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Product Liability

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TESTIMONY OF ROBERT TAFT, JR.
ON BEHALF OF
SPECIAL COMMITTEE FOR WORKPLACE PRODUCT LIABILITY REFORM

Before the Subcommittee on Consumer
Protection and Finance

Committee on Interstate and Foreign Commerce
U. S. House of Representatives

November 15, 1979

I am Robert Taft, Jr., General Counsel for the Special Committee for Workplace Product Liability Reform. This is a nonprofit corporation organized by a group of fifteen trade associations and other concerned parties for the purpose of seeking a remedy to the product liability crisis in the workplace. Those represented by the Special Committee include a wide spectrum of capital equipment machinery manufacturers, distributors, and marketers including approximately 7000 companies with a total annual sales volume in excess of $30 billion, employing approximately 2 million employees and operating in all 50 states.

On October 16, 1979, our Committee submitted a Statement to this Subcommittee to be included in the Record of your hearings on the product liability problem in general. We are making a copy of that Statement available and it is attached to this prepared Testimony. In that Statement we indicated that we have taken the position that the most fair and equitable solution to the product liability dilemma in the workplace is an exclusive remedy for workplace injuries as a part of a Federal minimum standard workers' compensation bill. Through such a "no fault" approach, we can achieve a fair distribution of the burden of

workplace injuries. A bill (S. 420) is pending before the Senate Labor and Human Resources Committee which could provide such a remedy. Hearings have been held and we offered testimony in September of 1978.

We recognize, however, that other approaches to the problem may provide substantial or partial relief that would be most welcome. In our Statement, we commented upon four different proposed remedies for the product liability problem. Today I will testify specifically on the substantive aspects of two legislative proposals which are pending before this Subcommittee.

We offer our enthusiastic support of H.R. 5571, the "Product Liability Risk Retention Act of 1979," co-sponsored by Congressmen Richardson Preyer, James Scheuer, and James Broyhill, and similar legislation, H.R. 5258, introduced by Congressman John LaFalce. This legislation offers viable short range relief for what has been termed the availability/affordability insurance problem. The costs of product liability insurance have risen so dramatically over the last nine years that many small and medium sized businesses either cannot afford product liability insurance or cannot get it at any price. As we indicated in our Statement, in some cases, insurance premiums have increased 7000% over an eight-year period, even for those companies with no loss experience. The Commerce Department found that "while rates did not increase in 1978, individual premiums often did. Moreover, there is some indication that premiums continued to increase in 1979." Deductibles have increased substantially with product sellers being asked to assume an ever increasing portion of their risk. The number of companies that are going bare without product liability insurance at all is also on the increase. The Department of Commerce has received reports from many observers of the insurance industry who predict a "sharp downswing in industry underwriting profits

as early as 1980, which will result in reduced capacity. If history repeats itself, this cyclical downswing could have a severe impact upon product liability insurance costs and availablility, compounding the existing problem."

Today, due to this lack of affordability and/or availability and large deductibles, 35% of the American Textile Machinery Association members and one-fifth of the members of the National Machine Tool Builders Association are without product liability insurance at all, each risking bankruptcy should a large judgment be entered against it and providing little incentive for keeping or expanding capital investment in the business. Moreover, this uninsured status provides little certainty of recovery by an injured worker who obtained such a judgment. The Risk Retention Act offers a competitive alternative for many businesses which are in such a vulnerable position.

The results of the work of the Interagency Task Force on Product Liability and the House Small Business Committee establish that one of the major causes of the product liability problem in recent years has been the unsubstantiated and subjective rate-making practices of the insurance industry. Haunted by reports of real or fictional product liability cases in which plaintiffs recovered excessive judgments, often based upon tenuous legal grounds, the insurance industry engaged in panic pricing of insurance premiums. Costs of product liability insurance skyrocketed without a factual basis to support such increases. Rates were not related to proven risks or any substantiated projection of future risks.

The Department of Commerce concluded that there were two approaches to resolving this problem. It could propose Federal regulation of insurance companies and their rate-making practices, or it could look

to the ingenuity of the American people and encourage a market approach to resolving this problem. Rather than creating a new bureaucracy and adding a new structure of regulatory burden, the Risk Retention Act incorporates regulatory reform and a market approach to solving the product liability insurance problem.

This legislation facilitates the formation and assures the fiscal integrity of product liability risk retention groups. It does this in two ways. Title I of the Act removes the regulatory barriers which currently exist at the state level to the formation of national risk retention groups. It recognizes that the product liability insurance problem is a national problem which requires a national solution, and that risk retention groups which do not sell insurance to the public at large should not be subject to the expensive and complicated regulation which is appropriate for commercial insurers which do sell to the public. The Department of Commerce would formulate appropriate regulations necessary to assure that risk retention groups have sufficient assets to meet the risks which are being shared by the members, and that they would be managed in a responsible manner with sufficient reserves and adequate loss prevention programs. Title II of the Act would enable product sellers to negotiate with commercial insurers for group discounts and benefits which should be especially beneficial to the very small firms which cannot achieve such cost savings on their own. There would be no Federal regulation of the groups formed to buy commercial insurance on a group basis under Title II.

The benefits of the risk retention legislation will be manifold to product sellers, consumers, insurers, and injured parties. By relating insurance costs directly to risk, there should be a substantial reduction in insurance costs for some businesses, particularly small firms which

have had good claims experience. Those companies which are currently going bare (because they either cannot afford current product liability insurance or are unable to get it at any cost) would be able to form risk retention groups in order to cover their product liability exposure. Companies with substantial deductibles would be able to fund them and take a tax deduction. This would insure the payment of legally valid claims made by injured parties. The loss prevention program which would be initiated under this legislation would help businesses produce safer products and thereby reduce injuries caused by them. The competition which these risk retention groups would create for the commercial insurers should encourage the commercial insurers to set rates as accurately as practicable, based upon the real risks and the loss experience of the insured. Competition in the marketplace should lower overall costs of product liability insurance and stimulate the creation of innovative and imaginative approaches to insuring product sellers. The insurance industry would have the challenge and the opportunity to service these new risk retention groups as consultants or by selling its insurance or reinsurance to large groups of insureds. Finally, by facilitating the creation of these risk retention groups or cooperatives, we could curtail the loss of capital and premiums to offshore captive insurance companies.

Some elements in the insurance industry have expressed concern about the Risk Retention Act and have suggested that the risk retention groups would have an unfair competitive advantage over commercial insurers. We disagree. Risk retention groups would be paying the same state insurance premium taxes paid by commercial insurers. The Department of Commerce would subject the risk retention groups to requirements similar to those which commercial insurers must meet at the state level.

For example, there are requirements for minimum financial and management standards and proper reserves. Unlike commercial insurers, however, risk retention groups would be subject to the Federal antitrust laws, and they could not make nonpro-rata assessments or retroactive adjustment of premiums paid by their members. While commercial insurers can offer a broad range of general liability insurance, the risk retention groups would be limited to offering only product liability and completed operations insurance. This legislation would not take business away from commercial insurers who offer an accurate and fair premium rate based on risk and loss experience. Rather, it would offer an alternative for those product sellers who cannot obtain adequate first dollar insurance coverage or who cannot afford the insurance at current commercial market prices. Looking into the future, the Risk Retention Act would absorb the impact of the projected downturn in the insurance underwriting cycle by creating new underwriting capacity. We would not be faced with the capacity crisis which we endured in 1973-76. Finally, if the insurance companies reform their own rate-making practices and offer product liability insurance at accurate and fair costs based on risk, there is little likelihood that product sellers will be motivated to form risk retention groups. If insurance is available in the commercial market at prices reasonably close to what the risk retention groups would offer, there would be no need to go through the expense and organizational problems of forming risk retention groups.

