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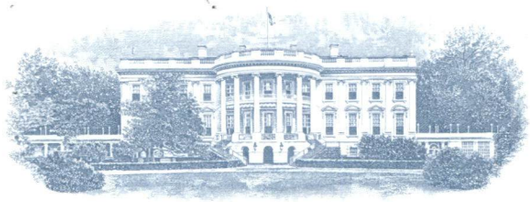
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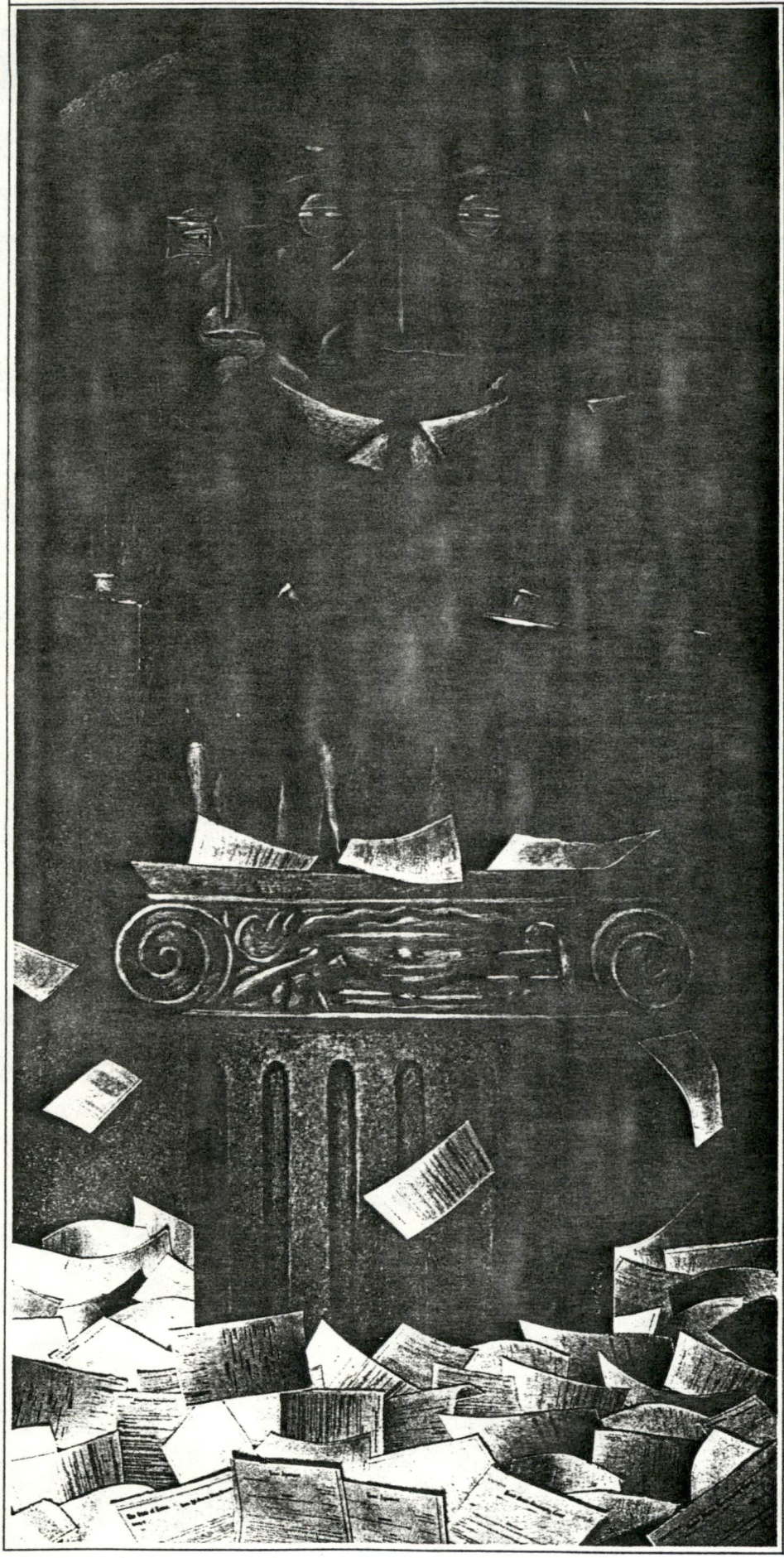
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TOM CURRY

GUI

Being a lawyer at Motorola Inc. is tough these days. While attorneys at other companies might churn out lawsuits against customers or suppliers with the push of a button, Motorola's 100 in-house lawyers must seek all possible alternatives to landing in court: arbitration, mediation, even private judges who settle disputes for a fee. After all this, Motorola lawyers who still want to go to trial must fill out a form estimating legal costs, likely damages, and chances of victory. "The form is so onerous that they gladly work out an alternative settlement rather than screw around with that form," says General Counsel Richard H. Weise, the architect of Motorola's resolution program.

If that sounds like an unproductive use of an attorney's time, think again. Since starting the program in 1984, alternative dispute-resolution techniques have slashed Motorola's litigation costs by as much as 75%. "It's that dramatic an impact," Weise says.

'LOST OPPORTUNITY.' Motorola's obsession with finding new ways to settle disputes isn't typical. But it is rapidly becoming so. After years of mounting frustration, disdain for the U. S. legal system is now so intense that corporations are taking the law into their own hands. From General Mills to General Motors, companies are fighting their battles privately, through such innovative techniques as rent-a-judge services and minitrials. Pacific Gas & Electric Co. even pays for its opponents to sit down with a mediator. "What's worse than the money wasted on the court system is the lost opportunity to find solutions," says Howard V. Golub, PG&E's general counsel. "Our energies should not be spent on recreational litigation."

The legal revolt among corporations is only one facet in an unprecedented rethinking of the U. S. civil justice system. Every branch of government is pushing some package of legal reform. Congress is overseeing "advisory committees" in every federal court to try to speed up cases and cut costs. Judges are overhauling the federal rules of civil proce-

LTY! TOO MANY LAWYERS AND TOO MUCH LITIGATION. HERE'S A BETTER WAY

dure. Even the White House is responding to the business backlash. Through the President's Council on Competitiveness, the Bush Administration is promoting an array of probusiness reforms, including such controversial measures as forcing losers to pay the victors' legal bills. The debate has inflamed the passions of everyone from defense lawyer Alan Dershowitz to legal scholars such as RAND researcher Deborah Hensler to lawyer and best-selling author Scott Turow.

Even the tort system, where injured parties sue for damages, stands a better chance of being reined in. Congress is again mulling a uniform product-liability law to replace the patchwork of state laws and make it tougher for plaintiffs to win damages. States are tightening up on punitive damages and pain-and-suffering awards. And they're finding faster and cheaper ways to resolve medical malpractice suits, such as by compensating injured patients regardless of whether the doctor is at fault. "There's a very strong popular revolt over excessive lawyering, excessive delays, and excessive costs," says Martin F. Connor, president of the American Tort Reform Assn. "When you add it all up, it's impressive."

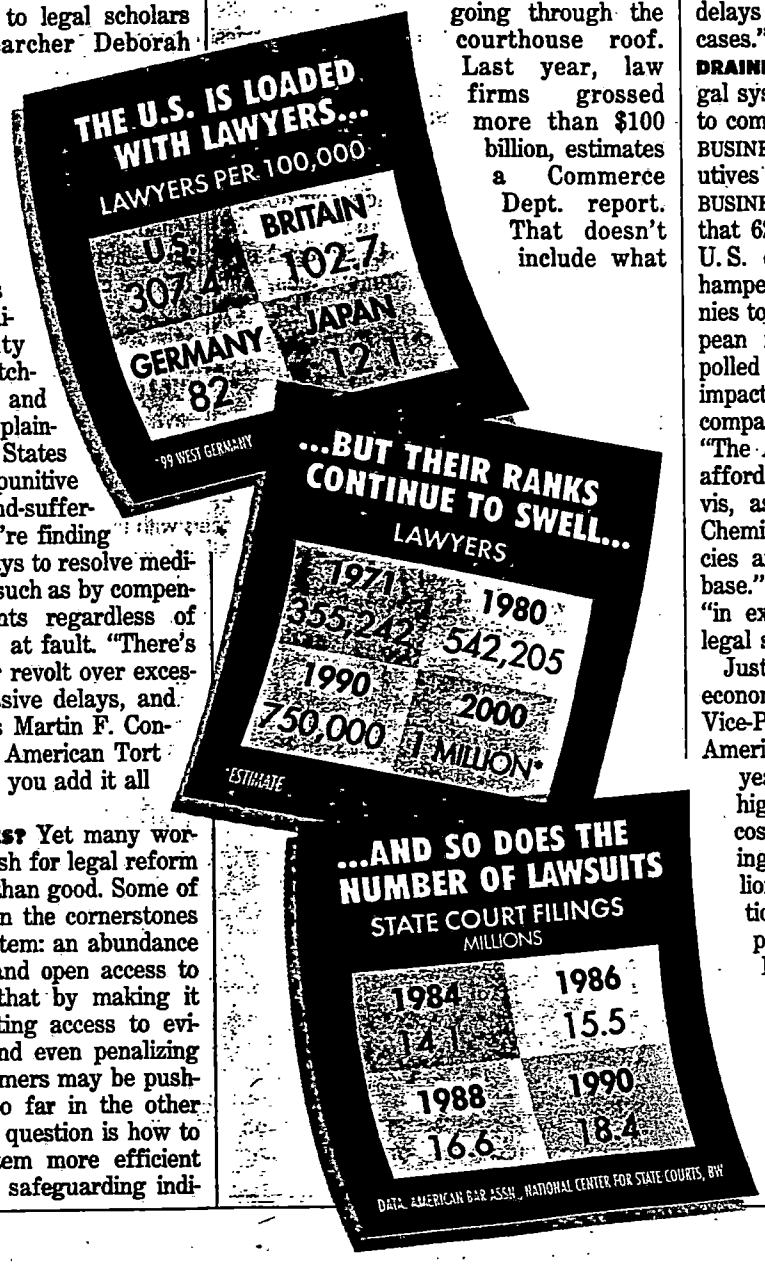
OVERBALANCED SCALES? Yet many worry that a headlong rush for legal reform could do more harm than good. Some of the proposals threaten the cornerstones of the U.S. legal system: an abundance of individual rights and open access to courts. Critics fear that by making it tougher to sue, limiting access to evidence before trial, and even penalizing those who lose, reformers may be pushing the pendulum too far in the other direction. The critical question is how to make the legal system more efficient and less costly while safeguarding individual liberties. "A broad statement that going to court is evil is very destructive to our democratic process," says Pamela Gilbert, legislative director for Ralph Nader's Congress Watch. "We should take pride in our legal system."

But even Gilbert agrees that parts of the system are breaking down. America's legal bills are going through the courthouse roof. Last year, law firms grossed more than $100 billion, estimates a Commerce Dept. report. That doesn't include what companies spend on their own legal departments—and what they must pay to resolve suits. Since 1971, the number of attorneys has almost tripled, to 780,000—far more per capita than in Britain or Japan (table). "The prime beneficiaries of the legal system are lawyers, not victims and not society as a whole," says Ralph Warner, co-founder of Nolo Press Inc., a Berkeley (Calif.) publisher of legal self-help books.

The overloaded courts are only making matters worse. Since 1960, the number of civil suits in federal courts has soared 300%, even after dropping from a peak in 1985. In the state courts, civil suits have jumped by more than 4 million in the past six years (table). And that's on top of an exploding backlog of criminal actions that push business cases to the back of the line. "You can't divorce the civil courts from the criminal courts," says Sol Wachtler, chief judge of the State of New York. "There are delays because of the clog in criminal cases."

DRAINING. Executives fear the U.S. legal system is crippling America's ability to compete in the global marketplace. A BUSINESS WEEK/Harris Poll of top executives at corporations drawn from the BUSINESS WEEK 1000 (page 66) found that 62% of those surveyed believe the U.S. civil justice system significantly hampers the ability of American companies to compete with Japanese and European rivals. A striking 83% of those polled say the fear of lawsuits has more impact on decision-making within their company today than it did 10 years ago. "The American economy can no longer afford this process," says Ronald L. Davis, assistant general counsel at Dow Chemical Co. "The system's inefficiencies are eating away at our industrial base." He says Dow Chemical spends "in excess" of $100 million a year on legal services and liability insurance.

Just how much litigation drains the economy is a matter of fierce debate. Vice-President Dan Quayle claims that Americans spend more than $80 billion a year on direct litigation costs and higher insurance premiums. Indirect costs, including the expense of avoiding liability, he says, reach $300 billion annually—about 1.8% of the nation's $5.7 trillion gross domestic product. But legal scholars such as Marc S. Galanter, a professor at the University of Wisconsin's school of law, attack those figures as "the product of casual speculation." Instead, he cites a 1986 study by RAND's Institute for Civil Justice. It put the cost of the U.S. tort system—including court ex-



penses, legal fees, and the value of lost work—at between $51 billion and $58 billion.

Whatever the tab, America's companies are fed up with watching their legal bills erode profits. Some are locked in unproductive court brawls with rivals. Four-year-old Cyrix Corp., a Richardson (Tex.) semiconductor maker, has been battling Intel Corp. In December, 1990, Cyrix filed an antitrust suit accusing Intel of an anticompetitive campaign to keep Cyrix co-processors out of the market. A month later, Intel sued Cyrix for patent infringement. While the judge has yet to rule in that case, Intel just filed another patent-infringement suit against Cyrix in response to reports that Cyrix was about to introduce a chip that mimics Intel's top-of-the-line 486 microprocessor. The Cyrix chip was introduced on Mar. 30 (page 95).

SUE CITY. Other companies, meantime, are shunning domestic markets out of fear of product-liability suits. Biomet Inc. sells spinal implants for back problems virtually all over the world—with one glaring exception. "We don't feel confident in the U.S. with such a product," says Dane A. Miller, CEO of the Warsaw (Ind.) orthopedics company. "Our legal system in America is totally out of control."

Countries such as Britain and Japan hold down costs by making it more difficult to sue and harder to win. In the U.S., each side in a lawsuit usually pays its own legal costs, regardless of the outcome. But Britain and other countries force losers to pay the winners' fees as a way to discourage frivolous suits. American companies spend as much as 80% of their legal bills on discovery, which lets parties review an opponent's evidence before trial. In Japan, discovery doesn't exist (page 64).

The hallmarks of the U.S. legal system—jury trials, contingency fees, and punitive damages—encourage the "I'll sue" mentality. Dow Chemical gets hit with some 2,000 new product-liability claims in the U.S. every year, but only about 20 such claims are filed against it in the rest of the world, says Davis. He notes that while many European countries have adopted broad U.S.-style product-liability laws, many lack such things as contingency fees, discovery, and jury trials. The Midland (Mich.) chemical maker spends an average of $250,000 just to get to trial. Says Davis: "Even when we win, we don't win."

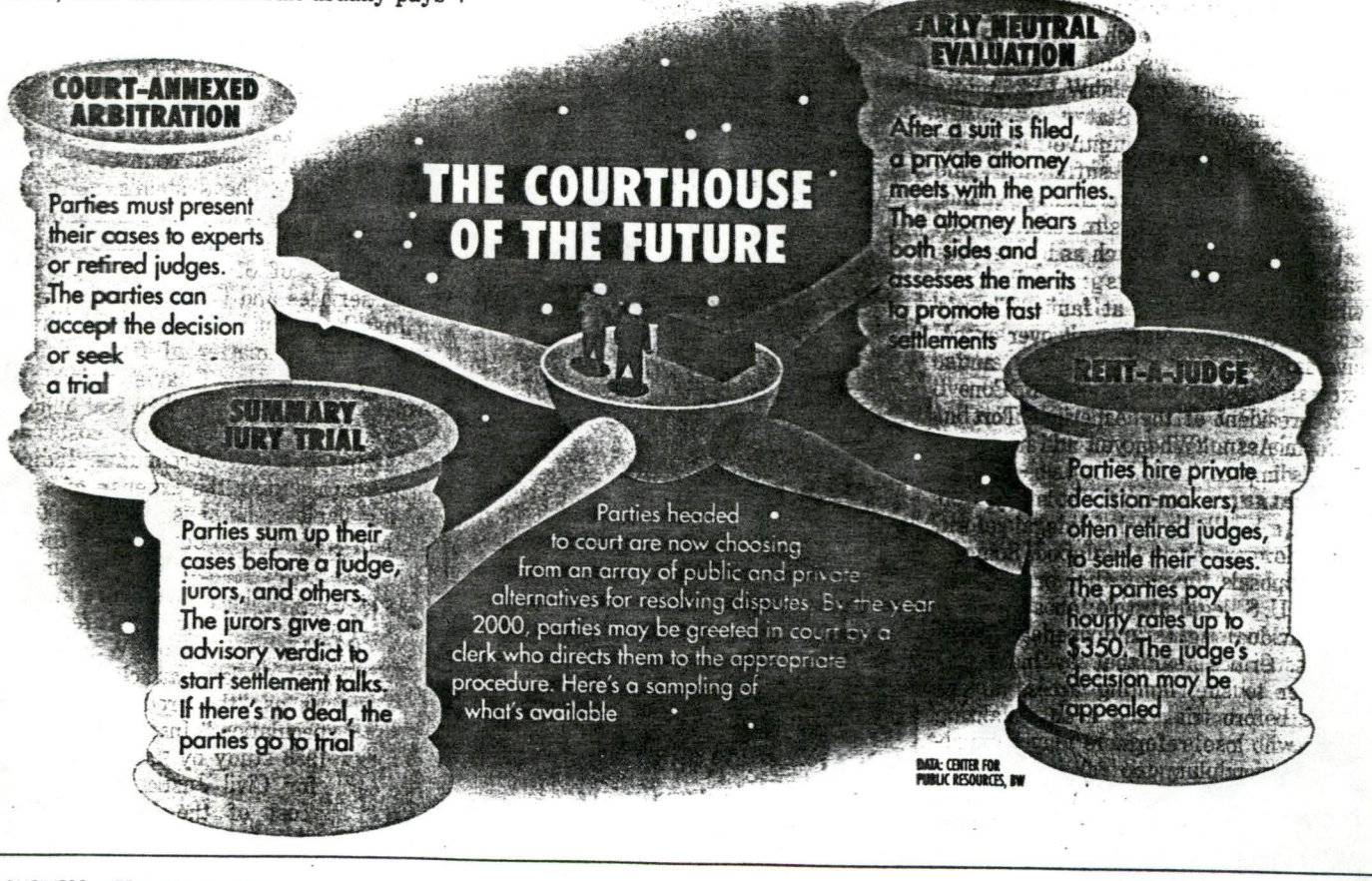
Many executives say they settle even frivolous suits to avoid the legal fees. Others settle, they say, to escape the long-shot risk of punitive damages. The claims are "used to extort money," says Robert W. Pommerville, general counsel of Beverly Enterprises Inc., a leader in the nursing home industry. Pommerville says it takes "a real gutsy individual" to go to trial on punitive-damages claims, because juries are so unpredictable.

But settling can bring its own headaches. In 1984, Alan F. Shugart, CEO of Seagate Technology, was accused in a class action of artificially inflating the stock price. Attorneys for the Scotts Valley (Calif.) disk-drive maker persuaded him to settle in 1991, for $9 million, he says. Two subsequent suits were filed in 1988 and 1991, which copied the class action verbatim—from the wording of the charges to the misspellings. Both



"If American businesses are concerned about the burdens of legal expense, they could control their own lawyers better"

DEBORAH HENSLER
RAND researcher who studies civil-litigation trends



PHOTOGRAPH BY EDUARDO CITRINBLUM; ILLUSTRATION BY RAY VELLA/BW

suits are still pending in the courts.

Now, Shugart goes on the offensive at any hint of a lawsuit. Last year, for example, the company laid off an undisclosed number of employees. When a group of them joined with a coalition of labor unions and sued for insufficient notice, Seagate publicly threatened to countersue, clearly stating it would fight to recover court costs as well as punitive damages on the grounds that the labor unions' suit was frivolous. The coalition later withdrew the case.

