The Legal and Economic Consequences of Wrongful Termination

James N. Dertouzos, Elaine Holland, Patricia Ebener
This research is supported by The Institute for Civil Justice.

ISBN: 0-8330-0915-X

The RAND Publication Series: The Report is the principal publication documenting and transmitting the Institute’s major research findings and final research results. The Note reports other outputs of sponsored research for general distribution. Publications of The RAND Corporation do not necessarily reflect the opinions or policies of RAND’s and the Institute’s research sponsors.

Published by The RAND Corporation
1700 Main Street, P.O. Box 2138, Santa Monica, CA 90406-2138
The Legal and Economic Consequences of Wrongful Termination

James N. Dertouzos, Elaine Holland, Patricia Ebener

1988
The Institute for Civil Justice

The Institute for Civil Justice, established within The RAND Corporation in 1979, performs independent, objective policy analysis and research on the American civil justice system. The Institute's principal purpose is to help make the civil justice system more efficient and more equitable by supplying policymakers with the results of empirically based, analytic research.

RAND is a private, nonprofit institution, incorporated in 1948, which engages in nonpartisan research and analysis on problems of national security and the public welfare.

The Institute examines the policies that shape the civil justice system, the behavior of the people who participate in it, the operation of its institutions, and its effects on the nation's social and economic systems. Its work describes and assesses the current civil justice system; analyzes how this system has changed over time and may change in the future; evaluates recent and pending reforms in it; and carries out experiments and demonstrations. The Institute builds on a long tradition of RAND research characterized by an interdisciplinary, empirical approach to public policy issues and rigorous standards of quality, objectivity, and independence.

The Institute is supported by pooled grants from corporations, private foundations, trade and professional associations and individuals. The Institute disseminates the results of its work widely to state and federal officials, legislators, and judges, to the business, consumer affairs, labor, legal, and research communities, and to the general public.
Board of Overseers

Jack G. Clarke, Director and Senior Vice President, Exxon Corporation; Chairman of the Board of Overseers, The Institute for Civil Justice
Stephen J. Brobeck, Executive Director, Consumer Federation of America
Edward H. Budd, Chairman and Chief Executive Officer, The Travelers Companies
Robert Clements, President, Marsh & McLennan, Incorporated
James A. Greer, II, LeBoeuf, Lamb, Leiby & MacRae
Morris Harrell, Locke Purnell Rain Harrell, former President, American Bar Association
Geoffrey C. Hazard, Jr., Nathan Baker Professor of Law, Yale Law School; Director, American Law Institute
Aileen C. Hernandez, President, Aileen C. Hernandez Associates
Edwin E. Huddleston, Jr., Cooley, Godward, Castro, Huddleston & Tatum
George N. Leighton, Of Counsel, Earl L. Neal & Associates; former Senior Judge, U.S. District Court
Ignacio E. Losano, Jr., Editor-in-Chief, La Opinion; Chairman of the Board, Losano Enterprises
C. Bruce Maines, President and Chief Executive Officer, SAFECO Corporation
Kevin F. McCarthy, Director, The Institute for Civil Justice
Robert F. McDermott, Chairman, President and Chief Executive Officer, United Services Automobile Association
Joseph W. Morris, Gable & Gable; former Vice President and General Counsel, Shell Oil Companies; former U.S. District Chief Judge
Donald E. Nickelson, President, Paine Webber Group, Incorporated
Franklin W. Nutter, President, Alliance of American Insurers
Howard Raiffa, Frank Plumpton Ramsey Professor of Managerial Economics, Harvard University
Paul D. Rheingold, Rheingold & McGovan
Alice M. Rivlin, Senior Fellow, The Brookings Institution
Edward B. Rust, Jr., President and Chief Executive Officer, State Farm Insurance Companies
Howard D. Samuel, President, Industrial Union Department, AFL-CIO
David S. Shrager, Shrager, McDaid, Loftus, & Flum, P.C.; former President, The Association of Trial Lawyers of America
Gustave H. Shubert, Senior Vice President, The RAND Corporation; former Director, The Institute for Civil Justice
Leonard Woodcock, Adjunct Professor of Political Science, University of Michigan; former President, United Auto Workers; former U.S. Ambassador to the People's Republic of China
Kathryn D. Wriston, Corporate Director
Honorary Overseers

Kenneth J. Arrow, Joan Kenney Professor of Economics and Professor of Operations Research, Stanford University
William O. Bailey, Vice Chairman, Aetna Life and Casualty Company
Irving A. Bluestone, Professor of Labor Studies, Wayne State University; former Vice President, United Auto Workers
Archie R. Boe, President (retired), Sears, Roebuck & Company
Guido Calabresi, Dean and Sterling Professor of Law, Yale Law School
Richard P. Cooley, Chairman of the Board, Seafirst Corporation
Donald F. Craib, Jr., Chairman and Chief Executive Officer (retired), Allstate Insurance Group
Thomas R. Donahue, Secretary-Treasurer, AFL-CIO
Laurence S. Gold, General Counsel, AFL-CIO
W. Richard Goodwin
Shirley M. Hufstedler, Hufstedler, Miller, Carlson & Beardsley; former U.S. Circuit Judge; former Secretary, U.S. Department of Education
Edward H. Levi, Glen A. Lloyd Distinguished Service Professor Emeritus, School of Law, University of Chicago; former Attorney General of the United States
John A. Love, Davis, Graham & Stubbs; former Governor of Colorado; former Chairman, Ideal Basic Industries
Laurence E. Lynn, Jr., Dean, The School of Social Service Administration, The University of Chicago
Robert H. Malott, Chairman and Chief Executive Officer, FMC Corporation
Richard L. Mathias, former President, Property-Casualty Insurance Council
Claudeo J. Madberry, III, Chairman of the Board (retired), Bank of America
Edward J. Nohs, Chairman and Chief Executive Officer, CNA Insurance Companies
Samuel R. Pierce, Jr., Secretary, U.S. Department of Housing and Urban Development
Barbara Scott Pretzel, Attorney at Law
Donald H. Rumsfeld, former Secretary, U.S. Department of Defense
William B. Schwartz, Vannevar Bush University Professor and Professor of Medicine, Tufts University
Eleanor B. Sheldon, former President, Social Science Research Council
Justin A. Stanley, Mayer, Brown & Platt; former President, American Bar Association
Ward Wagner, Jr., Cone, Wagner, Nugent, Johnson, Roth & Romano; former President, The Association of Trial Lawyers of America
Robert B. Wilcox, President (retired), Property-Casualty Insurance Council
Sandra L. Willett, former Executive Vice President, National Consumers League
Margaret Bush Wilson, Wilson Smith and Seymour; former Chairman of the NAACP National Board of Directors
Paul S. Wise, Chairman of the Board (retired), Alliance of American Insurers
Charles J. Zwick, Chairman and Chief Executive Officer, Southeast Bank, N.A., former Director of the U.S. Bureau of the Budget
Foreword

A central topic for research in the Institute for Civil Justice is: “How do substantive and procedural changes in legal rules affect the court system as well as the economy and society?” Answering such questions is often extremely difficult. Typically, the substantive legal changes that are the focus of current debate occur some years before the debate intensifies. Efforts to measure these effects are thus frustrated by the passage of time and the intervention of other factors.

Recent developments in legal policies relating to an employer’s rights to terminate employment provide a special opportunity to explore the relationship among substantive legal change, litigation rates, and their effects on economic and social behavior. In a matter of a half dozen years, states across the country have moved from the traditional doctrine of “employment at will” to policies that permit employees to challenge their terminations on the basis of theories of implied contract and good faith covenants. This recent and rapid change in substantive law has attracted increasing attention from corporate executives, employee representatives, and the bar. No one, however, has provided a clear picture of the consequences of the change.

In this report, ICJ researchers take a close look at the phenomenon of wrongful termination. Using a variety of data sources and statistical techniques and building on previous ICJ work, they consider such questions as “What is behind the recent shift in wrongful termination law? Have the changes led to an upsurge in litigation and by whom? How much are juries awarding in these cases? How much do successful plaintiffs actually pocket as a result of their suits? How much does it cost employers to dispose of these cases?” Some of the answers are surprising; others are consistent with previous ICJ research on trends in civil jury verdicts and litigation costs.

This volume is the first in a series of research reports on wrongful termination. It concentrates on changes in trial behavior. Later reports will analyze settlement behavior and investigate how corporate concerns about these legal changes have affected personnel management policies and costs. I expect these results to be valuable to public
policymakers and corporate decisionmakers concerned with employee-employer relations. But beyond that, I expect the research to enhance our understanding of how the legal system shapes economic and social behavior.

Kevin F. McCarthy
Director
The Institute for Civil Justice
Executive Summary

During the twentieth century, employers in the United States have generally had considerable discretion in hiring and firing workers. Under the prevailing tradition, managers were free to terminate an employment relationship at any time, for good reason, bad reason, or no reason at all. However, this employment-at-will theory has been eroding steadily. As a result of recent judicial decisions, firms in some state jurisdictions face important legal limitations on their ability to fire employees.

Wrongful termination litigation could result in firms having to pay substantial legal fees, liabilities, and settlement costs. To avoid legal action managers may have to engage in other costly activities. Companies may have to provide large severance payments or retain poor performers. They could respond to business expansion by using contractors, part time employees, or increased overtime. Higher administrative or personnel costs could also be a direct response to the threat of wrongful termination.

Our initial assessment of these changing laws examines the direct legal costs and liabilities of wrongful termination. By analyzing the magnitude and patterns of these costs, we can determine whether individual sectors of the labor force or business community are likely to be affected. By identifying systematic patterns in awards, post-trial adjustments, settlement offers, and legal fees we can evaluate several proposals for reform, including the limitation of tort liabilities, adoption of standardized severance payments, and mandatory arbitration of employee grievances over termination.

THE EROSION OF THE EMPLOYMENT-AT-WILL DOCTRINE

Early exceptions to employment-at-will were primarily statutory. One of the earliest, the National Labor Relations Act of 1935, recognized the legality of collective bargaining and provides for the possibility of arbitration of grievances over job termination. It also prohibits
terminations on the basis of union activity. The most important changes stemmed from the Federal Civil Rights and Equal Employment legislation barring employment discrimination directed against particular groups in society. A person can not be fired on the basis of race, color, religion, age, sex, or physical handicaps.

Several state courts have further modified the doctrine by recognizing further exceptions that apply to all employees. The most widely recognized is breach of public policy. In these states, employees can not be fired because they refuse to violate laws, blow the whistle on others, or exercise a legally protected right.

Some states' courts have gone even further by recognizing exceptions based on implied or oral contracts. In these jurisdictions, a contract requiring good cause for termination can be inferred from the circumstances of employment, which can include recruiting statements, handbooks, oral representations, past personnel decisions, performance reviews, and promotions.

Finally, several state courts have applied the covenant of good faith and fair dealing to the employer-employee relationship. This theory requires that all employees be treated fairly; and, at the very least, termination must be for good cause. Even when at-will rights are contractually explicit and an employee is fired for just cause, the circumstances of that discharge can violate this covenant. This doctrine is particularly applicable if the employee has had a long term of service, a record of promotions, and no documented record of inadequate performance. Awards under this exception typically allow for punitive as well as compensatory damages.

These theories of wrongful discharge were virtually nonexistent before 1980 when key cases were decided in California, Michigan, and other states. Since that date, however, the theory has spread rapidly, affecting employment law in some manner in a majority of all states. By 1985, 37 state courts recognized public policy, 31 recognized implied contract, and 5 recognized the covenant of good faith and fair dealing.

The pattern of judicial decisions on wrongful termination is, for the most part, unsystematic. The prevailing doctrine is not related to wage levels, population demographics, region, and measures of cyclical economic activity. Only the extent of unionization is correlated with the acceptance of implied contract or covenant of good faith and fair dealing theories. The state unemployment rate appears to be negatively but weakly correlated with the adoption of the covenant of good faith. These changes in judicial doctrine can be linked with discernible increases in legal activity. An analysis of wrongful termination suits filed in Los Angeles Superior Court and jury trials across the nation suggests a pattern of activity that is closely correlated with judicial differences over time and from state to state.
JURY VERDICTS IN CALIFORNIA

We analyzed 120 jury trials in California between 1980 and 1986 to determine systematic patterns in case characteristics and trial outcomes. Although trials represent only about 5 percent of all cases filed, jury awards can be a primary factor in motivating settlement behavior and inducing long-run changes in the way business and personnel practices are conducted. The threat of major legal consequences is a necessary condition for wrongful termination to have broader social and economic effects.

The population of terminated employees filing suit represents a broad cross-section of the California labor force. Overall, plaintiffs were victorious in about 68 percent of these cases, enjoying a greater success in the initial years following the revolutionary judicial decisions at the turn of the decade. Although the probability of victory appeared to be unrelated to a variety of plaintiff, defendant, law firm, and case characteristics, the status of insurance coverage was highly correlated with jury decisions. Cases in which both liability and defense costs were covered were much more likely to result in plaintiff victories. In contrast, when insurance companies accepted a duty to defend but were not liable for major damages, plaintiff victory had a much lower probability.

On average, winning plaintiffs won over $650,000 in the initial jury award. Except for the very smallest awards, about 40 percent of the amounts were for punitive damages. Of course, average awards are dominated by a few very large verdicts. Half of the victorious plaintiffs are awarded initial amounts of $177,000 or less.

Award amounts were strongly correlated with measures of economic loss. The earnings and age of the plaintiff can explain over 30 percent of the case-to-case variation in compensatory and punitive damages. With other factors held constant, differences in plaintiff salaries before termination are typically matched by equivalent percentage increases in the money awarded by juries. In addition, jury awards, holding salary constant, rise until age 50. For older employees expected to be in the work force for a short time anyway, awards diminish. For total awards, females appear to receive significantly lower damages. This difference may partially reflect less steep salary growth or lower expected labor force participation of women.

Although not statistically significant, there is some evidence that large and medium-sized defendants are assessed larger punitive damages, suggesting a "deep-pocket" effect. Analyses of several other case and plaintiff characteristics were inconclusive.
PAYMENTS, EXPENSES, AND SETTLEMENT OFFERS

As a result of post-trial activities such as appeal and settlements, final payments to plaintiffs can be considerably lower than the original verdict. On average, initial awards are reduced by about one half. These reductions are greater for large awards. Econometric analysis revealed few additional patterns, though large employers are somewhat more successful at reducing jury awards. Also, final payments appear to be rising about 12 percent per year, holding the original amount constant.

On average, defense billings add up to over $80,000 for a typical wrongful termination case between 1980 and 1986. These fees have been rising between 15 and 24 percent annually, holding other factors constant. In addition, billings increase with the size of the stakes and with the size of the defense firm. For example, a 1987 case involving a potential award of $1.5 million would cost almost $250,000 to defend. These billings would be even higher when the defendant is represented by one of the largest defense firms.

Plaintiff lawyers typically charge a contingency fee of 40 percent. This means that total legal fees, including defense billings, sum to over $160,000 per case. These defense and plaintiff lawyer fees represent more than half of the money changing hands in this litigation.

Despite the rather large average jury award of $650,000, the typical plaintiff receives much less. In fact, the median employee bringing suit can expect to pocket only $30,000 after we account for the losing cases, post-trial reductions, and deducting contingency fees.

Many of the trial participants would probably have benefited from an early resolution of the dispute. Considering legal fees, most defendants would be better off paying the initial demands rather than going to trial. Since the plaintiffs' average settlement demand is consistent with the average final payment, defendants could avoid large legal fees by settling before trial. Of course, this ignores the effect on other employees who may be contemplating wrongful discharge actions.

PROPOSALS FOR REFORM

In response to the rise in the frequency and magnitude of awards for wrongful discharge, several proposed reforms have surfaced. These generally call for solutions that reduce transactions costs, restrict available remedies, or directly control eligibility criteria or standards for wrongful termination.

In our analysis of case filings in California and frequency of trials across jurisdictions nationwide, it was apparent that judicial decisions
on wrongful termination have had measurable effects on the volume of legal activity. Since most of the changes have occurred in jurisdictions that permit punitive damages, proposals to restrict remedies or reduce punitive damages could well dampen the steady growth in wrongful termination litigation. Of course, the removal of a strong deterrent would also reduce any potential efficiency gains associated with induced changes in personnel practices and management.

Despite the visibility of million-dollar jury awards, most plaintiffs receive less than $30,000 after post-trial reductions and legal fees. This suggests that many terminated employees would have benefited from a system, like the one in Great Britain or West Germany, that calls for modest but automatic remedies when an employee is discharged. Of course, such standard severance payment would have to be given to all workers, not merely to those discharged unjustly.

Proposals for alternative dispute resolution such as mandatory arbitration may be sensible given the large transactions costs associated with wrongful termination litigation. For average payments of $208,000, total legal fees exceed the final transfer to the plaintiff. After deducting a 40 percent contingency fee, the plaintiff receives about $125,000. The contingency fees of $83,000 and defense fees of $81,000 sum to $164,000, meaning that transactions costs are nearly 60 percent of the total amount changing hands.

This does not mean that a reduction in per case legal costs necessarily reduces aggregate costs of litigation. High fees, to the extent that they deter litigation and encourage settlements, will reduce the number of trials as cases settle. If the frequency of (demand for) litigation increases by a greater percentage than the fall in fees (price of litigation), then total expenditures will rise, despite the reduction in per case legal fees.

CONCLUSIONS

Despite the uproar over wrongful termination litigation, the aggregate legal costs are really not very large. Annual trials in jurisdictions recognizing the covenant of good faith and fair dealing add up to only 8.8 trials per million workers. With an average final payment of $208,000 and $81,000 in defense fees, the annual cost of jury trials sums to $2.56 per worker. Even after we include estimates of payments and legal fees for the 95 percent of all cases that settle without going to trial, the total expense per worker still amounts to only $12.25.
These aggregate costs are not very large even in comparison with the number of involuntarily terminated employees who are not otherwise protected by collective bargaining agreements, civil service regulations, or explicit employment contracts. Thus, the average legal cost associated with the discharge of an at-will employee is about $200.

These direct costs probably understate the effects of wrongful termination suits. Firms may provide automatic severance payments to workers. Even in individual cases of inadequate performance, managers may be reluctant to terminate employees for fear of the legal consequences. Otherwise productive workers may not have the same motivation to perform, and general employee morale could suffer.

The fear of wrongful termination suits could prevent managers from being flexible in adjusting to business cycles, new investment opportunities, or evolving technologies. As market conditions fluctuate, firms might be unwilling to adjust the full-time labor force, relying instead on overtime, temporary agencies, or outside contractors during transitory expansions. This reluctance to fire anyone could discourage firms from locating in certain jurisdictions, attempting risky business ventures, or purchasing labor-displacing equipment.

In response to wrongful termination suits, administrative costs may rise substantially. Personnel decisions will become methodical and well-documented. Decentralized manager discretion in hiring, firing, promoting, and reviewing employees could be replaced by standard administrative procedures conducted by formal bureaucracies.

Such changes, though costly, could be balanced by a series of benefits stemming from a more efficient utilization of human resources. A central personnel manager is more likely to consider the full range of costs and benefits associated with workplace decisions. In addition, the internal mechanisms for due process, adopted by firms and guaranteed by the civil justice system, could very well enhance security for all workers, improve job allocations, and increase the aggregate wealth available to both employees and employers. Potentially, such benefits could dominate the direct and indirect costs of litigation, thereby making everybody better off. Full consideration of these indirect consequences must await future research.
Acknowledgments

Much of this research would not have been possible without the cooperation of nearly 200 plaintiff and defense lawyers who generously provided detailed information on their cases.

We are also very grateful to Survey Coordinator Nora Fitzgerald and to Survey Operation Supervisors Jennifer Duncan, Rebecca Mazel, and Eric Nilson. At an early stage, Alexis Baran and Helen Giglio made important contributions in extracting information from Los Angeles Superior Court records.

This report benefited from the thoughtful comments of several RAND colleagues and outside reviewers. In particular, Richard Victor, Arleen Leibowitz, and Deborah Hensler provided numerous valuable suggestions for improving this research. We also appreciated comments from Gustave Shubert and Syam Sarma, and outside reviewers Bruce Clements, Mary Gambardella, Arnold Gillmer, Jay Greer, William Quackenbush, George Noud, Wayne Sorenson, and Rogers Taylor.

