

A MACKINAC CENTER REPORT

JAN. 19, 1989

TORT LAW AND THE PRODUCTS LIABILITY INSURANCE CRISIS

by: Bradley A. Smith

Table of Contents

I.	INTRODUCTION.....	2
II.	THEORIES OF THE CRISIS.....	3
	Industry Collusion.....	3
	The Underwriting Cycle.....	4
	The New Litigiousness.....	5
	Insurance and the Changing Tort Law.....	7
III.	HOW INSURANCE MARKETS WORK.....	9
IV.	THE JUDICIAL REVOLUTION IN TORT LAW.....	11
	Causation and The Insurance Rationale.....	11
	Contract and the Endless Warranty.....	12
	Products Liability in Michigan-- The Insurance Rationale Revisited.....	16
	Joint Tort-Feasors and Risk Prediction.....	19
	Erosion of Affirmative Defenses.....	21
	Damages for All.....	24
	Summary - What the Court Hath Wrought.....	24
	... And Who Pays.....	25
V.	TORTS AND INSURANCE - SAVING THE SYSTEM.....	27
	Damage Caps.....	27
	Joint Liability.....	27
	Independent Design Standards.....	28
	Putting Meaning Back Into Causation.....	28
	Restoring Contract.....	30
VI.	CONCLUSION.....	32
VII.	ENDNOTES.....	34

published by:

The Mackinac Center, 119 Ashman St., P.O. Box 568, Midland, MI 48640: (517) 631-0900

I. INTRODUCTION

“Sorry, your policy is canceled,” proclaimed Time Magazine in a 1986 cover story. [1]

From 1984 through the summer of 1986, the news was saturated with stories of cities, non-profit groups, and businesses being left without liability insurance as a result of skyrocketing premiums and, in some cases, an unwillingness of insurers to underwrite liability coverage at any price.

As a result, cities and school districts have limited the use of parks and playgrounds, and products as diverse as vaccines, IUDS, American Motors “CJ” Jeeps, advanced aircraft ignition systems, and safer substitutes for asbestos have been withdrawn or withheld from the market. [2] In one recent survey of corporate chief executives, approximately one-third admitted they had not introduced new products due to concerns over liability and/or a lack of available or affordable insurance coverage. [3]

Various tort and insurance reforms enacted in over 40 states have alleviated the crisis somewhat, but few would maintain the problem is solved and concern over the issue remains high. [4] The problem has been greatest in the fields of medical malpractice and products liability insurance, reaching into such diverse areas of product liability as vaccines, general aircraft, sports equipment, ski lifts, and intrauterine devices. [5]

This study’s underlying hypothesis is that insurance markets reflect the world they insure. Thus, if products liability insurance is in crisis, one should look to the law governing products liability for the origins of that crisis. A review of recent products liability jurisprudence yields the most convincing explanation for the current crisis-- specifically, that a judicial mindset focusing on compensation rather than individual rights and causation has destabilized insurance markets. Since these markets rely on predictability, loss of stability has forced insurers to guess at future risk exposure. As protection from this lack of predictability, insurers have imposed what has been dubbed an “uncertainty tax” on insurance buyers. [6] In more extreme cases, the destabilization of the market has been so severe that insurance is simply no longer available.

This study begins with a critique of several common explanations for the crisis. Part III reviews certain factors vital to the proper functioning of insurance markets. Part IV then surveys current products liability law in Michigan and discusses its effects on these insurance markets. The study concludes by suggesting a few basic reforms aimed at addressing the problem, and offers a brief sketch of a properly functioning liability system which, the author believes, would both assure the availability of products liability insurance and create a more just, stable system for business and consumers.

II. THEORIES OF THE CRISIS

Three theories are popularly advanced to explain the insurance crisis. The first holds that the crisis is a contrived one, brought about by collusion among insurers looking for legislation to help them boost profits. The second theory suggests that the crisis is temporary, the result of what is known as the “underwriting cycle”. The third argues that America is suffering from a massive surge in tort litigation. This newfound determination of Americans to take every claim to court is supported, so this third argument goes, by “liberal” juries all too eager to make large damage awards against impersonal manufacturers and their insurance policies, in order to assist the visibly injured plaintiff seated before them.

This section will briefly examine the legitimacy of each of these theories, and suggest a fourth possibility that has been little discussed in the popular media or the political arena-- that the products liability insurance crisis is the natural result of an effort by a large segment of the legal community, including much of the judiciary, to change the underlying purpose of the tort system.

Industry Collusion

According to the theory of industry collusion, insurers have conspired to raise their prices and, to justify these price hikes, have manipulated their books to create a false appearance of financial distress.

This theory cannot be irrefutably disproved, but it is both factually and theoretically improbable. First, it contemplates what would surely be the broadest conspiracy in American anti-trust history. Over 3500 insurance companies are licensed to underwrite property and casualty insurance in the United States. It seems highly unlikely that so many companies have in some way conspired to control prices. The more plausible fallback position of the conspiracy theorists is that such a broad conspiracy is unnecessary. They claim that a handful of large insurers dominate the market and effectively control prices. A pending lawsuit, joined by the Attorneys General of nineteen states, alleges that 31 defendant insurers and co-conspirators have conspired to narrow coverage and in some way prevent their 3500 competitors from offering broader coverage. [7]

Even if we accept that this more limited conspiracy could be pieced together, many factors suggest that it has not. For one, the ease with which one can enter the insurance market (little fixed investment is required) would make it very difficult to protect such a monopoly. Second, conspiracies to raise prices are normally successful only where the sellers have a homogenous product. When the product differs in quality and/or design and manufacture, price fixing is more difficult, as it is both harder to agree on a price and easier for cartel members to cheat on that price by varying design or selling different quality goods.

It is hard to imagine a less standardized product than products liability insurance, the line of coverage in which the crisis has been most acute. Because the liability for a pharmaceutical company manufacturing vaccines differs so radically from that of a hardware manufacturer producing claw hammers, products liability policies tend to be tailored to specific customers. If insurers wished to conspire to raise prices and profits, why not do so in more uniform lines, such as fire insurance, in which a standard policy is used nationwide, or workers’ compensation or auto insurance, in which state laws require standardized coverage? Price fixing would also be difficult in products liability because insurers could cheat through premium dividends and discretionary credits against filed rates.

The collusion theory is also inadequate to explain why some insurers are withdrawing from the market completely, or refusing to underwrite certain types of insurance at all. The purpose of a price conspiracy is to raise the price at which goods are sold-- not to stop selling goods.

Even more baffling, for conspiracy theorists, must be the fact that the crisis has also affected self-insured municipalities, manufacturers, and non-profits. If the only problem were an insurance industry conspiracy, one would expect self-insureds to be insulated. Instead, they have been among the hardest hit.

Furthermore, the collusion theory fails on the facts. Its proponents argue that insurers have doctored their books to create the appearance of financial hardship where none exists. Insurers, they claim, have made unnecessarily large upward adjustments in the reserves they maintain to make future payouts on liabilities already incurred but not yet settled. These reserves are carried on the books as a liability (the money being earmarked to pay claims), thus making the insurers books look worse than they are even as the insurers collect interest income on the money set aside to cover the reserves. In fact, however, the available data strongly suggest the opposite conclusion-- that insurers have, in recent years, underestimated their needed reserves. For example, by the end of 1984, insurers had already paid out more than 100% of the funds reserved for claims occurring prior to 1976-- yet claims continue to be paid on these old policies. The numbers show the same pattern almost regardless of where one chooses to begin-- reserves set aside ten years ago, for all claims prior to 1979, were also all paid out by the end of 1984, though claims on those policies continue to roll in. [8]

The doctored books argument again fails to explain why insurers have manipulated reserves only in certain commercial casualty lines and not in others. And it still fails to account for the refusal to sell at any price. [9]

The collusion theory has been dismissed by both the Federal Trade Commission and the Antitrust Division of the U.S. Department of Justice. [10] An independent advisory commission appointed by New York Governor Mario Cuomo also rejected an insurance industry conspiracy as an explanation for the problem. [11]

Like all conspiracy theories, the idea of insurance industry collusion to set prices can never be firmly disproved-- its proponents can always argue that the smoking gun simply has yet to be found. However, given the factual evidence and theoretical arguments against it, this theory seems inadequate as a basis for public policy.

The Underwriting Cycle

A second theory, which most parties agree holds some validity, but which is nevertheless inadequate to explain the magnitude of the present crisis, is based on the underwriting cycle.

The theory of the underwriting cycle, simply put, is that insurers engage in price competition which causes falling premiums. Because insurers often don't know whether a particular price was correct until years later, when all claims resulting from that policy have finally been settled, it is easy to "guess" incorrectly, and continue price cutting until premiums become inadequate. Later, when the losses roll in, prices are raised to reflect the true, nature of the risk. Income rises, and new capital enters the market to buy up insurance stock, undervalued from prior losses. The companies return to financial health, and a new round of price cutting begins.

The particular severity of the cycle in this decade is explained by the extremely high interest rates of the 1979 to 1981 period. During this time, insurance companies cut rates in search of market share, and used the extraordinarily high interest income to cover losses from claims. When interest rates plummeted later in the decade, the insurers were left with thousands of new policies written at inadequate premiums. Insurers accused of irresponsible “price gouging” under the collusion theory are accused here of irresponsible competition.

This theory has some validity, and to the extent that interest rates have stabilized and policies been rewritten at new, higher premiums, it may help to explain what seems to be a gradual easing of the insurance crisis since its 1986 peak.

Yet if the problem was nothing but the underwriting cycle, exacerbated by insurance price cutting aimed at capturing premium dollars to invest at high interest rates, why have its effects been concentrated in a handful of liability lines? Why has there been no corresponding crisis in automobile insurance, [12] fire insurance, or at least in other “long-tail” lines such as workers’ compensation insurance? There must be something more.

The New Litigiousness

A final popular explanation for the liability insurance crisis is that the American people, for some indeterminate reason, have suddenly become more litigious, more eager to take perceived wrongs to court, and that judges and juries have supported this tendency by granting recovery more often and awarding higher damages than in earlier times.

This seems to be the theory that has motivated most of the forty-two state legislatures that have formed their tort systems in recent years. Proposals to cap damages, limit lawyers’ contingency fees, or restrict access to the courts would seem to be based on the idea that the number of suits and the amount of awards have gone beyond reasonable bounds.

To test the veracity of this theory, we must examine the answers to a series of questions: is it true that there is more litigation than in the past; do plaintiffs in fact win more often; are damage awards higher than before; and if so, why?

1. Is there more tort litigation than before?

Approximately 95% of all tort cases are filed in the state court systems. [13] Because many state courts do not differentiate between the various types of civil lawsuits filed (torts, contract and commercial disputes) the growth in tort litigation can only be estimated. Nonetheless, the growth of tort suits seems to be slow and gradual: the National Center for State Courts (NCSC), a private, non-profit group, estimates it at just 2.3% per year between 1981 and 1984, the period over which the current insurance crisis materialized. [14] The RAND Corporation’s Institute for Civil Justice (ICJ) places the growth rate slightly higher, at 3.9%. [15] This growth rate is lower if adjusted for population growth.