This will require a willingness on the part of the insurance industry to reform current rate making practices. The Insurance Services Office Closed Claim Survey data indicated that over 97% of product-related accidents occur within six years of the time that the product was purchased and, in the capital goods area, 83.5% of all bodily injury

accidents occur within ten years of manufacture. "Nevertheless, as the Task Force Report indicated, the underwriters concern about potential losses associated with older products may be an important factor in the recent increase in liability insurance premiums for manufacturers of durable goods."[1] The potential competition of risk retention groups would hopefully induce the insurance industry to take a closer look at its own statistics and adjust its rates accordingly. The insurance industry feels no such inducement today.

A major concern which we have about the implementation of this legislation is whether or not the Internal Revenue Service would treat risk retention groups as insurance companies for tax purposes. It is the intention of this legislation that risk retention groups be allowed the deduction of reserves for unpaid losses, which are not deductible under normal accrual accounting rules and the Internal Revenue Code. Group participants should also be allowed to deduct premiums paid to the group for risk protection as ordinary and necessary business expenses. I am aware that the five percent limitation on risk distribution set forth in the Act was taken from Revenue Ruling 78-338 in order to maximize the probability that a risk retention group which qualifies for approval under the Act would also qualify for the tax treatment available to insurance companies under the Internal Revenue Code. However, I would much rather see language in the Act which sets forth the tax treatment to be given risk retention groups and their members. The uncertainty of the tax treatment under the current language of the bill may discourage the formation of risk retention groups and act as a disincentive to full use of the Act. An alternative to specific language in the Act would be specific instructions in the Committee Reports, Floor debate, and Conference Reports directing the Internal Revenue

Service to interpret our tax laws and regulations in a manner most favorable to encouraging and facilitating the formation of risk retention groups.

I would also encourage legislative language directing the Department of Commerce to formulate such regulations as would be necessary to facilitate the formation of risk retention groups and that such regulations would not be overly burdensome or so strict in interpretation of the requirements of the statute as to discourage the fulfillment of its purposes. Similarly, we strongly support that provision in H.R. 5571 which exempts from the Freedom of Information Act all information submitted to the Secretary of Commerce pursuant to the Act. Without this exemption, we cannot expect to get the disclosures of relevant information necessary under the Act. Apprehension on the part of businesses that proprietary information would be made available to the public would discourage participation in risk retention groups.

We commend Professor Victor Schwartz and his staff on the Commerce Department Interagency Task Force for the thorough research and preparation that has gone into the development of the Risk Retention Act. Their outreach to all interests concerned with the product liability problem is evident from the fact that the Risk Retention Act has been endorsed by representatives of businesses, consumers, and trial lawyers. With such broad support, it should be clear that there is a great need for this legislation. The need is immediate. We urge that this legislation be given priority and that its passage be implemented as soon as possible.

While the "Risk Retention Act" will have a positive impact on insurer rate-making practices and offer a competitive alternative form of insurance coverage for businesses caught in the product liability

dilemma, there is a need to address the uncertainties in the tort litigation system as well. Product sellers, insurers, and risk retention groups need a uniform, unambiguous, and fair product liability law so that they will have a firm basis upon which to project their responsibility and liability exposure. Currently, the "rules vary from jurisdiction to jurisdiction and are subject to rapid and substantial change. These facts militate against predictability of litigation outcome."[2] In order to resolve this problem we need Federal legislation. In that regard, I also wish to comment specifically upon the "Model Uniform Product Liability Act" (Model Law) which was published by the Department of Commerce in the Federal Register on October 31, 1979. Again, we commend Professor Schwartz and his staff on the Commerce Department Interagency Task Force on the preparation of a comprehensive and precise product liability law. By specifying criteria for determining responsibility and limitations on responsibility, the Model Law should reduce uncertainty and ambiguity in the product liability field and restore fairness to product liability law by imposing liability only where there is responsibility for the injury. With certain changes, which I will discuss, our Committee supports enactment of the Model Law at the Federal level.

Because of the severe detrimental impact on interstate commerce of the current chaos among states regarding product liability, we question the recommendation that the Model Law be enacted on a state-by-state basis. Since product liability insurance rates are set on the basis of a nationwide and not individual state experience, variations on a state-by-state basis will impact adversely on the goal of achieving affordable and stable product liability insurance rates. We believe that the only way to alleviate that problem is to enact this tort reform legislation

on a nationwide basis, thereby insuring uniformity and stability in the law of product liability and hastening the implementation of this much needed reform.

I would like to focus on the uniqueness of the product liability problem as it relates to workplace injuries. We believe that workplace injuries and the product liability crisis are inextricably interwoven with the inequities and injustices inherent in our current system of compensating victims of workplace injuries. The Department of Commerce recognized this linkage in its Options Paper on Product Liability and Accident Compensation Issues, which it prepared for President Carter and released to the public on April 6, 1978. That document points out that, under present law, almost all state workers' compensation statutes (and/or their court interpretation) bar recovery or indemnification from the employer by a workplace product manufacturer, no matter how negligent the employer may have been in failing to guard and maintain that product properly or in failing to instruct and monitor his employees properly on how to use it. This inequity is further compounded by the fact that, in most jurisdictions, the employer and/or his workers' compensation insurance carrier obtains a subrogation lien against third party recoveries even though the employer may have caused or contributed to the cause of the employee's injury. The Insurance Services Office (ISO) study reveals that about 56% of product liability injury payment dollars paid involved cases where the employer arguably was negligent.[3] Thus, manufacturers of workplace products are, in effect, paying the entire costs of many industrial accidents, while users of the products are completely relieved of the financial responsibility despite the fact that they may have been in a better position (or the only position) to prevent the accident from occurring. For example, it is the employer who has control over the

equipment, its maintenance, and its use; and it is the employer who makes decisions determining whether potential injuries outweigh the costs of preventive measures. The injustice of insulating employers from the effects of their own negligence results in a disincentive for workplace safety. The present system is extremely unfair and wasteful and the wrong party is paying the bill for this wasteful system. I refer you to our Statement for statistics which verify the severity and inequity of the workplace product liablity problem. As we pointed out in our Statement, the House Subcommittee on Capital Investment in Business Opportunities concluded that "it is inequitable for manufacturers to shoulder the entire burden for workplace injuries when the employer's negligence contributed to the same."[4]

The Model Law recognizes the inequity in the current product liability system as it relates to workplace injuries. Section 114 provides that damages awarded to an injured employee shall be reduced by the amount paid as workers' compensation benefits for the same injury plus the present value of all future workers' compensation benefits payable for the same injury. Unless the product seller has expressly agreed to indemnify or hold an employer harmless, the employer and its workers' compensation insurance carrier shall have no right of subrogation, contribution, or indemnity against the product seller. This is the same proposal which has been developed by the American Insurance Association and which is currently incorporated in S. 420, "The National Workers' Compensation Standards Act of 1979." In drafting this language, the Commerce Department is attempting to rectify the unfairness of the current system wherein the manufacturer of the workplace product pays the out-of-pocket costs of a product related workplace injury and is unable to place any portion of the cost of that injury on an employer

whose negligence may have helped bring about the claimant's injury.[5] It was also focusing on one of its primary criteria utilized in preparing the Model Law, "to place the incentive for loss prevention on the party or parties who are best able to accomplish that goal."[6] The drafters of the Model Law recognized that the present system operates contrary to that principle and "dulls employer incentive to keep workplace products safe."[7] We commend the Department of Commerce for identifying the workplace product liability problem, for its efforts in confronting it, and its attempts to bring some relief.

