



Making the FAIR Act Fair

By Ted Frank

Welcome, reader! The AEI Liability Project hereby inaugurates its Liability Outlook series, designed to guarantee a paper trail to exclude any of its authors from Article III appointments. This Outlook examines the congressional attempts at asbestos liability reform. The eventual cost of asbestos litigation is estimated in the hundreds of billions of dollars, the majority of which will end up in the hands of attorneys, thus affecting thousands of corporate defendants with little or no culpability and costing tens of thousands of jobs. The trust-fund approach is a congressional attempt to reach a compromise on the liability problem, so long as nationwide reform is not politically feasible. While a trust fund has the potential to save tens of billions of dollars, the current legislation suffers from dangerous flaws that could make the cost of the asbestos litigation crisis far worse.

A funny thing happened in Georgia. On April 12, 2005, Republican governor Sonny Perdue signed a law requiring an asbestos plaintiff to present “prima facie evidence of physical impairment” from a qualified physician that shows “to a reasonable degree of certainty” that exposure to asbestos was “a substantial contributing factor” to his injuries.¹ And, amazingly, out of thousands of asbestos cases that were pending in the state, only a small fraction was able to meet this minimal standard. Trial lawyers in Georgia will tie up the reform for a few years, challenging the constitutionality of the law in front of a more pliable judicial branch there. Meanwhile, the gigantic asbestos litigation mess proceeds in the vast majority of states that have not passed reform at all, with the plaintiffs’ bar picking up stakes and bringing cases in new jurisdictions when even the most corrupt jurisdictions tire of their presence and kick tenuous cases out.

The proposed Fairness in Asbestos Injury Resolution (FAIR) Act, S. 852, would take asbestos cases out of the judicial system and move them into a Department of Labor–administered \$140-billion trust fund, paid for with assessments on businesses and insurance companies. It is no surprise that plaintiffs’ attorneys (and a series of

front groups for the plaintiffs’ bar) oppose the FAIR Act. By capping fees at 5 percent of recovery instead of the typical 40 percent, the FAIR Act would deprive attorneys of tens of billions of dollars. By imposing medical criteria, the bill has the potential to end the scandal of assembly-line medical diagnoses fraudulently rubber-stamping attorneys’ findings of asbestos injury. Surprisingly, numerous corporations and insurers oppose the FAIR Act, despite supposedly being its intended beneficiaries. This corporate opposition is not the result of mass irrationality; many corporate defendants will be worse off by the current formulas in the bill, and even worse, the bill in its current form suffers from potentially disastrous flaws that could affect taxpayers. This is unfortunate, because real liability reform is needed on this issue.

The FAIR Act was stalled temporarily by a 58 to 41 vote in the Senate that failed to reach the three-fifths majority needed to proceed over a budgetary point of order, thus sending the bill back to committee. But this procedural vote will not necessarily kill the bill. The vote was originally 59 to 40, but at the last minute, senator majority leader Bill Frist changed his yes vote to no, presumably to set up a later vote to reconsider—a motion that can only be made by a senator who voted on the winning side of the original motion.

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The absent hundredth senator, Daniel Inouye (D-Hawaii), was out of town, and would have been the critical sixtieth yes vote. The bill is thus likely to return to the floor in March.

There is no question that asbestos litigation in the United States represents a crisis. In the 1980s, there was concern that it would cost a “disastrous” \$8 billion. It turns out that those fearmongers underestimated the imagination of Trial Lawyers, Inc., which has expanded liability across multiple dimensions: by increasing the number of claimants who could expect to collect, eliminating proximate causation in assessing liability, and augmenting the size of damages awards. The cost to date is over \$70 billion, with no signs of dissipating, and over half of that sum pays for lawyers and legal expenses.

A Sorry History

Although asbestos use all but ceased by the early 1970s—and although asbestosis was called a “disappearing disease” in 1988—trial lawyers have filed hundreds of thousands of new claims in the last decade. As Lester Brickman, a professor at Cardozo Law School at Yeshiva University, has documented, the majority of these plaintiffs have suffered no impairment; the majority of the defendants they sued did not produce products to which they had substantial exposure.² According to a study by the RAND Institute there have been dozens of asbestos-related bankruptcies, the majority of which have taken place in the last five years; another study identifies tens of thousands of lost jobs.³ As the original manufacturers of asbestos went bankrupt, plaintiffs’ attorneys have greatly expanded the penumbra of liability to include companies that happened to have asbestos present in the workplace or manufactured asbestos-containing products. Over 8,000 companies in over 90 percent of American industries have been sued for asbestos-related claims.

