutional role under the Commerce Clause and Supremacy Clause.

If we ask why we use something like the Supremacy Clause in the Constitution, which is where preemption comes from, the answer is because we need to have a referee, and the referee's decision has to be final. And so it seems logical to refer that decision to a coordination objective. My challenge to Keith here, as it was in the prior panel, is to link his theory to what Congress was doing, rather than to what might seem a bit more satisfying theory of efficiency.

KEITH N. HYLTON: Thank you. First thing I want to say is that what I have tried to do in my paper, and in the previous paper that I referred to, is set up a positive theory of the preemption case law. I am taking a look at all these preemption cases, and I am saying, "Can I come up with a good economic story that explains the outcomes in these cases and does so in a way that is logically coherent, and simpler, and easier to follow than the stuff that is already out there in the Supreme Court's decisions?" And so, my assertion is that I think I have come up with that.

The stuff in the Supreme Court's case law talks about conflicts between state and federal law and that over-predicts preemption in every case because there is always some potential conflict between the federal regulation and state law. Based on the theory set out in the Supreme Court's decisions, you really cannot make sense of the Supreme Court's decisions on preemption. So, you have to come up with some alternative theory.

And when you come up with an alternative theory, it is going to be based on the facts in the cases and the trade offs; the social consequences that come out of the decision to choose one regulator versus another. That kind of reasoning makes sense of the cases, makes sense in terms of economics, and as I said before, offers a sparse and simpler explanation of what is going on in the case law.

Now, as for the issue of Congressional intent and Congress's power: it seems to me that the regulatory decision is a fact that any court is in a position to take into account when making a decision on whether to find, in a sense, that compliance with regulation is a defense to a state tort law claim or any tort law claim. So, there is certainly room there and a court has a power to find a common law basis for a defense that works in the same functional manner as a preemption defense. It can be called a regulatory compliance defense.

It could be called anything else, but it could be based on the factors that really count in a preemption decision and not on that nonsense in the

Supreme Court's case law about conflicts, because that stuff does not really tell you how to decide a case, at least from what I can see. Moreover, to the extent that you rely on the conflict's theory and Congressional intent, you get yourself into a problem of trying to figure out Congressional intent, which is very hard to do in the vast majority of cases, and you open the door up to gaming in the legislative process because industries know when they bargain with Congress about some regulatory statute, they know that what they would like to get is preemption.

What does that mean? That means they go to the legislators and they say, "Let's put some pieces of state common law on the trading table. Why don't we give you this and you give us preemption?" And that seems to me, a pretty crazy way to let the legislative process work, to let industries come in and buy off state common law. So, those are big problems that I think it would be good if courts could try to get themselves out of.

TODD J. ZYWICKI: I will just say a brief word to dovetail some of the preemption discussion that we have had and just talk about preemption in the context of consumer credit, because I mentioned this yesterday when I started talking about the CFPB and that Dodd-Frank makes it more difficult to preempt state laws.

We have this kind of cool and unusual sort of system in the United States of this dual banking system, where we have national banks that are regulated by the Comptroller of the Currency and we have state banks that are regulated by state bank examiners. What I like about that system is that it allows great competition.

So, the logic for preemption, is if you have an aggressive federal regulator who has set up to do things, which as I said yesterday I like the idea of an integrated federal regulator, I just wish it was done differently. But the idea is that, in theory, consumers can have a choice, right? If state regulators say, "We are going to give you a lot of consumer protection." Whenever you hear a lot of consumer protection when it comes to credit, that also means a lot fewer of you are going to get access to credit and it is going to cost more, right?

That is what the trade off is. In theory, you could go to a state bank and get that package or you could go to a federal bank and get a different package of less regulation, and less regulation in terms, and that sort of thing. And we have set up a process through the national banking system where consumers can shop among banks around the entire country. In fact, we saw that after the *Marquette*[7] decision in 1978, in which there was the Arkansas bank, which had very low interest rates but a 20% approval rate for a credit card and they gave a $600 credit limit and a $55 annual fee. Then, we had the South Dakota and the Delaware banks, which had market-based interest rates, no annual fee, benefits, everything else that we get along with it. And consumers obviously opted for the latter rather than the former. I think that the preemption fits into thinking about how to facilitate

that competition among different systems, and among different banks, and among different consumers.

GEOFFREY J. LYSAUGHT: Questions? I guess while we are thinking of questions, let me try to advance the discussion here in what I hope will illuminate the competing theories here or the ideas here, but perhaps drive us to some consensus on issues, and let us use the specific example of *Wyeth v. Levine* because I think we actually get to different answers. Professor Rubin, I think, articulates that he would be in favor of preemption. *Wyeth* was wrong, primarily because the FDA already overregulates in adding tort litigation on top of that, which gets us to an even worse result.

I think Professor Ribstein would articulate that the state tort litigation system is not well coordinated and therefore, preemption probably would have made sense in *Wyeth*. But Professor Hylton, I think, views *Wyeth* as potentially a good outcome or a right outcome, because we had reason to doubt the FDA's political independence and there was additional information that was not taken into account by the FDA in its decision. And so, therefore, there was an opportunity for the outcome to include that new information as well.

So, I guess to start with, did I get your judicial decision right? And then, help us understand a little bit better why you think your argument sort of gets to the right answer and is there room—given that you were not all considering the same factors—room to drive toward consensus?

LARRY E. RIBSTEIN: Yes, you are definitely right about my position, that this is an area where we really need coordination and keep in mind that Congress has acted. It is not just a matter of, we want the states to be better coordinated, but Congress has made the decision. The states are represented in Congress, so there is a political burden that you have to overcome in order to get Congressional action, but Congress overcame that burden and acted. So, what were they thinking?

We can fill in the gap a bit by saying, "Well, Congress was serving its umpire coordination role. With the states going off in all kinds of different directions, let us impose a national standard." And then, if it is in fact the case that Keith would go in a different direction, I would just ask, how do we know that Congress cares about the FDA's competence here? In other words, it might be a good thing to think about from an efficiency standpoint, but is this really something we should be thinking about under the Commerce Clause and the Supremacy Clause?

PAUL H. RUBIN: So Geoff, that is a great example and I want to congratulate you on choosing that one, but it strikes me, that that is also a good example because in the context of the Supreme Court's case law on preemption, which develops this complex theory, I find it hard to understand the decision in *Wyeth* on the basis of much of the theory that the Su-

preme Court has developed. So, there must be something else going on to explain how the Court could decide there is no preemption in *Wyeth*. In terms of the political independence part, that is a minor part of what I had to say about *Wyeth* because the Supreme Court was referring only to some statements that the FDA had said about the preemptive effect of its own decisions.

