The theoretical foundations of fault and no-fault compensation

By Barbara McDonald

The NSW government's proposal to introduce a no-fault scheme for the long-term care of those seriously injured in motor accidents must be carefully scrutinised to ensure that it is the best option for providing a fair, appropriate and humane system of care.

Photo: Bill Madden

This analysis of the major theoretical and policy foundations of fault-based and no-fault based systems draws predominantly on Australian and NZ sources. As a federation of states, Australia has a range of systems, some fault-based, some no-fault, some a combination of the two, in various contexts.

THE ROLE OF FAULT IN TORT AND NEGLIGENCE LAW

In the last edition of his great work, *The Law of Torts*, before his death in 1997, Professor John G Fleming wrote:

> 'Tort liability ... exists primarily to compensate the victim by compelling the wrongdoer to pay for the damage done. True, some traces of its older link with punishment and crime have survived to the present day, most prominently exemplary damages to punish and deter contumelious and outrageous wrongdoing. Yet the principal concern of the law of torts nowadays is with casualties of accidents, that is, of unintended harm. In this wider field, the law is concerned chiefly with distributing losses which are an inevitable by-product of modern living, and, in allocating the risk, makes less and less allowance to ideas of punishment, admonition and deterrence.'[1]

It is generally agreed that the law of torts, as it has changed and evolved over the centuries, has had three explicit purposes:

- to punish and deter;
- to provide compensation for those injured by the 'wrong' of another; and
- to distribute losses by allocating or shifting them from where they fell to another, when there is some justification for doing so.

In terms of distributing losses, Professor Fleming wrote:

> 'A shifting of the loss is only justified when there exists special reason for requiring the defendant to bear it rather than the plaintiff on whom it happens to have fallen ... The task confronting the law of torts is therefore, how best to allocate these losses, in the interests of the public good.'[2]

Corrective justice

Generally, the special reason for shifting the loss on to the defendant was that s/he was at fault: his or her activity was *deliberately* wrongful or constituted an *undue lack of consideration or care* for others. 'Corrective justice' thus satisfies the victim's desire for justice and retribution and negates or reduces their need or desire to exact revenge themselves.

Whether this function was ever 'intended' for the action of negligence is debatable. Certainly, in the case of the few torts that are *actionable per se* (without proof of damage) – namely all forms of trespass and also libel – tort is often concerned not so much with compensation as with vindicating rights and deterring wrongs. The vindication of rights has been emphasised as an important function of the tort of trespass as recently as 1991, when the High Court in *Plenty v Dillon*, in a judgment that shares some stirring rhetoric with that classic Australian film, *The Castle*, upheld an award of 'substantial damages' to redress the defendant's deliberate trespass.

Gaudron and McHugh JJ said:

> 'If the courts of common law do not uphold the rights of individuals by granting effective remedies, they invite anarchy, for nothing breeds social disorder as quickly as the sense of injustice which is apt to be generated by the unlawful invasion of another's rights...'[3]

The tort of negligence, on the other hand, has always required damage for the action to be complete. Only actual loss or damage persuaded the earliest courts to countenance an 'action on the case' from which our modern tort has developed. So, from its earliest form, compensation was a primary, if not *the* primary, rationale for the action.

Nevertheless, although damage caused by a defendant's conduct is a necessary element for the action for negligence, it is not a sufficient element: fault in the form of an unreasonable lack of care or a breach of duty was and is the essential condition for *shifting* the loss from plaintiff to defendant in cases of accidents or unintended harm.

> 'Fault alone was deemed to justify a shifting of loss, because the function of tort remedies was seen as primarily admonitory or deterrent.'[4]

Some historians saw the rise of the tort of negligence in the late 19th century not as an increase in liability, but as a subsidy or protection to those engaged in the industrial revolution, with its inherent or avoidable risks of injury to others from the use of machinery, from *strict* liability for dangerous activities. Despite the age of rampant free >>

enterprise, 'no liability' was no longer an option. 'No liability without fault' was the best available protection for the entrepreneur.

Oliver Wendall Holmes, on 'The Common Law', wrote in 1881:

> 'The true explanation of the reference of liability to a moral standard … is not that it is for the purpose of improving men's hearts, but that it is to give a man a fair chance to avoid doing the harm before he is held responsible.'[5]

Other legal historians disagree with this rather cynical view of 19th century tort law, showing how the courts were not shy to discern duties and fault so as to impose liability for negligence on rapidly growing industries and activities.[6] In some cases, they even imposed strict liability at common law on enterprises fraught with danger (for example, *Rylands v Fletcher*, in 1868) but such cases were rare, and certainly it was always necessary to prove fault in highway accidents. Legislators, too, played their part from the mid-19th century, introducing perhaps the most significant legislative extension of liability for fault: the fatal accidents or compensation to relatives statutes.

