LIMITATION OF ACTIONS: JUSTIFIED OR UNJUSTIFIED COMPLEXITIES?

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1. Introduction

The law governing the limitation of actions, that which govern the time period during which legal claims must be made, may appear to be a very technical subject, but it is one which provokes much litigation. The law is, indeed, hugely complex and, even more significantly, there are major differences both between national jurisdictions and within jurisdictions in relation to the periods governing different legal claims.

There has been much discussion, and criticism, of the law in legal-policy documents (se e.g.; Law Commission (England and Wales) 1998; New Zealand Law Commission 2000) and academic writings (for a useful if dated, comparative survey, see Hondius 1995), but it is not a subject which has attracted much attention in the law-and-economics literature. I am aware of only three papers (Baker and Miceli 2000, Miceli 2000, and Lando 2005) which deal directly with the issue and their focus is narrow.[1] This is surprising because the question what period of limitation is appropriate for a given legal claim has important economic implications which are neglected in the legal-policy literature. That literature tends to identify the key normative concern as being one of "fairness", and thus principally involving a trade-off between depriving claimants of the right to enforce their rights and imposing uncertainty on defendants (e.g. Hondius 2005, 29, 93-94, 261). The question of how the choice of a period of limitation might affect the incentives to perform legal obligations seems almost completely to be ignored.

My contention is that an economic perspective can generate important insights for the normative purpose of formulating appropriate limitation periods and also on whether the complexities and the differences between jurisdictions can be justified. In this paper I first identify the key legal questions and relate them to others which raise similar or analogous issues (section 2). I then describe the main features of the relevant law, concentrating on English law but making reference also to the law in other jurisdictions (section 3). In section 4 I explore the costs and benefits of periods of limitation, thus providing a framework for determining what, in relation to specific types of legal claims,

[1] Miceli and Baker and Miceli deal with tort claims and focus heavily on how the limitation periods affect incentives to take care, without much attention to the costs, private and social, arising from delays in bringing suit. Lando takes a somewhat broader approach, but his focus is on limitation periods in sale contracts.

might be considered optimal (section 5). Having considered the relevant legal rules in the light of that framework, I then in, section 6, consider what might justify the complexities of the law. Finally, in section 7, I add a public choice dimension, in the expectation that it might help to explain some of the those complexities not justified by the economic framework.

2. Key Issues

A claim arises under tort law, for breach of contract, or for the recovery of property. During what period must it be made? I am not here considering the equivalent question in criminal law or in public (administrative) law, though both areas can give rise to interesting discussion (see, on the criminal law, European Commission 2001, 40-42). Note that my question arises under procedural law, thus distinguishing it from the substantive law question of the temporal extent of liability, for example, whether liability arises in relation to damage which only occurs some years after the activity which was responsible for it. The latter question has some common features with limitations and is much discussed, particularly in the context of insurance cover (see e.g. Faure 1998). Analytically it is, perhaps, best kept distinct from the limitation issue.

The limitation issue, thus identified, itself gives rise to five principal policy questions on which there has been legal (but not economic) debate (Andrews, 1998).

(1) Should there be a uniform limitation period for all types of action? If so what should be the length of the period?

(2) If not, what different periods should be imposed for specific legal claims?

(3) From what date should the limitation period run?

(4) Should the parties to the claim be free to modify the rules?

(5) Should there be judicial discretion to depart from the rules? If so, in what circumstances should the discretion be exercised?

3. The Law: Principal Features

I first provide an overview on how legal systems, but mainly English law, have responded to these questions.

(1) A number of legal systems have a general period of limitation which provides a final time barrier for all types of legal claims. Traditionally this was, in many jurisdictions, 30 years (Jolowicz, 1972), but in recent years has, in some systems, been reduced to 15 or 10 years (Hondius, 1995). In any event, the general rule is invariably combined with a set of rules providing shorter periods for particular causes of action.

(2) "The legal systems … present a bewildering variety of solutions and, indeed, different periods for different kinds of case exist within individual legal systems" (Jolowicz 1972, 23). And a German commentator refers to the "extraordinary degree of differentiation between the various periods prescribed by the [civil] code as well as by countless statutes outside the code" (Zimmerman 1995, 173). Here I give a summary of the periods in English law and then only for the main categories (for other rules and more detail, see McGee 2002):

   (a) actions on formal deeds: 12 years
   (b) personal injury actions (tort or contract): 3 years
   (c) other contract and tort claims (except defamation): 6 years
   (d) defamation: 1 year
   (e) recovery of land: 12 years
   (f) collisions at sea: 2 years

