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Returning Justice to the Judicial System: Procedural Protections from Frivolous Litigation

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Recommendations

- Americans go to court more often—and at more cost—than any other people in the world.
- By 2008, the static cost of litigation had risen to $328 billion per year. Adding the indirect economic effects on society makes that figure swell to over $865 billion annually.
- Judicial backlogs caused by needless mass-tort litigation and other frivolous lawsuits prevent meritorious claims from getting to trial.
- A loser-pays statute would overcome high transaction costs and ensure that all tort plaintiffs with meritorious claims have access to the judicial system.

Introduction

Americans go to court more often—and at more cost—than any other people in the world.[1] As a result, many states, including Texas, have taken action to reduce those costs. These efforts are commonly known as tort reform.

Black's Law Dictionary defines a tort as a civil wrong for which a remedy may be obtained.[2] Tort reform is a movement to end lawsuits clogging our courtrooms that seek a remedy where no civil wrong has been committed, or a remedy out of proportion to the wrong that has been committed. These meritless lawsuits make litigation more expensive and reduce the number of meritorious claims that deserve access to the courts (i.e., those claims that are truly legitimate causes of action).

The purpose of tort reform is to reduce the amount of meritless—or frivolous—litigation and excessive awards. Doing so will reduce legal costs, provide greater access to the courtroom, lower insurance and health care costs, and prevent "windfalls"—unnecessarily large damage awards. Additionally, eliminating excessive windfall or "jackpot" awards and frivolous lawsuits from the American legal system will help return justice to the forefront of the judicial system.

Beginning in the 1970s, reformers began a major campaign to limit litigation abuse.[3] A second wave of reform occurred in the mid-1980s, and a third in the late 1990s.[4] A renewed push emerged in the states after the presidential election in 2000.

Texas has passed significant tort reform legislation, making Texas the national model for tort reform. Texas' landmark legislation was passed in 2003. Texas adopted a $250,000 cap on non-economic damages for pain and suffering in medical malpractice cases. This law dramatically reduced doctors' malpractice insurance premiums and cut the number of lawsuits filed against physicians in half. In fact, since 2003, medical malpractice lawsuits have dropped by more than 50 percent and the number of practicing physicians in Texas has increased from 35,000 to 55,000.[5] Nevertheless, Texas still faces a large number of frivolous lawsuits.

A significant reason for the high cost of litigation for Americans, and Texans in particular, is abusive litigation. Abuse occurs when a plaintiff's attorney files a case despite good reason to believe his client is not entitled to a recovery in order to coerce a settlement from the defendant. The plaintiffs' bar knows the high cost of defending a lawsuit makes it likely that many defendants will opt for settlement—regardless of the probable outcome of the lawsuit.[6] And because there are few negative consequences for a plaintiff's attorney that files abusive litigation, the practice still continues.

Because of this, tort reform recently started to focus on "loser-pays" proposals that would make unsuccessful litigants liable for their opponents' legal fees.[7] These loser-pays initiatives are designed specifically to target the backlog of abusive and frivolous litigation.

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Frivolous Lawsuits and the American Rule

The current system of tort litigation is expensive. In the United States, the direct costs of tort litigation reached $247 billion in 2006,[8] with these costs growing at an annual rate of 9.2 percent of Gross Domestic Product ("GDP") even as GDP was growing only at a 7 percent rate.[9] By 2008, the static cost of litigation—damage awards, defense costs, administrative costs, etc.—had risen to $328 billion per year.[10] Adding the indirect economic effects on society—as explained below—from tort cases, makes that figure swell to over $865 billion annually.[11] That number constitutes an annual "tort tax" of $9,827 on a family of four,[12] and equates to roughly 2.2 percent of GDP.[13] So, while we don't know the exact toll that frivolous litigation takes on the economy, we do know that frivolous lawsuits represent a significant portion of the total number of lawsuits.