However, this is not the whole story, because this data lump together all types of tort cases, including products liability, where the insurance crisis has been concentrated, and more “routine” cases, such as automobile accidents. In an attempt to determine the relative growth rates of different types of tort cases, ICJ extensively analyzed data from Cook County, Illinois (Chicago), and San Francisco, two districts for which reliable data is available. The results show that auto injury cases have increased at roughly the same rate as population growth. However, other personal injury cases, in particular products liability

cases, have grown at a much faster rate than population. The most explosive growth of all is concentrated in the area of mass torts, such as DES [16], asbestos, and agent orange litigation. [17]

These findings correlate strongly with the thesis of litigiousness. They would not only seem to explain why an insurance crisis exists, but why it is concentrated in particular lines—namely, products liability, medical malpractice and certain other commercial liability lines—but not in auto, fire, and others. However, it is not clear just why people should suddenly be more eager to take only certain types of claims to court.

One explanation might be that there are simply more of these types of torts occurring. However, this possibility, once injuries are adjusted for population growth (as with the figures on the number of tort suits) is probably incorrect. As societies grow wealthier, they grow safer:

“There is hardly a product in use today-- a car, plane, boiler, municipal water system, drug, vaccine, or hypodermic syringe-- that is not many times safer than its counterpart of a generation or even a decade ago.” [18]

Likewise, disease, including cancer, has sharply decreased on a per capita basis. [19] Who can doubt that today’s physicians are more skilled, and have better facilities at their disposal, than those of fifty years ago? Today life expectancies are far longer, and accidental deaths per capita far fewer, than fifty years ago. Our world is more complex, but it is nonetheless far safer.

A second explanation for the fact that lawsuits are increasing rapidly only in select lines is the theory that a glut of lawyers has resulted in frivolous lawsuits, and/or more legitimate lawsuits. Presumably, these suits are concentrated in products liability lines because such suits are the most lucrative for attorneys. While there are certainly more lawyers than in decades past, this theory falters on examination.

We would not expect such a pattern to continue if plaintiffs were not able to win a significant number of these suits, since the costs of instigating and carrying forward a lawsuit, particularly in such complex areas as products liability and mass torts, can be as devastating to plaintiffs as to defendants. While it is often pointed out that plaintiffs, paying contingency fees, have little to lose from filing a lawsuit, it is overlooked that the lawyers in such a case have little to gain from a frivolous suit.

So if plaintiffs are winning these new suits with greater frequency than before, the question is why? One possibility is that many people who have had legitimate claims in the past have been unable to bring them to court, either because they did not know their rights or because they could not find an attorney, in which case the increase in litigation should be considered a good thing. [20] A second possibility is that rules of law have been changed in a way that encourages, and makes plaintiffs more likely to be successful in a legal action. Before considering this latter proposition, we should first see if, in fact, plaintiffs are more likely to win lawsuits or get higher damages awards than in the past.

2. Are Plaintiffs More Likely to Win Verdicts or Large Damage Awards Than in the Past?

Again studying data from Cook County and San Francisco, ICJ determined that, “median awards have been strikingly stable over a 25-year period.” (The median is the midpoint in the distribution of jury awards.) However, when the data was separated by types of claims, ICJ found that, “the median for product cases has risen very sharply.” Looking next at average awards in each jurisdiction, ICJ found that the average award in Cook County, adjusted for inflation, increased from \$59,000 in the period 1960-1964 to \$187,000 for 1980-1984. In San Francisco, the increase was from \$66,000 in 1960-1964 to \$302,000 in 1980-1984. Though this upward trend did apply to routine torts such as auto accidents, the

most explosive growth, ranging from 200 percent to more than 1000 percent, came in the areas of products liability and professional malpractice. [21]

Furthermore, ICJ found that plaintiffs were “clearly” more likely to win in the 1980s than they had been 20 years earlier. Multiplying the probability of winning a lawsuit by the average award, ICJ created an “expected” award, i.e. what a plaintiff was likely to receive for what might be deemed an “average” suit. The result showed that over the study period, the expected award for routine torts, adjusted for inflation, rose by 140 percent to 260 percent, while the expected award in products liability cases rose between 400 percent and 900 percent. [22]

Finally, the data showed that:

... juries are likely to award substantially more money in a product liability, malpractice, or work injury case than in an auto accident case for an injury of the same degree of severity. And the premium awarded to these kinds of cases has been increasing over time. Juries also award more money when the defendants are institutions or organizations rather than individuals—the ‘deep pocket’ effect. (Emphasis in original). [23]

It would appear from the ICJ data, then, that there has been a real increase in both the value of damage awards and the probability of a plaintiff winning his case for all types of torts. However, in auto and other routine torts, neither increase seems sufficient to set off any type of insurance “crisis”. Nor has there been any real increase in the number of routine tort suits filed. However, in products liability cases, all three factors-- the number of lawsuits, the probability of winning, and the average damage award,-- have skyrocketed over the past 25 years, with the fastest growth coming in the 1980s. [24]

This would indicate that those who claim the crisis is the result of a new litigious attitude throughout society are, to a large extent, correct. Further, the solutions widely proposed, such as caps on awards and forcing cases into private arbitration, should have a positive effect. But this answer continues to beg the question of why this change should be taking place, and why only in certain types of tort cases and not in others.

It is possible that social, anthropological, and psychological explanations may be available to account for this phenomenon. However, it is more likely that these trends towards more lawsuits and higher damages in certain types of cases are the result of changes in legal doctrine that have made such lawsuits more profitable for plaintiffs. Failure to recognize these changes as the root cause of the problem leads to an incomplete understanding of the problem and, thus, to solutions that may have positive effects but are equally incomplete.

Insurance and the Changing Tort Law

The liability insurance crisis cannot be explained or solved by reliance on unsupported conspiracy theories. Nor can it be written off as a one time aberration caused by a confluence of the underwriting cycle and abnormally high interest rates.

The ICJ data supports the theory that the problem is simply an increase in the amount of litigation and the size of damage awards, but that alone suggests no cure. We must understand why such litigation is increasing, why plaintiffs win more often, and what this does to insurance markets. To do so, we must examine the progress of tort law over the past half century, and relate changes in the law to a handful of fundamental insurance concepts.

A revolution has occurred in tort law. This change is not so much in the formal doctrines of law as in the way in which judges conceptualize and apply those doctrines. This dramatic change, steadily accelerating in pace, has come about with virtually no action on the part of state legislatures, in Michigan or elsewhere. It is a judicial revolution, brought about by well-meaning judges and legal scholars armed with a theory of distributive justice, little knowledge of insurance, and no coherent system for determining right and wrong.

In putting this new system into place, the judiciary has not only created more causes of action for potential plaintiffs, leading to the visible effects of more awards and higher damages, but it has undermined the risk predictability on which the insurance industry relies, and thus made it virtually impossible for the industry to cope with the rising tide of liability. Higher premiums and, in some cases, a complete closure of the market have resulted. It is the contention of this study that while many factors have contributed to the insurance crisis of the 1980s, herein lies the crux of the problem, and until it is attacked, “the sort of reforms enacted thus far are likely at best to slow the rate of premium increases over the long run.” [25]

III. HOW INSURANCE MARKETS WORK

To understand the manner in which changing tort law has created a crisis in the insurance industry it is necessary to review the foundations of insurance underwriting.

Insurance pulls together a large number of risks in order to create a certain predictability. For example, a single homeowner may know that the odds are that only a few houses in his neighborhood will catch fire, but he cannot know whether or not one of those houses will be his. Thus he must either set aside enough money to rebuild his house in the case of a loss, or risk a total loss with no reserve. Saving individually, the homeowners would have to set aside a sum equal to the total value of all their homes. However, by combining with neighboring homeowners, each owner need only contribute an amount sufficient to assure that the total will cover the few expected losses, regardless of which owners suffer those losses.

While most people focus on the concept of large numbers, it is the predictability created by large numbers that is vital to the insurance function. That predictability comes not just from the law of large numbers but from the relative stability of the sources and causes of risks, in this case fires. A sudden but uncertain change in the statistical probability of fires would leave uncertainty as to how much money must be in the pool to cover losses. The prudent course for our group of homeowners, then, would be to charge each owner a bit extra to cover these possible extra losses-- what might be called an "uncertainty tax."

But our owners face another problem. Some of the houses in the neighborhood are made of wood. They have old wiring systems and occupants who keep gas cans and old rags in the basement. Other homes are brick, with new wiring and tidy owners. If each homeowner is charged the same price, the brick owners, who are less likely to suffer a fire, end up subsidizing the wood home owners, who are at greater risk. Some of the brick owners will decide this cost is not worth bearing, and will choose to drop out of the risk pool (or they may join other good risks and form a new insurance pool). With the better risks leaving the pool, the remaining, poorer risks, must pay a bit more. This will encourage the best remaining risks to leave the pool, and the cycle repeats until the original pool falls apart. This process is known as adverse selection.

The insurance function controls this process by subdividing the large risk pool back into smaller pools. Lower risks (the brick owners) will pay lower premiums, while higher risks (the wood owners) pay higher premiums. If, for some reason, the insurance function is not able to break the larger pool back into smaller pools of similar risks, the better risks will either cease the activity (in this case, it is unlikely they will cease living in homes, but they may move to different neighborhoods, leaving only higher risks individuals in the original neighborhood) or they will find a method to self insure, i.e. cover their risks themselves. Either way, the original pool breaks down. If an insurer is required to charge each customer the same amount for insurance, adverse selection will be the inevitable result, with a corresponding collapse of the insurance market and rapidly rising premiums. Yet, as we shall see in Section IV, this is precisely what the new tort law requires insurers to do.

The insurance function also relies on risks being independent of one another. Suppose, for example, that a fire in one house automatically caused a fire in every other house in the neighborhood; any one fire would result in a total loss to all homeowners. Each homeowner would be back in the original position of having to insure the total value of his home, since the total probable loss would equal the sum of the value of all homes. There would be no way to spread the risk. Looking at it another way, it is important that the outcome in one case not affect the probability of accident for the other risks in the pool. Inter-

related risks such as nuclear war cannot be insured against, as the purpose of insurance is to group together independent probabilities to predict losses statistically.

The insurer must also guard against what is termed “moral hazard” on the part of the insured. That is to say, the insured should not be able to benefit from his own “hazardous” behavior. Thus, fire insurance on a home is not written for more than the home’s value, lest the insured benefit from the destruction of the home. Likewise, health insurance usually includes deductibles and co-pays to give the insured an incentive to minimize expenses. A fundamental precept of insurance, then, is that the accident victim must have incentives to take precautions on his own.

Two other aspects of products liability insurance must also be kept in mind in considering the causes of, and solutions to, the liability insurance crisis. First, although insurers sell their products liability policies to manufacturers, the true insured risk pool is made up of consumers. In other words, liability insurance, unlike, say business interruption insurance, ultimately pays benefits to injured consumers, not the manufacturer holding the policy. Thus an insurance company underwriter, or a self-insured manufacturer, is attempting to guard against moral hazard, risk interdependence, and adverse selection not only in the products and manufacturers insured, but in the consumers using those products.

Second, in dealing with the effects of judicial decisions on products liability insurance, it is important to remember that rates for products liability are based on nationwide premium and loss data. This occurs partly because there are fewer state regulatory peculiarities to be met than in products such as workers’ compensation insurance, and partly to assure an adequate sample size from which to predict losses. However, the more obvious reason for this is that in a modern economy almost all marketing is done across state lines. This means that products liability cases may frequently be brought in multiple states. Thus rates in Michigan will be affected by legislative and judicial decisions from California and New Jersey, and vice-versa.

