THE DAVID HUME INSTITUTE

Contemporary Problems in Commercial Litigation

DAVID EDWARD
LORD ROSS
CATHERINE MONTGOMERY BLIGHT

Hume Occasional Paper No.11

THE AUTHORS

Professor David Edward CMG, QC is the Salvesen Professor of European Institutions University of Edinburgh and an Honorary Vice President of The David Hume Institute.

The Rt. Hon. Lord Ross, PC, FRSE is Lord Justice Clerk for Scotland and a Senator of the College of Justice.

Catherine Montgomery Blight is Lecturer in Economics, Edinburgh School of Agriculture and a Trustee of The David Hume Institute.

COMTEMPORARY PROBLEMS IN COMMERCIAL LITIGATION

DAVID EDWARD

LORD ROSS

With a Commentary by
CATHERINE MONTGOMERY BLIGHT

THE DAVID HUME INSTITUTE
1989

The David Hume Institute
16 Hope Street
Charlotte Square
Edinburgh EH2 4DD

ISBN 1 870482 06 9

Printed by Pace Print (Edinburgh) Ltd.

FOREWORD

One of the principal concerns of The David Hume Institute has been the investigation of areas in public policy which encourage links between legal and economic thinking. A timely opportunity to pursue these links was provided by the proposal emanating from Professor Jack Shaw, one of our Trustees, that the Institute should arrange a seminar on the economic problems of commercial litigation. These problems have exercised both the business and legal communities in Scotland but beset the legal systems of England and European countries generally.

The Seminar took place in the famous Advocates Library of the Faculty of Advocates at Parliament House, Edinburgh on 21st November 1988. The proceedings were opened by the Chairman, Lord Mackenzie Stuart, recently returned to Scotland from his Presidency of the Court of Justice of the European Communities. The first paper, presented by Professor David Edward, investigated commercial litigation in Scotland and, in particular, arguments concerning the use of the Scottish courts as forums for international litigation. Further, he examined the strengthening of the law of Scotland as an autonomous system. Lord Ross, the Lord Justice Clerk, presented the second paper, explaining the recent changes in the Rules of Court dealing with commercial causes and the implications of these changes for the commercial litigant.

Following the presentation of the papers, there were questions from the participants and general discussion. A summary of the main points of the discussion has been prepared by Mrs Blight, who has also written a Commentary on the papers which highlights some of the more important economic issues.

This Occasional Paper reproduces the Papers, Summary of Discussion and Commentary with the kind permission of the authors.

The Institute owes a special debt to several persons for making possible the Seminar and the publication of its proceedings. Our thanks go to Lord Mackenzie Stuart; to Mr David Hope QC, Dean of the Faculty of Advocates and to the Faculty of Advocates for accommodating the Seminar; to Scottish Financial Enterprise through Professor Jack Shaw for financial support which has enabled these proceedings to be published; and of course to the speakers Lord Ross, Professor Edward and to our Rapporteur, Mrs Blight.

The Institute issues the usual disclaimer that it has no collective view on policy questions, but it welcomes the opportunity of bringing this important issue of the economic problems of litigation to public attention.

Alan Peacock
Executive Director
January 1989

THE MARKET FOR COMMERCIAL LITIGATION

David Edward

No Seminar organised by Alan Peacock and The David Hume Institute would be complete without an analysis of the market. Like other markets, the market for commercial litigation has its demand side and its supply side, its costs and its benefits. On the demand side are the commercial litigants: those who want to litigate and those who are forced to litigate. On the supply side are the courts, the judges and the law they administer.

Operating to some extent on both sides of the market are the lawyers for the parties. They operate on the demand side to the extent that they advise their clients to go to law, and to the extent that they conduct their cases for them. They operate on the supply side because they are themselves, in the French phrase, auxiliaries of justice. They are part of the system. The advice they give and the way they conduct cases are circumscribed by rules of law and rules of professional ethics. Without them, it is hardly conceivable that a sophisticated system of commercial litigation could be made to work. Without them, equally, there might be less demand for such a system.

A full analysis of the market involves many interrelated questions:

(i) Why do commercial men resort to litigation — because they're forced to do so, because they're advised to do so or because they want to do so?