To fully understand the need for tort reform measures including loser-pays statutes, we must take the total cost of our tort system into account. As Lawrence McQuillen explains in *The Wall Street Journal*, "any true estimate of the costs of America's tort system must also include these dynamic costs of litigation—the impact on research and development spending, the costs of defensive medicine and the related risk in health-care spending and reduced access to health care, and the loss of output from deaths due to excess liability."[14] Additionally, the opportunity costs must be considered. Money spent defending frivolous lawsuits could be spent elsewhere in the economy.

PricewaterhouseCoopers calculates that medical liability concerns increased annual health care spending by $124 billion in 2006 dollars alone.[15] As costs related to medical liability increase, companies and small businesses are forced to respond by switching funds from research and development and innovation into litigation defense.[16] Foregone research and development due to excessive liability results in estimated lost sales of $367 billion in new products.[17] There is no way to properly calculate the opportunity cost from the billions of dollars that could have been invested or otherwise used for innovation and economic growth.

Many of these increased legal costs come from cases that are filed because of the American rule. Currently in the United States, each party to a lawsuit generally must pay its own legal expenses regardless of a case's outcome. This is known as the American rule, since many other countries have civil legal systems that operate under a loser-pays approach toward attorneys' fees. Under a loser-pays system, the loser in a civil suit generally must cover the reasonable legal expenses of the winner.

While the American rule can improve access to the courts, it also encourages frivolous lawsuits that make our civil justice system inefficient and costly as defendants face the choice of quickly settling meritless cases or defending against them at significant cost.[18] An innocent defendant almost always loses financially. Even if the case against him is dismissed, he generally will be required to pay his attorneys.

Frequently, defendants—even those relatively confident of prevailing in court—will settle frivolous or abusive lawsuits if the cost of filing an initial response to a complaint is significant, since the very cost of replying makes settlement attractive.[19] This occurs even in cases where filing an initial response is not overly expensive, because a defendant may be unable to initially tell whether a particular suit is an abusive suit. For example, in mass torts litigation, the transaction costs to sift through thousands of claims to separate the good cases from the bad can exceed the cost of settling the claim. This results in, as Marie Gryphon succinctly explains, "low-merit legal cases clog[ging] the American legal system and rais[ing] the cost of goods and services to consumers by forcing businesses that are sued to cover their legal expenses by raising prices."[20]

In addition, the backlog of cases currently in the judicial system ensures that many cases will take years before reaching trial. During that period, both parties file and argue motions, sift through massive amounts of discovery, depose witnesses, and otherwise prepare for trial. Years of attorneys' fees are included in a defendant's litigation expenses, making it even more likely that a defendant will settle regardless of the merits of the case.

Dealing with Frivolous Lawsuits in Texas

Loser Pays

Two states have implemented loser-pays. Alaska's version grants prevailing defendants 30 percent of actual attorneys' fees for tried cases, and 20 percent for cases settled or otherwise not tried.[21] Alaska's statute has been on the books for over 100 years, giving plenty of time to conduct an analysis of the effects of its loser-pays statute. The Alaska Judicial Council conducted a survey of Alaska attorneys and concluded that the loser-pays statute reduced the number of low-merit cases filed by rational, middle-income plaintiffs.[22] In addition, tort

suits constitute only 5 percent of all legal matters, or cases in Alaska—including those not necessarily reaching trial—approximately half of the national average.[23]

In 1980, Florida adopted a loser-pays statute that dealt expressly with medical malpractice lawsuits. The rule was seen as imperfect because it only related to medical malpractice claims and many plaintiffs were unable to pay when they lost.[24] The law drew criticism from both sides, and was dropped in 1985.[25] Economists Edward Snyder and James Hughes looked at the results of the rule, and the numbers show Florida's decision to revert back to the American rule might have been premature. The rule caused 54 percent of medical-malpractice plaintiffs to voluntarily drop their lawsuits—10 percent more than previously dropped under the American rule.[26] Additionally, the number of settlements for less than $10,000 also dropped by 12 percent while the rule was in place,[27] suggesting that the sort of nuisance lawsuits that loser-pays statutes are intended to prevent, were also declining.

