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Social Sciences 7218

Handout #8: Tort Law Basics

Review

1. The Language of Tort Law

(a) **Tort:** A wrongful act other than a breach of contract for which relief may be obtained in the form of damages or an injunction.

(b) **Plaintiff:** The party bringing a lawsuit. (Also a *victim*)

(c) **Defendant:** The party being sued in a lawsuit. (Also an *injurer* or *tortfeasor*)

2. Components of Tort Law

(a) **Harm:** The victim must suffer some actual harm for tort law to apply. Mere exposure to risk is not sufficient grounds for a Tort Law claim.

- *Safety Regulations* are used by government agencies to deal with exposure to risk of low-probability harms.
- *Perfect Compensation* restores victims to the level of utility experienced before harm. Perfect compensation encourages efficient risktaking, but can also lead to unpredictability.
- Harm can be *tangible* (damage to property) or *intangible* (emotional damages), although courts are often hesitant to award damages for intangible harms.

(b) **Causation:** The defendant needs to have caused the harm to the plaintiff.

- *Cause-in-Fact* (or *but-for Causality*): "But for the defendant's actions, would the harm have occurred?"
- *Proximate* (or *immediate*) *Cause*: Actions by the defendant cannot be too in the past.

(c) **Breach of Duty:** It must be shown that the defendant breached a duty he owed to the defendant, and that this breach led to the harm.

- Requisite standards of care may be explicitly specified by the law, or they may be vague (e.g. *reasonable care*).

Note: Tort Law covers situations where transaction costs are too high to agree to anything in advance.

3. Accidents Between Strangers

(a) **Various Liability Rules**

- **No Liability:** Neither the victim nor the injurer pays for an accident.
- **Strict Liability:** The injurer pays damages for any accidents they cause.
- **Simple Negligence:** Injurer is only liable if they breached the duty of due care.
- **Negligence with a Defense of Contributory Negligence:** Injurer owes nothing if the victim was also negligent.
- **Comparative Negligence:** If both parties were negligent, the cost is shared between defendant and plaintiff.
- **Strict liability with defense of contributory negligence:** The injurer is liable (even if they weren't negligent), unless the victim was negligent.

(b) **Observations**

- Under a strict liability rule, all that is necessary for liability is harm and causation.
- Negligence rules require all three elements – harm, causation, and fault.
- *Precaution*: Anything either injurer or victim could do to reduce likelihood of an accident (or damage done).
- All liability rules create incentives for activity levels as well as precaution. Activity levels are functionally just *unobserved precaution*, but its difficult to calculate optimal levels of activity, whereas optimal levels of observed precaution are easier to calculate.

(c) **Comparing efficient precaution and efficient activity for liability rules.**

	Injurer Precaution	**Victim Precaution**	**Injurer Activity**	**Victim Activity**
No Liability	**None**	Efficient	**Too High**	Efficient
Strict Liability	Efficient	**None**	Efficient	**Too High**
Simple Negligence	Efficient	Efficient	**Too High**	Efficient
Negligence with a defense of Contributory Negligence	Efficient	Efficient	**Too High**	Efficient
Comparative Negligence	Efficient	Efficient	**Too High**	Efficient
Strict Liability with a defense of Contributory Negligence	Efficient	Efficient	Efficient	**Too High**

(d) Four General Principles: The above results follow from the following principles:

- **(i)** If you don't bear any of the cost of accidents, you have no incentive to prevent them.
- **(ii)** If you do bear the cost of accidents, you'll do whatever you can to prevent them.
- **(iii)** If you can avoid liability by exercising due care, you'll do it, but then you won't reduce activity.
- **(iv)** If the other party can avoid liability through due care, you're the residual risk bearer, and you therefore exercise efficient precaution and engage in the efficient level of activity.

4. Accidents Involving Businesses

(a) Accidents Between Sellers and Strangers: The injurer is a competitive business but does not do business with the victim.

- We often make the assumption of perfect competition, which implies that the cost of accidents is included in prices.

	Injurer Precaution	**Injurer Activity**
Strict Liability	Efficient	Efficient
Simple Negligence	Efficient	**Too High**

(b) Accidents Between Sellers and Customers

- Efficiency of precaution and activity depend on how accurately customers perceive risks. Customers may either (i) be able to accurately assess risks of all businesses, (ii) be able to assess average risks in an industry, or (iii) be unable to assess risks entirely.