Finally, special thanks to Byron Phillips who provided general support and to Joanna Campbell for outstanding secretarial and research assistance.
Contents

FOREWORD ........................................ iii
EXECUTIVE SUMMARY .............................. v
ACKNOWLEDGMENTS ............................... xi
TABLES ............................................ xv

Section

I. INTRODUCTION ................................. 1

II. THE EROSION OF TRADITIONAL EMPLOYMENT-AT-WILL DOCTRINE .......... 4
Statutory Exceptions to Employment-at-Will ........ 4
Recent Judicially Created Exceptions to
Employment-at-Will ................................... 5
Prospects for the Future ............................ 11
The Pattern of Changes in Wrongful Termination
Law ...................................................... 13
Judicial Doctrine and a Rise in Litigation ............ 15

III. A DESCRIPTION OF WRONGFUL TERMINATION
TRIALS IN CALIFORNIA .......................... 19
The Participants ................................... 20
The Role of Insurance ............................... 23
Trial Outcomes: Case Characteristics and Jury
Awards ................................................... 24
Predicting Case Outcomes ........................... 26
Regression Analysis of Damages Awarded ............. 29

IV. PAYMENTS, EXPENSES, AND SETTLEMENT
BEHAVIOR .......................................... 33
Post-Trial Adjustments to Jury Verdicts ............... 33
Litigation Costs ..................................... 37
A Comparison of Awards, Payments, and Legal
Fees ................................................. 39
Settlement Offers, Demands, and Case
Characteristics ..................................... 41

V. POLICY IMPLICATIONS AND CONCLUSIONS .......... 44
Summary of Empirical Results ................. 44
Proposals for Reform ......................... 46
The Indirect Consequences of Wrongful
Termination ........................................... 47

Appendix
A. ECONOMETRIC RESULTS ............................. 49
B. DATA COLLECTION METHODS ..................... 59
C. SURVEY OF WRONGFUL DISCHARGE LITIGATION
   QUESTIONNAIRE ................................. 69

REFERENCES .................................. 73
# Tables

1. State court rulings: challenges to traditional doctrine ........................................... 13
2. Court filings, Los Angeles Superior Court .......................................................... 15
4. Plaintiff profile ........................................................................................................ 21
5. Size of defendant, number of employees .............................................................. 22
6. 1986 size frequency of law firms ............................................................................ 22
7. Insurance coverage in wrongful termination cases ............................................... 24
8. Miscellaneous case characteristics ........................................................................ 25
9. Summary of jury verdicts in wrongful termination trials ....................................... 26
10. Distribution of jury awards .................................................................................... 27
11. Employee age and jury awards ............................................................................. 31
12. Disposition of cases ............................................................................................... 34
13. Final payments ....................................................................................................... 35
14. Case disposition and post-trial payout ratios ......................................................... 36
15. Reported legal costs and fees ................................................................................. 38
16. Estimated final payments and legal costs for jury trials ......................................... 40
17. Distribution of estimated payments and costs for jury trials .................................... 41
18. Settlement demands and offers by verdict ............................................................. 42
19. A description of payments, costs, settlement offers, and demands .......................... 43

A.1. Systematic patterns in state law: a logistic analysis ............................................. 50
A.2. Regression analysis of reported trials nationwide .............................................. 51
A.3. Logistic analysis of jury verdicts .......................................................................... 52
A.4. Patterns in jury awards: Econometric analysis .................................................... 53
A.5. Econometric analysis of final payments ............................................................... 55
A.6. Patterns in legal fees for the defense ................................................................. 56
A.7. Regression analysis of settlement demands and offers ....................................... 58
B.1. Cases reviewed and candidate cases identified .................................................... 61
B.2. Unlocated cases .......................... 61
B.3. Court filings, Los Angeles Superior Court .......................... 62
B.4. Attorneys surveyed per jury verdict .......................... 63
B.5. Questionnaires mailed to attorneys .......................... 64
B.6. Number of questionnaires returned per jury verdict .......................... 66
B.7. Logistic analysis of case and attorney completion rates .......................... 67
B.8. Probability of cases being open: Logistic analysis .......................... 68
I. INTRODUCTION

Since the beginning of the Industrial Revolution, an individual's continued employment has normally been at the discretion of the employer. This "employment-at-will" doctrine has its philosophical roots in the laissez faire tradition of neoclassical economics,¹ under which managers are free to terminate an employment relationship at any time, for good or bad reason or for no reason at all.

Over the years, this employment-at-will theory has been eroding steadily. Initial challenges to the theory were primarily statutory and the changes came slowly. More recent judicial decisions have had swift and dramatic effects. Although not affecting all jurisdictions in the same degree, court decisions have limited the circumstances under which firms can fire employees legally.²

These judicially created changes could have far-reaching implications, both good and bad, for the workplace. At the very least, a large volume of wrongful termination litigation could impose substantial legal fees, liabilities, and settlement costs on businesses. These direct expenses, if large, might threaten the ability of marginal firms to survive in the marketplace, especially if these costs are not borne equally by firms of differing size or competitive circumstances. The threat of legal action could also alter the conduct of personnel management and employee relationships. The potential for litigation will affect hiring and firing decisions. Even in individual cases of inadequate performance, managers will be reluctant to terminate employees for fear of the legal consequences. In such circumstances, otherwise productive workers may not have the same incentives to perform and overall employee morale could suffer.

The spectre of wrongful termination could also prevent managers from being as flexible in their response to changing market conditions, risky investment opportunities, or technology advances. As business fluctuates, firms will be less willing to make short-run adjustments to the full-time labor force. Personnel managers might prefer maintaining a stable pool of permanent employees while relying on overtime, temporary agencies, or outside contractors during transitory

¹In particular, the perfectly competitive paradigm suggests that in a world characterized by absolute mobility, complete information, and the absence of market power, employment-at-will is economically efficient.
²See, for example, "When Can An Employee Be Fired?" Los Angeles Times, July 28, 1987.
expansions. This inability to reduce employment costlessly could also
discourage firms from locating in certain jurisdictions, attempting uncer-
tain business ventures, or adopting labor-saving technologies.

In order to avoid wrongful termination suits, firms may also incur
large administrative costs. Personnel decisions will become methodical
and well-documented. Decentralized manager discretion in hiring, fir-
ing, promoting, and reviewing employees could be replaced by standard
administrative procedures conducted by formal bureaucracies.

Such changes, though costly, could also result in a more efficient
utilization of human resources. An independent personnel manager is
more likely to consider the full range of costs and benefits associated
with workplace decisions. In addition, the internal mechanisms for due
process guaranteed by the civil justice system could very well enhance
security for all workers, improve job allocations, and increase the
aggregate wealth available to both employees and employers. Poten-
tially, such benefits could dominate the direct and indirect costs of litiga-
tion, thereby making everybody better off.

Although our study does not assess these broader economic effects of
wrongful termination suits explicitly, our empirical analysis is an
important initial step toward understanding the direct and indirect
consequences of the evolving doctrine. We evaluate the importance of
these changing laws by examining the magnitude of associated legal
costs and liabilities. By analyzing patterns in these legal outcomes, we
can also assess whether individual sectors of the labor force or business
community are affected more than others. If such distributional conse-
quences exist, the potential for economic distortion is higher.

Our research begins with a description of the evolving doctrines and
provides evidence on systematic patterns in court decisionmaking.
Such patterns, if indeed they exist, could provide important insights
into judicial motives and legal and economic consequences. The
growth and patterns of legal activities nationwide and in California,
believed to be the hotbed of wrongful termination litigation, are also
analyzed. We describe in detail 120 California jury verdicts on wrong-
ful termination. By identifying systematic patterns in awards, post-
trial adjustments, settlement offers, and legal fees, we address the fol-
lowing research and policy questions, among others:

---
3Our analysis of these cases should also be of interest to those more generally con-
cerned about the operation of the civil justice system. Wrongful termination law,
because of its rapid but uneven evolution across jurisdictions, provides a unique experi-
mental setting that automatically controls for several factors likely to complicate the
analysis of broader samples of litigation. Although varying along several dimensions of
research interest, the legal participants, issues, and court processes are fairly homogene-
ous, increasing our confidence that estimated relationships are not caused by spurious
correlations between measured variables and unobserved case characteristics.
— How big are the stakes? Are they large enough to induce changes in economic behavior?
— How important are punitive damages? What effect would the elimination of tort liabilities have?
— Who are the winners and losers? Do wrongful termination suits affect certain business sectors or labor groups more than others?
— Do jury awards reflect predictable economic losses or are they un��统atic? Could a system of standardized severance payments provide adequate compensation for most plaintiffs?
— How large are the legal fees in comparison with the amounts actually pocketed by plaintiffs. Do high transactions costs justify the adoption of alternative means of dispute resolution?
II. THE EROSION OF TRADITIONAL EMPLOYMENT-AT-WILL DOCTRINE

Despite rapid changes in the evolving law on wrongful termination, the prevailing doctrine varies widely from state to state. Although we were able to identify some interesting empirical patterns, they are, for the most part, surprisingly unsystematic. We link these changes in the law with increases in the volume of legal activity based on wrongful termination suits.

STATUTORY EXCEPTIONS TO EMPLOYMENT-AT-WILL

One of the earliest statutory restrictions of employment-at-will aimed solely at the employment relationship was the federal National Labor Relations Act of 1935, which recognizes the legality of contractual constraints achieved through collective bargaining, provides for arbitration of employment grievances, and prohibits employers from terminating employees because of union activity. Later laws also limited employment-at-will by creating rights or obligations of employees and prohibiting employers from terminating an employee for exercising those rights and obligations. These laws included the Fair Labor Standards Act of 1935 (setting wage and hour standards), the Selective Service Act of 1940, the Consumer Protection Act of 1968 (prohibiting termination of an employee for garnishment of wages in certain circumstances), the Occupational Safety and Health Act of 1970, and the Employment Retirement Income Security Act of 1974 (“ERISA”) (establishing standards for employee pension plans).

Even more important limitations on employment-at-will were the federal antidiscrimination laws of the 1960s and 1970s protecting certain classes of employees from termination, or any other discrimination, on the basis of their identifying characteristics. The earliest of these were the Equal Pay Act of 1963 and the Civil Rights Act of 1964 (primarily Title VII of that Act), which prohibits discrimination on the basis of race, color, sex, religion, or national origin. This was followed by the Age Discrimination in Employment Act of 1967, prohibiting discrimination against employees over 40 years of age, and the Rehabilitation Act of 1973, prohibiting discrimination against handicapped employees.
Not only has the federal government imposed such restrictions of the employers' right to terminate, many states have passed similar laws. For example, California has statutes prohibiting discrimination against employees on the basis of race, color, religion, sex, marital status, handicap, age or national origin (Government Code sections 12900 et seq.); filing a complaint concerning wage-hour violations (Labor Code section 98.6); filing a Workers Compensation claim (Labor Code section 132a); reporting wrongdoing to government or law enforcement agencies (Labor Code section 1102.5); missing work because of jury duty or appearance as witness (Labor Code section 230); refusal to take a lie detector or similar test (Labor Code section 432.2); union activity (Labor Code section 923); political activity (Labor Code section 1102); wage garnishment (Labor Code section 2929); exercising rights under the state occupational safety and health act (Labor Code sections 6310 and 6311); or, most recently, for having AIDS.

Despite this long list of federal and state statutory limitations on employment-at-will, the doctrine continued to be the dominant force in the workplace until the early 1980s. Many employees were still not covered by any special protection law. Even employees who did fall in a protected group could still be discharged for any or no reason as long as the reason was not membership in the protected group.

RECENT JUDICIAŁLY CREATED EXCEPTIONS TO EMPLOYMENT-AT-WILL

In the early 1980s state courts, led by the judiciary in California and a few other states, began creating additional limitations on the employment-at-will doctrine. For the most part they are not based on statute and, indeed, in some instances appear contrary to existing statute. For example, California Labor Code section 2922 states that "[a]n employment, having no specified term, may be terminated at the will of either party on notice to the other." Despite this language, the California courts have in recent years held that employment for an unspeciﬁed term may not be terminated by the employer in many circumstances. These judicially created limitations on the employers' right to terminate at will fall into three primary categories: contractual right to continued employment, terminations contrary to public policy, and terminations in violation of an implied covenant of good faith and fair dealing. All three categories are referred to as the theory of wrongful termination or wrongful discharge.
Contractual Right to Continued Employment

Even under traditional employment-at-will theory, the parties had the right to contract for employment for a specified term, and these contracts would be enforced by the courts. However, these contracts had to be clearly stated (generally in writing), they usually had to be for a set term, and courts normally required proof that the employee had given some consideration to the employer in return for the promise of continued employment. In recent years the courts have been much more willing to find a contractual right to continued employment even in the absence of these factors. The courts have found such contracts based upon express statements of the employer, indirect statements of the employer, and the general context of the employment relationship.

Express Statements. If an employer expressly states that it will not terminate an employee, it is a fairly easy step for a court to conclude that the employer should be held to its promise, even if the promise would be unenforceable under traditional employment-at-will because of technical defects. California courts took this step several years ago.

One of the typical early cases is Drzewiecki v. H & R Block, 24 Cal. App. 3d 695, 101 Cal. Rptr. 169 (1972). In that case the employee had a written document stating that he could be terminated only if he “improperly conducted the business.” Even though the employment was not for a specified term, and there was no evidence that the employee gave the employer any special consideration for this promise, the California court held the employer to its express, written promise.

Another early California case involving slightly different circumstances is Rabago-Alvares v. Dart Industries, Inc., 55 Cal. App. 3d 91, 127 Cal. Rptr. 222 (1976). In that case the employee was orally promised she would not be terminated “as long as she did her job” and that any decision to terminate her would be personally reviewed and approved by the management representative making her this promise. The promises were made to induce her to leave a secure job with another company because the employer had particular need of her skills. The court enforced this oral promise in these circumstances.

These cases, although moving beyond traditional employment-at-will doctrine, had little effect on the employment practices of California employers because few terminations presented similar facts of express promises of continued employment in writing or supported by special consideration by the employee. Later judicial exceptions based on contractual theory, however, applied to more employees and had a greater effect.
Indirect Statements. A step beyond finding contractual rights based on express statements is basing contractual rights on indirect statements of the employer that were never intended to create such rights. The leading case exemplifying this judicial exception came from the Michigan Supreme Court in 1980, approximately the same time as the first important California cases on wrongful discharge under other theories. In *Toussaint v. Blue Cross & Blue Shield*, 408 Mich. 579, 292 N.W. 2d 880 (1980), the employee admitted that he had no written contract and gave no special consideration for continued employment. He made only vague claims of oral promises of continued employment. However, he pointed to an internal policy manual of the employer that stated it was the company policy to terminate employees only for just cause and claimed that this gave him a contractual right to continued employment unless the company could prove it had just cause to discharge him. The Michigan court held that this internal policy manual did give the employee a contractual right to continued employment, even though that may not have been the employer's intention, the employer could have changed the policy unilaterally, and there was no evidence the employee had been aware of the policy manual or relied on it in deciding to accept employment.

Context of Employment Relationship. The third prong of the contractual rights exception to employment-at-will gives employees contractual rights to continued employment in the absence of any statement by the employer. The contractual rights are implied from the conduct of the employer during the course of the employment relationship.

One of the leading cases under this theory is the California Court of Appeal case of *Pugh v. See's Candies*, 116 Cal. App. 3d 311, 171 Cal. Rptr. 917 (1981). The court in this case relied upon several factors to find a contractual right to continued employment: 32 years of employment with many promotions and salary increases; the general company policy, as exemplified by its treatment of other employees, not to terminate without cause; company personnel policies implying fair treatment, although not explicitly promising continued employment; the general practice in the industry not to terminate without cause; some discussion at the time of the employee's hire 32 years before that he could expect to be with the company as long as he did a good job; the employee appeared to have a good work record; and the fact that the employee was terminated suddenly and not told why.

Following this case other courts in California, and in other states, have examined the total context of the employment relationship and implied a contractual promise by the employer of continued employment based on such factors as those listed in *Pugh*. This judicial
theory obviously erodes the doctrine of employment-at-will greatly because almost any long-term employee can argue under this theory that there was some implied promise of continued employment.

Terminations Contrary to Public Policy

In the cases discussed above, the courts limited the employment-at-will doctrine by finding that the employer and employee had, in effect, agreed that the employment relationship would be governed by rules other than those normally applying to employment-at-will. Under the public policy exception to employment-at-will, there is no finding of any agreement. Rather the courts refuse to allow the terminations because of the employers' reasons for termination. Thus, this theory is similar to the statutory restrictions discussed earlier. Indeed, the first cases in which the courts limited the employers' right to terminate as contrary to public policy were based on employees' exercise of statutory rights, or refusal to violate statutes.

One of the earliest cases under this theory was Petermann v. International Brotherhood of Teamsters, Local 396, 214 Cal. App. 2d 155, 29 Cal. Rptr. 399 (1964), a decision by the California Court of Appeal. In this case an employee of the Teamsters was fired for refusing to commit perjury before a legislative committee. Because perjury is obviously against the law, the court held that it would be contrary to public policy to allow the union to discharge the employee in these circumstances.

Perhaps the most important case under the public policy exception to employment-at-will is Tameny v. Atlantic Richfield Co., 27 Cal. 3d 167, 164 Cal. Rptr. 839 (1980), a decision by the California Supreme Court. The facts of the case are very similar to those in Petermann v. Teamsters. An employee claimed that he was discharged for refusing to fix gas prices in violation of antitrust laws, and the court held that discharge in these circumstances would be contrary to public policy. Until this case, employees suing for termination in violation of some contractual right or public policy had been able to recover only contractual damages; basically they were limited to recovering lost wages. The California Supreme Court in Tameny, however, held that discharging an employee contrary to public policy was a tort, and the employee was entitled to tort damages. Tort damages are much more extensive than contractual damages and can include punitive damages and recovery for emotional distress, both of which are difficult to quantify and can amount to millions of dollars, depending upon the jury's impression of the employee's distress and the employer's motive. By allowing tort damages in discharge suits, the California court
enormously increased the employers' potential liability and the incentive of discharged employees and their attorneys to bring suit.

The effect of the public policy exception to employment-at-will has been further increased by later cases in many states expanding the theory beyond public policy expressed in statute. For example, in 1981 in Palnmeteer v. International Harvester, 85 Ill. 2d 124, 421 N.E. 2d 876 (1981), the Illinois Supreme Court held that the discharge of a supervisory employee who, contrary to the wishes of his employer, reported possible crimes by fellow employees to the police was contrary to public policy. The employer pointed out that it could have good reason for not wanting its supervisors to report employees to the police—the effect on relations with the union or jeopardizing internal security investigations. The court, however, stated that as a matter of public policy it wanted to encourage citizen crime fighters, even though there was no statutory basis for this policy decision. Courts in other states have since also found discharges contrary to public policy even when the discharge was not for exercising a statutorily guaranteed right or refusing to violate a statute.

Implied Covenant of Good Faith and Fair Dealing

The third recent judicially created exception to employment-at-will, the implied covenant of good faith and fair dealing, is the most far-reaching of all, potentially giving any discharged employee the right to sue his employer. The most well-known and influential of the cases under this theory is Cleary v. American Airlines, 111 Cal. App. 3d 443, 168 Cal. Rptr. 722 (1980), a decision by the California Court of Appeal.

In Cleary an 18-year employee was discharged, allegedly for theft. Since the employee sued claiming his discharge was actually because of his union activities, the court could have decided the case on the public policy theory. Instead an entirely new limitation to employment-at-will was cited. The court stated that an employee could be wrongfully discharged even if there were no allegations of public policy violation, because the discharge violated an implied covenant of good faith and fair dealing that is present in every employment contract, even at-will employment. The court held that this covenant requires employers to treat employees in good faith and not take any action to deprive them of the benefit of their employment without just cause.1

1 The phrase "good faith" on the part of an employer implies honesty, no intention to defraud, and recognition of one's duty or responsibility. In contrast, "bad faith" describes an intention to mislead or deceive, or one in which the refusal to fulfill some obligation is not the result of an honest mistake, but arises out of a sinister motive.
The Cleary court stated that it based its finding of a covenant on two primary factors in the employment situation: long-term employment and a company-established internal grievance procedure. Since then, however, the courts in California and elsewhere have varied greatly regarding the factors required to find such a covenant. Some require more than Cleary, some require nothing more than employment.

Before Cleary the theory of covenant of good faith and fair dealing had been applied against companies that refused to honor insurance policies or other agreements with customers. Cleary’s decision created a potential lawsuit in every employment discharge, entitling the discharged employee to tort damages, including punitive damages and damages for emotional distress. It is plausible to argue that whenever there is a discharge in violation of contractual rights, the covenant of good faith and fair dealing is also breached. Thus Cleary potentially added tort damages to every claim for discharge in violation of contract, damages that had not before been available.

Combination of Other Legal Theories with Wrongful Discharge

Along with the development of these new causes of action has come an increasing use of existing legal theories. For example, it is now common for discharged employees suing for wrongful discharge under one of the theories set forth above to include in their suits claims for slander or libel, intentional infliction of emotional distress, negligent infliction of emotional distress, interference with contractual relationships, and interference with prospective business advantage.

All of these additional tort causes of action existed before the creation of wrongful discharge, but they were seldom used by employees in response to a termination of employment, perhaps because the chance of prevailing on these claims was so low that it was not economically worthwhile to bring suit. With the creation of wrongful discharge, however, that has changed. If a discharged employee is already suing for wrongful discharge, it involves little more effort or expense to add claims for other torts; and these additional claims may provide a judge or jury with grounds for assessing additional tort damages.

