

LEGAL INSURANCE, LITIGANT DECISIONS, AND THE RISING CASELOADS OF COURTS: A WEST GERMAN STUDY

ERHARD BLANKENBURG*

German prepaid legal insurance is growing both in terms of number of households insured and in terms of extending coverage to new legal areas. Fears for a litigation explosion, however, can be shown to be unfounded—just as are hopes that legal insurance would remove social inequalities of access to law. The use of legal insurance turns out to be much more limited than could have been expected. Major effects on financing lawsuits occurred only in defense against traffic fines and regulating traffic accidents. Litigation behavior as measured by indicators of litigiousness (such as risking a lawsuit with poor chance for success, resisting settlement, filing an appeal) does not seem to be affected by removing cost considerations. It appears that social costs determine inclination to litigate to a greater degree than do financial costs.

I. INTRODUCTION

The idea of an insurance plan covering lawyer fees and court costs seems like a prime example of a “moral hazard”¹: insurance should protect against risks which are beyond control, but it should not induce the risks which it covers. Prepaid legal insurance might be expected to induce the risks. Since the cost of lawyers and court fees may deter litigation and encourage avoidance of legal conflict, eliminating cost risks through insurance may lead insurees to risk lawsuits and to use lawyers’ services beyond reasonable chances for success. That, at least, is the argument of many judges in Germany who claim that rising caseloads are caused by the increased use of legal insurance.² It is also the assumption of legal-economic

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¹ Cf. the discussion of “risk” principles of insurance in Layard and Walters (1978).

² Survey evidence; cf. Blankenburg and Fielder (1981: 33-38).

theories which conclude that some cost deterrence is necessary to prevent too much litigation. Proponents of these theories propose to limit by legal regulation the activity of legal insurance companies.³ The same assumption is made by liberal reformers who look to solve inequality of access to law by introducing legal insurance for everybody.⁴

Thinking in economic terms, however, raises a paradox: why, if legal insurance induces more legal risk taking, would any insurance company offer such policies? Would they not invite especially poor clients; and as a consequence would not premiums go up, eventually to such a degree that policies would become unattractive for individuals with average legal risks? The financial success of legal insurance companies in Germany during the last 30 years is a cause for skepticism about the assumption that legal behavior is primarily dependent upon considerations of costs.

Similarly, we may find some hopes of liberal reforms unfounded. If it is not financial costs, but rather other factors which form the main barriers to obtaining legal services, then introducing universal legal insurance might create just another illusion of equality. Even worse, as any general insurance works as a device for redistribution from those who do not claim its services to those who do, it might have the effect of subsidizing legal services for a few clever users with the contributions of legally inexperienced non-users.

Before assessing these conjectures about legal insurance, we have to know more about how it actually works. West Germany forms a good testing ground, since about 40 percent of all households have insurance policies which cover some legal expenses. How these policies work must be seen against the backdrop of the German legal system, especially its regulation of lawyer and court fees. Some of these regulations caution us as to the limits of transferability of legal insurance schemes to other legal systems, but generalizations in the framework of litigation theory should be possible.

³ Cf. Adams (1981) for a remarkable example of how misleading logically elegant models of legal economics can be, if built on erroneous behavioral assumptions.

⁴ Kininger (1978) recommends general legal insurance without any hesitation. For a sophisticated feasibility analysis, see Stolz (1968). He discusses the different issues at stake which might make legal insurance more or less socially desirable. His negative evaluation is based, in part, on arguments which would not apply to German civil procedure because of its control of lawyers' fees.

We can formulate two hypotheses about the relationship between prepaid legal services and the inclination to invoke the courts:

- The *inducement thesis* predicts that people who have legal insurance will litigate more often *because* the cost factor is reduced.
- The *recruitment thesis* would predict, conversely, that people who litigate more often will *therefore* be more likely to buy legal insurance.

Of course, both hypotheses could be right and mutually reinforce the correlation of litigiousness with legal insurance. We shall try to test them separately as much as possible by developing our argument in separate steps.

The first step provides some evidence for the recruitment thesis by comparing the social characteristics of those who hold legal insurance in West Germany and the general population. These characteristics, together with data from legal insurance companies, provide the necessary background information on who uses legal insurance and the reasons for its use. Second, we analyze a representative sample of insurance claims files to see what kinds of services lawyers render when consulted by insured clients. It will show that, in spite of prepaid insurance, neither lawyers nor clients always go to court; indeed, they are still likely to seek solutions which avoid courts. Furthermore, we can obtain an informed estimate of how many parties involved in all court cases are covered by legal insurance. Interpreted within the framework of mobilization of law theories, these rates show the limited circumstances under which the inducement thesis is at all plausible. They also suggest those fields of law where we can rule out any relationship of legal insurance to rising court caseloads. Third, a stronger test of the inducement hypothesis is obtained by comparing insurance claims to all court cases. We examine three aspects of relative litigiousness: (1) whether those whose costs are covered by insurance take higher risks of losing a law suit; (2) whether they are less inclined to accept a settlement and more likely to seek a judgment; and (3) whether they appeal judgments more often. Our hypotheses predict that legal insurance holders will be more litigious because they do not incur any risk of costs. We find that none of these expectations holds true.

