

**TESTIMONY OF
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On behalf of
The U.S. Chamber Institute for Legal Reform**

Before

**COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON THE CONSTITUTION**

**Regarding
H.R. 966, THE LAWSUIT ABUSE REDUCTION ACT OF 2011**

MARCH 11, 2011

Chairman Franks, Ranking Member Nadler, and members of the Subcommittee, thank you for inviting me today to share my views regarding H.R. 966, "The Lawsuit Abuse Reduction Act of 2011" (LARA). There is a dire need for its enactment now.

By way of background, I have been an active participant in the development of tort law since I served as law clerk to a federal judge in 1965. I was a professor of law and dean at the University of Cincinnati College of Law. I practiced law on behalf of injured persons for fourteen years. I also served at the U.S. Department of Commerce under both Presidents Ford and Carter, and chaired the Federal Inter-Agency Task Force on Insurance and Accident Compensation. For the past 30 years, I have been a defense lawyer. I have co-authored the most widely used torts casebook in the United States, *Prosser, Wade & Schwartz's Torts* (12th ed., 2010).

I have had a deep interest in improving our civil justice system. Today, I have the privilege to testify on behalf of the U.S. Chamber Institute for Legal Reform. I wish to make clear that the views I am expressing today are my own and based on my academic and practice experience.

The Problem of Frivolous Lawsuits

The expression, "death by a thousand cuts," fits the problem of frivolous lawsuits. Most frivolous lawsuits are not high-ticket items, but relatively modest. As Ms. Milito of the National Federation of Independent Business (NFIB) will share with you today, they are brought against small businesses including mom-and-pop stores, restaurants, schools, dry cleaners, and hotels. Let's take an example that occurred to one of my clients. The client, who runs a successful Irish pub, called me because a barrage of frivolous claims threatened her business. An individual alleged that the pub served him alcoholic beverages when he was already inebriated. The individual drove while

intoxicated and was involved in a serious automobile accident. He sued the Irish pub. Police records showed, however, while he had listed numerous bars that he visited and enjoyed, he omitted the Irish pub from the list.

Working with the pub's local lawyer, we were able to get the claim dismissed and have the plaintiff's lawyer pay the legal costs generated by the frivolous claim brought by his client. Those costs were several thousand dollars. At the time, the state had a strong rule against frivolous claims. Unfortunately, that good ending is unlikely to occur in federal court today under Rule 11 of the Federal Rules of Civil Procedure. It is weak and many view it as virtually toothless. It encourages participants to game the federal civil justice system.

So, what happens today when a small business is hit with a frivolous claim? The defendant contacts his or her insurer (assuming that the small business actually has coverage for the type of lawsuit it is facing). The insurance company's counsel calls the plaintiff's lawyer, and suggests that there is proof that the plaintiff was never at the client's establishment. The plaintiff's lawyer responds, "Well, I know there is a dispute about this, and I have asked for \$50,000, but I think we can settle this for about \$10,000." The plaintiff's lawyer realizes that the cost to the insurer of defending the case will be more than \$10,000.

The defendant's insurer is then placed in a dilemma. It will cost several thousand dollars to defend the case and still more to prepare a separate motion for sanctions if it is to seek recovery of attorneys' fees and costs resulting from the frivolous claim. If the judge allows the case to go to a jury, and the jury renders a verdict above policy limits, the insurer could potentially be subject to a claim by its insured for bad faith if it does not cover the full award. If the insurer, realizing the legal trap it is in, settles such a case

and similar cases, insurance costs will increase. Because there is currently no swift and sound sanction against frivolous claims, this “death by a thousand cuts” will continue. The result over time is potentially hundreds of millions of dollars of unnecessary costs to small business and our Nation’s economy.

Earlier versions of LARA were considered in the 109th Congress. But, our economy was in a much better place then as compared to now. Today, our economy is more fragile. The need for Congressional action to stop frivolous claims is greater. As President Barack Obama observed in his State of the Union on January 25, 2011, “I am willing to look at . . . ideas to bring down costs including reform to rein in frivolous lawsuits.”

While the President was speaking of medical malpractice, as Ms. Milito of NFIB will share with you today, the real rainstorm of frivolous claims consists of the low ball, legal extortion claims aimed against small business.