Although some states require evidence of physical injury, intentional and negligent infliction of emotional distress may be alleged in connection with almost any termination because most discharged employees can honestly state that they experienced emotional distress as a result of the termination. (Courts generally require that the employee also allege some outrageous act by the employer to support a claim for intentional infliction and breach of some duty of care owed the
employee to support a claim for negligent infliction.) Slander or libel claims are often based on comments by the employer as to the reasons for the termination, either at the time of the termination or in later conversations with prospective future employers. Claims for interference with contractual relationships or prospective business advantage are also often based on interaction between the employer who discharged the employee and possible future employers. Sometimes these causes of action are also based on allegations that other employees of the employer caused the employee’s discharge.

Wrongful discharge claims have also been combined with claims of race, sex, or age discrimination. The use of these combinations has been reduced, however, by court decisions holding that an existing statutory remedy, such as the anti-discrimination laws, is the exclusive remedy available for discharge and preempts all other claims. In other words, the courts have held that an employee cannot sue for wrongful discharge if the employment termination was unlawful under some statute, but instead must sue only under that statute. Since the tort remedies under wrongful discharge are more extensive than the remedies normally available under the anti-discrimination statutes, most attorneys prefer to sue on a theory of wrongful discharge. When additional causes of action, whether tort or discrimination, are combined with wrongful discharge, they are generally secondary. The broadest theory, and the one offering the greatest potential recovery, is wrongful discharge.

PROSPECTS FOR THE FUTURE

Wrongful discharge was created only in the early 1980s, so the law is still in a state of flux in many states. Many are considering which theories to accept; others are still considering whether to adopt any form of the doctrine. Even in California, where the theory is most fully accepted, many questions remain unanswered in part because many of the major decisions on wrongful discharge have come from intermediate appellate courts, rather than the highest state court.

Montana recently became the first (and only) state to pass wrongful discharge legislation. This new law prohibits terminations that are not for good cause, defined as a failure to satisfactorily perform job duties, disruption of the employer’s operation, or other “legitimate” business reasons. However, remedies are restricted. The employee is entitled to lost wages and benefits for a period not to exceed four years from the time of termination. Punitive damages can be recovered, but only by establishing convincing evidence that the employer engaged in actual
malice or fraud. This new law does not allow for the recovery of damages for pain and suffering or emotional distress. Other states may enact similar legislation.

In California, the Supreme Court has only decided one wrongful discharge case, Tameny v. Atlantic Richfield Co., which involved the theory of discharge in violation of public policy. It allowed tort damages in that situation, but there is no indication in the case whether such damages would be available under other theories, such as breach of the covenant of good faith and fair dealing. Indeed, there is no indication in the case that the California Supreme Court even accepts that a theory of covenant of good faith and fair dealing exists; that theory was created by a lower appellate court.

Another major wrongful discharge case pending before the California Supreme Court is Foley v. Interactive Data Corp., which involved an employee who was terminated three months after accurately reporting that a new boss was under investigation for embezzlement on a previous job. Although the claimed reason was for "inadequate performance," the plaintiff had a seven-year history of regular promotions, and pay increases, and had just received a large bonus. This case presents issues as to the availability and extent of the theory of covenant of good faith and fair dealing, whether there must be an enforceable underlying contract before there is a covenant, what damages are available for breach of the covenant, whether a claim for wrongful discharge in violation of public policy must allege that the discharge violated a public policy embodied in statute, and whether the statute of frauds (which requires any contract for a term of more than one year to be in writing) is applicable to wrongful discharge suits based on oral employment contracts.

Foley was argued before the California Supreme Court, and briefs filed, by mid-1986. However, the Court did not issue a decision before Chief Justice Rose Bird and two associate justices left the Court in January 1987 after losing confirmation elections. Therefore, the case will probably not be decided until the three new justices have an opportunity to hear additional arguments on the cases.

Obviously Foley will have a tremendous influence on wrongful discharge law in California. It is also likely to affect the law in other states because California has been one of the leaders in developing the theory of wrongful discharge.
THE PATTERN OF CHANGES IN WRONGFUL TERMINATION LAW

As the discussion above indicates, the theory of wrongful discharge was virtually nonexistent before 1980 when key cases were decided in California, Michigan, Illinois, and other states. Since that date, however, the theory has spread rapidly, affecting employment law in some manner in a majority of all states. However, important differences remain between states. Table 1 provides a summary of the law prevailing in state courts for 1979, 1982, and 1985.2

In 1979, only 19 of the 51 state level jurisdictions (50 states plus the District of Columbia) recognized even the public policy exception to employment-at-will. By 1982, however, four new states adopted the public policy exception, California recognized the covenant of good faith and fair dealing, and two states accepted the theory of implied contracts in employment. Over the next several years, the changes accelerated rapidly with 18 more states rejecting the at-will doctrine in favor of more liberal case law on wrongful termination. By 1985, 37 state courts recognized public policy, 31 recognized implied contract, and 5 recognized the covenant of good faith and fair dealing.3

There is no obvious explanation for the timing or pattern of these rapid changes. Some might argue that the area of wrongful termination merely parallels the liberalization of the civil justice system more

Table 1
STATE COURT RULINGS: CHALLENGES TO TRADITIONAL DOCTRINE

<table>
<thead>
<tr>
<th>Prevailing Doctrine</th>
<th>1979</th>
<th>1982</th>
<th>1985</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employment at will</td>
<td>32</td>
<td>28</td>
<td>10</td>
</tr>
<tr>
<td>Public policy</td>
<td>19</td>
<td>23</td>
<td>37</td>
</tr>
<tr>
<td>Implied contract</td>
<td>0</td>
<td>2</td>
<td>31</td>
</tr>
<tr>
<td>Good faith covenant</td>
<td>0</td>
<td>1</td>
<td>5</td>
</tr>
</tbody>
</table>

2These categorizations were determined on the basis of our reading of case law as described in McCarthy (1986) and Cathcart and Dichter (1986). Although our interpretation provides an accurate summary of the patterns over time and across states, our earlier discussion makes it quite clear that there are important differences in state law within categories.

3In our interpretation, Montana, North Dakota, California, Indiana, and Massachusetts adopted the covenant of good faith and fair dealing by 1985. At the other extreme, at-will employment prevailed in Colorado, Delaware, Florida, Georgia, Iowa, Louisiana, Mississippi, Rhode Island, Utah, and Vermont.
generally, that the labor marketplace is but another target of litigious opportunity. Alternatively, these judicial decisions could be a response to pervasive economic changes that threaten the welfare of certain labor market segments. For example, increased merger activity and associated labor turnover, the decline in smokestack industries, the rapid emergence of electronic and information processing technologies, and the reduction of trade union power and influence have disrupted the workplace by leaving many workers with obsolete skills, reduced employment alternatives, and no institutionalized job security.

We attempted to gain some preliminary insights into these alternative explanations by conducting a statistical analysis of the cross-state pattern of judicial decisions on wrongful termination. We examined several variables describing economic characteristics of states in 1985 including unemployment rates, percent of the work force unionized, wage levels, population demographics, and measures of cyclical economic activity. Of all the factors considered, including economic measures, demographics, and region, only the extent of unionization was found to be strongly correlated with the acceptance of implied contract or covenant of good faith and fair dealing theories. For example, a state in which 30 percent of the labor force was unionized would have had an 80 percent chance of accepting the theory of implied contracts. At the other extreme, one of the Southern states with unionization rates closer to 8 percent would have a probability of only 23 percent. The same qualitative effect, though less important, occurs for the probability of observing public policy or the good faith and fair dealing covenant. Finally, the state unemployment rate appears to be negatively but weakly correlated with the adoption of the covenant of good faith.

These results are interesting though far from conclusive. High rates of unionization are correlated with traditionally liberal attitudes toward the rights of workers. Since many workers in these jurisdictions are already protected, the new doctrines may not have as far-reaching effects. Also, such states and their blue-collar workers have been hardest hit by the secular economic shifts that are likely to cause workplace disruption. Discharged workers in such states, regardless of the overall unemployment rate, are more likely to suffer long-term economic losses and need stronger protection. Firms in such circumstances, however, have a stronger economic incentive to reduce the work force. Pending further analysis, a precise identification of factors relating to the supply of or demand for legal doctrine will remain unresolved.

---

4Union contracts that provide explicit protection to workers often preempt actions under state law on wrongful termination. On occasion, however, workers have challenged decisions of union grievance committees successfully.

5Detailed statistical results are presented in Table A.1 of App. A.
JUDICIAL DOCTRINE AND A RISE IN LITIGATION

Case Filings in Los Angeles

A survey of court documents filed in Los Angeles Superior Court during March and April of selected years since 1980 documents a rapid rise in total cases filed. Los Angeles civil case filings represent about 60 percent of all civil activity in the state of California. Wrongful termination data are presented in Table 2. In 1980, immediately following the initial ruling recognizing the application of the covenant of good faith and fair dealing to employment relationships, 15 wrongful termination cases were filed in the two-month period. Four of these cases involved “upper management” plaintiffs and only two of the complaints referred to the good faith covenant. Two years later, more than twice as many cases were filed during the same period. Over 80 percent of these 39 cases asked for punitive damages under the covenant of good faith. In the following year, the volume of cases more than doubled again, rising to 83 during March and April of 1983. The trend stopped in 1984 but growth resumed, albeit more modestly, in later years. During the same period in 1986, over 100 cases were filed. This suggests that approximately 600 are filed in Los Angeles annually, and,

Table 2

<table>
<thead>
<tr>
<th>Year</th>
<th>Number</th>
<th>Public Policy</th>
<th>Covenant</th>
<th>Percent Upper Management</th>
<th>Unemployment Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>15</td>
<td>0</td>
<td>2</td>
<td>38</td>
<td>5.4</td>
</tr>
<tr>
<td>1982</td>
<td>39</td>
<td>2</td>
<td>32</td>
<td>28</td>
<td>8.3</td>
</tr>
<tr>
<td>1983</td>
<td>83</td>
<td>8</td>
<td>59</td>
<td>22</td>
<td>10.1</td>
</tr>
<tr>
<td>1984</td>
<td>78</td>
<td>6</td>
<td>63</td>
<td>10</td>
<td>7.9</td>
</tr>
<tr>
<td>1985</td>
<td>100</td>
<td>5</td>
<td>88</td>
<td>13</td>
<td>6.5</td>
</tr>
<tr>
<td>1986</td>
<td>102</td>
<td>11</td>
<td>85</td>
<td>20</td>
<td>5.4</td>
</tr>
</tbody>
</table>

See Peterson (1987). According to the 1987 Annual Report of the California Judicial Counsel there were over 90,000 civil filings during fiscal year 1985–86, not including probate and family law cases.

Although classifications are somewhat subjective, an effort to distinguish plaintiffs on the basis of job descriptions or titles was made. In general, officers of large corporations were classified as upper management.
if a proportionate share are filed elsewhere in the state, about 1000 in California.\textsuperscript{5}

The slowdown in the middle of this period could be due to a variety of factors. First, it is possible that the first cases filed were the most favorable to plaintiffs. With the new judicial precedents, many of these plaintiffs were victorious, thereby encouraging lawyers to bring suit under less favorable circumstances. As defense attorneys adjusted and firms learned how to protect themselves against liability, fewer of these marginal suits had the expected payoff. In the latter years, such cases were never brought. This explanation is consistent with evidence presented in the next section. Plaintiff victories were in fact very prominent in the early years, but the probability of a defense verdict was substantially higher between 1983 and 1985.

Other hypotheses are also consistent with the data. Firms may have been more willing to settle grievances outside the legal system after getting hit with large judgments during the earlier period. Also, improved personnel and business practices may have reduced the frequency of wrongful discharges. Finally, the escalation and then downturn in court filings duplicates the business cycle between 1980 and 1984. That is, unemployment rates doubled between 1980 and 1983, presumably creating more situations in which employee termination became an issue. As the economy improved, worker layoffs diminished and, following termination, alternative employment was easier to find. Thus, although the probability of a single discharged worker filing suit may have been steadily increasing over this period, the number of terminations may well have fluctuated largely as a function of general economic circumstances.

For the whole time period, only about 8 percent of the over 400 cases were filed on the basis of public policy. Thus, one would not expect the volume of legal activity to be as great in states that recognize only this exception to the employment-at-will doctrine. In addition, most cases filed include a claim under the covenant of good faith and fair dealing. These cases can involve quite substantial punitive damages. Furthermore, the legal protection afforded by wrongful termination rulings appears to be available to workers other than top executives. Fewer than 18 percent of the cases are filed by upper management employees.

\textsuperscript{5}This estimate assumes that annual totals amount to six times the number of cases during the two-month period surveyed.
Cross-sectional Differences in Wrongful Termination Jury Trials

The effect of judicial decisions on the volume of litigation is also apparent in patterns of wrongful termination trials across the nation. We collected data on numbers of trials for the 10-month period between October 1986 and July 1987.9 This information on trials, aggregated on the basis of the prevailing state doctrine as of 1985, is presented in Table 3.10 In states recognizing no exception to the at-will doctrine, only 15 total trials were reported. On an annual per capita basis, this translates to only 1.3 wrongful termination trials per one million employees. For jurisdictions accepting public policy restrictions only, the number of trials per one million employees is barely higher, 1.7. Although there were 100 trials in states recognizing implied contract theories (but no covenant of good faith and fair dealing) for the 10-month period, per capita trials were only slightly above those in

Table 3
REPORTED TRIALS NATIONWIDE.
NOVEMBER 1986–JULY 1987

<table>
<thead>
<tr>
<th>Prevaling Doctrine</th>
<th>Court Trials</th>
<th>Total</th>
<th>Per Capita¹</th>
</tr>
</thead>
<tbody>
<tr>
<td>At will</td>
<td>Federal 8</td>
<td>7</td>
<td>15</td>
</tr>
<tr>
<td></td>
<td>State 11</td>
<td>6</td>
<td>17</td>
</tr>
<tr>
<td>Public policy only</td>
<td>68</td>
<td>32</td>
<td>100</td>
</tr>
<tr>
<td>Implied contract only</td>
<td>68</td>
<td>82</td>
<td>150</td>
</tr>
</tbody>
</table>

¹Annual trials per one million employees.

9These compilations were extracted from the Wrongful Termination Reporter, Andrews Publications, Inc. Although the completeness of this reporting service has not been validated in this research, the number of trials listed for California is quite consistent with data provided from other sources. Given the estimated number of case filings in L.A. Superior Court during 1983 and 1984, one would expect about 40 annual trials by 1986-1987. This assumes that only 5 percent of the approximately 800 suits filed in California get to trial and that the average time to trial is three to four years. For evidence on settlement frequency, see Danzon and Lillard, 1982. The assumption on time to trial is supported by evidence presented in the next section. The listed number of state court trials in California was 33 for the 10-month period, projecting to 39.6 trials annually.

10For these purposes, we include Michigan in the most liberal category even though it is not, strictly speaking, a state that recognizes the covenant of good faith and fair dealing explicitly. Court rulings in Michigan do imply that employers are legally bound by "legitimate" employee expectations that can be considered part of an implied agreement.
states conforming more closely to the at-will tradition. Of these trials, over two-thirds were conducted in federal courts, indicating that a federal statutory claim probably was involved as well as the implied contract theory under state law. In contrast, 150 trials were reported in jurisdictions that recognize the covenant of good faith and fair dealing. On an annual per capita basis, 8.8 trials per one million employees were reported. Of these cases, approximately 55 percent were tried in state courts. This higher percentage probably reflects a decision on the part of plaintiff attorneys to forgo any federal statutory claims in favor of the more liberal judicial remedies available under the covenant of good faith and fair dealing rather than being constrained by federal statutes.

We identified systematic patterns in cross-state differences in the volume of wrongful termination litigation using regression analysis. These results are described in greater detail in Table A.2 of App. A. These formulations related the number of wrongful termination trials in a state to such factors as the number of employed workers, unemployment rates, changes in unemployment rates, percent labor force unionization, and prevailing state doctrine. The empirical estimates indicate that about 70 percent of the state-to-state variations in reported trials can be explained by these factors.

The number of wrongful termination cases in a jurisdiction is highly correlated with the number of workers. Estimates indicate that states with twice as many employees have about 70 percent more wrongful termination trials, holding other factors constant. The percent unionization also has a positive and significant effect. The effects of the prevailing legal doctrine were consistent with the simple tabulations presented earlier. That is, public policy and implied contract exceptions to at-will employment have negligible effects on the volume of litigation. However, jurisdictions accepting more liberal interpretations under the covenant of good faith and fair dealing can be expected to have about 2-1/2 times the number of trials, holding the number of unemployed workers constant.

These results imply that only the more extreme versions of the judicial changes in at-will employment have resulted in substantially different volumes of litigation. Of course, this conclusion should be made with caution pending more detailed analysis. In particular, the available cross-state data describe court trials only, and the more recent judicial decisions, especially given the long time to trial, may not yet be detectable.
III. A DESCRIPTION OF WRONGFUL TERMINATION TRIALS IN CALIFORNIA

This section describes 120 jury trials decided in California between 1980 and the first quarter of 1986. It presents detailed information on plaintiffs, defendants, law firms, and the extent of insurance coverage and the role of systematic relationships between such case characteristics and trial outcomes. Several questions of potential policy importance are addressed.

- What are the characteristics of plaintiffs? Do plaintiffs represent a typical cross-section of the labor force or are certain market segments affected more frequently?
- Which firms are being sued? Is wrongful termination a problem for "big business" or are all businesses potential targets?
- What are the characteristics of law firms representing wrongful termination clients? Are measures of firm size correlated with measures of case outcomes?
- Is insurance coverage for wrongful termination liability pervasive? Does the existence of insurance alter litigation strategies?
- What are the stakes in wrongful termination trials? Who wins these trials and, for plaintiff victories, how much is awarded? Are these outcomes predictable? Do the awards reflect probable variations in economic loss or are other factors affecting jury decisions?

This subset of cases was chosen for two reasons. First, California doctrine toward wrongful termination was the first to change and, in most respects, remains the most liberal. For other jurisdictions, the volume of cases and history of legal outcomes necessary for doing empirical research simply does not exist. In addition, the cases could be readily identified and information collected from existing ICJ databases compiled from the California publication, Jury Verdicts Weekly.¹

¹For a more detailed description of this source and a discussion of its reliability, see Shanley and Peterson (1983). In general, well over 80 percent of civil proceedings are listed in this reporting service. However, business and contract litigation appears to be less well represented. Although reliable statistics for this smaller category are not available, an inclusion rate of only 65–70 percent is probably more accurate. Wrongful termination cases, a subset of this general class of litigation, might well be similarly under-represented.
The information provided from this weekly newsletter was augmented with a mail and follow-up telephone survey that is reproduced and described in Apps. B and C.

Although this focus on jury trials, representing about 5 percent of all cases filed, is only the tip of the legal iceberg, we believe that it is the best place to begin an investigation of wrongful termination law. Jury verdicts may be a primary factor in motivating settlement behavior and inducing long-run changes in the way business and personnel practices are conducted. The threat of major legal consequences is a necessary condition for wrongful termination to have broader social and economic effects, especially if some sectors of the economy bear disproportionate burdens. Thus, although our work on trial outcomes and how they relate to characteristics of legal participants examines a small slice of the activity, it sets the stage for further work, if warranted by our findings, in the area.

THE PARTICIPANTS

As Table 4 indicates, the population of plaintiffs in wrongful termination suits constitutes a broad cross-section of the labor force. The average plaintiff is 45 years old and makes $36,000 annually. However, ages range from 24 to 65 and yearly salaries can be as low as $8,000 or as high as $250,000. About 13 percent of the sample were in upper management positions. On average, a terminated employee was at the job for eight years. However, over 18 percent of the plaintiffs were at work for less than one year while over 23 percent had job tenure of 15 years or greater. The sample included a large number of woman and minority plaintiffs even though these cases do not include trials based on any of the federal statutory prohibitions against employment on the basis of sex or race discrimination. Finally, in over 80 percent of the cases, the defense cited poor performance or misconduct as the reason for termination. The rest cited economic factors unrelated to the behavior or ability of the plaintiffs.

2Tables 4–6 present statistics describing claimants, defendants, and law firms. Although these descriptions suggest that a wide range of individuals and institutions participate in wrongful termination litigation, it is quite difficult to make definitive comparisons with the general populations. For example, complete data on business, law firm, and work force characteristics were not available. This was especially true for the more relevant population of employees who were involuntarily terminated.