Yet liability changes at the state level remain important. Changes in Michigan may have a small but direct beneficial effect nationwide. Further, the pattern of law is such that changes in one state frequently wash over to set judicial precedent in other states. And, despite the growth of interstate commerce, Michigan corporations are more likely to be sued in Michigan-- in particular, small businesses whose role in interstate commerce is limited can realize gains from action in their home state.

In Michigan, there is much that can be done to reform the tort system and restore liability insurance markets to good health.

IV. THE JUDICIAL REVOLUTION IN TORT LAW

Causation and the Insurance Rationale

Historically, the role of tort law was to redress attacks on an individual's personal interest. Such attacks could take the form of assault and battery to one's person, damage to one's land or property, or other traditionally recognized claims such as fraud or interference with business relationships.

If a harm was caused, the tort-feasor's intent was irrelevant. However, the tort-feasor had to cause the harm. Because the term "cause" can be stretched to extremes—one might go so far as to say that the mother of a criminal, having bore him, is the "cause" of the perpetrator's crime—courts further developed the idea of "proximate cause". By proximate cause, the courts intended to limit defendants to those who had been the direct source of the injury. While this was a concept that could always be stretched and tested by extreme cases, for most people, in most cases, the ideas of "cause" and "causation," retained meaning.

The revolution in judicial thought that is at the root of the present liability insurance crisis has cut a wide swath through traditional jurisprudence governing products liability, including such tort doctrines as negligence and such contractual theories as warranty and privity. However, its fundamental goal, and result, has been to destroy the idea that liability should be based on causation.

The assault on Causation stems from a school of legal thought that began to grow to prominence in the years prior to World War II. Heavily promoted by Fleming James of Yale Law School, this school held that the fundamental role of the tort system was not to right individual wrongs, but to guarantee that the unfortunate victims of accidents received compensation from some source [26] In this scheme of things, fault was not as important as guaranteeing compensation from some source, whether at fault or not.

This idea not only seemed compassionate, but since an injured person imposed costs on society, in the form of lost work days, medical bills, and social welfare services, assuring a source of compensation regardless of fault seemed efficient. Of course, these crusaders missed the obvious-- forcing an innocent person, corporation, governmental unit, or non-profit organization to pay for an accident it did not cause is hardly a standard of compassion that most Americans would accept in their ordinary dealings. Since compensation must come from somewhere, the cost is still imposed on society-- the burden is just shifted around. As we shall see, the process of shifting this burden has serious, harmful side effects for insurance markets, and ultimately, for progress and innovation.

The new judicial theory called for the creation of a new system of third party insurance, paid for by manufacturers through their liability insurance. According to the theory, these manufacturers will spread the cost of this insurance through society via incremental price increases. These ideas first entered the formal legal system in a concurring opinion by Justice Roger Traynor of the California Supreme Court in the landmark case of Escola V. Coca-Cola Bottling Co.:

[P]ublic policy demands that responsibility be fixed wherever it will most effectively reduce the Hazards to life and health inherent in defective products... Those who suffer injury from defective products are unprepared to meet its consequences. The cost of an injury and the loss of time or health may be an overwhelming misfortune to the person injured, and a needless one, for the risk of injury can be insured by the manufacturer and distributed among the public as a cost of doing business. [27]

This type of thinking-- that industry should play the role of societal insurer, is often mistakenly referred to as strict liability, i.e. a system in which the negligence, or lack thereof, of the manufacturer is not taken into account. However, it goes far beyond a system of strict liability, for strict liability takes into account causation, whereas the theory outlined by Traynor focuses only on compensation. Or, as one proponent of strict liability has commented, under the system outlined by Traynor in Escola, “why should any plaintiff ever lose.” [28] And, indeed, the natural result of the belief that the tort system’s purpose is merely to determine how to compensate victims of accidents is the present liability crisis.

When a manufacturer can be held liable for an accident it did not cause, it is virtually impossible to predict its liability in advance. The insurer’s ability both to classify risk and to predict future liabilities hinges on predicting the probability of its activities causing harm. But if causation doesn’t matter, these liabilities hinge on the entirely whimsical, unpredictable luck of the lottery as to how many times, and for what amounts, the manufacturer will be chosen as the one to pay the accident victim’s bills. To adjust for this lack of predictability, insurers impose an “uncertainty tax” on their clients or , if the uncertainty seems too large, simply pull out of the market.

In the remainder of this section, we will examine some of the key changes in tort law over the years, by tracing their introduction into Michigan jurisprudence. In the field of torts generally, and products liability more specifically, Michigan courts have usually been followers rather than leaders. In other words, most of the changes which have so twisted our tort system were first enacted by state and federal judges outside of Michigan, and only later filtered into Michigan law. Nevertheless, most of these theories have since been adopted by Michigan courts, either explicitly or implicitly, so that tracing the development of Michigan law also gives us a good feel for what has occurred nationally. Michigan’s theory of “Products Liability,” discussed below, is superficially unique from any other state’s, but in fact, does nothing more than combine and/or rename many of the national trends in products liability. In each area we will attempt to show how these changes have benefited plaintiffs at the expense of defendants, and more importantly, we will attempt to explain why these changes create further difficulties in insurance markets.

Contract and the Endless Warranty.

1. Contract and Tort

There are two fundamental principles around which people can structure their interactions: voluntary agreement, and coercion. In the world of law, agreement is expressed through contract. Tort takes over where agreement has failed or not been made.

A tort suit is filed when one feels his rights have been violated. The role of the court is to determine the rights and responsibilities existing between the parties to the lawsuit.

For example, I punch you in the nose. There is no doubt that I caused your injury. You did not agree to my action. Barring some claim of self-defense, a court is certain to determine that I violated your rights, and hold me liable for your injury.

Contracts, by contrast, revolve around voluntary relationships. In exchange for a certain fee, I agree to paint your house. We might further agree that you will supply the ladders, and I will supply the paint. But there is no reason that our contract cannot go further, and also specify who will bear the risk of something going wrong. Most commonly, I may guarantee, or warrant, my work. I promise that under

normal conditions, the paint job will last at least five years. If the paint turns out to be faulty, I bear that risk.

We might also agree on the distribution of the risk resulting from accidents. For example, you warn me that your ladders are old and rotten, and that if I am concerned about falling I should procure my own ladders. I agree to use yours, but note that I won't buy you a new ladder if it breaks during the painting. I am then injured when the ladder breaks, and sue you for my damages. You claim, correctly, that I had accepted the risk of accident. But when you sue me to recover the cost of your broken ladder, I win on the grounds that you had agreed to bear the cost of that possibility. Even more likely, having agreed to the distribution of rights and responsibilities before hand, neither of us go to court.

This voluntary distribution of rights and responsibilities is fundamental to efforts to manage liability. It allows the manufacturer or seller of a product to place restrictions on its use, or otherwise avoid liability. Contract allows both parties to know in advance what risk they are assuming. Where each side knows in advance both its own obligations and those of the other party, each party has strong incentive to take proper precaution to protect its interests. Contractual allocation of risk allows consumers willing to take risks to gain access to products that a manufacturer might withhold from the market, for lack of insurance, were it liable for all accidents resulting from use of the product. Contract-- the voluntary distribution of risks before an accident, when heads are cool-- is thus a vital part of the risk management and predictability needed for insurers to evaluate a risk.

In addition to its attacks on causation, a major effort of the new tort jurisprudence has been to destroy the voluntary, contractual distribution of rights and responsibilities regarding the possibility of accidents.

This assault began in a most innocuous fashion, with the elimination of a largely dated legal concept called privity.

2. The Abolition of Privity

Most modern products liability lawsuits claim a breach of warranty. A warranty is a representation, or promise (warrant) by the manufacturer or seller that the product meets certain specifications of performance and/or safety-- a guarantee.

Under the early common law in both England and the United States, warranty coverage was limited to persons in privity with the manufacturer or seller. That is to say, a person injured by a defective product was limited to suing the party from whom the product was purchased.[29]. The logic for this limitation was:

...there must be a fixed and definite limitation to the liability of manufacturers and vendors for negligence in the construction and sale of complicated machines and structures which are to be operated or used by the intelligent and the ignorant, the skillful and the incompetent, the watchful and the careless, parties that cannot be known to the manufacturers or vendors, and who use the articles all over the country hundreds of miles distant from the place of their manufacture or original sale... [30]

This rule allowed manufacturers to maintain some degree of control over the warranty that was sold with their products. They could be certain, for example, that the buyer was warned of the proper uses, or trained in the operation of the machine. They were also better able to keep track of potential claimants, and thus better able to monitor their own risk exposure. It was a doctrine based on contract, on

agreement between buyer and seller, and it allowed manufacturers and their insurers to control and predict risk.

In a modern industrial economy, however, the privity rule often makes no sense. Unlike earlier craftsmen, in the modern economy manufacturers typically put products into a broad market through middlemen, who sell the product to the general public without alteration or interim use (indeed, with many pre-packaged goods, use or testing by the distributor is impossible). In such an economy, it is often unfair to restrict a manufacturer's warranty to the immediate purchaser (the retailer), for as Justice Benjamin Cardozo correctly noted in the first U.S. case to broadly strike down the privity rule, "The dealer was indeed the one person of whom it might be said with some approach to certainty that by him the [product] would not be used." [31]

Once Cardozo's opinion in MacPherson v. Buick broke the ice, the states rapidly began to abandon the privity requirement in all warranty cases. Michigan was one of the last states to do so, in 1958. [32]

Even after abolishing the privity requirement, only a buyer or user could recover from the manufacturer on a warranty theory. A person injured by a product who was not a buyer or user could only sue the manufacturer under traditional tort law, which required a finding of negligence. However, Michigan soon after became the first state to push the removal of the privity requirement to the point where a person who was neither a buyer nor even a user of the product was able to recover under a warranty theory.

The case was Piercefield v. Remington Arms Co., Inc. [33] Piercefield was a bystander who was injured when a cartridge manufactured by Remington, and purchased and shot by a third person, caused a gun to explode. After Piercefield, essentially any person injured by any defective product could sue the manufacturer directly under a warranty theory, meaning no showing of negligence was required.

The abolition of the privity requirement was, for the most part, a very positive development in law. It recognized that a consumer who buys, say, an RCA television at an appliance store has a warranty contract with RCA, not the store. But it was not an unqualified good, for many chose to interpret the new rule as denying consumers and manufacturers the right to contractually allocate risk.

If warranty is taken out of its contractual context, then manufacturers and insurers lose the control and predictability contract gives to the risks involved. At the other end of the transaction, the buyer's incentive to learn about the product and to use it correctly are reduced-- the moral hazard problem.

Further, in a few cases-- but often those generating substantial litigation-- the requirement of privity may not be outdated. One such example would be Agent Orange, the defoliant used by the Army in Vietnam and later linked to various ailments in veterans. Here the Army had complete control of the product, and was in as strong a position as the manufacturer to determine any ill side effects of the product, as well as to decided how to use it. Further, it is fair to say that few, if any, veterans truly thought it was the manufacturer's duty to protect them in Vietnam-- they looked to the Army. A similar case might be made for asbestos manufacturers.