And they were fairly recent statements, the Supreme Court said, "Well, we are not going to really pay attention to those statements." So, that is sort of a side part. It is tangential. It is not really core to the case, but I guess what I am saying is that *Wyeth* was potentially a good decision, but it makes sense under the theory I am offering here. Why is that?

Well, based on the timing issue, the common law and regulatory standards are not really congruent in a case like that because the whole theory of the Court's decision is that there was later developing post-approval information that had developed on a risk that was not really fully incorporated by the FDA's own warning requirement. And to be specific, in *Wyeth*, we had an anti-nausea drug that if injected into the arm, could go into the artery and require the arm to be amputated. It caused gangrene and required the arm to be amputated. So, the plaintiff's theory was that the warnings should have been much more severe than they were.

They should have been more severe. You could say, "Well, you could get your nausea alleviated for a little bit, but the risk is you might lose your arm." Well, you might say, "In that case, I think I will just be nauseous for a little bit longer." And so, the plaintiff's theory was that the warning should have made clear to the doctor that given the late developing information on the risk of having your arm cut off, doctors should have been warned, "Hey, you should not do this." You just should not do this injection. To me, that is an important piece of information.

I can understand why a court might look at that and say, "Well, that is important enough information, that maybe the warning should have been updated as a result." Therefore, it breaks this congruence between the regulatory and common law standard under my approach, and it makes sense of the *Wyeth* decision.

GEOFFREY J. LYSAUGHT: Professor Rubin?

PAUL H. RUBIN: Well, it is my understanding there were several warnings. I think it was actually a physician's assistant or a nurse who violated those warnings. So then to say, "Well, had there been another warning, the person would have noticed it." And of course, there was liability. The person that did the actual injecting and the hospital both were held liable, as they should be. They clearly violated the policy in this case. There is always going to be post-approval information. We are going to open the system up again. Then the FDA has to take that into account, and they are already too slow and too restrictive in approving drugs.

And if you just add an extra burden, they are going to get worse, or you are going to have liability because there is always something you have learned after the case. So, there is always some stronger warning that you could have put on the product. Again, no matter how many warnings there are, there is always some stronger warning. Of course, you put more and more warnings on, you can lose even more valuable information. I saw that at CPSC.

Some of our products had long hang tags of warnings where maybe one of the warnings was important and the other fifteen were not, but consumers had no way of telling which of them were important. And you see that when you have lawyers write warnings, they become longer and longer and less and less valuable to consumers. The other thing about *Wyeth* was it was very similar to a previous case, with which Keith agreed, *Riegel v. Medtronic*, where the Supreme Court did find preemption, and at least the language of the Court was that it was because there was specific preemption in the statute for devices.

But then, in *Wyeth*, there was no specific preemption for products, for drugs. But from an economic perspective, it does not seem to matter. In fact, the approval process for drugs is more rigorous than for devices. So, if you are going to preempt in the case of devices, it does not make any sense not to preempt in the case of drugs as well.

We gave this paper at the previous conference that Geoff mentioned. The gentleman in the audience who was more of a consumer representative, he agreed with me that cases should have been decided the same way. But of course, he would have gone the other way then I went, but both of us agreed that it is hard to find consistency between *Riegel v. Medtronic* and *Wyeth v. Levine*.

LARRY E. RIBSTEIN: My doctor's known me for a long period, and he told me to disregard these warnings. Every time I keep coming back to him, telling him I am not going take a drug because of what I read. He says, "Just stop reading the warnings." For whatever that is worth.

GEOFFREY J. LYSAUGHT: Any other questions from the floor? Yes, sir?

AUDIENCE MEMBER: Let me back up. What bothers me is that if you recognize we have a federal structure in our country between national and state, Ribstein and Hylton, your positions are potentially inconsistent with that structure because of the way you are looking for a consensus or because of the factors you are looking at. And a good example is Truth in Lending Act. It is a disclosure statute, and it discloses and calculates the annual percentage rate based on how the statute decides it should be done. However, it does not deal with limitations on interest rates.

And so, you can effectively disclose an interest rate for Truth in Lending purposes. It is not mandating an interest rate. You can disclose an an-

nual percentage rate for Truth in Lending purposes that, in fact, is above usury rates in certain states. And one could argue under either of your theories that the Truth in Lending would effectively preempt the usury statutory provisions and cause a recalculation under state law based on the APR, and that is the concern. It is kind of a difficult issue on the calculation issue. That is my concern about both of your proposals.

KEITH N. HYLTON: It would create a recalculation under state law or it would just preempt the state cap?

AUDIENCE MEMBER: State law on interest rate calculation.

KEITH N. HYLTON: Oh, I see.

AUDIENCE MEMBER: The interest rate calculation is totally different.

KEITH N. HYLTON: From the APR.

AUDIENCE MEMBER: And so what I could argue under either of your proposals, is that the disclosure statute preempts the interest rate calculation.

LARRY E. RIBSTEIN: I would be looking for a coordination problem there, and that would really depend on whether you get chartering state limits on interest rates, or in other words, whether there is some national order to the way the interest rates have been imposed. If there is not, then it is possible that there is enough ambiguity in the statute that you would want to emphasize federal coordination. I just do not see a problem. I do not see that as being one of the more problematic applications of my analysis. I am not saying that there is no ambiguity.

AUDIENCE MEMBER: A federalistic [sic] nature is you are disclosing. You are not controlling the calculation for usury purposes, and the federalistic [sic] structure is that states can be oddballs. They can opt out of what may not be within the parameter of federal government.

LARRY E. RIBSTEIN: Right, and we ought to tolerate states being oddballs. I think that is clear and that we should have a policy, therefore, that takes states being oddballs into the calculus, and that is what we are trying to do. I am distinguishing what Keith is trying to do by not having a calculus that really takes all that into consideration.

KEITH N. HYLTON: Yes, I will admit that. In fact, I'm going to just pass on this one. I am not going to try to answer it because so much of what I am trying to deal with in my paper is regulatory agencies and the detailed

body of rules they are developing. And when Congress writes a statute that tells people what to do, I have not really tried to deal with those cases. That is one sense in which Larry's paper is complementary to mine because Larry is dealing with precisely those kinds of cases. So, I am not even going to try to deal with it.

PAUL H. RUBIN: There is a funny point about federalism, I think, that is kind of kicking around. Which is that—I have observed by looking at the Supreme Court over many years—in some sense the Supreme Court has flipped federalism on its head from how federalism was originally intended. This is a gross generalization, but basically, if you look at the original Constitutional structure, the purpose of federalism was to promote individual liberty, right? Federalism was a means of promoting individual liberty and integrated markets.

Over time, for whatever reason, federalism has come to be seen as a theory of state power as sort of an end in itself, and at least as I read the Supreme Court jurisprudence, it kind of lost the ideal of federalism as a means to the end of individual liberty. I will just express that view and will not belabor it because it is a little bit off topic here, but I think it relates to some of the questions in that it is related to preemption, sort of that orientation.