HUGE SAVINGS. Rather than get caught up in the system, corporations are dropping out. Already, some 600 top corporations have signed a pledge drafted by New York's Center for Public Resources, a nonprofit group that promotes alternatives to litigation. The pledge states that the signers will consider negotiation and other forms of "alternative dispute resolution" before running to court against other signers. Last year, for the first time, law firms nationwide made a similar pledge, and almost 800 firms have signed on. The Center found that avoiding court saved 142 companies more than $100 million in legal costs for disputes concluded in 1990.

General Mills Inc. has long required a commitment to alternative dispute resolution on all contracts it signs—cutting legal costs for contract disputes to a bare minimum, says General Counsel Clifford L. Whitehill. Now, the Minneapolis food company is moving toward requiring a similar commitment from employees. But the company's best single experience with such techniques occurred in 1987. On the verge of going to court with a supplier, Whitehill says, both sides agreed to argue their case before the CEOs of both companies. After six days of arguments, the parties agreed that General Mills would get a $45 million settlement.

Other companies are devising formal systems to settle routine disputes. In mid-1990, General Motors Corp. hired Endispute Inc., based in Washington, D. C., to set up systems in each of its divisions for resolving dealer disputes. The systems range from nonbinding, voluntary mediation at Cadillac to binding arbitration at Chevrolet, Pontiac, Oldsmobile, and GMC Trucks, and were written into the dealers' five-year franchise agreement. William Coulter of Phoenix' Coulter Cadillac just mediated a dispute with GM auditors over a warranty issue. Both sides argued their case before a GM executive, a dealer, and an Endispute staffer. They settled in a day, at a cost of $3,000 to GM and about $1,500 to Coulter. Says Coulter: "The process was fair."

For Motorola, the process of staying out of court starts early. Its lawyers worldwide learn how to counsel executives within the company on avoiding conflicts by focusing on better contracts, improved product quality, and truthful salesmanship. The law department also follows Motorola's total quality management program to eliminate wasteful labor and expensive errors. "Cutting legal costs is like reducing the cycle time in manufacturing," says Weise, the general counsel. "Our goal is to reduce the 'dispute cycle'—the time between the event that causes the dispute and the resolution."

There's more to Motorola's legal program than just staying out of court. The company rides herd on its outside lawyers to deliver quality service at the lowest possible cost. In a radical break with

COMING TO TERMS—WITHOUT BRINGING IN THE LAWYERS

Lawyers for Pacific Gas & Electric, Union Oil, and Thermal Power were preparing to fight one of the largest suits ever filed in Sonoma County (Calif.) Superior Court, when the three top executives decided that there had to be a better way. Rather than spend a year at trial, the executives resolved most of the issues privately—without their lawyers. To do the rest, they called in an outfit based in Orange County known as Judicial Arbitration & Mediation Services Inc. The JAMS mediator met often with the principals, even going up in a helicopter to survey the field at the heart of their contract dispute. The case settled last month, with JAMS's bill less than six figures.

Tapping into the fervor to cut litigation costs, JAMS is a part of one of the fastest-growing sectors of the law business: alternative dispute resolution. Started in 1979, it's the U.S.'s leading for-profit resolution company. This year it expects to hear 14,000 cases and see sales grow to $30 million, up 25% from 1991. JAMS has 18 offices in four states and a panel of 175 former judges. With $15 million from E. M. Warburg, Pincus & Co., JAMS plans to keep expanding.

It's not alone. Washington-based Endispute Inc. is also expanding its dispute-resolution services. And Philadelphia-based Judicate Inc. boasts more than 600 former judges offering arbitration and mediation. It's easy to see the appeal. Alternative resolution techniques save on discovery and provide privacy and flexibility in scheduling. But the driving force is the cost. JAMS charges between $300 and $350 an hour. Stacked against the $300 an hour a battery of lawyers might each charge litigants, it's unlike a litigated case, the typical JAMS case can be resolved in hours or days. "Alternative dispute resolution is like the hula hoop—why didn't someone else think of this before?" says JAMS CEO John K. Trotter, a retired state appellate judge.

Critics say problems arise when JAMS judges go beyond simple mediation and render decisions that can be appealed in the courts. Such private judging accounts for 1% of JAMS cases, but this tactic could soar in California, where parties can leapfrog the long court lines by getting a private ruling and then appealing it.

To head off government regulation, JAMS is developing guidelines for disclosing conflicts of interests, including prior contacts with parties. It's also devising a procedure for speedy handling of complaints. Given the need for faster and cheaper alternatives to the gridlocked courts, JAMS may soon be looking more and more like the Federal Express of the dispute business.

By Jane Birnbaum in Los Angeles and Morton D. Sosland in Philadelphia



SALES AT TROTTER'S RESOLUTION SERVICE ARE SOARING

MICHAEL GRECCO/OUTLINE

tradition, Motorola also refuses to pay for lawyers' travel, meals, and other incidentals. Instead, the law firms must figure such expenses into their hourly billing rate. Motorola forces the lawyers to follow a strict script that outlines a step-by-step procedure for resolving disputes. "They really bristle, because they're not used to that kind of participation by a client," Weise says. "Some outside counsel just can't do it."

Yet even companies that support such techniques remain skeptical that the new procedures will make a dent in the amount of litigation. Alternative dispute resolution works only when both parties agree to it, they say. A small company may be muscled into court by a larger rival with more resources. Other companies insist on trials to achieve public vindication. And individuals and their lawyers may be unwilling to step outside the system. Abandoning a trial "would do away with punitive and compensatory damages," says FMC Corp. General Counsel Patrick J. Head. "That's where the big scores have been."

It may not be that way for very much longer. More than 1,200 courts across the country are offering various alternatives to trials. In Texas, a court can order a case to mediation. In Colorado, lawyers who fail to tell clients about alternative dispute resolution now can be disciplined for breaching their ethical duties. And in California, some overworked judges refer cases to a private settlement company, Judicial Arbitration & Mediation Services Inc., based in Orange County (page 63).



"Lawyers get too much. I would cap fees and take some of what lawyers get and give that to elementary school teachers, nurses, health workers, people who really do good for society"

ALAN DERSHOWITZ
Harvard Law professor and criminal defense lawyer

Many courts are offering alternatives to trials right in the courthouse or other neutral sites. The federal court for the Northern District of California in San Francisco sends up to 300 cases a year through a settlement program known as "early neutral evaluation." Under it, the parties meet with a volunteer attorney who is an expert in the disputed subject matter. He sizes up the cases, gives his opinion, and then asks whether the parties want to work out a deal. An early study found up to 40% of these cases settled on the spot. Such programs are redefining the role of courts. "In the future, instead of walking into a building called a courthouse, you might walk into the Dispute Resolution Center," says Scott H. Bice, Dean of the University of Southern California's Law Center.

LOSERS WEEPERS. The debate over legal reform in Washington can only speed up these changes. Last year, President Bush signed an executive order to rein in the vast swarm of government lawyers—the largest group of lawyers litigating in the federal courts. And Vice-President Quayle delivered a scathing, widely publicized speech to the American Bar Assn., blasting lawyers for the nation's lack of competitiveness. In February, the White House unveiled a bill that draws from Quayle's 50-point agenda. The bill promotes such things as al-

THE JAPANESE SOLUTION: KILL ALL THE LAWSUITS

When IBM sued Hitachi Ltd. for industrial spying in 1982, the Japanese company got a shocking introduction to legal battles, American-style. Hitachi's first bill from its U.S. law firm exceeded its total payments for legal services in Japan since the company was founded in 1920.

No wonder legal reformers in the U.S. look wistfully at Japan. Its courts aren't cluttered with liability suits, and lawyers are about as scarce as American cars. While the U.S. prides itself on individual rights and equal access to the courts, critics charge that the Japanese legal system discourages litigation. Perhaps. But the culture's distaste for direct confrontation helps ensure that most legal disputes are resolved privately and more efficiently than in the U.S. "In Japan, a litigious person is not welcome," says Toshiro Nishimura, senior partner at Nishimura & Sanada, a top international law firm in Tokyo.

Barriers to litigation in Japan start with legal education (table). To become a *bengoshi*, or lawyer, one must win a spot in the Legal Training & Research Institute. But the government-run school admits 2% of its 35,000 applicants annually. So Japan's exclusive legal club has just 14,336 lawyers—and grows by only 400 *bengoshi* per year. There are 780,000 lawyers in the U.S., which has twice Japan's population.

COSTLY RECOURSE. Those who can find a lawyer to take their case encounter other roadblocks. Critics of the U.S. legal system complain that parties abuse discovery, which grants access before trial to potential evidence held by an opponent. Japan is at the other extreme. It has no discovery at all. And the difficulty of obtaining evidence makes it especially tough for consumers to win product-liability suits (BW—Mar. 9). "I have often said to clients that I am 100% certain that they would win their case—but where's the evidence?" says Nishimura. "You can't force the other side to disclose."

Plaintiffs also must have deep pockets. Japan bars two key methods of sharing the cost of litigation: class actions and contingency-fee arrangements. At the same time, plaintiffs must pay an up-front fee to their lawyers of up to 8% of the damages sought in liability suits, plus a nonrefundable filing fee to the courts of one-half of 1% of the damages. In 1991, a small Seattle-based log-home maker provided a Japanese customer with $240,000 worth of materials and labor for which the company claims it was never paid. To file a $240,000 suit, it must pay its lawyers $20,204, including the filing fee of $1,200. "It's too expensive for us to pursue that course," sighs a top manager at the company. "We've already lost a lot of money."

Damage awards in Japan don't come close to the estimated average of $1.5 million per case paid last year in U.S. product-liability suits in state courts. On Feb. 7, the Tokyo District Court ordered Chisso Corp., a chemical company responsible for one of Japan's best-known industrial poisoning cases, to compensate 42 victims. The award: $1.3 million, or $31,000 per victim.

When disputes arise between companies, attorneys often are the last to get involved. Salesmen and front-line managers are the chief problem-solvers. In part

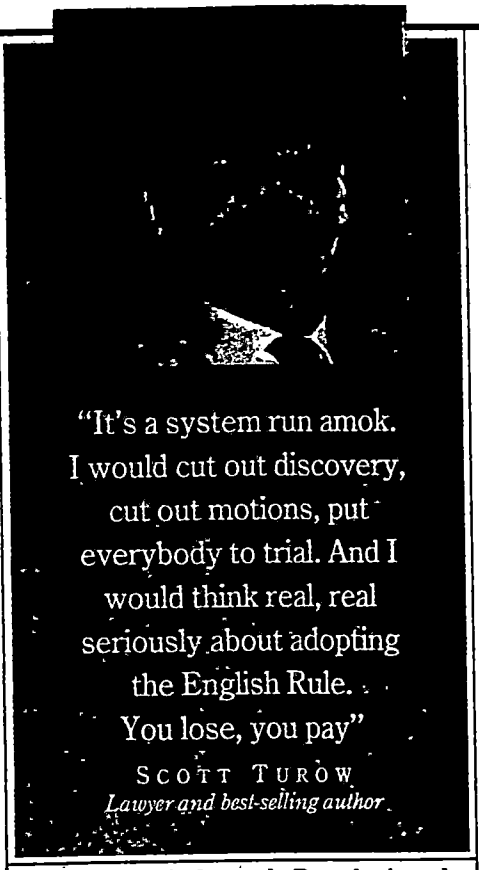
NAJLAH FEANNY/SABA

ternatives to litigation and the English Rule, which forces losers to pay the winners' legal fees.

While the bar blasted Quayle's lawyer-bashing rhetoric, it's taking his proposals seriously. "We ought to be extremely grateful to Dan Quayle for just getting this issue on the table," says Talbot S. D'Alemberte, president of the ABA. In February, it released a report supporting many of Quayle's proposals but criticizing him for ignoring the "broader and more significant problems of our justice system"—judicial funding and inadequate access for the poor.

Others have their own visions for the future. HALT, An Organization of Americans for Legal Reform, is pushing out-of-court alternatives to tort litigation, such as no-fault auto insurance and workers' compensation. Its aim is to ensure fair and prompt compensation for victims and more predictabilty for defendants. Advisory committees in each of the 94 federal courts, meantime, are experimenting with improving the litigation process, including making discovery voluntary. They're also forcing judges to be managers as well as decision-makers. "The greatest single forward step would be to have district court judges set schedules and require lawyers to live up to them," says former Supreme Court Justice Lewis F. Powell Jr.

Companies and judges are wise to put a premium on negotiation rather than on



"It's a system run amok. I would cut out discovery, cut out motions, put everybody to trial. And I would think real, real seriously about adopting the English Rule. You lose, you pay"

SCOTT TUROW
Lawyer and best-selling author

fighting until the end. But that's only the beginning. More attention must also be paid to state and federal courts so that they can run more efficiently. And Congress cannot continue to pass federal criminal laws that inundate court dockets without also quickly filling judicial vacancies. As of Mar. 31, there were 120 vacant federal judgeships, or about 14% of the federal bench.

CHEAP AND DIRTY? Alternatives to trials such as arbitration and mediation should help lighten the courts' burdens, but certain safeguards are needed. Now, proceedings are held in private without regard to whether a public interest or important legal question is at stake. And the resolution business is largely unregulated: Anyone with a business card or stationery can set up shop.

Instead, standards must be established so that mediators are qualified. The proceedings must also be open to the public—and the press. Alternative justice shouldn't become just another way to avoid disclosure of health and safety dangers. And some disputes involving novel or constitutional issues must remain in the public courts. Private dispute resolution can only follow the law, not set new precedents.

What's good in the legal system must be protected. As lawmakers, attorneys, and executives wrestle with legal reform, they must ensure that individual rights are not sacrificed in pursuit of swifter and more economical justice.

By Michele Galen in New York, with Alice Cuneo in San Francisco, David Greising in Chicago, and bureau reports

BW/Harris Poll appears on page 66.

that's to avoid spoiling a long-term relationship. "We may lose $1 million," says NEC Corp. legal chief Satoshi Nakaichi, "but the idea is to coexist and win that money back on the future deals."

NEVER SUE. Rarely do companies battle in court. Nissan Motor Co. is involved in 10 cases in Japan, only one of which involves another company. The rest concern labor and consumer disputes, which make up most of the suits against companies in Japan. "We would never sue a company like our own," says Nissan legal department manager Kenji Toriumi. Only when a case seems headed for court will companies call in a *bengoshi*. But to keep matters quiet, some companies may opt for arbitrated settlements, where three *bengoshi* arbitrators weigh the case privately and issue a binding decision. Nissan recently insisted on a 15% discount on faulty factory equipment supplied by an affiliate. Rather than sue, Nissan settled for half that. "It was an amicable agreement," says Toriumi, "and it saved us time, money, and the relationship."

That attitude keeps costs down. Most of Nissan's legal expenses go not for pricey outside legal help but for a modestly paid staff of a dozen tax sleuths, 50 patent experts, and 30 legal specialists. Lower bills free up cash for research and other areas, and enable more competitive pricing than U.S. companies can afford.

Suits are few, but some experts argue that Japan has more legal practitioners than the statistics reveal. Japan's corporate halls are stocked with non-*bengoshi* legal experts. Sony Corp. employs 120, for example. Japan also has about 50,000 licensed tax practitioners who offer services similar to those of U.S. tax lawyers. About the same number of scriveners draft court papers and give legal advice, while 5,000 non-*bengoshi* patent specialists perform services similar to those of U.S. patent attorneys. Add them all up, and Japan has more legal practitioners per capita than the U.S., or 42 per 10,000 people vs. 29, says Raymond August, assistant professor at Washington State University.

Some Japanese argue that Japan should have more lawyers and that certain laws should be rewritten to favor consumers. Critics also say it should be easier for the Japanese to redress clear wrongdoing. Still, the bias against courtroom solutions remains strong. "I work in the legal department," says Nissan's Toriumi, "but I would never ask a lawyer to resolve a problem in my own life." The belief that disputes should be settled amicably is something American legal reformers only now are beginning to embrace.

By Ted Holden in Tokyo

JAPAN'S APPROACH

- Limits the number of attorneys passing the bar exam to 2% of 35,000 applicants
- Forces would-be plaintiffs to pay an up-front fee to their lawyers of up to 8% of damages sought
- Bars contingency fees, class actions, and other fee-sharing devices that make it easier to sue
- Lets judges, not juries, set damage awards, which rarely exceed $150,000, even when the victim has been killed
- Bans discovery so that plaintiffs are denied access before trial to an opponent's potential evidence
- Nurtures a strong cultural attitude that confrontration is to be avoided and looks down upon those who sue

DATA: BW

T. WESTENBERGER/SYGMA

Business Week/Harris Executive Poll

THE VERDICT FROM THE CORNER OFFICE



Corporate executives think the high cost of civil justice is a drag on U.S. business and the economy. Fully 83% say their decisions are increasingly affected by the fear of lawsuits, and a 62% majority say the legal system significantly hampers U.S. competitiveness. Executives know whom they blame for the problem: plaintiffs, the contingency-fee system, and generous juries. They are also quite firm about the solutions. An overwhelming 97% favor much more use of alternative methods to resolve disputes, and 91% want judicial screening of cases. But most oppose restrictions on expert witnesses and don't want to see more government spending on the courts.

HIGH COURT COSTS

■ Here are some possible reasons for the high cost of litigation and civil justice. For each one, please say whether you think it is a major reason, a minor reason, or not a reason for the high cost.

	Major reason	Minor reason	Not a reason	Not sure
The knowledge that major corporate defendants and their insurance companies have deep pockets	92%	8%	0%	0%
Contingency fees that enable people to sue without any financial risk	85%	13%	1%	1%
Juries that hand out awards that are too high	79%	17%	3%	1%
Laws or regulations that make it too easy to sue	64%	29%	6%	1%
Outside corporate lawyers who drag out cases to jack up their hourly fees	47%	45%	7%	1%
Large corporate litigants that drag the process out in an effort to outlast opponents with fewer resources	34%	55%	9%	2%
Companies that compete in the courtroom instead of in the marketplace	13%	60%	26%	1%
Companies that rush potentially dangerous products to market, opening themselves to subsequent lawsuits	9%	70%	19%	2%

POSSIBLE REFORMS

■ Here are several proposals now under consideration to rein in frivolous litigation and cut legal costs and delays in the civil justice system. Please tell me whether you favor or oppose each of the following:

	Favor	Oppose	Not sure
Making much greater use of alternative dispute resolution methods, such as arbitration, mediation, and private judges	97%	2%	1%
The judicial screening of cases to eliminate apparently frivolous or very weak claims	91%	9%	0%
Requiring the loser in civil suits to routinely pay the winner's legal costs	83%	17%	0%
Restricting the pre-trial discovery process	49%	43%	8%
Restricting the use of expert witnesses	28%	66%	6%
Increasing federal and state spending on the courts	28%	69%	3%

LITIGATION'S IMPACT...

■ In your company, would you say that the following have a major impact, a minor impact, or almost no impact on your business?

	Major impact	Minor impact	Almost no impact	Not sure
The high cost of defending and protecting the company from litigation	40%	49%	11%	0%
Fear of litigation that hampers the introduction of valuable new products or entry into new markets	10%	47%	42%	1%
Legal issues that divert valuable management time and energy from running the business	44%	50%	6%	0%

...AND HOW IT'S GROWING

■ Would you say that the fear of lawsuits has more or less impact on decision-making within your company today than it did 10 years ago?

More impact	83%
Less impact	5%
No difference	11%
Not sure	1%

COMPETITIVE BURDEN

■ Do you feel that the U.S. civil justice system significantly hampers the ability of U.S. companies to compete with Japanese and European companies, or don't you feel that way?

Does hamper	62%
Does not	32%
Not sure	6%

Edited by Mark N. Vamos

Survey of 400 senior executives at corporations drawn from the BUSINESS WEEK Top 1000. Interviews were conducted Jan. 27-Feb. 11, 1992, for BUSINESS WEEK by Louis Harris & Associates Inc.

TOM CURRY

AMERICAN BUSINESS CONFERENCE
WILLARD HOTEL
TUESDAY, APRIL 7, 1992
2:00 PM

347-9564

500

reporters outnumbered audience!

