

# THE DISAPPEARING OPT-OUT RIGHT IN PUNITIVE-DAMAGES CLASS ACTIONS

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One of the most pressing issues in punitive-damages law today is how to protect defendants from multiple punitive-damages awards for a single course of conduct, while still ensuring that wronged plaintiffs can recover punitive damages. Numerous commentators have proposed non-opt-out class actions for punitive damages as the best solution to the multiple-punishment problem because they subject defendants to a single collective-punitive-damages award that can be distributed equitably across all injured plaintiffs. This Article takes a contrary view. It argues that mandatory classes improperly deprive class plaintiffs of their right to opt out and pursue their own individual claims while allowing defendants to self-servingly cap their punitive-damages liability at an artificially low level that thwarts the punishment and deterrence purposes of punitive damages.

First, this Article explains that because the Supreme Court has held that an individual plaintiff can collect punitive damages only for harm done to that plaintiff, allowing plaintiffs to opt out and pursue their own claims creates no risk of imposing duplicative punishment on defendants. Second, this Article suggests that mandatory classes are particularly inappropriate for class-action settlements because settlements are not punitive in nature. In a class settlement, parties have incentives to manipulate the settlement fund's allocation of punitive damages in ways that bear no connection to wrongdoing or punishment, and that allow defendants to significantly reduce their punitive-damages exposure. Instead, preserving class members' right to opt out best protects plaintiff autonomy and helps ensure that defendants pay an appropriate amount of punitive damages.

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#### INTRODUCTION

The problem of imposing multiple punitive-damages awards on defendants for a single act of misconduct—also known as the “multiple punishment problem”—has vexed scholars, practitioners, and judges for nearly forty years.<sup>1</sup> Multiple punishment concerns arise frequently in mass tort litigation.<sup>2</sup> The problem goes something like this: a defendant who engages in a widespread illegal practice that harms a large number of people faces exposure to hundreds or even thousands of lawsuits seeking punitive damages. Scholars, judges, and defendants have argued that repeated punitive-damages awards threaten to violate defendants’ due process rights by subjecting them to duplicative punishment that exceeds the level of damages necessary to sanction the defendant for the harm it caused and to deter future wrongdoing,

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1. See, e.g., Laura J. Hines, *Obstacles to Determining Punitive Damages in Class Actions*, 36 WAKE FOREST L. REV. 889, 889 (2001) (“For over three decades, courts and commentators have struggled to resolve the vexing dilemma of punitive damages in the context of mass tort: how to avoid duplicative punishment of defendants and foster equitable distribution of the punitive bounty among all injured persons.”); Catherine M. Sharkey, *Punitive Damages as Societal Damages*, 113 YALE L.J. 347, 432 (2003) (“The multiple punishments problem has confounded jurists and scholars for the better part of the past three decades.”).

2. See, e.g., *In re Simon II Litig.*, 211 F.R.D. 86 (E.D.N.Y. 2002) (addressing classwide punitive damages in a nationwide tobacco class action), *vacated*, 407 F.3d 125 (2d Cir. 2005). Numerous class actions have been filed against British Petroleum in response to the Gulf of Mexico oil spill. See Tresa Baldas, *Class Action Seeks to Unite Angry BP Investors Around the World*, NAT’L L.J., June 10, 2010, <http://www.law.com/jsp/nlj/PubArticleNLJ.jsp?id=1202462595756&slreturn=1&hbxlogin-1>.

resulting in what Judge Henry Friendly famously described as punitive-damages “overkill.”<sup>3</sup>

Multiple punishment is a problem not just for defendants, but for plaintiffs as well. A defendant’s obligation to pay punitive damages may be constrained by principles of substantive due process or by his own assets.<sup>4</sup> If earlier-suing plaintiffs collect all of the punitive damages that the defendant is required to pay, later-suing plaintiffs will be left with no punitive damages at all.

In response, numerous commentators, judges, and practitioners have proposed that the best solution to the multiple-punishment problem is to join all injured victims into a single class action proceeding that would determine the defendant’s total punitive-damages liability and equitably distribute those damages among all plaintiffs.<sup>5</sup> Unlike most damages class actions, however, in which class plaintiffs have a

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3. *Roginsky v. Richardson-Merrell, Inc.*, 378 F.2d 832, 839 (2d Cir. 1967); *see also In re “Agent Orange” Prod. Liab. Litig.*, 100 F.R.D. 718, 728 (E.D.N.Y. 1983) (“There must, therefore, be some limit, either as a matter of policy or as a matter of due process, to the amount of times defendants may be punished for a single transaction.”), *mandamus denied sub nom. In re Diamond Shamrock Chems. Co.*, 725 F.2d 858 (2d Cir. 1984); Laura J. Hines, *Due Process Limitations on Punitive Damages: Why State Farm Won’t be the Last Word*, 37 AKRON L. REV. 779, 809 (2004) (“Yet if courts impose significant punitive damages awards in every case brought by a plaintiff affected by the misconduct, the aggregate punitive damages liability may far exceed legitimate state interests in punishment and deterrence.”).

4. The Supreme Court has held that the Due Process Clause limits the range of permissible punitive-damages awards. *See, e.g., BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 574 (1996) (holding that “grossly excessive” punitive-damages awards violate due process); Rachel M. Janutis, *Fair Apportionment of Multiple Punitive Damages*, 75 MISS. L.J. 367, 368 (2006) (arguing that the Supreme Court’s punitive-damages decisions “seem to impose limitations on multiple punitive damages”); Victor E. Schwartz, Mark A. Behrens & Joseph P. Mastro Simone, *Reining in Punitive Damages “Run Wild”: Proposals for Reform by Courts and Legislatures*, 65 BROOK. L. REV. 1003, 1031–32 (1999) (noting that both judges and commentators “have expressed strong concerns that multiple punitive damages awards may violate constitutionally protected due process rights.”).

5. *See, e.g.,* Elizabeth J. Cabraser & Thomas M. Sobol, *Equity for the Victims, Equity for the Transgressor: The Classwide Treatment of Punitive Damages Claims*, 74 TUL. L. REV. 2005 (2000) (arguing in favor of using mandatory classes to address multiple punitive-damages claims); Howard A. Denemark, *Seeking Greater Fairness When Awarding Multiple Plaintiff’s Punitive Damages for a Single Act by a Defendant*, 63 OHIO ST. L.J. 931, 967 (2002) (“The [multiple punishment] problem simply disappears if all plaintiffs are joined into one class action.”); Richard A. Seltzer, *Punitive Damages in Mass Tort Litigation: Addressing the Problems of Fairness, Efficiency and Control*, 52 FORDHAM L. REV. 37, 83 (1983); Joan Steinman, *Managing Punitive Damages: A Role for Mandatory “Limited Generosity” Classes and Anti-Suit Injunctions?*, 36 WAKE FOREST L. REV. 1043, 1109 (2001) (acknowledging the procedural difficulties of putting all plaintiffs together in a single class but concluding that the benefits “seem to far outweigh the drawbacks”); *see also infra* note 116 and accompanying text.

protected right to opt out and pursue their own litigation if they so choose, punitive-damages class actions prohibit plaintiffs from opting out.<sup>6</sup> Supporters of the class action solution justify this restriction on the ground that if plaintiffs were permitted to opt out, the risk would remain that first-to-judgment plaintiffs would exhaust the available fund for punitive damages and leave other plaintiffs with nothing.<sup>7</sup>

In light of this tension between the right to opt out and the interest in treating plaintiffs equitably, supporters of punitive-damages class actions have latched onto Federal Rule of Civil Procedure 23(b)(1)(B)—which authorizes certification of a mandatory, non-opt-out class where the defendant has a “limited fund” from which to pay a judgment—as a way of resolving multiple punitive-damages claims in a single proceeding.<sup>8</sup> For these proponents, the limited-fund class provides the best of both worlds. It allows imposition of adequate, but not excessive, punishment on defendants and also ensures that every injured plaintiff obtains a share of the available punitive-damages pie by prohibiting plaintiffs from opting out and racing to the courthouse. Thus, virtually all commentators considering the issue have endorsed the idea of non-opt-out punitive-damages classes, also known as “limited punishment” classes, in some form.<sup>9</sup>

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6. See *infra* note 119 and accompanying text.