The experiences in the states shows just some of the benefits that the adoption of a loser-pays statute in Texas. A loser-pays statute would effectively decrease the number of nuisance suits filed in Texas. As Marie Gryphon explains, "Because 'loser pays' would make nuisance suits less valuable, the effective hourly rates of nuisance lawyers would decline. In the face of reduced earnings, some nuisance lawyers would surely choose to file different kinds of cases (such as meritorious small claims), or they would migrate to other specialties or careers."[28]

The reduction in nuisance suits would allow more meritorious claims to get to trial. Judicial backlogs caused by needless mass-tort litigation and other frivolous lawsuits cause excessive backlogs preventing meritorious claims from getting to trial. This amount of time also increases litigation costs, as parties spend more time answering discovery and responding to motions. A loser-pays statute would shift the break-even line for suits taken to trial,[29] because defendants would not have to consider the cost of going to trial against the cost of settling the case in doing their cost-benefit analysis.

Critics who worry that the rule would limit access to the courts often fail to acknowledge that the American rule essentially eliminates court access for small but strong claims of injury, unless the claims can be grouped into a class action.[30] So a loser-pays statute might mean that smaller, high-merit claims presently avoided by plaintiff's attorneys would find a place on the docket.

Also, a loser-pays statute should decrease the number of costly mass-tort claims. Plaintiffs' lawyers would no longer have the incentive to seek out potential plaintiffs with unmeritorious claims because cases would more likely go to trial rather than being settled, with plaintiffs being required to pay the cost of the fraudulent claims.[31] The emphasis of loser-pays on meritorious plaintiffs would ensure court access for plaintiffs with real injury.

Some argue that loser-pays would drive up litigation fees by making both sides more desperate to prevail. This argument incorrectly assumes that parties are not already maximizing their chances to win when the claim is serious enough to go to trial, and that increased spending increases the chances of success. In fact, the American rule is what leads to increased spending. Maria Gryphon has observed that "plaintiffs' attorneys in the United States bury defendants in onerous discovery requests, knowing that their clients bear none of the costs of document production; the cost of discovery itself increases cases' settlement value."[32] Therefore, a loser-pays statute will actually likely decrease the amount of money spent on litigation.

While the evidence consistently shows that adopting a loser-pays statute will decrease the filing of frivolous lawsuits, not everyone agrees on the best way to implement such a statute. Some questions that must be asked include: whether a straight, 100 percent loser-pays statute works, or whether a statute should only award a percentage of litigation expenses, such as Alaska's statute? Either way, which fees should be considered? Should the statute only apply to abusive lawsuits, or to all manners of litigation? If there is to be a finding of abuse first, who makes that determination? If you apply it to all types, should the pay be specific to the case? Should we give the defendant the ability to declare loser-pays at the beginning of the suit? Should the plaintiff's attorney be held accountable? If so, is that in all cases or just contingency fee cases? The best way to analyze these questions is to look at them individually.

We'll begin by examining a straight loser-pays system, which is the most pure form of the rule. In theory, this would be the highest deterrent to filing frivolous lawsuits, because the plaintiff would be forced to pay the entire amount of defend-

ing the lawsuit, as well as his own lawsuit. Of course, that wouldn't necessarily be the case if the plaintiff's attorney was working on a contingency fee basis. That would simply mean that the plaintiff's attorney did not receive a paycheck for his work on the case, and the plaintiff would have to pay for the defendant's costs of defending the case. Since most of the frivolous lawsuits that are filed are on a contingency fee basis, there is a very real concern regarding poor and middle-income plaintiffs who fear losing a lawsuit against a large company and thus incurring ruinous attorney fees. Or, on the defense side, a concern is the "judgment proof plaintiff," or a plaintiff who files suit and then cannot afford to pay the defense costs after losing or being thrown out of court. At that point, the system becomes a defendant pays system, which would likely not stem the tide of frivolous lawsuits.

To protect prospective litigants, lawmakers could put in place an insurance system.[33] Asking a plaintiff to show proof of insurance upon the filing a lawsuit would help ensure the system works for both plaintiffs and defendants. An insurance system could decrease frivolous lawsuits, while ensuring meritorious claims are still heard.