3Without controlling for other factors related to the probability of filing a suit, one cannot make any definitive judgment about whether the number of minorities and women in the sample are representative of their labor force participation. Controls for industrial composition, unionization, and civil service jobs would be required.
Table 4

PLAINTIFF PROFILE

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Average age</td>
<td>45.3</td>
</tr>
<tr>
<td>Median age</td>
<td>45.0</td>
</tr>
<tr>
<td>Age range</td>
<td>24-65</td>
</tr>
<tr>
<td>Average salary</td>
<td>$36,254</td>
</tr>
<tr>
<td>Median salary</td>
<td>$30,000</td>
</tr>
<tr>
<td>Salary range</td>
<td>$8,000-250,000</td>
</tr>
<tr>
<td>Tenure:</td>
<td></td>
</tr>
<tr>
<td>Under one year</td>
<td>18.2</td>
</tr>
<tr>
<td>1-5 years</td>
<td>34.2</td>
</tr>
<tr>
<td>6-10 years</td>
<td>15.7</td>
</tr>
<tr>
<td>11-15 years</td>
<td>8.3</td>
</tr>
<tr>
<td>Over 15 years</td>
<td>23.1</td>
</tr>
<tr>
<td>White</td>
<td>89.3</td>
</tr>
<tr>
<td>Male</td>
<td>68.6</td>
</tr>
<tr>
<td>Executive</td>
<td>13.6</td>
</tr>
<tr>
<td>Middle management</td>
<td>39.8</td>
</tr>
<tr>
<td>Defendant reason for termination:</td>
<td></td>
</tr>
<tr>
<td>Inadequate performance</td>
<td>80.8</td>
</tr>
<tr>
<td>Exogenous economic factors</td>
<td>19.2</td>
</tr>
</tbody>
</table>

Suits were filed against all sizes of firms, representing every industry. Retail trade, manufacturing, hospitals, insurance, and banking were among those included. Although information was not consistently available, data on firm size were available for over 75 percent of the sample.\(^4\) As reported in Table 5, about one-third of all defendants were identified as being large corporations, employing over 10,000 employees. These firms represented over 43 percent of the sample with known size. Over 18 percent of the sample defendants were small businesses employing fewer than 100 workers.

Additional data describing the law firm participants are presented in Table 6. These data were compiled from Martindale-Hubble Directories of Law Firms. Unfortunately, a large number of attorneys are not listed in those directories. However, most of these missing lawyers, representing 32 percent of all cases for defendants and 60 percent for plaintiffs, appear to be associated with the very smallest firms.\(^5\) Typically,

\(^4\) Several online databases compiled for publicly held and regulated firms were utilized. In addition, information on firms belonging to California business and trade associations were useful in obtaining employment data for a large percentage of the defendants.

\(^5\) This was confirmed by about 20 telephone calls to attorneys. One plaintiff attorney belonged to a 10-lawyer firm, and one defense attorney was a partner in a firm having 120 partners and associates. The rest were one- and two-partner firms.
Table 5
SIZE OF DEFENDANT, NUMBER OF EMPLOYEES

<table>
<thead>
<tr>
<th>Employee Category</th>
<th>Percent of Total</th>
<th>Percent of Known</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unknown</td>
<td>24.5</td>
<td>—</td>
</tr>
<tr>
<td>Under 100</td>
<td>18.4</td>
<td>24.4</td>
</tr>
<tr>
<td>100-10,000</td>
<td>24.0</td>
<td>31.8</td>
</tr>
<tr>
<td>Over 10,000</td>
<td>32.5</td>
<td>43.4</td>
</tr>
</tbody>
</table>

defense firms were larger than their legal adversaries on the plaintiff's side. About 40 percent of the defense firms had more than 20 partners and associates, with 12.8 percent having more than 150 attorneys. In contrast, only about 7 percent of the plaintiff attorneys belonged to firms having 20 or more lawyers. None were in the largest category of law firm size. This is not surprising given the standard practice of representing only defense clients on the part of the largest law firms.

Data on numbers of partners and associates in both defense and plaintiff law firms engaged in wrongful termination suits suggest a strong relationship between firm size and the percent of partners. That is, as law firms increase in size, the number of associates increases more than proportionately. For all defense and plaintiff firms combined, 85 percent of the lawyers listed in firms having five or fewer attorneys were partners. In contrast, only 43 percent of the

Table 6
1986 SIZE FREQUENCY OF LAW FIRMS

<table>
<thead>
<tr>
<th>Firm Size, Partners and Associates</th>
<th>Defense</th>
<th>Plaintiff</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Lawyers</td>
<td>Percent</td>
<td>Lawyers</td>
</tr>
<tr>
<td>Unknown</td>
<td>40</td>
<td>32.0</td>
<td>75</td>
</tr>
<tr>
<td>5 or lower</td>
<td>6</td>
<td>4.8</td>
<td>17</td>
</tr>
<tr>
<td>6-10</td>
<td>9</td>
<td>7.2</td>
<td>12</td>
</tr>
<tr>
<td>11-20</td>
<td>19</td>
<td>15.2</td>
<td>12</td>
</tr>
<tr>
<td>21-50</td>
<td>17</td>
<td>13.6</td>
<td>6</td>
</tr>
<tr>
<td>51-150</td>
<td>20</td>
<td>13.2</td>
<td>3</td>
</tr>
<tr>
<td>151+</td>
<td>16</td>
<td>12.8</td>
<td>0</td>
</tr>
</tbody>
</table>
attorneys in the biggest size category were full partners. Although a full-scale study of the law firm economic incentives and the consequences for legal outcomes will require more detailed information on firm characteristics and settlement behavior, this relationship suggests that partners of big law firms may have different incentives than partners in smaller firms. 6

THE ROLE OF INSURANCE

Insurance company participation could also influence the incentives faced by parties to a legal controversy. Because these cases constitute a potential liability that was largely unexpected before the judicial rulings of the early 1980s, most business and corporate insurance policies did not explicitly mention coverage for wrongful termination at first. Coverage was largely uncertain and frequently disputed. In recent years, general liability policies, officers' and directors' liability, and excess coverage insurance generally contain explicit language dealing with obligations for wrongful termination.

Provisions for wrongful termination raise some interesting issues. In general, insurers are reluctant to cover liability for actions that are patently illegal or avoidable. Because sound personnel practices and the exercise of due care could prevent unfavorable legal outcomes in most circumstances, insurers are concerned about firms having insufficient incentives to avoid wrongful termination suits. At the same time, conscientious managers would not wish to pay premiums that reflect the average expected liability since many companies do not adopt preventive policies. As a result, policies are often written to exclude wrongful termination or limit the duty of indemnification once liability has been established. These limits may involve a cap on total liability or, in the extreme, require that the insurance companies reimburse for legal expenses only. Clearly, a duty to defend but not indemnify will drive a large wedge between the insurer and insured. The defendant will wish to avoid liability at any cost; the insurance company would prefer to settle, especially for those cases involving lower expected liability (relative to litigation costs).

Table 7 describes the insurance coverage in effect for 92 of the sample of 120 wrongful termination jury trials. For the other cases, coverage was unknown or not provided. In 30 percent of the cases, no insurance coverage was available. Twelve percent of the defendants had coverage for legal fees, but were not covered for liability. For the

---

6For a discussion of such issues, see Leibowitz and Tollison (1980).
35.9 percent having liability coverage as well, most had no limit. However, about 8 percent of the defendants had limits of under $500,000.

TRIAL OUTCOMES: CASE CHARACTERISTICS AND JURY AWARDS

Table 8 presents basic case characteristics for the 120 jury verdicts reported for the period from 1980 through early 1986. Not unlike other classes of litigation in California, wrongful termination cases typically come to trial just over three years after they were initially filed. In this sample, the time to trial exhibits considerable variation from case to case—ranging from a low of 10 months to more than 5-1/2 years. Of course, with the appeal and post-trial settlement process, cases generally remain open well beyond the date of the original verdict. The closed cases in the sample typically took five additional months to reach final disposition. Some took as long as three extra years. For cases still open, the average time since the jury verdict is 28 months, ranging from 15 months to over four years. The trial length ranges from two to 30 days with an average of one week. Juries can

Table 7
INSURANCE COVERAGE IN WRONGFUL TERMINATION CASES

<table>
<thead>
<tr>
<th>Coverage</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal costs only</td>
<td>12.0</td>
</tr>
<tr>
<td>Legal costs and liability</td>
<td></td>
</tr>
<tr>
<td>No policy limit</td>
<td>20.7</td>
</tr>
<tr>
<td>Limit of one million plus</td>
<td>7.6</td>
</tr>
<tr>
<td>Limit 300-500 thousand</td>
<td>5.6</td>
</tr>
<tr>
<td>Limit under 300 thousand</td>
<td>1.8</td>
</tr>
<tr>
<td>Total with liability</td>
<td>35.9</td>
</tr>
<tr>
<td>No coverage</td>
<td>52.2</td>
</tr>
</tbody>
</table>

*aPercentages based on known insurance coverage. In 23.3 percent of the cases, the extent of coverage was unknown.

The open cases in the sample may be selectively different from those that have reached final disposition. Of course, some of the cases remain open simply because they were tried later in the time period. Efforts to identify systematic differences between cases are reported in subsequent sections.
Table 8  
MISCELLANEOUS CASE CHARACTERISTICS

<table>
<thead>
<tr>
<th></th>
<th>Average</th>
<th>Median</th>
<th>Minimum</th>
<th>Maximum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Time to trial</td>
<td>36 months</td>
<td>32 months</td>
<td>10 months</td>
<td>67 months</td>
</tr>
<tr>
<td>Verdict to disposition:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Closed cases</td>
<td>5 months</td>
<td>3 months</td>
<td>1 month</td>
<td>36 months</td>
</tr>
<tr>
<td>Pending cases</td>
<td>28 months</td>
<td>24 months</td>
<td>15 months</td>
<td>51 months</td>
</tr>
<tr>
<td>Jury deliberation</td>
<td>1.1 days</td>
<td>3.2 days</td>
<td>1 hour</td>
<td>5 days</td>
</tr>
<tr>
<td>Trial length</td>
<td>10.5 days</td>
<td>7.0 days</td>
<td>2 days</td>
<td>30 days</td>
</tr>
</tbody>
</table>

take up to five days to render a decision or, at times, deliver a verdict in under one hour.

As reported in Table 9, juries decided in favor of plaintiffs in 81 of the 120 cases, or 67.5 percent. Although plaintiffs appear to be somewhat more successful in wrongful termination cases than in most other tort cases, this rate is similar to related forms of business litigation.\(^8\) The average award, including defense judgments, was $436,626. On average, about 60 percent of this total was compensation. However, one-third of all trials, or about one half of the plaintiff victories, resulted in punitive damages being awarded. The average award, excluding defense judgments, was $646,855. For these 40 trials, the average punitive damages award was $523,170. Of course, “expected” verdicts or trial averages are reduced by about one-third when defense victories are included.

These award averages are quite large and it is hardly surprising that they are drawing a lot of attention to wrongful termination. To put them in context, recall that the average plaintiff is 45 years old and makes $36,000 annually. Under the assumption that the real rate of salary growth is equal to the discount rate, one can compute an estimate of the present value of future earnings as approximately $720,000.\(^9\) This implies that, on average, juries award victorious employees amounts that are 90 percent of future earnings. Of course, juries are supposed to consider that most workers who are fired

\(^8\)For example, Shanley and Peterson (1983) report that worker injury and contracts/business trials in San Francisco County have 69 and 66 percent plaintiff-win rates, respectively.

\(^9\)That is, salary times years left in the labor force gives a rough but reasonable approximation: $36,000(65-45) = $720,000. For a more detailed discussion of related issues, see King and Smith (1988).
Table 9
SUMMARY OF JURY VERDICTS IN WRONGFUL TERMINATION TRIALS

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of trials</td>
<td>120</td>
</tr>
<tr>
<td>Plaintiff verdicts</td>
<td>81 (67.5%)</td>
</tr>
<tr>
<td>Punitive damage awards</td>
<td>40 (33.3%)</td>
</tr>
<tr>
<td>Average total verdict</td>
<td>$436,626</td>
</tr>
<tr>
<td>Average compensatory</td>
<td>$262,237</td>
</tr>
<tr>
<td>Average punitive verdict</td>
<td>$174,389</td>
</tr>
<tr>
<td>Average total award</td>
<td>$645,555</td>
</tr>
<tr>
<td>Average compensation</td>
<td>$388,500</td>
</tr>
<tr>
<td>Average punitive award</td>
<td>$523,170</td>
</tr>
</tbody>
</table>

eventually find alternative employment, so this level of compensation may seem excessive.

Descriptions of average verdicts in civil litigation can be deceiving because of the statistical dominance of a few huge awards. To circumvent this problem, Table 10 presents information on the distribution of awards. Summary measures are tabulated by award-size quartile as well as for the 10 cases of over a million dollars. The average award within the lowest quartile, representing the smallest 25 percent of all cases, was $32,000. Only 8.4 percent of these smallest payments were for punitive damages. One half of the awards were smaller than $177,000. At the other extreme, the largest 10 awards, ranging from $360,000 to $8 million, averaged nearly $4 million. Despite representing 12.5 percent of the sample, these cases account for 75 percent of the total dollars awarded in 120 wrongful termination trials. In stark contrast, the cases falling below the sample median total 5.9 percent.\(^\text{10}\)

PREDICTING CASE OUTCOMES

To discern systematic patterns in jury decisions, we analyzed the effects of several factors on the probability of plaintiff victory. These econometric results are presented in App. A, Table A.3.

\(^{10}\)These distributional characteristics of wrongful termination awards are very similar to those found generally in civil litigation. See Shanley and Peterson (1983).
Table 10
DISTRIBUTION OF JURY AWARDS

<table>
<thead>
<tr>
<th>Quartile</th>
<th>Total</th>
<th>Lowest</th>
<th>Second</th>
<th>Third</th>
<th>Highest</th>
<th>Million $ Awards</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of cases</td>
<td>81</td>
<td>21</td>
<td>20</td>
<td>20</td>
<td>20</td>
<td>10</td>
</tr>
<tr>
<td>Average award (thousand $)</td>
<td>646</td>
<td>32</td>
<td>78</td>
<td>252</td>
<td>2,299</td>
<td>3,931</td>
</tr>
<tr>
<td>Minimum award (thousand $)</td>
<td>7</td>
<td>7</td>
<td>73</td>
<td>190</td>
<td>360</td>
<td>1,000</td>
</tr>
<tr>
<td>Maximum award (thousand $)</td>
<td>8,000</td>
<td>65</td>
<td>177</td>
<td>350</td>
<td>8,000</td>
<td>8,000</td>
</tr>
<tr>
<td>Percent of total</td>
<td>100.0</td>
<td>1.3</td>
<td>4.6</td>
<td>9.6</td>
<td>84.3</td>
<td>75.0</td>
</tr>
<tr>
<td>Punitive as percent of total damages</td>
<td>39.9</td>
<td>8.4</td>
<td>35.3</td>
<td>26.5</td>
<td>42.3</td>
<td>43.5</td>
</tr>
</tbody>
</table>

Several factors appear to be correlated with case outcomes. For example, plaintiffs enjoyed great success during the initial years following the revolutionary judicial decisions at the turn of the decade. However, after winning 75 percent of the cases between 1980 and 1982, the percentage of plaintiff victories dropped substantially during 1983 and 1984, holding other factors constant, to just under 50 percent. This decline could reflect a change in the mix of cases as plaintiff attorneys became more aggressive following the pronounced successes of the earlier years. With the failure of the marginal cases, the case mix may have then equilibrated at a higher level of plaintiff success.

These data are equally consistent with other hypotheses. Firms may have responded to the wrongful termination threat by altering personnel practices or providing generous severance payments or buyouts. Defense attorneys could have become more aggressive or experienced in mounting opposition or, in contrast, willing to settle cases that had a high probability of plaintiff victory.

We tested the last possibility indirectly by distinguishing cases where the defendants were unwilling to make any settlement offer at all. Such instances occurred in about 27 percent of the cases, possibly for reasons not directly related to the economics of a particular

---

11A significant relationship can reflect either a causal effect on jury behavior or differences in the selection of cases that go to trial instead of being settled. In the absence of a full model of litigant behavior and data on job market events, voluntary severance agreements, case filings, settlements, and court outcomes, these results must be regarded as purely descriptive.
termination. For example, employers may be more interested in conveying a message to other workers. Still, for most litigation, one would expect that plaintiffs would win a smaller percentage of cases in which no offer was made. Although the data gave some support to this hypothesis, the evidence was quite weak. Wrongful termination is such an evolving area that the absence of a defense offer could merely represent ignorance about the probable outcomes.

The status of insurance coverage was highly correlated with jury decisions. For example, cases in which coverage was provided for both liability and defense costs were much more likely to result in plaintiff victories. Predictions based on the statistical estimates indicate that plaintiffs could be expected to be victorious in 94 percent of such cases. This represents a 19 percentage-point increase in comparison with the case having no insurance whatsoever. This result is provocative but difficult to interpret. Once again, there are several plausible explanations. With complete coverage, firms have lower incentives to devote many resources to winning the case or documenting the circumstances of the termination; and they may be less willing to alter personnel practices in response to the changing judicial doctrine. They are therefore more likely to be liable for any given case. Also, insurance company attorneys and claims adjusters are not well prepared to deal with such nonroutine legal circumstances. Lacking relevant experience, they may be unwilling to settle cases even when they have little chance of winning. They may not be capable of mounting a strong defense. Either situation would make for higher frequency of plaintiff victories in cases going to trial.

Cases in which insurance companies accepted a duty to defend but not indemnify had a much lower probability of plaintiff victory. Liability limits of under $300,000 had the same effect.\textsuperscript{12} In these circumstances plaintiffs win much less frequently.\textsuperscript{13} These results strongly suggest that insurance coverage can matter quite a bit.

One could argue, perhaps simplisticly, that firms in this position would be willing to avoid liability at any cost. An aggressive and expensive defense lowers the probability of losing a particular case. We explicitly consider this possibility by including predicted defense fees as an explanatory variable. Because defense expenditures do not

\textsuperscript{12}We distinguished cases in which the settlement demands exceeded the liability limits of the coverage. Presumably policies with very high limits were no different from those paying full indemnification. Policies with low limits, of course, would result in behavior similar to cases in which there was no duty to pay damages, only legal fees.

\textsuperscript{13}To be precise, the statistical estimates indicate that, all things equal, plaintiffs win only 10 percent of the cases where there is defense coverage only. Although this estimate has statistical uncertainty, one can be reasonably sure (with 95 percent confidence) that the plaintiffs will win fewer than 50 percent of the time under these circumstances.
exert an independent influence on the probability of plaintiff victory, this explanation does not appear to have much validity.

As an alternative hypothesis, it is not difficult to imagine why an insurer accepts the duty to defend but not indemnify. Because bringing a case to trial is so costly, legal fees are a major inducement to settle out of court. Defense fees are transactions costs that drive an important wedge between what a plaintiff can expect to gain from winning a trial and what a defendant expects to lose.\footnote{Of course, settlement incentives will depend on several factors, including relative risk aversion, tax implications, likely effects on future litigation and employee behavior, and noneconomic considerations. See Danzon and Lillard (1982) for one example of a useful model of settlement behavior.} That is, both parties can gain from a settlement, especially in cases with low expected payoffs, because of either small prospective damages or low probability of plaintiff victory. The stakes may simply not justify the large fixed cost of going to trial. Plaintiffs are happy to accept a small payment and defendants are anxious to avoid legal fees. The elimination of legal fees but not liability removes the defendant firm's important motivation for settlement. Thus, small stakes cases, with a lower average probability of plaintiff victory, will no longer settle out of court. As a result, defendants will win a high percentage of cases going to trial when defense costs but not liability are reimbursed.

Although the above scenario is certainly plausible, several caveats are in order. For example, although defendant firms may not wish to settle, insurance companies with no duty to indemnify will certainly wish to minimize defense costs. Insurance companies should therefore settle for amounts less than litigation costs even if they are not obligated to pay an eventual award. The bargaining that goes on between the insurance company and the defendant may be very critical in understanding the settlement process.

REGRESSION ANALYSIS OF DAMAGES AWARDED

Although causal implications must be made cautiously, some interesting empirical relationships emerged from statistical analysis of damages awarded by juries.\footnote{Appendix Table A.4 reports econometric results.} The earnings and age of the terminated plaintiff go quite far in explaining the level of damages awarded. These variables can be used to explain over 30 percent of the variance in compensatory and punitive damages.

Plaintiff earnings, measured as the rough approximations to the present value of lifetime earnings discussed earlier, are highly
correlated with compensatory as well as punitive damages awarded. In each case, differences in plaintiff salaries are matched by similar differences in the money awarded by juries. With other factors held constant, a 10 percent increase in salary would generate 9.0 and 10.8 percent increases in compensation and punitive damages, respectively. In addition, holding estimated future earnings constant, the age of the plaintiff is positively correlated with damages. Of course, because salary profiles are shortened with age, the present value of future earnings will be lower for older workers.