Removing the privity requirement makes sense when dealing with pre-packaged goods over which the retail merchant has little or no real control. However, its removal has made it extremely difficult for manufacturers to control their liability, since they can be held liable even when intervening parties may have had considerable control over the product, including, for example, having it serviced, or using it improperly, etc. Its removal has all but infinitely increased the number of potential plaintiffs to whom each manufacturer is liable, adding to the difficulty of predicting and controlling liability.

Abolishing the privity requirement removed a serious obstacle to tort recovery for damages caused by defective products. But it raised problems for insurance markets, and the courts had nothing to put in privity's place to solve these problems.

3. Implied Warranty

If the changes in the privity rule went a bit too far, and created other problems as yet unsolved, they were at least a legitimate use of judicial power-- changes were needed in the privity doctrine, and the changes made were not so much an exercise in judicial legislation as an effort to bring legal doctrine into line with the reality of the modern economy. While the courts were clearly interested in helping plaintiffs recover, it was because such recovery was justified by causation, not simply the desire to see the plaintiff receive compensation from some source. In MacPherson, for example, the plaintiff was injured in an auto accident resulting from a defective wheel which the manufacturer had warranted to be in good condition.

However, it was not long before the courts explicitly embarked on a type of social engineering, attempting to use the tort system to do that which the legislature had declined to do-- create a system of social insurance for accidents.

While Justice Traynor's concurrence in Escola V. Coca-Cola signaled the intent of some judges to make war on the products liability system, it was not until some years after that decision that the battle was actually joined. One early victory for the judges was the creation of an implied warranty.

A lynchpin case was Henningsen v. Bloomfield Motors, Inc. [34] Henningsen's contract to purchase a new car explicitly disclaimed any warranty on the part of the dealer or the manufacturer except one limiting liability to replacement of defective parts for the first 90 days or 4000 miles. Yet after Henningsen's wife suffered injuries in an accident, the court upheld recovery on the grounds that, "[W]hen a manufacturer puts a new automobile in the stream of trade and promotes its purchase by the public, an implied warranty that it is reasonably suitable for use as such accompanies it..." [35] Other than a desire to see Mrs. Henningsen recover for her injuries, there seems to be no logical reason for the court's decision. Absent any element of fraud or duress, the court failed to explain why the explicit release signed by Mr. Henningsen should not be binding.

Traynor's California court soon did Henningsen one better. In Greenman v. Yuba Power Products, Inc., [36] the plaintiff was injured while working with a power tool. The defendant was not negligent and the plaintiff had indisputably violated the terms of his warranty agreement with the manufacturer. The Court finessed this by essentially ignoring any idea that recovery should be based on a warranty theory, refusing to even consider the warranty provisions which might have limited the manufacturer's liability. Wrote Traynor, for the Court, "The purpose of such liability is to insure that the costs of injuries resulting from defective products are borne by the manufacturers... rather than by the injured persons... Sales warranties serve this purpose fitfully at best." [37]

In other words, voluntary agreements made before the accident would be replaced by coercive tort rulings after the fact. And traditional notions of right and wrong, duty and responsibility, were to be swept aside, since the "purpose" of the courts was to make manufacturers pay.

In its 1965 decision, Piercefield v. Remington, [38] extending protection beyond the user or purchaser to encompass bystanders, the Michigan court declared its decision was "for the same reasons" as Greenman, and also endorsed Henningsen. [39] By 1978, the destruction of a manufacturer's or seller's ability to

place any restrictions on its warranty liability in Michigan had become so complete that in Blanchard v. Monical Machinery, the sale of an admittedly, obviously “ancient” machine with clear contract language that the sale was “as is” was found not to place limits on the seller’s liability. [40]

In addition to making it harder for the manufacturer to control his risk once the product is sold, this destruction of limits on warranties also makes it impossible for sellers to do any “underwriting” of their risks, *i.e.* they cannot eliminate certain unacceptable risks in advance, as the seller tried to do in Blanchard.

While the court reasons that sellers and manufacturers should insure the public, it is not clear exactly how an insurance company underwriter or actuary is to estimate the risk to the manufacturer resulting from the resale of an admittedly “ancient” machine, which has been out of the manufacturer’s possession for some years and no longer meets the needs of the original purchaser.

The result of these decisions, for insurance availability and price, should be clear. In Henningsen, the plaintiff expressly chose not to receive warranty coverage, presumably at some cost savings. Certainly, after the fact, such warranty coverage was desired. But in advance, not knowing when or where an accident might strike, the plaintiff had chosen to take his chances. The Court’s decision gives the plaintiff the best of both worlds-- the lower price of the disclaimer, coupled with the protection of the warranty. Insurers, however, are anything but dumb. They will soon charge all consumers the cost of insuring the risk as if no warranty restrictions existed. Those individuals who choose to live by their agreements, or prefer the risk associated with a lower price, are out of luck.

This is not the only ill side effect of the implied warranty concept. Manufacturers are forced to pass the cost of the warranty on to every buyer, which is precisely what the court intended. However, since it is unrealistic, (and in many cases illegal) for the manufacturer to price discriminate between consumers based on their risk characteristics, the result is that high risk individuals pay the same as low risk individuals. When low risk users decide the warranty is not worth the added cost, they can shift to other products or cease their activity. Thus only the poorer risks are left in the manufacturer’s risk pool, and the system begins to unravel due to adverse selection. [41]

The implied warranty, by switching contractual arrangements to coercive tort arrangements, adds to unpredictability and adverse selection that the insurance industry must deal with. The industry deals with it in the best way it can-- through higher premium charges.

Products Liability in Michigan – The Insurance Rationale Revisited

In 1984, Justice Patricia Boyle of the Michigan Supreme Court wrote, “When the societal goal of holding manufacturers accountable for the safety of their products has been threatened by the interpretation of technical rules of law, it has been the rules that have gradually given way.” [42]

Michigan has been more honest than most states in announcing this policy. We have already seen how rules relating to privity and warranties were knocked down in the 1960s. Finally, in 1970, Judge Levin, writing for the Court of Appeals in Cova v. Harley Davidson Motor Co., urged Michigan to quit playing with legal fictions, or trying to force opinions allowing recovery into modes consistent with prior judicial doctrine, and to instead recognize a theory of “products liability” which would include elements of duty and negligence, warranty, and ultrahazardous activity. [43] Wrote Levin, “The ‘product liability’ of the manufacturer... is simply the liability which... the law imposes on the manufacturer... for the loss suffered by reason of a defective product attributable to that manufacturer.” [44] It is fair to say that this

philosophy, though not then explicitly endorsed as Michigan law by the State Supreme Court, was the standard by which Michigan courts operated throughout the 1970s, until 1978, when Levin's suggestions were enacted into statutory law by the state legislature. [45]

The fundamental premise of enterprise liability, as the doctrine proclaimed by Traynor in Escola is widely known, is that causation is a hopelessly tangled web which is beyond the court's ability to determine. Therefore, the basis for deciding a tort claim is the ability of the defendant to pay damages. Michigan courts claim to have steadfastly refused to adopt Traynor's form of "strict liability" [46] However, the risk-spreading rationale of enterprise liability has nonetheless had its effect.

Much of the movement to eliminate archaic legal rules was legitimate and beneficial. But for all the problems they sometimes caused, rules such as privity and contractual concepts of warranty did serve valuable purposes. The emphasis on striking down barriers to recovery has inevitably led to a breakdown of all restrictions on recovery, including the fundamental element of causation.

As we examine just a handful of Michigan cases decided under the new rationale, the reader will note the extent to which causation and contract have been rendered meaningless before this judicial onslaught.

In Rutherford v. Chrysler Motors Corp., [47] the court determined a manufacturer had a duty to build a "crashworthy" car. Thus when the plaintiff's car skidded on ice and smashed into a bridge abutment at a speed of approximately 35 miles per hour, through no malfunction of any kind on the part of the car, the plaintiff was still allowed recovery on the grounds that the manufacturer was negligent in not making the car safer.

This use of an indefinite standard, "crashworthy," creates a situation in which an insurer or self-insurer cannot gauge the risk created, because the extent of the manufacturer's duty, and what constitutes his negligence, is unpredictable. One would expect, perhaps, that the duty would be less when manufacturing a small car, which most everyone knows is more dangerous in a crash than a full size auto. Yet if the duty is to build a crashworthy car, why should the standard ever vary? Further, what are we to make of competing desires, on the part of both auto consumers and the public at large, for more fuel efficient, and thus typically smaller, less crashworthy, cars? For less expensive cars? Must every car be as safe, and expensive, as a Rolls Royce? If the test is simply to become one of balancing competing goals, why should the plaintiff be allowed to substitute the ex post facto judgment of a jury regarding the appropriate balance for his own ex ante judgment of the proper mix of safety, fuel efficiency, cost and style at the time of purchase? Once again, the voluntary world of contract, with its maximization of choice, has been replaced by the coercive world of tort, where one style fits all.

From a risk selection standpoint, the idea of "crashworthy" cars begs for adverse selection. The manufacturer, expected to absorb this cost by the court, must charge all buyers of a particular model of car the same premium. When applied to sports cars or off-road vehicles, buyers who drive in a high risk fashion-- at high speeds, or bouncing through off-road terrain, will continue to buy such cars. Those who drive more safely, but simply prefer the feel of a sports car or the occasional usefulness of four wheel drive, may find indulging their preference is not worth the added cost. Thus only riskier drivers are left in the risk pool, and insurance costs rise still higher.

Where general passenger sedans are concerned, the higher insurance premium that must be added to inherently less "crashworthy" small, fuel efficient cars narrows the price differential between small and large cars. Some lower income buyers will be forced out of the new car market and into less safe used cars. Higher income buyers may decide to spend a bit more for a larger, but less fuel efficient car. The tort system is unable to evaluate such trade-offs.

A legal question similar to Rutherford was posed in the 1980 case of Chaney v. Whiting Corp., [48] The plaintiff was burned by an explosion of molten metal released from the defendant's properly functioning machine. The machine operator had failed to sound a warning alarm on the machine before release, and the plaintiff claimed that the machine should have been designed with an interlock system that would have made the release impossible while persons were on the opposite side of the firewall from the operator. The court ruled that because it was foreseeable that the operator would forget to sound the warning alarm, the manufacturer was negligently liable. The loose causation definition and the abolition of privity combine to relieve the employer and the machine operator of responsibility for their acts, leaving the, manufacturer liable, even though it was the employer who controlled the machinery, the workplace environment, and the training of the operator.

From a risk standpoint, Chaney asks the insurer not only to calculate the inherent risk of the product, but the odds that others will behave irresponsibly. If the manufacturer can be held liable for the unsafe behavior of others, it may be impossible to predict the risk and find insurance for the product.

In Koski v. Automatic Heating Service, [49] the defendant manufacturer was held liable even though the disease caused by fungal growth on his air conditioner was unknown to scientists or doctors at the time of manufacture. The court felt that this was nonetheless a foreseeable risk, thus creating a duty, negligently breached by the manufacturer, to protect the plaintiff. Of course, the defendant could not protect against an unknowable harm. But the court reasoned that the defendant should have known that fungal growth might spread some disease, and should have found a way to prevent it. Imagine the perplexed look on the face of the underwriter asked to make an insurance bid on that risk.

