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THE PRODUCT LIABILITY ALLIANCE
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ELEMENTS OF A FAIR FEDERAL PRODUCT LIABILITY STATUTE

Fairness and balance between the interest of product sellers and product users should be the guiding principle in any Federal product liability statute. Over the past few years, this essential balance has been lost in a maze of conflicting state court decisions and a hodgepodge of varying state statutes.

The uncertainty and unpredictability of the state-by-state approach to product liability law are a costly burden on interstate commerce and a major factor in the volatility of product liability insurance rates.

A uniform set of rules is essential and can be achieved only through enactment of a Federal statute. Such a statute ought to codify the law as it is practiced in the majority of jurisdictions and correct the inequities in the current system.

A balanced approach to the product liability problem, one that takes into account what is politically feasible as well as substantively necessary, ought to address at least the following issues:

(1) The Federal law ought to provide for an appropriate allocation of fault in design and failure to warn cases. The tort system was created to fairly allocate liability on the basis of fault. But in some jurisdictions, it has recently evolved into a compensation-oriented system which has eliminated fault as a consideration. In these jurisdictions, all that is required to establish liability is to prove a causal relationship between a product and an injury, regardless of the conduct of the parties involved. This imbalance must be corrected so that design and failure to warn cases are governed by a fault-based standard.

(2) It ought to reflect the fact that manufacturing defects and express warranty cases are governed in most, if not all, states by a strict liability standard. This is as it should be, and the Federal product liability statute should codify strict liability in manufacturing defect and express warranty cases.

(3) It ought to require a plaintiff to prove that the defendant actually manufactured or designed the product in question. A defendant should be held liable only for his own conduct, not that of unknown others.

(4) It ought to hold product sellers to a standard of conduct consistent with practical technological feasibility at the time of manufacture. The tendency of some courts to impose 20-20 hindsight based on new technological developments should be eliminated.

(5) It ought to eliminate subrogation of workers' compensation claims and automatically reduce a plainiff's award in workplace cases by the

amount of compensation. This would significantly reduce transaction costs in cases arising out of workplace incidents.

(6) The law ought to provide for a system of comparative fault in the workplace and in other product liability litigation and require courts to consider misuse or modification of a product in assessing the manufacturers' liability and/or damages.

(7) It ought to deal in a balanced way with over-age products, providing some form of repose for products that are over-age and providing that the technological feasibility of product design safety at the time the product was manufactured be the standard against which liability and fault are measured.

(8) It ought to foreclose -- as most states now do -- the introduction of evidence of post-manufacture design changes for purposes of proving that the design of the product was defective in the first place. The barring of such evidence is a time-honored tradition in tort law, which has long held that such evidence is irrelevant. Permitting its introduction would impede the development of safer products.

(9) It ought to require distributors and other non-manufacturing sellers to exercise reasonable care in their handling of products, but should not make them routinely liable for defects that an ordinarily prudent product seller would not discover.

(10) It ought to give extra weight to manufacturers' compliance with Government safety standards in product liability actions. Just as failure of a manufacturer to comply with such standards may be used to prove his negligence, so his compliance with them should mitigate his liability.

(11) It ought to separate the imposition of punitive damages from the principal claim for compensation. Evaluation of conduct meriting punitive action should be based on flagrant indifference to product safety and extreme departure from accepted practice. In addition, it should set appropriate limits on the amount of punitive damages in single or multiple actions.

(12) It ought to provide that proof of or acceptance of liability in one product liability action does not permit a judicial assessment of liability in future unrelated actions involving other claims. The use of the doctrine of collateral estoppel is unfair to defendants facing multiple claims.

A Federal product liability bill requires neither the creation of a new Federal agency nor the expenditure of Federal monies. It adds no new basis for bringing actions in the Federal courts. Limited Federal action along these lines will address the most serious aspects of the product liability problem and will benefit both business and consumers.

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THE PRODUCT LIABILITY PROBLEM

Because the rules determining the liability of product sellers for product-related injuries have been developed almost exclusively by judges on a case by case basis, they vary from state to state, sometimes resulting in direct conflict. Because they are judicially created, these rules may change as the judicial temperament of a court changes. The result is a crazy quilt of law which is constantly changing and which is totally unpredictable by consumers, product sellers, and insurers. Macroeconomic policy affecting consumer rights, manufacturer responsibilities, and technological development, has in effect, been made by judges on an ad hoc basis.

In an effort to remedy this imbalance, 31 state legislatures, including such major manufacturing states as Illinois and Michigan, have passed some limited form of product liability statute. Individually, most of these statutes provide only defenses of some type, and do not outline the basic elements of product liability claims; nor do they define standards for manufacturer responsibility. Most importantly, no two state statutes are exactly alike.

The wide variation among state product liability laws threatens insurers' efforts to accurately predict the potential liability of the manufacturers they insure and limits the ability of manufacturers to make informed decisions regarding the design of products for nationwide distribution and sale. Some state courts have expanded the strict liability concept (liability without fault) to include product design cases. Manufacturers have little incentive to improve the design or safety of their products where their actions may be judged without regard to whether they were at fault. Consumers ultimately pay the costs of this uncertainty in higher product prices.

Product liability has emerged as a costly impediment to interstate commerce. Uncertainties and imbalance in the product liability tort litigation system will continue in the absence of a uniform statute enacted at the federal level. Product liability is a national problem requiring a national solution.

THE BENEFITS OF FEDERAL UNIFORMITY

There is a growing consensus that balanced federal product liability legislation is needed to bring uniformity and certainty to the law and to stabilize what has become a serious burden on interstate commerce.

Congressional initiatives in the 96th Congress resulted in extensive public hearings and the introduction of various product liability bills in the House. Interest in the product liability problem has continued in the 97th Congress. The Senate Commerce Consumer Subcommittee recently held hearings on product liability reform. The Committee staff, under the direction of Consumer Subcommittee Chairman Senator Robert Kasten, prepared a draft bill last October establishing uniform rules of liability. Extensive public comment on the draft bill led to a revised version, released in early March. The revised Senate staff draft made several changes suggested by consumers.

Product liability tort law has been studied extensively by the government, by the business community and by consumer groups. The 97th Congress now confronts a timely opportunity to take action beneficial to consumers and product sellers alike:

* Federal product liability legislation will allow consumers to know their legal rights and product sellers to know their obligations. A uniform law will allow consumers and product sellers, both dependent on lawyers in the current litigation system, to more accurately assess in advance the consequences of their actions and the reasonableness of the fees they are charged by lawyers.

* Uniform product liability provisions, under which manufacturers would be liable when they are at fault, will encourage the design, manufacture and distribution of safe products. A strict or absolute liability system, prevelant in some states, does not properly allocate responsibility nor provide incentives for accident prevention where they will do the most good.

* A portion of the very high transaction costs currently associated with product liability actions is inevitably shouldered by the consuming public in the form of higher product prices. Today, seven dollars is spent for lawyers for every six dollars paid to claimants. Stability in product liability tort law, brought about by a federal fault-based standard, will reduce the excessive costs inherent in the current legal environment.

* Today's chaotic and unpredictable product liability litigation system primarily benefits plaintiff's and defendants' lawyers. It is not surprising, therefore, that the organized bar opposes federal product liability tort law modifications, which would result in a reduction of transaction costs.

CONCLUSION

Three Administrations have recognized the existence of a product liability problem. An Interagency Task Force on Product Liability, created in 1976, identified insurance ratemaking difficulties and uncertainty and imbalance in the tort litigation system as the primary contributors to the product liability mess. With regard to the former aspect of the problem, last year's passage of the Risk Retention Act will help assure that product liability insurance rates will remain competitive. But, because product liability is not solely an insurance problem, the Risk Retention Act provides a key first step towards solving the overall product liability crisis.

A federal product liability tort statute drafted with precision and care will go far toward improving the present climate of almost total uncertainty caused by the application of nonuniform standards in the various states. Although complete certainty cannot be legislated, the most effective step toward certainty should be taken. The swift enactment of an equitable and balanced federal product liability tort law will benefit the entire country, including the individual consumer, through a more innovative and productive national economy.

3/18/82

THE PRODUCT LIABILITY ALLIANCE
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COMPENDIUM OF COMMENTS

DEVELOPED BY
ISSUE WORKING GROUPS OF
THE PRODUCT LIABILITY ALLIANCE
ON
STAFF WORKING DRAFT NO. 1.
OF
THE CONSUMER SUBCOMMITTEE
COMMITTEE ON COMMERCE
SCIENCE AND TRANSPORTATION

Compendium Prepared by
Victor E. Schwartz
Crowell & Moring
Washington, D.C.