The first draft of the Model Law, which was published in the Federal Register on January 12, 1979, (Draft Law) took a different approach. It provided a right of contribution against a negligent employer up to the amount of the workers' compensation lien. In addition, it provided an absolute ten year statute of repose for workplace products. After the ten years had run, the worker could bring a claim against the workplace employer where he could prove by a preponderance of the evidence that the product causing the injury was unsafe. The worker's recovery was limited to loss of wages that otherwise would not be compensated under the applicable workers' compensation statute. Any employer held to be liable to the worker, would then have a right to seek contribution from the product seller in an arbitration proceeding under the basic standards of responsibility provided in Section 104 of the Act. There are also limitations to the statute of repose which deal with express warranties as to a longer period of life, misrepresentation about a product, and harm which was caused by prolonged exposure to the defective product; or where the injury causing aspect of the product existed at the time the product was sold but did not manifest itself until ten years after the time of the product's first use. The latter limitation

caused a great deal of confusion and could have provided an exception that swallowed the rule. It was triggered from the date of first use rather than the date of delivery. It was unclear whether first use was the first time the machine was used or the first time it was used by the particular employee. A similar limitation in the Model Law is preferable because it operates from the date of delivery and it goes to the question of whether a reasonably prudent product user could have discovered the injury causing aspect of the product within ten years. From the perspective of a capital equipment manufacturer, the confusion which arose from this exception and the right of the employer to contribution had the effect of substantially weakening the ten year statute of repose.

In comments received by the Department of Commerce, consumer groups and employer groups objected strenuously to the ten year statute of repose in the Draft Law on the grounds that it limited the employee's recovery rights and breached the statutory shield of workers' compensation thereby violating the bargain struck between employee and employer, which is the basis of the workers' compensation system. Nevertheless, we supported this provision on the basis that since 83.5% of all bodily injury accidents occurring from capital goods happen within ten years of manufacture, very few cases would arise where an employer would be subject to the additional liability and, in those few cases, that the product seller would be subject to a contribution claim from the employer.[8] An actuarially certain date could be fixed after which no liability could be assessed, thereby giving the predictability necessary for insurance rate setting and ultimately reducing the costs of insurance. It also placed an additional incentive upon the employer to keep his equipment in good repair and to maintain a safe workplace.

While we would prefer an absolute ten year statute of repose without limitations, we recognize the practical politial obstacles to passage of such legislation. This is obvious from the reaction received by the Department of Commerce to its compromise proposal, which appeared in its Draft Law. Therefore, we accept the reasonable approach of Section 110 of the Model Law which provides for a presumption that a harm arising after ten years from the time of delivery was caused after the useful safe life of the product had expired. This presumption may be rebutted only by clear and convincing evidence.

Section 110 also provides that a product seller shall not be subject to liability if it has proven by a preponderance of the evidence that the harm was caused after the product's "useful safe life" had expired. Justice and fairness require that the product seller be liable only for harms caused during the useful <u>safe</u> life of the product. Since the product can have some utility well beyond the period in which it is still safe, the user of the product should be held responsible for his choosing to take such a risk. In some cases, the useful safe life of the product is well short of the ten years provided by the statute of repose. The Model Law provides five criteria by which to measure the useful safe life of a product including any modification or alteration of the product by a user or third party. It should be made clear in legislative language that the "user" of the product includes employees as well as employers. We support the approach of Section 110 subject to clarification of other provisions of the Model Law regarding liability for workplace injuries.

We are concerned about a possible conflict between Subsection 112(C) and (D) and Section 114 of the Model Law. In the Analysis of Section 114, the drafters state that, "furthermore, proceedings under

this Act will be streamlined because in cases of employer negligence, there will be no three party litigation as to the relative percentages of fault of employers and manufacturers."[9] This suggests that the employer will never be included as a party in any product liability suit. Subsections 112(C) and (D) provide that where there is misuse, alteration, or modification, respectively, by the claimant or a party other than the claimant the damages shall be subject to reduction or apportionment, or the trier of fact may find that the harm arose solely because of the misuse or product alteration or modification. The reduction or apportionment of damages will be done in accordance with Section 111, which provides in Subsection (B)(2) that where the claimant's employer's or co-employee's fault is considered, damages shall be reduced in accordance with Subsection 114(A) (workers' compensation benefits paid and payable), or by the percentage of responsibility apportioned to such employer or co-employee, if that amount is greater. The Analysis of Section 111 recognizes that it will be difficult to apportion the responsibility of an absent employer or co-employee who is immune from tort liability due to workers' compensation laws, but that such an approach is necessary to insure fairness to product sellers. It is concluded that it is also fair to employees because they have given up their rights to sue in court for harms caused by their employer's or co-employee's fault in exchange for their workers' compensation benefits. It appears from the drafter's Analysis that through the interaction of these various sections of the Model Law that the employer would not be a party but might be called as a witness and that facts relevant to his negligence might be introduced in order to allow the trier of fact to apportion whatever percentage of fault is attributable to the employer, thereby reducing the damages payable by the manufacturer or relieving

the manufacturer of liability entirely if the employer's negligence was the entire cause of the harm. We urge that language be included in the Committee Report to make it clear that, while under the proposed system the employer would not be a party in three party litigation, as suggested by the Analysis of Section 114, the employer might be called as a witness and evidence relevant to his negligence would be admitted in a product liability law suit.

Subsection 111(B)(1)(b) makes it clear that comparative responsibility of an employer would be allocated only when it could be proved that it misused, modified, or altered a product under Subsection 112(C) or (D). Under both subsections the product seller must prove product misuse or alteration or modification by a claimant or by a "party other than the claimant" in order to make use of this defense. If the employer is not a "party" to the proceeding, as is suggested by the Analysis of Section 114, then can the employer's fault for misuse of a product be allocated under the comparative responsibility provision? The drafter's Analysis indicates his intent that the employer's fault for misuse, alteration, or modification of a product is subject to those provisions. However, the statutory language is ambiguous. Unless this ambiguity and confusion is clarified, the product seller could be forced to absorb the employer's percentage of fault under Subsections 11(B)(4), (5) and (6), which deal with the award and apportionment of damages among the parties according to common law concepts of joint and several liability. I do not believe that is the intention of this legislative proposal.

We suggest legislative language which would elaborate the interaction of these subsections in order to make it clear that the

manufacturer defendant will not be allocated the damages which were solely caused by the fault of the employer. To do otherwise would undermine the basic thesis of the Model Law which would impose liability only where it is fair to deem the product seller responsible for an injury.[10] It undermines the comparative responsibility method for allocating damages and the responsibility-equals-liability concept. We must be careful that the result of these subsections would not be to place liability on a party in excess of the degree of responsibility of that party. Again, it should be made clear that the employer's comparative responsibility is to be determined in the proceeding between the claimant and the employer.

If the effect of these sections is to impose liability upon a manufacturer defendant in excess of the degree of its responsibility then the manufacturer defendant should have the right to bring an action for contribution against the employer for the excess paid by the manufacturer.

Similarly, we believe that Section 119 of the Model Law should be amended to include workers' compensation benefits as an exception to the Collateral Source Rule. Workers' compensation, while not derived from general revenue funds, is required to be paid by state law. It is not the result of prior prudence of the claimant or his employer. While Section 114 does provide for reduction of damages by the amount of workers' compensation benefits paid or payable, the jury should be made aware that the claimant has in fact received compensation already for the injury and that the jury is not faced with an all or nothing decision as to whether the claimant will be compensated by the defendant product seller. In this manner, we could eliminate a subjective or emotional consideration by the jury.

