The U.S. Legal System: Good at Some Things, Wretched at Others

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One thing President Obama won't talk about in his jobs speech Thursday is the deadening effect of litigation on the U.S. economy.

And maybe he's right to ignore it. Turns out the U.S. doesn't differ much from other industrialized countries when it comes to everyday litigation. The predictable and relatively efficient way courts resolve business matters like contract disputes is probably one of the most important factors in U.S. economic superiority.

It's the unique aspects of U.S. law — specifically, class actions and mass torts — that give the entire system a bad name. That's the conclusion of Harvard Law School's J. Mark Ramseyer and Eric Rasmusen of Indiana University in a paper I recently stumbled across. The paper, "Are Americans More Litigious?" is filled with the statistics tort-reformers love to trundle out. For example: U.S. courts handle about 5,800 lawsuits per 100,000 citizens each year, compared with 1,500 in Australia and 1,800 in Japan. There are 391 lawyers for every 100,000 citizens in the U.S., compared with 23 in Japan. And Americans pay $1,400 a year for car insurance, more than double the rate in Australia and Japan.

Ramseyer, an expert on Japanese law, and Rasmusen quickly deflate any idea these stats portray an out-of-control legal system. Japan has a tiny number of lawyers, but it also allows non-lawyers to handle many of the routine tasks like tax and real estate advice that U.S. lawyers zealously guard for themselves. Judged by the number of university graduates with some legal training, Japan beats the U.S. (And maybe that's a bad thing, according to this study of GDP growth vs. law students.) Americans pay a lot for car insurance, but they also drive more and get in more accidents. The U.S. death rate per car of 302 is triple Switzerland's and second only to Korea. Americans drive twice as far each year as Swedes.

When it comes to resolving contract disputes, the U.S. and other industrialized nations do a far better job than emerging economies. The typical contract dispute consumes about 300 days and 24% of the value at stake, the authors conclude, compared with 400 days and 50% in Sub-Saharan Africa.

Where the U.S. diverges from virtually every country is its treatment of mass torts and class actions, procedures the authors call "second order."

> In the typical accident or contract claim, U.S. courts do reasonably well. They may face somewhat more litigation than other rich democracies, but not much. In the second-order cases, however, the U.S. courts entertain claims that courts in other well-functioning economies would dismiss in short order. In the process, they necessarily create a drag on American business.

Relatively few countries even allow class actions (Brazil and Canada do, although few cases are filed) and the track record of jailed mass-tort and class action lawyers like Dickie Scruggs, Bill Lerach and Mel Weiss speaks to the deep corruption that is always lurking around this form of litigation.

> Given the trivial size of their claim, few victims pay attention to settlement bargaining. The defendant can take advantage of that by negotiating a settlement that is generous to the lawyers and stingy to his clients. The attorney agrees to take a generous fee, always in cash, and a much smaller recovery for his clients, often "in-kind" as free samples of the defendant's product.

The costs of all this are hard to calculate. But one study found that asbestos litigation consumed $9 billion in 2003. From 1998 to 2000, 10% of all asbestos cases were filed in two Mississippi counties. It's this concentrated firepower that can do great damage to the economy, the authors say. Judges should be more vigilant over abuses, they say, but they're conflicted too:

> Accustomed to an adversarial system in which they seldom take initiative, judges defer. They are busy people. They like to please at least some of the people in front of them. And they are linked by social interactions, gratitude for appointment (if by "merit panel"), the old school tie, or campaign contributions to attorneys, defense and plaintiff, not to citizens without J.D.'s. Too often, the important conflict is not between the plaintiff and the defense with the judge staying neutral, but between the lawyers and the non-professionals.

These are all the kind of comments that get me nastygrams, but this isn't me writing, it's two professors who have studied the economics of the law. One of them relates how he was approached by a securities class action lawyer when he was teaching at the University of Chicago. The stock of a Japanese company had fallen and the lawyer wanted to sue over company misstatements. "What did the firm misstate," Ramseyer asked. "We don't know," the associate answered. "That's why we want to retain you." It was enough that the stock price had fallen; the excuse to sue could always be found if they hired the right expert.