After a century of enormous development, consolidation, expansion and delineation in the law of negligence, how has the picture changed in relation to the role of fault?

In Australia, the common law has tended to move away from strict liability altogether, and to renew the emphasis on the requirement of fault.[7] Yet, it is not uncommon to hear the view these days that the standard of care in negligence has become so easy to breach that, in effect, negligence has itself become almost a tort of liability without fault.

> The lump-sum system gives injured people the ability to decide their own future without needing to be dependent on others.

Such sentiments prompted the proliferation of state tort reform statutes in 2002 aimed at reducing liability either by reducing costs or damages or by increasing the number and power of defences. But legislation was not always so restrictive: previously, it had introduced either no-fault liability or strict liability,[8] or had reduced the impact of common law defences such as contributory negligence.

Distributive justice

Another theoretical rationale for loss-shifting is the notion of 'distributive justice' – that is, that loss should be shifted to those who stand to benefit most from the risk or to those who can best spread the loss among all those who benefit, either by increasing the cost or price of the activity or product or by taking out insurance, so that the risk is borne by all insured parties. This notion depends, of course, on either a capacity to absorb the cost of accidents in the cost or price of the activity, or a workable and affordable insurance market or scheme: the law of tort expanded so greatly in the 20th century because of the parallel increase in the insurance market. This is not necessarily bad or illogical, as many people imply, rather the opposite: the *point* of insurance is to spread losses.

What is unworkable is where the actual liabilities incurred by an insurance fund exceed the estimated risks undertaken in type or size. Either the contributions to the fund have to grow in number or size, or the payouts have to contract. NSW history implies that we prefer the latter option, at least in respect of motor accidents.

Law and economic theories

These theories seek an economically efficient solution to accidents and the allocation of risk. On the premise that prevention is better – and probably cheaper – than cure, they look for the person who can prevent the accident at the lowest cost and impose liability on him or her. Or they look to those who can *most* efficiently procure insurance for the risk on behalf of others. Again this burden tends to fall on the actor, not the victim, so that the cost of prevention or insurance is built into the cost of the enterprise and is passed on to those who benefit from it. Such theories find little explicit support in the case law, except in cases determining vicarious liability of employers and principals.[9]

NO-FAULT IN NEW ZEALAND: THE WOODHOUSE REPORT

Perhaps the most comprehensive statement of the arguments supporting a comprehensive no-fault scheme can be found in the Woodhouse Report (the Report of the Royal Commission of Enquiry into Compensation for Personal Injury in New Zealand in 1967), which preceded the setting up of its scheme in 1972.[10] It set out 'five guiding principles', or ideals, for such a system:

- community responsibility;
- comprehensive entitlement;
- complete rehabilitation;
- real compensation; and
- administrative efficiency.

As one commentator has noted, the Accident Compensation Scheme was immediately beset, as it still is, by problems relating to delineation of boundaries, particularly the distinction between compensation for accident or injury and compensation for illness, a distinction inconsistent with its first two stated principles of community responsibility and comprehensive coverage.[11] Much of the recent debate in New Zealand has been concerned with the boundaries of the scheme, the lump sum versus weekly payment issue, and new accident prevention strategies.

While the New Zealand scheme enunciates specific goals, it is clear that different proponents – academics, economists, retired and current judges, insurers, politicians, consumer groups, government departments, and professional groups such as doctors – have differing political, specialist and social views and agendas when advocating no-fault schemes. Despite this, they seem to share one central belief: that a no-fault system is a better, even if imperfect, alternative to the tort system.

CRITICISM OF THE NSW TORT SYSTEM

A good place to start identifying common criticisms of the tort system is the NSW Law Reform Commission Report on Accident Compensation in 1984,[12] which identified a number of criticisms of the fault-based common law system (although it should be stressed that many of the criticisms in fact concern the 'once and for all' system rather than, or as much as, the fault element).[13] The report also identified arguments in favour of the common law system.[14] The following is a brief summary.

The problems and advantages of once-and-for-all assessment

No principle necessarily or inherently ties the 'once and for all' rule to fault-based liability: while it is hard to imagine how the common law *could* have developed a workable 'come back later' or periodic-payment-and-review approach, there is certainly nothing to stop the legislature from introducing periodic payments and review as a feature of insurance-based compensation for fault, just as it may do for a no-fault system.

The main criticisms of a once-and-for-all system were stated as follows:

- the difficulty of accurately estimating future losses, given the uncertainty of life expectancy, medical prognoses, vicissitudes of life and employment, future care costs, changes in family support and circumstances;
- the risk that awards will be inadequate to cover losses in the long term because of underestimates or settlements; and
- the risk that awards will be badly managed or misapplied with the consequence that the victim will be left uncovered and will 'double dip' into the social security system.