Why Rule 11 Does Not Work

Under the current version of Rule 11, an individual or business has no effective recourse when hit with a frivolous claim. By “frivolous,” I mean a claim that is (1) presented for an improper purpose, such as harassment; (2) is not warranted by existing law or a non-frivolous argument for extending, modifying, or reversing existing law or for establishing new law; (3) has no basis in fact and is not likely to have evidentiary support after a reasonable opportunity for further investigation or discovery; or (4) involves denials of factual contentions not warranted based on the evidence. LARA does not alter the definition of a frivolous claim. Rule 11 also imposes a basic obligation on attorneys and unrepresented parties to undertake a reasonable investigation of the facts and law underlying a claim before filing it. Unfortunately, in

practice, the current version of Rule 11 permits attorneys to file the lawsuit first and try to back up their claims with law and fact later. There are three reasons why Rule 11 is ineffective and discourages those who are hit with a frivolous claim from seeking recovery of attorneys' fees and costs.

First, under the current rule's "safe harbor," after the defendant's lawyer prepares a motion for Rule 11 sanctions, he or she must first share it with the plaintiff's lawyer before filing it with the court. This must be a separate motion, in addition to the motion needed to dismiss the claim. The plaintiff's lawyer then has 21 days to withdraw the lawsuit without any penalty. Therefore, filing the motion for sanctions under Rule 11 may serve to only further increase the costs for a defendant.

Second, even if the plaintiff does not withdraw the claim, and the court finds that it is indeed frivolous, sanctions are entirely discretionary. The court may opt not to impose any sanction at all other than dismissing the case.

Finally, the current version of Rule 11 discourages judges from imposing sanctions for the purpose of compensating the party unfairly hit with a frivolous claim for its attorney's fees and costs. The rule provides that Rule 11 sanctions are "limited to what suffices to deter repetition of the conduct or comparable conduct by others similarly situated." Thus, a court may decide to fine the violating party in an amount that is paid into the court, but which does not make the defendant whole.

In sum, today, those that are subject to frivolous lawsuits are in a situation where their only assurance in seeking sanctions is that they will incur even more defense costs with an unlikely chance of compensation for their legal expenses.

The Weakening of Rule 11: Unsound Policy Falling Between the Cracks of Correction

The present, ineffective version of Rule 11 is a result of action taken almost two decades ago by the Federal Rules Advisory Committee, an extension of the federal judiciary that has the primary responsibility to formulate the Federal Rules of Civil Procedure. The Advisory Committee recommended weakening the rule despite the result of a survey it conducted of federal court judges, those who deal with the problem of lawsuit abuse on a day-to-day basis. That survey found that 95% of judges believed that the prior version of Rule 11, which had strict penalties against frivolous claims, had an overall positive effect on practice and procedure and should not be changed.¹ Three-quarters of those judges surveyed felt that the former Rule 11's benefits in deterring frivolous lawsuits and compensating those victimized by such claims justified the use of judicial time involved in resolving such motions.² The Advisory Committee itself recognized that while there was some legitimate criticism of Rule 11's application, such criticism was "frequently exaggerated or premised on faulty assumptions."³ The Advisory Committee has made many sound decisions, but it did not do so when it revised Rule 11 in 1993.

There are in place so-called "systems for correction of mistakes" made by the Federal Rules Advisory Committee, but they did not work well when Rule 11 was changed. The first potential correction system occurs when the U.S. Supreme Court reviews the Advisory Committee decisions about rule changes. But when the weakened Rule 11 was transmitted by the Supreme Court to Congress for its

¹ Federal Judicial Center, Final Report on Rule 11 to the Advisory Committee on Civil Rules of the Judicial Conference of the United States, May 1991.