March, 1982

SECTION 3

Sec. 3(a): TPLA recommends that the list of legal theories in lines 20-25, page 5 be retained and that a clause be added to the effect that the Act governs any civil action for product-related harms regardless of the theory on which the action would have been brought under prior state law. This would clarify that all product liability actions are subject to the rules and standards set forth in the Act, regardless of prior legal theories recognized at state law.

Sec. 3(b): TPLA recommends clarifying that there is no recovery for loss or damage unless it falls within the definition of "harm" in Section 2. TPLA agrees that actions for damage to the product itself or for purely commercial loss should be brought pursuant to contract or commercial law.

Sec. 3(c): TPLA recommends against preemption of Federal law because it is unnecessary, given that product liability tort law is exclusively state law, and because it may have unforeseeable, perhaps undesirable, consequences.

Sec. 3(d) and (e): TPLA recommends simplifying these jurisdictional provisions by stating simply that the Act does not confer new jurisdiction on any Federal court and that it does not create any basis for Federal question jurisdiction.

SECTION 4

General Comment: Determination of a manufacturer's responsibility is one of the most important provisions of the Staff Draft. The concept that a manufacturer's action should be evaluated according to its reasonableness is fundamental to equitable reform. These comments highlight areas that require further study, but our silence on other sections that do not require specific comment at this time does not reflect on their importance.

Relevant to Section 4(a)(2) as well as Sections 4(c) and 4(d), TPLA recommends that expert scientific or technical testimony be supported by substantial evidence in a particular field before it is considered by the jury. A manufacturer is expected to respond to scientific and technical information that is supported by recognized objective studies. He should not, however, be expected to respond to information that lacks substantial support in the scientific or technical community. Therefore, a claimant should not be permitted to offer unsubstantiated opinion to prove a manufacturer's responsibility.

In this regard, Section 4(a)(2) should be revised as follows:

> (2) A claimant shall introduce sufficient evidence to allow a reasonable person, by a preponderance of the evidence, to make the determination described in paragraph (1). Expert scientific or technical testimony shall not be deemed to be sufficient evidence unless it is corroborated by substantial objective evidence based on generally accepted scientific or technical knowledge.

Section 4(a)(1)(B): TPLA supports the requirement that the product unit which caused the claimant's harm must have been manufactured by the defendant. Responsibility for harm has been traditionally assigned only to those who actually caused the harm. The Staff Draft clarifies that relationship.

Section 4(a)(3): While collateral estoppel should not deprive litigants of their day in court, it can prevent unnecessary litigation in appropriate cases. Therefore, TPLA recommends adding "brought by another claimant" to clarify when the use of collateral estoppel is appropriate. An additional exception should be included to permit its use in litigation arising from a mass accident, e.g., where both claims arise out of an identical occurrence. TPLA recommends reference to an identical occurrence not a common occurrence.

Section 4(b): The Staff Draft properly distinguishes between defects in design and defects in construction, applying a strict liability concept to the latter. TPLA agrees that a manufacturer should be liable for harm caused by a defect in construction -- a material and substantial deviation from the manufacturer's product standards. The language should emphasize the causal link between the construction defect and the harm. TPLA recommends a modification to clarify this concept.

Section 4(c)(1): TPLA agrees that the conduct of the manufacturer in deciding to produce the product should be evaluated at the "time of manufacture." An earlier date does not give sufficient weight to a manufacturer's ability to reevaluate a design and a later date overemphasizes the use of developing, but unavailable, technology. In addition, TPLA agrees that the correct test is whether "a reasonably prudent manufacturer in the same or similar circumstances would have placed the product in commerce."

Section 4(c)(2): The Staff Draft should require that a product hazard be recognized as such by the scientific and technical community. The manufacturer cannot be expected to respond to hypothetical or speculative hazards, as was explained above.

Section 4(c)(4)(A): This should incorporate current law regarding unavoidably dangerous product characteristics. In addition, because the term "unavoidably dangerous" is of significance in several parts of the bill, it should be defined in Section 2.

Section 4(d)(1)(A): A manufacturer should be required to warn of dangers which create "an unreasonable risk of harm." Therefore, a new subparagraph 4(d)(1)(A)(i) should be added:

> (i) the danger created an unreasonable risk of harm to persons in the same or similar position as the claimant;

Subsections (i)-(iii) should be renumbered (ii)-(iv).

Section 4(d)(2)(A): Liability should not be imposed for failure to warn about dangers actually known to the user of the product. Therefore, Section 4(d)(2)(A) should be modified by adding:

> . . . or known to the user or to another in the position to act on his behalf, including the user's employer or physician, or other person in control of the product;

Section 4(d)(2)(C): Because the term "misuse" is also used in Section 8, it should be defined in Section 2. That definition should include use contrary to warnings or instructions available to the user.

Section 4(d)(2)(D): Again, liability should not be imposed for failure to warn about dangers known to the product user. Therefore, the following language should be inserted after "instruction" in line 13:

> and dangers which were a matter of common knowledge to persons in the same or similar position as the claimant.

Section 4(d)(3)(B): TPLA recommends deletion of the phrase "where such personal notice will be impossible or impracticable."

Section 4(d)(4): Manufacturers are required to warn of dangers identified after the sale of the product. This requirement should be limited to dangers that create an unreasonable risk of harm. Therefore, Section 4(d)(4) should be amended by adding after "product" in line 22:

> which creates an unreasonable risk of harm to persons in the same or similar position as the claimant.

The phrase "after a product was manufactured," should be inserted after the first word "If" in line 21.

Section 4(e)(1): TPLA agrees that a manufacturer should be responsible for failure to meet an express warranty, if that failure caused the claimant's harm. Therefore, subparagraph (C) is critical to the concept of liability for an express warranty.

SECTION 5

TPLA supports the general purposes of Section 5 and its companion definition of "manufacturer" in Section 2(6). These sections will fulfill two important goals. First, it will substantially reduce transaction costs by reducing the number of cases where retailers, wholesalers, and distributors are needlessly brought into product liability litigation. Second, it places incentives for risk prevention on the party or parties who are best able to accomplish that purpose. When the non-manufacturer product seller is at fault, he is specifically charged with responsibility. However, where the fault is not his, he is not faced with bearing unwarranted responsibility. Identified below are three areas in which the Staff Draft can be improved to help further these goals.

Section 2(6): TPLA recommends the deletion of the words "remanufacture" and "fabricate". These words do not have any legal meaning and, as a result, may lead to confusion and unnecessary litigation. With the deletion of those words, a retailer, wholesaler, or distributor would be responsible as a manufacturer to the extent it engages in the manufacturing process, e.g., "designs, produces, makes, constructs" a product.

TPLA further recommends modification of the provision in Section 2(6) which defines a manufacturer as including a non-manufacturing product seller which "holds itself out" as a manufacturer to the product user. The provision should permit the product seller to identify the actual manufacturer and, if that manufacturer is available for suit, the product seller should not be treated as a manufacturer. This modification provides, first, that a non-manufacturing product seller is not responsible for harms he did not cause and, second, that a claimant's injuries will be satisfied by the responsible party, the manufacturer.

Section 5(c): TPLA recommends deleting this section in order to adhere to the purpose of holding a product seller responsible only for its own fault. Section 5(c) deviates from that policy by imposing absolute liability on a product seller when the responsible manufacturer is out-of-business or not subject to service of process. While TPLA appreciates the desire of compensating an injured claimant, this section does so at an unfair cost -- the arbitrary selection of the non-manufacturing product seller as the responsible party.

SECTION 6

TPLA fully supports this provision clarifying the relationship between government regulatory standards, government contract specifications and product liability litigation. Section 6 will bring increased certainty to the rules governing product liability litigation, a fundamental goal of the Staff Draft. Identified below are the few areas where TPLA believes that Section 6 could be improved.

Section 6(a): In order to improve certainty and to further the overriding goal of uniformity, TPLA recommends that no special status be given to standards promulgated or adopted by state and local governments. These standards vary from state to state and from local community to local community. Presumptions based on compliance or noncompliance with such a diverse collection of rules and regulations are not warranted. In this regard, the words, "State or local" should be deleted wherever they appear in Section 6(a).

Sections 6(a)(1)(A) and 6(a)(2)(A): TPLA recommends clarifying the evidence necessary to rebut the presumption raised where a product complies with a government standard. The evidence required should not be a mere demonstration that additional precautions might have been taken. Most, if not all, standards are established in subject areas where different design approaches or performance levels are available. Indeed, if only one course of action were feasible, a standard may have been unnecessary. In adopting a standard, the government, in effect, makes an optimum and informed choice as to the "best" standard. That choice should not be subjected to "second-guessing" with evidence that additional or alternative precautions were available. Such "second-guessing" would render the presumption meaningless and would undermine the goals of certainty and uniformity sought by Section 6. Thus, where the governmentally-mandated standard has been met, a product seller should be liable only where there is clear and convincing evidence that the seller could reliably and reasonably anticipate that the compliant product is nevertheless unsafe.