The article concludes by discussing the consequences of our results for theories of litigation and for legal policy. As each stage of our argument is based on different sets of data, we shall indicate the methods used in data gathering in the footnotes. For more detailed documentation, our German

publication (Blankenburg and Fielder, 1981) should be consulted.

II. DEVELOPMENT OF LEGAL INSURANCE IN THE FEDERAL REPUBLIC OF GERMANY

Until the early 1950's the large insurance companies in Germany did not cover the risk of legal costs (presumably because they saw the dangers of the inducement thesis). But outsiders to the business tried it anyway, and when legal insurance turned out to be profitable the more established, large insurance companies followed suit.

The first major attempt to insure legal costs was undertaken by two small, specialized insurance companies in the 1920's. They grew considerably with the wave of mass motorization in the 1950's. At first their coverage was limited to traditional risks such as liability claims following automobile accidents. Here the insurance coverage was in accord with the principle of the risk being largely beyond control of the insured. Even if automobile accidents are not wholly independent of driving behavior, one can assume that nobody causes accidents voluntarily. Covering legal expenses connected with accidents seemed a reasonable and logical step from accident liability coverage itself. Gradually the scope of coverage was expanded to include defense against criminal prosecutions after accidents, use of lawyers to protest traffic fines, and civil matters connected with buying and operating an automobile. Later, other civil matters were included. Offering legal advice for rental problems and protection in labor conflicts proved to be good sales arguments. Thus, while the early concept of legal insurance resembled that of accident insurance, it increasingly moved into areas where the effect on inducing use of legal services was less predictable. Legal insurance companies had no systematic knowledge about litigiousness. However, they discovered from experience that private individuals in Germany avoid lawyers and litigation, even if they are free of any risks of costs.

Services of Legal Insurance Companies and the Regulation of Lawyer Fees

The strict regulation of lawyers' fees in and out of court in Germany made the provision of legal insurance much simpler than it would be in the United States with its negotiable fees. If lawyers' fees were not set by law, insurance companies would have to do it (as medical insurance companies

ultimately did in the United States). In Germany, court fees as well as attorneys' fees on both sides are tied to the monetary value of the claim (Gilles, 1977). Contingent fees are banned as unethical. In civil courts the principle of "loser pays all" (including the opposing party's lawyer fees) prevails. An insurance company thus has to pay only to the degree that its client loses the case (for details see Pfennigstorf, 1977). The insurance agents should not offer legal counsel or interfere in any way with their clients' choice of a lawyer; it is an "open panel" program in theory. In practice, however, agents recommend lawyers when asked, and they provide information on whether a legal claim seems worth pursuing. But they hardly ever refuse to cover a claim on the grounds that it seems "without reasonable chance of success," despite the fact that they are entitled to do so under the contractual terms of the insurance. Leading insurance executives explained this policy in interviews as a desire to avoid damage to the service image of the companies. Conflicts over refusals are so exceptional that the restrictive clauses in the insurance contracts proved to be practically irrelevant.

Who Are the Holders of Legal Insurance?

Statistics from insurance companies and survey data show that a steadily increasing proportion of the population is covered by legal insurance. Surveys in 1979 reported that 40 percent of all households in the Federal Republic of Germany are insured against legal risks. Sixteen percent were insured only against automobile-related risks, and 24 percent had policies encompassing general services. From a survey of West Berlin households in 1979, we correlated insurance holding with experiences of legal problems and other indicators of legal behavior. (In Berlin only 33 percent of all households had legal insurance: 22 percent had coverage for general legal services; 11 percent were insured only against automobile risks. The difference between Berlin and the rest of the Federal Republic stems from the low car ownership in a city which has no "hinterland" from which to commute.) These findings are presented in Tables 1 and 2.

As we can see from Table 2, insurance holders consult a lawyer more often, whether this is asked in general terms or in the context of reporting about some legal problem which they experienced within the last five years. They have also invoked the courts more often. (Additionally, they have been to court

Table 1. Percent of Occupational Groups With Legal Insurance

	Federal Republic of Germany ^a	West Berlin ^b
Professional	61%	43%
Civil Service	61%	62%
Other White Collar Employees	44%	46%
Skilled Workers	49%	31%
Semi and Unskilled Workers	31%	36%
Pensioners	13%	13%
Average for All Groups	40%	33%

^a Source: Representative survey of all households by Infas; Unpublished reports, Bad Godesberg (1979).

^b Source: Own Survey, Berlin, 1979; random sample of all households except foreign workers.

more often as a witness, and they have been sued by others more often.) While going to lawyers more often, the insured also consult public legal aid offices (which are found only in Berlin in this form and are offered free of charge by the city

Table 2. Legal Contacts of Insurance Holders Versus Others (In West Berlin)^a

	Insurance Holders (N=274)	Others (N=561)	Significance Level of Difference ^b
All respondents:			
Ever been to a lawyer?	54%	36%	.03
Invoked the courts themselves	22%	15%	.03
Been sued by others?	18%	13%	.10
Been before court as witness?	31%	20%	.10
Respondents with labor law problems:			
Seen a lawyer?	2%	1%	Not significant
Seen a trade union's legal aid?	7%	3%	.05
Respondents with consumer problems:			
Seen a lawyer?	10%	3%	.02
Been to public legal aid?	4%	2%	.06
Been to consumer board?	6%	5%	Not significant
Respondents with rental problems:			
Seen a lawyer?	9%	4%	.05
Been to a public office/legal aid?	9%	7%	.10
Been to renters' association?	8%	6%	Not significant

a) Source: Own survey West Berlin, 1979; random sample of all households, except foreign workers.

b) Chi² test with one degree of freedom.

and the bar for people with modest incomes) and legal advisers for consumer boards or renters associations (which give legal aid to members). Most revealing is that they go to trade union advisors for labor law problems twice as often as non-insurance holders.