LARRY E. RIBSTEIN: I definitely agree. I like that characterization because I do think you need to distinguish between good exercises of state power and bad exercises of state power, and I think that issue was raised by the last question.

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1 *See* Wyeth v. Levine, 129 S. Ct. 1187 (2009).

2 *See* Wilson v. Bradlees of New Eng. Inc., 96 F.3d 552 (1st Cir. 1996), *rev'd*, 1999 WL 816817 (D.N.H. 1999), *aff'd*, 250 F.3d 10 (1st Cir. 2001).

3 *See* Keith N. Hylton, *Preemption and Products Liability: A Positive Theory*, 16 SUP. CT. ECON. REV. 205 (2008).

4 *See* Medtronic Inc. v. Lohr, 518 U.S. 470 (1996).

5 *See* Riegel v. Medtronic Inc., 451 F.3d 104 (2008).

6 Truth in Lending Act, 15 U.S.C. §§ 1601-1667f (2010).

7 *See* Marquette Nat'l Bank of Minneapolis v. First of Omaha Serv. Corp., 439 U.S. 299 (1978).

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5TH ANNUAL JUDICIAL SYMPOSIUM ON CIVIL JUSTICE ISSUES
GEORGE MASON JUDICIAL EDUCATION PROGRAM
DECEMBER 5-7, 2010

EDITED TRANSCRIPTS

THE ROLE OF THE CIVIL JUSTICE SYSTEM IN ALLOCATING SOCIETAL RISK

Robert Cusumano, John E. Heintz, Philip K. Howard, John Vail
Moderator: The Honorable Ben F. Tennille

PAIGE V. BUTLER: Your moderator for this session is Ben Tennille. He is on the North Carolina Business Court. He was actually the only business court judge for many years in North Carolina. He was appointed in 1996 and I belive it was not until 2005 that you had company?

JUDGE TENNILLE: Yes.

PAIGE V. BUTLER: He's also was the founder and the first president of the American College of Business Court Judges. He has served in many capacities for the ABA in the business law section as a representative for the judiciary.

JUDGE TENNILLE: Thank you, Paige. You're here for the grand finale—this spectacular panel that's been put together. We're sorry Fidelma couldn't be here. Rumor has it she could not find a responsible defendant to charge with the snow in Buffalo. But she is seated at the airport working on a class action against TSA, the air traffic controllers association, and the major airlines, alleging that collectively they constitute a public nuisance. We won't miss her but John Vail is going to take her place very admirably.

We do have an all-star panel. To my immediate left is Phil Howard who is the founder of Common Good. A lawyer with Covington & Burling, he has written a number of books, starting with the "Death of Common Sense: How Law is Suffocating America." His last book is "Life Without Lawyers: Liberating America from Too Much Law." We're going to have a very short video of Phil's appearance on the Daily Show here shortly.

John Heintz is a partner with Dickstein & Shapiro, he's a leading litigator in both corporate insurance coverage and complex litigation.

Robert Cusumano who's the General Counsel of ACE Limited, which is a global insurance and re-insurance company. If we think we have problems dealing with risk everyday, they couldn't possibly compare to what Bob has to do on a daily basis as far as risk is concerned. I'm going to take the moderator's prerogative just to make a few comments at the outset here. I am a business court judge. I spend the majority of my time on corporate governance and as such, I have a very fortunate position in the judiciary. The field I work in, corporate governance, encourages risk on the part of directors and officers of a company. There is no value creation without risk.

I have the benefit of the business judgment rule, which restricts the scope of my review of either the inaction by, or the decisions of the boards of directors. Everyone in my court knows and generally agrees that I have the power to allocate risk. The allocation of risk is almost always in a contextually specific situation but I have well developed standards and guidelines, primarily from the Delaware Supreme Court, to help me. I get to look at process information, transparency, motivation, culture, and history, in reviewing the decisions of boards of directors that may have gone awry. I generally have good lawyers and well qualified experts to help me.

The result is a system that provides as much certainty as possible to the business world with respect to the corporate governance issues with which I deal. I am absolutely convinced that those of you in the audience who have to deal with other kinds of risk allocation are not so fortunate. So, we have this panel put together to give us their views of the big picture questions in the role of the civil justice system and allocating societal risk. To borrow a phrase from Larry Ribstein, this is what I would call "big law."

PHILIP K. HOWARD: Picking up on what Ben started out with, risk, I'd like to talk about what I think is a fundamental shift in the goals of civil justice needed to be one of the elements to put our society back on an even keel.

I'll start by saying civil justice is extraordinarily important in a free society. When you have an anonymous interdependent society where people can't count on community norms, you need a system of justice that Americans trust, to enforce contracts and to hold people accountable if they act unreasonably so that people can go through the day following their star and not worrying about protecting themselves.

We need incentives for people to make sure they stop for the red lights and also that they will, when they're making products, comply with reasonable safety norms and that sort of thing. Now, civil justice happens to be the mechanism by which we make those choices but we've been trained to think that civil justice is just a dispute resolution mechanism, and I submit that's not the case. Its main goal is actually to be a part of a platform for a free society. It's to enable people to make all these daily choices because again, the backdrop here is this reliable civil justice system that people can trust to enforce their contracts, and so on.

Now, if justice is not available, and big companies can get away with anything, or people can be abusive in their treatment of workers, then that undermines freedom because people are very nervous in their daily dealings because they're afraid they're going to be taken advantage of. But the similar effect occurs if justice is over inclusive. If any accident, if any disagreement in the workplace can have a similar effect, and you can be dragged into litigation for years, then similarly, people in their daily choices won't focus on doing the right thing, they focus on self protection.

They start listening to that little lawyer on their shoulders—and this is a lot of what's happened in modern society. The culture of healthcare has

been transformed in the last fifty years. I have a pediatrician friend of mine who used to be head of a medical association who said, "I don't deal with patients the same way anymore—you wouldn't want to say something off the cuff that might be used against you." Imagine going through the day as a pediatrician thinking that. How that affects your patient relations.

It's not just the cultural aspect. Defensive medicine is actually very hard to measure; the reliable estimates have it at between $50 and $200 billion dollars a year, which is a huge amount of money. That's just the practice of doctors: ordering tests that they don't think are medically indicated because they want to have something in the record in the unlikely event that the headache is a tumor or the like. The trial lawyers say that the civil justice system today is good because it makes us be careful. Well, that's been studied by the Institute of Medicine. It turns out that is not to the case.

There's distrust of justice in medical care because it has chilled the professional interaction needed for safe care; so doctors and nurses don't say things like, "Are you sure that's the right dosage?" "Are you sure that's the right prescription?" because they don't want to take legal responsibility. This has been studied. So, it doesn't work—the current cultural system of fear and distrust of justice doesn't work for society. Children's play has been completely transformed—there's nothing left in playgrounds for a kid over the age of five: no seesaws, merry-go-rounds, jungle gyms, or climbing ropes.