7. See, e.g., George Rutherglen, *Better Late Than Never: Notice and Opt Out at the Settlement Stage of Class Actions*, 71 N.Y.U. L. REV. 258, 272 (1996) (noting that allowing class members to opt out of mandatory classes would defeat their purpose); Seltzer, *supra* note 5, at 83.

8. Rule 23(b)(1)(B) permits class certification where “prosecuting separate actions by or against individual class members would create a risk of . . . adjudications with respect to individual class members that, as a practical matter, would be dispositive of the interests of the other members not parties to the individual adjudications or would substantially impair or impede their ability to protect their interests.” Courts have interpreted this rule to incorporate the limited-fund concept. See, e.g., *Ortiz v. Fibreboard Corp.*, 527 U.S. 815 (1999). Certifications under Rule 23(b)(1)(B) need not be accompanied by a right to opt out. See FED. R. CIV. P. 23(c)(2).

9. See, e.g., Jim Gash, *Solving the Multiple Punishments Problem: A Call for a National Punitive Damages Registry*, 99 NW. U. L. REV. 1613, 1640 (2005) (“A number of prominent legal organizations and commentators have argued that the best solution to the multiple punitive damages problem is to utilize class action lawsuits.”); Hines, *supra* note 1, at 899 (stating that the class action “has emerged as perhaps the most popular solution to the mass tort punitive damages dilemma”); see also *In re The Exxon Valdez*, 229 F.3d 790, 795–96 (9th Cir. 2000) (“Mandatory class actions avoid the unfairness that results when a few plaintiffs—those who win the race to the courthouse—bankrupt a defendant early in the litigation process. They also avoid the possible unfairness of punishing a defendant over and over again for the same tortious conduct. As a result, mandatory classes have been endorsed by many courts and commentators.”). See *infra* note 116–17 and accompanying text. But see Richard A. Nagareda, *Punitive Damage Class Actions and the Baseline of Tort*, 36 WAKE FOREST

To the contrary, and despite the scholarly and judicial support for using non-opt-out limited-punishment classes, such classes neither adequately protect a plaintiff's ability to recover punitive damages nor appropriately punish defendants. As this Article explains, instead of protecting class members, as Rule 23(b)(1)(B) is designed to do, mandatory classes actually harm plaintiffs by stripping them of their right to opt out and leaving them with a collectively lower punitive-damages recovery than they might obtain through individual litigation. Additionally, rather than requiring defendants to pay an appropriate level of punitive damages for their wrongful acts, mandatory classes allow defendants to artificially cap their punitive-damages liability at the expense of class members, thwarting the deterrence and punishment goals of punitive damages.

The misuse of mandatory punitive-damages classes has significant implications for ensuring that defendants who commit wrongdoing are appropriately punished and that the victims of their misconduct receive what they deserve. Because the limited-punishment theory applies to any case for punitive damages involving multiple victims, the reach of Rule 23(b)(1)(B) is "virtually limitless."<sup>10</sup> In recent years, class counsel and defendants have pushed for mandatory certification of punitive-damages claims under the theory that the Due Process Clause places a finite limit on the total punitive damages that a defendant can be ordered to pay, and courts have been increasingly willing to certify mandatory limited-punishment classes under Rule 23(b)(1)(B).<sup>11</sup> Moreover, as recent events involving the Gulf oil spill demonstrate, litigation involving multiple claims for punitive damages will only become more common as mass practices affect a wider and wider range of individuals.<sup>12</sup> Consequently, the use of mandatory classes to address

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L. REV. 943 (2001) (arguing that collecting all claimants together for a single punitive-damages proceeding is inconsistent with the decentralized tort system).

10. Gash, *supra* note 9, at 1624; *see* Seltzer, *supra* note 5, at 83 ("All mass tort cases with multiple claims for punitive damages present a potential Rule 23(b)(1)(B) limited fund situation . . ."); *see also* Brief of Amicus Curiae, Trial Lawyers for Public Justice, P.C., in Support of the Objectors to the Proposed Settlement at 1, *In re Cincinnati Radiation Litig.*, 874 F. Supp. 796 (S.D. Ohio Jan. 20, 1988) (No. C-1-94-126) (describing the use of non-opt-out punitive-damages classes as a "rapidly spreading practice").

11. *See infra* notes 116–20 and accompanying text.

12. *See, e.g.*, Elizabeth J. Cabraser, *Unfinished Business: Reaching the Due Process Limits of Punitive Damages in Tobacco Litigation Through Unitary Classwide Adjudication*, 36 WAKE FOREST L. REV. 979, 983 (2001) (describing the risk of mass injury from a defendant's misconduct as an "inevitably recurring" issue); Semra Mesulam, Note, *Collective Rewards and Limited Punishment: Solving the Punitive Damages Dilemma with Class*, 104 COLUM. L. REV. 1114, 1118 (2004) (stating that as corporations expand their power and reach, the issue of multiple punitive-damages awards is "becoming ever more pressing"); *see also In re Joint E. & S. Dist. Asbestos*

the multiple-punishment problem is one of the most pressing concerns regarding punitive-damages law today and sits “at the cutting edge of class action practice.”<sup>13</sup>

This Article identifies two main reasons why mandatory limited-punishment punitive-damages classes undermine the purposes they purport to fulfill and should not be used. First, the Supreme Court’s evolving jurisprudence on the due process limits on punitive damages, rather than justifying a mandatory punitive-damages class under Rule 23(b)(1)(B), actually shows that a mandatory class is inappropriate. The Supreme Court has held that, as a matter of due process, an individual plaintiff can collect punitive damages only with respect to a defendant’s misconduct as to that plaintiff rather than a defendant’s misconduct toward the class as a whole.<sup>14</sup> Under that reasoning, each plaintiff’s punitive-damages entitlement is unique to that plaintiff and is separate and distinct from the punitive-damages entitlement of any other plaintiff. Consequently, allowing a plaintiff to opt out and pursue his or her own individual claim creates no risk of causing duplicative punishment or of encroaching upon the punitive damages available to any other plaintiff.

Second, although many of the arguments in favor of mandatory classes assume a class action that is being litigated to judgment, in reality most class actions settle.<sup>15</sup> Limited-punishment classes are particularly inappropriate in the settlement context because a settlement negotiated and agreed to by the defendant does not constitute punitive damages in any meaningful sense. Punitive damages are supposed to constitute a state-imposed penalty that punishes the defendant for its misbehavior and deters future misconduct. Allowing a defendant to bypass a jury and set its own punitive-damages liability by private agreement and without admitting any wrongdoing, however, does not represent true punishment, let alone state-sponsored punishment. Additionally, settlement opens the door for the parties to manipulate the allocation of punitive damages to serve their own purposes rather than

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*Litig.*, 129 B.R. 710, 803 (E. & S.D.N.Y. 1991) (“Litigation arising from large-scale disasters is an inevitable consequence of the mass character of contemporary society and the complexity of ever-advancing technology.”).

13. Michael P. Allen, *The Supreme Court, Punitive Damages and State Sovereignty*, 13 GEO. MASON L. REV. 1, 64 n.289 (2004); see Thomas B. Colby, *Beyond the Multiple Punishment Problem: Punitive Damages as Punishment for Individual, Private Wrongs*, 87 MINN. L. REV. 583, 587 (2003) (stating that the multiple-punitive-damages issue has become “the single most discussed and debated issue in the law of punitive damages (and indeed one of the most hotly contested issues in all of tort law)”).

14. See *infra* Part II.A.

15. See *infra* note 144 and accompanying text.

to impose an appropriate level of punishment. As a result, instead of ensuring a fair distribution of the available pool of punitive damages, a non-opt-out settlement for punitive damages simply reduces the total size of that pool, threatening to leave plaintiffs worse off than if no settlement had been reached.