² See *id.*

consideration, Chief Justice Rehnquist included a telling disclaimer: “While the Court is satisfied that the required procedures have been observed, this transmittal does not necessarily indicate that the Court itself would have proposed these amendments in the form submitted.”⁴ Justice White warned that the Court’s role in reviewing proposed rules is extremely “limited” and that the Court routinely approved the Judicial Conference’s recommendations “without change and without careful study, as long as there is no suggestion that the committee system has not operated with integrity.”⁵ Justices Scalia and Thomas went even further and in almost unprecedented action, criticized the proposed amendment to Rule 11 as “render[ing] the Rule toothless by allowing judges to dispense with sanction, by disfavoring compensation for litigation expenses, and by a providing a 21-day ‘safe harbor’ [entitling] the party accused of a frivolous filing . . . to escape with no sanction at all.”⁶ Justice Scalia further noted:

In my view, those who file frivolous suits and pleadings, should have no ‘safe harbor.’ The Rules should be solicitous of the abused (the courts and the opposing party), and not of the abuser. Under the revised Rule [11], parties will be able to file thoughtless, reckless, and harassing pleadings, secure in the knowledge that they have nothing to lose: If objection is raised, they can retreat without penalty.⁷

The bottom line is that the Supreme Court corrective mechanism against unsound rule changes did not work in this instance.

**The Federal Rules Enabling Act:
The Place for Final Correction Did Not Work in this Instance**

³ *Amendments to Federal Rules of Civil Procedure and Forms*, 146 F.R.D. 401, 523 (1993).

⁴ *Id.* at 401 (1993) (transmittal letter).

⁵ *Id.* at 505 (Statement of White, J.).

⁶ *Id.* at 507-08 (Scalia, joined by Thomas, J.J., dissenting).

⁷ *Id.* at 508.

Through the Federal Rules Enabling Act of 1934, Congress created a system where it delegated its constitutional power to make rules for federal courts to the Judicial Conference of the United States. The Judicial Conference's Federal Rules Advisory Committee formulates the Federal Rules of Civil Procedure. It is clear that Congress has a Constitutional mandate to maintain the federal courts in Article 1, Section 8. It has the ultimate authority to design Federal Rules of Civil Procedures and change proposals about the rules from the Federal Rules Advisory Committee. In the mid-1970s, it did so with respect to the Federal Rules of Evidence.

But under this system, Congress only has seven months to make a "correction."⁸ Apart from matters of urgent immediate national concern, it is rare in 2011 that a bill can be passed by the Congress within seven months. Often, significant legislation that impacts the courts requires debate that can span one or more Congresses in order to reach consensus. Despite the introduction of legislation in both the House and Senate to delay the effective date of the proposed changes to Rule 11, time ran out before Congress could act and the revisions went into effect on December 1, 1993.⁹

Shortly after the revised Rule 11 took effect, Congress attempted to repeal the Federal Rules Advisory Committee's action to weaken Rule 11.¹⁰ By that time, some practitioners had already referred to the new Rule 11 as a "toothless tiger."¹¹ The

⁸ See 28 U.S.C. § 2074(a) (providing that the Supreme Court transmits to Congress proposed rules by May 1, and that such rules take effect no earlier than December 1 of that year unless otherwise provided by law).

⁹ See H.R. 2979 and S. 1382, 103rd Cong., 1st Sess. (1993).

¹⁰ *Attorney Accountability Act of 1995*, H.R. 988, § 4, 104th Cong, 1st Sess. (1995).

¹¹ See, e.g., Cynthia A. Leiferman, *The 1993 Rule 11 Amendments: The Transformation of the Venomous Viper into the Toothless Tiger*, 29 TORT & INS. L. J. (Spring 1994) (concluding that "[o]n balance, the changes made appear likely to undermine seriously the deterrent effect of the rule").

repeal passed the House.¹² Those opposing the bill, however, felt that there had not yet been adequate time to determine the effectiveness of the amended rule in practice.¹³

Again, it is now almost two decades since the Federal Rules Advisory Committee acted to weaken Rule 11, and the problem of frivolous claims has only increased. We know the consequences that flow from the weakening of the Rule. They are adverse to our economy, especially in 2011.

Since Rule 11 was weakened, frivolous claims have led to higher health costs, job losses, and an almost total failure of attorney accountability. As officers of the court, lawyers should be accountable to basic, fair standards: they should be sanctioned if they abuse the legal system with frivolous filings.