(3) The general rule in English law is that time runs from the date when the cause of action arises (tort or contract) or (recovery of land) from the date of the rightholder's dispossession. More specifically:

   (a) contract: from the date of breach of contract
   (b) tort law (except for personal injuries or cases of "latent damage"): from the date of damage
   (c) personal injuries[2] and latent damage: from when the claimant acquires knowledge of the wrong/claim

(4) It seems that, in general, English law allows, by contract, consensual variation of the limitation period, subject to considerations of public policy; [3] and the same is

[2] Includes fatal accidents.
[3] *Northern and Shell v John Laing* [2002] EWHC 2258.

true in France (Bandrac 1995, 156-157). In Germany, the parties can apparently agree to a shorter, but not a longer, period (Zimmerman 1995, 204-205).

(5) In English law judicial discretion to extend the period of limitation is allowed only in cases of personal injury and death. The legislation lists particular factors which the court should take into account in exercising the discretion. These include: the reasons for the delay; the effect of the delay on the cogency of the evidence; the conduct of the defendant and of the claimant (when aware of the legal right); and the existence and extent advice made available to the claimant.[4] Civil law jurisdictions have been reluctant to confer an equivalent discretion on the judges, although the courts have apparently found ways indirectly of extending the period through, for example, their findings as to when damage occurs. (Hondius 1995, 18).

4. Economic Rationalisation of Limitation Periods

An economic approach to the question of limitations must involve an investigation of the costs and benefits of imposing limits on the period during which a legal claim must be brought.

(a) costs of limitation period

There would seem to be two principal sets of costs:

(1) claimants who do not bring their claim within the period lose the value of the remedy, often compensation, which they would otherwise have obtained;

(2) defendants have a reduced incentive to perform their legal obligations, since some proportion of claims will not be brought within the period.

In their analysis of the issue, lawyers concentrate almost exclusively on (1), ignoring (2); and economists concentrate almost exclusively on (2), ignoring (1). The explanation for the economists' approach is that (1) is fundamentally a question of distributional justice, the failure to enforce rights having economic significance only if it reduces incentives to comply with the law. That does not, of course, mean that (1) is irrelevant to normative discussions.

Two further sets of costs should be included:

[4] Limitation Act 1980, s.33(3).

(3) some claims, particularly those where the evidence required is difficult to obtain, may not easily be substantiated, and the shorter the limitation period, the more the claimant will have to invest resources in obtaining the evidence or risk failing with the claim (with consequent error costs).

(3) Less obviously, the limitation periods also generate perverse incentives for defendants to engage in opportunistic behaviour, by attempting to induce claimants to delay in making claims.

(b) benefits of limitation periods

The benefits of limitation periods are less easy to specify because they cover a wider range of effects, but the main categories would seem to be as follows.

(1) reduction in litigation costs, since some litigation which would have taken place is now avoided; the costs are mainly incurred by the parties, but social costs are also involved to the extent that the judicial process receives public subsidies.

(2) reduction in the costs accruing to defendants and some third parties[5] from uncertainty as to whether (and when) a legal claim will be brought.

(3) reduction for both parties, and third parties (notably witnesses), in the costs of storing information that would be used in the trial (if any).

(4) reduction in the error costs of decisions made on the basis of information the quality of which, over time, deteriorates. These costs fall principally on the parties, even though ex post some of them may unjustifiably benefit from the error, because it is to be assumed that ex ante their preference is for a correct decision. To some extent, errors also give rise to social costs, as third parties may be affected and also, more generally, errors may undermine confidence in the judicial system.

5. Economic Rationalisation of Variations in the Law

For any legal claim, the optimal limitation period can thus be defined as the point where the costs in 4(a)(2)-(4) and those in 4(b)(1)-(4) are minimised. If distributional justice for rightholders is considered important, then some weighting can be used to reflect 4(a)(1).

[5] Particularly where there is a dispute over property entitlements which has implications for third parties.

Given the heterogeneous character of legal claims, the variables relevant to this analysis are likely to have significantly different values, thus justifying rule-diversity. The task now is to see whether the differences within (and to some extent between) legal systems can be rationalised on the basis of this analysis.

(a) Periods agreed in contracts

In England and France the rules governing contractual claims are effectively default rules since, subject to public policy considerations, the parties are free to choose their own period. That solution is, in economic terms, appropriate if the public policy constraints are well targeted to the existence of externalities, it being assumed that the parties will select a period which minimises their own sets of costs. It is not clear why German law should prohibit an agreed lengthening of the default limitation period, unless this will in the majority of cases lead to substantial externalised costs, for example, those incurred by state-financed institutions.