If mandatory punitive-damages settlement classes are a bad idea, then why do the parties use them? Although such settlements may be detrimental for individual class members, they are a huge boon for defendants and class counsel. They allow defendants to resolve all punitive-damages claims in a single action and avoid the uncertainty of facing multiple lawsuits brought by opting-out parties.<sup>16</sup> Class counsel prefers mandatory classes because they maximize the size of the class and therefore maximize the potential fee award, while at the same time shutting any competing counsel out of the case.<sup>17</sup> In short, with a mandatory punitive-damages class, class counsel and defendants win, and individual class members lose. While many class lawyers achieve significant justice for their clients, ably carry out their fiduciary responsibilities, and play a crucial role on curbing abusive corporate practices,<sup>18</sup> the use of mandatory classes presents a particular risk of an inadequate settlement, especially since class members cannot exclude themselves if they think the settlement is unfair.

This Article explains in five parts why mandatory classes should not be used to resolve claims for punitive damages. Parts I and II provide essential background on the two distinct doctrinal threads underlying non-opt-out punitive-damages classes: class action doctrine and punitive-damages doctrine. Part I discusses class action principles surrounding the right to opt out and the use of limited-fund mandatory classes under Rule 23(b)(1)(B). Part II explores the Supreme Court's punitive-damages jurisprudence and explains how it has revitalized calls for using limited-punishment classes under Rule 23(b)(1)(B) to address the multiple punitive-damages issue. Part III examines why the Supreme Court's decisions addressing the due process limits to punitive

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16. See *infra* notes 68–69 and accompanying text.

17. See *infra* notes 70–72 and accompanying text.

18. See, e.g., Brian Wolfman & Alan B. Morrison, *Representing the Unrepresented in Class Actions Seeking Monetary Relief*, 71 N.Y.U. L. REV. 439, 441 (1996) (emphasizing that “[c]lass actions are important and useful, both to deter wrongful conduct and to provide compensation for injured plaintiffs,” while cautioning that circumstances can arise where class counsel will settle a case in a manner that does not effectively protect absent class members); Leslie Brueckner & Arthur Bryant, *Fighting Class Action Abuse*, PUBLIC JUSTICE, <http://www.publicjustice.net/Key-Issues-Cases/Access-To-Justice/Class-Action-Preservation/class-action-preservation.aspx> (last visited June 29, 2010) (arguing that class actions play an indispensable role in halting corporate misconduct while noting that parties can abuse the class action process by restricting a party's right to opt out).

damages do not support certification of limited-punishment classes. Part IV addresses why class action settlements present unique difficulties for approving mandatory punitive-damages classes and suggests that such classes are never appropriate in the settlement context. Part V addresses objections to the critique of limited-punishment classes and explores the implications of refusing to allow them.

In challenging the conventional wisdom supporting mandatory punitive-damages classes, this Article does not contend that class actions should never be used to address punitive-damages claims. Rather, it argues that if they are used, class members must be given the right to opt out. Allowing class members to opt out maximizes plaintiff autonomy, increases the chances of fairer settlements, and helps ensure that defendants are held fully accountable for their misconduct.

#### I. THE RIGHT TO OPT OUT: A BENEFIT FOR CLASS MEMBERS BUT A NUISANCE FOR CLASS COUNSEL AND DEFENDANTS

Opt-out rights play a central role in class action jurisprudence. The ability to opt out is a valuable tool for plaintiffs because it gives them the power to pursue their own case if they do not like the way the class action is proceeding.<sup>19</sup> When that right is taken away by certification of a mandatory class, class members have much less control over their individual claims because they will be bound by the result in the class action whether they like it or not. In contrast to plaintiffs, for whom opt-out rights hold significant value, defendants and class counsel do not like opt-out rights and are constantly searching for ways to certify non-opt-out classes. That desire to restrict opt-out rights has driven the push to use limited-punishment classes to address punitive-damages claims. This Part discusses the legal and practical justifications for opt-out rights, how the right to opt out is placed at risk by class counsel's and defendants' desires for mandatory classes, and the doctrinal framework for certifying mandatory classes under the limited-fund theory of Rule 23(b)(1)(B).

##### *A. The Risks of Representative Litigation*

In single-party litigation, the plaintiff gets to decide whether or not to bring a case and gets to make major decisions regarding the course

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19. It also is possible to have a defendant class rather than a plaintiff class. See ALBA CONTE & HERBERT B NEWBERG, 1 NEWBERG ON CLASS ACTIONS §3:2, at 215–17 (4th ed. 2002). Because plaintiff classes are much more common than defendant classes, see *id.*, for ease of reference, this Article refers to the opt-out right as a plaintiff's right.

of the litigation. Ordinarily, an individual who does not bring suit in court or who is not made a party to a lawsuit by service of process is not bound by any judgment in that suit.<sup>20</sup> That fundamental notion of litigant autonomy does not operate in the same way in a class action. A class action binds all members of the class to the result—whether or not they have affirmatively consented to be part of the litigation—as long as their interests are adequately represented by the named plaintiffs and class counsel. In exchange for sacrificing some level of autonomy, class members receive the benefits of collective action. Specifically, class actions can vindicate victims’ rights in situations where the amounts at stake are too small to support individual action, create economies of scale by having common claims aggregated into a single action rather than a multiplicity of individual actions, and enable injured plaintiffs to purchase “higher quality” legal services.<sup>21</sup>

At the same time, as many scholars have documented, the representative nature of class litigation creates a risk of inadequate representation. Unlike an individual case, where there is a general alignment of interest between attorney and plaintiff, class counsel may have an incentive to collude with defense counsel to maximize their own interests at the expense of the class.<sup>22</sup> This collusion can play out in several ways. First, whether or not class members have an interest in settlement, the dynamics of class action litigation push both class counsel and defendants toward settling early in the litigation process. For class counsel who may be working on a contingency-fee basis, the expense of complex litigation is a high-risk proposition, which may make class counsel desire the certainty of settlement.<sup>23</sup> Defendants prefer early settlement so that they can minimize their legal expenses

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20. *Hansberry v. Lee*, 311 U.S. 32, 40 (1940) (“It is a principle of general application in Anglo-American jurisprudence that one is not bound by a judgment *in personam* in a litigation in which he is not designated as a party or to which he has not been made a party by service of process.”).

21. See, e.g., Christopher R. Leslie, *The Significance of Silence: Collective Action Problems and Class Action Settlements*, 59 FLA. L. REV. 71, 76 (2007) (quoting Charles Silver, “We’re Scared to Death”: *Class Certification and Blackmail*, 78 N.Y.U. L. REV. 1357, 1419 (2003)).

22. See, e.g., DEBORAH R. HENSLER ET AL., *CLASS ACTION DILEMMAS: PURSUING PUBLIC GOALS FOR PRIVATE GAINS* (2000); John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 COLUM. L. REV. 1343, 1370–73 (1995); Samuel Issacharoff, *Governance and Legitimacy in the Law of Class Actions*, 1999 SUP. CT. REV. 337, 388; Susan P. Koniak & George M. Cohen, *Under Cloak of Settlement*, 82 VA. L. REV. 1051 (1996); Leslie, *supra* note 21, at 83; John Leubsdorf, *Co-Opting the Class Action*, 80 CORNELL L. REV. 1222 (1995).

23. See HENSLER ET AL., *supra* note 22, at 79; Leslie, *supra* note 21, at 78 (“When working on a contingent fee basis, class counsel often have a strong preference for settling class action litigation instead of going to trial.”).

and litigation costs.<sup>24</sup> Where settlement occurs at an early stage, with less investigation into what the claims may be worth and less evidence gleaned from discovery, class counsel has less bargaining power to obtain an optimum settlement for its clients.<sup>25</sup>

Second, courts and scholars have identified the risk that class counsel may try to keep more of the settlement as attorneys' fees and leave less for the members of the class.<sup>26</sup> Generally, settling defendants are concerned only with their total liability and are indifferent as to how the money they pay out in settlement is distributed between class counsel and the class.<sup>27</sup> Consequently, class counsel may "urge a class settlement at a low figure or on a less-than-optimal basis in exchange for red-carpet treatment on fees."<sup>28</sup>

A third avenue for collusion arises from what are known as settlement-only classes. A settlement-only action is one in which potential class counsel and the defendant reach an agreement to settle claims on a class-wide basis before any class has been certified, and sometimes before a complaint has even been filed.<sup>29</sup> Once the two sides decide to settle, they file a class certification motion and motion for approval of the class settlement simultaneously.<sup>30</sup> From class counsel's perspective, a big advantage of the settlement-only action is that class certification is easier and settlement approval is more likely because the class is being certified purely for settlement and not for trial.<sup>31</sup> Specifically, a court can certify a settlement-only class even if the action presented manageability problems that would prevent the class from being certified for trial.<sup>32</sup>

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24. See, e.g., Leslie, *supra* note 21, at 79 (describing a defendant's incentive to settle "early and cheaply").