These estimates are consistent with the notion that damages are being assessed in proportion to economic loss. Presumably, the direct cost of losing one's job is a function of the employee's salary, expected duration of unemployment, and ability to find a job at an equivalent rate of remuneration. Unfortunately, the level of these variables is quite speculative and controversial in these legal settings.

Ideally, we would like to predict future salary and labor force participation of these plaintiffs on the basis of observable job and employee characteristics. Projecting future work experiences of these terminated employees on the basis of more general classes of workers probably ignores important selection effects. These plaintiffs are surely not representative of typical workers, perhaps not even of workers who have been recently discharged. So we plan in the future to collect information on the duration of unemployment subsequent to the termination and up to the time of trial. This should provide some additional information, although plaintiffs would certainly have few incentives to pursue alternative employment aggressively at least until after the trial.

Age is a proxy for the relevant calculus in two ways. First, older employees have shorter earnings profiles. That is, the economic losses associated with unemployment or lower wages become zero after retirement. Second, older workers can expect a longer duration of unemployment and may never find alternative work. Even if a new job is obtained, the likelihood of earning the same salary is not high, perhaps because older workers have reduced productivity or because salary profiles often reflect firm-specific or job-specific human capital. Either way, older workers will suffer the loss of a bigger percentage of the future earnings stream. Given these two countervailing effects of plaintiff age, awards should increase with age but eventually peak and then decline as the time remaining in the labor force becomes shorter.\textsuperscript{16}

\textsuperscript{16}In contrast to the present value of direct future remuneration, the value of pension plans of most companies peaks after the age of 60. Although we had no data describing the value of lost benefits, our age variable accounts for such effects, at least on average.
Based on econometric models described in App. A, we can compute indexes comparing awards at different ages with the maximum award. These indexes are reported in Table 11. With such other factors as salary held constant, total awards are likely to rise steadily before peaking at about the age of 49. Relative to this maximum, a terminated 30-year-old would receive half as much. In compensatory damages, this individual would receive only 36 percent of the award made to a person at the peak year for compensation. After the age of 49, however, total awards begin to fall, reflecting the shorter period of time over which potential damages can accrue. For example, a 60-year-old would, on average, receive less than two-thirds the award of a plaintiff 11 years younger.

For total awards, females appear to receive considerably lower damages. Because salary level is already included, this might suggest that the system is discriminating against women, but the difference in compensation may partially reflect less steep salary growth or lower expected labor force participation of women. Definitive conclusions must await further research.

With other case characteristics held constant, jury awards do not appear to be increasing substantially over time. Because salary levels, also expressed in nominal dollars, automatically control for inflation over this period, real awards have probably not changed since 1980. However, the selectivity issues discussed earlier may be relevant, so strong conclusions are not warranted.

Although the results are not statistically significant, there is some evidence that large and medium-sized defendants, measured as before

Table 11

<table>
<thead>
<tr>
<th>Award Index</th>
<th>Age</th>
<th>Total Award</th>
<th>Compensation</th>
<th>Punitive</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>30</td>
<td>.54</td>
<td>.36</td>
<td>.79</td>
</tr>
<tr>
<td></td>
<td>40</td>
<td>.86</td>
<td>.72</td>
<td>.99</td>
</tr>
<tr>
<td></td>
<td>50</td>
<td>.92</td>
<td>.99</td>
<td>.90</td>
</tr>
<tr>
<td></td>
<td>60</td>
<td>.66</td>
<td>.70</td>
<td>.23</td>
</tr>
</tbody>
</table>

*These indexes are computed as the ratio of the predicted award at the given age to the maximum award. The maximum occurs at age 49 for the total award, 52 for compensation, and 43 for punitive awards.
by the number of employees, are assessed larger damages. These effects are more pronounced for punitive damages, especially for firms having greater than 10,000 employees. This supports a "deep-pocket" theory, especially since the strongest effect occurs through punitive rather than compensatory damages. Of course, firms with large numbers of employees may, in fact, have empty pockets, a circumstance not identified by the available information. Perhaps more important, larger firms have to be more cognizant of the indirect effects of their actions on other employees. For fear of stimulating future legal difficulties, they may be more reluctant than their "mom and pop" counterparts to settle certain high stakes suits. Finally, legal strategies might be affected by differential tax implications of jury awards.

For large plaintiff law firms, firms having over 20 partners, awards are generally higher. Although that could be due to more effective trial strategies, it is probably the result of differential settlement incentives or a systematic sorting of cases. Large firms having a high volume of cases are able to spread risk and may be more willing, given contingency fees, to go to trial. In addition, through informal marketing, reputation, or referrals, the bigger firms may have greater opportunities to screen prospective clients and select cases with the highest potential payoffs.

We also analyzed several other case and plaintiff characteristics. Large defense firms of more than 150 partners appear to be involved in cases with lower punitive awards, but the evidence is weak. Other variables examined included measures of job tenure, race, insurance status, stated reason for termination, among others. Cited legal theories or alleged tort and contract actions were not significantly related to outcomes.
IV. PAYMENTS, EXPENSES, AND SETTLEMENT BEHAVIOR

To gain a broader perspective on the costs of litigation surrounding wrongful termination, we must look beyond the decisions of jurors. The rather large jury awards are not relevant unless these sums of money actually change hands. We first examine post-trial adjustments in the sample of wrongful discharge awards. An econometric analysis compares final payments with initial awards and other plaintiff, defendant, and law firm characteristics. We were interested in the relative magnitude of these final payments as well as systematic patterns suggestive of differences across economic sectors. Next, we analyze costs of litigation, defense expenses as well as plaintiff contingency fees. Such expenses are likely to be a major component of the total direct cost of this litigation. We then analyze data on settlement offers and demands. Because a vast majority of cases are settled, this exercise was undertaken to provide some insights into the cases that never get to jury trial.

POST-TRIAL ADJUSTMENTS TO JURY VERDICTS

Despite the publicity given the large damage payments awarded by juries for wrongful termination, no information has surfaced about the payments that plaintiffs actually receive. As is well known, many post-trial activities can modify these amounts substantially.¹ Thus, to gain a more complete perspective on this special class of litigation, we surveyed attorneys about the final disposition of cases.

Complete information was obtained for 104 trials, or 87 percent of the sample. Table 12 describes the status of these cases and, for closed cases, the activity that led to final disposition. About 24 percent of the cases were disposed on the initial verdict without additional post-trial activity. All of the closed cases ending in a defense judgment at trial were appealed, but the reversal rate was only 7 percent. In comparison, only 25 percent of the plaintiff victories were appealed. When they were, 28 percent of the original verdicts were overturned, resulting in no payment whatsoever. Finally, 18 percent of the cases, all plaintiff victories, were settled out of court for reduced amounts.

¹For a comprehensive overview of post-trial adjustments to civil damage suits more generally, see Shanley and Peterson (1987).
Table 12
DISPOSITION OF CASES
(Percent)

<table>
<thead>
<tr>
<th>Disposition</th>
<th>Original Verdict for</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>All Cases</td>
</tr>
<tr>
<td>Still pending</td>
<td>15</td>
</tr>
<tr>
<td>Disposed on</td>
<td></td>
</tr>
<tr>
<td>Original verdict</td>
<td>24</td>
</tr>
<tr>
<td>Settlement</td>
<td>18</td>
</tr>
<tr>
<td>Appeal</td>
<td>43</td>
</tr>
<tr>
<td>Plaintiff victory</td>
<td>17</td>
</tr>
<tr>
<td>Defense judgment</td>
<td>26</td>
</tr>
<tr>
<td>Appeals won by plaintiff</td>
<td>40</td>
</tr>
</tbody>
</table>

Defendants refused to settle in any case following an initial verdict favorable to them.

Efforts to identify patterns in the choice of post-trial settlement behavior were largely inconclusive. Although defense verdicts were more likely to be appealed, logistic regressions indicated that no other case, plaintiff, or defendant characteristics could explain post-trial activities. For example, law firm size, award amount, employer category, and insurance coverage were all unrelated to the probability of a case being appealed, settled, or disposed on original verdict. Of course, given the small sample, the empirical relationships between the nature of post-trial activity and case characteristics were insignificant but not very precisely estimated. The power of these tests was therefore quite small, and the best one can say is that there is no evidence one way or another.

At the time of the survey, 15 percent of the cases remained open. In general, cases originally resulting in plaintiff verdicts were somewhat more likely to remain open. No other case-related characteristic, with the exception of the trial date, was correlated with the likelihood of being open at survey time. However, the time between the initial trial date and final disposition depended on the nature of post-trial activity. On average, cases on appeal do not close until 1.5 years after the original trial. Award-reducing settlements are generally negotiated in about six months. All other cases do not remain open for more than a couple of months, suggesting that the “pending” cases in the wrongful termination jury verdict sample are probably cases on appeal.
As a result of these post-trial activities, final payments in wrongful termination trials are substantially below initial jury awards. Table 13 provides data for the cases reporting final disposition. Final payments averaged $150,000, 55 percent of the mean judgment of $272,000. As is typical of civil judgments more generally, final payout ratios decline with award size. Full payments are generally made for the smallest 25 percent of awards. For the mid-range of awards, reductions of 20 percent are typical. At the highest extreme, the ratio of mean final payment to mean original award is lower still. The payout ratio for the quartile of largest awards was .47.

The average awards and final payments reported in Table 13 are below the complete sample mean because plaintiff judgments were more likely to remain open than cases won by the defense. In addition, final payment data were missing from a couple of cases having the largest original awards. Although statistical tests indicated that, in general, larger judgments were not excluded significantly more often, the tabulations suggest a slightly higher payout ratio than prevails for the complete universe of 120 cases. However, the qualitative comparisons we are making are unaffected by these sampling differences.

Table 14 provides comparisons between the nature of post-trial activity and award reductions. About 54 percent of the overall reductions in jury awards were achieved by means of post-trial settlements. The final payments in this category were only 35 percent of the initial jury awards. In addition, substantial reductions were achieved through the appeal process. The bulk of this adjustment stemmed from five appeals that reversed the original plaintiff judgments. Without these reversals on initial awards that averaged over $800,000, the aggregate

<p>| Table 13 |
| FINAL PAYMENTS |</p>
<table>
<thead>
<tr>
<th>Initial Award</th>
<th>Final Payments</th>
<th>Payout Ratio*</th>
</tr>
</thead>
<tbody>
<tr>
<td>All casesb</td>
<td>$272,064</td>
<td>$150,000</td>
</tr>
<tr>
<td>Award averages by quartiles</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lowest</td>
<td>38,337</td>
<td>38,400</td>
</tr>
<tr>
<td>Second</td>
<td>123,899</td>
<td>97,930</td>
</tr>
<tr>
<td>Third</td>
<td>252,866</td>
<td>196,750</td>
</tr>
<tr>
<td>Highest</td>
<td>1,251,305</td>
<td>591,093</td>
</tr>
</tbody>
</table>

*Computed on the ratio of final payments to initial awards.

bIncludes only those cases that have reported reaching final disposition.

Again, see Shanley and Peterson (1987).
payout ratio would have been 73 percent. Although two decisions for
the defense were also reversed on appeal, their average final payment
was only $33,750 and did not greatly affect the totals. Even plaintiff
verdicts that are upheld typically reduce the initial award. For these
12 cases, the payout ratio was .85.

Econometric analysis suggests that large employers are able to con-
siderably reduce their final payments to plaintiffs.\(^5\) It may be that
these defendants are willing to fight awards, thereby sending signals to
employees who are potential legal adversaries. This reduction com-
pletely offsets the higher initial awards that some would attribute to
“deep pocket” jury prejudices. Although other results for large plaintiff
and defense law firms are not as important, these average post-trial
adjustments also appear to offset patterns in original awards.

Final payments appear to be increasing compared with original ver-
dicts. Payments have been rising about 12 percent annually, holding
awards constant. This temporal convergence of payments and jury
verdicts may reflect several factors. First, given the rapid evolution of
wrongful termination in case law, this pattern could be the result of
reduced uncertainty in the legal process as lawyers, judges, and clients
learn standard strategies and develop more accurate expectations about
likely outcomes. Thus, post-trial adjustments can be viewed as error

Table 14
CASE DISPOSITION AND POST-TRIAL PAYOUT RATIOS

<table>
<thead>
<tr>
<th>Disposition</th>
<th>Cases</th>
<th>Average Award</th>
<th>Payout Ratio</th>
<th>% of Total Reduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Still pending</td>
<td>15</td>
<td>$753,206</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Settlement</td>
<td>18</td>
<td>571,015</td>
<td>.35</td>
<td>54</td>
</tr>
<tr>
<td>Rulings on appeal</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Plaintiff reversal</td>
<td>5</td>
<td>833,600</td>
<td>.00</td>
<td>41</td>
</tr>
<tr>
<td>Defendant reversal(^a)</td>
<td>2</td>
<td>0</td>
<td>—</td>
<td>-1</td>
</tr>
<tr>
<td>Plaintiff upheld</td>
<td>12</td>
<td>299,330</td>
<td>.85</td>
<td>5</td>
</tr>
<tr>
<td>Defendant upheld</td>
<td>24</td>
<td>0</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Total appeals</td>
<td>43</td>
<td>180,464</td>
<td>.40</td>
<td>46</td>
</tr>
<tr>
<td>Payment on original plaintiff verdict</td>
<td>24</td>
<td>261,128</td>
<td>1.00</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
<td>$356,033</td>
<td>.55</td>
<td>100</td>
</tr>
</tbody>
</table>

\(^a\)These two cases averaged $33,750.

\(^3\)See App. A.
corrections that become less necessary as the process settles into an equilibrium. Alternatively, the time trend can be the result of changes in settlement behavior stemming from different risk perceptions or post-trial legal preparation on the part of defendants and their legal representatives who did not take the legal threat posed by wrongful termination suits as seriously in earlier years.

Research suggests that awards with a large punitive damage component are reduced more in post-trial activity, but the wrongful termination adjustments do not display this pattern. Of course, the estimated relationship between punitive damages and post-trial adjustments reported elsewhere could be spurious and the result of inadequate controls for case heterogeneity within cells of the tabulations by award-size category.

Empirical results provide weak evidence that post-trial reductions are smaller for older workers and for women. To the extent that an employable young individual has greater incentives to seek alternative work following a termination, compromise settlements are more likely. Because damage estimates will depend in part on the evidence provided by post-discharge labor force activity, young workers may wish to negotiate final payments before resuming their careers. For female plaintiffs, the smaller reductions partially offset the lower initial award they receive in comparison with men. No obvious explanation for this result is apparent.

LITIGATION COSTS

Taking a case all the way through trial can be very expensive, a primary motive for pre-trial civil dispute settlements. In addition, litigation fees are an important consideration in assessing the direct and indirect legal and economic consequences of wrongful termination law.

Approximately two-thirds of both plaintiff and defense attorneys provided information on legal costs and fees for our sample of wrongful termination trials. As displayed in Table 15, attorneys charged an average of about $80,000 for defense fees and expenses. These billings ranged from a low of $2,500 to a high of $650,000. In contrast, all plaintiff attorneys responding to our survey worked on a contingency fee. Over 50 percent of the attorneys charged a flat 40 percent fee. About 10.6 percent of the respondents charged over 40 percent, while about 5.4 percent had contingency rates of under one-third.


\*As we report below, our qualitative results do not appear to suffer from selectivity bias in any substantial way. See App. B for additional evidence.
Table 15
REPORTED LEGAL COSTS AND FEES

<table>
<thead>
<tr>
<th>Reported Defense Costs</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Average fees charged</td>
<td>$80,073</td>
</tr>
<tr>
<td>Median fees charged</td>
<td>65,000</td>
</tr>
<tr>
<td>Minimum fees charged</td>
<td>2,500</td>
</tr>
<tr>
<td>Maximum fees charged</td>
<td>650,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Plaintiff Contingency Rate (Percent)</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Under 33</td>
<td>5.4</td>
</tr>
<tr>
<td>33</td>
<td>19.6</td>
</tr>
<tr>
<td>34-39</td>
<td>9.0</td>
</tr>
<tr>
<td>40</td>
<td>55.4</td>
</tr>
<tr>
<td>Over 40</td>
<td>10.6</td>
</tr>
</tbody>
</table>

Legal fees and expenses for wrongful termination cases display some interesting and systematic patterns. For example, defense fees are higher when stakes are higher. A 10 percent increase in the expected award is typically matched by 5 percent higher defense fees for services and expenses. 6

Fees charged by large defense firms having 150 lawyers or more are substantially higher, with other case characteristics held constant. This result is provocative but unfortunately consistent with several alternative hypotheses. Among others, the largest law firms may charge higher hourly rates, perform more activities in case preparation, or be retained through a selection process whereby they more frequently represent clients who need or desire an aggressive defense. Finally, extra services provided by large law firms may protect the client under a wider set of contingencies that reduce risk in a manner that is not detectable in a small database.

With other factors held constant, defense expenses appear to be rising at the compound rate of 24 percent annually. Because the expected award is expressed in nominal dollars, this rate of growth implies a rapid real increase in legal fees. Once again, this empirical fact can reflect alternative phenomena. The defense bar may be taking

---

6Expected rewards were calculated on the basis of case characteristics and a statistical model of jury awards described in App. A. Predictions were obtained for plaintiff judgments as well as defense judgments for which no damages were actually awarded. Although one might argue that such "shadow" verdicts are for defense victories that systematically differ from plaintiff judgments, the average predicted award for these latter cases was $547,581. The average prediction for plaintiff judgments was slightly higher at $592,289. Even more convincing, results based on only the subset of plaintiff victories gave results that were almost identical.
wrongful termination more seriously following early setbacks, legal strategies may be becoming more sophisticated as this specialty evolves, or changes in settlement behavior may result in only the more complex, hence more expensive, cases coming to trial.

Other case characteristics, including insurance coverage, the size of the plaintiff law firm, and the number of employees working for the defendant, were not significant. However, statistical imprecision makes it difficult to have confidence about the role of these factors.

We found no interesting patterns in the contingency rates charged by plaintiff attorneys. The data suggest a slight recent increase in the number of plaintiff attorneys charging 40 percent or more but the difference is not statistically significant. Similarly, law firm, defendant, or case characteristics were unrelated to the pattern.

A COMPARISON OF AWARDS, PAYMENTS, AND LEGAL FEES

In Table 16, awards, payments, and legal fees are compared for the complete sample. Predictions based on econometric models were utilized to fill in missing observations.\(^7\) For plaintiff verdicts, the average award is $646,000 with a final payment of $307,628, a payout ratio of 0.48. This ratio is slightly lower than for the sample of closed cases reporting final payments because of the slightly greater reductions predicted for pending and large damage cases. Net payments, after plaintiff attorney contingency fees are deducted, average $188,520 with a median of $74,500. The average net payment, after post-trial reductions and legal expenses, is less than 30 percent of the original jury verdict. Remarkably, for all cases including defense judgments, the median payment is only $30,000. That is, despite the high frequency of success and large average jury rewards, half the plaintiffs actually take home a very modest compensation. After discounting this sum (assuming a 9 percent nominal interest rate over this period and a five-year delay from the date of termination to final payment), one is left with the conclusion that the typical plaintiff receives the equivalent of one-half year's severance pay. By inducing terminated employees to accept such a severance, employers could save $84,000 in defense fees.\(^8\)

\(^7\)For final payments, predictions based on the model described in Table 15 were substituted. Legal fees were estimated using the regression results reported above. Since no heteroscedasticity was detectable in either model using Breusch and Pagan (1979) tests, we employed the smearing estimate, developed by Duan (1983), which transforms the predictions for log dependent variables by a multiplicative factor equal to the sample average of exponentiated least squares residuals in each case.

\(^8\)With higher average payments, it is not clear that many plaintiffs would accept such an offer.
Table 16
ESTIMATED FINAL PAYMENTS AND LEGAL COSTS FOR JURY TRIALS

<table>
<thead>
<tr>
<th></th>
<th>All Cases</th>
<th>Plaintiff Verdicts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average award</td>
<td>$436,627</td>
<td>$646,855</td>
</tr>
<tr>
<td>Average final payment</td>
<td>208,212</td>
<td>307,628</td>
</tr>
<tr>
<td>Average net payment (minus fees)</td>
<td>127,590</td>
<td>188,520</td>
</tr>
<tr>
<td>Median net payment</td>
<td>30,000</td>
<td>74,500</td>
</tr>
<tr>
<td>Average plaintiff contingency fee</td>
<td>86,622</td>
<td>119,108</td>
</tr>
<tr>
<td>Average defense legal fees</td>
<td>83,862</td>
<td>90,483</td>
</tr>
<tr>
<td>Final payment/award</td>
<td>.48</td>
<td>.48</td>
</tr>
<tr>
<td>Net payment/final payment</td>
<td>.61</td>
<td>.61</td>
</tr>
<tr>
<td>Net payment/award</td>
<td>.29</td>
<td>.29</td>
</tr>
<tr>
<td>Net/final payment + fees</td>
<td>.44</td>
<td>.47</td>
</tr>
</tbody>
</table>

For all cases, average plaintiff contingency fees are roughly equivalent to legal fees charged by defense attorneys. However, the former are highly related to case outcome. On average, contingency fees are over 30 percent higher than defense fees when plaintiffs are victorious. The net transfer payment to plaintiffs is not even half the sum that eventually changes hands, including net payments, contingency fees, and defense billings.