(b) Types of damage

Over time information and error costs are likely to increase at a higher rate in relation to physical damage as compared with pure economic losses, due to the scientific nature of the evidence often involved. In addition, there are greater losses associated with the uncertainty resulting from delays in personal injury cases, because there are disincentives for injured claimants to recover from their sickness or injury, given that that will reduce the amount of their compensation (Lewis 1993, 26-27). These considerations help to explain the shorter time period allowed in personal injury actions, whether claims are brought in tort or in contract.

(c) Contract v tort

In practice the period under the contract (default) rule is generally shorter than in tort law, because in contract time begins to run from the date of breach, whereas the equivalent in tort is the date of damage. Now while it may true that contract claims are predominantly for pure economic loss and tort claims are mostly for physical damage, thus enabling us to invoke the argument used in the last paragraph, there are many exceptions. We need then to investigate how the variables may impact differentially as between the environments of tort and contract. One possible justification for the shorter

period in contract law is that contractual liability may be less important than tort liability in generating incentives for compliance with legal obligations. As is well known from empirical studies (e.g. Beale and Dugdale 1975), many promisors are motivated to comply with their contractual obligations because they are concerned to maintain their reputation in the marketplace or with particular customers, rather than because they apprehend the impact of legal sanctions. The same phenomenon may apply to some potential tortfeasors, but it cannot be so widespread. If that is right, it is relatively more important to maintain the incentive effects of tort liability, thus suggesting a longer limitation period.

Another explanation arises from the fact, already noted, that the contract rule is a default rule. While the benefits of a longer period, preserving the incentives to comply, accrue mainly to the contracting parties themselves, a shorter period generates benefits also for third parties: reductions in the costs of collecting and storing information. So, if the default rule, incorporating a shorter period, is not appropriate for the parties, they can extend it by contractual provision.

(d) Contracts by deeds

In English law, contracts formalised in deeds have a long limitation period (12 years). The evidentiary problems of enforcing contractual debts of this kind are small, since witnesses and documentation external to the deed are rarely required. Information, error and "storage" costs are, then, low, thus justifying the extended time period.

(e) Defamation

Defamatory statements give rise to reputational losses. An argument that has been made for the short period of limitation (one year) in English law[6] is that, at least where commercial reputation is not involved, "swift manifestation of hurt feelings" by the claimant is required (Andrews 1998, 596-597). But this is unconvincing: the consequences of a successful lowering of social reputation may continue long after the actionable publication. A better rationalisation would seem to be that, given the nature of the loss, and the subjectivity of perception of it, the reliability of evidence may decline

[6] Two years in New Zealand: see Todd 1995, 276.

relatively rapidly with the passage of time, and therefore – in comparison with other losses – may generate higher error costs.

(f) Recovery of land

On the face of it, the longer period of limitation allowed for the recovery of land in England (12 years) and elsewhere[7] is somewhat of a puzzle. Policy discussions (e.g. Law Commission 1998, para 1.34) point to specific characteristics of land-related claims which enhance the case for shorter periods. For example, to encourage the productive use of land, a shorter period rewards persons who take possession of unused land. It also facilitates conveyancing costs, at least of unregistered land and generates legal certainty, of particular benefit to third parties. Why then is the period so much longer than for ordinary tort and contract claims? It is unlikely to be the case that the "storage costs" of evidence relating to land claims are particularly cheap, nor that the cogency of that evidence have particular endurance over time. It may be the case, notably with unregistered land, that the information costs incurred by claimants in asserting title are significant and that they would become unjustifiably high with shorter periods (benefit 4(a)(3)). Or it may be that distributional considerations are at work, deprivations of rights in land being considered particularly objectionable.

6. Economic Rationalisation of Complexities in the Law

The policy question of the extent to which judicial discretion should replace the rules governing limitation period, or should enable judges to overreach the rules in particular cases, is linked to the issue of complexity which characterises this area of law. Given the wide range of legal claims, and the variety of circumstances in which they are brought, it is clear that there will be a large variance in optimal limitations period. That does not, however, necessarily imply that the law should prescribe these periods by means of rules. There are in fact four possible strategies:

(1) the law aims at high degree of targeting through a complex network of specific rules;

(2) the law aims at a high degree of targeting through general principles and judicial discretion;

[7] E.g. 10 or 20years in Canada: Des Rosiers 1995, 113.

(3) the law aims a high degree of targeting by combining a network of specific rules with judicial discretion, in appropriate cases, to override those rules;

(4) the law aims at a low level of targeting by limiting regulation to a relatively small number of specific rules.