Section 6(a)(1)(A): TPLA believes that an absolute presumption of safe design is appropriate in certain narrowly defined circumstances. Where the standard in question requires a level of safety performance similar to that required by the Staff Draft, i.e., the elimination of all unreasonable safety risks, compliance with that standard should prevent a later judgment that the aspect of the product in compliance with the standard was unreasonably unsafe, -- a judgment which substitutes the opinion of the trier of fact for that of the governmental agency with expertise in the matter. Thus, where the federal government has reviewed nonfraudulent data regarding the safety of a product and has approved that product for sale, perhaps with specific warnings, a jury should not be permitted to later conclude that the product was unsafe or the warning was inadequate.

Section 6(b): TPLA supports the goal of Section 6(b). It is not fair to hold a product seller liable for design choices that are made by a government contracting agency. While some mechanism for compensating harms resulting from unsafe government contract design specifications may be desirable, it is unfair to place liability on a person who did not, in fact, participate in the design process. Such liability on government contractors is inconsistent with the public interest to promote efficiency and competition by encouraging wide participation in government contract work at all levels of government.

Section 6(b)(1)(B) and 6(b)(2)(B): As drafted, these provisions regarding noncompliance with government contract specifications may impose liability on a product seller whose conduct is, in fact, reasonable and prudent. TPLA recommends clarifying these provisions to avoid "automatic" liability for "technical" breaches of contract specifications which were not imprudent and which may not have caused the harm in question.

SECTION 7

The provisions of Section 7 help to resolve the existing legal uncertainty about the relevance of a claimant's conduct and the comparative responsibility of others who contributed to the claimant's harm. Comparative responsibility principles further the interests of both product sellers and injured plaintiffs. Product sellers are not required to absorb liability to an extent greater than their culpability. At the same time, the provisions in Section 7 help insure that injured claimants are quickly and reasonably compensated for all injuries caused by defective products; they are also in a position to recover partial damages if they misused the product and if the product seller is also at fault. Moreover, the application of comparative responsibility principles will help reduce total transaction costs.

Section 7(a): TPLA recommends that where a claimant's responsibility for his own harm is equal to or greater than the defendant's responsibility, the action should be barred and judgment to that effect entered against the claimant. Such a modification to Section 7 is an intermediate position between the absolute bar of the contributory negligence rule and the almost total permissiveness of the pure comparative rule. The pure form of comparative responsibility, currently in Section 7(a), permits a grossly negligent claimant to recover substantial damages from a slightly negligent defendant. The modified approach recommended by TPLA provides an equitable and balanced apportionment of liability and damages. It is consistent with the important goals of basing liability on the relative fault of the parties involved and placing strong incentives for safety on the party who is best able to accomplish that goal.

Section 7(b)(2): This section is under study by TPLA.

Section 7(c)(3): TPLA maintains a preference for several as opposed to joint liability, because it is more consistent with the goal of allocating liability in accordance with the fault of all individuals involved and because it avoids the excess transaction costs inherent in the reallocation of the uncollectable obligation of a joint tortfeasor. TPLA does, however, appreciate the compromise embodied in Section 7(c)(3). This compromise can be made more equitable by requiring that, in any reallocation of the uncollectible obligation, the court must take into account the claimant's percentage of fault -- that is, the reallocated obligation would be reduced by the share of fault attributed to the claimant. TPLA is also concerned that Section 7(c)(3) would not be fair if it required reallocation of the obligation of a non-party joint tortfeasor.

SECTION 8

While Section 8 ensures that the product seller will remain liable to the extent that it is responsible for the harm, it addresses the problem of an overly broad imposition of liability where intervention by another party or misuse by the claimant was a cause of the accident. By taking into account situations involving misuse or alteration, the Staff Draft places an incentive for loss prevention on those who might engage in such conduct; it also simplifies the task of calculating the risk associated with the given product and, thus, helps stabilize product liability insurance costs.

Section 8(a)(2): TPLA recommends that the definition of "misuse" be included in Section 2, because the term is used in several places in the Staff Draft. Misuse is use for a purpose or in a manner that is not consistent with warnings or instructions available to the user or use that would not be expected of an ordinary reasonably prudent person in the same or similar circumstance. Further, misuse might include situations where a product user's failure to train its employee causes the claimant's harm and where a product user's failure to comply with government regulations regarding a product's use causing the claimant's harm.

Section 8(b)(1)(B): TPLA recommends that the reference to "implied consent" be deleted. The matter of consent can best be dealt with in examples contained in Committee Report language.

Section 8(b)(1)(C): The term "reasonably anticipated conduct" is not defined in this section. TPLA recommends that the term be defined in Section 2 just as it is defined in Section 4(d)(2)(D) of the Staff Draft.

Section 8(b)(2)(A): TPLA recommends that the words "safety devices" be added to Section 8(b)(2)(A), lines 21 and 22 on page 22, so that the phrase reads "warnings, instructions or safety devices." Because so many injuries arise out of the negligence in regard to safety devices, this problem should be specifically identified.

Section 8(b)(2)(B): TPLA recommends clarifying the meaning of the term "product user," which appears in Section 8(b)(2)(B) and elsewhere.

SECTION 9

Section 9 of the Staff Draft promotes the goal of placing the incentive for loss prevention on the parties who are best able to accomplish that purpose. Section 9, in conjunction with Sections 7 and 8, serves to increase employer incentives to keep work products safe and, at the same time, does not undermine the limited liability concept that is essential to the workers' compensation system. This approach also effects a substantial reduction in litigation transaction costs.

Section 9(a): TPLA recommends that this provision address the issue of the timely filing of worker compensation claims. In this regard, damages should be reduced by the amount of worker compensation benefits which a court determines has been paid and/or the present value of all such benefits to when the employee is or would be entitled to receive. A court is competent to make that determination, if not already made by the worker compensation carrier. A determination of future benefits is similar to determination of future wage loss, with which courts are familiar. By permitting the court to make that determination at the same time it determines the amount of product liability payment, transaction costs are reduced, see discussion of Section 9(c), and product sellers are protected from those injured employees who may attempt to waive their worker compensation claims in order to obtain a higher product liability judgment.

Section 9(c): If the court makes the judgment described above in Section 9(a), the procedure set forth in Section 9(c) is unnecessary. That procedure, covering situations in which a product liability judgment is rendered before a final determination of worker compensation benefits is made, adds transaction costs inherent in bringing a new action to reduce a judgment or to recoup payment of a judgment by the amount of the subsequent worker compensation award. These added costs can be avoided by following TPLA recommendations with regard to Section 9(a).

Section 9(d): TPLA recommends amending this provision to extend the prohibition against actions for indemnity or contribution to suits against coemployees.

SECTION 10

TPLA fully supports the establishment of a time limitation on liability. By creating separate repose periods for different categories of products, however, Section 10, as drafted, will encourage litigation on what product category and what repose period applies. In light of the goals of the Staff Draft to provide stability in the law and to reduce transaction costs, TPLA recommends uniform repose periods which focus on the type of harm rather than the type of product involved. Outlined below are TPLA's specific recommendations.

- TPLA recommends a reasonable uniform statute of repose of, for example, 10 years for traumatic injuries. Thirty years is an unreasonably long period for traumatic injuries. With regard to non-traumatic injuries, for example, those which fall within exceptions (2) and (4) of Section 10(b), TPLA endorses a longer period of repose, such as 20 years.

- TPLA recommends deleting the provision which would permit a product seller to fix his own period of repose through a warranty. This provision is not only inconsistent with the goal of uniformity, it is also contrary to public policy: the legislature, not individual product sellers, should determine how long product sellers should be responsible for their products.

- TPLA recommends one exception to the uniform statute of repose -- where the product seller intentionally misrepresented or concealed facts about the product. Exceptions (2) and (4) of Section 10(b) would not be necessary, because these situations would be covered by the longer repose period for non-traumatic injuries. Exception (3) of Section 10(b) should be eliminated, because, in TPLA's view, it would create a great deal of litigation with only little or no benefit to injured parties.

SECTION 11

Section 11(a)(1): TPLA recommends that the claimant recover punitive damages only on proof "beyond a reasonable doubt." Punitive damages are, by definition, punitive and not compensatory; thus, the appropriate standard of proof is that used in criminal proceedings: beyond reasonable doubt. TPLA is concerned that, in practice, the "clear and convincing evidence" standard will not be distinguishable from the "preponderance of the evidence" standard. There is, on the other hand, a universal understanding and acceptance of the difference between the "preponderance of the evidence" and "beyond reasonable doubt" tests.

Section 11(a)(2): Punitive damages should be available only in the case of intentional misconduct, *i.e.*, where a conscious decision has been made to disregard a significant safety consideration.

