

## New and emerging challenges to manufacturers and insurers in evaluating trial versus settlement | BY KENNETH R. LANG AND AMY M. DECKER

The classic evaluation of any product liability lawsuit to determine settlement value used to turn upon the amount of verifiable damages compared to the cost of defending the case. That analysis provided for both downside exposure and a litigation budget. The expansion of product liability throughout the last quarter of the twentieth century necessitated the refinement of that methodology to include a more in-depth analysis. Ultimately, the principal factors in evaluation of the 'risk' associated with the lawsuit became: (i) assessment of liability or fault; (ii) analysis of damages, including known or economic damages and non-economic damages, such as loss of life-style, pain and suffering, and punitive damages; (iii) exposure to adverse verdicts given the nature of claims and venue; and (iv) the costs of defending the case through trial.

This article first provides an overview of the elements of the classic risk analysis, which remains the accepted model for advising manufacturers in product liability claims and lawsuits. Next, the article addresses new and emerging factors manufacturers must consider in analysing the risks of trial versus settlement. Those new factors have emerged through the various supplier/vendor agreements required by mass retailers, which often expose manufacturers to expanded liability through the defence and indemnity provisions of those agreements. Finally, the authors suggest possible approaches to addressing these new factors and propose a model for risk evaluation into the future.

### Classic model

Any evaluation of liability for a death or injury allegedly caused by a manufacturer's product begins with investigating the accident scenario. That process allows the manufacturer to: (i) verify the product is indeed its product; (ii) inspect the accident site and gather facts either indicating the product's involvement or discovering other potential causes

of the accident; (iii) gain insight into the claimant's theory of how the accident occurred; and (iv) obtain and review official incident reports, among other fact-finding activities. This information is fundamental to evaluating the product's involvement, if any, in the incident and becomes crucial to the analysis of potential liability.

A claim or lawsuit is frequently preceded by contact from someone representing the injured or aggrieved party. Often that correspondence includes a statement of claimed damages, which may be itemised by economic losses and non-economic factors. It usually includes a statement, or more characteristically an 'over-statement', of the amount required to make the injured or aggrieved 'whole'. Generally, the itemised amounts are greatly exaggerated and the 'discount' settlement demand likewise is inflated. Therefore, the manufacturer's counsel must evaluate the damage elements, considering the venue and known and reported verdicts and settlements to give perspective to a reasonable amount, assuming liability could be established at 100 percent against the manufacturer. Then, the damage analysis is weighed with liability, exposure and venue factors.

Evaluation of exposure to a potential adverse verdict, while definitely not a precise science, is essential for advising the manufacturer whether to defend the action or to work towards an early amicable resolution. It is essential to research the history of verdicts (large or small) in the specific venue where the lawsuit will be filed. There may be many potential defendants or the manufacturer, and likely the retailer, may be the only defendants. The experience of opposing counsel bringing the lawsuit is also a consideration. Through consideration of liability percentage based on the likelihood the product was at fault versus possible fault of other actual or potential parties, including the claimant, exposure establishes a bottom line for defence or settlement. All of this must be considered in light of the particular venue's product liability laws.

It is impractical, if not impossible, for any manufacturer to make a reasoned decision of whether to settle or try any lawsuit without knowing the economics of the options, i.e., costs. In order to fairly compare exposure to costs, a manufacturer will seek its counsels' estimation of the major costs, such as projected legal and expert fees, depositions and other discovery, inspections, etc. Although not a precise calculation at the initial stages, such an estimation, based on counsels' prior experience, provides a ballpark figure for the manufacturer to make a reasoned business decision about how to proceed.

### New and emerging factors

Manufacturers have successfully applied the classic risk analysis, with some variation, for several decades. In the last two decades of the twentieth century, consumer product retailers began to require manufacturers to defend and indemnify them when demands 'arising from the sale or use' of the subject product were made upon the retailers. Reputable and responsible manufacturers were willing to oblige and stand behind their products through the products' purchase and use by consumers. For manufacturers who had insurance for product liability claims and

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lawsuits, their insurers were equally responsive to such demands. None of those demands by retailers required a shift from the classic risk evaluation described. For their part, retailers cooperated by providing information concerning the product's sale and its purchaser, if possible. They were aided in some jurisdictions by legislation exonerating them from liability arising solely from the sale of the product in question, provided they had not altered or changed the packaging of the product.

Recently, the sheer volume of business conducted by major consumer product manufacturers with extremely large retailers has changed the landscape for risk analysis in product liability claims. The new 'risk' to consider is the loss of large revenue streams from those retailers. The classic model is still viable, but not conclusive. The new factor has become the retailer's demand for defence and indemnity for any claim allegedly involving the manufacturer's product, regardless of whether the retailer's independent acts are claimed to be causative. In other words, the retailers seek indemnification for their own negligence or, in some cases, their own products.

The potential for assuming defences and indemnifying retailers for their own actions affects the 'exposure' evaluation in at least two respects. First, the manufacturer must consider whether the assumed liability is an insured event. Many, if not most, policies written at primary and excess levels for manufacturers do not cover the negligent or claimed negligent acts of third parties. Accordingly, the manufacturer must assess: (i) the percentage of fault that may be attributed to the retailer's independent acts; (ii) the likelihood those acts could 'trigger' punitive damages; and (iii) the retailer's cooperation in defending those claims. Second, the business the manufacturer enjoys with the retailer must be re-evaluated. This means involving representatives of the manufacturer's marketing, sales, and accounting departments and likely

the highest levels of the executive structure as part of the evaluation discussions. Additional, new considerations would include the number of expected assumptions of liability over time and attempts to place a value on those liabilities. Finally, all of this must be evaluated not only on the volume and amount of revenue generated by the retailer, but also the profitability of those sales by the manufacturer.

**A proposed model for the future**

When faced with the foregoing scenario, product manufacturers may wish to consider the following model for claim and product risk analysis: (i) analyse the risk initially under the classic model; (ii) determine whether the tendered claims are covered events under the manufacturer's insurance policy; (iii) commence a dialogue immediately with high levels of management in areas of finance, risk, marketing, sales and perhaps strategic planning; (iv) evaluate the 'risk of refusal' by considering the short-term and long-term economic effects and damage to the existing business relationship between manufacturer and retailer by refusing the demand of defence and indemnity for the retailer's independent acts, while accepting the defence of actions arising from the product itself; (v) determine what middle ground may exist to preserve the business relationship and insulate the manufacturer from uninsured losses resulting from acceptance; and (vi) encourage face-to-face discussions between manufacturer and retailer to attempt amicable resolution between them while maintaining a reasonable approach to defending the claim. ■

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