



Aggregate litigation and regulatory innovation: Another view of judicial efficiency

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ABSTRACT

In this article, we argue that aggregate litigation and the court system can not only restore the protection of victims and the production of deterrence, but also play a pivotal role in stimulating regulatory innovation. This is accomplished through a reward system that seems largely to mimic the institutional devices used in other domains, such as intellectual property rights, by defining a proper set of incentives. Precisely the described solution relies on creating a specific economic framework able to foster economies of scale and grant a valuable property right over a specific litigation to an entrepreneurial individual, who in exchange provides the venture capital needed for the legal action, and produces inputs and focal points for amending regulations. In this light, aggregate litigation thus can be equally seen as an incubator for regulation.

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1. Introduction

In 1961, Guido Calabresi's influential contribution, "Some Thoughts on Risk Distribution and the Law of Tort", challenged the then-prevailing assumption that spreading losses was more efficient than concentrating them only because "the real burden of a loss is smaller the more people share it" (p. 517).

Just a few years later another seminal work, *The Logic of Collective Action* by Mancur Olson (1965), provided evidence that the uncoordinated action of individuals can sometimes be less efficient than coordinated action. Olson's contribution then became a prominent explanation for the formation of groups and, by extension, the emergence of specific institutions whose purpose it is to make that coordination possible.

Though the above two works were unrelated, they are the two pillars which explain the emergence of aggregate litigation in legal procedure, and the reasons why it can be a powerful device for promoting social welfare when other institutional arrangements seem to be ineffective.¹ There are in fact many circumstances where torts systematically spread losses across multiple individuals, but which

individual action through the courts seems ill-equipped to tackle. This has become a major spur for amending regulation: to provide an alternative that complements or fully replaces legal action, in serving the interests of a multitude of interested parties (Glaeser & Shleifer, 2003).

However, there are various cases in which even regulation falls short, and substantial failures emerge with respect to minimising the social cost of accidents, but with much more far-reaching repercussions, for example impacting on the performance of the economic system as a whole (Porrini & Ramello, 2011).

The above two shortcomings have resulted in a systematic under-protection of victims in some jurisdictions, prompting national lawmakers to address the incompleteness of liability systems.

Aggregate litigation offers a reasonable solution midway between individual litigation and regulation, by creating a mechanism for gathering dispersed victims and channelling them into a type of action where the various parties jointly seek to promote their individual interests and those of society at large.

Though arguments can be made both in favour of and against aggregate litigation, multi-claimant disputes, resolved and litigated on a collective basis, thus far seem to be the most efficient institutional solution for protecting victims and society, to the point that some authors have even posited an "inevitability" of aggregate litigation (Erichson, 2005).

The aim of this work is to discuss one particular—often overlooked—argument in favour of aggregate litigation, as way in which liability can further serve society: it can contribute

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¹ The term "aggregate litigation" is used here to denote lawsuits that bundle together large numbers of similar claims (hundreds, thousands, or more) pursued in some collective manner, i.e. what it is sometimes termed "group litigation". The most well-known such procedural device—though not the only one—is class action. For a discussion see Hensler (2001).

significantly to regulatory innovation, by producing a set of outputs that, taken together, supply focal points and inputs to the regulatory rule-making process, which is in many cases fossilised by structural rigidity. In this respect, therefore, aggregate litigation can help avert future regulatory failures. It can thus be regarded as an alternative judicial market technology that transforms the lawsuit into a “regulation incubator”—a field experiment for ascertaining the necessity of change, and the ability of the proposed solutions to meet real-world needs, also thanks to the large number of plaintiffs who become a proxy for society.

Viewed in this light, aggregate litigation also pursues the goal of dynamic efficiency, by providing incentives that foster innovation, similarly to what happens, for example, with intellectual property rights.

The article is organised as follows: Section 2 uses the asbestos saga as an example of how aggregate litigation can promote regulatory change, whilst Section 3 further examines the nature and limitations of regulation and its rule-making process; Section 4 considers the different relationships that exist between regulation and litigation, discussing how aggregate litigation can become instrumental to regulatory innovation; Section 5 sketches out the rationale of aggregate litigation, discussing how this procedural solution is becoming significant in the tort system, whilst Section 6 disentangles the workings of the reward system set up by aggregate litigation, to determine the conditions under which this solution is superior to the alternatives for fostering innovation (but also for protecting victims); finally, Section 7 draws the conclusions.

2. A historical tale: the long and winding road of asbestos regulation

The story of asbestos—with particular focus on the US—provides an interesting example of the role of aggregate litigation in imparting momentum to regulatory change.

