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PERSPECTIVES ON LIABILITY: THE US versus THE UK

By Richard H. Murray
Chairman, Minet Professional Services & Minet Insurance Brokers

While the exposure to various forms of third party liability is great in both the UK and the US, it is widely believed that the problem is more burdensome for US businesses and those who insure them. The escalating pace of judgements and settlements in the UK during the past 5 years puts that assumption to the test. Meaningful measurements are difficult to obtain because the relevant data has no universal repository, and those who possess the data have legitimate proprietary reasons to resist disclosure. Nevertheless, after 25 years of dealing in various fashions with the liability exposures of the multi-national business and professional communities, the assumption of US "leadership" in the liability parade is one that I find quite appropriate.

Indeed, a comprehensive study recently published by the American Law Institute concluded that third party liability recoveries in the US had become a severe problem, both in the quantum of damages awarded and in the inequitable ways in which the system operates. The tendency for the American legal system to produce and sustain punitive damage awards illustrates the problem. The Association for California Tort Reform recently reported that in California alone during the past 10 years punitive damage awards exceeding $100,000 have accumulated to nearly $1.5bn. The Association suggests that if the pattern were similar throughout the US, the punitive damage exposure for the 1980s would be about $12bn, though I would not expect to find all of America quite as rabid in these matters as California.

The differential between US and UK experience is usually attributed to the combined effect of three structural factors:

- The availability of class action representation rights in the US legal system.
- The right to have civil damage claims tried before juries in the US.
- The deterrent effect in the UK of the right of recovery of costs by successful defendants, which exists in only very limited ways in the US.

I acknowledge the very strong influence of each of these factors, but I believe they are

themselves symptoms rather than underlying causes. In my view, the fundamental difference lies in the comparative social fabric of the two countries. Britain's long history of class orientation reflects a European sensibility that nobility tends to reside with the Monarchy at the top of the scale, and to be manifested in larger quantities among the affluent and successful than among the general populace.

By contrast, America's relatively short history has been dominated by a spirit of populism that rejects the legitimacy of class distinctions – a not surprising consequence of the motives and character of the masses of European ancestors whose emigration created the current American culture.

For purposes of this analysis, the essential feature of populism is its assumption that true nobility is to be found at the lower end of the economic spectrum. The "common man" is deemed more likely to be a worthy citizen than the affluent and successful, whose very success is suspect and perceived to be the result of greed and cunning rather than a product of noble character and effort.

The effect of this aspect of the social covenant on the legal system and on theories of liability is substantial:

- Large awards for physical or commercial injury are deemed to achieve the valuable social objective of rewarding the just and redressing the abuses they tend to suffer at the hands of the powerful. The tendency to be influenced by these basic assumptions is not limited to jury dynamics, but influences the pattern of judicial awards as well.

- The frequency and size of punitive and exemplary damages is the systemic manifestation of a desire to punish the powerful and deter them from continuing the assumed pattern of abuse.

Claims against large firms of professionals illustrate these dynamics all too frequently. The spirit of the day in America is well captured by an article by Davis J. Howard, published last Autumn by an institution no less august than the American Bar Association. Under the title "Accountants Should Be Held Liable" Mr Howard approaches the topic with a single minded ferocity that would have pleased Attila the Hun. He suggests that auditors are preferred defendants because

> *"it is likely that they will have appropriate errors and omissions insurance in place, with high limits of liability. By contrast those who mismanaged or defrauded their own concern may well have been remiss in purchasing adequate*

– or any – directors and officers coverage ... the larger ones, especially, are typically organised as general partnerships and have deep pockets...."

Mr Howard, who is an attorney, goes on to note that one should sue auditors even where the real perpetrators of fraud (who have deceived the auditors as well as the general public) have adequate insurance because their policies are likely to have fraud exclusions leaving the honest but unfortunate auditors as the prime recovery target.

Mr Howard blandly goes on to suggest that:

".... in order to induce an earlier and more favourable settlement, the liquidator will wish to charge the auditor not merely with negligence or breach of contract, but also with common law and statutory fraud (such as RICO), because the latter count creates the prospect of recovering punitive or treble damages as well as costs and counsel fees."

RICO is the acronym for the infamous Racketeering Influenced and Corrupt Organizations Act, passed in the late 1920s by the US Congress virtually without debate. Although intended to permit civil damage recoveries from real gangsters, it has been applied almost exclusively against honest institutions. Reluctance to sue the Mafia for damages speaks well of the prudence of US lawyers.

Mr Howard dismisses the problem of proving fraud against accountants by noting that:

*"As well established body of law provides that a trier of fact may infer actual fraud by auditors on the basis of evidence of gross negligence, recklessness, or a wanton disregard for the accuracy of the evaluations of their clients' financial statements .... **It is but a short, short distance from negligence to fraud when it comes to suing independent auditors."*** (emphasis added.)

It is symptomatic of the underlying assumptions about the social value of large liability awards that comments such as these should be condoned by the American Bar Association and pass largely unnoticed. However, the UK business and insurance community should not lightly overlook these trends and conditions in the US with an assumption that the British social fabric and the differences in legal framework will prevent such excesses from traversing the Atlantic.

The germs of the ailment arrived in the UK with the flood of American commercial influences following the "Big Bang" of financial deregulation in the 1980s. The

consequences of it can be followed daily in the financial press accounts of the major fraud trials now under way, in the number and significance of DTI investigations, and in the sudden litigiousness within the Lloyds community. Any sense of complacency should have been dispelled when Her Majesty's Government elected a few years ago to sue a major US professional firm, which had the misfortune of involvement with the De Lorean affairs in Northern Ireland, charging fraud and seeking treble damage recoveries under the RICO statute. The "short, short distance from negligence to fraud" manifest in that complaint is a fine reflection of the advice in the ABA article. If indulgence in American excesses is fine for Her Majesty's Government, can it be very far behind for her citizens?

Initiatives have begun in the US to treat some of the symptoms of the disease. A wide range of Tort Reform initiatives were undertaken following the mid-1980s hard market crisis of liability insurance capacity. Although the early initiatives were promising, the lengthy process of achieving legal and regulatory reform, coupled with the return of capacity, undermined most of those efforts. However, continuing attention is being paid to some of the most pernicious conditions requiring correction, including the need to revise "joint and several" liability rules and to constrain the award of punitive and exemplary damages.

Regrettably, I do not expect Tort Reform to achieve any significant successes in either the US or the UK until there is a general recognition of the nature and causes of the problem. Those who assume that liability insurance represents a "bottomless well" of resource that can be drawn upon to benefit society's noble victims must be made to understand that there is another side to the coin: excessive liability awards bearing little or no relation to the fault of the defendant, also represent a "bottomless pit" for the insurance industry and its clients.

1991 LONDON COLLOQUIUM

One hundred and seventy nine delegates and accompanying persons attended the 1991 BILA Colloquium held at University College London between 17th and 19th July. The subject matter was "Green Issues and Insurance Law" and delegates came from no less than twenty four countries as far apart as Japan, Taiwan, Argentina, Australia, Canada and United States. Nearer to home we welcomed delegates from Poland, Hungary and Rumania as well as the majority of the other European Countries which included fourteen delegates from Sweden alone.