Broward County, Florida, a few years ago, banned running at recess. Other schools have banned the game of tag because all of those activities not only involve risk, but the certainty that from time to time there, will be accidents. And when there's an accident in modern America, there's a lawsuit. Nobody's drawing the line on behalf of society whether that was a reasonable risk or not. So, the lawsuit goes on. Broward County banned running because it had 186 claims in the prior five years. They had to settle every one of them. They couldn't afford to go through the court process for years.

We have a crisis of childhood obesity which has many causes but one of them, according to the Center for Disease Control, is that kids don't do what they used to do and part of that is because they're not allowed to. Relations in the workplace have completely been transformed. Businesses, including my law firms, don't give job references anymore. I have a list of questions I'm not allowed to ask interviewees, including this one, which is bulging with innuendo, "Where are you from?"

You have this society where you have warning labels on everything: "Remove baby before folding stroller." My favorite, a five inch fishing lure—it's a big fishing lure—with a three prong hook in the back said, "Caution: harmful if swallowed." You have people putting all these warning labels on things that are not neutral—they're counterproductive. It's just like the boy who cried wolf: you need warnings for the things you need

warnings on, but you shouldn't put them on things you don't need. But we don't have anybody drawing that line anymore.

What I submit is, that it is wrong that nobody on behalf of society has the authority to draw the lines of what is a reasonable risk or not; what is a reasonable lawsuit; and what is a reasonable defense or not. We have this idea that civil litigation is a right. There's a right to sue just like the First Amendment. I submit that that's wrong—that suing is a use of state power, coming down to that verdict when the jury holds you guilty and the marshal will come and take your home away. It's just like indicting somebody—you're just indicting them for money.

We would never tolerate a prosecutor seeking the death penalty for a misdemeanor, so why do we tolerate some jerk in the District of Columbia suing his dry cleaners for $54 million dollars for a lost pair of pants? Completely absurd. The case went on for two years. The judge could have dismissed it in a minute—case dismissed without prejudice to refiling in small claims court. But the superior court judge in the District of Columbia didn't think he had that power because that's not what judges think they have the job to do anymore.

If one person brings a lawsuit because their child fell off the seesaw, it doesn't matter what the jury does—the juries are generally sensible. The fact that you're at risk and you might get sued for $50,000, or millions of dollars if a child happens to die, means that all of society will rip out the seesaws, which is what's happened because, why take that risk? How do you accomplish goals? How do you accomplish the goal of always keeping the courthouse door open? Which it should be—there's no rule that's going to arbitrarily shut a courthouse door for anybody.

It must be open, the question is how long the case is allowed to last, not let any disagreement, no matter how unreasonable, proceed all the way through to a jury trial. Where the British Law Lords said, "In a common law system, it is the job of judges to defend the freedoms of society," in that case, a person who suffered a tragic accident, paralyzed for life while swimming in a public lake, the case was dismissed because looking at the facts the Law Lords said, "As a matter of law, if we let claims like this proceed, the lakes and rivers in our country will be closed down because people won't take the risk."

It's the job of judges to draw the boundaries to defend the freedoms of everyone else in society. If you go back and read Justice Holmes, and Justice Cardozo, and Justice Trainer, they said the same thing we've just forgotten—Trainer said the same thing. If a lawsuit might affect the conduct not in the courtroom, I submit judges have to make legal rulings drawing the contours of the claim.

Otherwise, everything that involves a risk is potentially illegal, as one scholar put it, "and act as illegal if it is vulnerable to legal action." So it's the risk that you might get sued from an activity that undermines everyone's freedom, and that's what's happened in our society. H.L.A. Hart, the

famous legal philosopher, once said that the essential characteristic of every system of justice that we respect is this: like cases must be decided alike.

In our zest to provide justice to everyone—and there are a lot of things that we've had to overcome and abuses that we had to overcome in our lifetimes—we've lost sight of the fact that freedom not only means access for people to bring claims, but also requires the institutions of society, such as judges and others to make common choices about which other people could disagree. This has been surveyed area after area. Americans no longer trust the civil justice system, and it's materially undermining their freedom.

An essential aspect of restoring that freedom is for judges to take back control of the courtroom, and start making legal rulings—nothing unconstitutional about this. The role of juries in civil cases is to decide disputed issues of fact, not to make rulings on behalf of society. They don't have that power. That's one of the aspects of reform that my group, Common Good, has been working with some of the senior judges, the American Law Institute, and others, about pursuing. Thank you very much.

JUDGE TENNILLE: Thank you Phil. Here's John Heintz.

JOHN E. HEINTZ: Thank you. I learned earlier today that I'm one of the walking dead, and now I'm participating in a system that has gone awry. I want to talk a little bit about how we use the civil justice system to address this transfer of risks, because everything that happens in the system is affecting whether a risk that somebody bears is being transferred to somebody else through property rights, through property rights, through tort rights, or through contract rights. These are all areas through which our society transfers risk. Tort law defines who has the risk of unreasonable behavior and who has to compensate for the consequences of that.

Insurance, which is my area of the law, is the ultimate mechanism of the transfer of risk because that is the business's purpose. It's behind along side of, or, instead of these other mechanisms. But to me, it's really the legal system's definitions of rights and definition of what constitutes an interest—an invasion of that right that is subject to being remedied in a court of law. Everything that we litigate about is over, "Do I have the right and do I have a right to be compensated or given relief if that right is interfered with?" Every argument we have in the public domain, every argument we have in court, is somehow infused with that basic question.

Because the heading of our topic is societal risks, I want to distinguish the garden variety, although I think a very cogent argument has just been given about how even a simple slip and fall case off of a merry-go-round has a societal element to it, because the ruling has consequences that can be widespread. Many of the risks that we are dealing with in these kind of cases, are the risks of a hundred or more years of an industrial society engaging in the kind of economic activity that this country pursued, and doing

so in a way that created harmful side effects, and the question is how do we now allocate the burden of those risks?

There are some areas where we are allocating the burden of those risks that are only historical because the activity giving rise to the problem has long ago ceased. The use of asbestos in insulation material ended some time ago, but we're still allocating the current consequences of that historical conduct. On the other hand, in the climate change litigation, we're trying to allocate the risk not only of past conduct but of current conduct, and if emitters of CO2 are held liable in court then they will change their behavior in response to that allocation of risk to them.

But it is different than simply dealing with the legacy of a historical area of conduct, because we are not really—when we're dealing now with asbestos—creating incentives about future behavior except by way of perhaps, example. Early on in my career, I went to the 8th Circuit for a en banc rehearing on an insurance coverage dispute, and the first question that Judge McMillan raised was, "How is it fair to ask an insurance company that sold you a policy in 1972 to pay a liability that arose under a statute that was not passed until 1982?" The question of fairness.