Section 11(a): The standard for determining when punitive damages are appropriate should clearly state that a manufacturer's choice among competing product designs, warnings and instructions, made in the ordinary course of business, even if negligent or grossly negligent, cannot in itself be the basis for imposing punitive damages.

Further, a manufacturer should not be liable for punitive damages if the aspect of its product which caused claimant's harm was in compliance with a government standard. This is a different issue from whether compliance with government standards should be available as a defense in a product liability action. The point here is that a manufacturer has not acted with conscious indifference to human safety if it has complied with what the government has found to be, at least, the minimum relevant safety requirements.

Section 11(b): TPLA supports a procedure which assures that evidence relevant to the amount of punitive damages, but not relevant to the initial determination of liability for punitive damages (such as evidence of a defendant's financial condition or of previous punitive damages awards), do not reach the jury. The determination of liability may be unfairly prejudiced if evidence of a defendant's wealth is put before the jury. One way to prevent this is to require the jury to find the defendant liable for punitive damages and, then, to require the court to determine the amount of punitives.

TPLA has no recommendation with respect to proposals to place limits on the dollar amount of punitive damage awards.

SECTION 12

TPLA strongly supports the intent of Section 12 to prohibit the introduction of evidence of subsequent product repairs or improvements. This rule is consistent with the Federal Rules of Evidence, Rule 407 and has a sound public policy basis. First, such evidence is irrelevant on issues of fault or negligence. Subsequent improvements may be, and generally are, the result of improved technology or knowledge and have no bearing on fault or negligence at a prior point in time. Second, the use of such evidence would discourage product improvements. A manufacturer may forego product improvements rather than risk increased product liability exposure caused when those improvements are admitted in court. It is against the public interest to impede innovative safety measures.

In order to achieve these public policy objectives, Section 12 should deal specifically with two aspects of the subsequent repair rule which have created problems in product liability cases.

1. Section 12 should clearly provide that the evidence is excluded in all product liability actions regardless of legal theory. This would be consistent with Section 3(a) of the Staff Draft which eliminates the various legal theories. Further, this would prevent any attempt to circumvent the rule as was done in Ault v. International Harvester, Inc., 13 Cal. 3d 113, 117 Cal. Rptr. 812, 528 P.2d 1148 (1974), which held that evidence of subsequent repairs was admissible in strict liability cases.

2. Section 12 should take a strong position against the use of subsequent repair evidence in order that exceptions to the rule do not "swallow" it. There are several approaches which may achieve this goal, one of which is to delete the language in parenthesis.

SECTION 13

TPLA is continuing its study of this section and its application and relationship with Section 10, dealing with time limitations on liability. TPLA would like to offer its comments on this section when discussions have been completed.

SECTION 14

TPLA feels that the Staff Draft must provide an effective date after which its provisions would apply to product liability litigation. Some state courts have raised questions about the effective date of statutes of repose and their application to actions that may have occurred prior to the effective dates. TPLA would be pleased to provide any technical assistance which may be required to clarify the intent of this section.

THE SECRETARY OF COMMERCE
Washington, D.C. 20230

MEMORANDUM FOR: MEMBERS OF THE CABINET COUNCIL ON COMMERCE AND TRADE

FROM : Malcolm Baldrige, Chairman Pro Tempore
Cabinet Council on Commerce and Trade

SUBJECT: : PRODUCT LIABILITY

STATEMENT OF ISSUES

1. What are the specific problems being experienced by industry as a result of existing law.

2. What is the appropriate role of the Federal government in establishing uniform product liability standards.

BACKGROUND

A. State Law

The liability of manufacturers for injuries caused by their products has historically been determined under State law. There is now no single body of law governing product liability. Each State has its own case law, and many States have enacted legislation governing various aspects of product liability.

In recent years the product liability statutes of the States and case law interpreting those statutes have been subject to frequent and substantial revision. In addition, approximately thirty-one States have enacted some form of product liability legislation in the past six years. No State has adopted a comprehensive approach to product liability legislation.

Significant differences exist in the laws of the several States governing product liability.

- The Manufacturer's Duty of Care. The legal duty of the manufacturer toward the product user varies significantly from State to State. In some States, the manufacturer is not negligent if he utilizes existing and available technology in designing his product; while in others, he may be liable for injuries which could not feasibly have been "designed out" of his product with current technology.

  Most States now require warnings of dangers associated with the use of a product; however, the content and extensiveness of these warnings are judged by widely differing standards from State to State.

  Many States have enacted laws terminating the liability of manufacturers after a certain number of years; in others, manufacturers continue to be responsible for product safety performance for an indefinite period.

- Defenses. States differ sharply in the defenses available to a manufacturer/defendant. Those States employing "comparative negligence" rules have eliminated virtually all defenses, such as contributory negligence or assumption of risk. Other States retain such defenses, but only in certain circumstances. In many States, for example, a manufacturer is not at liberty to establish that his product had been significantly misused or altered after leaving his control, while other States consider such evidence. This problem is particularly severe in cases arising from workplace injuries.

- Local Rules. Rules governing the judicial determination of liability -- admission of evidence, standards of proof, the *prima facie* case, the award of punitive damages and the use of the doctrine of collateral estoppel -- differ significantly among the States. For example, most States prohibit introduction of evidence of subsequent safety improvements on the grounds that such improvements will not be made if their introduction can be used to establish liability for not introducing them earlier. A few States, however, do admit such evidence. This trend threatens to adversely affect the decision to improve the design of one's product.

While the substantive laws of each State differ, the ability of any State to "improve" the situation is sharply limited. An individual State cannot protect its manufacturers from the costs and uncertainties of product liability laws of other States. At the same time, a State that restricts the ability of local residents to recover from out-of-State manufacturers places local residents at a disadvantage compared to residents of other States -- with little corresponding gain for local manufacturers.

B. Problems Encountered by Manufacturers

Because of the rapid change in product liability law in each State, and because the case law on product liability varies from State to State, manufacturers of products sold throughout the United States cannot determine the standard of conduct to which they will be held. The existing uncertainty has injured manufacturers in a number of ways:

1. Increased Costs of Insurance.

Since the sale of products is not limited to the State in which they are manufactured, insurance companies must build a high contingency factor into their rates to take into account the experience in those States with the strictest laws.

2. Disincentives Toward Product Innovation and Development.

Because manufacturers cannot predict the standards by which new products will be judged, they are wary of innovation or design changes.

3. Increased Litigation Costs.

A significant percentage of legal costs are generated by the need to determine "what the law is" in a State. The American Insurance Association estimates that for every sixty-six cents a victim receives, seventy-seven cents is spent in legal costs. These legal costs to the manufacturer are eventually passed on to the consumer.

PREVIOUS FEDERAL INVOLVEMENT IN PRODUCT LIABILITY

In response to complaints from the business community that disarray among State product liability laws was creating an unmanageable problem, President Ford established a Federal Interagency Task Force in 1976 and appointed the Department of Commerce as its lead agency. The Task Force conducted a major survey of the product liability situation generally. It found that both liability of manufacturers and product liability insurance rates had increased dramatically. Among the principal causes identified by the Task Force for these increases were (1) overly subjective rate-making practices by major insurance carriers, and (2) uncertainties and imbalances in product liability law among the States.

In response to the problem of overly subjective rate-making practices, the Department of Commerce supported, and President Reagan approved, the Product Liability Risk Retention Act of 1981 (Public Law 97-45, September 25, 1981). The Risk Retention Act ensures objective underwriting by permitting manufacturers to form risk retention groups and insure themselves. The Act provides for a limited preemption of inconsistent State laws in order to achieve this purpose.

An outgrowth of the second Task Force finding -- uncertainties and imbalances in product liability tort law resulting from the growing differences among the States as to the standards of conduct to which manufacturers would be held -- was the publication, by the Department of Commerce in 1979, of the Uniform Product Liability Act. This model law for adoption by the States would, if fully adopted, have established uniform standards of conduct (as well as certain procedural and evidentiary rules) nationwide.

THE NEED FOR FEDERAL ACTION

The attempt to solve the problem by having the States adopt the Uniform Product Liability Act has been unsuccessful. Only four States have adopted portions of the uniform law; twenty-seven other States have adopted various other statutes, none of which is alike.

Individual States have not and cannot adequately address the need for uniform product liability laws. This fact has been noted by Governors in Kansas and Connecticut. In vetoing State product liability bills, these Governors have noted that they would make little difference in resolving the problem.

Federal intervention is necessary to alleviate the burdens inconsistent State product liability laws place on commerce. Federal product liability standards would bring greater predictability and uniformity to the product liability process and help stabilize product liability insurance rates. A measure of certainty for product sellers is important for it would encourage research, development, and innovation in product manufacturing and safety. A federal law would inform consumers of their rights while also giving product sellers some assurance of "what the rules are." Uniform standards would also expedite the reparations process and reduce transaction costs.