THANK YOU, JIM JONES. ((SOME PEOPLE SAY I'VE BEEN TRAVELING TOO MUCH. SO TODAY IS AN EXAMPLE OF MY NEW POLICY: NO TRIPS FARTHER THAN ONE BLOCK.)) 2 C

IT IS ALWAYS A PLEASURE TO SPEAK WITH MEMBERS OF THE AMERICAN BUSINESS CONFERENCE, BECAUSE IT IS ALWAYS A PLEASURE TO SPEAK WITH THE BEST.

Notre Dame
SMU
Fla. International

I WOULD LIKE TO TALK TO YOU TODAY ABOUT THE FUTURE -- THE FUTURE OF OUR COUNTRY GENERALLY, AND MORE PARTICULARLY THE FUTURE OF OUR COUNTRY'S BUSINESS ENVIRONMENT. IN FACT, WE CANNOT SEPARATE THE TWO. THE AMERICA OF THE 21ST CENTURY -- ITS ABILITY TO MAKE PEACE IN THE WORLD, TO FOSTER STRONG FAMILIES, TO CREATE REWARDING JOBS -- WILL BE SHAPED TODAY, IN LARGE PART BY HOW HOSPITABLE WE MAKE AMERICA FOR BUSINESS.

WE CAN LEARN FROM YOUR ACHIEVEMENT. THE KEY TO THE SUCCESS OF ANY HIGH-GROWTH COMPANY IS THE WISE DEPLOYMENT OF RESOURCES. THE SUCCESSFUL COMPANY CHANNELS LABOR AND INVESTMENT INTO THOSE AREAS WITH THE POTENTIAL FOR THE GREATEST EXPANSION AND THE HIGHEST RETURN. YOU TAKE THE RISK; YOU REAP THE REWARD; EVERYONE, MEANWHILE, BENEFITS FROM THE WEALTH YOU CREATE.

THAT, IN BRIEF, IS THE GENIUS OF ENTREPRENEURIAL CAPITALISM, A SYSTEM THAT HAS MADE AMERICA THE ENVY OF THE WORLD. FOR 200 YEARS OUR PROSPERITY HAS SPRUNG FROM OUR ABILITY TO INNOVATE, TO CHANGE AS THE WORLD CHANGES. BUT AMERICA'S WORLD LEADERSHIP IS NOT AUTOMATIC; IT IS NOT A BIRTHRIGHT. WE MUST CONTINUE TO EARN IT, DAY BY DAY, QUARTER BY QUARTER, YEAR BY YEAR. THE WORLD NOW IS CHANGING AT A PACE NO ONE COULD HAVE DREAMED OF A GENERATION AGO. AND AMERICA, WHICH HAS LED THE WORLD'S TRANSFORMATION, MUST CHANGE WITH IT.

OVER THE LAST SEVERAL YEARS DEADWEIGHTS HAVE BEGUN TO SLOW THE ENGINE OF GROWTH -- INEFFICIENCIES A COMPETITIVE ECONOMY CANNOT TOLERATE. TODAY I WANT TO DISCUSS FIVE AREAS OF REFORM, FIVE CRITICAL WAYS IN WHICH AMERICA MUST CHANGE IF WE ARE TO CONTINUE TO LEAD THE WORLD. YOU UNDERSTAND THE URGENCY, FOR EACH OF THESE PROBLEMS PRESENTS ITSELF TO AMERICAN COMPANIES NOT AS AN ABSTRACTION BUT IN THE MOST IMMEDIATE WAY: AS A COST OF DOING BUSINESS -- A COST YOU CAN'T CONTROL, AN EXPENDITURE WITH NO POSSIBLE RETURN.

WHEN OUR LEGAL SYSTEM BECOMES INCAPABLE OF RESOLVING DISPUTES IN A TIMELY AND CIVIL MANNER, BUSINESS LOSES THE INCENTIVE TO INNOVATE AND TAKE RISKS. WHEN HEALTH CARE COSTS ESCALATE, BUSINESS PICKS UP MUCH OF THE TAB. WHEN GOVERNMENT IMPOSES BARRIERS TO TRADE, BUSINESS PAYS THE PRICE IN OPPORTUNITIES LOST. WHEN OUR CHILDREN LEAVE SCHOOL WITHOUT RUDIMENTARY SKILLS, BUSINESS BEARS THE BURDEN IN LOWERED PRODUCTIVITY. AND WHEN GOVERNMENT FREEZES IN GRIDLOCK, BUSINESS CAN NO LONGER PLAN RATIONALLY FOR THE FUTURE.

LET ME BEGIN WITH THE CRYING NEED TO REFORM OUR COUNTRY'S CIVIL JUSTICE SYSTEM. EVERY AMERICAN HAS HEARD THE STORIES OF BIZARRE OR FRIVOLOUS LAWSUITS; BUT MOST OF YOU HAVE LIVED THEM, TALES THAT COULD HAVE BEEN TORN FROM THE PAGES OF KAFKA. CONSIDER ONE EXAMPLE, RELATED BY ONE OF YOUR MEMBERS, ROGER COLEMAN, PRESIDENT OF RYKOFF-SEXTON, A FOOD MANUFACTURER AND DISTRIBUTOR.

AFTER RECORD EARNINGS IN 1989, MR. COLEMAN PUBLICLY EXPRESSED HIS CONFIDENCE THAT 1990 WOULD BE EVEN BETTER. WHEN EARNINGS FELL SHORT, HIS HOPEFUL STATEMENT BECAME THE CAUSE OF A SHAREHOLDER CLASS-ACTION LAWSUIT.

FIRST CAME A MEETING WITH PLAINTIFFS' CONTINGENCY-FEE LAWYERS, AT WHICH THE MERITS OF THE CASE WERE NEVER EVEN DISCUSSED. "THE ISSUE," SAYS MR. COLEMAN, "WAS THE DEPTHS OF OUR POCKETS." NEXT CAME THE NIGHTMARE OF DISCOVERY: ENDLESSLY EXPENSIVE AND INVASIVE. THE COMPANY'S MANAGERS, INSTEAD OF MANAGING, SPENT THEIR TIME PREPARING FOR DEPOSITIONS. THE LAWSUIT, HE SAYS, "BROUGHT EVERYTHING TO A STOP."

IN THE END, RATHER THAN PERMIT THE TOTAL EXHAUSTION OF COMPANY RESOURCES, MR. COLEMAN DECIDED TO SETTLE. THE TAB FOR THIS EXERCISE IN FUTILITY: $8.7 MILLION. AS MR. COLEMAN SAYS: "THAT'S OVER $8.7 MILLION THAT WAS DIVERTED FROM NEW INVESTMENTS IN JOBS AND FACILITIES."

THE SCENARIO IS REPEATED DAILY THROUGHOUT AMERICAN BUSINESS. IT IS NOT REPEATED, LET ME STRESS, AMONG OUR WORLD COMPETITORS. ONLY THE UNITED STATES HAS SEEN THE NUMBER OF LAWYERS DOUBLE OVER A 20-YEAR PERIOD. ONLY THE UNITED STATES SPENDS MORE THAN $80 BILLION ANNUALLY IN DIRECT LITIGATION COSTS, PERHAPS FOUR TIMES THAT IN INDIRECT COSTS. ACCORDING TO A RECENT SURVEY, 40 PERCENT OF COMPANIES THAT HAD BEEN THE TARGET OF PRODUCT LIABILITY SUITS HAVE DISCONTINUED CERTAIN TYPES OF PRODUCT RESEARCH.

WE MUST REMOVE THIS BALL AND CHAIN FROM OUR ABILITY TO PRODUCE AND COMPETE WORLDWIDE. MY COMPETITIVENESS COUNCIL, LED BY VICE PRESIDENT QUAYLE, HAS OFFERED 50 RECOMMENDATIONS FOR LEGAL REFORM. THEY WOULD LIMIT DISCOVERY TO REASONABLE PROPORTIONS, DISCOURAGE SOME FRIVOLOUS SUITS THROUGH A "LOSER-PAYS" RULE, AND OFFER ALTERNATIVE MEANS OF RESOLVING DISPUTES.

THIS BROAD LEGAL REFORM WON'T BE EASY -- JUST LOOK AT THE FIGHT WE'VE HAD ON PRODUCT LIABILITY REFORM. WE INTRODUCED A REFORM BILL IN 1990, AND AGAIN IN 1991. SENATE DEMOCRATS REFUSE TO BRING IT TO A VOTE; IN THE HOUSE IT'S STUCK IN TWO COMMITTEES. THE SPECIAL INTERESTS ARE LINING UP AGAINST LEGAL REFORM, AND WE CAN USE YOUR HELP IN MOVING IT FORWARD.

IF WE'RE SUCCESSFUL, THE EFFECTS WILL BE FAR-REACHING, EXTENDING INTO ANOTHER AREA CRITICALLY IN NEED OF CHANGE. MEDICAL MALPRACTICE PREMIUMS ALMOST DOUBLED IN THE SECOND HALF OF THE 1980S. DOCTORS ARE PRACTICING "DEFENSIVE" MEDICINE, ORDERING AN ESTIMATED $20 BILLION A YEAR IN UNNECESSARY TESTS AND PROCEDURES TO PROTECT AGAINST FRIVOLOUS LITIGATION.

THE TRENDS IN HEALTH CARE COSTS ARE SIMPLY UNSUSTAINABLE. FROM LESS THAN 6 PERCENT 30 YEARS AGO, TOTAL HEALTH CARE EXPENDITURES ARE TODAY ABOUT 13 PERCENT OF GDP. SOME MID-RANGE ESTIMATES PUT THAT FIGURE AT 30 PERCENT BY THE YEAR 2030 -- THAT'S THIRTY CENTS OF EVERY DOLLAR OF NATIONAL INCOME SPENT ON HEALTH CARE. RIGHT NOW, ACCORDING TO ONE FEDERAL STUDY, AMERICAN CORPORATIONS ALREADY SPEND MORE ON HEALTH CARE EACH YEAR THAN THEY EARN IN AFTER-TAX PROFITS.

WE MUST REFORM THE SYSTEM -- BUT WE FACE A CROSSROADS. SOME HAVE ADVOCATED NATIONALIZED CARE; OTHERS PROPOSE THE SO-CALLED "PAY OR PLAY" APPROACH, WHICH I AM CONVINCED IS MERELY A STEP ON THE ROAD TO NATIONALIZED CARE.

NEITHER IS ACCEPTABLE. NEITHER WILL PRESERVE THE QUALITY OF OUR COUNTRY'S HEALTH CARE, WHICH REMAINS THE BEST IN THE WORLD. I WILL NOT LET THAT HIGH QUALITY BE TAKEN AWAY FROM THE AMERICAN PEOPLE THROUGH SOME SCHEME OF GOVERNMENT CONTROL.

NATIONALIZED CARE MEANS RATIONED CARE; ITS PROMISE OF COST CONTAINMENT IS A MIRAGE. "PAY OR PLAY" WOULD DUMP STILL MORE MANDATES ON BUSINESS. FOR EMPLOYERS, A 9 PERCENT PAYROLL TAX WOULD MEAN A 34 PERCENT INCREASE IN HEALTH INSURANCE COSTS. THAT MONEY MUST COME FROM SOMEWHERE -- AND FOR A COMPANY UNABLE TO PASS ALONG THE ADDED COSTS THROUGH HIGHER PRICES, THAT MEANS DECREASED INVESTMENT, LOWER WAGES, AND FEWER JOBS.

Huh?

THERE IS AN ALTERNATIVE. MY PROPOSED HEALTH CARE REFORM WILL BUILD ON OUR SYSTEM'S STRENGTHS, PRESERVING THE QUALITY OF CARE. WE WILL INCREASE CONSUMER CHOICE. THROUGH TRANSFERABLE CREDITS, WE WILL ASSURE ACCESS TO BASIC HEALTH INSURANCE FOR THE UNINSURED, AND CONTROL COSTS THROUGH MARKET INCENTIVES. AND WE WILL NOT RAISE TAXES ON AMERICAN EMPLOYERS.

I HAVE TARGETED A THIRD AREA FOR ATTENTION -- LIKE THE OTHERS, ABSOLUTELY CRITICAL TO OUR SUCCESS IN THE COMING DECADES. YOU UNDERSTAND THAT FOR AMERICA TO SUCCEED ECONOMICALLY AT HOME, WE MUST SUCCEED ECONOMICALLY ABROAD. THE FASTEST GROWING COMPANIES AMONG YOUR GROUP -- THE ONES CREATING THE GREATEST NUMBER OF JOBS HERE AT HOME -- ARE THOSE WITH FAR-REACHING INVOLVEMENT IN FOREIGN MARKETS.

I AM COMMITTED TO OPENING MARKETS TO AMERICAN GOODS AND SERVICES, REMOVING THE GOVERNMENT-IMPOSED BARRIERS THAT ACT AS A HIDDEN TAX ON AMERICAN BUSINESS. EACH MARKET SHUT OFF BY PROTECTION IS A LOST OPPORTUNITY TO SELL YOUR PRODUCTS. A SUCCESSFUL CONCLUSION TO THE CURRENT URUGUAY ROUND OF TRADE NEGOTIATIONS, FOR INSTANCE, COULD INCREASE WORLD OUTPUT BY $5 TRILLION OVER THE NEXT DECADE. MORE THAN $1 TRILLION OF THAT BOOM WILL GO TO THE UNITED STATES -- CREATING A HIGHER STANDARD OF LIVING AND MORE JOBS FOR AMERICANS.

EVEN CLOSER TO HOME, EXPORTS TO MEXICO HAVE MORE THAN DOUBLED OVER THE LAST FIVE YEARS -- CREATING MORE THAN 300,000 AMERICAN JOBS. OUR NORTH AMERICAN FREE TRADE AGREEMENT WILL LOCK IN AND EVEN MULTIPLY THOSE GAINS, CREATING A $6 TRILLION MARKET FOR AMERICAN PRODUCTS IN CANADA, MEXICO, AND THE UNITED STATES.

AS WORLD TRADE EXPANDS, THE NEED FOR A SOPHISTICATED, WELL-EDUCATED WORKFORCE WILL INTENSIFY. YET THE FACT IS GRIM AND UNDENIABLE: OUR CURRENT EDUCATIONAL SYSTEM IS UNABLE TO PRODUCE THE WORKERS THE HIGHLY COMPETITIVE WORLD MARKET DEMANDS.

OUR EDUCATIONAL FAILURES HAVE HIT AMERICAN EMPLOYERS HARD. ENGLISH IS NOW THE LANGUAGE OF INTERNATIONAL BUSINESS; YET ONLY 20 PERCENT OF 17-YEAR-OLDS CAN WRITE A SIMPLE TWO-PARAGRAPH LETTER APPLYING FOR A JOB. THE SITUATION IN GEOGRAPHY, MATH AND SCIENCE IS EQUALLY DIRE. TOO MANY BUSINESSES ARE FORCED TO PAY TWICE FOR THE EDUCATION OF PROSPECTIVE EMPLOYEES -- ONCE THROUGH TAXES THAT SUPPORT OUR SCHOOLS, AND AGAIN THROUGH JOB TRAINING TO REMEDY THE FAILURES OF THOSE SCHOOLS IN EDUCATING OUR YOUNG.

COMMUNITIES HAVE BEGUN TAKING MATTERS INTO THEIR OWN HANDS, WITH LOCAL BUSINESSES OFTEN ACTING AS CATALYSTS. ABC'S VITAL LINK, WHICH WORKS WITH LOCAL SCHOOLS TO ESTABLISH LEARNING INCENTIVES FOR STUDENTS, IS A PERFECT EXAMPLE OF THE COMMUNITY-BASED EFFORTS OUR CHILDREN NEED.

STILL, THERE IS MUCH FOR GOVERNMENT TO DO. THIS YEAR, SEVEN DIFFERENT FEDERAL AGENCIES WILL SPEND $18 BILLION ON A PATCHWORK OF 60 VOCATIONAL TRAINING PROGRAMS. IS IT ANY WONDER THAT SO MANY AMERICANS WHO SEEK TRAINING DON'T KNOW HOW TO GET IT? WORKING WITH STATE AND LOCAL GOVERNMENTS, OUR JOB TRAINING 2000 INITIATIVE WILL BRING COHERENCE TO THESE PROGRAMS AND OFFER "ONE-STOP SHOPPING" TO ASPIRING WORKERS.

JOB TRAINING 2000 PERFECTLY COMPLEMENTS THE REVOLUTION NOW TAKING PLACE IN AMERICAN EDUCATION AS A WHOLE. THROUGH OUR AMERICA 2000 INITIATIVE, WE WILL REINVENT OUR SCHOOLS. YOUR CHAIRMAN, JIM JONES, IS A LEADER IN THE NEW AMERICAN SCHOOLS DEVELOPMENT CORPORATION, A PRIVATE GROUP CREATED AT MY REQUEST TO LAUNCH AN ENTIRE GENERATION OF BREAK-THE-MOLD NEW AMERICAN SCHOOLS.

THIS REVOLUTION IS ESSENTIAL TO CREATING A WORLD-CLASS WORKFORCE. TO DO THAT, WE NEED TO SET WORLD-CLASS STANDARDS FOR STUDENTS AND CREATE A SYSTEM OF VOLUNTARY NATIONAL TESTS TO MEASURE THEIR PROGRESS. WE MUST REDOUBLE OUR EFFORTS TO RID OUR SCHOOLS OF DRUGS AND VIOLENCE -- TO CLEANSE AMERICA OF THIS SCOURGE THAT WASTES SO MANY YOUNG LIVES. AND WE MUST MAKE SCHOOLS MORE ACCOUNTABLE, BY FORCING THEM TO COMPETE. <u>THAT MEANS GIVING PARENTS THE OPPORTUNITY TO CHOOSE THEIR CHILDREN'S SCHOOLS -- PUBLIC, PRIVATE, OR RELIGIOUS</u>.

I AM CONVINCED THAT EACH OF THESE MAJOR REFORMS -- RESTORING SANITY TO OUR LEGAL SYSTEM, ENSURING QUALITY HEALTH CARE FOR ALL, EXPANDING WORLD TRADE, AND REINVENTING AMERICAN EDUCATION -- IS ESSENTIAL TO THIS COUNTRY'S FUTURE PRODUCTIVITY.

BUT EACH FACES POWERFUL OPPOSITION FROM SPECIAL INTERESTS WHO PROFIT FROM THE STATUS QUO. SO I HAVE TARGETED A FINAL REFORM, NO LESS IMPORTANT THAN THE OTHERS. IF AMERICA IS TO CHANGE, OUR GOVERNMENT MUST CHANGE.

LAST WEEK IN PHILADELPHIA, I PRESENTED SEVEN SPECIFIC PROPOSALS TO DEAL WITH THE PARALYSIS THAT GRIPS THE CONGRESS. THE RESULTS OF THIS GRIDLOCK ARE DISMALLY PLAIN. CONGRESS WAS INCAPABLE EVEN OF PASSING MY SHORT-TERM ECONOMIC GROWTH PACKAGE. BUT THEY MUST UNDERSTAND: I WILL CONTINUE TO FIGHT FOR MEASURES ESSENTIAL TO ECONOMIC GROWTH -- <u>INCLUDING A CUT IN THE TAX ON CAPITAL GAINS</u>. ☆☆

Stimulative

THE AMERICAN PEOPLE ARE RIGHTLY FED UP WITH BUSINESS AS USUAL: A DEFICIT THAT IS A FISCAL AND A MORAL OUTRAGE, A PERMANENT GOVERNING CLASS OBLIVIOUS TO THE NATIONAL INTEREST, AND HUNDREDS OF SELF-PERPETUATING PROGRAMS THAT DON'T EVEN AID THE PEOPLE THEY WERE DESIGNED TO HELP.

I REFUSE TO BELIEVE THAT THIS IS THE LEGACY WE WILL LEAVE OUR CHILDREN. BUT IT WILL BE -- IF WE DON'T REFORM THE UNITED STATES CONGRESS.