A good example of one such defendant is Peerless Pump Co., which, according to a recent *Indianapolis Star* story about the local company, has been sued in thousands of cases across the country.⁴ Peerless’s only connection to asbestos is that one of its water-pump products was made with a part that contained asbestos. The pump would have to be taken apart to expose the asbestos-containing part within, and even then, the likelihood of someone getting ill from the minute

exposure would be infinitesimal. Nevertheless, Peerless, which characterizes itself as one of asbestos manufacturers’ “customers’ customers’ customers,” has spent more than its entire profits over the last three years defending itself in court.

Liability has also expanded along the dimension of verdict size. U.S. Steel made the mistake of seeking to defend itself in one mesothelioma lawsuit in the trial bar mecca of Madison County, Illinois, in 2003, brought by one of its former employees, Roby Whittington. A plaintiff-friendly judge refused to apply the relevant Indiana state law that would have held that the claim belonged in the workers’ compensation system, refused to allow U.S. Steel to introduce evidence of the safety precautions workers in its plants took, and refused to allow U.S. Steel to introduce evidence that Whittington was exposed to substantially more asbestos in other jobs and from other sources. The result was a verdict for \$250 million, including \$200 million in punitive damages; U.S. Steel settled rather than risk the 9 percent interest prescribed by law waiting for vindication on the appeal.

Courts’ attempts to create shortcuts for asbestos claims and to clear their dockets by reducing procedural protections for defendants had the opposite effect, opening the floodgates for claims that had no merit. For example, West Virginia courts tried to solve their problems in one fell swoop with a flagrantly unconstitutional mass trial consolidating the mostly unrelated claims of over 8,000 plaintiffs against 250 defendants, hoping to force defendants to settle. True, as numerous scholars and judges have noted for decades, the risk of an all-or-nothing verdict creates enormous settlement pressure for a defendant to pay de facto blackmail for even meritless claims. But any benefit in reduced dockets from forcing unfair settlements was obviated by attracting more plaintiffs to sue in such a favorable environment.

A federal court hearing in Corpus Christi revealed how plaintiffs’ lawyers may be fraudulently conspiring with corrupt doctors to claim miscellaneous pulmonary disease as asbestos-related. An investigation matching plaintiffs in a multidistrict litigation against silica defendants against claimants from the Manville Trust found that thousands of the plaintiffs claiming silicosis injuries had previously claimed asbestosis and that the asbestosis claims made no mention of the alleged silicosis and vice versa, even though the two competing diagnoses were sometimes made by the same doctor.

Doctors who were revealed to have “manufactured” diagnoses for profit in the silicosis cases at the rate of hundreds of diagnoses a day were also providing the main evidence for asbestos “injury” in hundreds of thousands of cases.

Still unknown is the full scope of subornation of witness perjury in asbestos litigation. Defense attorneys would marvel at plaintiffs who had trouble remembering other events of decades past, but who could perfectly recall the details of working with individual asbestos-containing products and were quite confident that they were produced by solvent—rather than insolvent or settling—defendants. Some minor manufacturers complain that many more plaintiffs are claiming exposure to their product than could have possibly been affected. One clue came when a prominent asbestos firm, Baron & Budd, inadvertently disclosed to an opposing law firm a memorandum coaching witnesses how to testify about their experiences with products. (Examples: “Unless your Baron & Budd attorney tells you otherwise, testify ONLY about INSTALLATION of NEW asbestos material, NOT tear-out of the OLD stuff” and “You may be asked how you are able to recall so many product names. The best answer is to say that you recall seeing the names on the containers or on the product itself.”⁵) The firm was able to shut down an investigation of the memo, and the Texas state judge who had the temerity to suggest wrongdoing was defeated in a reelection campaign by an opponent with the sizable financial support of the plaintiffs’ bar. (Name partner Fred Baron, who in 2002 promised a “jihad” against politicians who supported liability reform, went on to be the finance chair of John Edwards’s presidential campaign and co-chair of the Kerry Victory ’04 Committee.)

What Is Feasible Politically?