We support the concept of "reasonably anticipated conduct" which is basic to the philosophy of responsibility for harm upon which the Model Law is based. This is not "foreseeable conduct," for almost any kind of misconduct with regard to products can be foreseeable using 20/20 hindsight. "Reasonably anticipated conduct" places incentives for loss prevention on both product sellers and product users. It includes "occurrences which are expected, ordinary, usual, and familiar. The definition focuses on the class of persons whom the product seller knows is likely to use the product."[11]

We commend the Department of Commerce on the objective criteria established for standards of responsibility for manufacturers and product sellers in Sections 104 and 105 of the Model Law respectively. This involved a difficult task of codifying the current theories of liability for defective construction, defective design, inadequate instructions, and express warranty. While we could disagree with some and add other criteria, on balance we think that the Department of Commerce did an excellent job and support these standards as being fair and reasonable. Strict liability is established in cases of defects in construction and breach of express warranty. While design and duty to warn cases are placed on a fault basis, it is important to note that the factor of hindsight is eliminated with the trier of fact focusing only on "the manufacturer's ability, at the time of manufacture, to be aware of the product's danger and the nature of the potential harm and the practical technological feasibility at the time of manufacture of eliminating the danger or warning against it."[12]

As we indicated in our Statement, the 1976 survey of the National Machine Tool Builders Association showed that 65% of the injured employees did not receive appropriate training from their employers on

how to operate the machine properly and safely and that 58% of the injured employees had been on the job for less than six months prior to the accident. I believe that Subsection 104(C)(5) which establishes standards where a product was unreasonably unsafe because adequate warnings or instructions were not provided, will give guidance in these situations. It provides that for "workplace products, warnings or other instructions may be provided to the employer or the employee/claimant if there is no practical and feasible means of transmitting it to the employee/claimant." With the complexity of modern technology and capital goods, it is important to recognize the obligation of the employer to transmit to the employees the instructions and training made available by the manufacturer of the product.

Under Section 105, product sellers, other than a manufacturer, must exercise reasonable care in their handling of products. This should reduce the excessive product liability costs for parties other than manufacturers in the distribution chain who have no responsibility for the harm caused to the claimant.

Section 106 addresses the problems of unavoidably dangerous aspects of products over which we express concern in our Statement. It is practical and fair that a product seller should not be held responsible for harms that are unavoidable. This section should encourage the development of new products and ease the fear that many manufacturers have of introducing new products to the market. As we indicated in our Statement, the threat of a product liability law suit has caused some companies to discontinue manufacturing or refuse to start making those products that are highly vulnerable to product liability suits, but possibly vital to our economy. This trend has exacerbated the already serious problem of the United States losing its competitive edge in technology and in certain product sales.

Section 107 and Section 108 deal with industry standards and legislative or administrative standards respectively and should inspire manufacturers to implement technological advances in their products. Moreover, they should increase the certainty with which an insurance carrier can predict liability exposure of manufacturers. Again, hindsight will not be a relevant factor. We believe that Section 109 requiring a notice of possible claim will promote product safety by giving manufacturers an early warning of a potential defect and allow them to take action to correct the condition in such products and thereby prevent future injuries. This section will help, in conjunction with Section 115, regarding sanctions against the bringing of frivolous claims, to prevent the multiplicity of lawsuits that are filed with no substantial basis in fact. Such cases are often filed with the intent of causing insurers to settle the nonmeritorious claim rather than incur the costs of defending the case at a greater amount than the settlement offer.

In conclusion, I repeat that both the Risk Retention Act and the Model Law are highly professional, well thought out, and articulate approaches to a multifaceted problem. The Model Law provides valuable guidance to courts which are presently facing amorphous and often conflicting hodgepodge of case law and statutes which make up "the product liability law" as it exists today in the various states. The Risk Retention Act will provide short term relief for those businesses that cannot afford or cannot obtain insurance in today's market. It is our belief that both product sellers and consumers will benefit substantially from the passage of these legislative measures at the Federal level. We offer you our assistance in gathering additional data or in the legal/technical aspects of these legislative proposals. We urge your passage of this legislation with the recommended changes we have made today.

END NOTES

1. 44 Fed. Reg. 62733 (1979)
2. Id. at 62716
3. 44 Fed. Reg. 62741 (1979)
4. H.R. Rep. No. 997, 95th Cong., 2d Session 74 (1978)
5. 44 Fed. Reg. 62739 (1979)
6. Id. at 62715
7. Id. at 62741
8. 44 Fed. Reg. 3009 (1979)
9. 44 Fed. Reg. 62741 (1979)
10. Id. at 62715
11. Id. at 62719
12. Id. at 62724

TESTIMONY OF ROBERT TAFT, JR.
ON BEHALF OF
SPECIAL COMMITTEE FOR WORKPLACE PRODUCT LIABILITY REFORM

Before the Committee on Commerce
Science and Transportation

U. S. Senate

April 22, 1980

I am Robert Taft, Jr., General Counsel for the Special Committee for Workplace Product Liability Reform. This is a non-profit corporation organized by a group of fourteen trade associations and other concerned parties for the purpose of seeking a remedy to the product liability crisis in the workplace. Our membership includes: American Textile Machinery Association; Bakery Equipment Manufacturers Association; Conveyor Equipment Manufacturers Association; Dairy and Food Industries Supply Association, Inc.; Food Processing Machinery and Supplies Association; Foundry Equipment Manufacturers Association, Inc.; Machinery Dealers National Association; National Machine Tool Builders Association; National Printing Equipment and Supply Association; Packaging Machinery Manufacturers Institute; Pulp and Paper Machinery Manufacturers' Association; Process Equipment Manufacturers' Association; Society of the Plastics Industry, Inc.; Resistance Welder Manufacturers' Association; Black Clawson Company; Dorr-Oliver Incorporated; Fike Metal Products Corporation; The Fitzpatrick Company; Kason Corporation; Littleford Bros., Inc.; Leslie J. Schmidt Associates; and Vulcan Tool Company. Those represented by the Special Committee include a wide spectrum of capital equipment machinery manufacturers, distributors, and marketers including approximately 7000 companies with a total annual sales volume in excess of $30 billion, employing approximately 2 million employees and operating in all 50 states.

On October 16, 1979, our Committee submitted a Statement to the House Subcommittee on Consumer Protection and Finance to be included in the Record of its hearings on the product liability problem in general. We are attaching a copy of that Statement as Exhibit I and ask that it be included in the Record of your hearings as part of this prepared Testimony. In that Statement we indicated that we have taken the position that the most fair and equitable solution to the product liability dilemma in the workplace is an exclusive remedy for workplace injuries as a part of a Federal minimum standard workers' compensation bill. Through such a "no fault" approach, we can achieve a fair distribution of the burden of workplace injuries. A bill (S. 420) is pending before the Senate Labor and Human Resources Committee which could provide such a remedy. Hearings have been held and we offered testimony in September of 1978.

We recognize, however, that other approaches to the product liability problem may provide substantial or partial relief that would be most welcome. In our Statement, we commented upon four different proposed remedies for the product liability problem. Today I will testify specifically on the substantive aspects of one legislative proposal which is pending before this Committee.

We offer our enthusiastic support of S. 1789, the "Product Liability Risk Retention Act of 1979," co-sponsored by Senators Culver, Inouye, Nelson, Pressler, and Tsongas. Similar legislation, H.R. 6152, was passed this year by the House with the overwhelming margin of 332-17. This legislation offers viable short range relief for what has been termed the availability/affordability insurance problem. I believe that our Statement attached hereto as Exhibit I and the Business Insurance Magazine articles attached hereto as Exhibits II and III thoroughly

document the severity of this problem. The costs of product liability insurance have risen so dramatically over the last nine years that many small and medium sized businesses either cannot afford product liability insurance or cannot get it at any price. As we indicated in our Statement, in some cases, insurance premiums have increased 7000% over an eight-year period, even for those companies with no loss experience. The Commerce Department found that "while rates did not increase in 1978, individual premiums often did. Moreover, there is some indication that premiums continued to increase in 1979." Deductibles have increased substantially with product sellers being asked to assume an ever-increasing portion of their risk.