In Table 17, data from plaintiff victories are presented by size quartile and for million-dollar awards. As before, payout ratios decline systematically with award size. Since contingency rates do not change with award size, fees earned by plaintiff attorneys remain steady at between 37 and 39 percent of the total payment. As the regression analysis described earlier suggested, defense fees do not exhibit the same pattern of growth over the complete range of outcomes. As a result, plaintiff attorneys appear to be undercompensated when final payments are small. However, they receive contingency fees of over $560,000 in cases with million-dollar awards, five times as much as their defense adversaries. Clearly, plaintiff attorneys will wish to settle smaller cases. Indeed, because going to trial imposes high fixed costs independent of the case size or complexity, both parties will wish to

---

9 Of course, these fees are not directly comparable if lawyers are risk-averse. Also, no data are available on the number of hours actually spent by defense and plaintiff attorneys.

10 In trials lost by the plaintiffs, defense fees average about $71,000.
settle small cases out of court. Even for the median case, net payments to the plaintiff are only about 27 percent of gross payments plus legal fees.

SETTLEMENT OFFERS, DEMANDS, AND CASE CHARACTERISTICS

The next two tables present information on reported settlement demands and offers. These cases represent failures in the bargaining process; the data may therefore not truly reflect the amounts at which the parties would have avoided the courtroom.

In Table 18, we find that the lowest demands made by plaintiff averaged $207,710 over the whole period. Average payments were almost identical at $208,212. For these same cases, the average offer was barely over $30,000, including the 25 percent in which no offers were made. When these are excluded, the remaining offers by defendants averaged about $40,000. Offers and demands did not appear to bear much of a relationship to case outcomes. That is, offer patterns were about the same, regardless of whether the plaintiff eventually won the case. For defense victories, the settlement demands were actually higher than for cases in which plaintiffs emerged victorious.
Table 18

SETTLEMENT DEMANDS AND OFFERS BY VERDICT

<table>
<thead>
<tr>
<th></th>
<th>All Cases</th>
<th>For Plaintiff</th>
<th>For Defense</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average payment</td>
<td>$208,212</td>
<td>$307,628</td>
<td>0</td>
</tr>
<tr>
<td>Average demand</td>
<td>207,710</td>
<td>189,318</td>
<td>243,526</td>
</tr>
<tr>
<td>Average offer</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>If offer &gt; 0</td>
<td>40,570</td>
<td>40,235</td>
<td>41,223</td>
</tr>
<tr>
<td>All cases</td>
<td>30,056</td>
<td>30,450</td>
<td>29,289</td>
</tr>
<tr>
<td>Percent offers made</td>
<td>75.1</td>
<td>75.7</td>
<td>71.1</td>
</tr>
</tbody>
</table>

The information provided in Table 19 underscores the evident lack of outcome predictability. For the smallest awards, both demands and offers are substantially below final payments. For the highest 25 percent of all original awards, defendants could have reduced their payment by an average of over two-thirds by agreeing to meet plaintiff demands. Although demands exceed final payments for all but the biggest cases, defendants may still find it worthwhile to settle earlier. Because of the high costs of defense, average plaintiff demands are only 70 percent of the total cost, including transfer payments and legal fees, incurred as a result of the trial.

Data for the median participants suggest similar conclusions. When offers were made, they exceeded final payments 47.0 percent of the time. Even when victorious, plaintiffs would have been better off accepting the original offer 19.6 percent of the time. On the defense side, the sum of costs and final payments exceed demands 54.4 percent of the time, even when considering victories. In over 20 percent of all cases, legal fees were greater than the offer to settle.\(^{11}\)

Although settlement demands fail to mirror eventual payments precisely, they appear to be roughly consistent with reasonable expectations about probable awards. The regression results reported in App. A provide an additional illustration of this point. Demands systematically rise as a function of predicted awards. With expectations held constant, demands are systematically higher when large defense firms are involved and for cases involving older clients. Over time, demands

\(^{11}\)Ignoring the important deterrence effect, the data suggest that most defendants would have been better off paying the demand. Unfortunately, we do not know when these offers and demands were made. Thus, many of the expenses may have already been incurred by the time the recorded demand was made.
Table 19

A DESCRIPTION OF PAYMENTS, COSTS, SETTLEMENT OFFERS, AND DEMANDS

<table>
<thead>
<tr>
<th></th>
<th>All Cases</th>
<th>Quartile</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Average</td>
<td>Median</td>
</tr>
<tr>
<td>Final payments</td>
<td>208</td>
<td>48</td>
</tr>
<tr>
<td>Offer (if &gt; 0)</td>
<td>40</td>
<td>20</td>
</tr>
<tr>
<td>Offer (adjusted)*</td>
<td>46</td>
<td>24</td>
</tr>
<tr>
<td>Settlement demand</td>
<td>204</td>
<td>88</td>
</tr>
<tr>
<td>Defense costs</td>
<td>84</td>
<td>65</td>
</tr>
<tr>
<td>Adjusted offer/final</td>
<td>0.23</td>
<td>0.50</td>
</tr>
<tr>
<td>Demand/final</td>
<td>1.00</td>
<td>1.83</td>
</tr>
<tr>
<td>Offer/final + costs</td>
<td>0.14</td>
<td>0.18</td>
</tr>
<tr>
<td>Demand/final + costs</td>
<td>0.71</td>
<td>0.78</td>
</tr>
</tbody>
</table>

*Excludes cases with no offers and inflates actual offer by 20 percent to account for lower contingency fee in nontrial cases.

have been increasing faster than seems warranted by trends in jury verdicts. This trend may be fueled by the unexpected success of plaintiffs in the early years.

Offers appear to be unrelated to expected jury awards. Instead, they are in the range of what the median plaintiff can expect to gain after post-trial adjustments and deductions for legal expenses. Although these offers may appear to be somewhat meager ex post, they may be acceptable for some risk-averse plaintiffs. The typical amount offered is out of line in comparison with average verdicts, but it is quite consistent with typical severance payments as well as with anecdotal evidence concerning the range of settlements plaintiffs actually accepted.

Because the defendant firm’s concerns extend well beyond minimizing the costs of litigating and resolving a single termination case, this strategy may be quite rational. Settlement offers will inevitably influence future legal outcomes and labor market flexibility, so prudent business practices may well justify taking an occasional legal bath. To the extent that a firm is not overly risk-averse, a tough posture in individual cases may well pay off in the long run.
V. POLICY IMPLICATIONS AND CONCLUSIONS

The 1980s witnessed a dramatic revolution in court doctrine toward wrongful termination. In many states, these judicial decisions have redefined the conditions under which business managers can make personnel decisions without suffering legal consequences. Our research described these rulings and evaluated their swift but uneven legal effects across state jurisdictions. In addition, we provided a detailed examination of the trial outcomes and the effects of defendant, plaintiff, and case characteristics. In this concluding section, we assimilate the major findings of this work and then draw some conclusions concerning wrongful termination and proposals for legislative or statutory reform. Finally, we consider the hidden but potentially more important economic consequences of wrongful termination law.

SUMMARY OF EMPIRICAL RESULTS

In an empirical analysis of several case measures, including jury decisions, damages awarded, legal costs, and trial length, several important patterns emerged. These results were, for the most part, quite consistent with many of the conventional beliefs about the role of economic loss, the significance of post-trial adjustments, and the distribution of jury awards. However, the unique data and institutions provided an excellent opportunity for gaining new insights as well.\footnote{To begin with, the focus on only wrongful termination guaranteed a degree of case homogeneity over several dimensions. Thus, the analyses did not have to be as concerned about controlling for various unmeasurable characteristics. Perhaps more important, the dataset contained information not generally available in the public domain. Detailed descriptions of insurance coverage, law firm characteristics, and the size of the defendant are not generally available. Despite a rather small sample, these variables often had remarkably strong correlations with the outcome measures of interest.}

Some of the more interesting findings include:

- Despite the rather large average jury award of $650,000, most plaintiffs do not receive such large sums. In fact, the median employee bringing suit can expect to pocket only $30,000 after accounting for post-trial reductions and deducting contingency fees.
- On average, defense billings and contingency fees add up to over $160,000 for a wrongful termination case. These lawyer fees represent more than half of the money changing hands in this litigation.
• Although jury awards do not appear to be rising over time, defense fees are escalating at the rate of between 15 and 24 percent annually. Thus, attorney fees are taking an increasing percentage of total legal costs.

• The magnitude of awards made by juries appear to be based on measures of economic loss. In particular, awards are higher for employees with higher salaries at the time of termination. In addition, expected awards, holding salary constant, rise until age 50. For older employees expected to be in the work force for a short time anyway, awards diminish.

• Considering legal fees, most defendants would be better off paying the demands rather than going to trial. Most plaintiffs, however, would have been made worse off accepting the offers.

• The average settlement demand made by plaintiffs is consistent with the average final payment in wrongful termination cases. Correlations between demands and eventual payments are very close.

• The average settlement offer made by defendants is consistent with the median final payment. Differences in these offers are only weakly correlated with final payments.

• On average, awards are reduced by over 50 percent, with large awards being reduced most. After award size is controlled for, punitive damages are no more likely to be reduced.

• Although jury awards do not appear to be growing over time, post-trial adjustments have been smaller recently. This means that final payments have been increasing almost 12 percent annually.

• The probability of plaintiff victory appears to be related to the status of insurance coverage. In particular, plaintiffs win a vast majority of cases in which complete insurance coverage is available. In contrast, defendants prevail more frequently when insurance covers only defense costs or when liability limits are binding. Although these phenomena are consistent with alternative explanations, induced settlement behavior is probably a key factor.

• With other factors held constant, awards appear to be somewhat lower for female plaintiffs, possibly reflecting expectations about future labor force participation or wage growth.

• Awards are higher for employees that have been discharged by large companies having more than 10,000 workers. Although this result suggests a "deep-pocket" conclusion, post-trial adjustments appear to eliminate this differential.
- Although plaintiff attorneys uniformly receive about 40 percent of the final payment, defense billings exhibit some interesting patterns. They are higher when the expected award is greater and legal fees are higher for large defense firms.

Even though the estimated relationships were statistically significant, the interpretation of results remains problematic. Indeed, case characteristics can alter outcomes through effects on the frequency of firm decisions to fire, worker incentives to file suits, and the desire of both legal parties to settle out of court. Without accurate settlement information and in the absence of a full model of plaintiff, defendant, and lawyer behavior, the analysis has limitations. However, the preliminary relationships are interesting enough to believe that gathering more appropriate data and developing a comprehensive model of litigant behavior could pay off handsomely and should have high priority in future research agendas.

PROPOSALS FOR REFORM

In response to the rise in frequency and magnitude of awards for wrongful discharge, several proposed reforms have surfaced. These generally call for solutions that reduce transactions costs, restrict available remedies, or directly control eligibility criteria or standards for wrongful termination. We believe that our research results have important implications for these policy issues.

In our analysis of case filings in California and frequency of trials across jurisdictions nationwide, it was apparent that judicial decisions on wrongful termination have had direct effects on the level of legal activity. Most of the changes have occurred in jurisdictions that allow punitive damages, suggesting that proposals to restrict remedies or reduce punitive damages could well dampen the steady growth in wrongful termination litigation. Of course, the removal of a strong deterrent would also reduce any potential efficiency gains associated with induced changes in personnel practices and management.

Despite the tremendous publicity given big jury awards, popular accounts of potential payouts are very misleading. After post-trial reductions and subtraction of contingency fees, most plaintiffs receive net amounts that are lower than a six-month severance payment. As many as half of the wrongfully terminated employees may have bene-
fited from a system like the ones in Great Britain or West Germany calling for modest but automatic remedies at discharge.\(^2\)

Proposals for alternative dispute resolution such as mandatory arbitration may be sensible given the large transactions costs associated with wrongful termination litigation. For example, for average payments of $208,000, total legal fees exceed the final transfer to the plaintiff. After deducting the typical 40 percent contingency fee, the plaintiff receives about $125,000. The contingency fees of $83,000 and defense fees of $81,000 sum to $164,000, meaning that transactions costs are 31 percent higher than transfer payments.

A reduction in per case legal costs may not reduce aggregate costs of litigation, however. High fees, to the extent that they deter litigation and encourage settlements, will reduce the number of trials as cases settle. If the frequency (demand for) of litigation increases by a greater percentage than the fall in fees (price of litigation), then total expenditures will rise, despite the reduction in per case legal fees. Indeed, the implied decline in settlement propensity of firms having insurance coverage for legal fees but not liability suggests that this outcome is certainly possible.

THE INDIRECT CONSEQUENCES OF WRONGFUL TERMINATION

Despite all the sound and fury over wrongful termination litigation, the aggregate legal costs are really not very large. To put these costs into an appropriate perspective, recall that annual trials in states recognizing the covenant of good faith and fair dealing add up to only 8.8 trials per million workers. If the average verdict results in a payment of $208,000, the sample mean after post-trial reductions, the annual cost of jury trials, including legal fees, amounts to only $2.56 per worker.\(^3\)

Even if we account for settlements, the total direct costs of wrongful termination remain quite small. For example, evidence obtained from

\(^2\)Of course, standard severance payments would have to be made to many more workers than are currently filing suit, thereby making this policy potentially quite costly. However, many workers are already compensated through informal channels quite independent of the civil justice system. For a case study of compensation in the face of labor-reducing technological change, see Dertouzos and Quinn (1985).

\(^3\)Although this per capita estimate has some uncertainty, we believe that, if anything, our calculations overstate the total legal fees associated with wrongful termination trials in California because the per capita measure includes cases heard in federal court. These cases generally combine traditional discrimination with wrongful termination, and they do not allow for punitive damages under federal statute. Thus, typical damages are lower than $208,000.
a mail survey of lawyers involved in settlements indicated that 95 percent of all wrongful termination cases settled for amounts averaging $30,000. Pre-trial defense costs averaged $25,000, bringing the total to $55,000 in direct expenses. These settlement costs, when added to the expense of jury trials, add to only $12.25 per worker.4

These aggregate costs are not very high even compared with those for subsets of the labor force. For example, about half of the workforce is unprotected by collective bargaining agreements, civil service regulations, or explicit employment contracts. Approximately 12 percent of all employees are involuntarily terminated annually under economic conditions that were prevailing in California over this time period. This implies that only about 6 percent of all employees would have any motivation in filing a wrongful termination claim. Thus, the average legal cost associated with the involuntary discharge of an at-will employee is a mere $200.

If we look only at the direct legal costs, it is hard to imagine why firms would be overly concerned about the threat of wrongful termination.5 This suggests that the hidden or indirect costs of wrongful termination will be central in evaluating this litigation. Firms may be avoiding legal action by engaging in other costly activities. Companies can provide large severance payments, retain poor performers, and expand the workforce, when necessary, by using contractors, part-time employees, or increased overtime. In addition, higher administrative or personnel costs could be a direct response to the threat of wrongful termination. Though much more difficult to quantify, such indirect costs must be considered in a comprehensive evaluation of the changing doctrine on employee rights.

In contrast, these costs could be balanced by a series of benefits accruing to firms. Explicit performance standards, centralized administration of personnel decisionmaking, and effective internal mechanisms for worker-manager dispute resolution can profit firms as well as workers. Indeed, to the extent that codified standards imply job security, workers may be willing to supply labor at a reduced level of remuneration, thereby making everyone better off. Such changes are more likely to be stimulated by a legal system that promotes and enforces uniform adoption of such standards for all firms.

---

4Because there are 20 times as many cases that settle, we can estimate that the number of cases per million employees is 20 times 8.8, or 176. Assuming an average settlement cost of $55,000 gives an additional cost of $9.68 per employee annually.

5One could argue that personnel managers are extremely risk-averse. However, many insurance policies cover wrongful termination, so this explanation is not satisfactory.
Appendix A

ECONOMETRIC RESULTS

This appendix presents a technical description of econometric analyses discussed in the text. The model descriptions and tables of estimations are included for the benefit of those wishing more statistical detail and documentation of empirical relationships.

PATTERNS OF JUDICIAL DECISIONMAKING

To identify systematic patterns in the cross-state patterns of judicial decisions on wrongful termination, logistic regressions were estimated. The logistic function is specified as:

$$\log \frac{p_i}{1 - p_i} = \alpha + \beta X$$

where \( p \) is the probability of state \( i \) adopting the doctrine, \( \alpha \) is a constant or intercept, and \( \beta \) are coefficients indicating the effect of explanatory factors, \( X \), on the probability \( p \). From the estimated coefficients reported in Table A.1, the effect of exogenous factors on the probability of adoption can be computed. Several variables describing economic characteristics of states in 1985 were analyzed, including unemployment rates, percent of the work force unionized, wage levels, population demographics, and measures of cyclical economic activity. For each of the major exceptions to the at-will-employment doctrine, a dichotomous variable was set equal to one for states that recognized that exception.

Alternative statistical formulations were examined and led to qualitatively identical results. For example, a proportionate hazard model was estimated, with the dependent variable representing the year of change. Also, an ordered probit characterization, with public policy, implied contract, and the covenant of good faith representing a continuum of outcomes provided no additional insights. For ease of exposition and interpretation, we report only the logistic results here.

As reported earlier, few explanatory factors were important and only those with a t-statistic greater than one are included. Of all the factors considered, only unionization was strongly correlated with the
Table A.1

SYSTEMATIC PATTERNS IN STATE LAW:
A LOGISTIC ANALYSIS
(Standard errors of estimates are in parentheses)

<table>
<thead>
<tr>
<th></th>
<th>Public</th>
<th>Contract</th>
<th>Covenant</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-.082</td>
<td>-1.928</td>
<td>-2.015</td>
</tr>
<tr>
<td></td>
<td>(1.381)</td>
<td>(1.340)</td>
<td>(2.143)</td>
</tr>
<tr>
<td>Unemployment</td>
<td>.081</td>
<td>-.029</td>
<td>-.369</td>
</tr>
<tr>
<td></td>
<td>(.150)</td>
<td>(.140)</td>
<td>(.277)</td>
</tr>
<tr>
<td>Unionization</td>
<td>.018</td>
<td>.119\textsuperscript{a}</td>
<td>.128</td>
</tr>
<tr>
<td></td>
<td>(.049)</td>
<td>(.051)</td>
<td>(.084)</td>
</tr>
</tbody>
</table>

\textsuperscript{a}Significant at 5%.

acceptance of implied contract or covenant of good faith and fair dealing theories. To illustrate, a state in which 30 percent of the labor force was unionized would have had a 80 percent chance of accepting the theory of implied contracts. A state with unionization rates of 8 percent would have a probability of only 23 percent. The same qualitative effect, though less significant, occurs for the probability of observing public policy or the good faith and fair dealing covenant. Although the state unemployment rate appears to be negatively correlated with the adoption of the covenant of good faith, this result is not precise, perhaps because of high collinearity between unionization and prevailing unemployment rates.

PATTERNS IN THE VOLUME OF LITIGATION

Systematic patterns in cross-state differences in the volume of wrongful termination litigation were identified using regression analysis reported in Table A.2. In these formulations, the natural log of the number of wrongful termination trials in a state was related to the log of the number of employed workers, unemployment rates, changes in unemployment between 1984 and 1987, the percent unionization, and dichotomous variables equal to one if the prevailing judicial doctrine accepted public policy, implied contract, or the covenant of good faith. Other exogenous variables representing the region, wage levels, and cyclical economic fluctuations were included in alternative model specifications but were invariably insignificant. Their inclusion did not alter the results reported here.
Table A.2
REGRESSION ANALYSIS OF REPORTED TRIALS NATIONWIDE

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Standard Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-5.316</td>
<td>1.236*</td>
</tr>
<tr>
<td>Log (employment)</td>
<td>0.678</td>
<td>0.097*</td>
</tr>
<tr>
<td>Log (unemployment rate)</td>
<td>0.163</td>
<td>0.359</td>
</tr>
<tr>
<td>Unemployment growth</td>
<td>0.583</td>
<td>0.557</td>
</tr>
<tr>
<td>Percent unionization</td>
<td>0.031</td>
<td>0.014*</td>
</tr>
<tr>
<td>Public policy</td>
<td>0.062</td>
<td>0.268</td>
</tr>
<tr>
<td>Implied contract</td>
<td>0.027</td>
<td>0.238</td>
</tr>
<tr>
<td>Covenant of good faith</td>
<td>0.906</td>
<td>0.337*</td>
</tr>
</tbody>
</table>

*Significant at 5%.