THE REFORMS I'VE OUTLINED HERE TODAY ARE GROUNDED IN BASIC PRINCIPLES, A WAY OF LOOKING AT THE WORLD. AS JEFFERSON SAID: "THE PILLARS OF OUR PROSPERITY ARE THE MOST THRIVING WHEN LEFT MOST FREE TO INDIVIDUAL ENTERPRISE." IN PRACTICE, THAT MEANS GOVERNMENT MUST TRUST THE WISDOM OF MARKETS MORE THAN THE WHIMS OF BUREAUCRATS. THE FREELY MADE DECISIONS OF BUSINESSMEN AND WOMEN MUST TAKE PRECEDENCE OVER THE ENGINEERING SCHEMES OF GOVERNMENT. AND ALL OF OUR INSTITUTIONS -- FROM THE U.S. CONGRESS TO THE LOCAL SCHOOL BOARD -- MUST BE ACCOUNTABLE TO THOSE THEY SERVE.

OVER THE LAST DECADE, AMERICA HAS CHANGED THE WORLD. TODAY WE ARE BLESSED WITH THE OPPORTUNITY TO CHANGE AMERICA. WITH THESE PRINCIPLES AS OUR GUIDE, WE WILL MEET THE CHALLENGES, AND EXPLOIT THE OPPORTUNITIES, OF THE WORLD THAT IS NOW BEING BORN.

THANK YOU, AND GOD BLESS THE UNITED STATES OF AMERICA.

# # # #

April 6, 1992

To: Bob Simon

From: John Howard JH x2816

Subject: American Business Conference
Tuesday, April 7, 1992

As we discussed, attached is information from the Department of Justice regarding the "progress" of the product liability and medical malpractice reform legislation over the past years. Our civil justice legislation, The Access the Justice Act of 1992, was introduced on February 4, 1992.

From my experience with ABC, I think that the group would respond favorably to a direct request for assistance. The following may be appropriate for inclusion on page 4 at the end of the first full paragraph (April 3, Draft Three):

> Reforming our legal system will not be easy. But with your help, it can be done. We need ABC members to help us fight the unnecessary lawsuits, the high costs and interminable delays in the system.

As a final comment, the litigation "horror story" that you use is one which would have been brought under the Securities Exchange Act of 1934, most likely SEC Rule 10b-5. Last year in Lampf, the Supreme Court interpreted the 1934 Securities Act to require a 1 year statute of limitations. The Lampf decision resolved years of uncertainty as to the appropriate statute of limitations (some Courts of Appeals had held that the statute was 2 years).

Within a matter of months, a legislative initiative was introduced to reverse Lampf. This proposal, the Bryan Bill, would extend the statute of limitation, and in general, encourage litigation of the type detailed in speech. I am also attaching examples of ABC's efforts to oppose the Bryan bill.

Please let me know if you would like any additional information.

Attachments

FACSIMILE TRANSMISSION

Office of the Assistant Attorney General
Civil Division
U.S. Department of Justice
Washington, D.C. 20530

Fax Number: (202) 514-8071 (Commercial)
368-8071 (FTS)

FROM: Janice Calabresi (Print Name) DATE/TIME: 4/6/92

TELEPHONE NUMBER: 514-3045

TO: John Howard (Print Name)

DESTINATION'S FAX NUMBER: 456-7044

DESTINATION'S VOICE VERIFICATION NUMBER: 456-2816

NUMBER OF PAGES (EXCLUDING COVER SHEET): 5

Message/comments: John-

By all reports over here neither Medical Malpractice nor Product Liability are going anywhere on the hill. They are both stalled. Faith Burton from OLA says no hearings have be held or scheduled--there is substantial resistance from the plaintiff's lobby -- S. 645 a general aviation bill got some hearings last fall and then stalled -- S. 640 the Kasten bill is out of Committee & pending on the Senate Calendar but is unlikely to see any action. Attached is a memo on product liability "progress" that I got from Jeffrey. I'll let you know if I learn any more. -Janice

CROWELL & MORIN
095:rmg
99260.011

MEMORANDUM

TO: Mr. Jeffrey Axelrad, Director - Torts Branch

FROM: Victor E. Schwartz, Esquire

DATE: March 23, 1992

RE: Federal Product Liability Update

Since S.640 was reported out of the Senate Commerce Committee in mid-October, Federal product liability appears to be at a stall. This is true because two of the principal Senate co-sponsors of S.640, Senators Rockefeller and Danforth, have not agreed on a strategy. Senator Rockefeller would prefer to have the Bill proceed "in the normal legislative process" and include a sequential referral to the Judiciary Committee. At one point in time in early December it appeared that the Judiciary Committee would be willing to agree to a referral date of March 15, 1992. Senator Danforth's staff did not accept this apparent offer. At present, Senator Rockefeller has been having discussions with Senator Biden to see if another date can be agreed upon.

Meanwhile, Senator Danforth wants to move the Bill directly to the Floor and offer it as an amendment on "an appropriate" bill. One possibility is the Civil Rights Bill, S.2062. That legislation would end punitive damages "caps" in civil rights actions dealing with sexual harassment. It is a bill sought by consumer groups, women's rights groups, and parts of the liberal element generally not enamored of the Federal Product Liability

Bill. On the other hand, many believe the Bill will pass and will be signed by the President. There is business opposition to S.2062, and the addition of product liability on that legislation would not necessarily kill that opposition.

The bottom line is that I expect Senator Danforth's strategy to be the one that will be pursued. It is likely that S.640 will be offered as an amendment to some legislation prior to the Easter recess.

There are now 37 co-sponsors of the Senate Bill. Senator Pete Domenici (R-NMX) joined as a co-sponsor a couple of weeks ago.

THE "SUBROGATION LIEN" PROBLEM.

As you know, both S.640 and H.R. 3030 eliminate the subrogation lien in workplace product liability cases when an employer has been at fault. The National Federation of Independent Business (NFIB), the principal lobbying group for small business, has opposed that provision in its present form. NFIB has indicated it will move to strike this provision of the Bill if it goes to the Floor and, if they are unsuccessful in that effort, they will oppose the measure as a whole. We have been conducting negotiations to try to bring about a reconciliation within the business community about this particular provision of the Bill. An approach that appears to be acceptable to all sides is to modify the Bill as it now stands. Currently, the Bill requires an employer to prove that he was innocent of fault if he is to retain a subrogation lien. Under the new approach, the

employer would be presumed to be "not at fault," and the manufacturer of the capital good or chemical would have to show that the accident occurred, at least in part, because of employer fault. The product manufacturer would have to bring the employer into the product liability action in order to prove this, although the employer could have the option of saying, "No contest." If the product manufacturer chooses to bring the employer in and fails to show employer fault, under the new approach, the manufacturer would have to pay the employers' reasonable attorneys' fees. Drafts are being exchanged within the business community at this time in regard to this compromise. The NFIB has indicated that if it decides that the new language is to its liking, it will put its full lobbying force behind Federal product liability. NFIB has never done this in the past ten years. In my judgment, NFIB's support could make a significant and favorable difference with respect to the Senate vote on product liability and the possibility of creating some meaningful action in the House.

THE HOUSE.

There has been virtually no movement of the companion bill in the House. There are approximately 150 co-sponsors and that drive has not flourished of late. We are still in a "chicken and egg" situation in the House. Mr. Dingell, a co-sponsor, continues to stress that he is for the legislation and points to the fact that his Committee, Energy and Commerce, approved a more "pro-defense" measure in the 100th Congress by a 30 to 12 vote. Nevertheless,

he does not want to put his "Committee through the ringer again" unless there are signs of life for the Bill in the House Judiciary Committee. As you will recall, the House Product Liability Bill, H.R. 3030, was jointly referred to both the Energy and Commerce and Judiciary Committees. It must be reported out by both Committees if it is to come up for a vote on the Floor. The Danforth Senate strategy cannot work in the House because there are "relevancy rules," and a Member simply cannot tack H.R. 3030 onto other legislation.

There will be showcase hearings on product liability before the Exports, Tax Policy and Special Problems Subcommittee of the House Small Business Committee on April 7. The Chairman of the Full Committee, John LaFalce, has indicated he will attend these hearings. It is also likely that showcase hearings will be held before the Technology and Competitiveness Subcommittee of the Science, Space and Technology Committee of the House. (Representative Valentine, Chair).

The business community has organized a very strong grassroots effort under the aegis of a firm called Direct Impact. They are working to assure that if S.640 hits the Floor, parliamentary devices will be beaten back, and the Bill will receive a favorable vote. It is the view of the various product liability coalitions, and mine also, that if the Bill passes the Senate, very strong pressure will be placed on Mr. Brooks, Chair of the House Judiciary Committee, to hold hearings. Nevertheless, I take very seriously the message given to me by the plaintiffs' bar sometime ago -- that they have Mr. Brooks "locked."

The Administration continues to support Federal product liability reform, and the general issue of liability and judicial process reform has been moved up to one of the key five points of the President's Domestic Policy Program.

If you have any questions, please call.

10-3

Breeden Defends Quayle's Preview Request

By David S. Hilzenrath
Washington Post Staff Writer

Securities and Exchange Commission Chairman Richard C. Breeden said yesterday it was "perfectly appropriate" for Vice President Quayle to request a preview of Breeden's congressional testimony in favor of a bill to give shareholders more time to sue corporations for securities fraud.

"I don't see anything sinister or unusual about their wanting to know what our views are on this issue," Breeden said following his appearance before a Senate subcommittee. Quayle made no effort to change his testimony, and Breeden "didn't move a comma," Breeden said.

Breeden told the Senate Banking subcommittee on securities that the longer statute of limitations the bill would provide is needed to protect the rights of defrauded investors, and he disagreed with arguments that the bill would encourage costly, frivolous lawsuits. A broad array of business groups opposes the bill on those grounds.

Quayle stepped into the fray over the bill Tuesday when he was asked a question about it in an appearance before a group of business executives. "I can assure you that the testimony of Mr. Breeden will be obviously very closely examined and we will make sure that this issue is properly ventilated before he testifies tomorrow," Quayle told the executives Tuesday.

Quayle's comment attracted attention because the SEC, an independent agency, does not answer to the White House.

"The branches of government do need to talk to one another, but I would hope that there would never be a time in which an independent agency would find itself in a situation where what it has to say had to be cleared in advance by any other part of the government," Banking Committee Chairman Donald W. Riegle Jr. (D-Mich.) said at the hearing.

Breeden said that he did not recall the vice president's office ever asking for an advance copy of his testimony before. But he said the SEC has sent advance copies of testimony to other White House offices and government agencies "on many occasions."

Breeden said Quayle's interest in the bill was natural in light of Quayle's concern that excess litigation threatens U.S. economic competitiveness. However, Breeden said the bill "may well result in less litigation, not more, as investors who may have been cheated will not have an incentive to file a hasty lawsuit due to an extremely fast shot clock."

Barry K. Rogstad
President

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MEMORANDUM

To: John Howard & David McIntosh
From: Barry Rogstad
Date: October 17, 1991

During our conversation last week, I promised to send you both the attached. It was prepared for a business coalition of which ABC is a member. The purpose of the coalition is to evolve proposals for combatting unwarranted litigation under SEC Rule 10b-5. Rule 10b-5 covers rights of action in cases of securities fraud.

If Congress adopts a proposal sponsored by Senator Bryan to broaden the statute of limitations beyond the standard set by the Supreme Court in the Lampf decision, it has an equal responsibility to see that such legislation carries solid reforms to counter the explosion in frivolous suits brought under 10b-5. This paper offers some suggestions to that end. Much of it was inspired by the very good work done by the President's Council on Competitiveness.

Absent a commitment to reform, the Bryan Amendment and similar legislation in the House, should be defeated.

I am very interested to know your current thinking in this matter. ABC wants to do more than simply carry water for the coalition: we are with you for the long-term in reforming the litigation system.

Barry

Measures To Combat Unwarranted 10b-5 Litigation

There is clear evidence that the implied right of action for violations of SEC Rule 10b-5 is not functioning as an effective remedy for securities fraud. The system of litigation spawned by this provision (which was established piecemeal by the courts and has never been examined on a comprehensive basis by Congress) neither channels benefits to investors actually injured by securities fraud nor focuses the burdens of litigation and liability for damages upon those who engage in fraudulent activities. Recent empirical studies of 10b-5 class actions have shown that virtually all claims -- meritorious and frivolous -- are treated alike. These actions are almost always settled -- in contrast to a settlement rate of approximately 60% for civil actions generally -- and in amounts bearing no relation to the merits of the underlying claim but linked only to the amount of damages sought in the complaint or the extent of the defendants' insurance coverage. See Alexander, Do the Merits Matter? A Study of Settlements in Securities Class Actions, 43 Stan. L. Rev. 497 (1991); O'Brien, The Class-Action Shakedown Racket, Wall St. J., Sept. 10, 1991. Thus, plaintiffs who have suffered genuine injury are not getting the compensation they deserve while plaintiffs who have brought unjustified lawsuits are receiving a windfall. And defendants who have not engaged in any wrongdoing are in effect forced to bear costs that should be paid by true fraud-doers.

The basic problem with the current system is that it imposes coercive pressure on defendants to enter into settlements in every case, even those in which the defendants have a strong defense on the merits. The system fails to distinguish efficiently between meritorious and unjustified claims at an early stage of the litigation, thereby forcing defendants to shoulder enormous costs in terms of attorneys' fees and disruption of business if they wish to defend the lawsuit. Even if the defendant ultimately prevails, he must absorb these costs. For these reasons, plaintiffs (and the plaintiffs' lawyers who actually control much of this litigation) have no incentive to focus their efforts on meritorious claims: they are assured of essentially the same recovery regardless of the actual strength of their position.

Reform of the 10b-5 system should focus on the foregoing considerations. Plaintiffs and their lawyers must be provided with incentives to concentrate their efforts on meritorious claims; defendants must be given incentives to fight unjustified claims and settle only meritorious ones; and the litigation system must be restructured to make possible, at least in some cases, early termination of unwarranted claims. The following reform measures will accomplish these goals.

- **Proportionate Liability**

Under the current 10b-5 system, a defendant may be forced to compensate the plaintiff for all of the damage that the plaintiff suffered, even where other parties bear the lion's share of the responsibility for the injury. A proportionate liability standard would require each defendant to compensate the plaintiff based on his own responsibility for the plaintiff's injury. That result is justified by basic fairness: a defendant would be liable for his share of the injury and no more. Especially in securities fraud actions, where some of the parties most frequently named as defendants -- such as accountants and underwriters -- typically are alleged to be liable not because they committed the basic fraud but only because they failed to uncover wrongdoing by others, it is grossly unfair to require comparatively nonculpable parties to shoulder the burden of the entire liability.

A proportionate liability rule would be a large step toward righting the skewed incentives in the current system. For example, in the typical action in which a number of defendants are named in the complaint, there is now considerable incentive to settle quickly because a defendant that does not settle may find himself faced with the possibility that -- if he loses at trial -- he will have to bear much more than his share of the damages. This potential doubling or tripling (or more) of the stakes in the litigation -- which is exploited by plaintiffs' lawyers who play the defendants off against each other in an effort to obtain quick settlements -- is a tremendous deterrent to defending on the merits even for completely blameless defendants. A proportionate liability rule would eliminate this means of pressuring defendants regardless of the merits of the case, and therefore would focus settlement activity on cases in which the plaintiffs deserve compensation because they have valid claims.

- **"Loser Pays" Rule For Attorneys' Fees**

Another significant problem with the current system is that the initiation of a lawsuit is essentially cost free to the plaintiffs and their attorneys. The most significant burden in 10b-5 actions -- responding to discovery demands -- falls almost exclusively on defendants because facts within the knowledge of the particular plaintiff usually bear little relevance to the issues in the litigation. (The courts have essentially eliminated the requirement that plaintiffs prove that they actually relied on the alleged misrepresentation or omission.) Because he must bear these tremendous costs, the defendant has an interest in settling the case regardless of the underlying merits. This, in turn, eliminates any incentive for plaintiffs' attorneys to carefully screen the cases that they file.

Providing that the party who loses the case must pay the winner's attorneys' fees will give plaintiffs' attorneys an incentive to file only those cases in which the claim appears to have merit. (To ensure that the parties could recover any fees eventually awarded, the court could require the posting of a bond (as in Section 11(e) of the Securities Act, 15 U.S.C. § 77k) or award fees against both the party and its attorneys.) As the President's Council on Competitiveness observed in its recent report, "[b]ecause the losing party will be obligated to pay the winner's fees, this approach will encourage litigants to evaluate carefully the merits of their cases before initiating a frivolous claim or adopting a spurious defense." Plaintiffs who institute meritorious claims will obtain a greater recovery (because they will be awarded attorneys' fees as well), thereby providing an additional incentive for such cases to be brought. And defendants will have an incentive to fight unjustified claims because they will be able to recover their attorneys' fees.

- Discovery Reform

The President's Council on Competitiveness found that "[p]retrial discovery is frequently the source of needless delay and expense. Currently litigants have virtually unlimited ability to take sworn deposition of witnesses, request documents and submit written questions to parties." These abuses are particularly prevalent in 10b-5 litigation. In such cases, unlike most civil litigation, plaintiffs frequently can interrupt the schedules of the highest executives in a company, forcing them to spend their time on wholly unproductive matters. The fishing expeditions permitted under the present rules often serve as means for pressuring defendants to enter into settlements and, in addition, for delaying resolution of the case on the merits. See Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 741 (1975).

Limitations on discovery along the lines suggested by the Council on Competitiveness and the Judicial Conference Advisory Committee on Civil Rules (see 137 F.R.D. 53) would eliminate these problems. Parties would be required to disclose certain "core" information regarding locations of relevant documents and individuals with knowledge of the matters at issue. The amount of discovery would be subject to presumptive quantitative limits, which could be exceeded only with approval of the court. In addition, discovery should be staged to allow defendants to determine whether the plaintiff has complied with Rule 11 of the Federal Rules of Civil Procedure (which prohibits the filing of baseless claims) and to allow plaintiffs to inquire into the relevant facts on a systematic basis. Regardless of whether these proposals are later adopted for a wider range of lawsuits, they are essential now to eliminate the especially coercive effect on defendants of present-day 10b-5 litigation.

- **Curbs On Litigation Abuses**

A number of practices unique to 10b-5 litigation are so clearly abusive that correction is plainly warranted. First, the current system of paying "bounties" to individuals who serve as "representative plaintiffs" in class actions should be abolished. Such payments provide a perverse incentive for individuals to become professional plaintiffs by buying a few shares of stock in many companies and joining forces with class action attorneys whenever the stock of one of those companies falls by enough to make a lawsuit economically worthwhile to the attorneys. See Coffee, Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions, 86 Colum. L. Rev. 669, 682 & n.38 (1986). Frivolous litigation will be discouraged by prohibiting representative plaintiffs from receiving more than their pro rata share of settlements. At the same time, this reform would make more of the settlement pool or final judgment available for all investors.

Second, Congress should reaffirm that attorneys may not act as counsel in cases in which they have a financial interest. Some law firms reportedly invest their own profit-sharing plans broadly in the stock of numerous companies in order to have an in-house plaintiff on hand in the event they wish to file a 10b-5 action against these companies. See Coffee, supra, 86 Colum. L. Rev. at 682. These attorney-class representatives have a built-in conflict of interest because they have much more to gain from a settlement (which comes with a guaranteed attorneys' fee) than from taking the case to trial. This conflict situation should be prohibited.

Third, class action attorneys should not be permitted to pay stockbrokers "forwarding fees" for referring their customers to attorneys bringing class action suits. This practice already is forbidden as a matter of professional ethics, but it apparently continues nonetheless. See Coffee, supra, 86 Colum. at 682-683. Prohibiting this practice by statute (and providing for substantial penalties -- such as disqualification as class counsel -- for violations) should help reduce the amount of collusive, meritless litigation.