These data offer some support for the recruitment thesis: legal insurance holders seem to be more active with respect to *all* legal activities. They are—as our data further show (Blankenburg and Fielder, 1981: 38-46)—more likely to be members of voluntary associations and of trade unions; they are better educated and better informed. They are “joiners,” and buying legal insurance is a reflection of their overall social activity.

Professional and Business Firms as Insurance Holders

While most insurance holders are private households, there are also policies for businesses and professionals. In our sample of insurance claims we found employers in labor cases, as plaintiffs in debt collection cases, and as landlords taking legal action against their tenants. As a rule, these policy holders are small firms or private individuals. Large firms customarily employ in-house counsel, and medium-size firms usually maintain ties to a law firm. If business firms or professionals use legal insurance, the insurance companies assess premiums according to their greater risks. Financing by insurance makes sense only if legal problems occur irregularly and if such firms are interested in keeping their costs at a steady and predictable level. As we report below, all indicators in our analysis of insurance claims show professionals and business firms to be more litigious than households with legal insurance. Consequently, they appear more in claims files than would be expected from the number of policies they hold.

When Is Legal Insurance Used?

About one-third of all private households buying legal insurance are covered for automobile-related legal risks only. Two-thirds have general coverage, which includes lawyers' services and court fees for automobile-related conflicts, labor law, and all other civil matters. The major exclusions are family law (divorce) and legal conflicts related to building a house, since both of these may be foreseeable and therefore lead to a recruitment of bad risks. Administrative law cases are also excluded, because insurance companies fear that risks may be unpredictably high. Criminal action is covered as long

as it is "by neglect" (for example, causing bodily injury in a traffic accident). This clause sounds like a distinction made in the penal code to determine the severity of a criminal offense. The explicit inclusion of drunk driving in the legal calamities covered by insurance, however, makes clear that insurance companies in fact draw a line between "normal" deviance and "true criminality." Excluding the latter is a device not only to prevent recruitment of bad risks, but also to protect the precarious image of insurance not as "for criminal law defense," but as "against legal risks."

Table 3. Type of Claims for All Legal Insurance Companies in West Berlin, 1976

	Percent	Cumulative Percent
Traffic tickets (minor violations)	27.7	
Traffic fines (violations of penal law)	11.4	
Traffic Violations	39.1	39.1
Liability regulation of traffic accidents	24.4	
Other civil law matters relating to automobiles	6.1	
Automobile related matters altogether	30.5	69.6
Consumer cases and debt collection	8.0	
Labor law conflicts	7.6	
Rental conflicts	6.2	
Other civil law	4.9	
Penal law (except traffic)	1.4	
Other	2.4	
All non-automobile related	30.5	100.1

Source: Legal insurance files, West Berlin, 1976. In the claim files there is no separation between policies which cover only auto-related matters and general coverage policies. Subtotals do not add exactly to 100 due to rounding.

Looking at the claims covered by legal insurance in Table 3, non-traffic-related fields play only a minor role: 70 percent of all claims are related to driving and owning automobiles, 30 percent are distributed over all other legal matters (recall that roughly one-third of all policies cover only automobile-related matters, while two-thirds cover all legal matters). It is quite apparent that most claims in the files of legal insurance companies arise from some accidental risks; traffic accidents and even traffic fines may be considered as events which can be minimized but not avoided altogether by anyone who drives

a car. Minor traffic tickets (for speeding, running red lights, or even for parking violations) are often considered to be an unavoidable levy on users. Their effects are especially onerous if several convictions result in the loss of a drivers' license. On the other hand, appeals against traffic tickets (which invoke a lower court) have a high chance of success. Backlogs at the courts have led to the practice of dropping minor tickets as soon as a driver contests the violation. Here legal insurance has a considerable share in the rising caseloads: our statistics show that in Berlin about 50 percent of all appeals against traffic tickets have been covered by legal insurance. Contesting traffic tickets is summarily handled by the courts. If the state's evidence is in any way challenged, the case is usually dropped; if not, conviction follows without much judicial scrutiny.

Contest of traffic tickets, although a simple bureaucratic routine, has increased to a degree that troubles court managers.⁵ The rise of caseloads occurred at a time when legal insurance policy holding was increasing. Our survey data, however, show that about two-thirds of all car owners hold legal insurance policies (car ownership is the strongest predictor of whether a household buys legal insurance or not). If exposure to traffic fines were equally distributed, we would have to conclude that at least some of the insured do not bother to use a lawyer to file a protest (a mere letter is sufficient to contest a traffic ticket; nevertheless, lawyers are entitled to collect several hundred marks as a fee). Thus coverage by legal insurance does not necessarily induce the high caseloads for handling traffic tickets and fines. Instead of considering legal insurance as a *reason* for increased court caseloads, we might see the decision to buy legal insurance as a *response* to increased legal involvement by drivers; and we might view rising traffic court caseloads as an *effect* of an ever-increasing (technologically refined and bureaucratized) police control of the roads (including campaigns against parking violations). Other areas of law which experienced an alarming rise in court caseloads are conspicuously absent from the insurance claim files. Case overloads are most urgently felt in administrative and tax courts, but cases in these courts are excluded from insurance coverage.