Another decision involves whether attorneys should be held accountable under a loser-pays statute. Many argue that the plaintiffs' attorneys that bring frivolous lawsuits should be held jointly and severally liable with their clients. Plaintiffs' attorneys are in a unique position since they often know the difference between meritorious claims and frivolous or abusive lawsuits. If plaintiffs' attorneys are not liable for the costs of filing frivolous lawsuits, a loser-pays statute will not deter them from continuing to file these cases. Plaintiffs' attorneys that operate on a contingency basis have an ownership interest in the case—and are thus driving the decision to continue with or drop the case. This is especially true in mass tort cases.

Another question is whether a loser-pays statute should apply to all lawsuits, or only those found to be abusive. By applying the statute to all lawsuits, there is a strong incentive forcing plaintiffs to ensure they have a valid, legal cause of action prior to filing the lawsuit. This would dramatically reduce the number of lawsuits filed, and would free up the backlog of cases that are currently on courts' dockets. However, there is risk that some poor and middle-class plaintiffs would be prevented from filing lawsuits, and applying a loser-pays statute to all cases could prevent meritorious claims from being filed.

If the loser-pays statute should only apply to abusive lawsuits, the next question is who determines whether a lawsuit is abusive? While the trier of fact would be the most likely source, does this mean that the jury must make this determination? If a jury is empaneled, they are the most logical choice. Our current system allows for the jury to determine the questions of fact during trial.

There is also debate about when that determination should be made—during the case, or after the verdict is rendered? If it is to be made after the verdict, do you ask the same jury to deliberate further or do you empanel a new jury for this question? Asking a new jury to look at the facts would not only decrease the efficiency of the court system, but the new jury would not have the knowledge that the original jury gained from actually sitting through the trial. It seems in the best interests of justice and efficiency to ask the same trier of fact that heard the case to make the determination, and to have them make that determination at the time of the initial verdict.

Another consideration is whether the statute would allow the defendant to decide to opt-in to the loser-pays system. For example, if a plaintiff brings a lawsuit against a defendant, and the defendant believes the case to be frivolous, could that defendant decide that the case should move forward under a loser-pays system? Having this kind of system could lead to more sincerity in case filing. This would help reduce the backlog of cases, because plaintiffs' attorneys would not want to pay the costs of preparing and filing frivolous lawsuits, without receiving any compensation.

All of these questions need to be researched to ensure that Texas would have the best possible loser-pays statute. A statute that is good for Texas and good for our judicial system. The final bill must be created to ensure efficiency, certainty, and fairness to all the parties involved with meritorious claims.

Federal Rules of Civil Procedure 9 and 12

In Texas, having a case dismissed prior to trial is difficult. Generally the option available to a defendant for dismissal is under a "no evidence motion for summary judgment." What that means is that, if after the discovery period has finished, there is still no basis for the lawsuit, then the judge can dismiss the case. There are two problems with this motion. First, this motion to dismiss the case cannot be made until after all the pleadings have been filed, and discovery has been completed.

This can be several years after the initial filing of the case, and after significant costs have accumulated on both sides. Second, there is a reluctance amongst the judiciary to grant a summary judgment. A significant reason for this reluctance comes from the fact that a large amount of time has been spent on the case prior to making the motion. If the amount of time spent on the case prior to trial decreased, the judicial preference towards continuing to trial would likely decrease significantly.

The federal system works differently using Rule 9 and Rule 12 under the Federal Rules of Civil Procedure (FRCP). FRCP 12 grants defendants a mechanism that allows judges to dismiss a case soon after the lawsuit is filed. FRCP 12 is one main reason why Federal courts do not have the same litigation backlog as Texas. The key aspect of the Rule is what's commonly referred to in the legal community as a Rule 12(b)(6) motion. Rule 12(b)(6) states "… the following defenses may at the option of the pleader be made by motion: (6) failure to state a claim upon which relief can be granted."[34] This language gives the judge the right, once the motion is granted, to dismiss a frivolous lawsuit. The most important aspect of this motion is that it can be filed at any time after the plaintiff files suit. A defendant would no longer have to wait for the conclusion of discovery before moving to dismiss a frivolous claim.