The report also noted, however, that a significant and highly valued advantage of the lump-sum system was the independence it gave to accident victims. It restores the independence victims previously enjoyed due to their earning capacity which they lost in the accident. It also gives them the ability to decide their own future without the need to be dependent on others. The report also made reference to the freedom and dignity conferred by lump-sum payments as opposed to the 'charity' of weekly payments.

The adverse effects of the common law action on rehabilitation for many victims

Again, many problems are associated with other aspects of a common law system of compensation – for example, the once-and-for-all system, the expert evidence system and, perhaps, to a greater or lesser degree, to any system of assessment for injury, whether by a court or a bureaucracy. The report also referred to arguments that the lump-sum method *aided or improved* rehabilitation rather than >>

inhibited it. Periodic review can inhibit recovery even more, because the victim has to maintain disability to maintain support whereas the lump sum encourages finality, pushing the trauma into the past and aiding the victim to look to the future.

CONCLUSION

It is clear from the experience in New Zealand that it would be a mistake to assume that a change to a no-fault system would remedy all the shortcomings of the common law and provide all the answers to problems of compensating and caring for injured people in a fair, dignified and humane way. Debate continues there as to extent and level of cover, how to deter accidents, how to enhance incentives to recovery and rehabilitation, how to reduce overall expense, and how to achieve efficient but fair administration. Another important issue is the extent and financing of supplementary common law rights. Even where no-fault compensation is payable, entitlement to benefits may not always be straightforward: claimants, many of whom are vulnerable in some way, may need personal representation and protection from overzealous guarding of the insurance fund by those handling the claims. These are all important practical and social issues and should be carefully considered.

But the fact that problems remain should not deter us from filling the gaping holes in the protection we offer to injured people.

In fact, we should ask ourselves whether the proposals go far enough.[15] Why, for example, in a sporting nation such as ours could we not have a national insurance and compensation system financed by contributions from the vast numbers who participate in organised sport every week? ■

Notes: **1** JG Fleming, *The Law of Torts*, 9th edition, 1998 at 3. **2** *Ibid* at 5. **3** *Plenty v Dillon* (1991) 171 CLR 635 at 655. **4** Fleming, note 1, at 10, citing both Austin and Salmond in footnote 35. **5** *Ibid* at footnote 34. **6** Gary Schwartz, 'Tort Law and the Economy in Nineteenth Century America: A Reinterpretation', in Saul Levmore, ed, *Foundations of Tort Law*, Foundation Press, 1994. **7** See, for example, *Burnie Port Authority v General Jones* (1994) 179 CLR 520 in which the High Court abolished the rule in *Rylands v Fletcher* in Australia and *Northern Territory v Mengel* (1995) 185 CLR 30, in which it overturned the principle from *Beaudesert Shire Council v Smith* for lack of appropriate fault. **8** For example, workers' compensation legislation, s52 of the *Trade Practices Act* 1974 (Cth) in relation to misleading and deceptive conduct and, more recently, part VA in relation to product liability. **9** For example, *Hollis v Vabu Pty Ltd* (2001) 207 CLR 21. **10** See S Todd, 'Negligence Liability for Personal Injury: A Perspective from NZ' (2002) 8(2) UNSWLR 55. **11** K Oliphant, 'Beyond Woodhouse' (2004) 35 VUWLR 915 at 917. **12** NSWLRC 1984 Report 43, *Accident Compensation: A Transport Accidents Scheme for NSW into Motor Accident Compensation*. **13** The tort system produces a single lump-sum payment as compensation 'once and for all', whereas the no-fault scheme discussed in the report provides ongoing benefits. **14** A succinct summary of the arguments on both sides, for and against the tort system, is to be found in the NSWLRC 1984 Report 43, *Accident Compensation: A Transport Accidents Scheme for NSW into Motor Accident Compensation*. This report is still influential today as many of the points it makes are still highly relevant (Harold Luntz, 'The Australian Picture' (2004) 35 VUWLR 879 at 893 and 902), although it has to be noted that both the *Motor Accidents Act* 1988 and the *Motor Accidents Compensation Act* 1996 introduced measures that respond in part to some of the problems identified in the 1984 report. **15** Professor Harold Luntz, writing in a symposium at Victoria University Wellington NZ on 'The Future of Accident Compensation', recently provided some figures that indicate that we have continued to take the option of reducing compensation rather than increasing premiums. Average CTP premiums in NSW were the same in 2002 as they were in 1989/1990. It would be interesting to compare these figures with the average cost of medical care over that 13-year period. It is inconceivable that medical costs could have stayed the same. One only has to compare increases in private health insurance to know that they have not. Yet, as a community we have tolerated, perhaps through ignorance, the gradual erosion of compensation for motor accidents injuries even when caused by the fault of another, and the shifting of costs on to an already struggling public health system, in order to make it as cheap as possible for people to drive cars. Why on earth do we do this?

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