	Risk Perception?	**Seller Precaution**	**Buyer Activity**
Strict Liability	**Yes**	Efficient	Efficient
	No	Efficient	Efficient
Negligence	**Yes**	Efficient	Efficient
	No	Efficient	**Too High**
No Liability	**Yes**	Efficient	Efficient
	Average	**None**	Efficient
	No	**None**	**Too High**

Problems

1. (From Problem Set 3: Question 4) In 1887, the Michigan Supreme Court decided the case Sherwood v. Walker. The defendant, Hiram Walker (yes, that Hiram Walker), contracted to sell a cow to the plaintiff, Sherwood, for $80. A barren cow is worth its weight in beef, around $80; a fertile cow is worth much more (at least $750) as a breeder and milk-producer.
   Before Walker delivered the cow, he discovered she was pregnant, and refused to hand her over. Sherwood sued, asking that the contract be honored.
   The court ruled for Walker, saying, "A barren cow is substantially a different creature than a breeding one"; as long as both Walker and Sherwood both believed the cow was barren, there was a mutual mistake about the object being sold, and the contract was void.
   The dissenting opinion, however, thought Sherwood believed the cow might be able to breed, in which case there was simply a disagreement over what the cow was worth, and Sherwood shouldn't be penalized for being right.
   In general, mutual mistake (both sides being mistaken about the true value of an object) is grounds for voiding a contract, but unilateral mistake (one of us being mistaken) is not.
   (a) Consider a contract to sell an old piece of furniture which looks worthless, but turns out to be a valuable antique. Explain how the principle of "uniting knowledge and control" supports this rule.
   (b) Consider a contract to buy farmland that may or may not have oil underground. Give another argument against voiding a contract due to "unilateral mistake".
   (c) Do the same arguments hold with a painting that appeared to be valuable, but turned out to be a worthless forgery?
   (d) (From Thomas Miceli, "The Economic Approach to Law (Second Edition)" Stanford University Press, 2009, p. 106): Consider a contract for the sale of a parcel of land from seller S to buyer B at a price of $15,000. After the sale is complete, the local government announces plans to build a highway near the property, which raises its value to $100,000. S sues to have the contract invalidated on the grounds of mistake. Suppose it is learned at trial that the land would only have been worth $5,000 if the highway had not been approved. What does this information tell you about S's claim that the mistake was mutual?

2. Suppose that I own a house, and it is my duty to shovel the sidewalk when it snows. Shoveling reduces the risk of a bike accident on the sidewalk from 1/10 to 1/100, but it costs me $5. A biker can choose to wear a helmet or not wear a helmet. Wearing a helmet costs a biker $3, but reduces the cost of a bike accident from $1000 to $500.
   (a) What is the efficient level of precaution for me and the biker to take?
   (b) What levels of precaution will the biker and I choose to take under:
   (i) a rule of no liability?
   (ii) Strict liability?
   (iii) Simple negligence?
   (iv) Negligence with a defense of contributory negligence?
   (v) Comparative negligence?
   (vi) Strict liability with defense of contributory negligence?

3. (From sample exam questions) Here are two observations about voluntary cosmetic surgery:
   • anyone who wants to have it done can probably find a doctor happy to operate; so we can assume that the number of operations is driven by how many people request the surgery.
   • once a patient is under anesthesia, there's very little he or she can do to contribute to the safety of the operation.
   Thus, it's probably reasonable to think that the number of plastic-surgery accidents is determined by the levels of doctor (injurer) precaution and patient (victim) activity.
   On the other hand, consider the health and environmental risks posed by privately-owned nuclear power plants. There are no feasible precautions for potential victims; the number of accidents depends on the level of care taken by plant workers (injurer precaution) and the original decision of how many plants to build and their locations (injurer activity).
   Assume that perfect compensation is possible in both cases, and neither cosmetic surgeons nor nuclear power plant owners are judgment-proof.
   (a) First, suppose the price of cosmetic surgery is set without regard for the liability rule – say, by government regulation – and that patients correctly perceive the risks of surgery.
   Cosmetic surgery and nuclear power favor different liability rules: strict liability leads to more efficient outcomes in one case, simple negligence leads to more efficient outcomes in the other. Explain which situation favors which rule, and why.
   (b) Now suppose instead that the supply of plastic surgery is perfectly competitive, so that surgeons earn zero profits and surgeons' expected liability costs are incorporated into prices.
   (i) Explain why either strict liability or simple negligence will lead to efficient outcomes in plastic surgery if patients correctly perceive the risk of accidents.
   (ii) Which rule will lead to better outcomes if patients underestimate the risk of surgery? Explain why.