It seems to me that fairness is a principle that every lawyer, every public policy advocate in support of his or her position, and every judge has to grapple with—it infuses our civil justice system. So, one has to ask in the context of dealing with these mass torts or these global warming problems or other comparable problems, "Is our civil justice system handling this efficiently and is it fair?" Well, I don't think anybody who has had any experience in the asbestos world would say that that system has been either efficient or fair.

They ran studies suggesting that less than half of the total cost of dealing with asbestos related claims ultimately gets into the hands of asbestos claimants—of course, not all those asbestos claimants who get paid had an impairment—getting a real fraction of every dollar went to people who really had injury. Well, that's certainly not efficient. Is it fair? I think it depends on which state you're in, which lawyer you hire, and who's lawyer is on the other side, and—we heard yesterday—that one of the single most important factors affecting the settlement of the case, is the jury pool. That has a dramatic affect on what the value of a case is.

If you're talking about a system whose objective is to treat similarly situated people in a similar way, that is not a recipe to accomplish that in a mass tort problem of that sort. But fairness is, it seems to me, the important thing that drives the proposition that Phil put to you, and that I think every speaker I've heard today and yesterday put to you. Because we will all argue fairness. Is it fair that a young woman with cervical cancer allegedly caused by the DES her mother took to prevent miscarriage, is deprived of relief because her mother was given the drug in the hospital in a paper cup, and therefore did not know which manufacturer made the drug? Is it fair?

Is it fair that a paper company that recycled paper, that's the whole source of its paper stock, but didn't know that some of that recycled paper was carbonless copy paper that contained PCB's on the backside in which the ink was suspended, didn't know it was discharging PCB's into the river, should pay for the cost of cleaning up the PCB's thirty-five, forty years later? Is it fair? Is it fair to hold a company that is admittedly a substantial emitter of CO2 for having made hurricanes more severe in Louisiana, and therefore should somehow compensate or abate the nuisance it created because it is within twenty or thirty or fifty miles of the New Orleans where the hurricane hit?

Every litigator, every person who is representing one side or the other of those interests is arguing about whether it's fair. Fairness indeed governs the principles we have to reflect upon and in your jurisprudence make decisions on. We start with principles that are in the Declaration of Independence, The Bill of Rights, the 14th Amendment; all of those have concepts of fairness in them. But standing—the articulation of that test is a fairness test. Is the injury the plaintiff complains of fairly traceable to the actions of the defendant before the court? And if I ask the defendant to do what you are asking me to do, if I make them do that, will it remedy your injury?

That's a question, ultimately, of fairness. Our tests of causation are questions of fairness. A but-for test. Be it in the [inaudible] the problem of course was that the plaintiff couldn't [inaudible] by traditional tests. So, her lawyer argued it's not fair. California Supreme Court included that that's why we would adopt market share liability, that we knew that six companies manufactured this drug, it had to be one of the six.

If we allocate the liability in accordance to market share over the course of all the cases, it will be a fair imposition of the transfer of risk from the individuals who end up with cervical cancer to all six of the companies whose drugs in the aggregate contributed proportionately to all the cervical cancers. That was a fairness driven result. The question I think that is the most challenging in a very complex society is how do you address fairness in dealing with the known—knowable as well as the unknowable—risks of a very complex industrial society in which we live? And of course that I leave to you all.

ROBERT CUSUMANO: I'm so pleased to be a part of this wonderful panel at this wonderful conference. As many of you have noticed probably, I've been here throughout the whole conference and that has caused me to rip up all my notes that I started with and try to reframe my thoughts in the context of what I've heard so far. I'll start with a metaphor. I feel that about thirty years ago I married the civil justice system and maybe we can characterize my remarks as an attempt to get some therapy. In order to get some therapy, first, we have to emote a little.

I'm going to have to tell you a little about myself, and then I have to talk about what we might do to make our marriage better. Always, you start therapy by telling your spouse, "I love you very much. You're good at almost everything. You're very functional, the kids are getting raised well. A lot of our problems are in a place that doesn't involve day to day life." And I think everything I've heard in the last two days works along those lines.

But I also feel bad. I feel bad for you, the judges, because you need to decide practical things every day with real people banging the table for what we call justice, this intangible good. You're doing it within a basic existential conflict in America about democracy and the role of the courts. And you've heard that conflict from both sides, maybe all sides, of a multi-dimensional, political battle that's going on, one that has to do with the very role of courts in allocating societal risk. That debate, if that's what it is, goes forward with the benefit or detriment of some very incoherent faux political philosophies, and we've heard a little bit of that in my opinion over the last couple of days as well. And the debate always goes forward, now, in a highly politicized environment in which the courts themselves are political footballs.

The result is that for you, the judges, and a little bit for me as general counsel of a major insurance company, we have become the dumping ground for unanswerable questions. We are the pooper scoopers of society. As the general counsel of a global insurance company, I may scoop more poop than all of you combined. The result is that I'm not an ideologue—I'm probably the least wedded to any philosophical point of view of anybody you've heard over the two days, other than perhaps on this panel.

I would say that my point of view, which will color the rest of my comments in this request for therapy, is vaguely meritocratic, centrist, capitalist. I'm a social liberal; I tend to be pragmatic; I'm a little oriented toward making things work in the real world; I like to get things done; I like to solve problems. I take complicated legal or judicial situations and try to reduce them to a single number. The result of this is that it tends to focus one's attention on systemic issues, on the way we do business in the civil justice system. I preside over, or I certainly have an affect on, the movement of some billions of dollars every year from our coffers into the hands of plaintiffs in lawsuits.

My job, honestly, touches often on every single issue that people talked about through this whole couple of days. I don't represent any particular ideology about those things, but I do feel like I represent the financial plumbing. It is here where the poop goes after the pooper scoopers are finished, and we try to deal with it and disperse it and make it less toxic. In the world that plumbing is not quite as extensive as you might think it is—the entire capitalization of the worldwide insurance industry is about $300 billion to $500 billion. That's in the whole world, and you might estimate that that's somewhat less than just the global warming tort would cost.

My company has between 5% and 10% of that. There are reserves for existing claims, mostly what you all do for a living everyday—in the workman's compensation area, auto accidents, everyday insurance, real people suing real people. Those reserves probably approximate a little more than the global capital of the industry. That compares, not favorably, to a one year budget for the federal government—it's less than half. Since World War II—I ask for any guesses from the audience: for the worldwide insurance industry, if you have premiums on your left hand, and you have claim payments on your right hand, what's the relationship between the two?