The Domino Effect of the Weakening of Rule 11: Many State Courts Followed the Fall

For reasons of public policy, mainly to discourage forum shopping, many states tend to change their court rules when the federal rules change. This occurred with respect to the weakening of Rule 11, even when judges disagreed with that unwise change. For example, an Advisory Committee note following a 2000 amendment of Minnesota Rule of Civil Procedure 11.01 states:

Rule 11 is amended to conform completely to the federal rule. While Rule 11 has worked fairly well in its current form . . . , the federal rules have been amended to create both procedural and substantive differences between state and federal court practices. . . . On balance, the Committee believes that the amendment of the Rule to conform to its federal counterpart makes the most sense, given this Committee's long-standing preference for minimizing the differences between state and federal practice unless compelling local interests or long-entrenched reliance on the state procedure makes changing a rule inappropriate.

¹² Rule No. 207, 104th Cong., 1st Sess. (Mar. 7, 1997) (passed by a recorded vote of 232-193). The Senate did not act on H.R. 988.

¹³ See H. Rep. No. 104-62, at 33 (dissenting views).

LARA can bring about welcome change by providing a model for state courts.

What H.R. 966 Does and Why it is Sound

Judiciary Committee Chair Lamar Smith of Texas has introduced a vitally needed bill that restores Rule 11 to its strength and purpose prior to the 1993 changes. The Lawsuit Abuse Reduction Act of 2011, H.R. 966, reverses the 1993 amendments that made sanctions discretionary rather than mandatory. It also eliminates the 21-day “safe harbor” that allows unscrupulous lawyers to game the system. Finally, LARA replaces language in the rule that discourages judges from making victims of lawsuit abuse whole with language that fully authorizes judges to order a party that brings a frivolous claim to pay the defendant’s attorney’s fees and costs.

H.R. 966 Addresses Past Concerns and Focuses Like a Laser on Frivolous Claims

When I last testified about this issue in 2004, a bill that I will call “old LARA,” raised several concerns from members of the full Committee.

First, there were questions about whether the bill could stifle legal developments in the area of civil rights. The drafters of the new LARA could not be clearer. It will not do so. The bill states a rule of construction, “Nothing in this Act shall be construed to bar or impede the assertion or development of new claims, defenses, or remedies under Federal, State, or local laws, including civil rights laws.”

Second, there were some members who raised federalism concerns that old LARA impeded states rights because it was to apply in state courts in cases involving “interstate commerce.” Regardless of the merits of such concerns, new LARA applies solely in federal courts. As noted earlier in my testimony, by tradition many states change their civil procedure rules in accord with changes in the federal rules, but such changes are purely voluntary.

Third, old LARA addressed forum shopping and limited where cases could be filed. This provision had merit, but out of deference to those Members who raised federalism concerns about this provision and those who also questioned its wisdom, the drafters of the new LARA removed that provision. The result is that the new LARA focuses like a laser on helping to abate the problem of costly, frivolous claims filed in the federal courts.

Four Incorrect Arguments Against LARA

There are four repeated incorrect arguments raised against LARA.

1. LARA Will Not Create Prolonged Satellite Litigation

The first argument is that LARA will create unwarranted and inefficient satellite litigation over whether a claim is frivolous. That is untrue.

While there will be some degree of litigation over the imposition of sanctions, this Subcommittee should consider the alternative. The alternative is a system in which an individual or business hit with a lawsuit that has no reasonable basis in law or fact does not have an effective means to recover thousands of dollars in defense costs to have the case dismissed and is forced to settle regardless of the merits. I submit that this is a far greater injustice than providing litigants with the opportunity to determine whether a filing is frivolous or not.

It is vital that Congress, in examining this issue, look at the total picture in terms of costs and benefits. The simple fact is that with stronger Rule 11 sanctions, there is substantially more risk involved in making a frivolous claim because a claimant cannot just withdraw the frivolous claim without consequence. This will produce an overall result of fewer frivolous lawsuits being attempted. Any increase in the level of satellite litigation over whether a claim is frivolous would impact only that subset of claims upon

which reasonable minds could differ. It is also important to appreciate that invoking Rule 11 is at the parties' discretion; they will not expend the time and cost to pursue such sanctions unless they truly believe sanctions are warranted. Therefore, the total effect would be to reduce wasteful litigation.