The plainest solution is to shut down the shenanigans that have expanded the scope of the asbestos crisis well beyond any conceivably responsible parties. H.R. 1957, the Asbestos Compensation Fairness Act of 2005, introduced by representative Chris Cannon (R-Utah), adopts measures similar to those proposed in state reforms in Texas. The Asbestos Compensation Fairness Act of 2005 would move cases to federal court, impose stringent medical criteria before suit could be brought, and limit liability to proportionate responsibility, with limits on noneconomic and punitive damages. It is no betrayal of

federalism principles to take cases out of state courts that are unfriendly to out-of-state corporate defendants and move them to federal courts with stricter evidentiary rules; indeed, such a rule is precisely what Alexander Hamilton proposed in *Federalist* no. 80.

Senator John Cornyn (R-Tex.) proposed an amendment to the FAIR Act that would replace its trust-fund approach with the methodology of H.R. 1957. But there was strong opposition. Senator Patrick Leahy (D-Vt.), who cosponsored the FAIR Act, objected to the Cornyn approach, noting that many asbestos victims would end up without compensation because they were employees of firms that went bankrupt. It is hard to establish public-policy grounds as to why this should make any difference. After all, in most cases, we do not allow victims of crimes by judgment-proof criminals to collect from innocent bystanders; millions of people suffer from cancer without any evident fault and make do without multimillion-dollar compensation. Sometimes losses simply fall where they do, without compensation. And if we are to compensate people for asbestos injury (including, as the current FAIR Act does, injury from “naturally occurring” asbestos) but not other injury, why require random businesses such as Peerless to suffer the consequences, while other taxpayers share none of the burden? Nevertheless, there does not appear to be the political willpower to implement either of these hard facts: Cornyn’s proposed amendment was tabled by a 70 to 27 vote, and it would almost certainly be filibustered by the Democrats if it were to return to the floor in its current form.

So the question becomes not only what is desirable in asbestos reform, but what is politically feasible.

The trust-fund approach attempted to thread that needle. Estimates of the future cost of asbestos litigation range from \$150 billion to \$200 billion, though previous estimates of decades past have failed to account for the creativity of the plaintiffs’ bar and the malleability of the bench in expanding liability. The RAND Institute estimates that only 42 percent of the expenses of asbestos litigation go to victims and ostensible victims.⁶ This suggests that a trust-fund approach that caps attorneys’ fees at 5 percent and has administrative expenses of another 3 percent could save \$75 billion to \$100 billion of dead-weight loss that would otherwise go mostly into attorneys’ pockets. (Senator Harry Reid’s [D-Nev.] attack on the bill as a creature of lobbyists is thus ironic, given the multimillion-dollar

lobbying campaign launched against the bill by its trial-attorney opponents.) And that is even before accounting for the savings from the trust fund's medical criteria preventing uninjured claimants from recovery or the benefits other participants in the judicial system would get from removing what the Supreme Court called an "elephantine mass of asbestos cases"⁷ from crowded dockets.

The savings the trust-fund approach could create have been misinterpreted. For example, in bankruptcy court, USG recently sought to resolve its asbestos liabilities with a contingent settlement: \$900 million up front, and a \$3.05 billion note contingent upon the failure of the asbestos trust-fund bill to pass this year. Trust fund opponents such as Public Citizen immediately portrayed the settlement as evidence that the bill was a corporate bailout. But the attacks misrepresented the difference in cash flows under the status quo and under the FAIR Act. Under the status quo, USG would pay \$4 billion, plaintiffs' attorneys would skim about \$1.5 billion from that sum, and USG would be reimbursed in part by insurance companies. Under the FAIR Act, USG would pay \$900 million into the trust fund, USG's insurers would contribute between \$1 billion and \$2 billion in additional moneys to the trust fund on USG's behalf, and asbestos victims would get the lion's share of the amount. The \$3 billion difference can be accounted for almost entirely by the difference in attorneys' fees and the difference between direct and indirect payments by insurers, rather than from payouts to victims.

Nevertheless, there is substantial opposition to the bill from many in the corporate community who would be called to contribute to the trust fund. While some in the media have portrayed this as small companies opposing a bill that benefits larger companies, the opponents count Liberty Mutual and ExxonMobil among their numbers.

There are certainly legitimate problems with the FAIR Act as currently constituted. The medical criteria of Section 121 are too lax or vague in many instances and open up the bill for potential abuse. The bill contemplates allowing certain cases to "leak" back into the court system and will be subject to manipulation by plaintiffs' lawyers to maximize that leakage. A provision for the automatic payment of claims that the Department of Labor fails to resolve after 180 days is also a potential blank check for abuse: the recent multiyear

backlog of immigration cases created during the transformation of the Immigration and Naturalization Service into the U.S. Citizenship and Immigration Services shows that a new federal bureaucracy will not be well situated to handle new claims from the get-go. To attract the votes of Montana senators, exceptions of questionable scientific validity were written into the bill for residents of Libby, where an asbestos mine was located. If the fund unravels for constitutional reasons or otherwise—including lack of funding—then asbestos cases are thrown back into the litigation system and it is unclear whether participants will not be made worse off than if there was no fund at all.