I think most people would think, "Well, there's some profit margin, maybe it's not a huge amount but there's something." That relationship is actually negative. Our business model works on making money while we hold it. We as an industry have almost always, and almost every year, paid more in claims than we collected in premiums. It is a fiduciary investment model, and I consider myself a fiduciary to the world. I have to manage the allocation of the money to all the things that are delivered through the civil justice system.

I find that system to be haphazard, chaotic, mostly effective, vaguely unfair, and occasionally very unfair.

It's part of my job to rationalize outcomes, and I have some power to do that, but it's the power of influence; it is not the power to decide anything. Contrary to what you may believe about insurance companies and lawyers in them, we don't hate torts or the tort system. We like it, it is our lifeblood. We manage it for a chance at a profit. What we hate is a tort system that delivers retroactive liabilities that no one could have understood at the time we collected premiums for those liabilities. And we hate that with a truly blinding passion.

In my therapy session, I would tell my lovely spouse, the civil justice system, three things about our relationship and about us. One is that the failure of the political process—that is, the refusal of the political branches to make clear and final decisions about the "allocation of societal risk"—is at the heart of our problem. I believe that it is inevitable that when the credible political institutions don't decide something, someone else is going to decide for them. And I think that that is the common theme throughout this whole couple of days: You and I are going to decide these things because of a political vacuum.

I decide them by writing insurance coverages, deciding what's going to be covered and what can't be covered, finding exclusions to deal with whatever's delivered to me—particularly things that I can't underwrite or that actuaries can't understand. I also get to choose when and how hard to litigate. That is a very big and influential factor, and when you see an insurance company, as they say, "litigating like hell," you can count on the fact that you touched a nerve, because we would rather just process claims through the system. Sometimes we can't do that.

I also participate in claim handling decisions. That is, where there's an ambiguity and you're not sure how the facts fit into a policy, I can decide, with my colleagues, to pay that claim anyway, or not to. That's power. Those are all default powers given to me because no one else is going to decide these things.

Think about the example of so-called "death panels," so much discussed in a very unfair way a year ago or so. If the idea is that we're concerned about governments deciding who gets what kind of care or not, especially at the end of life, especially with new technologies—and the concern is government specifically—then that concern has to be informed by the following fact: if they don't decide it, I decide it. I don't think Sarah Palin or anybody else wants me doing this, but I have to do it. That's the default—that's the job of the pooper scooper. If I don't do it, then no one does. So I do it.

Yes, I have all of you overseeing my decisions, and I try to make rational decisions—in part for that reason, in part for my own reasons. *But someone will in fact decide these things*. So, to decide that the law articulated by democratic processes has no role in something is not to say nothing gets done; it is simply to move the decision point to another actor. It's critically important that everyone understands that, and the fact that those non-statutory decision paths have very different characteristics.

When these non-statutory decision makers (or processes) are funded by what I'll call "externalities," that is, by other people's money (OPM), I find that all hell breaks loose. Every panel through these two days has dealt with an externality—and a big one—and it's always at the center of their problem. Externalities cause bad incentives. And these externalities lead to decision-making by institutions that are not competent, frankly, to make those decisions, including me and my company. We have juries making scientific decisions, we have judges, as you heard, making information technology decisions, we have me making strategic resource deployment decisions. And, of course, we have self-interested lawyers making decisions about everything.

As a result, you have a certain failure of basic cognitive abilities: you have a problem with judgment, you have decisions being made that are not as fully informed as they would be if we were taking in the expertise of everyone in the way you would in a fully functioning political process.

When legal outcomes are driven by the supply of money, rather than by other things—as we must all admit they often are, especially when we have deep-pocket defendants—you lose sight of justice or rationality. And then that feeds on itself. The result of that is under-funded courts, as courts rush through and try to get claims paid, become ineffective at what they are fundamentally designed to do, that is, deliver just outcomes. What they're doing, actually, is in a sense undermining their social purpose.

The second thing in my therapy session that I would say is that we have to get past "wrongdoing." I agree with everything John just said about

the search for justice and fairness. But frankly, we're in a world of complexity where old notions of justice and fairness don't make any sense anymore. We're in a postmodern world of enormous complexity, and the result of that is that you can't sit down very often in these gigantic new tort environments and come up with gut justice. And if you did come up with gut justice, what you would be doing is supplanting a societal decision that we're not going to tax our people to solve a social problem with a judicial decision that we're going to collect money, probably from me and from companies, as another way to solve that problem less well.

So, the movement away from wrongdoing in torts, including the whole strict liability concept itself, I applaud, because we're not dealing with wrongdoing. We're dealing with social allocation of responsibility. I would rather see it done at the political level, but if we're going to do it in the context of the relationship between courts and litigants, then we have to do it in a way that is, quite simply, more detached and more rational and more multi-disciplinary.

The third and final thing that I would say to kick off a productive therapy session, is that causality jurisprudence is impossible in the modern technical age. Get over it. Causality can't be done.

Unfortunately, everything in the tort system and in the civil justice system is dependent on the old-fashioned notion of cause: this causes that, but-for cause, proximate cause, etc. "Proximate cause" is itself a political phrase, not a legal one. It is hard to understand mainly *because* it is a political phrase, and it reflects a general understanding that we're going to take causality thus far and no further. We take it no further because we understand that we can get, at that point, outside the normal cognitive range of human vision. And we don't know what the consequences are going to be if we impose fault-based financial liabilities on the basis of arguable causalities that everyday people cannot, or did not, understand when they were acting.

The result of these three things is that, as we do our pooper scooping and everybody sends us their intractable risk allocation problems, sometimes we have to say, "You know what? We can't solve that for you or for society, because we will, in fact, make it worse. This problem is just too complicated, and requires all of society to be involved."

I'm going to end this therapy session by telling my spouse what we might do very quickly to ease our problems, if not solve them.

I think, first of all, that we need to be nice to each other. What really concerns me is that, with all the ideologies flying around, you can get enormous meanness. And it is so destructive.

The second thing is that I think we have to keep in mind that the public is watching us. As we conduct these debates, hopefully in a civil way, we have to understand that they don't understand what the hell we're talking about. None of this makes any sense to the average person on the street. The result of this is that our profession, which I love and want to stay mar-

ried to, and the judiciary, which I also love, come under constant criticism. This, simply because of the fact that we've taken on the job of being society's pooper scoopers, and because it has become so complicated that we can't explain perfectly how it works to people.

I think I'll end by saying that, for all these reasons I want to slightly alter, and re-name, the political question doctrine. This doctrine, which we heard about earlier today, is a very interesting phenomenon to me because it started out about politics and government and the judiciary and the relationship among them. I want to call it the "judicial humility doctrine" because that's what's going to get litigated in front of the Supreme Court this year on the global warming cases. The real question is not which branch should act so much as it is this: "What is the civil justice system institutionally qualified to do?" The political question doctrine is situated in a place in our jurisprudence from which it can easily be used to grapple with these questions of institutional competence. In the end, the courts cannot solve global warming, nor possibly allocate its financial consequences. We need to be judicially humble, and accept that this is one of the ultimate political questions. Beyond fault, still largely beyond human understanding, and certainly beyond future prediction or spreadsheet loss calculation. I can't allocate it, and neither can the judiciary.