(ii) Should the courts make special arrangements for commercial litigation and, if so, how? Should there be special courts and specialist judges, or should businessmen wait in the queue like everyone else?

(iii) Is our law adequate to deal with commercial disputes? Why, as anecdotal evidence suggests, do businessman prefer to write their contracts under English law and go to England to litigate? Is the substance of Scots law defective, or our procedures, or both?

(iv) Are our lawyers properly trained and sensibly organised? If not, what should we be doing about it?

I propose to address myself principally to two aspects of the subject. My first concern is to offer some words of caution to those who say, without really arguing the point, that we must at all costs set out to create a market for commercial litigation in Scotland. My second concern is to deal with the suggestion that we must strengthen the position of Scots law as an autonomous system and the opposing suggestion that we ought to abandon Scots law and adopt English Law.

So let me begin with the demand side of the market — the commercial litigant.

The conventional, or polite, view of the commerical litigant is that he is a robust, practical businessman faced with a commercial problem to which he needs a quick, practical and commercially realistic answer. The author of the Aspect column in this month's Journal of the Law Society puts it this way:

> "In commerce and industry recourse to litigation takes place only after all avenues of negotiation have been explored and exhausted. Litigation may therefore be joined some considerable time after the events leading to the dispute have occurred. By that stage what is required above all is a speedy answer. Indeed there are those who believe that a speedy answer is perhaps more important than the right answer."

In fact, those who are most in need of a speedy answer are probably those, like receivers and liquidators, who are in no position to negotiate because the nature of their position forces them to look for the legally correct answer, rather than the commercially convenient one.

Otherwise the picture of the unwilling commercial litigant, driven to the courts after all other options have failed, seems to me to be somewhat rosy. The reality surely is that the market for commercial litigation exists, like the market for other types of litigation, because **people** (including the human beings who manage corporations) cannot agree.

Other societies, notably the Japanese, prefer that those who cannot agree should contribute to the peace of society by resolving their disputes as quickly as possible. It is a matter of honour and social obligation for them to do so.

We don't take that view. We accept that the courts exist to provide a normal and honourable way of resolving disputes. All the same, it's perfectly legitimate to argue that the courts should not be **too** accessible, since there will then be no incentive to negotiate and settle.

Indeed, if we look at what is happening down South, where the facilities for commercial litigation are said to be better, there is ample evidence of a tendency to sue first and negotiate later. This may be symptomatic of a society that is increasingly influenced by transatlantic habits, including the habit of litigation. But where America leads, we do not always or necessarily want to follow.

Furthermore, it takes two to litigate. When the pursuer says that he wants a quick answer to the question, he frequently means that he wants a quick answer to **his** question. For a variety of reasons the defender may not agree with the question, and he will almost certainly disagree with the pursuer's version of the facts on which that question is based.

Litigation, as a way of deciding who has the better of the argument, is bound to be fairly expensive; particularly in our system when fact-finding is involved, and the threat of litigation can be an unfair weapon in the hands

of the party with economic clout. Even in that odd new corner of the market place which seems to be known as the level playing field, the resources spent on litigation might sometimes be more profitably deployed elsewhere.

As well as the obvious costs such as lawyers' fees, litigation has hidden costs in terms of the management time that litigants need to devote to it. It has hidden costs, too, for the taxpayer who pays the judges and provides the court facilities. So, even in purely economic terms, use of the law-courts to settle commercial disputes involves a range of costs as well as benefits.

There are social costs as well. If special arrangements are made for the speedy disposal of commercial litigation, other litigants will probably have to wait. There is evidence that they have had to do so in England, and we have a particular problem in Scotland since we must, to some extent, choose between speed in civil litigation and the 110 day rule which ensures that no-one is kept in prison for longer than necessary before trial.

I've stressed these points at the beginning, not to denigrate commercial litigation (from which, after all, I made much of my living) but because I hope this discussion will help us to define what the demand is, and how far it is justified, before we try to decide whether adequate steps have been taken to meet it.

I think we also have to consider whether there are other ways of meeting the demand apart from litigation in the courts — for example, by developing conciliation and arbitration services at less economic and social cost. Without necessarily sharing the current rage for privatisation, it is reasonable to suggest that, in some cases at least, private arbitration at the cost of the disputants is preferable as a way of resolving commercial disputes than the publicly-funded arena of the courts.