The number of companies that are going bare without product liability is a frightening example of the "American roulette" that has resulted from the product liability insurance crisis. Due to this lack of affordability and/or availability and large deductibles, 1978 surveys revealed that 35% of the American Textile Machinery Assoication members and one-fifth of the members of the National Machine Tool Builders Association have gone without product liability insurance at all, each risking bankruptcy should a large judgment be entered against it and providing little incentive for keeping or expanding capital investment in the business. Moreover, this uninsured status provides little certainty of recovery by an injured worker who obtains a judgment. The Risk Retention Act offers a competitive alternative for many businesses which are in such a vulnerable position.

The Department of Commerce has received reports from many observers of the insurance industry who predict a "sharp downswing in industry underwriting profits as early as 1980, which will result in reduced capacity. If history repeats itself, this cyclical downswing

could have a severe impact upon product liability insurance costs and availability, compounding the existing problem." In his testimony before the House Subcommittee on Consumer Protection and Finance, James Shamberger, a vice-president of the Reinsurance Association for America, confirmed this when he testified that while he thought the crisis had diminished recently, "the [product liability] crisis will reappear in the '80s."

The results of the work of the Interagency Task Force on Product Liability and the House Small Business Committee establish that one of the major causes of the Product Liability problem in recent years has been the unsubstantiated and subjective rate-making practices of the insurance industry. Haunted by reports of real or fictional product liability cases in which plantiffs recovered excessive judgments, often based upon tenuous legal grounds, the insurance industry engaged in panic pricing of insurance premiums. Costs of product liability insurance skyrocketed without a factual basis to support such increases. Rates were not related to proven risks or any substantiated projection of future risks.

The Department of Commerce concluded that there were two approaches to resolving this problem. It could propose Federal regulation of insurance companies and their rate-making practices, or it could look to the ingenuity of the American people and encourage a market approach to resolving this problem. Rather than creating a new bureaucracy and adding a new structure of regulatory burden, the Risk Retention Act incorporates regulatory reform and a market approach to solving the product liability problem.

This legislation facilitates the formation and assures the fiscal integrity of product liability risk retention groups. It does this in two ways. Title I of the Act removes the regulatory barriers which currently exist at the state level to the formation of national risk retention groups. It recognizes that the product liability insurance problem is a national problem which requires a national solution, and that the risk retention groups which do not sell insurance to the public at large should not be subject to the expensive and complicated regulation which is appropriate for commerical insurers which do sell to the public. The Department of Commerce would formulate appropriate regulations necessary to assure that the risk retention groups have sufficient assets to meet the risks which are being shared by the members, and that they would be managed in a responsible manner with sufficient reserves and adequate loss prevention programs. As an alternative, Title II of the Act would enable groupings of product sellers to negotiate with commercial insurers for group discounts and benefits. This should be especially beneficial to the very small firms which cannot achieve such cost savings on their own. There would be no Federal regulation of the groups formed to buy commercial insurance on a group basis under Title II.

The benefits of the risk retention legislation will be manifold to product sellers, consumers, insurers, and injured parties. By relating insurance costs directly to risk, there should be a substantial reduction in insurance costs for some businesses, particularly small firms which have had good claims experience. Those companies which are currently going bare (because they either cannot afford current product liability insurance or are unable to get it at any cost) would be able to form risk retention groups in order to cover their product liability exposure.

Companies with substantial deductibles would be able to fund them and take a tax deduction. The payment of legally valid claims made by injured parties would be assured. The loss prevention program which would be initiated under this legislation would help businesses produce safer products and thereby reduce injuries caused by them. The competition which these risk retention groups would create for the commercial insurers should encourage the commercial insurers to set rates as accurately as practicable, based upon the real risks and the loss experience of the insured. Competition in the marketplace should lower overall costs of product liability insurance and stimulate the creation of innovative and imaginative approaches to insuring product sellers. The insurance industry would have the challenge and the opportunity to service these new risk retention groups as consultants or by selling its insurance or reinsurance to large groups of insureds. Finally, by facilitating the creation of these risk retention groups or cooperatives, we could curtail the current loss of capital and premiums to offshore captive insurance companies.

Some elements in the insurance industry have expressed concern about the Risk Retention Act and have suggested that the risk retention groups would have an unfair competitive advantage over commercial insurers. We disagree. Risk retention groups would be paying the same state insurance premium taxes paid by commercial insurers. The Department of Commerce would subject the risk retention groups to requirements similar to those which commercial insurers must meet at the state level. For example, there are requirements for minimum financial and management standards and proper reserves. Unlike commercial insurers, however, risk retention groups would be subject to the Federal antitrust laws, and they could not make nonpro-rata assessments or retroactive adjustment

of premiums paid by their members. While commercial insurers can offer a broad range of general liability insurance, the risk retention groups would be limited to offering only product liability and completed operations insurance. This legislation would not take business away from commercial insurers who offer an accurate and fair premium rate based on risk and loss experience. Rather, it would offer a facility for those product sellers who cannot obtain adequate first dollar insurance coverage or who cannot afford the insurance at current commercial market prices. Looking into the future, the Risk Retention Act would absorb the impact of the projected downturn in the insurance underwriting cycle by creating new underwriting capacity. We would not be faced with the insurance capacity crisis which we endured in 1973-76. Finally, if the insurance companies reform their own rate-making practices and offer product liability insurance at accurate and fair costs based on risk, there is little likelihood that product sellers will be motivated to form risk retention groups. If insurance is available in the commercial market at prices reasonably close to what the risk retention groups would offer, there would be no need to go through the expense and organizational problems of forming risk retention groups.

This will require a willingness on the part of the insurance industry to reform current rate making practices. The Insurance Services Office Closed Claim Survey data indicated that over 97% of product-related accidents occur within six years of the time that the product was purchased and, in the capital goods area, 83.5% of all bodily injury accidents occur within ten years of manufacture. "Nevertheless, as the Task Force Report indicated, the underwriters concern about potential losses associated with older products may be an important factor in the recent increase in liability insurance premiums for manufacturers of

durable goods."[1] The potential competition of risk retention groups would hopefully induce the insurance industry to take a closer look at its own statistics and adjust its rates accordingly. The insurance industry feels no such inducement today.

Some elements of the insurance industry have also taken the position that there is no need for this legislation because the states have provided mechanisms whereby risk retention groups may be formed. Our members have found such state laws to be useless in fulfilling their risk retention needs. As is stated in the article attached hereto as Exhibit III, "state laws requiring high capitalization rates and imposing other restrictions have sharply limited the use of risk pools." If one of our trade associations wanted to form a risk retention group in Colorado, it must have over $1 million in premiums, it must have been in existence for at least one year, the state must approve its rates, the applicant must show that the insurance coverage was otherwise unaffordable or unavailable, and the actual operating offices of the captives must be located in the state. In addition, the captive could only insure companies operating in Colorado. If it wanted to cover companies in other states, it would have to be licensed to sell insurance in those states. Such restrictions make it difficult if not impracticable for trade associations with members throughout the United States whose products are sold throughout the world to cover their product liability risks through a Colorado captive.

The Risk Retention Act would abolish fictitious group laws currently on the books in 46 jurisdictions which prohibit companies from joining forces to negotiate and purchase product liability insurance on a group basis. Under current state law, group product liability insurance

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1 44 Fed. Reg. 62733 (1979)

would be unavailable to a multi-state association, so long as one of the states involved has a fictitious group prohibition.