There are other dangers of a trust fund. Once it is in place, political pressures will exert upwardly to expand the medical criteria; as programs such as Social Security and disability have shown, there is rarely the political willpower to shrink a government benefit program.

Patrick Hanlon, speaking in favor of the trust-fund approach at an AEI event,⁸ argued that fears of the trust fund being underfunded are overstated. If estimates of the trust fund becoming insolvent are to be believed, he argues, businesses that support the trust fund would have the worst of both worlds. Are those companies closest to the asbestos disaster really acting against their self-interest by underestimating the demands that would be made against the trust fund? The argument is too clever. Numerous companies will be bankrupted by the status quo; even if the trust fund had only a 10 percent chance of success, these companies would be better off with the long-shot risk, because they (unlike many other players) will be made no worse off by the failure of the approach. In short, the American taxpayer's interest does not correspond directly to that of building products manufacturers threatened with bankruptcy.

Ideally, one would see meaningful reform, like that proposed by Cornyn and Cannon, such that innocent defendants would no longer be held hostage to the deep-pockets search by hundreds of thousands of plaintiffs. Unfortunately, the litigation lobby has such a lock on the minority party that it seems unlikely that Cornyn and his allies can obtain the supermajority in the Senate needed to pass true Texas-style reform. While Reid and Richard J. Durbin (D-Ill.), who normally carry water for the trial bar, expressed a willingness to cooperate with Cornyn in creating an alternative to the trust-fund approach, one fears that they are doing so disingenuously, to either pass a minor reform that ends political momentum to solve the

asbestos problem but fails to make more than a dent in the status quo, or to peel off enough conservative votes to kill the trust-fund approach entirely. And every term that ends without meaningful asbestos reform means several billion dollars more are transferred from American consumers and asbestos victims into the trial bar's pockets.

A well-designed trust fund is hypothetically capable of saving \$75–\$100 billion in the here and now by replacing the huge costs of attorneys in asbestos litigation with a more efficient administrative process. There is something terribly wrong with the sausage-making of legislation if that surplus cannot be divided among victims, insurers, and corporate victims of asbestos litigation, such that all find it in their economic self-interest to support it. The fact that small companies like Peerless Pump—companies that are victimized most unfairly by the predations of the asbestos trial bar—oppose the FAIR Act in its current form should be of tremendous concern to those seeking a comprehensive solution to the asbestos crisis. A monumental effort is needed to fix the problems in the FAIR Act; the returns from such fixes could be enormous, but without them, the current version of the act makes a bad situation even worse.

Research assistant Philip Wallach and AEI editorial assistant Nicole Passan worked with Mr. Frank to edit and produce this Liability Outlook.

Notes

1. Georgia Code, 05 HB 416, title 51, chap. 14, sec. 5(a)(1) and 2(15)(A), available at www.legis.state.ga.us/cgi-bin/gl_codes_detail.pl?code=51-14-5 and www.legis.state.ga.us/cgi-bin/gl_codes_detail.pl?code=51-14-2.
2. Lester Brickman, "On the Theory Class's Theories of Asbestos Litigation: The Disconnect Between Scholarship and Reality," 31 *Pepperdine Law Review* 33 (2004).
3. Stephen J. Carroll et al., *Asbestos Litigation Costs and Compensation* (Santa Monica, Calif.: RAND, May 2005); Joseph E. Stiglitz et al., *The Impact of Asbestos Liabilities on Workers in Bankrupt Firms* (Washington, D.C.: Sebago Associates, December 2002).
4. Maureen Groppe, "Industry, Victims, Congress at Odds over Asbestos Claims," *Indianapolis Star*, February 19, 2006.
5. "Baron Budd Asbestos Memo," Documents in the News, AEI Liability Project, available at www.aei.org/research/liability/subjectAreas/pageID.1006,projectID.23/default.asp.
6. Stephen J. Carroll et al., *Asbestos Litigation Costs and Compensation*.
7. *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 821 (1999).
8. Patrick Hanlon, "Will the FAIR Act Fix the Asbestos Mess?" (panel discussion, American Enterprise Institute, Washington, D.C., January 19, 2006), available at www.aei.org/event1234.