FRCP 9 works to ensure accuracy and detail in a plaintiff's filing by mandating a plaintiff in a lawsuit plead any special matters. Special matters include things like fraud or mistake. Rule 9(b) states "In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake."[35] By forcing a lawsuit to be specific when it is filed, judges can more accurately determine meritorious cases from frivolous cases. This level of specificity is necessary to help determine when a case should be dismissed as frivolous.

Interlocutory Appeals for Controlling Issues of Law

A second procedural tool that should be considered by Texas is allowing interlocutory appeals on controlling issues of law, such as a summary judgment motion (i.e. motion to dismiss). An interlocutory appeal is one that can be reviewed by an appellate court immediately, without having to wait for the end of the trial. The advantage of interlocutory appeals is that an appellate court could immediately rule whether a claim is frivolous and have it dismissed. In this instance, parties to a suit would not have to continue with an expensive trial, nor pay for attorneys to draft appellate briefs, etc. Additionally, there would be more incentive for a trial court judge to make the correct determination, because he would risk being overturned by the appellate court.

Currently, in Texas, interlocutory appeals are only allowed if they are on the list of items allowed, or if both parties and the trial court judge agree to allow the ruling to be appealed. The latter avenue practically never occurs. There is no incentive for the prevailing party to agree to have the ruling reconsidered, and generally the trial court judge does not agree. It is not in the judge's best interest to risk having another court disagree with his decision.

Changing the law to allow for interlocutory appeals on controlling issues of law would improve the effectiveness and efficiency of the court system. The disagreements over this statutory change revolve around defining how exactly to implement the rule. For example, would the appeal be automatic? Does the trial judge act as the gatekeeper? If trial judge act does as the gatekeeper, the same scenario we have today would likely reoccur—that the trial judge does not want to be overturned, and thus would be unlikely to send the appeal up to the appellate court.

If not the trial court judge, would the appellate court be the gatekeeper? This would help to ensure that more interlocutory appeals are heard at the appellate level, but with the influx of interlocutory appeals, there is a risk that the number of appeals could overwhelm the appeals courts. If that happens, then many valid appeals may not be heard. Therefore, an independent regulatory official who decides which interlocutory appeals get heard by the appellate courts may be needed. Such an independent regulatory official would prevent bias in the decision making process while ensuring that justice is served to litigants.

Creation of an Expedited Claims Docket

A third procedural mechanism to be considered is the creation of an expedited claims docket. Such a docket would be set up for smaller claims, such as cases where the damage award amounts being sought are between $10,000 and $100,000. Creating a new docket would primarily accomplish two things. One, the new docket would ensure recourse for small meritorious claims that are not currently being litigated due to the high cost and low profits for plaintiff attorneys. If there was an avenue to move smaller claims quickly through the system, costs could be kept low, and plaintiffs' attorneys

would then be incentivized to bring the smaller meritorious cases that they are not currently bringing. Second, a new docket would probably decrease costs for all cases. Creation of a new docket would move some cases off of the current trial court dockets, allowing for quicker access to the courts for all claims, even the ones that stay at the trial court level.

Creating an expedited claims docket would not be expensive, as it could be added to the current role of the Justices of the Peace with no new courtrooms or judges being needed. However, some tactical issues must be considered. For example, what if a plaintiff certifies that he is seeking damages for under $100,000, but then is counter-sued by the defendant for $150,000? Or, what if during the discovery phase, the plaintiff unveils enough evidence to seek additional damages pushing him over the $100,000 threshold? In those and similar cases, there would have to be a provision in the statute that allows or forces a case from the expedited claims docket to the regular docket. In an opt-out or force-out situation, the statute must be conscientious of a deadline—such as X number of days before trial—to make sure that the law is fair to all parties and prevent any unfair surprise.