Archaeological digs in Scandinavia have shown that, as early as 5000 years ago, asbestos was being used in crockery for its fire resistance properties. Subsequent history evinces an almost sacral respect for this ‘indestructible’ (this is the meaning of the Greek word “asbestos”) mineral fibre and its widespread use in many cultures for a variety of purposes (e.g. fireproofing, insulation, etc.). However, almost from the earliest times, we find suspicions of a link between asbestos and health problems. The first-century geographer Strabo noted that workers exposed to asbestos experienced diseases, whilst Pliny the Elder advised against purchasing slaves from asbestos mines because “they die young” (Barbalace, 2004a).

Still, nothing substantial happened in the centuries that followed to reduce asbestos use, which on the contrary saw a dramatic rise during the industrial revolution. Since then, and for much of the 20th century, asbestos was extensively employed for building ships, water pipes, clothing, hair dryers, children’s toys, and many other consumer and construction products.

During those years, use of asbestos continued even as more definitive proofs began to emerge that asbestos exposure caused a number of serious diseases, including mesothelioma (cancer of the pleural lining of the chest and abdomen), lung cancer, gastrointestinal cancer and asbestosis (a disease affecting the breathing capacity of the lungs, which can range from non-disabling to fatal).

First of all, there was no shortage of market signals, if we consider that by 1918 life insurance companies started to charge higher premiums for asbestos workers.

Scientific evidence also began to abound during those years: in 1924, Dr. Cooke, an English pathologist, published a number of reports identifying asbestos as the cause of various diseases. These prompted a public investigation and calls for improved regulation,

but led to no severe penalties for asbestos use (Barbalace, 2004a, 2004b).

Almost at the same time, a number of lawsuits were filed by asbestos workers. The first known US compensation claim for asbestos disease was in 1927, and during the 1930s many other individual actions were filed.

Notwithstanding all these developments, and the scientific recognition of the dangers of asbestos, regulatory agencies failed to take their cue and amend the system, whilst tort law on its own was unable to impart the momentum for serious change (White, 2004).

During that period, some states set up workers’ compensation programs that paradoxically acted as a safe harbour for producers against subsequent liability. Apart from that, for a long time regulators were essentially asleep at the wheel, and asbestos use continued to increase unhindered in the US and many other countries over the decades. In spite of mounting evidence that asbestos exposure posed serious health risks, in the US—the pioneering nation for regulatory change—asbestos use continued to grow up until the early 1970s, and it was only then that regulatory agencies—the Environmental Protection Agency (EPA), the Occupational Safety and Health Administration and, later, the Consumer Safety Product Commission—began to seriously take note and amend the restrictions. Increasingly stringent regulations were then put in place over the ensuing years, culminating in the total ban proposed by the EPA in 1989. Though this ban was later overturned by a federal circuit court,² allowing some products to still legally contain trace amounts of asbestos, by 1990 overall asbestos use had become tightly controlled, and in most products it could no longer be used.³

Now, the main reason advanced to explain this regulatory shift is that the liability environment became less favourable to asbestos producers during the 1960s. This was due to various factors, including the transition of product liability law from a negligence rule to a strict liability rule, the mounting scientific evidence, and some changes to the legal technicalities of lawsuit claims, not the least of which was the newly introduced possibility of filing aggregate lawsuits—in general under Rule 42a, available since 1966—and the resultant awarding of compensation to victims (Hensler, 2001; White, 2004).

The turning point occurred in 1969, with the compensation paid by the largest US asbestos producer to 285 of its employees, who were able to access a consolidated litigation. After that, many other aggregate litigations were filed that resulted in the victims receiving compensation (Carroll et al., 2005). This seems to have had a significant effect in attracting the attention of regulators and triggering regulatory change. The consequences extended beyond the borders of the US, with other countries implementing similar regulatory regimes in their own national systems.

It is worth noting that this pattern of causal links between aggregate litigation and regulatory change has also occurred in other situations. For instance, a comparable sequence of events unfolded in the case of breasts implants, which “demonstrates how manufacturers control the flow of information and how [aggregate] litigation can provide information that stimulates regulation” (Hersch, 2002, pp. 143–144).⁴ In this case, too, there was the recognition of a previous regulatory failure by the Food and Drug

² Corrosion Proof Fittings v. EPA, 947 F.2d 1201 (5th Cir. 1991).

³ The described dynamic also had consequences in other countries, which at the turn of the century completely banned the use of asbestos; this naturally entailed further restrictions on US productions that were partly intended for export.

⁴ An interesting observation is that, also in this case, there were individual litigations that awarded damages to the plaintiffs. However regulation only received a significant push with the launch of the first class action, in which over 440,000 women took part (Hersch, 2002).

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