Fourth, the SEC has authority to obtain disgorgement relief in the context of administrative actions for violations of Rule 10b-5. See 15 U.S.C. §§ 78u-2(e) & 78u-3(e). These disgorgement funds are then made available to investors injured by the violations. A controversy apparently has arisen in connection with two aspects of the disgorgement process: whether private attorneys may be paid with the disgorgement funds and whether payments from the disgorgement funds must be credited against any possible recovery by the same individual in private litigation under Rule 10b-5 and other provisions of the securities laws. Congress should preserve such recoveries for investors and affirm that private lawyers are not entitled to any of these funds -- which were recovered solely

through the efforts of the SEC. Congress also should protect defendants against potential double liability by making clear that any payments to plaintiffs from these funds will offset future awards in 10b-5 actions growing out of the same alleged misconduct.

- **Clear Proof Of Violation**

The area covered by 10b-5 actions -- identifying and trying to ensure the accuracy of information disclosed about a company -- is peculiarly vulnerable to second-guessing. Evaluating and describing the economic prospects and condition of a company is an extremely difficult task. With the benefit of hindsight, plaintiffs usually are able to find some statement that did not turn out to be correct or some statement that should have been made to provide full disclosure. Rule 10b-5 is supposed to be an anti-fraud rule, however, and proof of scienter -- that the defendant acted with fraudulent intent -- is the key factor that distinguishes between investors who are victims of fraud and investors who are merely disgruntled because their investment did not turn out as expected.

Because of the inherent danger of second-guessing in this type of litigation, it is imperative that juries be certain that defendants in fact engaged in fraud before imposing liability. At common law, courts required proof of fraud by "clear and convincing evidence." The same standard should apply to 10b-5 actions.

- **Pleading Reform**

Rule 9(b) of the Federal Rules of Civil Procedure states that "[i]n all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally." Several courts have recognized that, due to the special dangers of unjustified 10b-5 actions, this standard must be enforced vigorously. Those courts hold that "[a]lthough states of mind may be pleaded generally, the 'circumstances' must be pleaded in detail"; the plaintiff must "point to some facts suggesting that" the defendant acted with the requisite state of mind (which the courts have held to be knowledge of the falsity of the allegedly deceptive statement or extreme recklessness with respect to the statement's truth or falsity). See, e.g., Robin v. Arthur Young & Co., 915 F.2d 1120, 1127 (7th Cir. 1990); DiLeo v. Ernst & Young, 901 F.2d 624, 627 (7th Cir. 1990); Stern v. Leucadia National Corp., 844 F.2d 997, 1004 (2d Cir.), cert. denied, 109 S. Ct. 137 (1988).

This pleading requirement should be codified for 10b-5 actions. It would prevent plaintiffs from simply pointing to a downturn in a company's fortunes and contending that the difference

between the earlier, favorable performance and the more recent, less favorable condition is attributable to fraud. "Because only a fraction of financial deteriorations reflects fraud, plaintiffs may not proffer the different financial statements and rest. Investors must point to some facts suggesting that the difference is attributable to fraud." DiLeo, 910 F.2d at 627. Such a requirement would discourage unwarranted lawsuits and, in addition, provide defendants with a means for cutting off such lawsuits at an early stage in the litigation process.

- **Clarify Principles For Aiding And Abetting Liability**

Some courts have concluded that defendants may be held liable under Rule 10b-5 for "aiding and abetting" another defendant's violation of the provision. The typical scenario involves a claim against an attorney, accountant, underwriter or other professional for failure to "blow the whistle" on a misrepresentation made by another party. The parameters of this form of liability are at best murky; indeed, the Supreme Court has never even considered whether aiding and abetting liability is permissible. Plaintiffs' attorneys frequently try to use this theory to avoid the requirements that apply to 10b-5 actions generally. The confusion about the existence and scope of aiding and abetting liability leads to both unnecessary litigation and settlements by defendants fearful of unjustified liability.

Congress should affirm that even if a plaintiff proceeds on an aiding and abetting theory, he must prove that the defendant acted with scienter -- that he knew of the misrepresentation by the third party and intended to assist the third party in deceiving the plaintiff. Rule 10b-5 is a fraud remedy, and proof of fraud should therefore be required in all circumstances.

ANOTHER PROPOSAL TO KILL OFF JOBS

If you wonder why entrepreneurs sometimes feel abandoned by Washington lawmakers, take a close look at a legislative proposal likely to receive action very soon.

An amendment to the Senate banking bill (S. 543) would go a long way to protect the one industry in which America has achieved undisputed world leadership: the manufacture of lawsuits.

The amendment seeks to legislate a reversal of a recent Supreme Court ruling concerning private actions under the securities laws.

Although the amendment's author intends to protect investors who are victims of fraud, the amendment's net effect will be to declare open season on small companies that can't afford the management time or the heavy costs of defending predatory or frivolous suits.

Small and medium-sized businesses can literally be ruined by costly and time-consuming suits that have no merit. They don't ask for protection against such suits, they only ask for fairness.

If Congress feels compelled to reverse the Supreme Court through new legislation, at least write the bill so only legitimate victims of securities fraud will benefit.

Here's all business owners ask:

1. Limit the incentives for predatory trial lawyers and professional plaintiffs who might sue in search on an up front settlement despite the merits of the allegation.

2. Prohibit attorneys from paying "finders fees" or "bounties" to induce potential plaintiffs to sue.

3. Require the loser to pay attorneys' fees.

4. Place reasonable time and cost limits on pretrial discovery.

5. Target actual wrongdoers by establishing a proportionate liability rule.

America's entrepreneurs are not looking for special treatment. They only ask us not to burden them with counterproductive disincentives that make it impossible to be competitive in an already difficult economic environment.

AmericanBusinessConference

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BACKGROUND: THE BRYAN AMENDMENT TO S. 543

Senator Bryan's amendment to the banking bill proposes to rewrite the Supreme Court's decision in Lampf et al which established a uniform statute of limitations for private actions under the Securities Exchange Act of 1934. Senator Bryan's legislation would loosen the statute of limitations established by the Court while removing any "due diligence" requirement on the part of investors.

The American Business Conference vigorously oppose the Bryan Amendment. ABC firms have long been bedeviled by frivolous suits brought by unscrupulous lawyers and their professional plaintiffs. High-growth companies are especially attractive to these modern-day ambulance chasers because their stock typically sells at a price many times greater than earnings. Obviously these high P/E multiples are attractive to investors; at the same time such stocks can be subject to severe fluctuations in price. It is all too easy for lawyers to convince disappointed investors that they are the victims of fraud rather than risk. The Dickensian nightmare that is our current civil justice system allows the lawyers to force target companies to settle regardless of the merits of the case.

ABC members believe that any changes in the statute of limitations should be accompanied by reform of the litigation system. Proportionate liability, the "loser pays" principle for attorney's fees, limits on the time and expense associated with discovery, requiring "clear and convincing" evidence of fraud, and limits on abuses like attorney payment of finders fees and bounties to identify and recruit potential plaintiffs are all steps that can help.

If Congress wants to rewrite the Lampf decision, it should do so only after careful consideration and only in the context of enacting reforms to eliminate frivolous suits.

Technology firms have volatile earnings. Lawyers have figured out how to get fat off this fact of life.

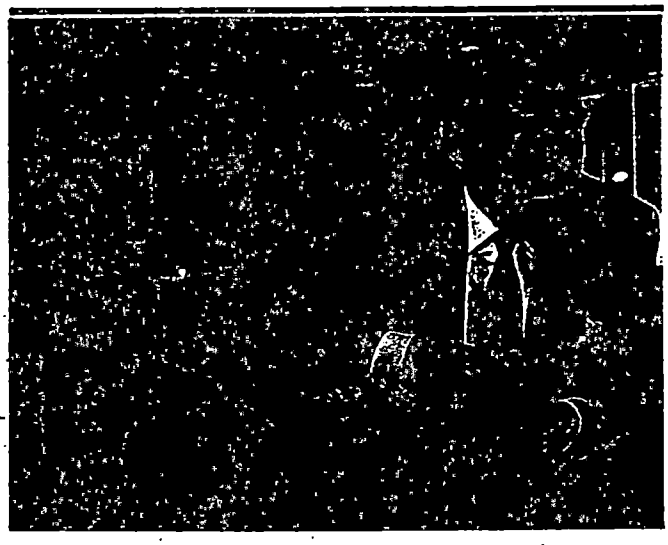
Shakedown?

By William Tucker

WHEN A Silicon Valley company issues an unexpected change in earnings, the race is on to the San Jose or San Francisco Federal Court House.

Earnings less than anticipated? The company is served with a class suit for failing to tell shareholders the bad news. Earnings better than expected? A company may be sued for withholding the good news that would have prevented impatient shareholders from unloading.

More than 98% of the suits are settled without trial, according to Newman. The officers and directors agree to pay money to the class of disaffected shareholders the attorneys represent. The lawyers typically get 30% of the settlement. The insurance company pays, but the cost of insurance is just one more burden on the sometimes struggling businesses. If a firm has gone bankrupt, the plaintiffs are still eligible to collect from the insurance company, and they also pursue claims against the accountants, lawyers and underwriters who worked with the defendant.



Melvyn Weiss, dean of the plaintiff's bar **"We're doing what the SEC doesn't have time to do."**

"Shareholders' suits have become a sport in Silicon Valley," says Melvin Goldman, a San Francisco attorney who represents corporate defendants. "They take every unexpected movement of a stock and try to call it fraud. High-tech companies are volatile, so they're easy game."

At any one moment, there are about 500 to 700 shareholder suits outstanding across the country, according to James Newman, editor of *Securities Class Action Alert* in Cresskill, N.J. Milberg Weiss Bershad Specthrie & Lerach, of New York and San Diego, is the most active firm in this bustling industry. Milberg Weiss has over 150 active suits all by itself.

Typical case: Lawyers sue Verbatim Corp., a floppy disk manufacturer, when its stock drops more than $2 a share at the end of 1983. Six years later, after the defendants have spent almost $2 million on legal fees, the case is settled: a $4.3 million recovery for investors who bought the stock between June 1983 and January 1984 of which plaintiff lawyers pocket $1.5 million in fees and costs.

"It's legalized extortion," complains Alan Shugart, chief executive of Seagate Technology, a disk drive firm that has been sued by 13 different plaintiffs. "They know how expensive it is for us to take our case to court. We're supposed to give them a few million dollars so they'll go away."

In 1988, after a jury ruled for defendants in a case against Nucorp Energy Inc., Silicon Valley executives were beginning to think they might not have to make such payoffs in the future. But on May 30 a San Jose Federal jury returned a $100 million verdict against A.C. (Mike) Markkula, a cofounder and vice chairman of Apple, and John Vennard, a former vice president. Markkula and Vennard had been responsible for optimistic statements in the fall of 1982 about Apple's Twiggy disk drive at a time when corporate records showed Twiggy mechanisms to be failing. When Apple finally abandoned Twiggy in September 1983, its stock opened down $8 a share the next day. The jury attributed $2.90 of this loss to misrepresentation on the part of the officers.

Melvyn I. Weiss, founding partner of Milberg Weiss, argues that his firm and others like it are helping keep business honest: "We're doing the job that the SEC doesn't have the time or the resources to do."

Weiss says his firm has recovered $2.5 billion for aggrieved shareholders. But Joseph Grundfest, former Securities & Exchange Commissioner and now a Stanford Law School professor, takes issue with the notion that these victories amount to a great public service. Grundfest says: "There is no question that there are instances of outright fraud and that directors and officers should be made to pay compensation in some cases. But in many cases, perfectly honest people are being forced to pay outrageous sums, simply because they didn't have perfect foresight.

"These cases fail to make clear that, while some buyers and sellers lost money through market movements, the winners are other buyers and sellers, not necessarily the corporation or its current shareholders."

Actually, you can make a case that the losers are the American people, since these suits and settlements become a kind of tax on American businesses trying to survive in a tough industry and a tough world.

MAJOR BUSH ADMINISTRATION TRADE INITIATIVES

The Bush Administration has for the past three years deployed a three-prong strategy to open markets and expand trade throughout the world for U.S. goods, services, and agriculture:

- First, we are working to achieve a successful conclusion of the Uruguay Round of global trade talks, held under the auspices of the General Agreement on Tariffs and Trade (GATT);

- Second, we are launching broad-based, market-opening negotiations with our key trading partners; and

- Third, we are using the strength of our domestic market to open specific sectors in foreign markets.

The Uruguay Round

The Uruguay Round of global trade talks is being held under the auspices of the General Agreement on Tariffs and Trade in Geneva. 108 countries, representing more than 90 percent of world trade, are working to:

- Reduce tariffs and non-tariff barriers by a third, thereby pumping $5 trillion into the global economy over the next decade. The U.S. share of this increased output would be well over $1 trillion, which would be like writing a check for $17,000 to every American family of four, payable over 10 years;

- Cut the $60 billion lost annually through theft and counterfeiting of America's patents, copyrights, and trade marks -- our best ideas;

- Create new export opportunities for America's service industries -- like construction, accounting, and insurance -- which export $115 billion annually and create 9-out-of-10 new jobs;

- Increase opportunities for international investment, which generates more than $240 billion of U.S. exports, or two-thirds of total U.S. exports in goods;

- Expand trade for U.S. farmers, already the world's most productive with more than $40 billion in annual exports.

- Ensure the full participation of developing countries in the global trading system, which could increase U.S. exports by half between now and the year 2000.

North American Free Trade Agreement (NAFTA)

The reasons for our interest in a North American Free Trade Agreement are plain: Canada is our largest trading partner; Mexico is our third largest trading partner. Linking our complementary economies through free trade will strengthen these economic bonds and increase regional political stability.

The North American Free Trade Agreement will create one of the world's largest markets with 360 million producers and consumers and $6 trillion in annual output and so generate new opportunities and new jobs for America.

- Already we have seen the benefits of liberalizing trade with Mexico. Since 1986, when Mexico joined the General Agreement on Tariffs and Trade, and reduced its tariff protections from 100 percent to a high of 20 percent, U.S. exports to Mexico have more than doubled, rising from $12.4 billion to an annualized rate of $28.4 billion in 1990. This doubling of U.S. exports created 264,000 U.S. jobs.

- Today, our exports to Mexico are growing twice as fast as compared with our exports to the rest of the world. Mexico buys a full 35 percent more from us per person than does the far more affluent European Community.

- A free trade agreement in North America would not only lock in these gains, but also create new openings for U.S. industry. The agreement will improve access for U.S. exports to a market which is expected to have 100 million Mexican consumers by the year 2000.

The Enterprise for the Americas Initiative

The Bush Administration has been more active and successful than any previous Administration in opening markets for U.S. goods, services, investment, and encourage market-oriented

economic reform in Latin America and the Caribbean. Our major economic policy effort is the President's Enterprise for the Americas Initiative (EAI) launched in June 1990. The EAI contains three elements, investment, debt, and trade.

The trade element of the EAI envisions a hemispheric zone of free trade stretching from Alaska to Argentina that would generate new economic activity and increased prosperity throughout the hemisphere and at home.

- The groundwork for this hemispheric free trade area has been laid by 15 trade and investment framework agreements designed to encourage additional market opening for U.S. firms have been negotiated with all but 3 Latin American and Caribbean countries (a total of 30 countries, excluding Mexico). These agreements contain a declaration of sound trade and investment principles, a commitment to consult on a regular basis, and an initial agenda for our consultations.

The EAI is designed to encourage the dramatic transformation ongoing in Latin America and Caribbean towards open economies, free trade, and a more limited role for government in the economy. Virtually every significant economy in the region has reduced barriers to trade and investment, including in some cases significant reductions in tariffs and previously rigid import licensing and quantitative restrictions.

Total U.S. exports to Latin America and the Caribbean (excluding Mexico) have risen from almost $31 billion in 1986 and have risen to $53 billion in 1990, including an increase of $10 billion from 1988 to 1990 alone.

Trade with Japan

Our negotiations with Japan are designed to open the world's second largest market economy to U.S. exports. The Bush Administration is working to open the Japanese market by eliminating barriers to in specific sectors using our trade laws and other means, and by lowering structural barriers through the Structural Impediments Initiative (SII). This policy is working:

- Since 1988, U.S. merchandise exports to Japan have risen by an astounding 30 percent to $49 billion.

- Since the Bush Administration took office, U.S. merchandise exports to Japan have grown 50 percent faster than U.S. exports to the rest of the world. As a result, American exports to Japan in 1990 were

greater than our exports to West Germany, France and Italy combined. In fact, our exports to Japan are about 35 percent greater on a per capita basis than our exports to all of Europe.

- In manufactures, U.S. export growth since 1988 has been particularly strong to Japan: up 45 percent to $30.1 billion in 1990.

We are encouraged by the fact our exports to Japan are growing. But there is still much work to be done. The Bush Administration is working to reinvigorate the SII process and on a number of bilateral issues.

# # #

FACSIMILE COVER SHEET

OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE CHIEF TEXTILE NEGOTIATOR

Executive Office of the President
Washington, D.C. 20506

Date 4/6/92

Number of Pages Excluding Cover 3

TO:	AGENCY:	PHONE #:	FAX #:
Andy Feldman	White House Communications	( ) 2930	( ) 6218
		( )	( )
		( )	( )
		( )	( )
		( )	( )
		( )	( )

FROM: AMBASSADOR RONALD J. SORINI
PHONE: (202) 395-3026 FAX #: (202) 395-5639

CONTACT: David Walters

SUBJECT: As per Telcon

Andy, Amb. Hills has never used these stats nor has CEA signed off. That said, this were I came out on condensing the $1.1 trillion into an employment effect. David Walker

What does the Uruguay Round Mean for U.S. Jobs and Wages: An Extension of the USTR/CEA Analysis on the GNP Gains from The Uruguay Round

Summary

The Uruguay Round is likely to benefit U.S. labor both through increased average real wages (resulting from higher productivity) and some increase in U.S. net employment. How the gain would be divided between higher wages and more jobs is unknown. Using the USTR/CEA estimates of potential GNP gains from the UR and a plausible outlook for the growth of the U.S. labor force, it is possible to deduce the following two limiting cases:

1) If all the GNP gain is reflected as higher labor productivity, the average U.S. worker ten years after the Round would produce annually $1,655 (at 1989 purchasing power) more output if the UR is successful than if it is unsuccessful.

2) If, instead, all the GNP gain is reflected as higher employment (with no productivity gains), 10 years hence there would be 4 million more Americans employed with a successful UR than without.

The actual outcome, based on the USTR/CEA trade gain estimates, will certainly be some combination of higher productivity/wages and more jobs within the limits for each described above.

The Joint USTR/CEA Estimated of the UR Benefits to U.S. GNP

In the fall of 1990, USTR and CEA jointly developed a scenario intended to illustrate the type and magnitude of benefit the United States might expect from the Uruguay Round. The Uruguay Round was assumed to achieve a one-third reduction in global barriers to trade.

The Round was assumed to conclude in 1990. The assessment considered the positive impact on U.S. GNP from both static and dynamic gains from trade over the 10 years: 1990 to 2000. All values were calculated in constant 1989 dollars.

The baseline scenario (no Uruguay Round) adopted the then Administration long-term economic forecast for U.S. GNP growth of 3 percent. Baseline GNP thus rose from $5,356.8 billion in 1990 to $7,199.1 billion in 2000.

With trade gains from the Uruguay Round (described in attachment dated 10/17/90), the U.S. GNP was estimated to rise to $7,417.7 billion in 2000. Cumulatively over the ten years, the U.S. GNP

gain totalled $1,116.2 billion. In the tenth year of the analysis (2000), the U.S. GNP with a successful Round was estimated to be $218.6 billion or 3 percent higher than in the absence of the Round.

Implications of the UR Estimates for U.S. Labor

With respect to U.S. employment, the additional $218.6 billion in U.S. output in 2000 would be reflected in some combination of two effects:

- o an increase in U.S. average labor productivity (output per hour worked); and
- o an increase in total employment.

There are many elements which would have to be taken into consideration in order to judge how much of the trade gain would be reflected in higher U.S. productivity and how much in increased net employment. Either way, however, U.S. labor benefits -- either through higher wages (the counterpart higher productivity) or more jobs.