REGULATION OF INTERSTATE COMMERCE IS HISTORICALLY A FEDERAL FUNCTION •

The regulation of interstate commerce has historically been the exclusive province of the Federal government. It is the interstate character of this problem that creates the need for Federal uniform standards. Such standards in other contexts have been uniformly upheld by the Supreme Court as an appropriate exercise of Federal power under the Commerce Clause. For example, a State may not limit the length of trains operating within the State; regulate the design and structure of ships; or require trucks to be equipped with mudguards which are different from those permitted in other States.

The Federalist Papers consistently support the need for uniform regulation of Commerce. One of the principle failures of the Articles of Confederation was the ability of States to regulate and tax products produced in a neighboring state as they passed through its borders. Both Alexander Hamilton and James Madison agreed on the power of the Federal government to "provide for the harmony and proper intercourse among the States." (Madison, Federalist No. 42).

FEDERAL INTERVENTION TO ALLEVIATE BURDENS ON INTERSTATE COMMERCE IS CONSISTENT WITH THIS ADMINISTRATION'S VIEWS ON FEDERALISM.

The Administration has defined the "New Federalism" in the context of returning local life style decisions to the people affected. Health and welfare standard-setting as well as as food stamp administration and education policies are examples of areas appropriate for local decision makers. Product liability law, as commercial regulation, stands on a different footing.

The request for Federal intervention in this area does not originate in Washington. Rather, the request for relief was brought to Washington by small businessmen frustrated in their attempts to deal with the product liability problem in their respective States.

The Administration has previously employed a limited Federal approach to problems having interstate implications.

The Administration strongly supported enactment of product liability risk retention legislation as a solution to the "insurance side" of the product liability problem. The Product Liability Risk Retention Act of 1981 provided for Federal preemption of State insurance laws as necessary to permit the formation by manufacturers of risk retention groups.

The President's statement upon signing this bill bears repeating:

> "This Act is a marketplace solution designed to provide product manufacturers, distributors and sellers with affordable product liability insurance. In keeping with the Administration's policies, this goal is accomplished without imposing any new Federal regulations or expenditures.
>
> "In particular, the Act removes selected State regulatory barriers so that product sellers can form self-insurance cooperatives... .
>
> "In short, the Act is a good example of how the Federal Government can resolve a nation-wide problem without creating additional programs or agencies."

CONCLUSION

It is highly unlikely that states acting individually through their legislatures or courts can establish uniform product liability standards. It is appropriate for the Federal government to legislate uniform product liability standards. There is an urgent need to achieve such uniformity now.

RECOMMENDATION

1. The Administration support uniform Federal product liability standards.

2. A Working Group of this Cabinet Council be established to develop an Administration position on product liability in response to legislative proposals pending before Congress.

MEMORANDUM

THE WHITE HOUSE

WASHINGTON

April 7, 1982

make file

MEMORANDUM FOR: CHRIS DEMUTH
JOHN FOWLER
MICHAEL HOROWITZ
WILLIAM NISKANEN
JONATHAN ROSE
TIMOTHY RYAN
MICHAEL UHLMANN

FROM: DENNIS KASS
Special Assistant to the President
for Policy Development

SUBJECT: Working Group on Product Liability

The Cabinet Council on Commerce and Trade has designated you a member of the Product Liability Working Group. The Working Group has been directed to identify and analyze the economic and intergovernmental policy arguments for and against a new federal statute on product liability that would preempt jurisdiction of the states in this area. The Working Group is to report its findings and any recommendations to the Cabinet Council in 30 days.

Sherman Unger will serve as Chairman of the Working Group and will contact you directly concerning your participation.

cc: Secretary Baldrige
Edwin Harper
Sherman Unger

PRODUCT LIABILITY

MEMBERS

General Counsel, Department of Commerce	Sherman Unger, Chairman
Assistant Attorney General for Legal Policy	Jonathan Rose
Counsel for Policy Analysis and Law, OMB	Mike Horowitz
Administrator, Office of Information and Regulatory Affairs, OMB	Chris DeMuth
Member, Council of Economic Advisors	William Niskanen
General Counsel, Department of Transportation	John Fowler
Solicitor, Department of Labor	Timothy Ryan
Special Assistant to the President, Office of Policy Development	Michael Uhlmann

DATE ESTABLISHED: April 7, 1982

CABINET COUNCIL ON COMMERCE AND TRADE

STATEMENT BY

JAMES H. MACK

PUBLIC AFFAIRS DIRECTOR

NATIONAL MACHINE TOOL BUILDERS'ASSOCIATION

BEFORE THE

SUBCOMMITTEE ON COMMERCE, TRANSPORTATION, AND TOURISM

COMMITTEE ON ENERGY AND COMMERCE

UNITED STATES HOUSE OF REPRESENTATIVES

APRIL 9, 1981

The National Machine Tool Builders' Association (NMTBA) is a national trade association representing over 400 American machine tool manufacturing companies, which account for approximately 90% of United States machine tool production.

Although the total machine tool industry employs approximately 90,000 people with a combined annual output of around $4.0 billion, most NMTBA member companies are small businesses with payrolls of 250 or fewer employees.

While relatively small by some corporate standards, American machine tool builders comprise a very basic segment of the U. S. industrial capacity, with a tremendous impact on America. It is the industry that builds the machines that are the foundation of America's industrial strength.

We welcome this opportunity to again visit with a Subcommittee of your Committee on the extremely important issue of products liability. It has been slightly over a year since we last reported to you the serious nature of the product liability mess facing our industry. Our 1981 product liability survey shows that almost 60% of our members still either have no primary coverage or have substantial deductibles under their 1981 policies. The average NMTBA member is paying $91,900 this year for primary products liability coverage. This figure represents some easing from 1980's average of $111,700 and is a significant reduction from 1979's average of $143,900. However, in 1976 the average products liability premium was only $71,000 which still seems large when compared to 1970's average of $10,000.

Interestingly, 59% of our members reported that they were able to negotiate a reduction from initial quotations, once they had the opportunity to review their own claims experience (or lack thereof) with insurance underwriters. One out of ten members reported no products liability coverage. This is better than 20%

without coverage two years ago. Forty-eight percent (48%) of our members reported average deductibles or self-retentions, of $42,700. This is up from 39% last year and 30% two years ago.

Some of our members have only nominal primary products liability insurance. These companies have purchased this paper insurance to satisfy customers' sales requirements or to qualify for umbrella coverage, which protects the insured from catastrophic claims which threaten their assets. And even at these staggering prices, still an appalling one-sixth of machine tool builders with annual sales in excess of $2.5 million are unable to secure umbrella coverage.

Although our 1981 Product Liability Survey indicates some softening of insurance markets, I would caution you that the softness of the product liability insurance market is likely to be only temporary.

In the first place, the property-casualty insurance industry is highly cyclical in nature -- even more cyclical than our own industry, if that is possible. The insurance industry has been in a "peak" situation during the last two years, following a "valley" during the mid-late '70's. It was during this "valley" that the annual geometric increases in product liability insurance premiums and -- for some -- absolute unavailability of product liability insurance occurred.

In addition, extremely high interest rates have given insurance underwriters a great deal of capacity through investment income profits of over $11 billion. This has been a "silver lining" in the storm clouds of 20% plus prime interest rates. As interest rates go down and as the property-casualty insurance industry approaches another valley in its cycle, another tightening of insurance markets is almost certain to occur.

The Insurance Service Office (ISO) reports that the property-casualty insurance industry suffered underwriting losses of well over $3 billion during 1980. These data indicate that this tightening is likely to occur sooner, rather than later.

NMTBA strongly supports the compromise products liability Risk Retention legislation encompassed in H.R. 2120, and we commend, you, Mr. Chairman, for having introduced it. H.R. 2120 facilitates the formation of product liability risk retention and insurance purchasing groups, while responding to the principal objections of the insurance industry to H.R. 6152, as it was passed by the House last year.

H.R. 2120 removes the federal regulatory presence, which was contained in last year's legislation; and it defers to state regulation by requiring risk retention groups to be formed under the laws of a state, before federal pre-emption of their regulation by other states comes into play.

Insurance industry objections to last year's House bill have been met and dealt with affirmatively. Indeed, virtually the entire insurance industry has acted responsibly and in a spirit of compromise. They have withdrawn their objections to the passage of H.R. 2120.

But a small but vocal minority have raised new objections. They continue to greet responsible solutions to very real problems with intransigent opposition to anything other than the maintenance of an unacceptable _status quo_.

Their arguments against H.R. 2120 are totally without merit, and the amendments they suggest.would effectively gut the bill. Their earlier arguments against last year's House bill did have the redeeming quality of expressing support for state regulation and opposition to a federal regulatory bureaucracy. Although we believed then (and believe now) that their concerns were unfounded, we were willing to concede that they had a justifiable philosophical foundation.