25. See, e.g., *In re Community Bank of N. Va.*, 418 F.3d 277, 307 (3d Cir. 2005) (finding it "questionable whether class counsel could have negotiated in [the class's] best interests" where class counsel admitted that it had conducted no formal discovery in the action); Leslie, *supra* note 21, at 79.

26. See, e.g., Coffee, *supra* note 22, at 1376; Leslie, *supra* note 21, at 79–81.

27. See, e.g., Leslie, *supra* note 21, at 79–80.

28. *Weinberger v. Great N. Nekoosa Corp.*, 925 F.2d 518, 524 (1st Cir. 1991).

29. *In re Gen. Motors Corp. Pick-Up Truck Fuel Tank Prods. Liab. Litig.*, 55 F.3d 768, 778 (3d Cir. 1995) (describing settlement classes); Coffee, *supra* note 22, at 1378.

30. See *In re Gen. Motors*, 55 F.3d at 778.

31. See, e.g., Alexandra D. Lahav, *The Law and Large Numbers: Preserving Adjudication in Complex Litigation*, 59 FLA. L. REV. 383, 419 (2007) ("Because manageability standards with regard to settlement-only classes need not be the same as those applied to a litigated class action, it is considerably easier to obtain certification for an existing settlement than for a litigation class action.").

32. See *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 620 (1997) (holding that while settlement classes must satisfy Rule 23, "a district court need not inquire

But the fact that settlement-only classes can be approved even if they can never be litigated is exactly what creates incentives for collusion. With a settlement-only class, any potential class counsel loses much of its bargaining leverage with the defendants.<sup>33</sup> Class counsel can no longer threaten to litigate if the settlement negotiations fall through.<sup>34</sup> If the settlement collapses, the case disappears. A potential class counsel trying to generate a settlement-only agreement also knows that the defendant can try to reach a settlement with another attorney if negotiations falter. Thus, counsel has every incentive to reach an agreement with the defendant lest counsel lose out to a competitor or find that the case is not triable. This creates a risk of a “reverse auction” in which the attorney who agrees to the most defendant-friendly settlement terms will be the one who becomes class counsel in a settlement-only class action.<sup>35</sup>

### *B. The Value of the Right to Opt Out*

Providing a right to opt out of a class action helps address these concerns about autonomy and collusion. Federal Rule of Civil Procedure 23 provides that for class actions certified under Rule 23(b)(3), the portion of the rule most commonly used to certify class actions for significant money damages, class members must be given the opportunity to opt out if they so desire.<sup>36</sup> Rule 23(b)(1)(B) provides a narrow exception to the right to opt out of damages actions where there is a limited fund, on the rationale that allowing opt outs would lead to exhaustion of the fund and defeat the purpose of the limited-fund class.<sup>37</sup>

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whether the case, if tried, would present intractable management problems, for the proposal is that there be no trial” (internal citation omitted).

33. Coffee, *supra* note 22, at 1378–79; Samuel Issacharoff, *Class Action Conflicts*, 30 U.C. DAVIS L. REV. 805, 812–13 (1997).

34. Coffee, *supra* note 22, at 1379.

35. See *Reynolds v. Beneficial Nat'l Bank*, 288 F.3d 277, 282 (7th Cir. 2002) (defining reverse auction as “the practice whereby the defendant in a series of class actions picks the most ineffectual class lawyers to negotiate a settlement with in the hope that the district court will approve a weak settlement that will preclude other claims against the defendant”); Coffee, *supra* note 22, at 1379 (noting how settlement-only classes are a “no lose” proposition for defendants and how class counsel has little bargaining leverage).

36. Rule 23(c)(2)(B)(v) states that for (b)(3) classes, the parties must notify the class that, among other things, “the court will exclude from the class any member who requests exclusion.”

37. Class actions that are predominantly for injunctive relief fall within Rule 23(b)(2) and do not require an opt out right because injunctive relief benefits all affected parties whether or not they are in the class. See FED. R. CIV. P. 23(b)(2).

The primary justifications for allowing plaintiffs to opt out of class actions reflect both the constitutional concern about preserving plaintiff control and the practical concern about preventing collusive settlements. Regarding the former, opt-out rights can restore a degree of plaintiff autonomy that is lost through the collective process.<sup>38</sup> In this way, opt-out rights keep class actions consistent with what the Supreme Court has described as the “deep-rooted historic tradition that everyone should have his own day in court.”<sup>39</sup> Opt-out rights also ensure that class members do not have their rights decided against their will. It is one thing to say that individuals who do not affirmatively consent, or opt in, can be bound by a class action. It is quite another to say that individuals should be bound even where they actively oppose being included in the class and would prefer to pursue their own lawsuit. The opt-out right reflects the fact that a plaintiff has a protected property interest in his or her cause of action and should be able to control how that property is utilized.<sup>40</sup>

Indeed, there is a strong argument that the interest in plaintiff autonomy creates a constitutional basis for the opt-out right, at least with respect to class actions predominantly for money damages (including punitive damages).<sup>41</sup> In *Phillips Petroleum Co. v. Shutts*,<sup>42</sup> the Supreme Court held that “due process requires at a minimum that an absent plaintiff be provided with an opportunity to remove himself

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38. See, e.g., Richard A. Epstein, *Class Actions: Aggregation, Amplification, and Distortion*, 2003 U. CHI. LEGAL F. 475, 510 (“[A]ll options have some positive value, and the control of one’s own litigation cannot be regarded as a small detail within the overall scheme of civil procedure.”); John E. Kennedy, *Class Actions: The Right to Opt Out*, 25 ARIZ. L. REV. 3, 79 (1983); Michael A. Perino, *Class Action Chaos? The Theory of the Core and an Analysis of Opt-Out Rights in Mass Tort Class Actions*, 46 EMORY L.J. 85, 106 (1997) (describing how opt-out rights help preserve client autonomy and control); Peter H. Schuck, *Mass Torts: An Institutional Evolutionist Perspective*, 80 CORNELL L. REV. 941, 964 (1995) (stating that opt-out rights “institutionalize and enlarge the central value of client autonomy”).

39. *Martin v. Wilks*, 490 U.S. 755, 762 (1989) (quoting the first edition of CHARLES ALAN WRIGHT, ARTHUR R. MILLER & EDWARD H. COOPER, 18A FEDERAL PRACTICE AND PROCEDURE § 4449, at 346–47 (2d ed. 2002)).

40. See *Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 428 (1982) (“[A] cause of action is a species of property protected by the Fourteenth Amendment’s Due Process Clause.” (discussing *Mullane v. Cent. Hanover Bank & Trust Co.*, 339 U.S. 306, 313–16 (1950))).

41. Although one could argue that in referring to money damages, the court really meant compensatory damages, most courts have treated punitive damages similarly to compensatory damages for class certification purposes. Most courts have required class actions seeking punitive damages to be certified under Rule 23(b)(3), on the ground that actions seeking punitive damages are money damages and cannot be considered an “incidental” form of relief. See, e.g., *Allison v. Citgo Petroleum Corp.*, 151 F.3d 402, 417–18 (5th Cir. 1998).