Statutory Causes of Action

Another potential reform is requiring that causes of action must come from statute. Under current Texas law, causes of action can come from statute or common law, or some combination of the two. This makes it very difficult to initially screen a frivolous lawsuit from a meritorious one. In addition, there is no certain understanding of what defendants can and cannot be sued for under the law. Making this small revision to the Texas Civil Practices and Remedies Code would bring certainty to litigation, ensuring meritorious claims are heard, and—if instituted in conjunction with FRCP 12 as outlined above—by guiding judges to determine which claims have merit and which claims do not.

Recommendations

- Amend Sec. 38.001 and 38.002 of the Civil Practices and Remedies Code (CPRC) to allow for recovery of attorney fees once an offer of settlement is made and rejected according to Chapter 42 of the CPRC.

- Amend Chapter 38 of the CPRC to allow defendants to opt-in to the loser-pays provision to any civil action in which a claimant has asserted a claim against the defendant. If the case is filed under a contingency fee arrangement, the opt-in provision should hold the plaintiff's attorney responsible as well. Otherwise, there is no incentive for a contingency fee attorney to refrain from filing abusive and frivolous lawsuits.

- Amend Sec. 51.105 of the CPRC regarding interlocutory appeals. The current law states that in order for interlocutory appeals to be heard, the parties must agree to the order. Because the non-appealing party will hardly ever agree, this provision should be changed to say that the appeal may happen upon the court of appeals' acceptance of the appeal.

- Create statutory language in the CPRC that is similar to FRCP 9 and FRCP 12. As previously explained, there is no true mechanism under Texas law for early dismissal of claims. Creating law similar to the Federal rules would allow Texas courts to dismiss frivolous lawsuits without first having to go through discovery and other costly legal actions.

- Create statutory language in the CPRC establishing an expedited docket for claims not less than $10,000 and not more than $100,000. The provision should allow the claimant to elect to be placed in the expedited docket to ensure that the claimant is not restricted on his ability to bring a claim as he desires.

- Amend Chapter 311 of the Government Code to ensure that Texas courts can no longer take claims based on implied causes of action. The language should say that "a statute may not be construed to create a cause of action unless a cause of action is created by clear and unambiguous language in the statute." Creating clear causes of action should eliminate many meritless claims from being filed.

Conclusion

A loser-pays statute would overcome high transaction costs and ensure that all tort plaintiffs with meritorious claims have access to the judicial system. Such a statute would decrease the cost of litigation and ensure that only meritorious claims are heard. Plaintiffs' attorneys would be disincentivized from bringing fraudulent and abusive lawsuits. Implementing a loser-pays system, along with the other procedural changes recommended in this paper, would reduce the high cost of litigation today and significantly improve access to the Texas courts. ✯

Endnotes

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About the Author

Ryan Brannan joined the Texas Public Policy Foundation's Center for Economic Freedom in 2009. Since joining the Foundation, he has written and worked on numerous regulatory issues, such as telecom, electricity, insurance, tort reform and property rights. Specifically Ryan has done work on net neutrality, broadband deployment, windstorm insurance, homeowner's insurance, eminent domain, regulatory takings, tort reform, renewable energy, smart meters, franchise fees, etc.

In addition, Ryan has several years of legal experience, working on corporate litigation matters including patents, copyright infringement and contract disputes. He has also worked in a Dallas medical-malpractice defense firm working on med-mal issues, hospital regulatory disputes, health care law and other forms of insurance defense.

Ryan established and served as Director of The Dallas Philanthropic Society, a 501(c)(3) non-profit. He also returned to school in the evenings to earn his M.B.A. from the Cox School of Business at Southern Methodist University, concentrating in Strategy and Entrepreneurship. At SMU, Ryan was a member of the Cox Leadership Forum and contributed to the SMU business plan competition.

He received his Juris Doctorate at the University of Oklahoma where he was a member of the American Indian Law Review, Dean's List, Dean's Counsel, and several trial teams including the National Trial Team. He received special recognition in advocacy and public service by receiving the Dean's Award for Advocacy and the Dean's award for Service, respectively. Ryan graduated with honors from Southern Methodist University with a Bachelor's in Political Science and minor in History.

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