We reject the suggestion by some elements of the insurance industry that these laws can be circumvented by devious and indirect means. I am sure that the members of this Committee would be as offended as we are at such a suggestion. To urge that private companies and associations find methods "to get around" state restrictions is to offer a strong argument in favor of the need for the Risk Retention Act. Small companies that are so desperate to cover their product liability exposure should not be forced to find devious means of getting around state laws. We need the Risk Retention Act in order to offer a straightforward and honest means of insuring against the ever growing product liability exposure of American businesses.

We also reject the insurance industry's suggestion that our members can go offshore to Bermuda or the Grand Cayman Islands to form a captive insurance company. Why should we send American businesses to a foreign country in order to protect against a national American problem? Certainly the current state of our economy does not suggest that we should encourage the movement of American capital overseas.

In reality, the insurance industry is confusing the issue. This Committee is not faced with a choice of whether risk retention groups should be formed at the state or federal level. It is clear that as a practical matter group risk retention is not available to national association members at the state level. The real issue is whether this Committee will facilitate the formation of risk retention groups in the United States through passage of this legislation or relegate our members to the difficult choice of either going to a foreign country for the product liability protection that they must have or going without any protection at all.

A major concern which we have about the implementation of this legislation is whether or not the Internal Revenue Service would treat risk retention groups as insurance companies for tax purposes. It is the intention of this legislation that risk retention groups be allowed the deduction of reserves for unpaid losses, which are not deductible under normal accrual accounting rules or the Internal Revenue Code. Group participants should also be allowed to deduct premiums paid to the group for risk protection as ordinary and necessary business expenses. The five percent limitation on risk distribution set forth in the Act was taken from Revenue Ruling 78-338 in order to maximize the probability that a risk retention group which qualifies for approval under the Act would also qualify for the tax treatment available to insurance companies under the Internal Revenue Code. The uncertainty of the tax treatment under the current language of the bill may discourage the formation of risk retention groups and act as a disincentive to full use of the Act. I would like to see specific instructions in the Committee Reports, Floor debate, and Conference Reports directing the Internal Revenue Service to interpret our tax laws and regulations in the manner most favorable to encouraging and facilitating the formation of risk retention groups.

I would also encourage legislative language directing that the Department of Commerce formulate such regulations as would be necessary to facilitate the formation of risk retention groups and that such regulations not be overly burdensome or so strict in interpretation of the requirements of the statute as to discourage the fulfillment of its purposes. Similarly, we strongly support that provision in H.R. 5571 which exempts from the Freedom of Information Act all information submitted to the Secretary of Commerce pursuant to the Act. Without

this exemption, we cannot expect to get the disclosures of relevant information necessary under the Act. Apprehension on the part of businesses that proprietary information would be made available to the public would discourage participation in risk retention groups.

We commend Professor Victor Schwartz and his staff on the Commerce Department Interagency Task Force for the thorough research and preparation that has gone into the development of the Risk Retention Act. Their outreach to all interests concerned with the product liability problem is evident from the fact that the Risk Retention Act has been endorsed by representatives of business, consumers, and trial lawyers. With such broad support, it should be clear that there is a great need for this legislation. The need is immediate. We urge that this legislation be given priority and that its passage be implemented as soon as possible.

The Need and Importance of Enacting the Product Liability Risk Retention Act

March, 1981

A paper providing background information on the history, purpose and evolution of the Risk Retention Act, prepared by the Risk Retention Strategy Group, an ad hoc coalition of business, trade and professional interests seeking resolution of the product liability problem.

Current Legislative Status

The Product Liability Risk Retention Act (RRA) has already been reintroduced in the 97th Congress. In the Senate, Commerce, Science and Transportation Committee Ranking Minority Member Howard Cannon (D-NV) introduced S. 69 on January 5, 1981. In the House, Representative Jim Florio (D-NJ), Chairman of the Energy and Commerce Committee's Subcommittee on Commerce, Transportation and Tourism, introduced H.R. 2120 on February 25, 1981.

Both bills utilize the state regulatory approach developed by the Senate Commerce Committee during the 96th Congress to oversee risk retention group formation and operation.

The Problem

In 1976, President Ford established a Federal Interagency Task Force to analyze the causes of a severe contraction in the property-casualty insurance market. That contraction adversely affected the affordability and availability of product liability insurance for a broad spectrum of businesses. During the 1975-1978 period, premium escalations of 300% and up were recorded by many companies, and some product sellers were unable to obtain product coverage at any price.

The Task Force issued its Final Report in 1977. That report identified overly subjective insurer rate-making practices as one of the principal causes of the product liability problem.

Product liability insurance cost problems became less severe in the 1978-1980 period, but this easing was temporary at best. Recent underwriting losses, new extensions of liability and the potential for lower interest rates all suggest that product liability costs will again begin to soar in 1981.

The costs of coverage and related product liability concerns adversely affect new product development and productivity, and fuel inflation. As more product sellers go without adequate product liability insurance, their very existence is threatened. The time has come to take the first major step to address the problem. Fortunately, a consensus has arisen among consumers, product sellers and recently some insurers that that step should be the enactment of the RRA. The full House and the Senate Commerce Committee in the 96th Congress as well as newly appointed Secretary of Commerce Malcolm Baldrige have agreed.

Background

The Department of Commerce (DOC) developed a legislative proposal to address the insurance rate-making problem. The RRA, as drafted by DOC staff, would have established a regulatory framework within DOC to regulate the chartering and financial integrity of self-insurance cooperatives called risk retention groups. The proposal would have permitted product sellers to form such groups and to purchase product liability insurance on a group basis.

The objective of the DOC proposal was to promote and encourage competition and stability within the property-casualty market by providing an affordable alternative to current product liability insurance options. Without such an alternative, product sellers would remain at the mercy of a highly cyclical market and erratic, unsubstantiated insurer pricing practices.

The DOC risk retention proposal was introduced in the House and Senate respectively as H.R. 6152 and S. 1789. H.R. 6152 won overwhelming approval (332-17) in the House March 10, 1980 following a series of hearings on the product liability problem and remedies that might address it.

During subsequent deliberations the Senate Commerce Committee was concerned with the creation of a new regulatory authority within DOC. However, as a result of testimony from proponent groups during hearings held April 22 and July 30, 1980, the Committee was convinced of the need for such legislation.

In rejecting any federal role in the formation of risk retention groups, the Committee directed the development of a Staff Working Draft that utilized existing state mechanisms to regulate the activities of risk retention groups.

Over 200 business trade groups and corporations, representing well over one million businesses, supported the Senate Commerce Committee's new approach (see appendix A for complete listing) as did DOC and the Administration. The National Association of Insurance Brokers also

indicated support for the Staff Working Draft, and some insurers said they did not oppose it.

Several revisions were undertaken by Committee staff to accommodate further concerns expressed by representatives of the insurance industry. During this revision process debate was extensive and productive. Most, if not all, of the insurer objections were met with language strengthening the financial solvency and state regulatory authority over risk retention groups. The measure received final approval by the Committee September 22, 1980 and was reported out as a substitute to H.R. 6152.

The bill became intertwined with other non-germane legislation, delaying its consideration until the Lame Duck Session of the 96th Congress; the objections of one defeated Senator then prevented consideration of the measure by the Senate before final adjournment.

For additional congressional background consult House Report No. 96-791 and Senate Report No. 96-984.

Opposition Arguments Dispelled During the 96th Congress

With the early introduction of S. 69 and H.R. 2120, the RRA will soon become the focus of hearings and renewed congressional dialogue. Some arguments and considerations presented by opposing insurance concerns during the 96th Congress may again surface, and warrant some discussion here.