The USTR/CEA exercise was intended as no more than a plausible scenario of the type of gains that could be expected from a one-third cut in global trade barriers. Attempting to predict the productivity versus job benefits implicit in the USTR/CEA scenario is, in fact, not necessary for illustrating the type of gains to U.S. labor likely to accrue from a successful Round. Instead, the USTR/CEA scenario can be extended to the labor market to estimate two limiting cases: 1) all the labor gains reflected as productivity increase and 2) all the labor gains reflected as employment increase. The most likely outcome, of course, would be somewhere between these two extremes.

Employment in the United States totaled 119.55 million in 1990. The U.S. labor force and employment grew at roughly a 1.7 percent average annual rate in the 1980s. This rate is widely expected to slow down in the 1990s. The baseline scenario assumes a 1 percent average annual growth rate in employment from 1990 to 2000 which, together with a 2 percent productivity growth rate, would achieve the base line forecast of 3 percent average annual GNP growth. Employment reaches 132.057 million in 2000 for the baseline scenario.

If all the UR gain is expressed in terms of productivity, U.S. net employment does not rise, but output per worker (assuming constant hours worked across the period) rises from $54,515 in the base line to $56,170 with a successful UR. This is a 3 percent or $1,655 average increase for all U.S. workers in the year 2000.

If, on the other hand, gains from the UR were entirely reflected in increased U.S. employment (with no productivity gain), there would be nearly 4 million additional persons employed in the U.S. in the year 2000. Employment would rise to 136.056 million, an increase of 3 percent or 3.999 million workers.

attachment

THE WHITE HOUSE

WASHINGTON

April 7, 1992

MEMORANDUM FOR DAVID DEMAREST
DAN McGROARTY
SPEECHWRITERS
RESEARCHERS

FROM: BOB SIMON

SUBJECT: AMERICAN BUSINESS CONFERENCE SPEECH

This was an odd little event that went surprisingly well. Eighty CEOs were seated in the Willard's ballroom. Once the pool arrived, reporters almost had the audience outnumbered.

The President looked great and sounded great, even though he had to plow through 25 minutes of the Five Pillars for the umpteenth time. His delivery was quite strong and confident, and he did not lose interest, even though the small audience only applauded three times (on legal reform, private school choice, and that all-time fave -- cap. gains). Furthermore, the President sounded like he really believed in what he was saying -- that governmental change is essential for business growth.

All in all, it was a thoughtful address which could get some favorable press even though there was no news in it.

Since we were just across the street at the Willard, the President got a big laugh when he announced his new travel policy: "no trips farther than one block from the White House." (Well, it was just a medium chuckle, but hey -- I wrote it, OK?)

AMERICAN BUSINESS CONFERENCE
Tuesday, April 7, 1992

Gloria Bohan
President
Omega World Travel, Inc.
Falls Church, Virginia

John S. Chalsty
President & C.E.O.
Donaldson, Lufkin & Jenrette
New York, New York

James R. Jones
Chairman, American Business Conference
Chairman, American Stock Exchange
New York, New York

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Chairman & C.E.O.
Pinkerton Security and Investigation Services
Van Nuys, California

AMERICAN BUSINESS CONFERENCE

Tuesday, April 7, 1992

"Capital Gains, Economic Growth, and Jobs"

J.P. Barger
Chairman & C.E.O.
Dynatech Corporation
Burlington, Massachusetts

W.L. Lyons Brown, Jr.
Chairman & C.E.O.
Brown-Forman Corporation
Louisville, Kentucky

James R. Jones
Chairman, American Business Conference
Chairman, American Stock Exchange
New York, New York

George N. Hatsopoulos
Chairman & President
Thermo Electron Corporation
Waltham, Massachusetts

Barry K. Rogstad
President
American Business Conference
Washington, D.C.

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APRIL 6-8, 1992

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Albertine Enterprises, Inc.
Washington, DC

John Ballard
President & C.E.O.
TCI International
Fremont, CA

J. P. Barger
Chairman & C.E.O.
Dynatech Corporation
Burlington, MA

Bim Black
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Teleflex Incorporated
Plymouth Meeting, PA

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Omega World Travel, Inc.
Falls Church, VA

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Chairman & C.E.O.
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Fort Smith, AR

Jim Brocksmith
Deputy Chairman
KPMG Peat Marwick
New York, NY

John Brown
Chairman, President & C.E.O.
Stryker Corporation
Kalamazoo, MI

Lee Brown
Chairman & C.E.O.
Brown-Forman Corporation
Louisville, KY

John Chalsty
President & C.E.O.
Donaldson, Lufkin & Jenrette
New York, NY

Bob Chilton
Chilton Investments
Dallas, TX

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Chairman, President & C.E.O.
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Barrie Damson
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Fruit of the Loom, Inc.
Chicago, IL

Walter Forbes
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CUC International Inc.
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Jerry Ford
C.E.O.
United New Mexico Financial Corp.
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Lynn Fritz
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Fritz Companies, Inc.
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Tech-Sym Corporation
Houston, TX

Fred Gerstell
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Los Angeles, CA

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Baltimore, MD

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New York, NY

Howard Solomon
President & C.E.O.
Forest Laboratories, Inc.
New York, NY

Michael D. Sullivan
President & C.E.O.
Merry-Go-Round Enterprises, Inc.
Joppa, MD

Lillian Vernon
Founder, C.E.O. & Chairman
Lillian Vernon Corporation
Mt. Vernon, NY

Tom Wathen
Chairman & C.E.O.
Pinkerton Security & Investigation Services
Van Nuys, CA

Larry Weinbach
Managing Partner-Chief Executive
Arthur Andersen & Co.
New York, NY

Stanley A. Weiss
Chairman & C.E.O.
American Premier, Inc.
Washington, DC

Hall Wendel
Chairman & C.E.O.
Polaris Industries, L.P.
Minneapolis, MN

Kelley Williams
Chairman & C.E.O.
First Mississippi Corporation
Jackson, MS

Angus Wurtele
Chairman & C.E.O.
The Valspar Corporation
Minneapolis, MN

Phil Zeidman
Brownstein Zeidman and Lore
Washington, DC

To speechwriters *

April 5, 1992

On liability reform

we need to show that we have been trying to bring about the **change** by getting legislation passed. Need a couple of sentences about what we have been trying to get done on the hill. For example:

On _ '90 I send legislation to hill..same thing in 91 and again in 92... Get the facts,show that we've been trying but congress unwilling to even bring for a vote (if that is correct).

Page 5- Health Care.... work in some language on the cost of frivolous mal practice suits... (I have used estimates $20-$40 **billion.** Double check).

I need ABC's help.

On trade section (top of p.6) we **must** mention NAFTA. Mexico by name.

On Page 7 I have noted a **"B"**. In there insert some language on drug-free environment. We must mention drugs free schools, or drug free work place all along the line. We do not have anti narcotics as one of our five categories and it is essential that we keep supporting our anti drug programs...

On Congress reform refer in one sentence to the number of specific reforms I have proposed for Congress. May not have to list them all but audience must know that we're not just carping-rather seriously **proposing answers.**

(Ferguson/Simon)
April 5, 1992
Draft Three

PRESIDENTIAL REMARKS: AMERICAN BUSINESS CONFERENCE
WILLARD HOTEL
TUESDAY, APRIL 7, 1992
2:00 PM

Thank you, Jim Jones. ((Some people say I've been traveling too much. So today is an example of my new policy: no trips farther than one block.))

It is always a pleasure to speak with members of the American Business Conference, because it is always a pleasure to speak with the best.

I would like to talk to you today about the future -- the future of our country generally, and more particularly the future of our country's business environment. In fact, we cannot separate the two. The America of the 21st Century -- its ability to make peace in the world, to foster strong families, to create rewarding jobs -- will be shaped today, in large part by how hospitable we make America for business.

We can learn from your achievement. The key to the success of any high-growth company is the wise deployment of resources. The successful company channels labor and investment into those areas with the potential for the greatest expansion and the highest return. You take the risk; you reap the reward; everyone, meanwhile, benefits from the wealth you create.

That, in brief, is the genius of entrepreneurial capitalism, a system that has made America the envy of the world. For 200 years our prosperity has sprung from our ability to innovate, to change as the world changes. But America's world leadership is

not automatic; it is not a birthright. We must continue to earn it, day by day, quarter by quarter, year by year. The world now is changing at a pace no one could have dreamed of a generation ago. And America, which has led the world's transformation, must change with it.

Over the last several years deadweights have begun to slow the engine of growth -- inefficiencies a competitive economy cannot tolerate. Today I want to discuss five areas of reform, five critical ways in which America must change if we are to continue to lead the world. You understand the urgency, for each of these problems presents itself to American companies not as an abstraction but in the most immediate way: as a cost of doing business -- a cost you can't control, an expenditure with no possible return.

When our legal system becomes incapable of resolving disputes in a timely and civil manner, business loses the incentive to innovate and take risks. When health care costs escalate, business picks up much of the tab. When government imposes barriers to trade, business pays the price in opportunities lost. When our children leave school without rudimentary skills, business bears the burden in lowered productivity. And when government freezes in gridlock, business can no longer plan rationally for the future.

Let me begin with the crying need to reform our country's civil justice system. Every American has heard the stories of bizarre or frivolous lawsuits; but most of you have lived them,

tales that could have been torn from the pages of Kafka. Consider one example, related by one of your members, Roger Coleman, president of Rykoff-Sexton, a food manufacturer and distributor.

After record earnings in 1989, Mr. Coleman publicly expressed his confidence that 1990 would be even better. When earnings fell short, his hopeful statement became the cause of a shareholder class-action lawsuit.

First came a meeting with plaintiffs' contingency-fee lawyers, at which the merits of the case were never even discussed. "The issue," says Mr. Coleman, "was the depths of our pockets." Next came the nightmare of discovery: endlessly expensive and invasive. The company's managers, instead of managing, spent their time preparing for depositions. The lawsuit, he says, "brought everything to a stop."

In the end, rather than permit the total exhaustion of company resources, Mr. Coleman decided to settle. The tab for this exercise in futility: $8.7 million. As Mr. Coleman says: "That's over $8.7 million that was diverted from new investments in jobs and facilities."

The scenario is repeated daily throughout American business. It is <u>not</u> repeated, let me stress, among our world competitors.

<u>Only the United States</u> has seen the number of lawyers double over a 20-year period. <u>Only the United States</u> spends more than $80 billion annually in direct litigation costs, perhaps four times that in indirect costs. According to a recent survey, 40

percent of companies that had been the target of product liability suits have discontinued certain types of product research.

We must remove this ball and chain from our ability to produce and compete worldwide. My competitiveness council, led by Vice President Quayle, has offered 50 recommendations for legal reform. They would limit discovery to reasonable proportions, discourage some frivolous suits through a "loser-pays" rule, and offer alternative means of resolving disputes.

This broad legal reform won't be easy -- just look at the fight we've had on product liability reform. We introduced a reform bill in 1990, and again in 1991. Senate Democrats refuse to bring it to a vote; in the House it's stuck in <u>two</u> committees. The special interests are lining up against legal reform, and we can use your help in moving it forward.

If we're successful, the effects will be far-reaching, extending into another area critically in need of change. Medical malpractice premiums almost doubled in the second half of the 1980s. Doctors are practicing "defensive" medicine, ordering an estimated $20 billion a year in unnecessary tests and procedures to protect against frivolous litigation.

The trends in health care costs are simply unsustainable. From less than 6 percent 30 years ago, total health care expenditures are today about 13 percent of GDP. Some mid-range estimates put that figure at 30 percent by the year 2030 -- that's thirty cents of every dollar of national income spent on

health care. Right now, according to one federal study, American corporations already spend more on health care each year than they earn in after-tax profits.

We must reform the system -- but we face a crossroads. Some have advocated nationalized care; others propose the so-called "pay or play" approach, which I am convinced is merely a step on the road to nationalized care.

Neither is acceptable. Neither will preserve the quality of our country's health care, which remains the best in the world. I will not let that high quality be taken away from the American people through some scheme of government control.

Nationalized care means rationed care; its promise of cost containment is a mirage. "Pay or play" would dump still more mandates on business. For employers, a 9 percent payroll tax would mean a 34 percent increase in health insurance costs. That money must come from somewhere -- and for a company unable to pass along the added costs through higher prices, that means decreased investment, lower wages, and fewer jobs.

There is an alternative. My proposed health care reform will build on our system's strengths, preserving the quality of care. We will increase consumer choice. Through transferable credits, we will assure access to basic health insurance for the uninsured, and control costs through market incentives. And we will not raise taxes on American employers.

I have targeted a third area for attention -- like the others, absolutely critical to our success in the coming decades.

You understand that for America to succeed economically at home, we must succeed economically abroad. The fastest growing companies among your group -- the ones creating the greatest number of jobs here at home -- are those with far-reaching involvement in foreign markets.

I am committed to opening markets to American goods and services, removing the government-imposed barriers that act as a hidden tax on American business. Each market shut off by protection is a lost opportunity to sell your products. A successful conclusion to the current Uruguay round of trade negotiations, for instance, could increase world output by $5 trillion over the next decade. More than $1 trillion of that boom -- providing as many as two million jobs -- will go to the United States.

Even closer to home, exports to Mexico have more than doubled over the last five years -- creating more than 300,000 American jobs. Our North American Free Trade Agreement will lock in and even multiply those gains, creating with Canada a $6 trillion market for American products.

As world trade expands, the need for a sophisticated, well-educated workforce will intensify. Yet the fact is grim and undeniable: our current educational system is unable to produce the workers the highly competitive world market demands.

Our educational failures have hit American employers hard. English is now the language of international business; yet only 20 percent of 17-year-olds can write a simple two-paragraph

letter applying for a job. The situation in geography, math and science is equally dire. Too many businesses are forced to pay twice for the education of prospective employees -- once through taxes that support our schools, and again through job training to remedy the failures of those schools in educating our young.

Communities have begun taking matters into their own hands, with local businesses often acting as catalyst. ABC's Vital Link, which works with local schools to establish learning incentives for students, is a perfect example of the community-based efforts our children need.

Still, there is much for government to do. This year, seven different federal agencies will spend $18 billion on a patchwork of 60 vocational training programs. Is it any wonder that so many Americans who seek training don't know how to get it? Working with state and local governments, our Job Training 2000 initiative will bring coherence to these programs and offer "one-stop shopping" to aspiring workers.

Job Training 2000 perfectly complements the revolution now taking place in American education as a whole. Through our America 2000 initiative, we will reinvent our schools. Your chairman, Jim Jones, is a leader in the New American Schools Development Corporation, a private group created at my request to launch an entire generation of break-the-mold New American Schools.

This revolution is essential to creating a world-class workforce. To do that, we need to set world-class standards for

students and create a system of voluntary national tests to measure their progress. We must redouble our efforts to rid our schools of drugs and violence -- to cleanse America of this scourge that wastes so many young lives. And we must make schools more accountable, by forcing them to compete. That means giving parents the opportunity to choose their children's schools -- public, private, or religious.

I am convinced that each of these major reforms -- restoring sanity to our legal system, ensuring quality health care for all, expanding world trade, and reinventing American education -- is essential to this country's future productivity.

But each faces powerful opposition from special interests who profit from the status quo. So I have targeted a final reform, no less important than the others. If America is to change, our government must change.

Last week in Philadelphia, I presented seven specific proposals to deal with the paralysis that grips the Congress. The results of this gridlock are dismally plain. Congress was incapable even of passing my short-term economic growth package. But they must understand: I will continue to fight for measures essential to economic growth -- including a cut in the tax on capital gains.

The American people are rightly fed up with business as usual: a deficit that is a fiscal and a moral outrage, a permanent governing class oblivious to the national interest, and

hundreds of self-perpetuating programs that don't even aid the people they were designed to help.

I refuse to believe that this is the legacy we will leave our children. But it will be -- if we don't reform the United States Congress.

The reforms I've outlined here today are grounded in basic principles, a way of looking at the world. As Jefferson said: "The pillars of our prosperity are the most thriving when left most free to individual enterprise." In practice, that means government must trust the wisdom of markets more than the whims of bureaucrats. The freely made decisions of businessmen and women must take precedence over the engineering schemes of government. And all of our institutions -- from the U.S. Congress to the local school board -- must be accountable to those they serve.

Over the last decade, America has changed the world. Today we are blessed with the opportunity to change America. With these principles as our guide, we will meet the challenges, and exploit the opportunities, of the world that is now being born.

Thank you, and God bless the United States of America.

# # # #

(Ferguson/Simon)
April 2, 1992
Draft Two
BUSINESS

PRESIDENTIAL REMARKS: AMERICAN BUSINESS CONFERENCE
WILLARD HOTEL
TUESDAY, APRIL 7, 1992
2:00 PM

[Acknowledgments, joke]

It is always a pleasure to speak with members of the American Business Conference, because it is always a pleasure to speak with the best.

I would like to talk to you today about the future -- the future of our country generally, and more particularly the future of our country's business environment. In fact, we cannot separate the two. The America of the 21st century -- its ability to make peace in the world, to foster strong families, to create rewarding jobs -- will be shaped today, in large part by how hospitable we make America for business.

We can learn from your success. The key to the success of any high-growth company is the wise deployment of resources. The successful company channels labor and investment into those areas with the potential for the greatest expansion and the highest return. You take the risk; you reap the reward; everyone, meanwhile, benefits from the wealth you create.

That, in brief, is the genius of entrepreneurial capitalism. Our system has made America the envy of the world, the most prosperous country on earth, affording the highest standard of living to the largest number of people in history. With one-

twentieth of the world's population, we produce one-fourth of the world's goods and services.

What accounts for our preeminence? The answer, I believe, lies in our resiliency, our historic ability to innovate, to change as the world changes. America's world leadership is not automatic; it is not a birthright. We must continue to earn it, day by day, quarter by quarter, year by year. The world now is changing at a pace no one could have dreamed of a generation ago. And America, which has led the world's transformation, must change with it.

Over the last several years deadweights have begun to slow the engine of growth -- inefficiencies a competitive economy cannot tolerate. I have isolated five areas for reform, five critical ways in which America must change if we are to continue to lead the world. You understand the urgency, for each of these problems presents itself to American companies not as an abstraction but in the most immediate way: as a cost of doing business -- a cost you can't control, an expenditure with no possible return.

When our legal system becomes incapable of resolving disputes in a timely and civil manner, business loses the incentive to innovate and take risks. When health care costs escalate, business picks up much of the tab. When government imposes barriers to trade, business pays the price in opportunities lost. When our children leave school without rudimentary skills, business bears the burden in lowered

productivity. And when government freezes in gridlock, business can no longer plan rationally for the future.

Each of our system's failings saps your resources, drawing away your investment and manhours from productive tasks. Allow me to address them one by one.

I'll start with the crying need to reform our country's civil justice system. Every American has heard the stories of bizarre or frivolous lawsuits; but most of you have lived them, tales that could have been torn from the pages of Kafka. Consider one example, related by one of your members, Roger Coleman, president of Rykoff-Sexton, a food manufacturer and distributor.

Roger Coleman 213-622-4131

After record earnings in 1989, Mr. Coleman publicly expressed his confidence that 1990 would be even better. When earnings fell short by two percent, his hopeful statement became the cause of a shareholder class-action lawsuit.

First came a meeting with plaintiffs' contingency-fee lawyers, at which the merits of the case were never even discussed. "The issue," says Mr. Coleman, "was the depths of our pockets." Next came the nightmare of discovery: endlessly expensive and invasive. The company's managers, instead of managing, spent their time preparing for depositions. The lawsuit, he says, "brought everything to a stop."

Statement by Roger Coleman see file

In the end, rather than permit the total exhaustion of company resources, Mr. Coleman decided to settle. The tab for this exercise in futility: $8.7 million. As Mr. Coleman says:

"That's over $8.7 million that was diverted from new investments in jobs and facilities."

The scenario is repeated daily throughout American business. It is not repeated, let me stress, among our world competitors. This absurd drain on productivity is a peculiarly American phenomenon, putting us at an increasing disadvantage in the international marketplace.

American Bar Foundation see file

Only the United States has seen ~~a 382 percent increase in~~ the number of lawyers double over a ~~twelve~~ 20 year period. Only the United States spends more than $80 billion annually in direct litigation costs, perhaps four times that in indirect costs. Fear of lawsuits has driven almost half of U.S. manufacturers to withdraw products from world markets. One out of every four American companies has discontinued certain types of product research for the same reason.