Our data from insurance files permit us to calculate roughly the proportion of cases covered by insurance in the

⁵ Most prominently expressed by Pfeiffer (1980), the President of the highest German civil court (Bundesgerichtshof).

courts of West Berlin.⁶ We estimate that in 1979 legal insurance in West Berlin covered the cost for:

- about 52 percent of all those contesting traffic tickets, but only 13 percent of those defending against traffic fines in penal courts;
- about 45 percent of all plaintiffs in liability suits after traffic accidents;

but only for

- about six percent of all parties before the labor courts; and
- about three percent of all parties in other civil suits.

The low share of coverage by legal insurance before civil and labor courts leads us to conclude that legal insurance has developed mainly as a defense against the handling of accident claims by liability insurance companies and against an overregulative control of traffic by the police.

III. DOES LEGAL INSURANCE INCREASE THE LIKELIHOOD OF INVOKING COURTS?

Pre-Court Activities of Lawyers

If we consider traffic accidents and fines to be relatively unavoidable risks, legal insurance makes their cost predictable. The legal costs of traffic accidents and fines are similar to medical costs: everyone tries to avoid doctors—some people less, some more (for example, by smoking or not smoking)—but everyone wants to be free of cost considerations once they need medical help. Even though going to a lawyer or to court for a traffic ticket or after a traffic accident means, in a formal sense, that the insurance holder has invoked legal action, it is a response to a legal decision of another party (e.g. the police or an insurance company). Not mobilizing some legal defense would mean more than simply avoiding a conflict: “lumping it” means, here, paying for it.

Legal mobilization does not, however, always lead to court. Merely protesting a traffic fine may cause the fine to be waived, and in cases of accidents (as in other civil law conflicts), a single letter from a lawyer may be a sufficient threat to induce the other side to give in. We do not know how many of the noninsured clients of lawyers can be satisfied without invoking court procedures, but our data from insurance files show that, for the insured, this is frequently the case (See Table 4).

⁶ Random sampling of all legal insurance claims files in West Berlin in 1976 allowed us to extrapolate their caseload and compare them to the number of cases in West Berlin court statistics. For the sources, which are partly unpublished data, see Blankenburg and Fielder (1981: 69-74, 87-91, 96).

Table 4. Types of Lawyer Services to Insured Clients

	Traffic Fines	Traffic Accidents (Civil Law)	Other Civil Law Cases
Consultation Only	1%	3%	16%
Pre-Court Activity Only	43%	77%	46%
Invoked Court Procedure	56%	20%	38%
	100%	100%	100%
(N)	(537)	(517)	(627)

Source: Legal Insurance Files, West Berlin, 1976.

It is quite significant that the minor cases—like traffic fines—go to court more often than do major ones. The procedure is merely a routine which happens to be done by a court, but it does generate lawyers' fees. In most other cases, clients in our insurance file sample prefer pre-court solutions or only seek advice, while avoiding litigation. Considering the interest of lawyers in higher fees we would expect them, without reluctance, to urge their insured clients to go to court. Most of the lawyers' services in the insurance files, however, were restricted to consultation or out-of-court activities, such as writing a letter or negotiating by phone. Recent sociology of law writings stress litigation cost as an inducement to mediated or negotiated settlements. We might not expect to find much of that in the files of legal insurance companies, because the incentive for avoiding the costs of litigation is missing. However, the limited amount of litigation activity by lawyers in insurance-paid cases, noted above, raises doubts about that assumption.

Active versus Defensive Mobilization of Courts

Since we were unable to compare the litigation rates of the insured with the noninsured in strictly similar situations, we looked for further evidence to test whether those with legal insurance would more often be the parties who actively invoked the courts, rather than defending themselves against the legal action of others. The assumption that this contrast would coincide with the roles of plaintiff or defendant in court turned out to be misleading. Often, a look at the history of conflict behind a lawsuit revealed that the decisive step which turned a conflict into a legal dispute was taken by the party who appeared in court as the defendant. Parties often base calculations on opponents' desires to avoid lawyers and courts. They therefore may breach legal obligations because they do

not expect the other side to take the matter to court. In court, such cases often turn out to be uncontroversial. The defendant acknowledging the claim, gives in once the plaintiff shows its willingness to mobilize the courts (debt collection cases, resolved largely by default, are a good example). Legal insurance might encourage people to risk such enforcement by courts, as it would be free of cost for the potential defendant.

Thus, both because some people might more readily invoke courts and others might take greater risks of being sued, legal insurance might increase litigation rates. The discussion of this hypothesis runs into the same difficulties as arguments about “non-issues” in community power studies (Bachrach and Baratz, 1970). Such arguments must first explain why an issue could have occurred in order to then explain why it did not in fact do so. This is the logic of our discussion of the striking absence of effect of legal insurance on most types of litigation. However, we also have information about which cases courts usually deal with. We shall order them according to different functions of courts, ask which issues might be expected to increase with legal insurance, and then check the prevalence of these issues among court cases and legal claims.