The gist of this new thinking on causation in products liability is seen in the case of Moning v. Alfono, [50] in which the manufacturer was held liable for marketing a slingshot which could be bought by children. Plaintiff sued when another child hit his son with a rock hurled from one of the defendant's slingshots. In this case, no one, using common language, would claim that the manufacturer hit or injured the plaintiff. Still, one might find causation if it were determined that the plaintiff, by marketing the product to children, had created an inherently dangerous situation in which otherwise harmless activity might cause injury.

But the Court did not address the issue in this fashion. Instead, it delivered a rambling opinion attempting to weigh the relative social costs and benefits of slingshots. It is not entirely clear what this issue, important as it may be, has to do with causation of the plaintiff's injury. If a manufacturer can be found liable for an injury it did not cause, based on a court's ex post facto decision that society-- though not necessarily the plaintiff-- doesn't benefit from the defendant's legal activity, is there any method by which an insurer can predict future liabilities with any degree of certainty?

Yet this thinking, based not on causation but on an analysis, with the benefit of hindsight, as to who best could have prevented the accident-- not the same as who caused it-- is the law of Michigan.

In reaffirming the doctrine of "products liability" in Prentiss v. Yale Manufacturing, Co., the court noted, "The term 'defect' in design cases is 'an epithet--an expression for the legal conclusion rather than a test for reaching that conclusion.'" [51] What the court is saying is that products liability is not a prospective standard under which insurers and self-insured manufacturers can evaluate risk with confidence, but a retroactive determination that a plaintiff should be compensated by a defendant.

Despite the Prentiss court's declaration that, "Courts have never made manufacturers insurers", [52] this is precisely what was urged in Traynor's Escola concurrence and what has occurred in Michigan law.

For example, in Bleeda v. Hickman-Williams & Co., the Court of Appeals found liability, "...because [the manufacturer] is better able to absorb [costs], and to distribute them, through prices, rates, or liability insurance, to the public, and so to shift them to ... the community at large." [53]

It is difficult to imagine what rationale, other than insurance, could have been lurking in the mind of the court in cases such as Moning v. Alfano or Koski. The court rationalized its Koski decision by noting that the air conditioner was placed where it was more likely to grow fungi, and thus it was foreseeable that a disease then unknown to modern medicine might result. But in that respect, it is always "foreseeable" that a product may contain an "unforeseeable" defect, regardless of where installed. Liability on such grounds can only be called insurance.

Then there is the very difficult case of Abel v Eli Lilly Co. [54] Eli Lilly was one of the myriad of DES cases flooding U.S. courts in the early part of this decade. DES was a drug used to prevent miscarriages in the immediate post-World War II period. It was eventually found to contribute to vaginal and cervical cancer in the daughters of women who had taken the drug. Because plaintiffs were unable to determine from which of the many DES manufacturers they had obtained the drug decades earlier, proving causation on the part of any particular defendant was problematic. Further, as in Koski, there was no sign of negligence, or even that the problems resulting from DES were in any way medically foreseeable at the time of manufacture and sale.

The Court's resolution was to change the burden of proof in this one case. Whereas traditionally the accuser must prove his charge, the Court held here that the DES manufacturers would be held liable unless they could prove that their product had not harmed the plaintiff. The Court did so with the knowledge that such proof was unobtainable. This creation of a "DES-unique" theory [55] to allow recovery can only be justified as an insurance measure, one that, "raises the possibility that the 'DES-unique' theory of alternative liability may be extended to create other product-unique solutions to class action product liability claims." [56]

Such a development would be the natural evolution of a system that is based on how to compensate rather than whether to compensate. If the Prentiss court meant to say that Michigan has rejected the enterprise liability theories of Fleming James and Justice Traynor, the case law doesn't show it.

Joint Tort-Feasors and Risk Prediction

Torts are sometimes committed by two or more persons acting in concert. Under a long established common law rule known as joint and several liability, any of these "joint tort-feasors" could be held liable for the full damage caused not only by his acts, but by the acts of those with whom he was working in concert. This doctrine allows plaintiffs to recover their full damages when one or more of the defendants are insolvent or cannot be located. Yet as one can easily see, when a person can be held liable for harm done by another party, predicting one's own liability is little more than a random guess.

Thus the doctrine of joint and several liability was applied only to a narrow class of cases. The first was those in which the defendants truly acted in concert-- to use a simple example, a case where two men stand together and take turns throwing rocks at your windows. The other class was an even smaller group of cases in which the defendants acted separately, but in which the action of any one defendant would have caused the entire harm even if the other defendants had not contributed to the harm, as when two people carelessly start separate fires, each of which burns half of the plaintiff's house, but either of which would have destroyed the house on its own.

In the modern liability system, however, the emphasis is on compensating plaintiffs, not determining fault. Thus the goal is to have as many potential defendants held liable as possible. That way, the plaintiff is likely to collect from somewhere. As a result, courts have expanded the definition of acting in concert to include independent actors who just happen to be in the same place at approximately the same time. And where that is not enough, courts have simply changed the rules and forced defendants, not plaintiffs, to prove whodunit.

An extreme example of this judicial magic is McCoy v. DeLiefde. [57] Four hunters went out, and when game was flushed, three shot, with one hitting and wounding McCoy. There was no doubt that the defendants had no intention of harming McCoy, and certainly had no conspiracy to do so. In fact, McCoy admitted that he knew which two of the three defendants had not caused him any harm. Yet the Court still imposed joint liability, on the theory that the defendants had a tacit conspiracy to be out hunting together, and that this somehow made each liable for harm caused by the others.

In products liability cases, Michigan courts have been a bit more subtle, but joint and several liability has still been used to hold manufacturers liable for harm that they did not cause or conspire to cause.

One common tactic has been to shift the burden of proof from the plaintiff to the defendant. This is done precisely in those cases in which the Court knows that the defendants cannot prove they did not cause the harm, even though all know that one or more of the defendants did not cause the harm.

In Green v. Union Optical Center, Inc., [58] the plaintiff was unable to remember, or to produce evidence, as to whether the shattered eyeglass lens that caused the harm was purchased from Union Optical or from NuVision. The Court's response was to shift the burden of proof to the defendants to show that they were not the cause of the harm. Here, this decision may have been defensible, for the two manufacturers had both failed to maintain records, required by law, keeping track of all lens sales. Thus it could be said that the plaintiff was prejudiced in producing proof by the defendant's failure to live up to statutory obligations.

However, from Green it was a short step to Abel v. Eli Lilly. [59] In creating its afore-mentioned "DES unique" theory, the court again shifted the burden of proof onto the defendants, although the defendants had not violated any sort of statutory record-keeping duty. Since the defendants were obviously more able than the plaintiffs to know to whom sold the drug in question (in fact, they were probably less able to know), the court was, "clearly motivated not so much by legal reasoning, as by considerations of social policy." [60] It is, perhaps, unfair to be too critical of the courts in the DES cases, which involved a difficult set of facts in which it was clear that the plaintiffs had suffered harm as a result of taking DES, but it was not possible to match plaintiffs to the defendants whose product they had taken. Under the circumstances, perhaps "considerations of social policy" was the best way to decide. [61] Yet, even accepting this, it is clear that the courts did not consider the desirable social policy of competitive markets and affordable liability insurance in its decision. [62]

When joint and several liability is used to force a defendant manufacturer to pay for harm it did not cause, it can only be justified as redistribution, or social insurance. A manufacturer's liability depends less on its own behavior and the characteristics of its product than on the products and behavior of other manufacturers over whom it has no control, and the amount that a defendant must pay under the doctrine depends on who else is available to pay. The doctrine is a prime cause of uncertainty in the insurance industry. [63]

In sum, judicial policy where joint tort-feasors are concerned has frequently been to rely on an insurance rationale to determine liability, without regard for actual causation. This makes liability insurance rate

setting little more than guesswork, and as a result insurers add a margin for error to their premiums, or, in some cases, decide not to take an unknown risk.

Recognizing the fundamental unfairness of forcing a party to pay for damage it did not cause, the Michigan legislature in 1986 reformed joint and several liability rules to limit liability to a defendant's percentage of fault. However, for inexplicable reasons, the new rule was not applied to products liability actions. [64] Thus the state passed up a major opportunity to restore sanity to insurance markets.

Erosion of Affirmative Defenses

Once the decision was made that the role of the system is to compensate, there was little reason to allow the deep pocket defendant to avoid liability based on any notion of the plaintiff's own negligence, intervening cause, compliance with regulatory standards, or other defense, including lack of causation. Thus, we find marching arm and arm with the expansion of liability theories, the erosion of the meaning of causation, and the destruction of contractual limitations to liability, an erosion of the affirmative defenses once available to manufacturers. This subsection examines a few of the more significant changes.

1. Contributory Negligence

Contributory negligence was, historically, a harsh doctrine, holding that a plaintiff would be barred any recovery if he was the slightest bit negligent. Thus a person one percent at fault could be denied recovery against a party whose negligence was 99 percent to blame for the injury.

Michigan, like most other states, has now replaced contributory negligence with comparative negligence. [65] Under the latter doctrine, the plaintiff's recovery is reduced only by that percentage of the accident caused by his own negligence. As a practical matter, this change clearly increases corporate liability and, therefore, insurance rates. However, it would not seem to have any effect on the broader insurance functions of accepting and determining risks, and it is hard to argue with this change from a standpoint of justice.

Unfortunately, this clear expansion of liability is exacerbated by the refusal of the legislature to extend the same concept of proportional liability to defendants under joint and several liability. Plaintiffs are no longer precluded, by their own negligence, from collecting damages for that part of the accident for which the defendants are at fault. They are expected to bear only that portion of the loss caused by their negligence. Defendants, however, operating under joint and several liability, must still pick up the cost of damages caused by other defendants unable to pay their share. Thus comparative negligence, without a corresponding shift on the defendant's side, hit defendants from both sides, further pushing up liability costs.

2. Product Misuse

One could easily conclude that there is no need for a separate defense of product misuse. After all, what is the misuse of a product if not contributory negligence (or, under the modern standard, comparative negligence)? Nevertheless, Michigan courts have found manufacturers of products liable for failing to guard against their misuse, and not allowed that misuse to reduce the award even under comparative negligence standards.

In Crowther v. Ross Chemical & Manufacturing Co., [66] the plaintiff suffered injuries from sniffing glue manufactured by the defendant. The Court found that the manufacturer had a duty to warn the

plaintiff of possible ill effects of glue-sniffing, ignoring the argument, raised by the defendant, that a warning would have been worthless since the plaintiff intentionally sniffed the glue in order to get “high”, and knew that doing so entailed certain health risks.

This decision came hot on the heels of the Court of Appeals decision in Byrnes v. Economic Machinery Corp., [67] holding the defendant liable for failing to guard against foreseeable misuse of the product. Two years later, the Court consolidated the thesis of these decisions in Thomas v. International Harvester Co. [68] In this case, the plaintiff, after reading a warning on a box of bearings, proceeded to act against that warning by hitting a bearing with a hammer. The bearing shattered and a piece flew into his eye. The Court adopted the position that the defendant was liable for damages resulting from any foreseeable use of the product, not merely the intended use of the product. Based on that rationale, one could safely infer that placing a warning on the package was conclusive evidence of the foreseeability of misuse. Yet not placing a warning would violate the standard of Ross Chemical. In other words, despite its protestations that Michigan does not accept strict liability, the court has imposed such liability, but with no affirmative defenses and little regard for causation.