Not surprisingly, the number of wrongful termination cases in a jurisdiction appears to be highly correlated with the number of workers, with an estimated elasticity of almost .7. In addition, the percent unionization has a positive and significant effect. As discussed earlier, public policy and implied contract exceptions to at-will employment have negligible effects on the volume of litigation. However, jurisdictions accepting more liberal interpretations under the covenant of good faith and fair dealing can be expected to have about 2-1/2 times the number of trials.

PREDICTING CASE OUTCOMES

In order to discern systematic patterns in jury decisions, logistic regressions related the probability of plaintiff victory to several possible explanatory variables including the time period, extent of insurance coverage, legal expenditures, and whether a settlement offer was made.

---

*Given the logistic results reported earlier, one might argue that the prevailing doctrines should be treated as endogenous variables. If so, the results in Table A.2 suffer from simultaneous equation bias. Given identification problems, this is impossible to test directly. However, elimination of the dummy variables for state doctrine did not change the remaining coefficients significantly.

**The dummy coefficient of .906 implies a factor of 2.5 since the relevant conversion is exp (.906). See Kennedy (1981).
Coefficient estimates and standard errors are presented in Table A.3. In addition, several variables describing plaintiffs, defendants, and their law firms were initially included. Among these were sex, plaintiff's race, job category, salary, tenure, and age. For the defendant, firm size and stated reasons for dismissal were analyzed. Law firm size categories, for plaintiff and defense firm, were also examined. None of these factors were even marginally significant.

Although these results must be interpreted with caution, some patterns emerged. For example, the percentage of plaintiff victories dropped substantially during 1983 and 1984. The status of insurance coverage was highly correlated with jury decisions. Plaintiffs were much more likely to be victorious when insurance coverage was for defense costs only. Defendants had a better chance in cases in which there was complete liability coverage.

In addition, cases in which a settlement offer was made were no more likely to be won by plaintiffs. Although one could reasonably argue that making an offer is endogenously determined by other factors also included in the regression, we could detect no correlations between the probability of making an offer and any other case, plaintiff, or defendant characteristics.

Finally, the amount of legal fees did not appear to be related to case outcomes. Since defense fees and court outcomes are both likely to be simultaneously determined as a function of other case characteristics (such as the existence of insurance), we used a two-stage least squares methodology. In regressions discussed in Sec. IV and reported below, several exogenous variables not included in the logistic regression of

Table A.3

<table>
<thead>
<tr>
<th></th>
<th>Coefficient</th>
<th>Standard Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-1.300</td>
<td>2.890</td>
</tr>
<tr>
<td>Period 1983–1984</td>
<td>-1.117</td>
<td>.559*</td>
</tr>
<tr>
<td>Liability insurance</td>
<td>1.666</td>
<td>.843*</td>
</tr>
<tr>
<td>Insurance unknown</td>
<td>-.391</td>
<td>.539</td>
</tr>
<tr>
<td>Defense fee insurance only</td>
<td>-3.709</td>
<td>1.111*</td>
</tr>
<tr>
<td>Liability limit</td>
<td>-3.312</td>
<td>1.564*</td>
</tr>
<tr>
<td>Log of legal fees (predicted)</td>
<td>.249</td>
<td>.272</td>
</tr>
<tr>
<td>No settlement offer made</td>
<td>-.692</td>
<td>.519</td>
</tr>
</tbody>
</table>

*Significant at 5%.
Table A.3 were used in a first-stage expression explaining the level of legal expenses. In these regressions, insurance coverage of expense costs appeared to have a positive but weak effect on legal expenditures.

PREDICTING JURY AWARDS

Econometric analysis of jury awards for the 81 wrongful termination cases is presented in Table A.4. In these models, the natural log of total, compensatory, and punitive damages awarded were regressed on several plaintiff, defendant, and case characteristics. The estimated earnings stream is highly correlated with damages. In each case, the estimated elasticity is insignificantly different from 1.0. Holding estimated future earnings constant, the age of the plaintiff is positively correlated with damages.

Table A.4
PATTERNS IN JURY AWARDS:
ECONOMETRIC ANALYSIS

<table>
<thead>
<tr>
<th>Variable</th>
<th>Total Award</th>
<th>Compensation</th>
<th>Punitive</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-9.025</td>
<td>-14.255(^a)</td>
<td>-10.656(^a)</td>
</tr>
<tr>
<td>(6.858)</td>
<td>(5.971)</td>
<td>(9.302)</td>
<td></td>
</tr>
<tr>
<td>log (earnings)</td>
<td>0.809(^a)</td>
<td>0.857(^a)</td>
<td>1.060(^a)</td>
</tr>
<tr>
<td>(0.278)</td>
<td>(0.241)</td>
<td>(0.364)</td>
<td></td>
</tr>
<tr>
<td>log (age)</td>
<td>2.544(^a)</td>
<td>3.486(^a)</td>
<td>2.058</td>
</tr>
<tr>
<td>(0.973)</td>
<td>(0.848)</td>
<td>(1.360)</td>
<td></td>
</tr>
<tr>
<td>Female</td>
<td>-0.688(^a)</td>
<td>-0.433</td>
<td>-0.652</td>
</tr>
<tr>
<td>(0.344)</td>
<td>(0.304)</td>
<td>(0.506)</td>
<td></td>
</tr>
<tr>
<td>Time</td>
<td>0.076</td>
<td>0.080</td>
<td>-0.064</td>
</tr>
<tr>
<td>(0.092)</td>
<td>(0.090)</td>
<td>(0.144)</td>
<td></td>
</tr>
<tr>
<td>Medium employer</td>
<td>0.691</td>
<td>0.658</td>
<td>1.162</td>
</tr>
<tr>
<td>(0.450)</td>
<td>(0.393)</td>
<td>(0.609)</td>
<td></td>
</tr>
<tr>
<td>Large employer</td>
<td>0.638</td>
<td>0.424</td>
<td>2.061(^a)</td>
</tr>
<tr>
<td>(0.483)</td>
<td>(0.429)</td>
<td>(0.753)</td>
<td></td>
</tr>
<tr>
<td>Large plaintiff firm</td>
<td>0.8050</td>
<td>0.765(^a)</td>
<td>0.331</td>
</tr>
<tr>
<td>(0.424)</td>
<td>(0.369)</td>
<td>(0.581)</td>
<td></td>
</tr>
<tr>
<td>Large defense firm</td>
<td>-0.3592</td>
<td>-0.154</td>
<td>-1.188</td>
</tr>
<tr>
<td>(0.485)</td>
<td>(0.422)</td>
<td>(0.766)</td>
<td></td>
</tr>
<tr>
<td>(R^2)</td>
<td>.291</td>
<td>.377</td>
<td>.400</td>
</tr>
</tbody>
</table>

\(^a\)Significant at 5\%.
Since age will also shorten the earnings profile, the model should allow awards to increase with age but eventually peak and then decline as the expected time remaining in the labor force becomes shorter. The specification employed captures these potential nonlinearities in the relationship between age and economic loss due to termination. Although several alternative specifications were investigated, including quadratic formulations and a variety of splined functions for age, none of these alternatives changed the qualitative nature of the results. In addition, they failed to explain as much of the variance in awards and were more difficult to interpret.

For total awards, females appear to receive substantially lower damages. With other case characteristics held constant, jury awards do not appear to be increasing significantly over time. Since salary levels, also expressed in nominal dollars, automatically control for inflation over this period, this result suggests that real awards have been stable.

Although the coefficients are not always significant at the 5 percent level, there is some evidence that large and medium-sized defendants, measured as before by the number of employees, are assessed larger damages. These effects are more pronounced for punitive damages, especially for firms having over 10,000 employees. Jury awards appear to be different for large plaintiff law firms. In general, awards are higher for firms having over 20 partners. Large defense firms appear to be involved in cases with lower punitive awards, but the evidence is weak.

Several other case and plaintiff characteristics were included in alternative specifications. Other variables in regressions not reproduced here included job tenure, race, insurance status, and stated reason for termination, among others. Cited legal theories or alleged tort and contract actions were not significantly related to outcomes.

PATTERNS IN POST-TRIAL ADJUSTMENTS

The relationships among payments, awards, and other case characteristics were also examined using regression analysis. Table A.5 documents the results of this effort. In model I, the actual original award was used in the regression. The natural log of the final payment was regressed on the natural log of the original award as well as several independent case, plaintiff, and defendant characteristics.

Model II uses a measure of the predicted award based on case characteristics. This allows for possible biases in the estimates due to the simultaneous determination of the award and final payment. The first stage of model II included earnings in the expression for the
Table A.5
ECONOMETRIC ANALYSIS OF FINAL PAYMENTS
(Dependent variable: log (final payment))

<table>
<thead>
<tr>
<th>Variable</th>
<th>Model I</th>
<th>Model II</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-.623</td>
<td>-1.073</td>
</tr>
<tr>
<td></td>
<td>(1.670)</td>
<td>(2.410)</td>
</tr>
<tr>
<td>log (award)</td>
<td>.815*</td>
<td>.869*</td>
</tr>
<tr>
<td></td>
<td>(.071)</td>
<td>(.219)</td>
</tr>
<tr>
<td>Punitive %</td>
<td>.102</td>
<td>.130</td>
</tr>
<tr>
<td></td>
<td>(.220)</td>
<td>(.319)</td>
</tr>
<tr>
<td>log (age)</td>
<td>.542</td>
<td>.500</td>
</tr>
<tr>
<td></td>
<td>(.389)</td>
<td>(.431)</td>
</tr>
<tr>
<td>Female</td>
<td>.216</td>
<td>.231</td>
</tr>
<tr>
<td></td>
<td>(.189)</td>
<td>(.207)</td>
</tr>
<tr>
<td>Medium employer</td>
<td>.071</td>
<td>.066</td>
</tr>
<tr>
<td></td>
<td>(.245)</td>
<td>(.248)</td>
</tr>
<tr>
<td>Large employer</td>
<td>-.619*</td>
<td>-.624*</td>
</tr>
<tr>
<td></td>
<td>(.278)</td>
<td>(.281)</td>
</tr>
<tr>
<td>Large plaintiff firm</td>
<td>-.270</td>
<td>-.329</td>
</tr>
<tr>
<td></td>
<td>(.245)</td>
<td>(.334)</td>
</tr>
<tr>
<td>Large defense firm</td>
<td>.495</td>
<td>.497</td>
</tr>
<tr>
<td></td>
<td>(.260)</td>
<td>(.261)</td>
</tr>
<tr>
<td>Time</td>
<td>.116*</td>
<td>.114*</td>
</tr>
<tr>
<td></td>
<td>(.051)</td>
<td>(.053)</td>
</tr>
<tr>
<td>R^2</td>
<td>.801</td>
<td>.581</td>
</tr>
</tbody>
</table>

NOTE: Model I treats the initial jury award as predetermined while Model II uses a two-stage procedure, treating award as endogenous.
\*Significant at 5%.

original award. Although the exclusion of earnings from the second regression seems arbitrary, it was justified by the results of a regression of final payments on all independent variables. For this equation, interpreted in this context as a reduced-form, the coefficient on earnings was virtually identical to the same coefficient in the award equation. Thus, the assumption that earnings had no independent effect on final payment, after adjusting for the effect on original award, seemed reasonable and necessary for purposes of statistical identification. In addition, when the earnings variable was included in model I, it had an insignificant coefficient estimate of .004.

The estimated elasticity of the final payment with respect to the original award is .815, confirming that larger awards are reduced by a
greater percentage. These final payments appear to be increasing in comparison with original verdicts, rising about 12 percent annually, holding awards constant.\footnote{These regressions exclude the five plaintiff verdicts that were completely reversed on appeal. This accounts for a divergence between a predicted payout ratio of .6 for million-dollar awards and the somewhat smaller ratio apparent in simple tabulations by award category.}

The coefficient estimates suggest that large employers are able to substantially reduce final payments to plaintiffs. Although not significant at the 5 percent level, post-trial reductions are somewhat lower for older workers and women. Finally, awards with a large punitive component are not typically reduced any more.

PATTERNS IN LEGAL FEES

Legal fees and expenses for wrongful termination cases were examined for systematic patterns. For model I, the natural log of fees was regressed on the log of the "expected" award and other case characteristics. The expected awards were calculated on the basis of the econometric model of jury awards described earlier. Predictions were obtained for plaintiff and defense judgments. The coefficient estimates and standard errors are presented Table A.6.

Table A.6

<table>
<thead>
<tr>
<th>Variable</th>
<th>Model I</th>
<th>Standard Error</th>
<th>Model II</th>
<th>Standard Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>3.780</td>
<td>1.533*</td>
<td>3.365</td>
<td>1.049*</td>
</tr>
<tr>
<td>log (expected award)</td>
<td>0.471</td>
<td>0.128*</td>
<td>0.549</td>
<td>0.184*</td>
</tr>
<tr>
<td>Log (trial length)</td>
<td>—</td>
<td>—</td>
<td>0.462</td>
<td>0.100*</td>
</tr>
<tr>
<td>Log (settlement demand)</td>
<td>—</td>
<td>—</td>
<td>0.292</td>
<td>0.261</td>
</tr>
<tr>
<td>Large plaintiff firm</td>
<td>-0.133</td>
<td>0.310</td>
<td>0.843</td>
<td>0.297*</td>
</tr>
<tr>
<td>Large defense firm</td>
<td>0.685</td>
<td>0.342*</td>
<td>0.211</td>
<td>0.289</td>
</tr>
<tr>
<td>Large employer</td>
<td>0.150</td>
<td>0.223</td>
<td>0.204</td>
<td>0.186</td>
</tr>
<tr>
<td>Liability insurance</td>
<td>0.234</td>
<td>0.268</td>
<td>0.211</td>
<td>0.289</td>
</tr>
<tr>
<td>Defense insurance</td>
<td>0.532</td>
<td>0.455</td>
<td>-0.235</td>
<td>0.341</td>
</tr>
<tr>
<td>Time</td>
<td>0.240</td>
<td>0.069*</td>
<td>0.150</td>
<td>0.060*</td>
</tr>
<tr>
<td>(R^2)</td>
<td>0.397</td>
<td>0.704</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\*Significant at 5%.
Defense fees rise with the expected award but at a slower pace. The estimated elasticity of fees with respect to the award was .471. Of the other independent case characteristics included, only representation by defense firms having 150 or more lawyers made a difference. However, the large standard errors associated with these estimates suggest strong inferences not be made. In addition, nominal legal fees appear to be rising by about 24 percent annually.

The alternative specification of model II tests for the robustness of empirical results while providing additional insights. Instead of the expected award, the expression substituted the natural log of trial length and the pre-trial jury demand as proxies for case complexity and potential damages. In this alternative regression, both trial length and settlement demands are highly significant and related positively to legal fees. The elasticity of defense fees with respect to settlement demands is virtually identical to the elasticity with respect to the expected award. The R² is quite high for a cross-section analysis, at .704. However, despite the differences, the positive effects of defense firm size and calendar time are retained.

Results from alternative specifications, not reported here, did not yield substantially different conclusions. For example, the predicted probability of plaintiff victory did not affect legal expenditures. The route to final post-trial disposition was not significantly correlated with legal costs. A combination of both models that included all three outcome measures—trial length, settlement demand, and expected award—had no effect. Finally, efforts to allow for more extreme non-linear relationships between fees and expected awards were only marginally successful. Allowing the coefficients to change over arbitrarily determined higher ranges suggested that fees increase at a slower pace as award expectations rise. However, these differences were minor and provided results that were invariably similar to simpler specifications.

REGRESSION ANALYSIS OF SETTLEMENT OFFERS AND DEMANDS

In Table A.7, we present estimates from regressing the natural log of reported settlement offers and demands on a variety of case characteristics. Settlement demands systematically rise with expected awards though not to the same degree. Demands have been rising at the rate of 12 percent annually, holding other factors constant. In addition,

4 An alternative treatment of these variables as endogenous case outcomes did not change the results qualitatively. A standard test for endogeneity (see Hausman, 1978) supported the assumption that these variables can be viewed as predetermined.
demands appear to be higher when there is a large defense firm involved or when plaintiffs are older. In contrast, there is almost no predictability in the pattern of offers.

Table A.7

REGRESSION ANALYSIS OF SETTLEMENT DEMANDS AND OFFERS

<table>
<thead>
<tr>
<th>Variable</th>
<th>Log (Demand)</th>
<th>Log (Offer)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Estimate</td>
<td>Standard Error</td>
</tr>
<tr>
<td>Intercept</td>
<td>1.477</td>
<td>1.674</td>
</tr>
<tr>
<td>log (predicted award)</td>
<td>0.443</td>
<td>0.115*</td>
</tr>
<tr>
<td>Time</td>
<td>0.122</td>
<td>0.055*</td>
</tr>
<tr>
<td>Large defense firm</td>
<td>0.592</td>
<td>0.259*</td>
</tr>
<tr>
<td>Large plaintiff firm</td>
<td>-0.206</td>
<td>0.266</td>
</tr>
<tr>
<td>Large employer</td>
<td>-0.067</td>
<td>0.188</td>
</tr>
<tr>
<td>log (age)</td>
<td>1.086</td>
<td>0.382*</td>
</tr>
<tr>
<td>R²</td>
<td>.326</td>
<td>.999</td>
</tr>
</tbody>
</table>

*Significant at 5%.
Appendix B

DATA COLLECTION METHODS

We conducted two surveys, described below, in the course of this study. A survey of cases filed in the Los Angeles Superior Court determined the pattern of changes in filing wrongful termination lawsuits. The results of this survey are described in Sec. II. Results of a separate survey of wrongful termination jury verdicts are presented in Secs. III and IV. In this appendix we describe the data collection methods used in each survey.

SURVEY OF CASES FILED IN THE LOS ANGELES SUPERIOR COURT

Identifying wrongful termination cases from among all civil filings in Los Angeles is an especially difficult “needle in a haystack” type of problem. At their highest rate of filing in 1986 we found that they represent only 1 percent of all civil filings, and there is no convenient system for identifying this type of case in Los Angeles. Wrongful termination cases can be identified only by examining the complaint filed by the plaintiff. Our search for wrongful termination case filings involved a two-stage process. First, cases that potentially involved wrongful termination were identified from a listing of all civil case filings. Data coders then pulled the court case file for each candidate case and reviewed the complaint to determine whether wrongful termination was involved. In this section we describe the process we used in more detail.

The Register of Actions, maintained by the Clerk of the Los Angeles Superior Court (LASC), provides the only listing of all cases filed in this court. There are separate registers for criminal, family, probate, and civil cases. The civil register includes personal injury, property damage, wrongful death, civil petitions, and other civil complaints. While each of the 11 branches of the LASC has its own set of registers, only the register at the downtown Los Angeles central branch was used for this survey. That branch accounts for about 60 percent of all general civil complaints filed in the Los Angeles Superior Court.

Each civil case filed is entered in the civil case register at the time the complaint is filed. The register is organized by date and includes
hundreds of volumes of approximately 200 cases each. Cases are entered in order of date filed and are numbered sequentially. Minimal information, including the names of the parties and the attorneys, is entered on the register at the time of filing. In addition, clerks assign a case type classification, based on a quick review of the complaint. Throughout the life of a case the clerks enter in the register a record of all events scheduled, proceedings, and documents filed in the case.

During the 14 month period we reviewed, 54,344 civil cases and petitions were entered in the Register of Actions. There are only a handful of classifications employed by the Clerk's Office for describing the civil caseload, most of which are quite broad. Wrongful termination cases have no classification of their own and fall under the category, "Miscellaneous Civil Complaint—Money Involved." This classification includes all contract, debt, business tort, and other miscellaneous civil cases where money damages are claimed. From 1980 through 1986 this category, on average, represented 13 percent of all civil filings included in the civil Register of Actions.

Data coders looked up all cases in the civil register for the two month period of March and April in each year from 1980–1986. To involve wrongful termination the plaintiff must be an individual whose employment was terminated. If the plaintiff named on the register was a business or agency, we assumed that wrongful termination was not involved in the case and did not list it for further checking. Any case initially filed in the central branch but subsequently transferred to a different court would have no file at central. Transferred cases could be identified from the register and also were not listed.

Altogether, more than 9000 cases were listed for further checking on the nature of the case. Table B.1 shows the breakdown of total cases entered in the register and the number of candidate cases we identified by year.

Some case files could not be found. Some were probably misfiled, and others were in use somewhere in the courthouse. Coders checked on different occasions to find returned files, and court personnel assisted with our search for missing cases, but 2 percent of the case files could not be located for review. Table B.2 shows, for each year, how many candidate cases were not checked because files were unavailable.

Altogether coders reviewed the complaint in the files of 9383 cases. The coders were instructed to look for the terms "wrongful discharge," "wrongful termination," or other indication of unlawful firing or discrimination in firing in the wording of the complaint.