42. 472 U.S. 797 (1985).

from the class by executing and returning an ‘opt out’ or ‘request for exclusion’ form to the court.”<sup>43</sup> Although the Court’s statement concerned whether a state court could exercise personal jurisdiction over class members who did not have minimum contacts with the forum state as long as they received notice of the class action and an opportunity to exclude themselves, the Court’s reasoning, along with similar statements it has made in later cases, strongly suggests that *Shutts* establishes a constitutional due process right to opt out of class actions that are predominantly for money damages.<sup>44</sup>

A second justification for the right to opt out is that it can reduce the risk of collusive or unfair settlements.<sup>45</sup> High opt-out rates may indicate that many class members believe that they can get better results through individual litigation. Opting out also signals to the judge evaluating the proposed settlement that perhaps the settlement is inadequate and should not be approved.<sup>46</sup> In this way, the right to opt out can function as a “market check” against the agency problems arising from class members’ inability to effectively monitor class counsel and ensure that class counsel adequately represents their interests.<sup>47</sup> Opting out therefore can induce the settling parties to make the settlement more beneficial to the class or can lead to judicial rejection of the settlement if they fail to do so. Although in most class actions the opt-out right is rarely exercised because the class members’ individual stakes may be too small to support an individual action,<sup>48</sup> where class members have higher-value claims, such as claims involving punitive damages, the incentives to opt out are much

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43. *Id.* at 812.

44. *See, e.g.*, Brian Wolfman & Alan B. Morrison, *What the Shutts Opt-Out Right Is and What It Ought to Be*, 74 UMKC L. REV. 729, 733–34 (2006) (arguing that the right to opt out is grounded in due process). When the Supreme Court did address the issue of mandatory classes—and (b)(1)(B) classes in particular—more directly, it reiterated that there were “serious constitutional concerns” with resolving a class action for money damages on a mandatory basis. *See Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 845–47 (1999).

45. *See, e.g.*, Perino, *supra* note 38, at 105; Wolfman & Morrison, *supra* note 44, at 743.

46. *See, e.g.*, Coffee, *supra* note 22, at 1382–83 (“Yet, the existence of substantial opt outs may be the best evidence that the original settlement was inadequate (and possibly collusive).”).

47. *See, e.g.*, Perino, *supra* note 38, at 105 (“Scholars have argued that opt-out rights can serve as a market check on the fairness and adequacy of class action global settlements that may limit the opportunities for class counsel to ‘sell out’ the class for a significant fee award.”).

48. *See, e.g.*, Theodore Eisenberg & Geoffrey Miller, *The Role of Opt-Outs and Objectors in Class Action Litigation: Theoretical and Empirical Issues*, 57 VAND. L. REV. 1529, 1541–42, 1548–49 (2004).

greater.<sup>49</sup> Several class actions involving significant individual damages have seen thousands or even tens of thousands of opt outs.<sup>50</sup>

Although this Article assumes that opt-out rights are valuable for class members with claims for punitive damages, not everyone agrees that opt-out rights serve a useful purpose. Professor David Rosenberg, for example, has argued that opt outs undermine the economies of scale and collective-action benefits that come from class litigation, which can reduce class counsel's bargaining power with the defendant and leave the class as a whole worse off.<sup>51</sup> He proposes making every class action a mandatory class action.<sup>52</sup> Regardless of the merits of Rosenberg's proposal, however, it does not reflect the reality of current class action practice. First, it gives short shrift to the autonomy and due process values that the Supreme Court has relied upon in defining the scope of opt-out rights.<sup>53</sup> Second, it would require dramatic changes to current class action practice, such as awarding class members an average level of damages instead of awarding damages based on each class member's specific harm.<sup>54</sup> It is not clear that courts would have the authority to

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49. See Coffee, *supra* note 22, at 1382 (noting that "high stakes" class members are more likely to exercise opt-out rights); Stephen J. Newman, *Certifying Mandatory Punitive Damages Classes*, [6] Class Action Litig. Rep. (BNA) No. 7, at 255-56 (Apr. 8, 2005) (noting how the usual opt-out calculus is "disrupted" when punitive damages are at stake); Wolfman & Morrison, *supra* note 44, at 731 (arguing that there are many class actions where "opt-out matters").

50. More than 236,000 plaintiffs opted out of the *Amchem* asbestos class action, see Coffee, *supra* note 22, at 1383-84, more than 12,000 plaintiffs opted out of the silicone breast implant class action, see Perino, *supra* note 38, at 150, and approximately 1,200 plaintiffs sought to opt out of the *Tower Loan* consumer fraud class action. See Wolfman & Morrison, *supra* note 44, at 740.

51. See generally David Rosenberg, *Mandatory-Litigation Class Action: The Only Option for Mass Tort Cases*, 115 HARV. L. REV. 831 (2002).

52. See *id.* at 831-32.

53. Rosenberg significantly downplays the importance of plaintiff autonomy, see *id.* at 864 ("The 'autonomy' espoused by the proponents of class action opt-out reflects a narrow, unworldly, and professionally self-serving conception of how individuals might enhance their well-being through self-determination."), even though the Supreme Court has described plaintiff autonomy and the day-in-court ideal as a primary justification for the right to opt out. See *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 846 (1999).

54. See Rosenberg, *supra* note 51, at 854-57. For example, Professor Coffee contends that Rosenberg's view of damages averaging across class members "is the polar opposite of client control," and focuses too much "on the interests of the average plaintiff and ignore[s] differences among the merits of various plaintiffs' claims." John C. Coffee, Jr., *The Regulation of Entrepreneurial Litigation: Balancing Fairness and Efficiency in the Large Scale Class Action*, 54 U. CHI. L. REV. 877, 878 (1987); see also Richard A. Nagareda, *Autonomy, Peace, and Put Options in the Mass Tort Class Action*, 115 HARV. L. REV. 747, 792-94 (2002) (critiquing Rosenberg's proposal for not ensuring fair allocations among class plaintiffs). Others have questioned Rosenberg's view on more philosophical grounds. See Martin H. Redish & Clifford W.

redistribute wealth from plaintiffs with stronger claims to plaintiffs with weaker claims, as Rosenberg's proposal requires. Third, it does not adequately safeguard against the risk of collusive settlements and does not account for the reality that trial judges are unlikely to police class settlements as vigilantly as Rosenberg's proposal demands.<sup>55</sup> Thus, whether or not opt-out rights would be as valuable if courts adopted all of the requirements of Rosenberg's theory, they currently have not. Unless and until courts do, it is important to focus on what is actually occurring in class action practice in determining whether class members should have their right to opt out taken away from them.<sup>56</sup>

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Berlow, *The Class Action as Political Theory*, 85 WASH. U. L. REV. 753, 780-90 (2007).

55. Rosenberg and his colleague Professor Hay acknowledge the risk that class counsel will enter into "sweetheart" settlements with defendants that sell out the interests of unnamed class members. See Bruce Hay & David Rosenberg, *"Sweetheart" and "Blackmail" Settlements in Class Actions: Reality and Remedy*, 75 NOTRE DAME L. REV. 1377, 1390-91 (2000) (describing "sweetheart" settlements). Their solution is not to allow class members to opt out, but to require judges to reject any settlements that would leave class members worse off than if the case went to trial. See *id.* at 1394-401. This proposal, while laudable, may not be fully realistic. It requires either establishing additional procedures, such as allowing some individual cases to go to trial so that the judge overseeing the class action can roughly estimate the value of the class claims, see *id.* at 1396-97, or assuming that judges will have information at their disposal that will allow them to make those estimates. Rosenberg and Hay's general model is the mass tort class action, where "[s]ettlement-only class actions usually culminate [after] years or even decades of separate action litigation of claims." *Id.* at 1400. They propose that courts can appoint experts to develop information and use it to estimate both class size and claim value. See *id.* However, not all class actions are mass tort actions, and many do not culminate after years or decades of individual litigation that provide an easy reference point. See Nagareda, *supra* note 54, at 792-94 (questioning the feasibility of Rosenberg's and Hay's proposal and arguing that some plaintiffs would have to receive an opt-out right in order to bring the individual cases that would set the benchmark for the class recovery). Moreover, even if rigorous investigation would enable a judge to accurately gauge a settlement's fairness, a busy trial judge looking to clear a crowded docket has little incentive to undertake that investigation, especially where both parties have committed to settling the action. See *infra* notes 191-203 and accompanying text. Thus, judges have approved class settlements where the class recovery did not correspond to individual trial outcomes. In *Baker v. Washington Mutual Finance Group, LLC*, 193 F. App'x 294, 298 (5th Cir. 2006), the Fifth Circuit affirmed the district court's approval of a \$7 million settlement for a 45,000 person class even though 23 other plaintiffs had received a jury verdict of almost \$57 million for identical claims.