Once again, the effects of this rule are to prohibit manufacturers from controlling their liability, to promote adverse selection of the risk pool by imposing a uniform “insurance cost” on the manufacturer, to be passed on to consumers, and to create uncertainty of liability, since manufacturers must now engage in a sort of mind-reading game, trying to predict every possible misuse of the product. Indeed it is not clear, in International Harvester, how the manufacturer could have prevented the misuse, even had he foreseen it. Presumably, his only alternative was to make sturdier bearings, thus driving low cost bearings out of the market. If bearings could not be made sturdier, those who used them safely would be forced to pay a higher price until they chose not to use bearings at all, in which case they would leave the risk pool and begin the process of adverse selection.

3. Assumption of Risk

Assumption of risk was a traditional defense that took two forms. In its primary form, it denied that the defendant had any duty to take steps to protect the plaintiff. As we have seen, this defense has been totally emasculated by the broad conception of duty courts in Michigan and elsewhere have used. Defendants are now said to have a duty to protect plaintiffs from unknown diseases (Koski), from their own intentional misuse (International Harvester) or from injuries resulting from slamming their car into a bridge abutment at speeds of up to 35 miles per hour (Rutherford).

In its secondary sense, assumption of risk was used to negate a defendant’s breach of duty by arguing that the plaintiff, knowing of the breach of duty and its hazards, voluntarily undertook the risk anyway. In the 1950s, it became fashionable to view this secondary use of the defense as merely a form of contributory negligence, [69] a view soon adopted by most states. [70] Michigan followed this line and abolished the defense, save for employer/employee disputes, in the 1965 case of Felgner v. Anderson. [71]

With contributory negligence an available defense, it may be that abolition of assumption of risk as a separate defense might not have had a negative impact, had “duty” not been broadly interpreted and contributory negligence so narrowly interpreted as to make both concepts meaningless. Even then, however, assumption of risk is probably a better concept. If the plaintiffs in International Harvester and Ross Chemical were not negligent (it appears, at least in Ross Chemical, that the plaintiff had fully considered potential consequences of his actions and acted with care), they were clearly “assuming the risk”. If this is not a defense, the manufacturer is attacked from all quarters-- he faces a strict liability standard should anything be wrong with his actions or product; even the remotest connection between his product and the injury will be deemed sufficient to establish causation; and he is provided with no

defense based on the plaintiff's behavior. It is a situation that makes liability unpredictable and is rife with moral hazard because the plaintiff is not held accountable for his actions.

Assumption of risk is, ultimately, another expression of the contractual notion that people can agree on who will bear various risks of an accident occurring. Its abolition, therefore, has much the same effect as the destruction of the contractual notion of warranty. It decreases consumer choice, damages efforts to control and predict risk, removes incentives to safe behavior, and encourages morally hazardous behavior by plaintiffs.

4. The Use of Independent Standards

With the extremely broad definitions of causation and duty we have seen adopted by the courts, and the destruction of such defenses as privity, assumption of risk, and product misuse, defendants have frequently looked to compliance with independent standards as a final safeguard against liability.

In a system in which liability was founded strictly on causation, without regard to the defendant's intent, care, or negligence, such a defense would not be successful. Our system, however, is at least theoretically based on fault. In this system, compliance with independent standards set by the government or a trade organization, or simply by common use in the industry, would seem to imply non-negligence per se, particularly since negligence is usually defined in terms of "reasonable" behavior. Surely meeting government standards, or doing what everyone else in the market is doing, would seem to be "reasonable". If accepted, the defense would add considerable certainty to efforts to predict liability, especially in cases such as Koski and Eli Lilly, in which the injury was either not foreseeable--or not preventable at the time of manufacture, because the manufacturer could meet definite standards and know that his product would be presumed non-defective by the courts.

Courts have long been reluctant to find defendants non-negligent on this basis, however, apparently on the theory that to do so would inhibit further safety developments by producers knowing that they were protected from liability so long as they adhered to standard methods. [72] Thus it is not a defense that a manufacturer complied either with statutory or regulatory requirements. [73] The Michigan products liability law of 1978 [74] does allow such evidence to be taken into consideration by the jury in determining negligence, but compliance with independent standards is not a defense. [75]

The result is that proper design standards and standards of due care are determined by juries with no particular expertise in design or manufacture. These juries develop their standards on an ad-hoc basis influenced by the particular facts of each case and the emotional impact of the plaintiff's injuries. Further, no matter how many lawsuits the defendant wins, he is never off the liability hook, since the next jury may decide that the design approved by other juries, a government regulatory agency, and the industry, is defective. Previous jury decisions exonerating the product and defendant are, of course, not admissible as evidence in the trial.

Naturally, when a jury can overrule a clean bill of health a product has received not only from the industry, but from government regulators, the insurer attempting to provide liability coverage for the manufacturer of the product can't predict his liability exposure. Since this threat of liability always hangs over the product, the seller or insurer again resorts to adding an "uncertainty tax" to the premium.

Damages For All

In Section II, we noted the recent increase in the size of damage awards. Given the difficulty of understanding jury behavior, speculation as to the causes of this trend is risky. [76] Still, one judicial trend deserves at least brief mention.

Historically, damages have been limited to actual physical damages except that, where physical injury was sustained, some allowance might be made for pain and suffering. The reason was to keep out of the courts speculative, impossible to measure claims. If people could claim damages for fears, phobias, or worries, there would seem to be no end to the number of possible lawsuits.

In 1970, Michigan began to allow emotional damages even though no physical injury had occurred. [77] In 1973, Michigan became just the second state (after California), to allow recovery for emotional distress caused by witnessing harm to a third person. [78] Though both cases were automobile accidents rather than products liability actions, they foreshadowed a trend to allow recovery for intangible harms that is rapidly giving way, in many jurisdictions, to allowing recovery for speculative harms.

In Ayers v. Jackson Township, [79] a New Jersey case, plaintiffs were allowed to recover more than \$13 million to monitor medical expenses and compensate for worry of potential harm, though the plaintiffs failed to prove any physical harm or disease from the contaminants which had entered their water supply. In another case, plaintiffs were again rewarded damages for “cancerphobia”, even though no harm had yet manifested. [80] To date, no such outrageous case has appeared in Michigan, but the barriers to such rulings have already been knocked down.

Unfortunately, the traditionalists were right. When plaintiffs begin to collect because they think they might be harmed in the future, or saw someone else harmed, liability becomes all but unlimited and totally unpredictable. The result is higher prices for insurance, where it remains available at all.

Summary-- What Hath the Courts Wrought... ?

It is not too cynical to suggest that a manufacturer’s product liability, under judicial precedent in Michigan find most other states, may now be summarized as follows:

A manufacturer is liable to any person who can trace his harm to the manufacturer’s product, even if that person has voluntarily waived that protection, or if the precipitating cause of the harm was the misuse of the product by a third person; the manufacturer may be held negligent even if the harm was not foreseeable at the time of manufacture; the manufacturer is liable if he fails to warn the user of the dangers of misusing the product, even if the user misuses the product precisely because he wants to experience those dangers; the manufacturer is also liable if he warns the user regarding misuse and the user chooses to disregard the warning. He can be liable even though the product has not failed in any way; and he can be liable even if there is no proof that his product caused the harm, or even if his product did not cause the harm.

Under these standards, can there be any doubt that manufacturers have been asked to provide blanket insurance to any person who suffers any harm remotely tied to use of a product?

Unfortunately, manufacturers are uniquely unsuited to fill this role. The risks for which any manufacturer is liable, are unpredictable, and largely uncontrollable, by either the manufacturer or his insurer, when the only rules are how a plaintiff should recover, and not when or whether a plaintiff should recover. Furthermore, because manufacturers must normally charge the same price to all

consumers, adverse selection of the risk pool takes place whenever manufacturers try to pass this insurance cost on to consumers, as Professor James and Justice Traynor theorized they should.

The risk independence necessary to the proper functioning of insurance markets is also destroyed when a court rules that an entire product was negligently designed or marketed, even though that product does what it was intended to do and meets the non-negligent safety standards it was intended to meet. For example, after the decision in Rutherford, the manufacturer faced liability for every such model auto it had manufactured. In a more typical situation, testing and quality control can catch manufacturing defects. If a defective product gets through the system and causes an injury, the plaintiff can be awarded restitution. The defendant's total potential liability has not increased, as the defendant can still predict the number of products which will slip through its quality control system, and a defect in one particular product does not render the entire product line a source of liability. When one judicial ruling can create liability for an entire product line, this predictability disappears. An underwriter considering insuring the product must consider the possibility that the entire product line will be declared defective, generating massive liability. And because the manufacturer can be held liable even if the defect was not foreseeable, there is no realistic way to control or predict this potential liability.

The plaintiff is frequently exempted from any responsibility for his own misuse of the product (so long as his misuse was foreseeable by the manufacturer). Coupled with awards of punitive damages and the incipient trend to award damages for intangible harms, this creates an element of moral hazard that undermines the insurance system.

Plaintiffs are insulated from their own risky behavior. The assumption grows that any product must be safe in all circumstances, which of course is not true. Products must be used correctly, and if they are not, some danger of accident exists no matter how carefully designed the product is. Liability is no longer based on causation, but on loss spreading. This idea is not only based on the incorrect assumption that, "... the risk of injury can be insured by the manufacturer and distributed among the public as a cost of doing business," [81] but it fails to take into account any notion of the justice resulting from its implicit redistribution scheme. Indeed, even in its redistributive function it has failed.

... And Who Pays?

As the final insult, the judicial revolution in tort law has placed its heaviest burdens on the poor. Under the risk spreading rationale, companies must pass a huge liability insurance premium on to all consumers equally. This has the same regressive distributive effects of a sales tax, in that this premium is a higher percentage of the income of low-income individuals than high-income individuals. Moreover, the insurance premium added to the price of the product tends to be highest on otherwise inexpensive versions of products, which are made from lower quality materials. It is the poor, of course, who prefer these less expensive options. The system also penalizes the poor by pushing some less expensive products and services out of the market entirely.

On the receiving end, the system is equally regressive. The poor are less likely to recover than others because they are less likely to have the money or the familiarity with the legal system to take their claim to court. If they should win, their damage awards are the smallest, since they have low levels of both current and predicted future income. [82] Thus the final indignity of the insurance rationale is that, to the extent it works at all, it serves as a subsidy to the rich, rather than the intended poor.

Though the poor bear a disproportionate share of the burden, they do not bear it alone. The direct cost of liability insurance in America has now topped \$80 billion a year. [83] And all of us suffer when safe contraceptives and other drugs are kept off the market for want of insurance, when people drive less safe

used cars because new cars are too expensive, or when research and development in airplane design halts because liability insurance is not available for new products.

We can, of course, blame the messenger. We can cross our fingers and hope this is a one-time aberration caused by high interest rates, though the evidence suggests it is not. Or we can begin fundamental reform of the system.

V. TORTS AND INSURANCE-- SAVING THE SYSTEM

Resolving the crisis in the products liability insurance market requires fundamental reform in judicial and legislative thinking about the purpose of the tort system.

Problems in insurance markets tend to reflect underlying problems in the industry, product, or activity insured. While insurance and interest rate cycles, and patterns of state regulation and taxation, affect the insurance market, to a significant extent a rapid rise in auto insurance rates reflects increased car thefts and other risks; climbing health insurance costs indicate increased use and cost of hospital and physician services, and so on.