Having said that, there are obviously some commercial problems which can only be resolved by the courts, and that brings me to the difficult question of Scots law in commercial litigation.

Most of us have been taught to believe in the inherent merits of Scots law. The leader writer in the Law Society Journal treats it as self-evident that commercial contracts, to be performed in Scotland by at least one Scottish party, should be interpreted in accordance with Scots law.

But an important characteristic of commercial law is that the parties frequently have a choice — a choice of forum (Scotland, England or elsewhere) and a choice of law (Scots law, English law or Islamic law). In others, when it comes to choice of law and choice of forum, businessmen can vote with their feet and there is fairly reliable evidence that they are doing so.

This has prompted one of our Senators to argue that we should harmonise our mercantile law with that of England before our system becomes moribund. There is nothing new in that. If I remember rightly, James

Sutherland (later President of the Law Society and of the International Bar Association) made the same point many years ago when he was Dean of the Faculty of Procurators in Glasgow.

Over-enthusiastic votaries at either shrine would do well to read Bell's Preface to his **Commentaries** because we have passed this way before. Writing at the beginning of the nineteeth century, Bell tells us:-

> "Towards the end of the century before last, there was some appearance of a growing attention to (mercantile law), proceeding partly from the influence of foreign example, chiefly, perhaps, from the circumstances of the country . . . But this dawning of Mercantile Jurisprudence was soon overcast. The failure of the Darien Expedition . . . and the Union with England . . . (were) . . . soon followed by two rebellions, which not only disturbed the tranquillity and interrupted the natural advancement of industry, wealth and commerce, but produced a similar effect on the progress of law. The numerous forfeitures which followed the rebellions of 1715 and 1745 gave rise to a multitude of difficult questions of high interest relative to the connection of superior and vassal, the nature and efficacy of destinations in deeds of entail, and the force of real securites over land. All the learning of the Feudal Law came more immediately to be called into use, and the professional success, as well as the character of a lawyer, was estimated chiefly according to his skill in the law of heritable property. The jurisprudence of mercantile dealings, fitted for times of a different complexion, was almost entirely abandoned . . . The merchants were left to struggle with all the evils of our old law, little suited to the occasions of commercial intercourse; and a proposal, made by merchants, to introduce a system of Bankrupt Law similar to that of England met with the most determined opposition from our lawyers . . ."

Can the Scots lawyers present here put their hands on their hearts and say that they find no echo there of what has been happening in our own day? Bell goes on to contrast the position in Scotland with that in England:

> "During the troubles which agitated and depressed this country, England was triumphantly proceeding in her great career of commercial prosperity; and the progress of her jurisprudence, which might naturally be expected to accompany that of her trade, was happily directed by the successive wisdom and learning of many great men . . . Lord Mansfield . . ., who has been called the father of the Commercial Law of England, devoted his splendid talents, during an uninterrupted period of thirty years, to the great duty of constructing . . . a system of Mercantile Jurisprudence . . ."

The message, I think, is clear. Development of the law to meet the contemporary needs of industry and commerce depends partly on the economic condition of the country and partly on the skills and attitudes of lawyers, including academic lawyers and judges. Conditions favourable to the

development of mercantile law are an active economy, imaginative judges, good legal writing and an appropriate attitude of mind amongst lawyers generally. A stagnant economy and stagnant attitudes to legal practice produce stagnant law.

We are not responsible for the state of the Scottish economy, but we are responsible, each of us, for the attitude to legal practice in Scotland. And we shouldn't fall for the false dichotomy between those who would force Scots law like castor oil down the throats of businessmen who don't want it, and those who say we should adopt English law holus-bolus, warts and all.

Bell's approach was different. He treated the development of mercantile law as an attempt to deduce general principles of natural equity from the way businessmen behave in their dealings with each other — illustrated, but not fixed, by the decisions of courts and the writings of lawyers in different countries. In short, mercantile law is not a single indivisible package of national law. You don't have to have all of it as it stands, or none of it — like a fly fixed in amber. On the contrary, mercantile law is, and ought to be, a constant exercise in comparative law.