Issues and Non-Issues by Functions of the Courts

It is well understood that only a fraction of potential legal disputes lead to the filing of a lawsuit, and that only a fraction of lawsuits filed go to the final judgment rather than being settled at some earlier stage (Miller and Sarat, 1980-81). In theory, lawsuits are unpredictable gambles, but in fact the most frequent cases in court are those in which both plaintiff and defendant know very well who will win. In such essentially nonadversarial actions, litigation serves the goal of *enforcement*—that is, to provide a legal title—or it serves a *notary* function—that is, the court certifies an agreement previously negotiated between the parties. The outcome is predictable in both of these situations, although in the first the parties disagree, while in the second they agree on what they want to achieve in court.

The dimensions of predictability and agreement yield a four-fold scheme of court functions, shown in Table 5. Types I and II describe situations in which the results are usually unpredictable: the truly adversary conflicts which must be decided by a judge; and cases in which there is at least a partial accord between the parties which leaves room for mediation by the court.

Table 5. Functions of Courts

		Predictability of Outcome	
		Low	High
Agreement Between Parties	Low	I. Adversary Litigation	II. Enforcement
	High	II. Mediation	IV. Notary

The most frequent cases in civil courts (about two-thirds of the caseload) involve Type III *enforcement issues*. The plaintiff is certain about having a rightful claim, and the defendant does not seriously contest it. These cases typically end in a default judgment for the plaintiff. Debt collection is the most common example. Litigation in such cases is usually initiated by professionals, either legal departments of large firms or specialized debt collection agencies, who normally insure themselves for their own legal costs. They are not typically holders of legal insurance, and we should not be surprised when we do not find plaintiffs from debt collection cases in our claim files. However, we might wonder about the scarcity of defendants in the insurance files. If insurance cases equally represent all private persons as parties in court, we should expect the insured to appear in the files as defendants against debt collections. This is not, however, the case: of all insurance claims (including nonlitigious lawyer consultation), only five percent are for defenses against debt collection.

The expectation that legal expense insurance would compensate for some of the barriers to consumer litigation is thus unfulfilled. Consumer complaints are only five percent of all insurance cases. This is considerably more than their share in courts, but still only a small fraction of overall litigation by insurance holders.

Courts have merely a “notary” function (Type IV) in uncontested cases, such as most divorce suits. At least two-thirds of all divorce cases are uncontested; parties have come to an agreement out of court, and they need court procedures only to render it legally valid. Insurance clauses exclude these cases because they are foreseeable risks; clients might buy legal insurance because they are planning a divorce.

Automobile accident cases, which have unpredictable outcomes and low agreement most often fall into category I. Both sides have to fight for evidence, and typically they are

unwilling to compromise. Settlements are rare; indeed these are the only types of cases in the West German civil courts where plaintiffs lose more often than they win. Accident cases have additional features which set them apart. First, they are left over from the practice of settling claims among accident insurers. Even though the plaintiff is formally suing the other driver, he is usually challenging a decision by the insurance company. Splitting the loss, as often happens in court-mediated settlements, would be detrimental to both drivers, since both would lose their "no-claim" premium reductions (this is, however, the most likely outcome). Plaintiffs are thus encouraged to gamble on a favorable judgment by the court, even though most accidents usually involve fault on both sides. This unpredictability is certainly some incentive to insuring against risk. In German civil courts, accident cases comprise about ten percent of the caseload. But such cases amount to about 50 percent of all the civil law cases found in the legal insurance files. It appears that legal insurance is used for a type of case which is litigious (e.g., unpredictable) by its very nature.

Summary

A major correction of the image of legal insurance is provided by our finding that most claims are for lawyer consultation or out-of-court activities only. Cost-free access apparently does not necessarily lead to invoking courts without prior attempts at settlement.

If we expect that the insured were more often plaintiffs than defendants, we would find this true only for liability suits arising from traffic accidents. As a rule, these are protests against a settlement between liability insurance companies, the claim being against the other driver as well as his insurance company. In all other civil suits (including those in labor court), the insured are defendants as often as they are claimants.

However, as the role which parties play in court is not always indicative of who is active in turning a conflict into a legal one, we looked at the cases in insurance claims files by court functions. Predictable cases, where courts act as notary or enforcement agency, are not found in the insurance files. Legal insurance is used for cases which are less predictable, most frequently liability cases after traffic accidents (which more than any other case in court resembles a gamble where

plaintiffs lose as often as they win⁷). It would be plausible to assume, therefore, that legal insurance is purchased in order to underwrite such risks. Part IV examines this assumption.

IV. DOES LEGAL INSURANCE ENCOURAGE MORE RISK TAKING IN LITIGATION?

Our conclusions about the propensity of insured clients to *initiate* lawsuits are merely suggestive; we do not have data on comparable groups of noninsured clients. We can, however, make some comparison with those cases which go to court. Insured parties, we believe, have higher risks of losing, and once involved in legal procedures, might be induced by insurance to “go all the way.” We tested this by comparing data on insured parties (taken from insurance files) with data on all litigants (taken from random samples of cases in German courts).⁸ We have no means of identifying the noninsured in court files, but we know their share among all court cases. Three indicators of litigiousness were available: success rates, rates of proceeding to final judgment rather than settling, and rates of appeal.