56. Rosenberg is not the only critic of opt-out rights. Others have argued that an attorney representing individual clients may encourage those clients to opt out so that the attorney can salvage some attorneys' fees by keeping his or her clients from being absorbed into the class action, even if opting out is not in the client's best interest. See Coffee, *supra* note 54, at 925-26. But even if that is true, the attorney must believe that he or she has a decent chance of getting as an effective result in individual litigation as was achieved in the class settlement, or else the attorney likely would not waste time pursuing the case. See Wolfman & Morrison, *supra* note 44, at 744 ("[A] contingent

*C. Rule 23(b)(1)(B)—A Narrow Exception*

Although an opt-out right ordinarily must be provided in class actions for money damages, a narrow exception exists, as codified in Rule 23(b)(1)(B), where allowing potential class members to bring separate actions would prejudice the rights of other class members.<sup>57</sup> A classic example is where the defendant has a “limited fund” from which to pay out potential judgments.<sup>58</sup> In a limited-fund situation, requiring all claimants to stay in the class is considered acceptable in order to ensure that all class members are treated equitably. Thus, class plaintiffs, rather than defendants, are the intended beneficiaries of Rule 23(b)(1)(B).<sup>59</sup>

As an example, suppose that a defendant has \$100 in assets and that twenty individuals each have a \$10 claim against that defendant. In an opt-out class action, ten plaintiffs could opt out and get their full \$10 recovery. In doing so, however, they would exhaust the fund and leave the other ten plaintiffs with nothing. Thus, Rule 23(b)(1)(B) permits joining all twenty plaintiffs—whether they like it or not—into a mandatory class and giving \$5 to each one. Each plaintiff receives “something less than a full recovery” so that every plaintiff can receive something.<sup>60</sup>

In *Ortiz v. Fibreboard Corp.*,<sup>61</sup> the Supreme Court addressed Rule 23(b)(1)(B) and clarified that non-opt-out limited-fund classes must

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fee plaintiff’s lawyer presumably would have had better things to do than represent opt-out clients, unless those clients stood a chance of obtaining considerably more than the small amounts being offered in the class action settlement.”). Professor Perino, using a game theory analysis, concludes that in some scenarios, allowing individuals with strong claims to opt out could cause the settlement to unravel entirely by disrupting the equilibrium favoring settlement. Perino, *supra* note 38, at 119–31. As explained later, certain assumptions underlying Perino’s analysis do not apply to limited-punishment classes. *See infra* note 124.

57. Rule 23(b)(1)(B) states that certification may be appropriate where separate actions would create a risk of “adjudications with respect to individual class members that, as a practical matter, would be dispositive of the interests of other members not parties to the individual adjudications or would substantially impair or impede their ability to protect their interests.” FED. R. CIV. P. 23(b)(1)(B).

58. *See Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 834 (1999) (describing the history of the limited-fund class action).

59. *See* Issacharoff, *supra* note 33, at 821; Mesulam, *supra* note 12, at 1139 (listing “distributive justice, equity, and fairness” as justifications for mandatory limited-punishment classes); Steinman, *supra* note 5, at 1048 (noting that (b)(1)(B) classes ostensibly are certified “for the benefit of the class members and to ensure equitable distribution of the monies that the law permits to be recovered”).

60. Perino, *supra* note 38, at 99 (describing the rationale for a (b)(1)(B) class).

61. 527 U.S. 815 (1999).

meet strict requirements. The Court established three “presumptively necessary” criteria for certification of a limited-fund class.<sup>62</sup> First, the fund must have a fixed limit that is inadequate to satisfy all claims against it.<sup>63</sup> Second, the entire fund must be devoted to paying the injured victims, because otherwise the class as a whole will not get as good a deal as it could through separate individual actions.<sup>64</sup> Third, the class must include everyone with a claim against the fund because if some individuals are not included and can still pursue individual litigation, the risk remains that those individuals will exhaust the fund and leave others with nothing.<sup>65</sup>

Although some commentators pronounced that the Supreme Court’s strict reading of Rule 23(b)(1)(B) heralded the end of limited-fund classes,<sup>66</sup> litigants have continued to push for mandatory classes, and courts have shown themselves willing to approve them.<sup>67</sup> Litigants have done so because although opt-out rights may be good for class members, they are a thorn in the side of both defendants and class counsel. All things being equal, both defendants and class counsel prefer a non-opt-out class, especially a non-opt-out settlement class. A defendant’s goal in resolving a class action is to achieve closure, and it can only achieve such finality, or global peace, if everyone’s claim is resolved.<sup>68</sup> Mandatory classes are even more desirable for defendants in the settlement context. Defendants not only get global peace, but they get it for a price to which they voluntarily agree rather than one determined by the whims of a jury.<sup>69</sup>

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62. *Id.* at 838–39, 842.

63. *Id.* at 838–39.

64. *Id.* at 839.

65. *Id.* at 839–40.

66. *See, e.g.,* Colby, *supra* note 13, at 664–65.

67. *See infra* notes 116–19 and accompanying text; *see also* Wolfman & Morrison, *supra* note 44, at 746 (explaining that lower courts have continued to certify mandatory classes after *Ortiz*).

68. *See, e.g.,* Coffee, *supra* note 22, at 1382; Linda S. Mullenix, *No Exit: Mandatory Class Actions in the New Millennium and the Blurring of Categorical Imperatives*, 2003 U. CHI. LEGAL F. 177, 240 (“As is well known, what defendants seek most from class action litigation is closure, or ‘global peace.’”).

69. *See* Wolfman & Morrison, *supra* note 44, at 731 & n.18 (“[D]efendants want to cut off opt-out rights through a mandatory settlement, which, if approved by the court, fixes the price of an all-purpose ‘cram down’ at the figure agreed to by plaintiffs’ counsel.”). When defendants oppose certification of a mandatory class, it often is not because they oppose the mandatory nature of the class, but because they want to stop any class from being certified at all. Mandatory classes, which can be certified under Rule 23(b)(1) or (b)(2), are considered easier to certify than opt-out classes because they are not subject to the predominance and superiority requirements of Rule 23(b)(3). Thus, if the defendant can stop a class action from being certified on a mandatory basis, it may avoid a class action altogether if the case is one that could

For class counsel, there are several reasons to favor a mandatory class over an opt-out class. A mandatory class maximizes the size of counsel's client base, and therefore maximizes counsel's potential fee recovery.<sup>70</sup> If other attorneys represent hundreds or even thousands of potential class members, those individuals would automatically be absorbed into a mandatory class. Additionally, class counsel can save significant notice costs through mandatory classes. Unlike opt-out classes certified under Rule 23(b)(3), individualized notice is not required for mandatory classes certified under Rule 23(b)(1) or (b)(2).<sup>71</sup> Also appealing for class counsel is the fact that mandatory classes do not need to satisfy the predominance and superiority requirements of Rule 23(b)(3).<sup>72</sup>

Given that class counsel and defendants prefer mandatory classes, particularly at the settlement stage, they have aggressively attempted to "shoehorn" damages class actions that ordinarily would be certified as opt-out classes under Rule 23(b)(3) into one of Rule 23's mandatory class provisions.<sup>73</sup> Several commentators have argued that "the

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not be certified on an opt-out basis under Rule 23(b)(3). This is what appears to have happened in the *Simon II* nationwide tobacco litigation. There, the tobacco industry defendants vigorously opposed certification of a mandatory punitive-damages class and succeeded in convincing the Second Circuit to vacate the district court's mandatory class certification order. *See In re Simon II Litig.*, 407 F.3d 125 (2d Cir. 2005). Once the order was vacated, class counsel did not attempt to certify the class on an opt-out basis but instead voluntarily dismissed the action. *See In re Simon II Litig.*, 233 F.R.D. 123 (E.D.N.Y. 2006). Similarly, in class actions where each class member's claim is too small to support individual litigation, defendants might oppose mandatory class certification because they know there is no risk of facing individual lawsuits if class certification is denied. For most class actions seeking punitive damages, however, the individual claims will be large enough to make individual litigation a realistic possibility.