In a relatively small country like ours, with a relatively small domestic economy, we cannot hope to have everything. We do, however, enjoy one particular advantage which the lawyers of big countries do not share. Almost from his first day in law classes, the Scots lawyer is taught that there are other systems of law besides his own. Every Scots lawyer — at least every good Scots lawyer — is a comparative lawyer. Furthermore, we share a common system of legal education based on a system of law which, for all the strengths of English law, will be the majority system in the internal market of 1992. As a basis for creating a vigorous market for commercial litigation, that is not a bad start. Have we anything to lose but the chains of our past attitudes?

THE PRACTICE OF COMMERCIAL LITIGATION IN SCOTLAND

Lord Ross

I began with the premise that the law is here to serve the public and this must always be kept in view. As Lord Justice Clerk Thomson said in his preface to Thomson and Middleton's **Manual of Court of Session Practice**, "Law is the servant of the community and it can render its service only if it is in harmony with the main tendencies of social life and enjoys the confidence of the nation. Legal procedure is the means by which justice is made available to the community." Subsequently, he said, "The health of a legal system depends to no small extent on the aptitude of its procedure." The law must be flexible and there must be capacity for change.

In the area of commercial litigation in Scotland until recently there was undoubtedly room for change. Prior to September 1988, the Rules of Court did provide for commercial causes but not in a very satisfactory way. A cause could only be put on the list of commercial causes in the Court of Session with the consent of both parties. In practice, little use was made of these provisions in the Rules, presumably because of the difficulty of obtaining the necessary consent of both parties. On 27th September 1988, new Rules of Court were brought into force for commercial actions. This was done by substituting new Rules of Court 148 to 151. The most significant change is that the pursuer may elect to adopt the procedure relating to commercial actions, subject to the right of the court **ex proprio motu** or on the motion of any party, if it thinks it appropriate to do so, to withdraw an action from the commercial roll. There are also provisions enabling an action which has not started as a commercial action to be transferred to the commercial roll.

A commercial action will be heard by a nominated judge. Four judges have been named in this connection. All have experience of this type of work and there are obvious advantages from having cases of this kind heard by selected judges. This was done with judicial review and has proved beneficial. The judge has wide powers to control the procedure to be followed and the rules make it clear that speed is important. Within 14 days of defences being lodged, a commercial action is put out by order, and at the By Order hearing the court "may make such further order as it thinks fit for the speedy determination of the question in dispute between the parties". Rules also contain provisions for inspection and recovery of documents, exchanging lists of witnesses, and where possible, agreement of statements or documents without the necessity of a witness being called. Special provisions are made regarding the custom of trade or commercial usage where these have been pled.

I would differ from Professor Edward by saying that where disputes occur in the commercial field, parties want a speedy decision, and simply cannot afford to wait — perhaps two years — while protracted legal procedure is followed through. The new procedure for commercial actions should mean that from the initiation of the action to the proof would take for the average case no more than six months and if the case perhaps concerned the contruction of a commercial document, and only required one day for the proof or hearing, then the whole case could be completed in a much shorter time.

There is, of course, a problem of judicial resources. The Deputy Principal Clerk is here and could deal with that better than I, but I understand that if parties go to the Keeper of the Rolls when the record in a commercial action is closed and state that one day only will be required for the proof or hearing, he should be able to give them a very early diet. If the case is to need two to four days, at present it should be possible to get a diet within about three months.

The Court wants to ensure a speedy determination of commercial actions, and will do everthing possible to expedite matters. The court can do so as the history of judicial review shows. There again, the court has introduced new rules to cover such cases and experience has shown that these cases are determined quite speedily. Sadly, if such cases are appealed to the Inner House, it is sometimes a long time until they are put out by hearing but this is the fault of parties rather than the court.

So I believe that our new Commercial Actions Rules should improve the way in which commercial litigation is dealt with in Scotland, and should result in commercial actions proceeding much more speedily than ordinary actions. In both judicial review and in commercial causes, the judge is given power to control procedure and to ensure that the cause proceeds quickly, and if judicial review is any guide, the procedure seems to work.

Of course, there are other ways in which commercial litigation may be dealt with, and dealt with speedily. Interdict may provide a quick remedy. Only a week ago a case appeared before the Second Division by way of reclaiming motion against the decision of Lord Ordinary refusing to recall interim interdict granted **ex parte.** Within days the case was before the Second Division.