Success in Court

The principle of “loser pays all” in German procedural law is designed to deter frivolous litigation. For claimants who have no doubt about their chances for success there is no financial risk: the loser will have to pay the winner’s lawyer and court fees. If legal insurance covers the costs, however, a claimant could risk any suit, even one in which his chances of winning are minimal. A defendant usually would be wise to settle in the initial stages of a lawsuit, since costs will rise as the litigation progresses toward final judgment. However, an insured defendant might be less disposed to settle. As a result, one would expect insurance to encourage more “bad risks” than an average litigant would take. We should find a disproportionate share of losers among insurance holders. But this hypothesis was not easy to test. To control for the effect of the lawyer being paid by insurance, we had to compare only

⁷ For discussion of success rates as contingent upon issue at stake cf. Blankenburg (1980).

⁸ Only a few court studies were available for comparison, as we had to differentiate not only by the issue at stake but also by plaintiff/defendant constellation. Fortunately we could use the very reliable data of the Gesellschaft für Mathematik und Datenverarbeitung, Birlinghoven bei Bonn (Steinbach, 1979) based on files from a random sample of all West German lower courts 1974-1976.

court cases where both parties were represented by a lawyer. Furthermore, we had to consider that different issues carried different chances of success. We thus had to differentiate by kinds of cases. Then we had to match the kind of parties which we find among the insured. For example, in debt collection cases the plaintiff is usually a business, and in labor courts the defendants are usually professional litigants. We thus have to differentiate cases both by the role of the insured client in court and by whether the client is a private person or a business. As the few business clients of legal insurance companies are overrepresented among those involved in court cases, we can make comparisons with court data on only a few issues. However, frequencies in our insurance file sample are often too small to make tests of significance. Rather than being a deficiency, this could be seen as a finding in itself; court cases in the insurance claims files are much rarer than had been expected.

Overall Success

Unfortunately, data sources do not allow us to hold constant all the involved factors at once. We therefore have to proceed step by step, arguing by the consistency of a number of indicators rather than by one strict test. As shown in Table 6, if we compare all civil suits (controlled by issue), the success rates of insurance holders is higher among traffic accident cases. The data for sales and service contracts, however, reflects a higher share of debt cases where the courts serve

Table 6. Rates of Success of the Plaintiff by Issue and by Lawyer Representation

Issue	Lower Court Files			Significance level of difference between 1 and 3 ^b
	Legal Insurance Files ^a	All civil suits	Suits with lawyers on both sides	
	1	2	3	4
Traffic accidents	40% (112)	23% (100)	22% (59)	.05
Sales contracts	39% (39)	56% (269)	36% (92)	Not significant
Service contracts	41% (38)	44% (232)	25% (96)	.10

^a Cases where the insured is the plaintiff.

^b Chi² test, one degree of freedom.

mainly an enforcement function. These cases are virtually absent in the legal insurance files. Comparing only those cases where there is a lawyer on both sides, the legal insurance cases show higher success rates for plaintiffs throughout.

Differentiations by Party Constellation

Since traffic accident cases predominate among the issues for which legal insurance is claimed, their success rate is dominant in evaluating the risks that legal insurance covers. Only 20 percent of traffic accidents (as might be recalled from Table 4) lead to court; as these survived all attempts at out-of-court settlement, they are usually litigated all the way to a judicial decision. Insurance files here only show plaintiffs; defendants are backed by their liability insurance company so that they do not have to use legal insurance if they have it. As shown in Table 7, compared to other litigation issues, plaintiffs' chances of success in court are low: 23 percent. It is even lower if the plaintiff goes all the way to a final judgment. Split success results are more frequent than in any other issue before courts (35 percent of all cases, 43 percent of all those which go to final judgment). Among the cases of the legally insured, settling before final judgment is remarkably rare. Their success rate, however, is higher than that for all plaintiffs in court.

Table 7. Rates of Success: Traffic Accident Cases in Civil Courts

	Legal Insurance Files ^a	Court Files ^b	Significance level of difference ^c
<u>All cases filed</u>			
Plaintiff wins all	40% (112)	23% (100)	.10
<u>Only Cases Going To Final Judgment</u>			
Plaintiff wins all	34% (90)	19% (42)	Not significant

^a Legal insurance files, West Berlin, 1976 (*No data for defendants as there are none in the files.)

^b Steinbach, Study of Court Files, random sample of Lower Courts, 1974-1976.

^c Chi² test, one degree of freedom.

Table 8. Rates of Success: Debt Collection Cases in Lower Civil Courts^a

	Percentage Successful	
	Plaintiff	Defendant
<u>Insurance holder^b is</u>		
An entrepreneur or firm	72% (52)	
A private person		17% (6)
<hr/>		
Debt collection in the lower Court of Stuttgart (Amtsgericht) ^c	64% (2962)	16% (1660)

^a (N) refers to the total number (=100%) in each cell.

^b Legal insurance files, West Berlin, 1976.

^c Bender and Schumacher, 1980.

Results contrary to our hypothesis were also found for other types of civil cases if we separate businesses and private individuals (which are most of the insured). Among debt collection cases in the insurance company files, as shown in Table 8, 72 percent of the non-individual plaintiffs prevailed, whereas in studies of courts only 64 percent of the plaintiffs prevailed in all debt collection cases. On the other hand, insured private defendants lost their cases at the same rate as all debtors in court. (However, the small number of insured private defendants precluded statistical testing).