The solution to the liability insurance crisis lies more in the tort system than the insurance system, although intelligent regulatory policy vis a vis the industry and a positive swing in the insurance cycle can buy time for a more permanent solution.

Seeking that solution, over forty states have passed some type of tort reform in the past three years. The reforms tend to focus on damage caps and, in some instances, joint and several liability. These reforms are generally helpful, but fail to attack the core problems of the destruction of traditional notions of causation and contract.

Damage Caps

One of the most popular areas of reform is to place caps on non-economic damages. These proposals increase the predictability of risk by narrowing the range of awards, but they do not affect the frequency of such awards. Thus their impact on an insurance underwriter's ability to evaluate and accept risk is limited. A more successful approach, particularly if tied to caps on non-economic damages, would be to limit recovery for non-physical injury to persons who had also received physical injury. A return to this traditional doctrine would do far more to return predictability to the market because it would limit the number of potential plaintiffs a manufacturer and its insurer face.

Along the same lines, damages for "cancerphobia" and other harms not yet suffered should be removed from a system. Both such changes are justified not only as a means to restore some sanity and predictability to the tort and insurance systems, but on contractual grounds. Virtually no private market exists for first party insurance for "pain and suffering". It is not unfair to say that such damages in a tort setting amount to a windfall bonanza for a risk that the plaintiff, *ex ante*, would choose to bear himself. The *ex post facto* switching of this burden is unfair to the majority of consumers who eventually pay the bill through higher prices.

Joint Liability

A second popular area for reform has been joint and several liability. Unfortunately, most reforms, including Michigan's, have not gone far enough in this area.

Joint and several liability is an unjust doctrine except when the defendants involved truly acted in concert (I add the adjective "truly" to exclude the judicial fiction that all defendants who happen to be in the same place at the same time are acting together).

Courts have defended its use in other circumstances on the grounds that, when one or more tort feasers are insolvent or otherwise unable to pay, it is better to place the remaining burden of the loss on the other

tortfeasor rather than an innocent party. This does not consider that the other defendant, having paid for the harm he caused, is also an innocent party relative to the remaining harm. This focus on compensation, rather than justice, treats people as ciphers on a ledger, focusing on distribution of loss rather than right and wrong.

From an insurance standpoint, predictability of risk, and the ability to monitor and control risk, are destroyed when one party can be held liable for another's acts. Envision an insurance underwriter attempting to determine the risk exposure of a potential client when that client may be held liable for the actions of other parties. Such liability cannot be reliably predicted, no matter how much the underwriter knows about the safety record of the manufacturer and the product.

The proportional liability system that Michigan adopted in 1986 for all tort cases except products liability is the proper solution-- no party should be held liable for more than its share of fault for an accident. It is unclear why Michigan chose to exclude products liability, the center of the liability insurance crisis, from this decision.

Independent Design Standards

For liability to become predictable, actors must have some idea, in advance, of the standard they will be asked to live up to. Retrospective determination of an applicable standard by juries eliminates predictability. This is especially true where specific harms are not foreseeable, as in Koski or Eli Lilly, or where product design calls for tradeoffs among various objectives.

Recognizing that their decisions involve judgment calls from among various options, each with unique potential hazards and rewards, physicians in malpractice cases have long had available the defense of compliance with professional norms. Similar tradeoffs are made in product design, and this defense to charges of negligence should be available to manufacturers in product design cases. Compliance with the independent standards of government, legitimate private organizations, or industry norms should constitute a defense in design defect actions.

In addition to the predictability created by a known standard of care, this defense would reduce the number of whole product lines declared defective and thus bolster the risk independence needed for intelligent underwriting decisions. Whenever a product is declared to have a defective design, it means all such products are sources of liability, even if they function exactly as intended. Allowing independent standards to affirm the acceptability of a design will eliminate this catastrophic possibility and allow the insurance industry to do what it does best-- determine the statistical probability of independent occurrences, such as manufacturing defects.

As important as reforms in the areas of damages, joint and several liability, and standards are, they only skirt the fundamental problem areas of the new tort law-- the destruction of contract and causation. It is in these two areas that a more permanent solution to the products liability insurance crisis must be found.

Putting Meaning Back Into 'Causation'

As we have seen, since the 1944 decision in Escola v. Coca-Cola, the courts have been steadily removing the link between causation and compensation. This has shattered the ability of insurers and their clients to predict risk, since accidents with only the most tenuous links to, the manufacturer's actions or products become a source of liability. A desk underwriter simply cannot imagine every possible connection, however remote, between the product and accidents, and thus cannot guard against them. This judicial

bias aimed at reaching the “deep pocket” is void of justice and fails to consider the broader effect of such decisions on the public and the market.

Yet in fairness to the legal scholars and judges of this century, they are not the first to tinker with the idea of causation in an attempt to support their notion of redistributive justice.

Early tort law found liability on the basis of causation-- not only was the defendant’s motive of secondary concern, but so too was the care he took to avoid harm. In the absence of a contractual agreement to distribute risk, causation and liability were tied together. This was called “strict liability.”

Negligence replaced strict liability as the legal norm in this country over the course of the 19th century. At the time, a negligence standard was viewed as necessary to support economic growth-- it was a subsidy to industry. [84] The negligence standard allowed industry to avoid paying for harms caused by its activities if it had not acted “negligently.”

This system is fundamentally at odds with a system of justice based on individual rights and responsibilities. When an individual’s rights are violated, he should receive restitution from the party responsible, regardless of the reason for that violation of his rights.

A negligence standard denies that a person has absolute rights. It says, instead, that restitution for harm suffered does not depend on whether rights were violated, but whether the defendant acted negligently. In shifting to negligence, the courts abandoned the idea that causation creates liability, instead hanging their hats on the still more inchoate concepts of duty and foreseeability.

Having determined that liability is a matter of social policy, there is no reason to construe the concepts of duty or foreseeability narrowly if the judiciary’s view of social policy dictates otherwise. If it is instead decided that it would be a wise social policy, for example, to require manufacturers to compensate accident victims regardless of causation, why not do so? Once the link between causation and liability has been severed, liability can be expanded as well as limited. Thus, in addition to ignoring individual rights, a negligence system is far less predictable than one based on causation and rights-- a system of strict liability.

The words “strict liability” send shivers up the spines of many business people, who pine instead for the days when non-negligent often was synonymous with pro-industry. They forget that every Michigan case discussed in this paper was decided on a theory of implied warranty or negligence, as “strict liability” has been firmly rejected by Michigan courts.

The endless expansion of the legal meaning of “causation” to include actions far beyond the word’s meaning in normal conversation is primarily the responsibility of the courts. They created the mess, and they must bear the brunt of the burden in cleaning it up.

An ultimate solution to the causation problem will probably have to include a return to a system of strict liability. Such a system removes judicial notions of appropriate social policy-- an area constitutionally ascribed to the legislature--from the equation, allowing the courts to return to their mission of determining where rights lie. Though the term “causation” will remain a pliable concept in the hands of judges, several other equally elastic concepts will be largely removed from tort law, including “negligence”, “duty”, and “foreseeable”, thus eliminating at least a few possibilities for judicial mischief.

A strict liability system does not, of course, mean that manufacturers and others will face absolute liability for all their products. For a proper strict liability not only requires a meaningful definition of

causation, but it allows for parties to limit, increase, and otherwise specify their own risk allocation through contract.

Restoring Contract

A major step to improving the liability insurance crisis is to remove disputes from the system by returning to the voluntary system of contracts and agreement that long governed tort law. Changes in the application of contract should focus on two areas—warranties, and the defense of assumption of risk and its subset, product misuse.

1. A Meaningful Warranty

We have already discussed the problems in risk prediction, allocation, and control created by implied warranties, particularly where the “implied warranty” runs directly counter to an express warranty, as in Henningsen v. Boomfield Motors.

The primary argument against strong warranties has been that they are merely an escape from liability that powerful merchants and manufacturers force onto powerless consumers. Those whose view of society centers around the individual tend to reject this idea, believing that consumers are capable of making informed, intelligent decisions. However, even those who accept the coercive view of consumer-business relationships should tend to agree that, when possible, voluntary agreements are preferable to settling disputes in court, particularly when the rush to court has created the existing tort and liability insurance morass. And this paper has not even considered the enormous administrative burden of the present system, now accounting for roughly half of all tort costs, or some \$20 billion per year. [85]

Modern contract laws emphasizing full disclosure and warnings have softened the “buyer beware” doctrines of 19th century jurisprudence. Allocation of risks by agreement among the parties before an accident is consistent with notions of individual rights and responsibilities, with the proper functioning of liability insurance markets, and with prompt compensation for deserving recipients.

2. Assumption of Risk and Product Misuse

The defenses of assumption of risk and product misuse are simply logical applications of contract notions.

In the simplest cases, the plaintiff may specifically sign a waiver of liability. In somewhat more difficult cases, the circumstances of the plaintiff’s activity and the accident may suggest an implicit agreement about who assumed the risk of an accident. For example, a player hurt in routine action in a football game, through no equipment malfunction, is generally considered to have assumed that risk, even if such assumption was not included in a specific agreement beforehand.

Product misuse is an obvious extension of this idea. For example, in International Harvester, the case in which the plaintiff read the warning on a box of bearings, understood it, and proceeded to act against it, resulting in his injury, one could justifiably say that the plaintiff had “assumed the risk” of such an accident occurring. He acted in a way which he knew created hazards, even if he did not know precisely what hazard awaited him. Any system which claims to promote individual responsibility and care would have found the plaintiff responsible for his own injuries.

Where an injury results from knowing misuse, it is the plaintiff, and not the manufacturer, who has caused the harm. That the manufacturer should be liable because the misuse was foreseeable makes no

more sense than denying the plaintiff recovery for a truly defective product because the defect was foreseeable-- an idea which would effectively deny any plaintiff recovery under the same definitions of foreseeability used by the courts against manufacturers.

A contractual analysis based around the distribution of risk is also the best method for solving certain thorny causation problems that will still exist.

In a simple case, say Rutherford, the question would be: Who assumes the risk that a serious injury will occur when a car hits a bridge abutment at speeds of 35 miles per hour? I believe that most auto buyers quite willingly and knowingly accept that risk, though the hypothetical of such an accident may not appear in any contract before hand. But my analysis is open to challenge. Perhaps the car was marketed as being extremely safe, indeed far safer than most cars (as is presently the case in the marketing campaign of at least one European import sedan). If so, questions might be raised as to whether the owner assumed the risk. But normally speaking, people who drive on icy roads at relatively high speeds recognize the chance of skidding, and suffering serious injury, as a result of their decision to drive. Indeed, few would expect not to be hurt in such an accident. It is a risk they assumed.

To take what is perhaps a harder example, in Eli Lilly the risk of vaginal cancer to children born of - mothers who used DES was unknown, and unknowable to scientists, at the time of manufacture, and at the time the drug was taken. Since an unknowable risk cannot be guarded against, the question is whether the risk of presently unknowable future harms lies with the party producing the product or is assumed by the party choosing to try a new product. In this case, I would argue the latter, an argument made stronger because the drug carried a warning that it was an experimental drug.