The case concerned the construction to be placed on a contract for the sale of licensed premises. An instant decision was required as the meeting of the Licensing Authority was due to take place on the day following the hearing before us. Parties appreciated that normally we would be asking ourselves if the pursuer had made out a **prima facie** case, but they both invited us not to approach the case in that way but to express a concluded view on the question of construction. This was on the basis that both parties would then accept and act upon our decision. We agreed to do just that, and intimated

our decision at the end of the hearing with written reasons being provided the following week. Parties therefore had a decision from the appeal court as to the proper construction of their contract within two or three weeks of the action being raised. Of course, that could not be done in every case, but it shows what can be done in special circumstances.

I would like to mention one other procedure that is available in the field of commercial litigation, and that is arbitration with a judge as the arbiter. Since 1980 a Senator of the College of Justice is enabled to accept appointment as an arbiter by virtue of an arbitration agreement where the dispute is one of a commercial character. This is subject to the proviso that he shall not accept such appointment unless the Lord President has informed him that, having regard to the state of business in the Court of Session, he can be made available to do so. (Sec 17 of LR (MP) (S)Act 1980).

To date, little use has been made of this provision. Lord Jauncey did so once. When I was in the Outer House, I accepted appointment several times, and sat in one arbitration for several weeks in a summer vacation before it was settled. There has been difficulty in the past in making judges available, but now that the Court can use retired judges to help out, more use could be made of these provisions. Admittedly we may be stretched for the next year with one judge taking the Piper Alpha Inquiry, but even so, provided an arbitration was not to take more than four or five weeks, I would hope that a judge could be made available.

It would be preferable for the hearing in the arbitration to be during vacation, but even during term time, now that the duties in court of the judge who was arbiter could be performed if need be by the retired judge, we would hope to be able to accommodate parties seeking a judge for an arbitration. I have discussed this with the Lord President and although it would not be possible to make a judge available for a very lengthy arbitration, he feels that it should be possible now to make a judge available for arbitrations of the four or five week variety. So that is another way in which commercial litigation could be accommodated here.

The Court does wish to see litigation of that nature being dealt with in Scotland, in the courts or by arbitration with possibly a judge as arbiter. It is to that end that the Rules of Court have been altered.

DISCUSSION

Following the presentation of the papers, there were questions from the participants and general discussion. The text which follows incorporates the main points which emerged in the discussion. It is a precis, rather than a verbatim report.

Scotland as a forum for commercial disputes.

Problems were identified as arising from the ambit of jurisdiction of individual Member States, from cases where the litigants were in two separate Member States and also where the dispute involved interests in a Community country and a Third World country. There may be a role for Scots law in international arbitration, if the new structure is adequate to provide an effective remedy, but the effectiveness may depend on the implementation of the decision. It was argued from the floor that we do have in Scotland a benign, brisk and simple system compared with England, and that these benefits to the litigant should be promoted more widely. This proposition was tempered by another speaker who suggested that there is some suspicion in Third World countries of the Scottish legal system, but it was accepted that efforts should be made to counter such attitudes.

An eminent Edinburgh solicitor emphasised important points of practice to encourage the use of Scots law: Scottish disputes should, if possible, be dealt with under Scottish system; there should be due weight given to drafting contracts under Scots law, rather than in English terms and that the distinction between the two systems should be made clear to parties.

Scottish commercial procedure.

The background to the changes in the procedure was that there had been a fear that unless there were improvements in the system, legal and commercial business would be forced out of Scotland. The general view of the speakers appeared to be that the changes were potentially helpful, but that time was needed to promote the advantages offered. Who was to be responsible for the promotion was not clarified — as one speaker commented "The Bench may not see itself as being in the business of promotion." Another suggested that the maintenance of Scots law as an international presence was not just a matter for the lawyers, and that an analogy could be drawn with the lead achieved by Scottish business in fund management. There appeared to be agreement that exposure to international law work is currently not wide enough.

The law of contract requires the consent of parties in an agreement, and hence, there had to be benefits perceived by businessmen in using Scots law. This comment raised the question of price competition in legal services and the reply, from an informed source, that on price, Scots law probably

had the advantage over other systems. Again here, the problem of time-lag in proceedings emerged.