But their objections having been met, and their concerns having been accommodated, these insurance industry spokesmen are today engaging in the rankest kind of sophistry. Their arguments, when wrung dry of the crocodile tears they weep for an inappropriate and burdensome fabric of state over-regulation, reveal the _real_ purpose for their opposition to legislation facilitating the formation of risk retention groups: _They simply don't want the competition these groups would provide._

Last year insurance industry spokesmen argued with some justification against the creation of a federal agency regulatory presence in the narrow field of products liability insurance. Today, a small minority argue that a federal law which requires a state to recognize the approval by another state of a products liability risk retention group is somehow inappropriate.

We are told by these zealous defenders of the status-quo that your action to remove state barriers to the formation of products liability risk retention and group purchase arrangements would create a "regulatory vacuum". Some have even argued that the removal of these barriers would encourage a spate of illegal activities by unscrupulous risk managers, group promoters, brokers, and agents. It is incumbent upon those who parade these horribles to immediately advise this Subcommittee which state or states are so lax in their regulation of insurance that such illegal practices would flourish unchecked were H.R. 2120 to be adopted.

Furthermore, Sec. 3 (C) permits non-chartering states to license agents and brokers (and to revoke their licenses for fraudulent behavior), thus protecting against abuse.

Your bill, Mr. Chairman, exempts no risk retention group from government regulation. It merely provides that a group, which has been chartered and regulated by a state, may not be regulated out of existence by another state.

The only risk retention groups eligible for preferential treatment are those which have complied with <u>all</u> the insurance regulatory laws of the chartering jurisdiction.

A risk retention group's activity <u>outside</u> its chartering jurisdiction <u>can</u> be regulated by that jurisdiction. For example, a licensing jurisdiction can take action against an insurer who writes risks for insufficient premiums even though those premiums were collected outside of the jurisdiction.

Further precautions are included in H.R. 2120. <u>Subsection 3 (a)(1)(F)</u> permits a non-chartering commissioner to require a risk retention group to submit to an audit, paid for by the group, if he has reason to believe that the group is financially impaired and if the chartering commissioner has failed to act.

<u>Subsection 3 (a)(1)(G)</u> permits a non-chartering commissioner to commence a deliquency proceeding to secure a lawful order terminating or otherwise restricting a group's operations, if the audit mentioned in (F) reveals financial impairment, and the chartering commissioner fails to act within 30 days of his notification of such financial impairment.

Some suggest that the states may find H.R. 2120 attractive and compete for risk retention group business. Since these same people also represent that the states are, in fact, the most appropriate forum for the regulation of insurance, we fail to see why they are concerned if such competition should result. Or is it <u>another</u> kind of competition which the opponents of this legislation fear?

They have proposed that Subsections (3) (a)(1)(F)and (G) be amended so as to remove the protections these subsections currently afford to risk retention groups against being harassed out of existence by over-zealous state regulators. And they have further proposed adding a new Subsection (3) (e) which would make each state insurance commissioner the monitor, interpreter, enforcer, and -- we might add -- manipulator of the entire body of each other state's rules and regulations. Passage of these three amendments would lead to endless litigation, as one state attempts to subtitute its own body of regulation for the regulatory scheme of the chartering jurisdiction under color of "interpretation" and/or "enforcement".

These are "Killer Amendments". They would effectively undo the pre-emption of overlapping and conflicting state regulation provided in H.R. 2120.

When applied to Risk Retention groups, the current fabric of state regulation, rather than fostering a uniform regulatory environment, has created a crazy-quilt of varying state laws. H.R. 2120's opponents apparently believe that compliance with one state's laws should not necessarily be sufficient to permit an insurer to do business in a sister state. Which states do these opponents believe have inadequate regulatory mechanisms?

They have become advocates of a fabric of regulation, which, although appropriate for overseeing an arms-length business relationship between a multiline commercial insurer and its customers, becomes a burdensome patchwork of over-regulation when applied to a group of businessmen who seek the option of pooling their own products liability risks and who will deal only with themselves.

Risk retention groups will be chartered by a jurisdiction which can impose upon them appropriate capitalization requirements. There is very strong self interest on the part of risk retention group members to adequately capitalize their self-insurance fund. If a risk retention group cannot pay its claims, the assets of the individual members being sued will be fully exposed.

Some opponents argue that a risk retention group should be subject to regulation in every state it has members, because the alternative to such regulation would subject to antitrust liability any person who provides services to a risk retention group.

This is clearly not a reasonable interpretation. The antitrust laws would only apply to the extent that the commercial insurer was not regulated by state law by virtue of its specific transaction with a risk retention group. These opponents apparently also assume that risk retention groups will be formed by businesses which will seek to avail themselves of ISO's rates. As a practical matter, groups will be formed and used, precisely because ISO rates are substantially in excess of those indicated by the experience of the prospective group members.

Opponents contend that Section 2 (a)(4)(D) would permit discrimination against similarly situated small businesses who could be denied membership in a particular risk retention group for competitive advantages. However, a careful reading shows that this sub-section is not permissive. It does not authorize the exclusion of any person; rather, it prohibits discrimination for the purpose of providing for a competitive advantage.

The opponents have offered as a "remedy" an amendment which would effectively prohibit any discrimination for any purpose (including normal risk selection) where the effect of membership denial would be anti-competitive. Adoption of this amendment would effectively require a risk retention group to accept any similarly situated business, no matter how bad its record of financial or product liability experience, and would thus defeat the purpose of the act.

Questions have been raised as to whether the exemption from multistate regulation should be extended to risk retention groups chartered in Bermuda or the Cayman Islands, both of which have substantial bodies of responsible insurance regulations. Given the opposition by some insurance industry spokesmen to the entire concept of permitting a risk retention group chartered and regulated in one state to operate free of conflicting and onerous regulations in all other states, the answer should be obvious. Insurance industry lobbying at the state level could cause states to make their laws chartering and regulating risk retention groups so burdensome that the beneficial effects of H.R. 2120 would be undercut. Should this occur, the availability of responsible foreign licensing jurisdictions would become most important and desirable.

Many commercial insurers own at least one foreign insurance affiliate. Should <u>their</u> activities be proscribed? They also engage in fronting activities for Bermuda captives. Should the practice of fronting be abolished by Federal or state statute?

In the spirit of compromise, we agreed last Fall to an amendment "Sunsetting" Bermuda and the Caymans as prospective chartering jurisdictions and requiring that groups chartered there certify that they have met the capitalization requirements of at least one state. We urge the adoption of this provision as an amendment to H.R. 2120. This compromise has been greeted with intransigents by H.R. 2120's opponents. They insist that the offshore safety valve be eliminated altogether. Does anyone doubt their true intentions? Their past record of opposition to state captive laws should be most instructive in this record.

The opposition of some insurance industry spokesmen extends not only to the opportunity for our members to form competitive options to commercial insurance markets in the resolution of their products liability problems. They also question the need for effectively pre-empting state laws, which prohibit or otherwise restrict the group purchase of products liability insurance.

They oppose the expansion of the pre-emption from state laws to include general liability insurance. Products liability insurance is most usually sold as part of an insurance package which includes comprehensive general liability. Thus, its permitted sale by purchasing groups will merely serve to facilitate the formation of such groups and make them more attractive for insurers to do business with.

Conversely, adoption of an amendment <u>prohibiting</u> the group purchase of a combined product liability/comprehensive general liability insurance package will effectively prohibit the group purchase of product liability insurance in the form it is normally offered for sale by the very same people who urge its adoption.

Last year, we confessed that, "We fail to understand the intensity with which some insurance industry spokesmen have approched this legislation.". In the interim, we have come to understand the reasons for that intensity; and we are sorely disappointed.

For what we had earlier belived was a principled defense of state's rights has degenerated into a misguided attack on competition.

If further evidence is needed of the opponents' disingenuous attack on competition, one need only look at their suggestion that H.R. 2120's pre-emption of state laws regulating risk retention groups and purchase groups be sunsetted in 3 years. How many groups could be reasonably expected to be formed, if they know that, in just 3 short years, they will be right back in the same crazy-quilt morass of over-regulation that effectively prevents their formation and operation today?

Sunsetting a federal bureaucracy, if a minimal number of groups are formed within a reasonable time period made some sense; and we supported such a provision in the bill you overwhelmingly adopted last year. But sunsetting the prospective pre-emption from state regulation overkill provided in this year's version makes no sense at all, and those who propose it well know it. Their real motive is to prevent the formation of any competitive mechanisms at any time -- now or in the future.

We urge this Committee to immediately adopt the compromise product liability risk retention and group purchase legislation contained in H.R. 2120 and the offshore jurisdiction sunset amendment we have agreed to. It will foster competition, will appropriately regulate the interstate sale of product liability insurance, and will provide a meaningful (albeit partial) resolution of American industry's product liability problems.