Labor Conflicts

In the Federal Republic of Germany, specialized labor courts handle employment disputes. More than 90 percent of these cases are invoked by an employee (cf. Blankenburg *et al.*, 1979). In our sample from insurance files, we found the insured to be plaintiffs in two-thirds of the labor court cases and defendants—usually small firms—in one-third. Only the rate of complete success for insured employers (who are always in the role of defendants) displays any marked difference from overall court figures (Table 9). Insignificant differences are found for all employed plaintiffs; they are taking only slightly greater risks than the courts' average. If we include split decisions, however, insured plaintiffs appear to do better than plaintiffs in general.

Ratios of Settlement to Judgment

If the insured were inclined to greater risk taking, they would be more likely to press for judgments than would

Table 9. Rates of Full Success in Labor Court Cases

Issue and Party	Insurance Files ^a	Labor Court, Berlin ^b	Significance level of difference ^c
Termination of work contract:			
Employee plaintiff	13% (39)	19% (5300)	Not Significant
Employer defendant	4% (20)	31% (5300)	.10
Other issues:			
Employee plaintiff	35% (41)	37% (5300)	Not Significant
Employer defendant	37% (19)	22% (5300)	Not Significant

^a Legal insurance files, West Berlin, 1976.

^b Labor court study, West Berlin, Blankenburg, Schönholz, and Rogowski (1979) pp. 108, 111.

^c Chi² test, one degree of freedom.

Table 10. Ratio of Settlement to Judgment, by Issue
Settlement: Judgment

Issue	Insurance files ^a	Court files ^b	Significance level of difference ^d
Traffic Accident	1:13.0 (112)	1:10.0 (100)	Not Significant
Debt Collection	1: 1.5 (130)	1: 2.7 (501)	.05
Service Contract	1: 2.2 (60)	1: 2.4 (97)	Not Significant
Rental Conflict	1: 1.7 (48)	1: 1.7 (225)	—

Settlement Rate

	Insurance Files ^a	Court Files ^c	
Labor Court Cases	47%	41%	90%

^a Legal insurance files, West Berlin, 1976.

^b Steinbach, study of court files, random sample of lower courts in the Federal Republic of Germany, 1974, only cases where both parties were represented by a lawyer.

^c Labour Court Berlin, study of court files, cp. Blankenburg, Schönholz, and Rogowski, 1979, at 108.

^d Chi² test, one degree of freedom.

uninsured parties in similar cases. Lawyer and court fees are lower if the parties agree to settle rather than continue to a final judgment. Thus, parties have a special inducement to settle where the terms of settlement are similar to those which

might come from a judicial decision. If insurance removes these incentives for settlement, we would find the ratio of settlements to judgments for insured litigants to be lower than that for noninsured litigants.⁹

A comparison of insurance data with court studies, however, shown in Table 10, only partly confirms this expectation. For service contracts and rental issues, the ratios for insured and noninsured parties are similar, suggesting that insurance is not influencing the decision to settle. We find a difference in the expected direction only in traffic cases. In debt collection cases the insured show above average likelihood of settling. In every other legal area the insureds' settlement rate does not differ significantly from overall court figures.

Rates of Appeal

German procedural law does not seriously restrict appeals unless the claim is very small. About one-third of appeals in German courts result in some modification of the lower court decision. The rate of appeal rises when larger sums are at stake. Decisions of the small claims courts (*Amtsgerichte*) are appealed less often than those of the higher claims courts (*Landerichte*). This difference is shown clearly in Table 11. There is essentially no difference between insurance cases and all cases decided in the lower courts; both categories show appeals in the 20-25-percent range. However, there is a substantial difference between insurance cases and all cases appealed from the higher courts: only 32 percent of insurance cases were appealed, compared with 52 percent of all final judgments in the higher courts.

This cannot be a mere extension of our earlier finding that plaintiffs in the insurance files win more often than plaintiffs in general (by issue at stake); in those cases the other side would have reason to appeal. Further differentiation of appeals shows that the opposite party was as often the plaintiff as were the insurance holders. Apparently, the decision to appeal is independent of its cost being covered by insurance. Lower appeal rates in our insurance files can be explained partly by the kind of issues insurance covers: traffic accidents have a low

⁹ "Settlement" in German procedure does not include various forms of withdrawal from a lawsuit, judgments by default, and so on, which are sometimes counted as such in American statistics. They include only those cases where a compromise has been negotiated with the help of the judge. Since litigants are not pressured by the potential for lengthy trials, as is the case under an adversary system, settlements are much less frequent than in most American courts.

Table 11. Rates of Appeal of Judgments in First Instance

	Files of	
	Insurance ^a	Courts ^b
Lower courts (<i>Amtsgerichte</i>)	21%	24%
Higher courts (<i>Landgerichte</i>)	32	52

^a Legal insurance files, West Berlin, 1976.

^b Computed on basis of Official Court Statistics, Stat. Bundesamt, Fachserie 10, 2.1. Zusatzprogramm, 1976.

overall appeal rate in court (22 percent). But the difference persists even when the kind of case is held constant: in the insurance claims files the traffic accident appeal rate of 10 percent is significantly lower than the 22 percent rate found in the court data. Compared to other issues, judgments are few, because the likelihood of a total reversal is very remote and so the costs of an appeal exceed its benefits.