70. *See, e.g.*, John C. Coffee, Jr., *Class Action Accountability: Reconciling Exit, Voice, and Loyalty in Representative Litigation*, 100 COLUM. L. REV. 370, 420 (2000) (noting that opt outs reduce class size and consequently class counsel's expected fees); Nagareda, *supra* note 9, at 973 (noting that a mandatory class empowers class counsel over other plaintiffs' attorneys and allows them to shut out any potential attorney competitors).

71. *See* Rutherglen, *supra* note 7, at 271 ("Nothing has stimulated certification of (b)(1) and (b)(2) class actions as much as the strict requirements of individual notice in (b)(3) class actions."); Wolfman & Morrison, *supra* note 44, at 738.

72. Under Rule 23(b)(3), which governs opt-out class actions, certification is permitted only if the court finds that common issues predominate over individual issues and that the class action is "superior to other available methods for fairly and efficiently adjudicating the controversy." FED. R. CIV. P. 23(b)(3).

73. *Bolin v. Sears, Roebuck & Co.*, 231 F.3d 970, 976 (5th Cir. 2000) (warning of the risk that class counsel and defendants will seek mandatory classes because class counsel "effectively gathers clients—often thousands of clients" while allowing defendants to "purchase res judicata").

settlement class action is a breeding ground for manipulating mandatory certification,”<sup>74</sup> asserting that parties have engaged in “opportunistic gaming” of the system by strategically seeking mandatory class certification,<sup>75</sup> and by designing class settlements that ostensibly permit an opt-out right, but are structured in a way to penalize those who choose to exercise their right to opt out.<sup>76</sup>

Opt-out rights therefore reflect both constitutional and practical values about the importance of giving individual plaintiffs control over their legal claims. Consequently, the Supreme Court has emphasized that opt-out rights should be circumscribed only in narrow circumstances. Nonetheless, because class counsel and class defendants have a strong desire for mandatory classes, they have found creative ways to try and restrict opt-out rights. Of particular relevance here, they have combined the limited-fund theory of Rule 23(b)(1)(B) with the Supreme Court’s punitive-damages jurisprudence in order to certify mandatory punitive-damages classes, as the next Part discusses.

## II. THE RISE, FALL, AND RESURGENCE OF THE “LIMITED PUNISHMENT” MANDATORY PUNITIVE-DAMAGES CLASS

Soon after judges and scholars became concerned about the problem of multiple, overlapping punitive-damages awards, they started looking to the limited-fund theory of Rule 23(b)(1)(B) as a potential solution. They were receptive to the idea that the Due Process Clause placed some finite limit on the amount of punitive damages a defendant could be forced to pay and on “the amount of times defendants may be punished for a single transaction.”<sup>77</sup> According to this view, if Plaintiff A sues the defendant and receives punitive damages to punish the defendant for its wrongdoing, and then Plaintiff B (who was harmed by the same conduct that harmed Plaintiff A) sues and also receives punitive damages for the defendant’s wrongdoing, the defendant has been subjected to a form of double-counting because it is being punished twice for the same harm.

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74. Wolfman & Morrison, *supra* note 44, at 740.

75. Mullenix, *supra* note 68, at 215.

76. See Richard A. Nagareda, *Closure in Damages Class Settlements: The Godfather Guide to Opt-Out Rights*, 2003 U. CHI. LEGAL F. 141, 142 (arguing that “a pervasive feature of class settlement design consists of efforts, in one way or another, to minimize the number of opt-outs”).

77. *In re “Agent Orange” Prod. Liab. Litig.*, 100 F.R.D. 718, 728 (E.D.N.Y. 1983) (citing C. Delos Putz, Jr. & Peter M. Astiz, *Punitive Damages Claims of Class Members Who Opt Out: Should They Survive?*, 16 U.S.F. L. REV. 1, 18–40 (1981)), *mandamus denied sub nom. In re Diamond Shamrock Chems. Co.*, 725 F.2d 858 (2d Cir. 1984).

Under this scenario, if a defendant's actions harm multiple people, and if each person brings an individual action for punitive damages, there will come a point where the cumulative level of punitive damages paid out by the defendant to individual plaintiffs will satisfy the societal interest in punishment and deterrence. Any future punitive damage awards for later-suing plaintiffs would be constitutionally excessive and disallowed. Consequently, later-suing plaintiffs would be left with no punitive damages because the available fund of punitive damages would have been already exhausted.

Starting in the early 1980s, district courts began certifying punitive-damages classes on a non-opt-out basis under Rule 23(b)(1)(B) in several mass tort cases. These cases involved large numbers of claimants and potentially astronomical total punitive damages, including litigation involving asbestos, Agent Orange, defective drugs and devices, and the collapse of a hotel skywalk in Kansas City.<sup>78</sup>

Notably, although virtually all of these certification decisions were vacated on appeal, they were vacated on fact-specific grounds or for procedural failings that doomed those particular classes.<sup>79</sup> The appellate courts did not reject the limited-punishment theory, and in several decisions applauded the district court's creative efforts and indicated that the limited-punishment theory could support mandatory punitive-damages classes in appropriate situations.<sup>80</sup> Several courts did note,

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78. See *In re Asbestos Sch. Litig.*, 104 F.R.D. 422, 434–38 (E.D. Pa. 1984); *In re "Bendectin" Prods. Liab. Litig.*, 102 F.R.D. 239 (S.D. Ohio 1984); *In re "Agent Orange,"* 100 F.R.D. 718; *In re Fed. Skywalk Cases*, 93 F.R.D. 415, 424–25 (W.D. Mo. 1982); *In re N. Dist. Cal. "Dalkon Shield" IUD Prods. Liab. Litig.*, 526 F. Supp. 887, 896–900 (N.D. Cal. 1981).

79. For example, in *In re School Asbestos Litigation*, the Third Circuit vacated class certification because the class was not defined broadly enough, and because it excluded other claimants who would still have an opportunity to individually litigate and deplete the available fund of punitive damages. 789 F.2d 996, 1005–07 (3d Cir. 1986). In *In re Bendectin Products Liability Litigation*, the Sixth Circuit faulted the district court for failing to give opponents of class certification the opportunity to show that a limited fund did not exist. 749 F.2d 300, 306 (6th Cir. 1984). Similarly, the Ninth Circuit vacated class certification in the *Dalkon Shield* class action because the district court engaged in no factfinding to determine what the defendants' available assets were. See *In re N. Dist. Cal. Dalkon Shield IUD Prods. Liab. Litig.*, 693 F.2d 847, 852 (9th Cir. 1982); see also Thomas M. Sobol & Elizabeth J. Cabraser, *Complex Litigation: Punitive Damages Class II*, NAT'L L.J., Mar. 6, 2000, at A17 (stating that most judicial rejections of mandatory punitive-damages classes "stem[] more from lack of evidentiary presentation than from unrealistic legal barriers").

80. See, e.g., *In re Sch. Asbestos*, 789 F.2d at 1005 (noting that "powerful arguments have been made" regarding the courts' responsibility to prevent multiple punitive-damages awards and assuming that Rule 23(b)(1)(B) could be used to certify a mandatory punitive-damages class); *In re Bendectin Prods.*, 749 F.2d at 307 (finding the district court's decision "commendable" on "pure policy grounds" and noting that several scholars have encouraged the use of Rule 23(b)(1)(B) to address multiple

however, that the fact that the Supreme Court had not set any specific legal constraint on punitive damages made it difficult to establish whether there was a truly limited fund of punitive damages.<sup>81</sup>

A few years later, however, the Supreme Court determined that the Due Process Clause did restrict the amount of punitive damages awardable by a jury,<sup>82</sup> and as the Court increasingly tightened its controls on punitive damages, practitioners and scholars began using the Supreme Court's decisions as a hook for certifying the same type of non-opt-out punitive-damages classes that had previously been rejected. But while the Supreme Court has continued to find that the Due Process Clause limits the size and type of punitive-damages awards and has progressively tightened those constraints, it also has increasingly concentrated on regulating individual punitive-damages awards in individual cases. Over time, the Court's focus has moved progressively toward defining the constraints on punitive damages as ones that limit plaintiffs to collecting punitive damages only for the harm done to those individual plaintiffs and not for the defendant's wrongdoing as a whole or for the injuries it inflicted on other individuals not before the court. This trend has significance for addressing the propriety of mandatory punitive-damages classes.

