

The Mounting Assault By Trial Lawyers, Inc.

CEOS MUST HELP DRAIN THE LITIGATION SWAMP. BY STEVEN B. HANTLER

The risks posed by an out-of-control civil justice system are mounting. Managing these risks is no longer a peripheral function for a CEO. After all, the tort process can distort every aspect of a company's business. Like any corporate counsel in an industry perceived as having "deep pockets," I am at the eye of this storm.

The stakes have increased because the trial bar—dubbed "Trial Lawyers, Inc.," by The Manhattan Institute—no longer tries lawsuits only before juries. Lawsuits are now tried before shareholders and customers in the court of public opinion. This is a much more sophisticated—and dangerous—game. In fact, Trial Lawyers, Inc., now conducts briefings for financial analysts on its litigation portfolios against companies. Why? It seeks to drive those companies to the settlement table or risk losing share value. Many of these lawsuits are filed in venues so inhospitable to business defendants that the American Tort Reform Association dubs them "judicial hellholes." These are the places where, one of the most successful plaintiff's lawyers in the country conceded, "it's almost impossible to get a fair trial if you're a defendant."

There are three ways in which lawsuits abuse can affect a business at its core.

Shareholder Value: Consider the case of Bayer, whose stock price lost 25 percent of its value in the first few days of a trial in a Texas courtroom last year. "Your stock price is going in the tank," the plaintiffs' attorney reportedly whispered to the Bayer counsel. Of such tactics, George Priest of Yale Law School writes, "It's the fear of the nuclear-bomb verdict that gives leverage to plaintiffs' lawyers to make threats and play off a company's stock price." When the threat of

lawsuits caused health maintenance organizations to lose \$12 billion in stock value in a single day, Richard Scruggs—the "king of tobacco" torts—actually participated in a conference call with institutional investors on the exposure of HMOs. Former U.S. Attorney General Richard Thornburgh has noted that plaintiffs' attorneys first threaten a lawsuit, "then use the legal system to coerce the beleaguered company into a large settlement."

Cost Structure: Some industries, such as



pharmaceuticals, are seeing five-fold increases in their insurance premiums for product liability. Companies also have had to salt away hundreds of millions of dollars in reserve just to handle legal expenses. These reserves are necessary because if tort costs continue to escalate, today's insurance coverage cannot possibly cover the actual costs of lawsuits brought a decade from now.

The greatest cost of all, however, is the distortion of a company's willingness to innovate and bring new products to mar-

ket. When legal concerns can seriously affect—or even put on hold—an R&D effort, a company's very business model is at stake.

Brand Equity: Research shows that as much as 96 percent of a company's stock market valuation is determined by that company's brand value. In today's legal environment, plaintiffs' lawyers are given considerable latitude to besmirch any brand for virtually any claim (witness the dozens of companies that never manufactured asbestos, but were nevertheless bankrupted by asbestos verdicts).

The filing of a suit allows trial lawyers to level outrageous and unfounded charges that would be libel-bait in any other forum. Do unproven charges matter? A 2002 survey by AcuPoll Precision Research found that 68 percent of consumers said they are less likely to trust brands when they hear of corporate malfeasance. Take note—all they need is to "hear" of such allegations.

CEOs should rightly be concerned about the litigation environment. The risks can be reduced by common sense legal reforms that fairly balance the interests of consumers and producers. This requires greater CEO participation in public policy. Only when CEOs lend their prestige to legal reform will we begin to see policymakers get serious about draining this swamp.

Internally, CEOs also need to establish a separate budget for legal reform, typically the first item in general counsel budgets to get squeezed out. But the legal reform budget must be protected because it is proactive—if successful, legal reform will avoid or lessen the impact of the next lawsuit. ▲

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