Further differentiation of appeal rates by type of case is made difficult by low frequencies. Traffic accident judgments are the only ones which lead to appeals by private insurance holders in numbers which permit significance tests. Higher appeal rates are found among the insured in debt collection, in rental disputes, and in the labor courts. However, a breakdown of the data by type of party showed that, in all cases of appeal found in the insurance files, the insurance holders were small firms, landlords, or employers. As they are more likely to be repeat players in legal conflicts, their decision to appeal may be related to considerations beyond the single case at issue. For these types of cases, there was not a single instance of an appeal by private insurance holders in our claims files.

Summary

Using several indicators of litigiousness, we found that private insurance holders do not seem to engage in more risky litigation than does the average party in court. In liability suits after traffic accidents (the most frequent kind of litigation in the insurance claim files) the success of the insured plaintiffs is much higher than the average; on the other hand this is the only kind of case where the insurance files show (insignificantly) lower settlement rates than the court files. All other types of court cases occur only rarely among the insurance claims, since lawyers handle the majority of claims without going to court. Only the few businesses and small firms who hold legal insurance show lower than average success rates when being sued as employers, less inclination to

settle when collecting debts, and some likelihood of appealing after losing at trial. As they are likely to be repeat players who calculate legal costs, they might be using legal insurance to cover higher litigation risks.

V. CONCLUSIONS

Looking at any one of our indicators does not allow for firm conclusions about the impact of legal insurance on the propensity to use lawyers' services or to invoke the courts. Combining these indicators, however, creates a clearer picture. Legal insurance does not appear to induce more litigation. Even though two-thirds of all insurance policies cover general legal risks, claims are concentrated on legal problems arising from driving. Legal insurance here resembles the model of accident insurance—hardly anyone would cause accidents simply because they are insured against some of the financial consequences.

Litigation is generally considered to be undesirable. Therefore legal insurance resembles accident, fire, and theft insurance, which protect against risks occurring largely outside of preventive possibilities of the insured. Like accidents, legal conflicts are avoided even when (some of) their costs are covered by insurance. "Social costs" of litigation, which the insurance cannot cover, seem to be more important than the financial costs which prepaid legal cost insurance does cover. Therefore legal insurance does not *cause* legal costs any more than accident insurance causes accidents.

Our data also raise some questions about proposals to use general legal insurance to lower barriers of access to lawyers and courts. Writers making such proposals assume that not having to pay would increase the use of lawyers and litigation, particularly by the poor, by eliminating the deterrent effect of cost. They consequently recommend a policy of encouraging litigation by furthering equal conditions of access. Engaging the courts and consulting lawyers would be considered a public good like health and consulting doctors. They recommend legal insurance, like health insurance, as an inducement to using services because these services are seen as preventing greater damage (to the individual as well as to the public good). The difficulty of such insurance for the public good is to forestall overuse. Specifying limiting clauses and levying "deductibles" are devices to that effect.

But our data suggest that the "public good theories" of more equal distribution overestimate the price elasticity of

legal services. The social costs of spoiling a relationship by threats of lawyers and courts render it very unlikely that people will go to court over conflicts in ongoing relationships.¹⁰ Lawyers are consulted and courts invoked when social ties break up or in anonymous situations like traffic accidents. The decision to invoke the legal system is less dependent on financial than on social cost considerations. Therefore, we are led to be skeptical about the idea of using legal insurance schemes as compensation for social barriers to access to law. Just as we find social costs ranked before financial costs in leading people to *not* litigate, social contacts with lawyers and shared social class are more essential in overcoming access barriers than is financial aid. Insofar as legal insurance companies act as referral institutions, we found them to be helpful in finding a lawyer (but only for those who asked). In general, however, legal insurance seems to cover only those services which people would use anyway. People seem to buy insurance because of the possibility of litigation; there is no evidence that they litigate more because they have legal insurance.

The stability of litigation avoidance has no doubt encouraged insurance companies: were it otherwise they might be less eager to sell legal insurance policies. Their interest after all is in selling insurance policies, and not in promoting their use (at least not in innovative and unpredictable ways). By trial and error they found that the assumptions about the effects of removing cost barriers to litigation did not hold true; there are more deterrents to litigation than the financial one. But legal cost insurance leads clients to traditional law offices, and if it lowers some of the barriers to litigation, it does so in traditional areas. Innovative trends in lawyers' services, such as giving more attention to the legal problems of the poor, would occur only if lawyer activism were rewarded, and legal insurance companies are not interested in doing that.

From the perspective of the legal profession, legal cost insurance has the effect of stabilizing lawyers' income, just as health insurance does for medical professionals. Legal insurance does not change the patterns of using lawyers; it only provides a mode of paying for their services. In the United States, contingent fees and the possibility of advertising lawyers' services may have had a more activating impact on American lawyers than legal insurance has had on German

¹⁰ Numerous authors have made this observation; see Black (1976), Sarat (1976), Blankenburg *et al.* (1979). For a detailed discussion see Gessner (1976).

lawyers. German lawyers form a comparatively uniform and traditional profession to begin with (cf. Rueschemeyer, 1973); legal insurance has had the effect of stabilizing, rather than expanding, the scope of their activities.

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