A critic might argue that this is as unpredictable a test as one for negligence in a design defect. I cannot agree, but even if I did would find it preferable-- at least the jury is asking the right question, which is: How did the parties voluntarily allocate the risk beforehand? Of course, had the injury occurred due to an improperly manufactured batch of the drug that had escaped inspection, or been the result of a side-effect that the manufacturer had warranted would not occur, the result would be different, since the consumer would not have received what was bargained for. But that was not the case in Eli Lilly, and should not have been the result.

The importance of reestablishing contractual allocations of risk is brought home in the search for an AIDS vaccine. Liability expert Peter Huber predicts that were a vaccine discovered, no pharmaceutical company would market it in the United States. The enormous potential liability from unknown side effects would make liability insurance unavailable, and under current tort doctrine, which ignores contract, the manufacturer could not shift this risk even to willing consumers. [86]

Contract, and the ability to voluntarily distribute risk, is fundamental both to individual autonomy and to assuring an available, properly functioning liability insurance market for beneficial products.

VI. CONCLUSION

The products liability insurance crisis which has plagued Michigan and the rest of the nation is not the result of industry conspiracies, fluctuating interest rates, or a mad desire to sue on the part of the American public.

Rather, its primary cause is a mode of judicial thinking which has placed its emphasis on how to compensate plaintiffs rather than when to compensate them. To achieve desired results, courts have stretched the meaning of causation” beyond all recognition and driven voluntary, contractual agreements on the distribution of risk out of the market. They have stripped away affirmative defenses once available to defendants, and, through joint and several liability, held defendants liable for damages for which they were not at fault. This activity has taken place with little regard for its effects on insurance markets.

The result has been to shatter the predictability on which insurance markets rely, resulting in higher premiums that might be termed an “uncertainty tax”. This mode of judicial thought has also eliminated the ability of manufacturers to control the risks they accept and has built in an element of adverse selection in insurance markets. Radically higher premiums, and in some cases a complete breakdown of the supply side of the insurance market, have resulted.

The effects of this judicial trend can be mitigated by efforts to cap non-economic damages and to restrict the application of joint and several liability. Reestablishing neo-contractual affirmative defenses such as product misuse and assumption of risk, and allowing compliance with independently established standards or industry norms to establish non-negligence, hold still greater promise.

A more comprehensive, long range solution, however, will require a change in thinking about the purpose of the tort system, away from compensation at any price and toward individual responsibility and causation. To this end, the courts must restore voluntary contracts to their proper place as delineators of rights and responsibilities, and provide a meaningful definition of causation that focuses responsibility on those actors whose behavior was truly the cause of, and not merely antecedent to, the accident.

In the long run, a system of strict liability, with a proper definition of causation and healthy contractual notions, including an assumption of risk defense, is the system most compatible with a stable, predictable determination of liabilities, affordable, available liability insurance, and a system of individual rights and responsibilities.

The Author

Bradley A. Smith is a Senior Policy Analyst with the Mackinac Center for Public Policy. He has worked as an Economics Officer in the United States Department of State and as a private health benefits consultant. He is presently studying law at Harvard University, and is a Senior Editor of the Harvard Journal of Law and Public Policy.

The Report

This report is published by the Mackinac Center for Public Policy. Nothing in this report should be construed as necessarily reflecting the views of the Mackinac Center or as an attempt to aid or hinder the passage of any particular legislation before the United States Congress or the Legislature of the State of Michigan.

Copyright 1988 by the Mackinac Center. For additional copies or reprint permission, contact the Mackinac Center, 119 Ashman, P.O. Box 568, Midland, Michigan 48640; (517) 631-0900. With appropriate credit, excerpts may be reprinted without further permission as part of a review or news story.

VII. ENDNOTES

- [1] Sorry, Your Policy is Canceled, Time, March 24, 1986 , at 16 .
- [2] P. Huber, Liability: The Legal Revolution and Its Consequences 3-4 (1988).
- [3] The Angry Retort Against Tort Law, Insight, Oct. 31, 1988, at 13.
- [4] Liability's Creative Clamp Holds Firms to the Status Quo, Insight, August 29, 1988, at 38.
- [5] Priest, The Current Insurance Crisis and Modern Tort Law, 96 Yale L. J. 1521, n. 1-9 (1987).
- [6] K. Abraham, The Causes of the Insurance Crisis, from galley proofs for inclusion in Manhattan Institute, New Directions in Liability Law (1988).
- [7] Insurance Conspiracy? A Response to the Attorneys General Lawsuit, American Legislative Exchange Council, Vol. 14, No. 6, August, 1988, at 1.
- [8] Insurance Profitability - The Facts, Insurance Services Office, February, 1986.
- [9] Priest, supra note 5, at 1529.
- [10] R. Willard, Remarks before the Alliance of American Insurers concerning The State of Tort Reform in America. (Oct. 1, 1987).
- [11] Governor's Advisory Commission on Liability Insurance, Insuring Our Future (State of New York, April 7, 1986).
- [12] In fact, in many states, most notably Massachusetts, there has been an auto insurance crisis during this period. However, few attribute it to the underwriting cycle. In states where an auto crisis is severe, the blame has correctly been placed on government regulation of the market. See e.g. Melloan, How to Create an Automobile Insurance Mess, The Wall Street J., Sep. 13, 1988 at 15, col. 3.
- [13] Hensler, Vaiana, Kakalik, and Peterson, Trends in Tort Litigation: The Story Behind the Statistics, 6 (RAND Corporation, Institute for Civil Justice, 1987) (Hereinafter RAND Study).
- [14] Id.
- [15] Id.
- [16] See infra text accompanying notes 51-53.
- [17] Id. at 6-11.
- [18] Huber, supra note 2, at 161.
- [19] Id. at 160.

- [20] There is reason to believe this is a contributing factor. The plaintiffs bar is far more organized than in the past, and the field, once shunned by most top attorneys, has gained considerably in prestige over the last two decades.
- [21] RAND Study , supra note 13 , at 16-18.
- [22] Id. at 19.
- [23] Id. at 21.
- [24] Id.
- [25] Abraham, supra note 6.
- [26] Priest, The Invention of Enterprise Liability: A Critical History of the Intellectual Foundations of Modern Tort Law, 14 J. of Legal Studies 461 (1985).
- [27] 24 Cal. 2d 453, 462, 150 P.2d 436, 440-41 (1944) (Traynor, concurring).
- [28] Epstein, Products Liability as an Insurance Market , 14 J. of Legal Studies 645, 647 (1985).
- [29] e.g. Winterbottom v. Wright , 10 M&W 109, 152 Eng. Rep. 402 (Ex. 1842).
- [30] Husett v. J. I. Case Threshing Machine Co., 120 F. 865, 868 (8th Cir., 1903).
- [31] MacPherson v. Buick Motor Co., 217 N.Y. 382, 391, 111 N.E. 1050, 1053 (1916). Plaintiff sued after his car crashed due to a defective tire.
- [32] Spence v. Three Rivers Builders & Masonry Supply Inc., 353 Mich. 120 (1958).
- [33] 375 Mich. 85 (1965).
- [34] 32 N.J. 358, 161 A.2d 69 (1970).
- [35] 32 N.J. 358 at 384.
- [36] 59 Cal. 2d 57, 377 P.2d 897 (1962).
- [37] 59 Cal. 2d at 63-64.
- [38] See supra note 32 and accompanying text.
- [39] 375 Mich. 85 at 99-100.
- [40] Blanchard v. Monical Machinery Co., 84 Mich. App. 279 (1978)
- [41] See supra text at 12-13.
- [42] Prentiss v. Yale Manufacturing Co., 421 Mich. 670, 681 (1984).

[43] 26 Mich. App. 602

[44] Id. at 615.

[45] MCL 600.2945.

[46] See, e.g. Phillips v. J. L. Hudson, 79 Mich. App. 425 (1977).

[47] 60 Mich. App. 392 (1975).

[48] 100 Mich. App. 108 (1980).

[49] 75 Mich. App. 180 (1977).

[50] 400 Mich. 425 (1977).

[51] 421 Mich. 670, 684 (quoting Wade, On Product Design Defects and Their Accountability, 33 Van. L. R. 551, 552 (1980).

[52] 421 Mich. at 682-83.

[53] 44 Mich. App. 29 (1972), quoting Professor, Law of Torts, 3d Ed. P. 68, p.471.

[54] 94 Mich. App. 59 (1980), 418 Mich. 311 (1984).

[55] 418 Mich. at 332.

[56] Calton, Tanase, and Turnbull, Annual Survey of Michigan Law--Torts, 31 Wayne L. Rev. 815, 831 (1984).

[57] 376 Mich. 198 (1965).

[58] 95 Mich. App. 167 (1980).

[59] 418 Mich. 311 (1984).

[60] Silver and Toth, 1980 Annual Survey of Michigan Law--Torts, 27-Wayne L. Rev. 967, 976 (1980).

[61] The author disagrees with this contention. See infra p.48.

[62] For a somewhat different handling of the problem, with equally destructive results, see Sindell v. Abbott Laboratories, 26 Cal. 3d 588, 607 P. 2d 924 (1980).

[63] Abraham, supra, note 6, at 6.

[64] MCL 600.6304 (4)-(6).

- [65] MCL 600.2949 made the switch for products liability cases in December, 1978. Weeks later, the State Supreme Court made comparative negligence the rule in all cases with its decision in Placek v. City of Sterling Heights, 405 Mich. 638 (1979).
- [66] 42 Mich. App. 426 (1972).
- [67] 41 Mich. App. 192 (1972).
- [68] 57 Mich. App. 79 (1974).
- [69] See, e.g., Harper & James, Law of Torts, P.21.8, p.1191 (1956).
- [70] e.g. Meistrich v. Casino Arena Attractions, Inc., 31 N.J. 44, 155 A.2d 90; Williamson v. Smith, 83 N.M. 336, 491 P.2d 1147 (1971).
- [71] 375 Mich. 23 (1965).
- [72] See The T.J. Hooper, 60 F.2d 737 (2d Cir. 1932). This argument seems to assume, probably incorrectly, that defendants have no market incentives to make their products safer.
- [73] Emery v. Chesapeake & Ohio Railway, 372 Mich. 663 (1964).
- [74] 56. MCL 600.2946.
- [75] Owens v. Allis-Chalmers Corp., 414 Mich 413 (1982).
- [76] RAND Study, supra note 13, at 19-24.
- [77] Daley v. LaCroix, 384 Mich. 4 (1970).
- [78] Toms v. McConnell, 45 Mich. App. 647 (1973).
- [79] 106 N.J. 557 (1987).
- [80] Hagerty v. L&L Marine Service, 788 F.2d 315 (5th Cir. 1986).
- [81] Escola v. Coca Cola Bottling Co., 24 Cal. 2d 453, 150 P.2d 436 (1944) (Traynor, concurring).
- [82] Priest, supra note 5, at 1552, 1585-86.
- [83] Huber, supra note 2, at 4.
- [84] Gregory, Trespass, to Negligence, to Absolute Liability, 37 Va. LL. Rev. 359 (1951); Horwitz, The Transformation of American Law, 1780-1860 (1977); contra Schwartz, Tort Law and the Economy in Nineteenth-Century America: A Reinterpretation, 90 Yale L. J. 1717 (1981).
- [85] RAND Study, supra note 13, at 26.
- [86] P. Huber, remarks before meeting of the Harvard Federalist Society For Law and Public Policy, Nov. 21, 1988.