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

April 14, 1982

MEMORANDUM FOR: CHRIS DEMUTH
JOHN FOWLER
MICHAEL HOROWITZ
WILLIAM NISKANEN
JONATHAN ROSE
TIMOTHY RYAN
MICHAEL UHLMANN

FROM: SHERMAN E. UNGER SEU

SUBJECT: Meeting of the Working Group on Product Liability

The first meeting of the Working Group on Product Liability will take place in my office, Room 5870, Department of Commerce, on Monday, April 19 at 3:00 P.M. At that time, the agenda of the working group will be established and a timetable determined.

Please call my Secretary, Brenda Lodge (377-4772) if you are unable to attend.

THE PRODUCT LIABILITY ALLIANCE
1725 K Street, N.W Suite 710
Washington, D.C. 20006
(202) 872-0885

file

MEMORANDUM

April 15, 1982

TO: Members of the Working Group of the Cabinet Council on Commerce and Trade

FROM: The Product Liability Alliance

RE: The Case for Federal Product Liability Legislation

Gentlemen:

The Product Liability Alliance (TPLA) is an organization of more than 150 businesses and trade associations whose membership is a cross-section of those subject to product liability claims. It includes small, medium-size and large businesses; manufacturers, wholesalersand retailers; and insurers and insurance brokers.

TPLA was formed to support the enactment of a balanced and effective Federal product liability statute. TPLA is not a policy making entity; it takes no position on particular provisions of pending proposals. Rather, it serves as a forum for communication among groups with widely divergent views on product liability, a catalyst for consensus.

TPLA members believe that the rules governing the obligations of product sellers and the rights of product users should be codified in a statute; that such a statute will be effective only if it is enacted at the Federal level; and that such a statute should be balanced -- fair to those who make and sell products as well as to those who use them.

The businesses belonging to TPLA are firm believers in President Reagan's economic recovery program, and strong supporters of his efforts to delegate to the States and the private sector regulatory and other functions that do not require Federal involvement. At the same time, they recognize that some problems cannot be dealt with by the States. Product liability law is such a problem.

Products made in one State may be distributed in several others, sold in still more, and used in all. The rules governing the manufacturer's liability for harm caused by his products are established primarily on a case-by-case basis not merely in his home State courts but by courts in every other American jurisdiction. These rules vary widely from State to State, and are becoming progressively less predictable and increasingly unfair.

Individual States have attempted to deal with this problem by codifying their product liability rules. Some 28 States now have product liability statutes, but all of them are different. Worse, some of them have impaired in-State consumer rights while doing nothing to make a manufacturer's out-of-State liabilities less uncertain. Ironically, these good-faith efforts by the States to cope with the interstate product liability problem have, if anything, compounded it.

The interstate movement of products requires product liability insurers to make rates on a nationwide basis, whereas rates for all other lines of insurance are made on a State-by-State basis. Individual State aberrations from the majority rule on a given issue thus have repercussions for premium payers in all other States, since it cannot be predicted when these "highest common denominator" rules may come into play for a given manufacturer's products.

The inability of the States to deal effectively with the interstate nature of products liability suggests the appropriateness of limited Federal intervention in the process of balancing product sellers' and product users' rights and duties.

TPLA believes that the Federal role in product liability should be limited to the determination of the policy governing the obligations of businesses whose products move in interstate commerce, since the States cannot, by their own actions, achieve the uniformity essential to a stable and predictable product liability law. TPLA also believes that the mainspring of Federal policy should be fairness to both product sellers and product users.

At the same time, TPLA believes that the States will be able and should be permitted to implement Federal product liability policy through their court systems. A Federal product liability statute, applied in individual State court actions, would add no costs to State judicial systems. Moreover, since uniform rules would tend to discourage the "forum shopping" now prevalent in product liability cases, Federal court caseloads in actions based on diversity jurisdiction should decline.

TPLA believes that the Working Group will find the case for a fair Federal product liability law persuasive, and suggests that the Group's recommendations to the Cabinet Council focus first upon the need for such a law. The development of the statutory details will be an evolutionary process, and we believe that it would be premature for the Working Group to base its overall policy judgment on specific provisions of legislative proposals subject to change.

It has been suggested that Administration policy toward product liability legislation should be developed in the analytical framework commonly applied to proposed Federal programs or economic regulations. Some have argued that because a Federal product liability law would to some extent "regulate" State courts, any such proposal should therefore be evaluated in terms of relative economic costs and benefits.

While a Federal product liability law would certainly limit the range of State court discretion on broad legal questions, it would in no way impinge upon the current method State courts use to determine liability in individual product injury cases. Indeed, it would make that task easier. Thus, to characterize a Federal product liability law as a "regulatory" statute misconstrues its purpose, which is to fairly balance the interests of plaintiffs and defendants in product liability law.

Similarly, while a Federal product liability law would certainly affect the costs associated with product liability, it does not, as a proposed Federal program or economic regulation would, involve an expenditure of tax dollars against which its benefits can be weighed. Indeed, while some of the economic benefits of a Federal product liability statute could be quantified (e.g., reduction in transaction costs resulting from the elimination of subrogation and contribution actions in workplace product liability cases), others cannot be (e.g., economic implications of a fault standard in product design defect and duty to warn cases). Moreover, how can an economic value be assigned to the concept of fairness?

To apply cost-benefit analysis to what amounts to a codification of the law in the majority of States assumes that there are tangible costs against which the largely intangible benefits of such a codification can be balanced. We can see no such costs.

The difficulties of trying to weigh a Federal product liability law in the traditional cost versus benefit scale are best illustrated by the fact that most of the pending legislative proposals preserve traditional causes of action in product injury cases. For example, all pending proposals preserve claims alleging strict liability in tort for product manufacturing defects. Thus, there is no way of estimating whether there will be more or fewer such claims.

Similarly, it would be impossible to calculate the value of legal man-hours saved by a Federal law's elimination of the current need to brief every legal issue over and over again in every action in every State court.

It has also been suggested that the recent stability of product liability insurance rates is barometric evidence that there is no product liability problem. This is emphatically not the case. Product liability is a "long-tail" line of insurance in which the majority of claims arising during the policy period are settled years later. Thus, the impact of the near tripling in the number of product liability claims filed in Federal District Courts alone during 1975 (2,886) and 1981 (9,071) will not begin to be felt until sometime after those cases go to verdict or are settled in the years to come. Moreover, most major product manufacturers substantially or entirely self-insure their product liability, so that insurance data does not fully represent the frequency or severity of product liability losses. An enclosed TPLA "Background Paper on Product Liability Insurance" addresses these and other points in detail.

The adversary system of justice is enormously expensive, and will remain so with or without a Federal product liability law. A Federal product liability statute would preserve -- indeed it would strengthen -- the fault basis for assignment of liability in product injury cases, and therefore does not have as its sole purpose a reduction in the transaction costs of the tort system. Thus, to analyze a concept whose thrust is equitable in economic terms is a disservice both to the concept and to cost-benefit analysis.

We are enclosing several TPLA documents which you may find useful in your analysis of the product liability issue:

(1) "The Product Liability Problem" -- This is a two-page summary of the case for Federal product liability legislation.

(2) "Elements of a Fair Federal Product Liability Statute" -- This document outlines the key issues TPLA recommends be dealt with in Federal product liability legislation.

(3) "Background Paper on Product Liability Insurance" -- This paper relates the history of Federal examination of the role of insurance rate making practices in the product liability problem and describes the Congressional resolution of the insurance issue (the Product Liability Risk Retention Act).

(4) "Summary of Public Comment" -- This compendium of all public comment on the Senate Consumer Subcommittee's Staff Draft No. 1 of the Product Liability Act, prepared by TPLA Counsel Victor E. Schwartz, is a useful guide to the perspectives the entire spectrum of affected interests have on product liability.

(5) "Compendium of Comments" -- This document synthesizes the views of TPLA members on the first Staff Working Draft, and is a useful illustration of the consensus approach the TPLA has taken toward the substance of Federal product liability legislation.

We think these documents make a strong case for the need for a Federal product liability statute that fairly balances product seller and product user interests. They show that while there may be divergence as to precisely what such a statute should contain, there is little doubt as to its necessity. The last two in particular show how quickly a consensus can be developed on details among those with a common goal.

With the first meeting of the Working Group scheduled for Monday, April 19, we wanted to get this preliminary material in your hands as quickly as possible. While we will be following up with you individually in more detail next week, please feel free to call upon any of the TPLA member organization representatives listed below if we can be of assistance to you prior to your April 19 session.