VP's Civil Justice Report Aug. 91

We must remove this ball and chain from our ability to produce and compete worldwide. My competitiveness council, led by Vice President Quayle, has offered 50 recommendations for legal reform. They would limit discovery to reasonable proportions, discourage some frivolous suits through a "loser-pays" rule, and offer alternative means of resolving disputes.

WH Fact Sheet 2-4-92

Some of these 50 comprehensive recommendations I have instituted by Executive Order; others are contained in our Access to Justice Act; and still others will take place at the state level, using the model reforms we have proposed.

The effects will be far-reaching, extending into another area critically in need of reform. Medical malpractice premiums almost doubled in the second half of the 1980s. Doctors have begun practicing "defensive" medicine, ordering unnecessary tests and procedures to protect against litigation.

This too drives up health care costs. The trends are simply unsustainable. From less than 6 percent 30 years ago, total health care expenditures are today about 13 percent of GDP. Incredibly, some mid-range estimates put that figure at 30 percent by the year 2030 -- that's thirty cents of every dollar of national income spent on health care.

It is not hard to imagine what this would mean for American business. ~~The average~~ American corporations already spends more on health ~~premiums~~ care each year than ~~it~~ they earns in after-tax profits. And this trend too is heading upward toward disaster.

Reform of the system is inescapable. But we face a crossroads. Some have advocated nationalized care; others propose the so-called "pay or play" approach, which I am convinced is merely a step on the road to nationalized care.

Neither is acceptable. Neither will preserve the quality of our country's health care, which remains the best in the world. I will not let that high quality be taken away from the American people through some scheme of government control.

Nationalized care means rationed care; its promise of cost containment is a mirage. "Pay or play" would dump still more mandates on business. A 9 percent payroll tax would mean a 34

percent increase in a company's insurance costs. That money must come from somewhere -- and for a company unable to pass along the added costs through higher prices, that means decreased investment, lower wages, and fewer jobs.

There is an alternative. My proposed health care reform will build on our system's strengths, preserving the quality of care. We will increase consumer choice. Through transferable credits, we will assure access to basic health insurance for the uninsured, and control costs through market incentives. And we will not raise taxes on American employers.

I have targeted a third area for attention -- like the others, absolutely critical to our success in the coming decades. You understand that for America to succeed economically at home, we must succeed economically abroad. The fastest growing companies among your group -- the ones creating the greatest number of jobs here at home -- are those with far-reaching involvement in foreign markets.

I am committed to opening markets to American products, removing the government-imposed barriers that act as a hidden tax on American business. Each market shut off by protection is a lost opportunity to sell your products. A successful conclusion to the current Uruguay round of trade negotiations, for instance, could increase world output by $5 trillion over the next decade. More than $1 trillion of that boom will go to the United States.

Even closer to home, exports to Mexico have more than doubled over the five years -- creating more than 260,000

American jobs. Our North American Free Trade Agreement will lock in those gains, creating with Canada a $6 trillion market, the largest in the world.

As world trade expands, the need for a sophisticated, well-educated workforce will intensify. Yet the fact is grim and undeniable: our current educational system is unable to produce the workers the highly competitive world market demands. And make no mistake: a failure to produce a world-class workforce will only provide an incentive to move new jobs overseas.

Our educational failures have hit American employers hard. English is now the language of international business; yet only 20 percent of 17-year-olds can write a simple two-paragraph letter applying for a job. The situation in geography, math and science is equally dire. Too many businesses are forced to pay twice for the education of prospective employees -- once through taxes that support our schools, and again through job training to remedy the failures of those schools in educating our young.

Communities have begun taking matters into their own hands, with local businesses often acting as catalyst. ABC's Vital Link, which works with local schools to establish learning incentives for students, is a perfect example of the community-based efforts our children need.

Still, there is much for government to do. This year, seven different federal agencies will spend $18 billion on a patchwork of 60 vocational training programs. Is it any wonder that so many Americans who seek training don't know how to get it?

FY93 Budget Part I p. 62

Working with state and local governments, our Job Training 2000 initiative will bring coherence to these programs and offer "one-stop shopping" to aspiring workers. Private industry councils, composed mostly of businessmen, are crucial to our strategy. They would manage programs tailored to the specific needs of local labor markets. And they will be accountable for the quality and efficiency of their programs.

[Placeholder for Labor announcement]

In stressing accountability and local control, Job Training 2000 perfectly complements a revolution now taking place in American education as a whole -- a revolution essential to creating a world-class workforce. Our America 2000 initiative aims to reinvent American schools. We know how to do it. We set high standards for students. We make teacher training a top priority. And we make schools more accountable, by forcing them to compete. That means giving parents the opportunity to choose their children's schools.

I am convinced that each of these major reforms -- restoring sanity to our legal system, ensuring quality health care for all, expanding world trade, and reinventing American education -- is essential to this country's future productivity. The time for tinkering is done; we can afford no more half-measures, no more pondering and chin-pulling. If business is to get on with its work of creating wealth and jobs for America, we must undertake real reform -- root-to-branch change -- whereever our system has failed us.

No wonder, then, that each of the reforms I speak of faces powerful opposition from special interests who profit from the status quo. So I have targeted a final reform, no less important than the others. If America is to change, American government must change. Last week in Philadelphia, I spoke in some detail on the paralysis that grips the federal government. This paralysis prevents Washington from making even the most rudimentary decisions of public policy. The results are plain: a deficit that is a fiscal and a moral outrage, a permanent governing class oblivious to the national interest, hundreds of wasteful programs that live in perpetuity.

The steps I outlined in Philadelphis will restore accountablity and responsiveness to a system that has been broken for too long. [Placeholder for economic analysis insert.]

A responsive government will give the reforms I've outlined today a fair hearing, even though the special interests are arrayed against them. These approaches are grounded in basic principles, a way of looking at the world. Government must trust the wisdom of markets more than the whims of bureaucrats. The freely made decisions of businessmen and women must take precedence over the engineering schemes of government. All of our institutions -- from the U.S. Congress to the local school board -- must be accountable to those they serve.

Over the last decade, America has changed the world. Today we are blessed with the opportunity to change America. With these principles as our guide, we will meet the challenges -- and

exploit the opportunities -- of the world that is even now being born.

God bless you, and God bless the United States of America.

# # # #

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

February 13, 1992

NOTE FOR JEANNIE BUNTON

FROM: BERNARD H. MARTIN

Attached, as you requested, is an illustrative list of Administration bills transmitted to the 1st Session of the 102nd Congress upon which Congressional action was delayed or not taken.

Attachments

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1. AMERICA 2000 Excellence in Education Act -- Supports the National Education Goals through activities to promote education reform and improve educational achievement.

   -- Transmitted to Congress by the President on 5/21/91.

   -- Introduced as HR 2460 (Michel) on 5/23/91, and as S. 1141 (Kennedy, by request) on 5/23/91. Referred to House Education and Labor Committee on 5/23/91. No action on Administration bills.

   -- HR 3320 (Kildee) introduced on 9/12/91. Reported by House Education and Labor Committee on 11/7/91. Administration position: Governor Sununu sent letter to Chairman Goodling on 10/16/91 stating that school choice provision in the bill as introduced was acceptable, but the Administration has concerns about other provisions.

   -- S. 2 (Kennedy) introduced on 1/14/91. Passed Senate on 1/28/92. Administration position: Statement of Administration Policy sent to the Senate on 1/21/92 stating that the President's senior advisors would recommend that he veto S. 2 because it fails to carry out the President's AMERICA 2000 program.

2. Andean Trade Preference Act of 1990 - Authorizes a trade preference program patterned after the Caribbean Basin Initiative (CBI) for the four Andean countries of Boliva, Colombia, Ecuador, and Peru.

   -- Transmitted to Congress 10/5/90 by the President.

   -- Introduced as H.R. 661 (Crane) on 1/28/91
   S. 275 (Dole) on 1/29/91.

   -- Administration bill included in H.R. 1724 (Gibbons), which was signed 12/4/91 as P.L. 102-182.

3. California Public Lands Wilderness Act - Designates as wilderness certain California public lands managed by the Bureau of Land Management.

   -- Transmitted to Congress by the President on 7/29/91.

   -- Introduced as H.R. 3066 (Rep. Lewis, et. al.) on 7/29/91.

   -- Democratic alternative bills introduced as H.R. 2929 (Rep. Levine, et. al.) on 7/17/91 and S. 21 (Cranston, et. al.) on 1/14/91.

-- Statement of Administration Policy sent to Congress 10/31/91 strongly opposed H.R. 2929, indicating the Secretaries of Defense and the Interior would recommend a veto if the bill were presented to the President in its current form. Of particular concern, the bill would designate an amount of land that far exceeds what is suitable for protection as wilderness. The bill would also adversely affect operations at five major military installations in southern California.

-- H.R. 2929 reported by House Interior Committee on 11/4/91 and passed by the House on 11/26/91 by a vote of 297-136.

4. Civil Rights Act of 1991 - Strengthens laws against employment discrimination.

-- Transmitted to Congress on 3/1/91.

-- Introduced as S. 611 (Dole et al.) and H.R. 1375 (Michel et al.) on 3/12/91.

-- H.R. 1 was the subject of a veto threat in a 6/3/91 Statement of Administration Policy and passed the House on 6/5/91.

-- S. 1745 was the subject of a veto threat in a 10/23/91 Statement of Administration Policy, passed the Senate amended on 10/30/91, and passed the House on 11/7/91.

-- S. 1745 was enacted as P.L. 102-166, approved 11/21/91. The major objectionable provisions were removed or modified.

5. Comprehensive Violent Crime Control Act of 1991 - Principal provisions establish constitutional sound procedures for applying existing death penalty laws; allow the death penalty in other cases; limit the use of habeas corpus petitions; and allow certain evidence found in unconstitutional searches to be used in court.

-- Transmitted to Congress by the President on 3/11/91.

-- Introduced as H.R. 1400 (Michel et al.) on 3/12/91 and as S. 635 (Thurmond et al.) on 3/13/91.

-- S. 1241 was the subject of a veto threat in a 6/19/91 Statement of Administration Policy and passed the Senate on 7/11/91.

-- H.R. 3371 was the subject of a veto threat in a 10/15/91 Statement of Administration Policy and passed the House on 10/22/91.

-- The House agreed to the conference report on H.R. 3371, notwithstanding a Presidential veto threat, on 11/27/91. The Senate failed to invoke cloture (49-38) on the conference report on 11/27/91.

6. Enterprise for the Americas Initiative (EAI) - Restructures trade, investment, and debt to advance the economies and environment of certain Latin American and Caribbean countries.

-- Transmitted to Congress on 2/26/91 by the President.

-- Introduced as S. 553 (Pell) on 4/23/91
H.R. 3267, Title V (Oakar/Leach) on 8/2/91.

-- Administration bill modified by Congress and incorporated into the International Cooperation Act of 1991 (H.R. 2508). (See above)

-- Conference report, which included EAI, was defeated in House on 10/30/91.

7. Enterprise Zone-Jobs Creation Act of 1991 - Authorizes tax incentives for job creation and entrepreneurial activity in up to 50 distressed urban and rural communities.

-- Transmitted to Congress on 2/25/91.

-- Introduced as H.R. 23 (Rangel) on 1/3/91 and as S. 1032 (Danforth et al.) on 5/9/91.

-- No action was taken in either House in 1991.

-- Resubmitted by OMB on 1/29/92 as part of the "Economic Growth Tax Act of 1992."

8. Financial Institutions Safety and Consumer Choice Act of 1991 - Principal provisions authorize interstate banking and branching; authorize commercial ownership of financial services holding companies; and recapitalize the Bank Insurance Fund.

-- Transmitted to Congress on 3/20/91.

-- Introduced as H.R. 1505 (Gonzalez/Wylie) and S. 713 (Riegle/Garn) on 3/20/91.

-- H.R. 6 was the subject of a veto threat in a 10/31/91 Statement of Administration Policy and was defeated on the House floor on 11/4/91.

-- H.R. 2094 was supported in a 11/13/91 Statement of Administration Policy and was defeated on the House floor on 11/14/91.

-- H.R. 3768 was supported in a 11/20/91 Statement of Administration Policy and passed the House on 11/21/91.

-- S. 543 was supported in a 11/13/91 Statement of Administration Policy and passed the Senate on 11/21/91.

-- The conference report on S. 543 was enacted as P.L. 102-242, approved 12/19/91. The enacted version recapitalized the Bank Insurance Fund and contained other Administration proposals (with modifications), but did not authorize interstate banking and branching or commercial ownership of banks.

-- Unenacted portions of the Administration's 1991 proposals were resubmitted in draft by OMB on 1/29/92 and introduced as part of H.R. 4150 (Michel et al.) on 2/4/92.

9. Health Care Liability Reform and Quality of Care Improvement Act of 1991 - Provides incentives through the States to control medical malpractice litigation and improve the quality of health care.

-- Transmitted to Congress by the President on 5/15/91.

-- Introduced as S. 1123 (Hatch/Danforth) on 5/22/91 and as H.R. 3037 (Archer et al.) on 7/25/91.

-- No action was taken in either House in 1991.

-- Introduced as part of H.R. 4150 (Michel at al.) on 2/4/92.

10. Higher Education Act Amendments of 1991 -- Reauthorizes the postsecondary education student aid grant and loan programs by changing award amounts and eligibility.

-- Transmitted to Congress by the Department of Education (ED) on 6/5/91.

-- Introduced as S. 1246 (Pell) on 6/6/91, and as HR 2627 (Goodling) on 6/12/91. Referred to Senate Labor and Human Resources Committee on 6/21/91, and to House

Education and Labor Committee on 6/12/91. No action on Administration bills.

-- HR 3553 (Ford) introduced on 10/11/91. Ordered reported by House Education and Labor Committee on 10/23/91. Administration position: ED report sent to House Education and Labor Committee on 10/21/91 stating the President's senior advisors would recommend that he veto HR 3553 because it would make Pell grants an entitlement and establish a direct student loan program, in place of the guaranteed student loan program.

-- S. 1150 (Pell) introduced on 5/23/91. Reported by Senate Labor and Human Resources Committee 11/12/91. Administration position: ED report sent to Senate Labor and Human Resources Committee on 10/29/91 stating that the President's senior advisors would recommend that he veto S. 1150 because it would make Pell grants an entitlement.

11. International Cooperation Act of 1991 - Revises the Foreign Aid statutes to update, streamline, and provide greater flexibility for the administration of international development and security assistance programs. This proposal would also authorize special assistance initiatives for Eastern Europe and the Philippines.

-- Transmitted to Congress on 4/12/91 by Department of State.

-- Introduced as H.R. 1792 (Fascell/Broomfield) on 4/16/91 S. 956 (Pell) on 4/25/91.

-- Administration bill significantly modified by Congress and considered in form of H.R. 2508 (Fascell), which passed both Houses in different form.

-- Administration strongly opposed conference report on H.R. 2508 because of objectionable abortion-related provisions, cargo-preference requirements, and other restrictions which limited Presidential flexibility to administer foreign aid programs.

-- Conference report on H.R. 2508 passed Senate on 10/8/91 but was defeated in House on 10/30/91.

-- Defeat in House attributed to: (1) member objections to providing foreign aid while domestic economy in recession; and (2) Administration's strong objections.

12. International Monetary Fund (IMF) - Authorize appropriations for U.S. participation in an IMF quota increase.

-- Transmitted to Congress on 3/26/91 by Department of the Treasury.

-- Introduced as S. 819 (Pell) on 4/16/91, H.R. 3267, Title I (Oakar/Leach) on 8/2/91.

-- Administration bill incorporated into the International Cooperation Act of 1991 (H.R. 2508). (See above)

-- Conference report, which included IMF, was defeated in House on 10/30/91.

13. National Energy Strategy (NES) Act - Encourages growth of future energy supplies of oil, natural gas, nuclear power and enhanced energy efficiency.

-- Transmitted to Congress by the Secretary of Energy on 3/4/91.

-- Introduced as S. 570 (Johnson/Wallop) and H.R. 1301 (Dingell/et. al.) on 3/6/91.

-- Senate Energy Committee reported S. 1220, a comparable bill except for inclusion of Corporate Average Fuel Economy (CAFE) provisions, on 6/2/91.

-- Senate attempt to invoke cloture on S. 1220 failed (50-44) on 11/11/91.

-- Senate cloture achieved (90-5) on 2/4/92 on S. 2166, a revised bill which excludes CAFE and Arctic National Wildlife Refuge provisions.

-- Senate began consideration of S. 2166 the week of 2/3/92.

-- House Energy s/c referred its version of a NES bill, H.R. 776, for full committee consideration on 10/31/91. H.R. 776 contains a number of problematic provisions.

14. Resolution Trust Corporation (RTC) Funding and Restructuring - Provides $80 billion for the RTC and restructures its management.

-- Transmitted to Congress on 9/27/91.

-- Introduced as H.R. 3435 (Gonzalez et al.) on 9/30/91 and as S. 1896 (Riegle/Garn) on 10/30/91.

-- H.R. 3435, as reported amended by the House Banking Committee, was the subject of a veto threat in a 11/23/91 Statement of Administration Policy, passed the House with further amendments on 11/27/91, and passed the Senate on 11/27/91.

-- H.R. 3435 was enacted as P.L. 102-233, approved 12/12/91. It provided $25 billion through 4/1/92, and restructured the RTC's management.

-- A new bill to provide the remainder of the $80 billion was transmitted to Congress on 1/22/92.

15. Surface Transportation Assistance Act of 1991 - Provides FY 1992-1996 authorizations for highway and transit programs; extends highway-related taxes through FY 1998; and establishes a new Federal-State framework for highway and transit programs.

-- Transmitted to Congress on 2/12/91.

-- Introduced as S. 610 (Chafee et al.) and H.R. 1351 (Roe et al.) on 3/7/91.

-- S. 1204 was the subject of a veto threat in a 6/11/91 Statement of Administration Policy, and passed the Senate on 6/19/91.

-- H.R. 2950 was the subject of a veto threat in a 10/22/91 Statement of Administration Policy and passed the House on 10/23/91.

-- The conference report on H.R. 2950 was enacted as P.L. 102-240, approved 12/18/91. It provides program authorizations through FY 1997, extends taxes through FY 1999, and restructures the programs, in part as recommended by the Administration. The major objectionable provisions were removed or modified.

CAPITAL GAINS, ECONOMIC GROWTH, AND JOBS

VIEWS OF LEADING CEOS

An incentive to take risks



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Capital Gains, Economic Growth, and Jobs

Views of Leading CEOs



AmericanBusinessConference

PREFACE

For most Americans, the issue of whether to restore a capital gains differential to the tax code remains an obscure, if highly-charged, question.

This report tries to dispel at least some of that obscurity. We have asked four American Business Conference (ABC) chief executives — J.P. Barger, Lee Brown, George Hatsopoulos, and Roger Johnson — to talk about how the tax treatment of capital gains influences the ability of their firms to grow and create jobs. In addition, ABC's Chairman, James R. Jones, provides a political context for the debate based upon his experience as a Democratic Congressman and co-sponsor of 1978 legislation to lower the tax on capital gains. We think the results are enlightening.

Capital gains represent the increase in the value of assets between the time they are bought and sold. The members of the American Business Conference, chief executives of fast-growing, midsize companies, support lowering the tax on capital gains on equities — that is, stock. Reducing the tax on such gains will encourage people to invest in stock and will lower the cost of equity capital for our nation's businesses.

In an era of increasing global competition, lowering the cost of equity capital is essential for all American companies. It is particularly crucial for those firms that must rely almost exclusively on stock issues to finance their growth. This latter category includes start-up companies and those cutting-edge corporations, often in the technology sector, that seek to commercialize new ideas and processes.

It cannot be said too often: greater investment means greater growth and job creation. Enacting a significant capital gains tax differential for equities is an important means to that end.

To our knowledge this is the first time business leaders have spoken out with such candor on the impact of capital gains taxation on their business decision-making. We hope this report will expand the public's understanding of why a capital gains differential is essential for the continued vitality of the American economy.