I want so much to close my therapy session by saying to society, "You know what? There are some things I just can't do for you. Some things I don't understand any better than you do." I would say that global warming is one of them, but there are many others. And the sooner we make that into its own judicial doctrine, I think the better our relationship will be. Thank you.

JUDGE TENNILLE: Thank you, Bob. I'm reminded of Nassim Taleb's quotation, "Emotions are the lubricants of reason." They have their place. John?

JOHN E. HEINTZ: Let me start with a big point. And this is a big point—you've been hearing a lot about market economics, but we don't allow markets in injuries. We don't allow people to consent to batteries; generally, we don't allow transfers of body parts. There's a substantial number of economists who argue that we should, and that's a different question than the one I'm addressing here, because we don't, and we've created a substitute—the substitute is the civil justice system.

The civil justice system is the way that we evaluate those kinds of injuries. I think it's useful. It can be useful to think of it in those terms. One of the things it does, is it sets property boundaries. And it does that. I want to talk specifically about a global warming case. One of the things that's happened is, we never charged people for putting crap into the air or into the water, because we had a lot of it. Now we're figuring out that that's a mistake, that those indeed are finite resources.

It's kind of a classic problem about regulating a commons. You know, and what we're doing is taking it from what was a commons and saying, "No, we can't let people just do anything they want there."

John's paper talks about the tort of public nuisance. Public nuisance is generally defined as an unreasonable interference with a right common to the public. Now you pose the question, "Is it fair to hold emitters of CO2 liable for emitting CO2 when they always did it?" Under that exact standard—that's a common law standard—you can say, "Well, maybe, yeah," because just because it was reasonable then, doesn't mean it's reasonable now. External conditions have changed. It seems to me that's a kind of question that's wholly within the institutional competence of the judiciary.

Let me respond to a point that Robert made about the political question doctrine. The political question doctrine is a federal doctrine. You don't have political question doctrines in your state courts generally, at least not the way that they're talking about it here. Indeed, we specifically did not envision the federal courts as makers of tort law, right?

The constitutional convention reacted really badly to that idea. They said, "No, no, no, no, no! We don't want federal courts involved in mucking around with tort law." Why did they say that? It's not because they wanted state legislators to do it; it's because they wanted state courts to do it. State courts have been lawmakers in our common law systems for 1,000 years. You are supposed to make law of this kind. You are supposed to look at evolving doctrines.

I would suggest one of the things that's going on here—Fidelma Fitzpatrick has a case that's pending in the Seventh Circuit now, that involves market share liability in Wisconsin. The defendant is a lead company—it's a lead paint case—that acquired a company that used to make lead. When they acquired them there wasn't market share liability, but there were a lot of extent liabilities out there, and they certainly knew lead was dangerous. Applying established Wisconsin doctrine to this, you would hold them liable under a market share theory. A federal district court judge in Milwaukee—I think in Wisconsin—held that that theory of liability violated the due process clause.

That's essentially holding the method of the common law unconstitutional. I happen to think it's a ridiculous ruling; these guys might not, but you can talk about that. One of the things you're doing as market share liability evolves, is adapting the common law to new conditions that we encounter in society, which is what the common law has done—and I think has done marvelously well—for centuries. It encounters new phenomenon. Think of MacPherson-Buick. You say, "No, what's wrong? [inaudible] is not so important in what we do anymore." No, we aren't going to hold the manufacturer liable when they should have known. We allocate risk in that way. We do it interstitially.

Market share liability is a way of adapting to new phenomena that we see. One of the clearest, most important new phenomena is that we now

have institutions that last longer and are solvent longer, and are more ubiquitous than they ever were before. It's very common now to have very big, very diverse corporations that continue to exist. You didn't encounter those as much historically because they weren't so big, they weren't so [inaudible], and they just disappeared. But they're there now, and the question is, "What should they be responsible for?" Interstitially, the courts are figuring that out, and they're evolving rules.

So you have two choices. You have the system that we have that draws on experiences interstitially and pulls lessons from them and collectively evolves rules. Or you can think maybe you've got the ten smartest folks in the room—you can put them in a room and set them up and say, "Well, we're the ten smartest folks in the room, and we thought about it and we decided prospectively, this is the way it should be. All right?" That's basically the basis of the civil law system.

We don't have a pure system either way. We have this dynamic that occurs between what happens in the courts and between what and what happens in the political branches. I would suggest to you that having both of those systems in place has served us very, very well. There's a reason America is viewed as one of the best business environments in the world—still. Although they all complain about our legal system, they all still invest here.

A couple of points. You're state court judges. Forty or so of you have open courts time clauses in your state constitution, which say a man has a right to sue.

Marbury v. Madison[1]: Chief Justice Marshall says one of the first duties of the government is to provide remedies when someone is injured. We're children of the enlightenment. We think of the Bill of Rights as restrictions on state government. We tend not to think about providing remedies of this type, providing your judicial review is one of the fundamental elements of why [inaudible].

It's *Bill Johnson's Restaurants v. NLRB*[2]: the right of access to the courts is an aspect of the First Amendment right to petition the government for redress of grievances. The draft of the First Amendment said you had the right to petition the legislature. As it came out of committee—we don't have any notes of the committee—it was the right to petition the government, to petition all three branches—made effective against the states by the 14th Amendment. It's a fundamental right; it's not only a right to speak, it's a fundamental right.

Juries decide fact. That's not quite true. That's a construct that we put onto what juries do. Juries decide facts and judges decide the law. You all know your pattern jury instructions. Who decides the question of negligence in your state? Is it you or is it the jury? You submit that question to the jury, right? Is that a question of law or fact, or a mixed question of law and fact? I don't need to categorize it, but I know that since this country was started, that's what juries do. See, you don't have to create the intellec-

tual construct, and then go back and try to fit what juries do into it. That's backwards. That's imposing your order on what exists. Those are the questions that juries decide and always have decided. That is their role.

Phil raised the notorious case in Washington—the guy who might have been a little off-base. His dry cleaners lost his pants, and he sued them, and the case dragged along forever. If there are any of you who feels that you do not have the tools to deal with—I want to say a child—who brings a $54 million suit for lost pants. Do any of you really think you have a problem taking some control of that? I mean, I want you to raise your hands if you do. I didn't think anybody would. It's really an anomalous thing that happens, regrettably.

JUDGE TENNILLE: All right. I wanted to give the panel a minute or two to respond to what's been said up here, and then open it up to questions from the audience. Phil?