For each wrongful termination case identified, the coders recorded the grounds for the suit, the date filed, and a crude designation of the
Table B.1
CASES REVIEWED AND CANDIDATE
CASES IDENTIFIED

<table>
<thead>
<tr>
<th>Time Period (March/April)</th>
<th>All Civil Cases Filed</th>
<th>Candidates for Further Checking</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>6,426</td>
<td>762</td>
</tr>
<tr>
<td>1981</td>
<td>7,890</td>
<td>947</td>
</tr>
<tr>
<td>1982</td>
<td>7,458</td>
<td>1,449</td>
</tr>
<tr>
<td>1983</td>
<td>7,415</td>
<td>1,474</td>
</tr>
<tr>
<td>1984</td>
<td>7,959</td>
<td>1,555</td>
</tr>
<tr>
<td>1985</td>
<td>8,715</td>
<td>1,769</td>
</tr>
<tr>
<td>1986</td>
<td>8,481</td>
<td>1,618</td>
</tr>
<tr>
<td>Total</td>
<td>54,344</td>
<td>9,574</td>
</tr>
</tbody>
</table>

Table B.2
UNLOCATED CASES

<table>
<thead>
<tr>
<th>Time Period (March/April)</th>
<th>Candidate Cases Not Found</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>23</td>
</tr>
<tr>
<td>1981</td>
<td>12</td>
</tr>
<tr>
<td>1982</td>
<td>25</td>
</tr>
<tr>
<td>1983</td>
<td>35</td>
</tr>
<tr>
<td>1984</td>
<td>16</td>
</tr>
<tr>
<td>1985</td>
<td>42</td>
</tr>
<tr>
<td>1986</td>
<td>38</td>
</tr>
</tbody>
</table>

employment position held by the plaintiff at the time of termination. The coding instrument used is shown in App. C. Table B.3 shows the number of wrongful termination cases identified.

JURY VERDICT DATA COLLECTION

Data for the analysis of jury verdicts were derived from two sources: *Jury Verdicts Weekly* and a mail survey. The California jury verdict reporter, *Jury Verdicts Weekly*, provides summary information about the parties, claimed reason for employment termination, settlement demands and offers, and verdict amount in each case. These data were
coded for each of the 120 wrongful termination cases published in the reporter from 1980 through the first quarter of 1986. To obtain information often missing from the reporter and additional information about insurance coverage, legal fees, and the final outcomes in these cases, we also conducted a mail survey with the attorneys of record for the plaintiff and defendant who were listed in the jury verdict reporter. This section describes the sample preparation, survey procedures, and response rate for this survey.

Sample Preparation

The jury verdict reporter named 277 attorneys on the 120 jury verdicts—132 plaintiff attorneys for an average of 1.2 plaintiff attorneys per case, and 145 defense attorneys, 1.2 defense attorneys per case. Because they were counsel for unions or for disability insurance companies, not involved in the wrongful termination aspect of the case, 13 attorneys were eliminated. Although some cases had more than one plaintiff or defense attorney involved, some attorneys had more than one case in the sample. After identifying individual attorneys named on more than one case, we found a total of 238 individuals involved as counsel in the 120 cases—114 plaintiff attorneys, 121 defense attorneys, and three attorneys who represented both plaintiffs and defendants.

Usually the jury verdict reporter provides the plaintiff and defense attorneys’ names and law firms, but not addresses. Even though lawyers would typically be listed in phone books and directories, obtaining addresses was difficult because, other than the names, we

<table>
<thead>
<tr>
<th>Year (March/April Filings)</th>
<th>Wrongful Termination Cases</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>15</td>
</tr>
<tr>
<td>1981</td>
<td>20</td>
</tr>
<tr>
<td>1982</td>
<td>39</td>
</tr>
<tr>
<td>1983</td>
<td>83</td>
</tr>
<tr>
<td>1984</td>
<td>78</td>
</tr>
<tr>
<td>1985</td>
<td>100</td>
</tr>
<tr>
<td>1986</td>
<td>102</td>
</tr>
</tbody>
</table>
had only the county where the case was tried as a starting point. Attorneys' offices are not necessarily located in the county where they tried a particular case, and, because the time of trial in many cases was several years ago, some might have moved in the interim. We could find no directory of California attorneys organized by attorney name. Instead we used as our main source the Parker Directory, a listing of California attorneys organized by county and major urban areas. We attempted to find addresses for all 238 attorneys but were unable to locate 10—five plaintiff and five defense. The unlocated attorneys were dropped from the survey sample, but because we were able to find an address for at least one attorney in all 120 jury verdicts, we did not have to drop any cases.

We mailed 254 questionnaires to 228 attorneys involved in the 120 selected cases tried to jury verdict. Most of the 120 cases had two attorneys involved—one plaintiff and one defense. A few had only one because of difficulty in finding addresses for both, and a few had additional attorneys on the case. Table B.4 shows the number of attorneys per case.

The 228 attorneys surveyed were divided into 109 plaintiff and 116 defense attorneys and three attorneys who represented plaintiff and defense in different cases. Most of the attorneys were involved in only one case and received only one questionnaire. However, 18 attorneys were involved in more than one of the jury verdicts and received one questionnaire for each of their cases. No attorney received more than four questionnaires. Seven of the 18 attorneys with more than one case were defense attorneys, eight were plaintiff attorneys, and three represented the plaintiff in one case and the defendant in another. Table B.5 shows how many questionnaires attorneys received.

Table B.4
ATTORNEYS SURVEYED
PER JURY VERDICT

<table>
<thead>
<tr>
<th>Attorneys Surveyed in Case</th>
<th>Questionnaires Mailed</th>
<th>Cases</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>8</td>
<td>8</td>
</tr>
<tr>
<td>2</td>
<td>91</td>
<td>182</td>
</tr>
<tr>
<td>3</td>
<td>20</td>
<td>60</td>
</tr>
<tr>
<td>4</td>
<td>1</td>
<td>4</td>
</tr>
<tr>
<td>Total</td>
<td>120</td>
<td>254</td>
</tr>
</tbody>
</table>
Questionnaire

We prepared two versions of the questionnaire. Plaintiff attorneys with more than one client in a case received a version of the questionnaire designed to capture information on multiple plaintiffs. Attorneys received the multiple plaintiff version of the questionnaire in nine cases.

The final questionnaire contained 21 questions about the parties in the case and the outcome. It asked for the plaintiff's age, sex, race, type of occupation, salary, length of employment, year of termination, type of employer, and claimed reason for termination. The questionnaire included questions on pre-trial and post-trial settlement demands and offers, as well as the actual verdict and final disposition of the case. Finally, we attempted to determine whether there was insurance coverage in the case for liability or defense and the total legal fees and costs billed to the client in the case.

No identifying information about the case, the parties, or the attorneys was requested. In the cover letter attorneys were assured that the information they provided about the case would be kept strictly confidential and would not be identified with specific cases.

Survey Procedures

A copy of the description of the case as it appeared in the jury verdict reporter was attached to each questionnaire. It was hoped that with this information attorneys would be able to easily recall the case we were interested in. Questionnaires were sent to attorneys with a personalized letter from the project director and a pre-addressed postage-paid envelope in which to return the completed questionnaire. An identification label was attached to the questionnaire to link the returned form to the sample list. No monetary incentive was offered

<table>
<thead>
<tr>
<th>Questionnaires</th>
<th>Attorneys</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>210</td>
</tr>
<tr>
<td>2</td>
<td>12</td>
</tr>
<tr>
<td>3</td>
<td>5</td>
</tr>
<tr>
<td>4</td>
<td>1</td>
</tr>
</tbody>
</table>
the attorneys, but they were offered a copy of the report on the survey's results.

Questionnaires were mailed in late February 1987. One week later a letter was sent to all attorneys in the sample as a thank-you and a reminder to those who had not yet responded. Four weeks after the initial mailing a second questionnaire was sent to those who had not yet responded. This mailing was followed several days later with a telephone follow-up call. The purpose of the call was find out if the attorney had received the questionnaire, urge him or her to return it, or obtain the requested information over the telephone if that proved more convenient for the attorney. Often attorneys' secretaries took our call. When the attorney was unavailable we asked the secretary to find out if the questionnaire had been received and to ask the attorney to complete and return it. We arranged a call back to the secretary to find out about the status of the questionnaire. When we were able to reach the attorney, we asked if he or she could provide the requested information at that time over the phone, rather than by mail. In many cases, this approach was agreeable to the attorney.

Telephone follow-up calls to attorneys began five weeks after the initial mailing of the questionnaires. About 40 percent of the sample, 101 questionnaires, were still outstanding when calling began.

Response to Survey

In this section we report on response to the survey for three dimensions of the sample. First, we report on the number of jury verdicts for which we obtained survey data. We then report on the response rate among the 228 attorneys surveyed, and finally we indicate the number of questionnaires returned among the 254 mailed.

Case Completion. We obtained survey data on 91 percent of the 120 jury verdicts sampled. At least one attorney returned a completed questionnaire or provided the data over the phone in 109 cases. The number of questionnaires returned per jury verdict is shown in Table B.6.

Half of the cases for which we did not obtain survey data were cases where we had identified only one attorney or found that the address we had was incorrect. The other half were cases where the attorney failed to return the form and could not be reached by phone during the survey period.

For 58 percent of the jury verdicts we obtained responses from more than one attorney. Because of reporting errors, the responses to identical questions occasionally differed between lawyers. In these cases, we simply took averages. Since regressions based on the plaintiff, defense,
and combined sample of respondents were invariably similar, this approach seems acceptable.

**Attorney Response.** Of the 228 attorneys surveyed 75 percent provided information about one or more cases. Altogether, we obtained completed questionnaires from 172 of the 228 attorneys to whom we mailed. Most completed the questionnaire(s) by mail, but 29 preferred to answer by phone. Plaintiff and defense attorneys cooperated at about the same rate, with 76 percent of the defense attorneys responding and 74 percent of the plaintiff attorneys.

Attorneys with multiple cases were slightly more likely to respond than attorneys with only one case. We received questionnaires from 14 of the 18 attorneys who had more than one case. Attorneys with multiple cases are likely to be specialists in this area of law. Perhaps they were particularly interested in the research results and therefore willing to accept the additional inconvenience of responding on more than one case.

Of the 228 attorneys, 44 had been surveyed in previous ICJ studies of jury verdicts. Their rate of response in this survey was almost exactly the same as it had been in the past, and the same as the rate for attorneys who had not been previously contacted. Some who had not previously responded did so in this study, and some who had returned completed questionnaires in a previous study failed to do so this time.

We failed to reach 15 attorneys whose questionnaires were returned to us as undeliverable, eight defense attorneys and seven plaintiff attorneys. If we subtract these 15 from the 228 initially mailed, our response rate increases to 80 percent. Other nonrespondents included attorneys who refused and those who failed to send back the questionnaire(s) even after our telephone follow-up call.

**Questionnaires Returned.** From the mail survey we received 144 completed questionnaires before telephone calling began. From the
telephone follow-up calls we were able to complete 33 questionnaires with the attorney on the phone. We also received 11 questionnaires in the mail after the telephone calling began. The total number of completed questionnaires was 188, 74 percent of the total.

At the time of the telephone follow-up, 101 questionnaires were still outstanding. One-third of these cases were completed by telephone. Another 11 percent were received by mail after the telephone reminder. In total, 17 percent of the survey sample was completed as a result of the telephone follow-up.

Response Bias

To test for possible response biases, we ran a series of logistic regressions for the combined, defense, and plaintiff attorney sample. The dependent variable was given a value of 1 for a completed response. The probability of a response was related to the time period of the trial as well as trial outcome. Other factors, including law firm, plaintiff, and defendant characteristics, were initially analyzed but were found to be statistically unrelated to the completion rate. Table B.7 presents these results.

Table B.7
LOGISTIC ANALYSIS OF CASE AND ATTORNEY COMPLETION RATES

<table>
<thead>
<tr>
<th>Variable</th>
<th>Case</th>
<th>Defense</th>
<th>Plaintiff</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>0.858</td>
<td>0.172</td>
<td>-1.897a</td>
</tr>
<tr>
<td></td>
<td>(0.608)</td>
<td>(0.476)</td>
<td>(0.569)</td>
</tr>
<tr>
<td>Trial date 1982–85</td>
<td>0.569</td>
<td>0.768</td>
<td>0.933</td>
</tr>
<tr>
<td></td>
<td>(0.684)</td>
<td>(0.478)</td>
<td>(0.533)</td>
</tr>
<tr>
<td>Trial date 1985–86</td>
<td>0.870</td>
<td>0.441</td>
<td>0.566</td>
</tr>
<tr>
<td></td>
<td>(0.781)</td>
<td>(0.482)</td>
<td>(0.526)</td>
</tr>
<tr>
<td>Million dollar award</td>
<td>-0.354</td>
<td>-0.457</td>
<td>0.111</td>
</tr>
<tr>
<td></td>
<td>(0.839)</td>
<td>(0.740)</td>
<td>(0.904)</td>
</tr>
<tr>
<td>$250,000 award</td>
<td>1.542</td>
<td>-0.785</td>
<td>2.133a</td>
</tr>
<tr>
<td></td>
<td>(1.123)</td>
<td>(0.597)</td>
<td>(0.662)</td>
</tr>
<tr>
<td>Small award</td>
<td>1.478a</td>
<td>-0.343</td>
<td>1.864a</td>
</tr>
<tr>
<td></td>
<td>(0.730)</td>
<td>(0.449)</td>
<td>(0.500)</td>
</tr>
</tbody>
</table>

aSignificant at 5%.
In general, no important biases seem to emerge. On a case level, however, trials resulting in small awards appear more likely to be reported than either defense victories or million dollar cases, primarily because of plaintiff attorney response rates. This tendency is mitigated in part by the fact that defense lawyers are somewhat less likely to provide information on cases they lose. These differences, however, are small and not significantly different from zero.

The results also suggest that responses were more likely for trials that took place more recently, although the differences were not significantly different from zero. The case response rate, for example, was about 18 percent higher for trials occurring after 1982.

Although attorneys recall recent cases more easily, those cases are more likely to still be open, making the information more sensitive. Table B.8 provides a regression of case status on trial date and award outcome. Recent trials were much more likely to have still been pending at the time of the survey. Although the cases resulting in the largest awards remain open the longest, the difference is not significant.

### Table B.8

**PROBABILITY OF CASES BEING OPEN: LOGISTIC ANALYSIS**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Standard Error</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-3.661</td>
<td>1.155&lt;sup&gt;a&lt;/sup&gt;</td>
</tr>
<tr>
<td>Trial date 1982-85</td>
<td>1.749</td>
<td>1.116</td>
</tr>
<tr>
<td>Trial date 1985-86</td>
<td>2.472</td>
<td>1.023&lt;sup&gt;a&lt;/sup&gt;</td>
</tr>
<tr>
<td>Plaintiff verdict</td>
<td>0.388</td>
<td>0.668</td>
</tr>
<tr>
<td>Million dollar award</td>
<td>0.973</td>
<td>1.017</td>
</tr>
<tr>
<td>$250,000 award</td>
<td>-0.061</td>
<td>0.764</td>
</tr>
</tbody>
</table>

<sup>a</sup>Significant at 5%.

**Dependent Variable:**
- Case Still Pending = 1
- Case Closed = 0
Appendix C

SURVEY OF WRONGFUL DISCHARGE LITIGATION QUESTIONNAIRE

SURVEY OF WRONGFUL DISCHARGE LITIGATION

INSTRUCTIONS - PLEASE READ FIRST

These questions apply to the award and payments made in the case described in the attached report from Jury Verdicts Weekly. Please take a few minutes to look up this information in your files and record the answers on this form.

To answer these questions, please place an X in the box next to the response that you choose or fill in your response on the line provided. You should answer all questions, unless an answer you select is followed by an instruction to skip to a specific question.

If you have any questions, please call Pat Ebenor or Nora Fitzgerald at 213-393-0411.

Thank you for your cooperation.

First, please verify the information contained in the attached report.

1. What was the total amount awarded by the jury to all plaintiffs in the wrongful termination action in this trial?
   - Compensatory damages: $ ____________
   - Punitive damages: $ ____________

2. Plaintiff's age at time of employment termination: _________

3. Plaintiff's sex:
   - [ ] Male
   - [ ] Female

4. Plaintiff's race:
   - [ ] Black
   - [ ] White
   - [ ] Other
   - [ ] Don't know

5. Year of employment termination: 19 ______

CARD 20 9-10/

11-18/

19-26/

27-28/

29/

30/

31-32/

69
6. Salary at time of employment termination: $ ________________
   Salary period: □ 1 Per hour
                 □ 2 Per day
                 □ 3 Per week
                 □ 4 Every two weeks
                 □ 5 Per year

7. Approximate length of employment at time of termination:
   □ 1 Less than 1 year
   □ 2 One to five years
   □ 3 Six to ten years
   □ 4 Eleven to fifteen years
   □ 5 Over fifteen years

8. Type of occupation at time of termination:
   □ 1 Executive
   □ 2 Middle management or supervisor
   □ 3 All other

9. Defendant's claimed reason for termination:
   □ 1 Poor job performance or misconduct
   □ 2 Economic/business considerations
   □ 3 Other, please specify ________________

10. Plaintiff's lowest pretrial settlement demand:
    $ ________________
    □ 0 No demand

11. Defendant's highest pretrial settlement offer:
    $ ________________
    □ 0 No offer

CARD 01
The following questions pertain to activity in this case since the trial described in the attached report.

12. What was the plaintiff's lowest post-trial settlement demand?
   $ ____________________________ 11-18/
   □ No demand 19/

13. What was the defendant's highest post-trial settlement offer?
   $ ____________________________ 20-27/
   □ No offer 28/

14. Has this case reached a final disposition?
   □ No, still pending (appeal, settlement negotiation, court decision). ----> Skip to Q. 17, page 4 29/
   □ Yes, settled after trial. 30/
   □ Yes, disposed of on appeal, new trial or other post-trial court order. 31/
   □ Yes, disposed of on original jury verdict. ----> Skip to Q. 16 32/
   □ Other, please specify ____________________________ 33/

15. What was the final judgment or post-trial settlement amount?
   $ ____________________________ 34-38/

16. Has the settlement or final judgment been paid?
   □ Yes, full payment made. ---> Final payment date / 39/
       Month Year 40-43/
   □ No payment due, defense judgment _______________________ ---> Disposition date / 44-47/
       Month Year 48-51/
   □ No, partial payment made. ---> Latest payment date / 49-51/
       Month Year 52-56/
   □ No, payment pending.

Continue to page 4 ------------------

17. Was there insurance coverage for legal fees in this suit?
   - Yes
   - No
   - Don't know

18. Was there insurance coverage for liability in this suit?
   - Yes
   - No (skip to Q. 20)
   - Don't know (skip to Q. 20)

19. What was the limit of the liability coverage?
    $ ____________________________

20. Was insurance coverage contested in this suit?
    - Yes
    - No
    - Don't know

21. What would you estimate are the total legal fees and costs for which you billed your client in this case?
    $ ____________________________
    or contingency fee rate: _____%
REFERENCES


ICJ Publications

Process: Courts


Priest, G. L., Regulating the Content and Volume of Litigation: An Economic Analysis, R-3084-ICJ, 1983.


Process: Lawyers and Litigants


**Process: Juries**


**Process: Alternative Dispute Resolution**


**Costs**


**Alternative Compensation Systems**


**Toxic Substances**


**Trends in Outcomes**


**Understanding Outcomes**


Danzon, P. M., New Evidence on the Frequency and Severity of Medical Malpractice Claims, R-3410-ICJ, 1986.

———, The Frequency and Severity of Medical Malpractice Claims, R-2870-ICJ/HCFA, 1982.


**Interaction Between the Civil Justice System and the Economy**


**Legislative Testimony**

Danzon, P. M., *The Effects of Tort Reforms on the Frequency and Severity of Medical Malpractice Claims: A Summary of Research Results*, P-7211-ICJ, 1986. (Testimony before the Committee on the Judiciary, U.S. Senate.)


———, *Summary of Research Results on the Tort Liability System*, P-7210-ICJ, 1986. (Testimony before the Committee on Commerce, Science, and Transportation, U.S. Senate.)

———, *Trends in California Tort Liability Litigation*, P-7287-ICJ, 1987. (Testimony before the Select Committee on Insurance, California State Assembly.)

Kakalik, J. S., and N. M. Pace, *Costs and Compensation Paid in Tort Litigation*, P-7243-ICJ, 1986. (Testimony before the Subcommittee on Trade, Productivity, and Economic Growth, Joint Economic Committee of the Congress.)

**Syntheses and Policy Implications**


———, *What We Know and Don’t Know About Court-Administered Arbitration*, N-2444-ICJ, 1986.


A subject bibliography (SB 1064) provides a list of other RAND publications in the civil justice area. To request the bibliography or to obtain more information about The Institute for Civil Justice, please write the Institute at this address: The Institute for Civil Justice, The RAND Corporation, 1700 Main Street, P.O. Box 2138, Santa Monica, California 90406-2138, (213) 393-0411.