Barry Rogstad, President
John Endean, Vice President, Policy

American Business Conference

Washington, D.C., March 1992

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I.
CAPITAL GAINS AND ENTREPRENEURSHIP

J.P. BARGER
Chairman & C.E.O.
Dynatech Corporation
Burlington, Massachusetts

I ASSOCIATE CAPITAL GAINS WITH BUMPY TRAINS.

In the late 1950's, I was a graduate student at the Massachusetts Institute of Technology. To supplement my income as a teaching assistant, I went to work for my adviser, MIT Professor Warren Rohsenow, in his part-time consulting business.

One of our contracts obliged us to make frequent trips to Washington. We would take the evening train from Boston and arrive in Washington for morning appointments.

In those days the train bed and tracks in the Northeast Corridor were not nearly so smooth as they are today. To get any sleep back then, you first had to visit the club car. Over a couple of bourbons, Warren and I would talk about our work and our future.

During one of those chats, I suggested to Warren that if we were ever going to make any real money we would have to incorporate and build a full-time business. He agreed. The reason was obvious: the tax burden on ordinary income was three times greater than the tax burden on capital gains.

That substantial differential drove our decision to start the company that became Dynatech. Today, Dynatech, with Warren as its Honorary Chairman and me as its Chief Executive Officer, is a high-technology manufacturing and service company employing over three thousand people.

"How can we confront our children with the imperative of building a better country if we do not supply them with the tools for economic growth?"

Were Warren and I young again, travelling over smoother tracks, I might still have a couple of bourbons, but I would not be able to offer the same advice.

Sadly, entrepreneurship has become much more expensive. Regulatory and litigation costs have raised the threshold for starting a business. Moreover, and of paramount importance, the absence of a significant tax break for capital gains means that there is no offsetting prospect for reward to compensate for the investment of capital.

That's bad news not just for aspiring entrepreneurs and investors, but for the entire country. We need new businesses because we need new jobs. The best of our large corporations are cutting employment to stay competitive. The creation of new enterprises can take up the slack.

That is the context with which I view the current debate over capital gains. Simply put, do we want young Americans to have opportunities to become successful entrepreneurs and create new jobs? If so, we must provide them with sufficient financial incentives to undertake the risk and effort starting a company demands.

Throughout most of this century — since the establishment of the income tax — such financial incentives have been available. We owe the next generation no less: an economic environment in which initiative can flourish. How can we confront our children with the imperative of building a better country if we do not supply them with the tools for economic growth?

I noted with interest the recent remarks of the Japanese Prime Minister to the effect that talented young Americans are flocking to Wall Street rather than committing themselves "to producing things and creating value." This he sees as evidence of societal decline.

I don't believe young Americans today are much different from their counterparts of three decades ago. Many still dream of starting their own businesses or expanding existing ones. Our task is to nurture such ambitions beyond the talking stage. One very good route to that end would be Congressional enactment of a meaningful capital gains differential. It worked for me and the many other entrepreneurs of my generation. It can work again.

II.
CAPITAL GAINS, JOBS, AND COMPETITIVENESS

ROGER W. JOHNSON
Chairman, President, & C.E.O.
Western Digital Corporation
Irvine, California

I HAVE LONG ARGUED TO ANYONE WHO WOULD LISTEN THAT A capital gains differential, by lowering the cost of capital, would encourage greater domestic job creation and increase the international competitiveness of American companies.

What precisely do I mean when I say that?

The answer resides in the cost structure faced by companies like my own, Western Digital. The main components of our total costs are, in descending order of importance:

1. cost of market access
2. cost of capital
3. cost of customer support
4. cost of labor

For most growth companies, the first two cost components are by far the most important. Because of the favorable tax treatment of capital gains on equities in Japan, my Japanese competitors have a clear and compelling cost advantage over me right off the bat. Their equity capital is cheaper.

Other nations know this. Countries like Northern Ireland, Singapore, Korea, and Taiwan use favorable tax policies, and sometimes outright grants, to compete for American manufacturing jobs. Since I cannot afford the cost differential enjoyed by my Japanese competitors, I must seek equal treatment and that means, ultimately, locating some new manufacturing facilities offshore.

Fortunately, this is not quite a zero sum game. Western Digital has been a net creator of jobs here in the United States. Producing new products offshore does not take away jobs in the absolute sense because the alternative is simply not building the product at all.

Nevertheless, the high cost of equity capital in the United States has meant that Western Digital has not created as many new jobs here as we would have liked. That's what I mean when I say that a significant capital gains differential, by lowering the cost of capital, would create new American jobs.

"Because of the favorable tax treatment of capital gains on equities in Japan, my Japanese competitors have a clear and compelling cost advantage over me right off the bat. Their equity capital is cheaper."

Now what about the competitiveness angle? Why would a capital gains differential increase the competitiveness of American companies?

The fact is, those nations, particularly in Asia, that offer better capital costs to American companies usually do so as part of an overall development strategy. The first step is encouraging foreign direct investment. Once American facilities are in place, the host country usually provides further incentives for expansion and technology transfer. The next rung on the development ladder often involves an equity stake in the American operation.

"We simply have to recognize that other countries use foreign investment to bootstrap their own industries and technology base. Why should we make it easier for them by keeping our cost of equity capital above competitive rates?"

There is nothing nefarious about this. We simply have to recognize that other countries use foreign investment to bootstrap their own industries and technology base. Why should we make it easier for them by keeping our cost of equity capital above competitive rates? The *status quo* works to our competitive disadvantage.

We live in a global market and the best companies are the ones that establish a presence in key areas around the world. This process is an inevitable part of good business strategy. What is not inevitable, and what we should therefore change, is the siphoning of American jobs and competitive technologies away from our shores because of a tax structure that rewards investments in homes over equity investments in companies. I simply do not understand why we tolerate this state of affairs.

There are more risk takers today than there ever have been. Fewer of them are American and fewer of the rewards of entrepreneurship — money and jobs — are going to the United States. A capital gains differential cannot in and of itself change that. But it is an indispensable first step toward the creation of a sensible economic strategy for the nation.

III.
CAPITAL GAINS AND THE COMMERCIALIZATION OF NEW TECHNOLOGIES

DR. GEORGE HATSOPOULOS
Chairman & President
Thermo Electron Corporation
Waltham, Massachusetts

OVER THE YEARS, I HAVE WRITTEN FREQUENTLY ON TOPICS IN macroeconomics. I have concerned myself with issues relating to changing patterns in American savings and consumption, the cost and patience of capital, and the fiscal and budgetary roots of our competitiveness problems.

I could easily demonstrate theoretically why Congress should reduce the tax on capital gains on equity investments. But the debate over capital gains will not turn on theory. A tax cut on capital gains will happen only if a sufficient number of legislators understand in real world terms why entrepreneurs like me support a differential. So I would like to frame my views from the perspective of my company, Thermo Electron.

Thermo Electron is in the business of commercializing new technologies based on ideas generated by our ongoing work in energy, the environment, and biotechnology. We identify major needs that surface in the economy and ask ourselves if we can address those needs through the appropriate application of one or another of our technologies.

If so, we create a new public subsidiary to put our ideas into action. Thermo Electron typically holds a controlling stake in the new venture and provides it with technical, managerial, and financial expertise.

Thus far we have created eight subsidiaries that are world leaders in businesses as diverse as the manufacture of environmental monitoring and analytic instruments, artificial hearts, cogeneration and alternative fuel power plants, soil remediation equipment, recycling equipment, and systems to detect explosives, drugs, and carcinogens. By spinning off our most promising new ideas into public subsidiaries, we have been able to preserve entrepreneurial discipline even as Thermo Electron itself has grown large enough to join the *Fortune* 500.

"Changes in tax policy, beginning in 1986, have made it impossible for Thermo Electron to fully commercialize all the technologies we possess."

High cap gains tax

Changes in tax policy, beginning in 1986, have made it impossible for Thermo Electron to fully commercialize all the technologies we possess. These tax changes have effectively made the taxation of income from equity investments double that of the taxation of returns from debt-financed instruments.

Before 1986, interest income was taxed as ordinary income while capital gains were subject to a differential tax. Thus, before 1986, for the top income brackets, interest income was subject to a marginal rate of about 50 percent while capital gains were taxed at 20 percent.

Tax reform in 1986 changed that. It eliminated the capital gains differential and lowered the personal tax rates. The result: capital gains and interest income were taxed at the same rate — 28 percent. It is true that the budget agreement of 1990 raised the top tax bracket to 31 percent while keeping the capital gains tax at 28 percent. But this slight differential has had no measurable influence on investment decisions. Essentially, from a tax point of view, investors today are indifferent regarding equity and debt instruments.

Consider these developments from a corporate point of view. When a corporation issues debt, it can write off its interest payments. On the other hand, equity is taxed twice: first as corporate income, then as dividend income. By equalizing the tax treatment of capital gains at the investor level, we have, from the corporate level, raised the cost of equity relative to the cost of debt. Investors demand a higher price for their equity investments because equity income is taxed twice and capital gains receive no significant tax relief.

At Thermo Electron, we have no choice but to rely on equity to finance the commercialization of our technologies. You cannot underwrite ideas with debt — there is no collateral to balance the risk.

Let me try to quantify what this means for Thermo Electron. Because of the tax changes beginning in 1986, I have been obliged to cultivate European investors who, because of tax and other reasons, are willing to take equity stakes in our new companies at a cost of capital lower to that demanded by American investors. The mix of American and European investors in our new ventures is now about 50-50. If we did not have recourse to Europe, Thermo Electron would have had to curtail our new ventures by a factor of two.

By the same token, if by some sort of magic Thermo Electron were operating under the capital gains taxes that prevailed in this country in 1979, we would have generated twice the number of ventures we have created in the current environment. And finally, if Thermo Electron operated with the capital gains treatment currently afforded to investors in our Japanese and German competitors, we could have enacted three times the number of new ventures.

The fact is, Thermo Electron possesses more commercially promising ideas than we can finance. My friends in Europe know this. They often tell me that the United States is second to none in entrepreneurial and technical expertise. They ask me why our government, through appropriate tax policy, does not cultivate that expertise. Where, they ask, are the tax incentives to invest in the equities of high technology companies?

I have never found a good answer to their question.

IV.
CAPITAL GAINS AND THE MATURE CORPORATION

W.L. LYONS BROWN, JR.
Chairman & C.E.O.
Brown-Forman Corporation
Louisville, Kentucky

MY COLLEAGUES IN THE HIGH TECHNOLOGY SECTOR DESERVE considerable credit for advancing the case for a capital gains differential. But I would hate to think that, as a result of their efforts, the public believes that capital gains is an issue uniquely tailored to any one industry. You do not have to run a high-tech company, or a brand-new venture, to recognize the competitive advantages a significant capital gains differential would spur.

My company is not exactly a start-up; it was founded in 1870. Nor are we a high-tech company; Brown-Forman is the producer and marketer of high-quality consumer products. But Brown-Forman would decidedly benefit from the lower cost of equity capital that a capital gains differential would bring about.

The price of capital is as much a cost of doing business as are wages, employee benefits, raw materials, advertising, distribution, taxes, and new investments in property, plant, and equipment. Under certain circumstances, the cost of capital can determine whether a given product is competitive in the marketplace. To illustrate this latter point, let me cite an example from our Lenox subsidiary.

"Under certain circumstances, the cost of capital can determine whether a given product is competitive in the marketplace."

For over a century, Lenox has been recognized worldwide as a manufacturer of fine china and crystal. Currently, Lenox controls a third of the American market for china. Our main competitor, a Japanese company, also has about a third of the market. A variety of smaller companies, domestic and foreign, share the final third.

Several years ago, it came to my attention that our Japanese competitor was selling its china at a price significantly lower than we were. Although quality and design are also important in governing a consumer's decision to purchase fine china, we could not ignore this challenge from our largest rival.

I asked to see one of our competitor's plates. I placed it on my desk beside a similar one made by Lenox. The quality of the Japanese china was not quite up to Lenox's standards, but it was very good. Good enough, in fact, that its lower price was not the result of a decision to sacrifice quality or design.

I asked some of my colleagues in corporate development to investigate further. They did an exhaustive study comparing the way Lenox does business with what we knew about our Japanese competitor. They looked

at labor costs and labor productivity, materials costs, administrative overhead, plant and equipment efficiency, and every other factor that contributes to the manufacture and distribution of our products.

They found only one advantage that our Japanese rival had over Lenox: their cost of capital was about half what we paid. It was that difference that ultimately got translated into a lower price for their china.

We had to compensate for our competitor's capital advantage. In theory, we had three choices. First, we could abandon the business in favor of other ventures. Second, we could manufacture offshore to cut costs. Third, we could stay in the United States and find alternative ways to economize.

We had no intention of getting out of the business: Lenox is one of the crown jewels of America's consumer goods industry. Nor did we wish to move offshore. So, we chose the third and riskier route. We built a new plant in an area of the country where labor costs were lower and installed the very finest production and systems equipment available. We got our costs down without compromising our product standards.

Lenox remains a dominant and growing manufacturer of china because we found a way to circumvent the problem of higher capital costs. But, while we did not move offshore, we were obliged to seek labor at a lower cost. That was the trade-off the current tax regime forced.

I think the problem we faced at Lenox will be one that other American firms will be obliged to confront. Capital costs will soon be the last comparative advantage other nations will enjoy over the United States.

Wage rates are converging throughout the developed world. With instantaneous communication, no one has a monopoly on information or know-how. And we are all learning to adjust our marketing and advertising to the peculiarities of various national markets. In short, many business costs and practices are becoming the same in different countries.

What is not converging is the cost of equity capital. Because Japan and Germany tax capital gains as well as a number of other capital-related factors at lower rates than the United States, manufacturers in those two countries enjoy a cost advantage. In a world in which many other of the costs of doing business are the same, that edge can only increase in significance. Indeed, it will become decisive.

That's why I support a significant capital gains differential. Ideally, to be truly competitive with the Japanese and the Germans, we would not tax capital gains at all.

V.
CAPITAL GAINS: THE SEQUEL

JAMES R. JONES
Chairman, American Stock Exchange
Chairman, American Business Conference
New York & Washington, D.C.

HOLLYWOOD ISN'T THE ONLY PLACE THAT PRODUCES SEQUELS. Washington is pretty good at it too.

Take the present debate over capital gains. It is very reminiscent of the controversy surrounding Congress's decision to lower capital gains rates in 1978. As we await the climax of the current version, perhaps we can learn something from the earlier script.

I had a meaty role in the 1978 production. At the time I was a third-term Democratic Congressman from Oklahoma. Together with another junior member of the Ways and Means Committee, Bill Steiger, I sponsored legislation to establish a differential rate on capital gains. I believed that cutting the capital gains tax would result in new investment and new jobs.

As they do today, opponents to capital gains reform in 1978 made two arguments. First, they said capital gains relief would be a drain on the Treasury.

The revenue projections bandied about back then look pretty crude compared to today's computer simulations. But taking an erroneous estimate to a few extra decimal places does not make it any more accurate.

Those who predicted a fiscal nightmare in 1978 typically ignored the behavioral changes a lowered rate on capital gains would spark. Their counterparts in 1992 usually make the same mistake.

The fact is, people do adapt their economic decisions in the face of tax changes. In 1978, our legislation lowered the maximum tax rate on capital gains from 49 percent to 28 percent. In the years following, tax revenues from capital gains realizations increased sharply. In addition, the 1978 tax cut spurred greater overall growth. When more wealth is created, government revenues rise. Whatever an estimator's crystal ball may say, experience shows that cutting taxes on capital gains is a money-generator for the government.

In their second argument, our opponents claimed that capital gains relief disproportionately benefitted the idle rich. Our bill was dubbed "The Millionaire's Relief Act of 1978," by one critic while another told the *New York Times* that capital gains was a "fat-cat-versus-the public issue."

Such zingers played just as well in the press fourteen years ago as they do today. Ultimately, though, they failed to persuade Congress in 1978 and I think they will fail this year as well.

Then as now, the American economy was stagnant. Business confidence was low. Growth seemed impossibly elusive. The country desperately needed to channel more money into productive investments. A capital gains differential provided the incentive to make that happen.

In 1978 just as much as in 1992, American society suffered from severe social problems. People differed then as they do now on the solutions to those problems. One thing was — and remains — clear: whatever the solutions, they invariably presuppose economic growth and job creation. The reason is simple: you can't redistribute wealth if you aren't willing to help create it. Greater economic equity means little unaccompanied by greater economic opportunity.

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Risk is the raw material of growth. Every job that exists today originated in the willingness of someone at some time to take a risk with his or her money. Every new job we create will have a similar origin. At present, the United States taxes capital gains at a higher rate than any of our major international competitors. When a high tax rate on capital gains retards economic risk-taking and therefore job creation, it is the general public, not the "fatcats," who suffer the most.

We can enact a tax cut on capital gains that does not cut government revenues but does spur greater economic growth. We can do it because we did it before — in 1978.

Congress should and I believe Congress will cut the tax rate on capital gains. Why? To borrow a term from Hollywood, economic growth is always great political box office.

VI.
FINAL THOUGHTS: CAPITAL GAINS AND BASIC TAX REFORM

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AS THIS REPORT MAKES CLEAR, ABC BELIEVES THERE ARE SOUND reasons to support a capital gains tax differential on the sale of equity securities. Such a differential is a way to mitigate the double taxation on equity investment.

Unless equity investment is afforded tax treatment comparable to debt financing, Americans will not direct an adequate amount of new investment into stock. Yet it is upon such comparatively risky investments that start-up firms and most of our competitive, idea-driven companies rely.

"... the debate over the revenue effects of a capital gains differential is beside the point. The tough issue is whether or not a differential would positively influence long-term growth. ABC emphatically believes that it would."

By lowering the cost of equity capital, a differential can

- promote overall economic growth of the American economy
- improve the rate of domestic job creation
- increase the competitiveness of U.S. companies by lowering their cost of doing business relative to competitors in Japan and Germany
- encourage the commercialization of new technologies
- spur entrepreneurship

Critics of a capital gains reform argue that such a tax cut would be too costly. Proponents argue that the cut would generate greater tax revenues. The difference between the revenue estimates offered by both sides is quite small and well within normal forecasting margins of error. For that reason, I would argue that the debate over the revenue effects of a capital gains differential is beside the point. The tough issue is whether or not a differential would positively influence long-term growth. ABC emphatically believes that it would.

Apart from the clashing of revenue estimates, the most startling aspect of the battle over capital gains has been the very deep rancor it has stirred. Part of the problem has surely been the tendency to discuss capital gains in isolation. Opponents argue that a differential would inequitably benefit the rich. Proponents, for their part, appear to regard the differential as some sort of universal solvent, that, if enacted, would miraculously dissolve all of our economic ills. By not seeing capital gains taxation as part of a larger economic strategy for long-term saving and investment, both sides have painted themselves into an ideological corner.

Basic Tax Reform

The best way to think about a capital gains differential on the sale of equities is to regard it as a milestone on the road toward basic tax reform. That reform would place the tax burden on activities that extract resources from the economy — consumption — while encouraging activities that put resources back into the economy — saving and investment.

There is today a clear trend toward moving tax policy in that direction. For example, in addition to capital gains, there have been a variety of proposals, emanating from both political parties, to expand Individual Retirement Accounts, accelerate depreciation of assets, and integrate the personal and corporate tax systems. All seek to promote saving and investment.

Measured against the long-term goal of removing the tax bias against saving and investment, a capital gains differential on the sale of equities is a step in the right direction. Eventually, we should change when and how we tax every form of income — wages, dividends, interest, as well as capital gains. Income in whatever form should not be taxed unless and until it is used for consumption.

"Income in whatever form should not be taxed unless and until it is used for consumption."

We need as a national goal the establishment of a tax system that falls only on consumption and exempts from taxation all forms of income that are saved. If we had such a goal, the ideological objections to near-term initiatives such as a capital gains differential would, I believe, disappear.

Instead, a capital gains differential would be seen for what it is: part of a larger program for tax reform to build for America's future.

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