Public interest.

An eminent jurist participating in the Seminar questioned the extent to which there is a conflict between the public and the private interest in the matter of adjudication of commercial disputes. While it could be argued that where each individual pursues his own interest, the public interest is most efficiently achieved, nevertheless in practice, there was a danger that the use of the Scottish courts as a forum for international disputes in commercial law might overload the facilities of the sytem, to the detriment of private individuals. In support of that proposition, there was general agreement that the principal concern of the courts in Scotland must be with Scottish cases or cases which have a Scottish element.

THE ECONOMICS OF LITIGATION

A Guid-ganging Plea

Catherine Montgomery Blight

Recent events have forced the consideration of the economics of litigation on to the legal profession in Scotland. For example, large scale accidents, such as the Piper Alpha and Lockerbie disasters involve multi-national companies and claimants from several different countries in proceedings before the Scottish courts. Highly complex technology and heavily regulated industries, such as the pharmaceutical industry create a situation where the injured party may only be able to afford legal advice if it is on a contingency fee basis; and the expertise of the Scottish financial industry in management has led to some suggestions that Scotland could develop a similar standing in the settlement of financial disputes among parties of differing nationalities. The resulting volume of litigation puts a strain on the court system. The legislation is complicated, there may be many aggrieved or injured pursuers, the sums at issue are huge and establishing the cause of the injury raises exceptional problems.

Although these are recent developments, the analysis of the economics of litigation has long been an intellectual tease to students of law and economics, in the United States more than in Scotland. Questions arise such as : is the process of the emergence of rules through judicial decision-making, entirely random; is it a triumph of efficient rule-making; is it a haphazard response to political interests, or more frivolously does it owe something to the state of the judge's digestion?

A more credible theory suggests that the evolution of legal rules through the common law provides a system which is efficient in the economic sense. The argument is that in the sifting process of litigation, there is a likelihood of the emergence of a solution which allows for the least-cost outcome. Frequent re-examination of the rule of law, of principle and of precedent arises through the litigation process, as parties seek to find the basis for obtaining their desired result. Decisions provide a statement of a principle of the law or a clarification of a previously uncertain or doubtful rule, thus conferring a benefit on future contestants. In subsequent disputes, it is more likely that the parties will resort to litigation where there is a wide divergence between their perceptions of the probable decision. By providing a framework for a settlement of disputes outwith the judicial system, therefore, the accepted rule of law, principle or precedent (these survivors of the process of litigation) reduce transaction cost for the parties in dispute.

There was an assumption in the preceding paragraph that the provision of the judicature is a duty of the government and that the judges are public officials with no personal interest in the process. Economists may argue that the payment of taxes entitles the public to have recourse to a court system for the referral of disputes, provided by the state. Yet, private judicial set-

tlement of disputes is widely used, and is a popular form of dealing with a dispute in certain areas of business, notably in commercial cases and in cases concerned with agricultural tenure.

Analysis of competition in litigation is illuminated when private arbitration is compared with the operation of the public bench. The common factor is that parties resort to the judge or to the arbiter for the resolution of a dispute. Private arbitration in this country usually follows a contractual relationship between the parties, a dispute in the performance of the contract and a prior agreement to refer such disputes to an arbiter. Private arbitration of this nature does not occur where the parties were unknown to each other, but an analogous situation is becoming more common, in, for instance, the provision of services such as gas, telecommunications and even legal services, where an official, in the position of an ombudsman, has the role of an independent, neutral judge. Trade organisations have also begun setting up arbitration schemes, so that an aggrieved customer can seek recompense outwith the judicial system. An example is the Association of British Travel Agents. Parties, however, need not necessarily have planned in advance that they were to resort to arbitration in the event of a dispute — it may be agreed on after the dispute has begun.

The attraction of private arbitration to commercial enterprises prima facie rests on assumptions of speedy process and preservation of confidentiality (although Lord Ross and Professor Edward appeared to be at odds on the value of quick decision-making to the businessman). However, the structure of the legal argument and the final decision do not become part of the texture of the law in the same way as reports of cases heard before the judicature. This is because there is no appeal to a court, except on certain specific grounds — for example, the arbiter went beyond the matter referred to him, or he showed bias, or he was mistaken as to the topic he was to decide, or he had an interest in the result. The effect is that in private arbitration in general, one aim, the aim of settling the dispute is achieved, but the other desirable outcome, i.e. the emergence of the preferred, efficient rule of law is not achieved. It is accepted that a litigant to the judicature does not actively intend to confer a benefit on the public at large by his litigation, although that is the result, at least according to the "emergence of the most efficient rule of law" theory as explained above.