1. <u>Certain insurance groups have falsely argued that the "soft" market conditions in today's property-casualty market negate the need for the RRA.</u>

During the 1978-1980 period there was a slight mitigation of the affordability and availability problem. However, in order to understand why the RRA is still vitally important, one must take a closer look at the property-casualty market and present underwriting practices.

Today's record high interest rates are changing the nature of property-casualty underwriting. Insurers are writing policies at an underwriting loss with increasing frequency to obtain the use of investment capital. The problem with such "cash flow" underwriting is that if interest rates suddenly drop and the investment profit cushion disappears, insurers may abandon product liability underwriting to reduce their losses as they did in the mid-1970s. The risk retention alternative will be a safety net for businesses if such an insurer exodus occurs. Many insurance industry experts predict a downturn will occur in the property-casualty market within the next two years, prompting just such an exodus.

As new profit and loss statistics are being tabulated, it is significant to note that 1980 was the property-casualty industry's second largest underwriting loss year ever recorded, $3.4 billion. While investment income of $11.2 billion amply buffered these record losses,

declining interest rates in the coming months may again result in affordability and availability problems for product liability insurance.

2. <u>Recently enacted state association captive laws do not provide product sellers with a risk retention alternative as was maintained by certain insurer groups during the 96th Congress.</u>

The Senate Commerce Committee, during its consideration of risk retention legislation last year, struggled with this problem. To resolve it, the Committee instructed the DOC Task Force on Product Liability and Accident Compensation, under the able direction of former Interagency Task Force Chairman Dr. Victor Schwartz, to conduct a forum to consider the issue. A panel of business risk retention supporters and representatives of the insurance community met to resolve the dispute. The forum convinced Senate staff and Committee members that multistate operation of such groups is essential, and that a variety of duplicative, conflicting state insurance regulations effectively prevent such operation currently. The Committee became convinced that a narrow federal preemption of certain state regulations and laws, including fictitious group laws, qualifications on collective merchandising plans, capitalization requirements, countersignature laws and "Blue Sky" laws,

was necessary to facilitate such interstate operation of risk retention groups.

3. <u>The Act's inclusion of Bermuda and the Cayman Islands as chartering jurisdictions is necessary to facilitate the formation of risk retention groups, contrary to the arguments of certain insurance groups.</u>

Bermuda and the Cayman Islands were included as chartering jurisdictions to discourage obstructionism in state legislatures by opposing interests. Such activity has occurred in the past as is amply documented by Colorado's experience in adopting an association captive law: Opposing insurer groups fought successfully to make capitalization and other regulatory requirements of the law so burdensome as to render it a useless alternative for most businesses. Proponents of the RRA would be wary of a similar effort were state licensing the exclusive means for establishing risk retention groups.

Nevertheless, some insurers have expressed concern that the bill gives too much unsupervised power to insurance regulators in Bermuda and the Cayman Islands. The American Insurance Association (AIA) has recently recommended an amendment that will solve the problem. It has the full support of the Risk Retention Strategy Group and we recommend its inclusion in the bill:

Amend Section 2 (a) (4) (C):

"which is authorized to engage in the business of insurance either through chartering or by being licensed under the laws of any state or, until January 1, 1985 Bermuda or the Cayman Islands; provided that a group authorized in Bermuda or the Cayman Islands must also certify to the insurance commissioner of at least one state that it has met the capitalization requirements of such state."

This amendment would permit groups to be chartered or licensed as insurance companies under the laws of Bermuda or the Cayman Islands until January 1, 1985. Thereafter, newly formed groups would have to be chartered or licensed under the laws of a state; however, groups previously chartered or licensed under the laws of Bermuda or the Cayman Islands would continue to be risk retention groups.

The inclusion of this sunsetting amendment, in addition to a recognition by AIA that risk retention is what the business community wants, has led the association to withdraw its opposition to the legislation. AIA Senior Counsel Dennis Connolly indicated AIA's new position in a February 18, 1981 letter to Senators Packwood, Kasten and Cannon and Representatives Dingell, Florio, Broyhill, and Lent. This was a significant step for AIA, which represents a majority of the commercial property-casualty underwriting companies in the U.S. today.

A similarly-worded amendment was also agreed to last December by representatives of the National Association of Casualty and Surety Agents and the Professional Insurance Agents.

4. Specific insurer groups have incorrectly maintained in the past that there is no reason to include comprehensive general liability coverage in risk retention legislation as is currently the case.

There is a very basic reason why the RRA, as reported by the Senate Commerce Committee last year and as provided in Section 4(b)(1) of S. 69 and H.R. 2120, permits purchasing groups to purchase comprehensive general liability insurance: It is a recognition of current marketing practices and arrangements surrounding the sale of product liability insurance. As the Committee report clearly stated, "This portion of the Act includes comprehensive general liability because product liability insurance is usually sold as an endorsement to such coverage." This provision was not intended to permit the formation of purchasing groups solely for the purchase of comprehensive general liability; rather, the bill expressly states that comprehensive general liability insurance can only be provided in connection with the purchase of product liability insurance. Failure to recognize such practices could result in needless difficulties for purchasing group arrangements.

5. <u>Certain insurance groups may continue to falsely maintain that the RRA does not provide adequate safeguards or protection against the operation of fraudulent or insolvent risk retention groups.</u>

During the Senate Commerce Committee's July, 1980 hearing on the Staff Working Draft document, insurance industry witnesses expressed concern at the lack of regulatory controls in the proposal, particularly with regard to insurance commissioners in non-chartering states; this was also a concern of the National Association of Insurance Commissioners.

In response to these legitimate concerns, the Staff Working Draft was subjected to further revisions. Under Section 103 of the draft (Section 3 of S. 69 and H.R. 2120) two new subparagraphs, (F) and (G), were added. Subparagraph (F) empowers insurance commissioners of non-chartering states in which risk retention groups operate to conduct financial examinations of specific groups if there is "reason to believe" a group is functioning in a financially impaired manner. Under this subsection, a commissioner may utilize examiners from other states to complete a thorough investigation.

Subparagraph (G) provides that commissioners, upon finding that a risk retention group is operating in a financially impaired manner, may issue a "lawful order" outlining the steps necessary to "correct, eliminate or remedy any act, practice or transaction by a risk retention group that would subject it" to a liquidation, rehabilitation, reorganization, or conservation proceeding under the laws of that state.

The Committee felt that subparagraphs (F) and (G) amply addressed insurer concerns and included report language more fully discussing these important additions.

Sections 3(c) and 4(c) provide that non-chartering states may require agents or brokers doing business with risk retention or purchasing groups to be licensed. Since each state retains the right to license agents, they can, through their regulatory authority, prevent unscrupulous agents from promoting such groups in a fraudulent or improper manner.

The Support Grows

Support for this legislation continues to grow in the business community. All of the business support from last Congress remains with the addition of other groups now becoming aware of the importance of enacting this legislation. Consumer groups, concerned about avenues of recovery for injured consumers, are expected to continue to support the RRA, as is the Association of Trial Lawyers of America.

The insurance community has also seen some recent converts. In January, the Insurance Company of North America (INA) became the first carrier ever to offer unqualified endorsement of the bill. This represented a virtual milestone in insurance industry sensitivity to business customer needs, and was well received by proponent groups. The recent announcement that both the American Insurance Association and the Alliance of American Insurers, the other major insurance company trade association, have moved to a position of neutrality on the bill is an

extraordinary gesture of statesmanship and a recognition of the needs of the business community.

The National Association of Insurance Brokers continues to strongly support passage of the RRA. By and large, a majority of the insurance community is willing to live with the competitive effects of this marketplace solution.

One insurance trade group, the Independent Insurance Agents of America, may continue to oppose enactment of risk retention legislation by offering a variety of damaging amendments.

Conclusion

A broad and diverse coalition of trade associations and corporations believes passage of the RRA is essential to remedy the product liability insurance problem. We urge expeditious consideration and passage of this legislation.