A comparison of the approaches taken in different jurisdictions proves to be interesting. Civil law jurisdictions have tended to adopt strategy (1), being culturally resistant to conferring broad discretion on the courts. However, as limitation periods have, as a result of legislative reform, become shorter, in order to help claimants, courts have looked for ways of extending the period. They have done this by, for example, a determination that the "damage" or awareness of it occurred at some period after the commission of the tort (Hondius 1995, 18). In practice, therefore, there appears to have been an evolution towards strategy (3).

Common law jurisdictions seem also to prefer strategy (3). So, for example, English law combines a complex network of rules with some explicit legislative authorisations of discretion. Most famously, there is the Limitation Act 1980, s.33, which grants the court power to allow a claim for death or personal injuries to proceed, notwithstanding the limitation period, where this would be "equitable". In determining what is "equitable the court must have regard to "all the circumstances", but should also take into account a statutory list of considerations which makes reference to the level of awareness of claims and the conduct of both parties. Unsurprisingly, this provision has given rise to a huge case law which one commentator describes as "both scandalous and disastrous" (Andrews 1998, 608).

In striking contrast, the Israeli legislature decided not to confer a discretion on the courts. The explanation given by one commentator - "the huge discrepancy in scale and magnitude between the injustice that such discretion may prevent and the uncertainty it produces" (Gilead 1995, 210) – can be related to the classic law-and-economics literature on the choice between general principles (combined with a significant degree of judicial discretion) and specific rules (Ehrlich and Posner 1975; Kaplow 1992). According to that literature, a trade-off must be made between the

benefits of the reduction in uncertainty arising from the specific rule and the costs arising from imperfect targeting.

Applying this approach to the limitation issue would require us, first, to specify the benefits of good targeting. Focussing on the major variables identified in 4(a)-(b). that suggests the benefits arising from increased incentives to perform legal obligations, combined with a reduction in information, storage and error costs. Those benefits then have to be assessed and compared with the costs, private and social, arising from the different methods of achieving better targeting. In summary these are as follows.

> Strategy (1) (complex network of specific rules): high information costs to the parties and high legislative formulation costs.
>
> Strategy (2) (general principles and judicial discretion): high information costs to the parties – exceeding those incurred in (1) because of the lower visibility of case-law and increased uncertainty as to outcome - and high adjudication costs.
>
> Strategy (3) (network of specific rules combined with judicial discretion): the costs incurred in (1), subject to some reduction if there is less complexity in the rules, combined with a proportion of the costs in (2) for situations where judicial discretion overrides the rules.

It is, of course, impossible to quantify these costs and benefits and it is even difficult to make an impressionistic assessment of what strategy is likely to be optimal. However, if I were asked to make guesses on these issues, I would be tempted to suggest the following:

> The benefits of better targeting in strategies (1)-(3) are unlikely to exceed the costs, with the implication that strategy (4) would get closest to the optimal outcome.
>
> Strategy (1) is preferable to strategy (2),because the high information costs arising from lower visibility and increased uncertainty are unlikely to justify any benefits from finer tuning provided by judicial discretion.
>
> The compromise strategy (3) is likely to be preferable to strategy (2), because the reduced area of discretion will lead to lower information costs,

but it would probably compare unfavourably with strategy (1), given the costs that arise from combining specific rules with discretion.

7. Public Choice Rationalisation of Complexities in the Law

If, on the basis of the above analysis, the conclusion is reached that the law in England and Wales, and in many other jurisdictions, is more complex that economically is justified, the interesting question arises why it should be so. As an addendum to the paper, I wish to relate that question to another area of my work (Ogus, 2002). I have argued that practising lawyers have an incentive to persuade legislature and policymakers to adopt legal rules and legal procedures which are more complex than that which is optimal, because this is likely to increase demand for their services. Given the power of lawyers within legislative, particularly drafting, processes, they are likely to be successful in having their preferences met.

The tendency of law to become excessively complex may, however be thwarted by either or both of two countervailing forces. First, if the relevant issues are transparent, and hence information costs are low, interest groups representing the purchasers of legal services may be able to generate sufficient opposition to the lawyers' lobbying. Secondly, if – and to the extent that – the legal system in question faces competition from other legal systems for processing relevant legal claims, then the threat of loss of business to lawyers who charge less for providing an equivalent service, may constrain the lawyers' desire for complexity.

Applying these ideas to the present context, we may note, first, that the law on limitations is unlikely to be transparent. The second countervailing force may, in relation to some areas of law, have greater potential. Competition between legal orders has its greatest impact in relation to legal disputes with a transboundary dimension or where some degree of forum shopping is possible. The implication is that the law of limitations is likely to be more complex in areas where an international dimension is relatively rare, such as personal injuries and land disputes, rather than in areas where such a dimension often exists , such as commercial transactions.

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