When it comes to the enforcement of a decision by a private arbiter, difficulties may be met. If a party refuses to conform, the dispute may ultimately have to be referred to the state court system, by the arbiter registering his decision in the court registers. The decision then becomes as enforceable as a court decree. Otherwise, pressure from a peer group or professional association may be sufficient. However, the popularity of arbitration procedure suggests that it is an acceptably efficent form of decision-making, as it survives in a competitive environment, where there are other alternatives available, and it is chosen by the parties.

The competitive environment in which these choices are made provides other alternatives as well as private arbitration or the public judicature. For example, in commerce, there is the powerful sanction of a refusal to do any further business with the offending party; or an aggrieved consumer may make vivid use of the media to expose an injury, and in so doing may wipe out the manufacturer's market; or parties may have agreed at the outset on a formula for the calculation of damages should they arise.

Discussion of the economics of litigation must include not only the competition between public or private decision-making, but also the competition for a forum. Certainly, within the European Community, it is logical to suggest that transnational economic activity creates a situation where parties in a dispute are at liberty to choose between several different legal systems, and therefore a pursuer would elect to raise the action in a Member State where he perceives that the legal rules or the procedure are most favourable to his case. Thus, a company which is jealous of its trade data, would prefer to go to court in a country where weight was given to securing confidentiality in proceedings. Acknowledgement of such an argument appears to underlie the recent changes in the procedure in the Scottish courts so admirably explained by Lord Ross in his paper, although the Scottish concern was more for simplifying and hastening the settlement of disputes rather than preservation of confidentiality.

An integral part of the decision on locus is the cost of the professional services which the litigant requires. The problem is most acute in countries where the successful litigant is not necessarily awarded costs. In such circumstances, the practice has evolved of the contingency fee contract. The solicitor in effect lends his expertise against a share of the claim, and advertises a "no win, no fee" service. By specialisation, by pooling resources and by acting on behalf of a class of claimants, he may reduce the risk of variance in his returns. Where there exists a level of legal fees which is beyond the capacity of the potential litigant to meet and where he is not eligible for state legal aid, there is an incentive for a solicitor to offer a contingency fee service and for a potential litigant to take advantage of it. In these examples, the lawyer is acting almost as a private arbiter of the first instance in making a unilateral decision as to whether he will act for the client or not. There is even a possibility that recent changes in the law on liability for defective products, introduced into UK law through the Consumer Protection Act 1987, may give an impetus to the demand for contingency fee contracts. Currently, in Scotland, there is a variation of the contingency fee contract attracting comment. A speculative fee is quoted to the client by the solicitor, determined before the action and not relative to the quantum of damages awarded, and if there is "no win", there is "no fee". It is understood that this type of arrangement may be about to be tested in court. The outcome of the decision will undoubtedly affect the choice of forum by potential litigants. It may be to the advantage of the legal profession in Scotland if the contingency fee contract becomes acceptable here.

It is possible to consider the argument on the contingency fee versus the fixed fee in the light of the economic theory of behaviour under uncertainty. (The fixed fee is quoted at the outset and is payable whether the action is successful or not). Assuming that potential litigants are risk averse, one can suggest:- the higher the level of the fixed fee and the higher the possible damages, the more likely it is that the contingency fee will be preferred; the higher the probability of winning the case, the less attractive is the choice of the contingency fee; the higher the proportion of damages to be paid out in contingency fees, then the less likely it is that the contingency fee will be chosen; the less risk averse clients will be more likely to choose the contingency fee option.

However, potential litigants are not necessarily risk averse. It may be that it is the solicitor who is more risk averse than the client. His preferences may also be forecast: the higher the level of the fixed fee and the higher the level of damages, the more likely it is that he would prefer the fixed fee; the higher the probability in his opinion of winning the case, the more attractive to him is the contingency fee; the higher the proportion of damages to be paid out in the contingency fee, the more he would prefer the contingency; the more risk averse the solicitor, the more he would prefer the fixed fee. The conclusion to be drawn from these propositions is that acceptance of the contingency fee contract by the legal profession would operate to introduce an element of competition into the legal fee structure.