PHILIP K. HOWARD: Just in response to John's points. To clarify, what I'm saying is I don't think you have a right to take every claim to a jury. The role of the rule of law is that I can't sue John because I don't like his tie or because he disagrees with me. There's not a claim for that. So the question isn't what should be decided is a matter of law, and what should be decided by a jury in a matter of disputes. I don't think that's a good construct. That's been there since Lord Cooke and before that—centuries ago.

So the question is simply not whether you close the courthouse doors, which I don't want to do. The question is how long these claims last. So that's what I think is an issue. Ultimately justice is supposed to serve society, so the arbiter of this question to me is not what John and I might agree or disagree on, but how the society is working. That's the test of justice. Is it working well? Is it fair? Do people feel comfortable as they go through the day in interpersonal relations? Are people acting reasonably in running classrooms or letting kids go play? If not, why not? Are judges acting reasonably? If not, why not?

Justice is not an abstract construct. It's something that's a tool of a free society. So if you want to know how you're doing, look at how the society's working. The system of justice in commerce works extremely well because contracts are decided as a matter of law by judges. No one in this room will allow someone to bring a case that alleges that the contract was unfair because it didn't work out. You won't let that claim go to the jury. That's the reason that people invest here; because courts honor the words in a contract. Reliability and consistency are essential to the rule of law. I will acknowledge what John said, which is that what I'm suggesting is certainly not the current orthodoxy.

UNKNOWN: You know, one thing that I didn't get a chance to say, but I think is a very important thing that underpins all of the debates of all of the

panels, is that a lot of what we're talking about is changing or challenging whether the status quo distribution of risk is appropriate. Doing nothing is a decision; it's not simply that the problem goes away. It's simply allowing those on whom the system outside of the civil justice system, or the legislature allows the risk to end. All of the litigation and all of the fight in the political arena is about changing who ends up with the right and who has to compensate toward interference. In that, one thing that I'm concerned about is that there is a misunderstanding about the economic consequences of these choices. Because economics [inaudible]. It only tells us that once you know who has those rights, how we reach an efficient allocation of resources.

ROBERT CUSUMANO: I think a lot of the discussion here is about what I call "new age torts" over the years. And some of those torts actually became traditional torts over those same years, and the question looking forward, is "How far are we going to take it?" I know most of my comments were directed at trying to find at least some articulable, if imperfect, boundary between what the legislature and what society as a whole should do through democratic institutions, not necessarily free markets, and what is the job of the civil justice system.

I think in evaluating these new age torts, it's entirely fair and it's becoming more and more necessary, to understand that every right that we offer someone implies a countervailing responsibility. We have to understand what that responsibility is, and what that means for the people who live in corporations and what it means for their behaviors and what it means for the meaning of life—frankly, not to get too deep about it. I think courts are better with direct impact, tangible, direct causality cases, than they are with this more esoteric and scientific stuff. This of course is not to say that a direct impact case involving scientific evidence is not justiciable; but only to say that science moves faster than courts and juries, and that some things are not decided in science yet and should not be decided in courts.

The more complicated that causality mechanisms become, the more attenuated they become, the more we, in the civil justice system need to say, "Hey, wait a second! This is not a matter of justice and fairness anymore; this is a matter of something much more complicated, involving many more constituencies than I could ever have in my courtroom." And at that point my so-called judicial humility doctrine might kick in.

The fundamental point for me throughout this whole conference and this panel is that too often the social justice system becomes the ultimate arbiter in our society because it offers the false appearance of being fully funded. In fact, for the most part, on day-to-day direct impact torts, we *are* fully funded. People do not focus on this, but on "new age" the stuff we are *not* fully funded.

Our society has made a conscious decision that we will not impose taxes to compensate victims of traditional direct impact torts. There you

have your risk allocated; courts need to do justice on the facts and law; and you don't need to re-decide the basic question "who decides?" We have also made, in effect, a societal and political decision that certain injuries are not wrongs, or cannot be redressed, or should not be paid for through taxes or mandates. However, lawyers—being goodhearted people and inhabiting one of the few professions that has a mandatory pro bono aspect to what we do, and an ethical mandate of "independence"—simply cannot leave any problem unsolved until we try to tackle it. As a result, we have created an environment in which we're only *pretending* to be doing risk allocation for society. It is doubtful that we were actually appointed for this job. And if we were in fact appointed, I think that appointment was unwise at best, and we should do our best to re-recruit the rest of society to help us with the assignment.

JUDGE TENNILLE: Do you have any questions for John?

PHILIP K. HOWARD: How would health courts work? So, this idea has been developed in a joint [inaudible] case [inaudible] compensation system in which you would have full time judges who just did medical malpractice cases. They would have funding for neutral experts, and there would be a trial, and you would even do a special medical appellate court with written rulings in each case and standards of care. The goal would be to minimize the cost and time of the current system, which consumes upwards of sixty cents on the dollar in legal fees and [inaudible] costs with an average of five years [inaudible].

It's hard to imagine a worse compensation system while having all these second-level effects of defensive medicine, decline, and [inaudible]. There would be an appeal up to the regular court system, but only for issues of a constitutional nature. It's not unlike other administrative compensation systems and justified constitutionally the same way workers' compensation or other systems have been justified, but it's overall better for the constituency.

We've done maybe a dozen public forums over the years on it, at Brookings and elsewhere. There's a lot of material on our website, www.commongood.org, and a lot of commentary about it. Virtually everyone in healthcare is in support of it, including the large consumer groups like AARP, virtually all of the patient safety experts, and President Obama wrote a letter to the Congress in March saying he would support it. The Plaintiff's Bar does not like it, and has opposed it successfully so far. We're just trying to do pilot projects at the moment. It's designed to be quicker and better for whoever's right; but most importantly, it's designed to be consistent, based on current medical standards of care.

UNKNOWN: Phil, that's not a no-fault system, right? You still have to prove fault in the health court.

PHILIP K. HOWARD: You have to prove that it shouldn't have happened, that's correct.

UNKNOWN: Because on the surface it sounds like workers' compensation, which was the great constitutional bargain of the progressive era; where it said we're going to take away your common law right to sue, but we're going to replace it with this reasonable quid pro quo—a system that provides you a remedy, and you don't have to prove fault. So there's a big difference between this and workers' compensation. Don't walk away thinking they're the same.

PHILIP K. HOWARD: There is a difference, but there's a vaccine liability system—administrative law system—that involves finding the causal relationship [inaudible] constitutional. I'm sure [inaudible]—but we're not too insecure about that. But maybe we can meet in the courtroom on it.

UNKNOWN: I expect we will.

JUDGE TENNILLE: Any other questions? Let's thank our panel.

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1 *See* Marbury v. Madison, 5 U.S. (1 Cranch) 137 (1803).

2 *See* Bill Johnson's Restaurants, Inc. v. NLRB, 461 U.S. 731 (1983).