Les Cheek	Crum & Forster Insurance Companies	296-5850
Bob Fields	FMC Corporation	293-7900
Jim Mack	National Machine Tool Builders Assn.	893-2900
Victor Schwartz	Crowell & Moring	452-5873
Dirk Van Dongen	National Association of Wholesaler-Distributors	872-0885

THE PRODUCT LIABILITY ALLIANCE
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BACKGROUND PAPER ON
PRODUCT LIABILITY INSURANCE

The Federal Interagency Task Force on Product Liability, after a two-year study of the severe product liability insurance market dislocations of 1974-76, concluded in November, 1977, that the insurance availability and affordability crisis experienced by many American businesses was the manifestation of a problem with three discrete elements: (1) <u>overly subjective insurer rate-making practices;</u> (2) <u>unsafe manufacturing practices;</u> and (3) <u>growing uncertainty in the State laws governing product liability</u>.

The Task Force developed proposals to address each of these elements concurrently.

To encourage safer manufacturing practices and to stabilize the legal environment, the Task Force drafted a model State statute, the Uniform Product Liability Act (UPLA), which codified the rights of persons injured by defective products and the obligations of product sellers.

With respect to insurance, the Task Force proposed the Product Liability Risk Retention Act, to facilitate business use of competitive alternatives to commercial coverage; and undertook a two-year study of product liability insurance rate-making processes.

The genesis of the Risk Retention Act was the complaint by many sellers that their product liability insurance rates (or rate increases) did not fairly or accurately reflect their loss experience or loss potential. In some cases, these complaints were justified, since product liability insurance rates generally are based on the experience of entire industries, not of individual companies within these industries.

The Risk Retention Act was designed to enable product sellers who believed they were being overcharged by their commercial product liability insurers to join together either to form their own insurance companies (called "captives") or to organize "purchasing groups" to obtain rate concessions through the purchase of group coverage in the commercial market. The theory of the Act was that potential competition from product seller captives and purchasing groups would both encourage commercial insurers to price their policies accurately and fairly and relieve market pressures in the event of a tightening of commercial insurance availability.

Initial insurance industry opposition to the Act, based on its creation of a Federal chartering authority for risk retention groups, was dissipated through revisions permitting the groups to be chartered under State law or (until January 1, 1985) in Bermuda or the Cayman Islands, and by the time the bill became law (P.L. 97-45, September 25, 1981), all semgents of the industry either supported it or did not actively oppose it.

In July, 1978, the Task Force asked the Commerce Department to undertake a study of product liability insurance ratemaking procedures, evaluating, among other things, "the appropriate Federal role in product liability insurance;" "the effectiveness of initiatives by State regulators and the insurance industry to address the problem;" and "whether the product liability premiums can more closely reflect actual product risk."

The Department's Report, issued in August of 1980, concluded that "all of our proposals can be accommodated without a Federal intrusion," and that "the present system of State regulation... can, at least theoretically, take our concerns into account." Any "Federal regulatory presence," the Department said, "would be premature."

The Report noted that "the insurance industry and State regulators are taking certain steps to improve" overly subjective ratemaking practices, but set forth "a number of recommendations for improvements in product liability ratemaking methodology" and allocated "responsibility for their implementation among ISO (the Insurance Services Office), insurers, State regulators, the NAIC (National Association of Insurance Commissioners), and State legislatures."

Many of the Report's recommendations focused on the incompleteness of the industry's product liability data base; the ISO, the principal insurance statistical advisory and rate service organization, could not separate product-related losses from other losses covered under the Comprehensive General Liability (CGL) policy, the form in which a large portion of all products coverage is sold.

But, the Report noted that "ISO has made substantial improvements over the practices that existed prior to 1974 in its collection of product liability data," and concurred with ISO's belief that, with the 1978 revisions to its Commercial

Statistical Plan (CSP), "it is collecting sufficient data to enable it to (make rates) adequately."

The Report also warned that limitations inherent in data required by the NAIC and under a variety of State statutes "render it ineffectual in drawing inferences concerning industry wide product liability insurance experience:"

> The NAIC supplement to the annual convention statement, as well as the reporting requirements of individual States, are providing an over-abundance of product liability information. Much of the information being requested is of marginal utility.
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> The NAIC supplement is subject to a number of difficulties, one of which is its failure to match losses and expenses with appropriate periods giving rise thereto....
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> If one is seeking to ascertain the profitability of writing product liability insurance this cannot be fully gleaned from the NAIC supplement.
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> State reporting statutes which require nationwide experience are needlessly duplicative of the NAIC supplement. Moreover, such requirements are subject to the same limitations and criticisms as are the nationwide data on the NAIC supplement, and from the vantage point of the State regulator (appear) to be of marginal utility.
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> Since product liability experience is generally required to be furnished on a State basis pursuant to these reports, the reported experience is subject to difficulties in connection with the allocation of experience attributable to multi-State activity. The most appropriate allocation for multi-State business would be to allocate premiums on the basis of exposures generated by activities within a State, and to include losses attributable to such exposures (regardless of where they occur). This would equate a multi-State enterprise with a business situated solely in a single State.

The Report recommended that State legislatures "repeal State product liability reporting laws, assuming the State uses the NAIC product liability supplement, as amended with recommendations proposed herein."

Finally, the Report recommended that NAIC revise its product liability reporting form to more accurately reflect the role that income from investment of premiums plays in a line of insurance in which many losses are paid years after the premium is collected. The Report observed that

> ...insurers potentially earned substantial amounts of investment income from the writing of product liability insurance which is not reflected in product liability rates; and...the product liability underwriting losses complained of may be significantly offset by the substantial amounts of investment income.

A significant number of the Report's recommendations have been adopted by both the industry and its State regulators. <u>Moreover, many of the problems addressed by the Report have disappeared as a result of changing market conditions and competitive considerations</u>.

Indeed, even as the Commerce Department began its study, the product liability rate increases and market restrictions of earlier years disappeared. The following table shows the countrywide effect of the combined rate level changes for ISO product liability bodily injury and property damage coverages, basic and increased limits, from 1975 through the first nine months of 1981:

1975	+ 117.3 percent
1976	+ 35.7 percent
1977	+ 3.1 percent
1978	+ 0.1 percent
1979	- 1.6 percent
1980	- 0.7 percent
1981 (9 months)	- 5.8 percent

Attractive investment returns precipitated a competitive struggle for premium dollars among insurers and their reinsurers in recent years that shows no sign of abatement despite steadily worsening loss ratios. The "cash flow underwriting" phenomenon of the past two years is based on insurers' belief that in "long-tail" lines like product liability, returns on the investment of premiums will make up for the inability of those premiums to cover anticipated losses and expenses.

Given the historically cyclical nature of the insurance business, it is likely that product liability rates will move upward again at some point in the future. The current price war among insurers is artificially depressing rates and must inevitably give way to a recognition of underlying cost pressures -- inflation, increasing claim frequency, and radical changes in the tort litigation system.

Future increases, however, will not likely replicate the "panic pricing" crisis of the mid-1970's. A more complete and substantial data base exists today, giving both insurers and their regulators greater confidence in pricing product liability coverage; consequently, future rate adjustments are likely to be more gradual than those the precipitated the crisis of the 1970's.

Moreover, the availability of competitive alternatives to commercial insurance (self-insurance, risk retention groups, etc.) assures that market forces will temper any upward movement of rates that is inconsistent with actuarial experience.

Two major imponderables remain: If interest rates drop precipitously, prices in the marketplace are likely to rise.

And it is difficult to anticipate the effect that several recent court decisions (e.g., Sindell, Schiavone) will have on product liability claim frequency and/or severity. But even if interest rates drop dramatically and claim frequency and severity soar, these developments will likely be reflected gradually, rather than suddenly.

The ISO generally uses the countrywide experience of all reporting companies for five years as its data base in the development of future rates. Thus, a dramatic increase in claim frequency or severity in the latest year would be tempered by the experience of the previous four years in developing rates for the future. Presumably the ISO trend factors would also pick up the upward trend in cost or frequency.

As the Task Force Report observed, the impact of one State's court decisions is national, rather than local. Not only is one State's experience for all companies meaningless for ratemaking purposes, even it it involves five years of data, but also, the movement of products among all the States renders any attempt to produce State-by-State product liability rates futile. A product made in one State may be sold and used in dozens of other States, each with quite different rules governing the manufacturer's tort liability. Moreover, legal precedents in one State may encourage the filing of suits there.rather than in other jurisdictions. Thus, realistically, rates for even a localized business must be based on its national exposure, rather than its potential liability in its home State.

Conclusion

Any insurance system ultimately reflects the underlying costs of the legal system to whose liabilities it must respond. Improved data collection and statistical analysis, and competitive alternatives to commercial insurance, assure that product liability insurance prices will be increasingly responsive to losses and expenses. For insured and self-insured businesses alike, the amount of those losses and expenses depends on the success or failure of efforts to create better incentives for safe manufacturing practices and to restore balance to the tort litigation system.

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