So far in this paper, we have dealt with the provision of public versus private solutions to disputes and the competition which can be identified for these services. However, the provision of the judicial system itself forms a type of market. The source for the authority of the courts ultimately rests with the legislature, Parliament, so that the market for litigation seen in that light is analytically a subset of the market for regulation. I have described that market elsewhere as follows: "On the one hand, the supply of regulation is generated from the legislature and its delegated agencies. On the other hand, the demand is generated by those who identify the opportunity for benefit or competitive advantage through the enactment, amendment, or rescinding of a regulation. The source of the demand for regulation is not a simple matter of producer protection. Producers, consumers, bureaucrats and even at times coalitions of these, all instigate a demand for regulation. This grouping includes associations acting for interests such as occupational organisations (lawyers, doctors, taxi-drivers), highly organised interests such as trade unions and also inchoate inter ests such as small business or conservationists."

The supply and the demand generated for a judicial structure and for changes in the existing system are therefore derived as much from the self-interest of sometimes competing groups as from a neutral public welfare demand. It is predictable, and it was borne out in the Seminar discussion, that the practising Scottish lawyer interprets the term "economics of litigation" from the viewpoint of how to provide a judicial system which would

be attractive to litigants not only in Scotland, but also from other countries. Ideally, it would be a system which would entice here, as the pursuer in the celebrated causes of **Peebles v Plainstanes** so aptly described, "mony a guid-ganging plea."

THE DAVID HUME INSTITUE

REGISTERED OFFICE
12 Hope Street, Charlotte Square, Edinburgh EH2 4DD
Tel: 031 225 6298
(Registered in Scotland No. 91239)

PUBLICATIONS BY THE DAVID HUME INSTITUTE

Hume Papers

No.1 *Banking Deregulation: the Scottish Example* (Out of print) Michael Fry
No.2 *Reviewing Industrial Aid Programmes: The Invergordon Smelter Case* Alex Scott and Margaret Cuthbert, with an Introduction by Alan Peacock
No.3 *Sex at Work: Equal Pay and the 'Comparable Worth' Controversy* Peter Sloane
No.4 *The European Communites' Common Fisheries Policy: A Critique* Anthony W. Dnes'
No.5 *The Privatisation of Defence Supplies* Gavin Kennedy
No.6 *The Political Economy of Tax Evasion* David J. Pyle
No.7 *Monopolies, Mergers and Restrictive Practices: UK Competition Policy 1948-87* E. Victor Morgan

Published by Aberdeen University Press:

No.8 *The Small Entrepreneurial Firm* Gavid C. Reid and Lowell J. Jacobsen
No.9 *How Should Health Services be Financed?* Alan Massie
No.10 *Strategies for Higher Education - The Alternative White Paper* John Barns and Nicholas Barr

Hume Occasional Papers

No.1 *What to do about the Over-Valued Dollar* Ronald McKinnon
No.2 *The Political Economy of Pension Provision* Alan Peacock and Norman Barry
No.3 *The Regularities of Regulation* George J. Stigler
No.4 *How Safe is the Banking System* Richard Dale
No.5 *Economic Issues in Merger Policy* (Out of Print)
No.6 *The Regulation of the Telecommunications Industry* Brian Carsberg
No.7 *The Novelist's View of the Market Economy* Allan Massie
No.8 *Understanding Mrs Thatcher: Coservative Economic Policy 1979-1987* David Simpson
No.9 *Adam Smith and Economic Liberalism* Andrew Skinner
No.10 *Long-term Savings in an Enterprise Economy: A Case Study of the Principles and Practice of UK Economical Policy* Jack Wiseman

Books

The Deregulations of Financial Markets
edited by Richard Dale, Woodhead-Falkner, London, 1986

Governments and Small Business
Graham Bannock and Alan Peacock, Paul Chapman, London, 1989

Inquiries should be addressed to The Secretary, The David Hume Institute, 16 Hope Street, Charlotte Square, Edinburgh EH2 4DD.