2. Sanctions Against Frivolous Claims Will Not Impede Justice

Some interest groups have argued that putting sanctions in place against frivolous claims will somehow impede justice and hurt the ordinary consumer. This is simply not true. If we look to the words of Rule 11 of the Federal Rules of Civil Procedure and congruent state rules, frivolous claims include those "presented for improper purpose" or to "harass or cause unnecessary delay or needless increase in the cost of litigation."¹⁴ They also include claims that lack a factual or evidentiary basis.¹⁵ But they do not include claims based on "nonfrivolous argument[s] for the extension, modification, or reversal of existing law or the establishment of new law."¹⁶ The very words of Rule 11 allow for growth of the law. H.R. 966 keeps the faith with respect to that public policy goal.

¹⁴ Fed. R. Civ. Proc. 11(b)(1).

¹⁵ *Id.* 11(b)(4).

¹⁶ *Id.* 11(b)(2). Some have argued that the manner in which judges implemented the pre-1993 version of Rule 11 disproportionately impacted civil rights plaintiffs. Even if this was initially the case, by 1988, a survey conducted by the Federal Judicial Center as well as other scholarship demonstrated that courts were construing Rule 11 more favorably to most litigants and practitioners, especially civil rights plaintiffs. See Carl Tobias, *Reconsidering Rule 11*, 46 U. MIAMI L. REV. 855, 860-61, 864-65 (1992) (citing Thomas Willging, Deputy Research Director of the Federal Judicial Center, Statement at Advisory Committee Meeting, Washington, D.C. (May 23, 1991); Elizabeth Wiggins et al., Rule 11: Final Report to Advisory Committee on Civil Rules of the Judicial Conference of the United States, § 1D, at 1 (Federal Judicial Ctr. 1991)). This led even some critics with "the general impression that Rule 11's implementation was not as problematic as many civil rights plaintiffs and attorneys had contended." Tobias, *supra*, at 864-65.

3. The “Bring Me More Data” Argument

Perhaps, the most virulent argument against LARA has focused on data. “Bring me data that shows millions of frivolous claims” and maybe I will vote for LARA. I call that the “bucket of steam” argument. Bring me a bucket of steam and I will support the bill. It simply cannot be done. This is why.

As every small business knows, frivolous claims begin with a demand letter. “My client fell in your restaurant. He was seriously injured . . . ,” and so it goes. The small business gives this letter to his or her insurer. As I have indicated, the insurer often settles the baseless claim because going to court will cost more than the ultimate demand. There is no practical way to keep track of the number of these demand letters or an easy way to place legal sanctions against baseless demand letters. Demand letters are the rattlesnake’s nest of frivolous claims. You can hear them rattle, but you do not see them in court. A strong Rule 11 will limit this sort of practice because everyone will then know that the threat of a frivolous lawsuit is just a baseless threat. In other words, the lawyer will be disinclined to follow through on the demand letter and file such a lawsuit.

Some federal judges may also share with you that they rarely see a frivolous claim in their courts and understandably so. Not only do many such cases settle before a case is even filed, as I have discussed with you, the current Rule 11’s “safe harbor” allows the plaintiff’s attorney to withdraw the claim before it is ever considered in court.

A wise Member of Congress once said to me, “when an issue arises about small business, I do not turn to data, I turn to my small business constituents. If they say it’s a problem, I regard it as a problem.” As Ms. Milito of NFIB will tell you, and as I believe

your small business constituents, will tell you, there is a need for strong and reliable sanctions against those who bring frivolous claims.

4. The “LARA Just Helps Business” Argument

The final argument against LARA is that it just benefits business. Benefits to business are not a bad thing, especially in our current economy, but LARA will not benefit business alone. It applies to all parties to a lawsuit and sanctions both frivolous defenses as well as frivolous claims. It applies to individuals in your districts who were forced to hire a lawyer to defend against a frivolous lawsuits and who had almost no chance of recovering the thousands of dollars in attorneys’ fees and court costs likely spent to have the claim dismissed.

* * *

Mr. Chairman, in sum, as part of our national effort to promote our economy, jobs, eliminate needless wasteful costs, and restore very basic fairness to stop lawsuit abuse, LARA needs to be enacted now. Thank you again for inviting me to testify today and I look forward to answering any questions that the Subcommittee members may have.