APPENDIX A

ORGANIZATIONS ENDORSING RISK RETENTION
COMMERCE COMMITTEE DRAFT

National Federation of Independent Business

National Association of Manufacturers

National Association of Wholesaler-Distributors (affiliates listed separately)

National Machine Tool Builders Association

National Tool, Die & Precision Association

National Product Liability Council

Alliance of Metalworking Industries

Society of Plastics Industry

Associated Equipment Distributors

Special Committee for Workplace Product Liability Reform

Scientific Apparatus Makers Association

American Surgical Trade Association

Outdoor Power Equipment Institute

Gulf & Western Corporation

Chemical Manufacturers Association

American Mining Congress

The Material Handling Institute, Inc.

Airline Services Association

American Association of Nurserymen

American Metal Stamping Association

American Textile Machinery Association

Association of Diesel Specialists

Association of Independent Corrugated Converters

Association of Physical Fitness Centers

Association of Steel Distributors

Automotive Warehouse Distributors Association

National Building Material Distributors Association

National Candy Wholesalers Association

National Coffee Service Association

National Concrete Masonry Association

National Electrical Contractors Association

National Family Business Council

National Home Improvement Council

National Independent Dairies Association

National Insulation Contractors Association

National Meat Association

National Office Machine Dealers Association

National Office Products Association

National Paper Box Association

National Paper Trade Association

National Parking Association

National Patent Council

National Pest Control Association

National Precast Concrete Association

National Small Business Association

National Society of Public Accountants

National Tire Dealers & Retreaders Association

Printing Industries of America

Sheet Metal & Air Conditioning Contractors' National Association

Specialty Advertising Association Internation

National Association of Food Equipment Manufacturers

Bakery Equipment Manufacturers Association

Building Service Contractors Association International

Business Advertising Council

Christian Booksellers Association

Direct Selling Association

Eastern Manufacturers & Importers Exhibit

Electronic Representatives Association

Furniture Rental Association of America

Independent Bakers Association

Independent Business Association of Michigan

Independent Business Association of Washington

Independent Sewing Machine Dealers of America

Institute of Certified Business Counselors

International Franchise Association

Local and Short Haul Carriers National Conference

Machinery Dealers National Association

Manufacturers Agents National Association

Marking Device Association

Menswear Retailers of America

MN Association of Commerce & Industry Small Business Council

Narrow Fabrics Institute

National Association for Child Development & Education

National Association of Brick Distributors

National Association of Catalog Showroom Merchants

National Association of Floor Covering Distributors

National Association of Plastic Distributors

National Association of Plumbing-Heating-Cooling Contractors

National Association of Retail Druggists

National Beer Wholesalers Association of America

National Wholesaler-Distributor Organizations
Affiliated with the National Association of Wholesaler-Distributors

Air-conditioning & Refrigeration Wholesalers
American Dental Trade Association
American Jewelry Distributors Association
American Machine Tool Distributors' Association
American Supply Association
American Surgical Trade Association
American Traffic Services Association
American Veterinary Distributors Association
Appliance Parts Distributors Association, Inc.
Associated Equipment Distributors
Association of Footwear Distributors
Association of Steel Distributors
Automotive Service Industry Association
Aviation Distributors & Manufacturers Association

Bearing Specialists Association
Beauty & Barber Supply Institute, Inc.
Bicycle Wholesale Distributors Association, Inc.
Biscuit & Cracker Distributors Association

Ceramics Distributors of America
Ceramic Tile Distributors Association
Copper & Brass Servicenter Association
Council for Periodical Distributors Association
Council of Wholesale-Distributors
American Institute of Kitchen Dealers

Distributors Council, Inc.
Door & Hardware Institute
Drug Wholesalers Association

Electrical-Electronics Materials Distributors Assn.
Explosive Distributors Association, Inc.

Farm Equipment Wholesalers Association
Fireplace Institute
Flat Glass Marketing Association
Fluid Power Distributors Association, Inc.
Food Industries Suppliers Association
Foodservice Equipment Distributors Association
Foodservice Organization of Distributors

General Merchandise Distributors Council

Hobby Industry Association

The Irrigation Association

Laundry & Cleaners Allied Trades Association

Machinery Dealers National Association
Mass Merchandising Distributors Association
Material Handling Equipment Distribution Association
Monument Builders of North America - Wholesale Div.
Motorcycle Trades Association
Music Distributors Association

National-American Wholesale Grocers' Association
National Appliance Parts Suppliers Association
National Association of Aluminum Distributors
National Association of Brick Distributors
National Association of Chemical Distributors
National Association of Container Distributors
National Association of Decorative Fabric Distributors
National Association of Electrical Distributors
National Association of Fire Equipment Distributors
National Association of Floor Covering Distributors
National Association of Marine Services, Inc.
National Association of Meat Purveyors
National Association of Plastics Distributors
National Association of Recording Merchandisers, Inc.
National Association of Service Merchandising
National Association of Sporting Goods Wholesalers
National Association of Textile & Apparel Wholesalers
National Association of Tobacco Distributors
National Association of Writing Instrument Distributors
National Beer Wholesalers Association
National Building Material Distributors Association
National Business Forms Association
National Candy Wholesalers Association
National Ceramic Association, Inc.
National Commercial Refrigeration Sales Association
National Electronic Distributors Association
National Fastener Distributors Association
National Food Distributors Association
National Frozen Food Association
National Independent Bank Equipment Suppliers Assn.
National Industrial Belting Association
National Industrial Glove Distributors Association
National Lawn & Garden Distributors Association
National Locksmiths' Suppliers Association
National Marine Distributors Association
National Notions Wholesaler Distributor Association, Inc.
National Paint Distributors, Inc.
National Paper Trade Association, Inc.
National Plastercraft Association
National Sash & Door Jobbers Association
National School Supply & Equipment Association
National Solid Waste Management Association
National & Southern Industrial Distributors Associations
National Swimming Pool Institute
National Truck Equipment Association
National Welding Supply Association
National Wheel & Rim Association
National Wholesale Druggists' Association
National Wholesale Furniture Association
National Wholesale Hardware Association
Northamerican Heating & Airconditioning Wholesalers
North American Wholesale Lumber Association, Inc.

Optical Laboratories Association

Pet Industry Distributors Association
Power Transmission Distributors Association, Inc.

Safety Equipment Distributors Association, Inc.
Scaffold Industry Association
Shoe Service Institute of America
Specialty Tools & Fasteners Distributors Association
Steel Service Center Institute

Toy Wholesalers' Association of America

United Pesticide Formulators & Distributors Association

Wallcovering Wholesalers Association
Warehouse Distributors Association for
Leisure & Mobile Products
Watch Materials & Jewelry Distributors Association
Wholesale Florists & Florist Suppliers of America
Wholesale Stationers' Association
Wine & Spirits Wholesalers of America, Inc.
Woodworking Machinery Distributors Association

File:
PRODUCT LIABILITY

3/81 mtg. in Gray's office w. Bob Taft, Wash

Tort Bill : a federal pre-emptive tort statute

S: Kasten
- Staff of Commerce Subc. will prepare [Steve Holloway - maj. staff]

Draft by Easter, hearings this summer

H: Broyhill lead, looking for Dem. (Dingell?)

Risk Retention

H.R. 2120 - Florio.
S. 69 - [Kasten/Packwood will put in variation soon]
Cannon

[Baldridge asked by Kasten during confirmation about both, said favored risk retention, wanted to work w. Committee on tort bill]

- NAM, Chamber, etc. support

- ATLA opposed

- Governors? State AG's?

1. stats
2. state awareness on prod. liability
3. A-T
4. constitutionality