#### *A. Due Process Limitations on Punitive Damages*

The Supreme Court first held that the Due Process Clause restricts punitive-damages awards in *Pacific Mutual Life Insurance Co. v. Haslip*.<sup>83</sup> The Court did not define any explicit substantive limitation on the amount of punitive damages that can be awarded, but held that due process requires states to place some constraints on the jury's discretion in awarding punitive damages to ensure that the award is appropriately tailored to reflect the state's interests in punishment and deterrence.<sup>84</sup> The Court upheld the punitive-damages verdict in the case, finding that

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punitive-damages awards); *see also In re Fed. Skywalk Cases*, 680 F.2d 1175, 1184-91 (8th Cir. 1982) (Heaney, J., dissenting) (arguing in favor of mandatory punitive-damages classes).

81. *See, e.g., In re Sch. Asbestos*, 789 F.2d at 1007 (noting that state decisions in individual asbestos cases had not established limits on the amount of punitive damages that juries could award); *In re Dalkon Shield Prods.*, 693 F.2d at 852 (“[N]o rule of law limits the amount of punitive damages a jury may award.”).

82. *See Pac. Mut. Life Ins. Co. v. Haslip*, 499 U.S. 1 (1991).

83. *Id.*

84. *Id.* at 18-20 (stating that giving a jury unfettered discretion with respect to punitive damages “may invite extreme results that jar one’s constitutional sensibilities” but also that “[a]s long as the discretion is exercised within reasonable constraints, due process is satisfied”).

the trial court's jury instructions and the state's procedures for judicial review of the jury's award satisfied due process.<sup>85</sup>

Two years later, in *TXO Production Corp. v. Alliance Resources Corp.*,<sup>86</sup> the Court again upheld a state jury's punitive-damages award. In this case, the ratio of punitive to compensatory damages was 526:1 (in *Haslip*, the ratio was 4:1),<sup>87</sup> but the Court found that the award was constitutional because the jury was entitled to consider (a) the potential harm to the plaintiff rather than just the actual harm suffered, (b) the potential harm to future victims of the defendant's scheme if the unlawful conduct were not deterred, and (c) the intentional nature of the defendant's conduct in determining how reprehensibly it behaved.<sup>88</sup> At the same time, however, the Court emphasized that the Due Process Clause "imposes substantive limits 'beyond which penalties may not go,'"<sup>89</sup> and specifically noted that the parties "do not dispute the proposition that the Fourteenth Amendment imposes a substantive limit on the amount of a punitive-damages award."<sup>90</sup>

The Supreme Court first struck down a punitive-damages award as substantively excessive in *BMW of North America, Inc. v. Gore*.<sup>91</sup> In doing so, it began to articulate its view that a plaintiff can recover punitive damages only for the harm suffered by the plaintiff and not for the harm caused by the defendant as a whole.<sup>92</sup> In *Gore*, an Alabama jury awarded Mr. Gore \$4000 in compensatory damages and \$4 million in punitive damages (subsequently reduced to \$2 million by the Alabama courts), for selling him a BMW as new without disclosing that the car had been repainted before the sale.<sup>93</sup> The jury appeared to

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85. *Id.* at 19–21. The Court found that (a) the jury instructions provided by the Alabama trial court informed the jury that punitive damages are designed to punish the defendant and should not be given as compensation, (b) the trial court excluded evidence of the defendant's wealth as required by state law, (c) the state provided for post-verdict review by the trial court and the appellate courts. *Id.*

86. 509 U.S. 443 (1993).

87. *Id.* at 459.

88. *See id.* at 460–62.

89. *Id.* at 453–54 (quoting *Seaboard Air Line Ry. v. Seegers*, 207 U.S. 73, 78 (1907)).

90. *Id.* at 455.

91. 517 U.S. 559 (1996).

92. *See id.* at 568–85. Prior to *Gore*, the Supreme Court struck down a \$5 million punitive-damages award in *Honda Motor Co. v. Oberg*, 512 U.S. 415 (1994), but its decision rested on procedural grounds. It did not find that the \$5 million award was necessarily excessive, but instead found unconstitutional a rule of the Oregon constitution which prohibited judicial review of the amount of a jury's punitive-damages award unless the trial court found that there was no evidence to support the award. *Id.* at 418.

93. 517 U.S. at 562–67.

calculate punitive damages by considering evidence that on a national level, BMW had resold 983 re-painted cars as new as part of its policy, and multiplying that number by the \$4000 in damages.<sup>94</sup> The Court rejected the jury's approach, noting that while BMW's conduct may have been illegal in Alabama, it was not illegal in all fifty states.<sup>95</sup> It then concluded that the Due Process Clause prohibited the jury from awarding punitive damages "to punish BMW for conduct that was lawful where it occurred and that had no impact on Alabama or its residents."<sup>96</sup>

The Court also found that even after the award was reduced to \$2 million, it violated due process because it was "grossly excessive."<sup>97</sup> In reaching its conclusion, the Court established three guideposts for evaluating the legitimacy of a punitive-damages award: (1) the degree of reprehensibility of the defendant's conduct; (2) the ratio of punitive to compensatory damages; and (3) the sanctions permitted—such as civil or criminal penalties—for comparable misconduct.<sup>98</sup> The Court found that all three factors, including the 500:1 ratio of punitive to compensatory damages, which far exceeded the range of typical civil or criminal penalties for BMW's behavior, favored striking down the punitive-damages award.<sup>99</sup> Importantly, by prohibiting the jury from considering BMW's nationwide practices, and by requiring courts to evaluate a punitive-damages award in light of the amount of compensatory damages recovered by the plaintiff, the Court began to tie the limits on punitive-damages awards to the harm directed to the specific plaintiff before the court rather than the harm inflicted by the defendant as a whole.

In *State Farm Mutual Automobile Insurance Co. v. Campbell*,<sup>100</sup> the Court took *Gore* one step further and held not only that a jury cannot award punitive damages to punish a defendant for out-of-state conduct that was lawful where it occurred, but also that a jury cannot punish a defendant for out-of-state conduct at all, even if it were illegal everywhere.<sup>101</sup> In reaching its decision, the Court became more explicit in tying the legitimacy of punitive damages to the wrongdoing inflicted on the plaintiff rather than on society generally. A jury had awarded the

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94. *See id.* at 564–65.

95. *Id.* at 572–74.

96. *Id.* at 572–73.

97. *Id.* at 574.

98. *Id.* at 574–85.

99. *Id.*

100. 538 U.S. 408 (2003).

101. *Id.* at 421 ("Nor, as a general rule, does a State have a legitimate concern in imposing punitive damages to punish a defendant for unlawful acts committed outside of the State's jurisdiction.").

Campbells \$145 million in punitive damages (which the trial court later reduced to \$25 million) based in part on evidence that State Farm's actions were part of a nationwide fraudulent scheme.<sup>102</sup>

In reversing the award, the Court began by distinguishing compensatory damages from punitive damages, noting that compensatory-damages remedy a plaintiff's concrete loss while punitive damages promote a state's interest in punishing unlawful conduct and deterring its repetition.<sup>103</sup> The Court then made clear that the amount of a punitive-damages award must be tailored to the defendant's misconduct toward the plaintiff, stating that the flaw in the jury's award was that "State Farm was being condemned for its nationwide policies rather than for the conduct directed toward the Campbells."<sup>104</sup> The Court emphasized this point repeatedly, stating that conduct supporting a punitive-damages award "must have a nexus to the specific harm suffered by the plaintiff,"<sup>105</sup> that "[a] defendant should be punished for the conduct that harmed the plaintiff, not for being an unsavory individual or business,"<sup>106</sup> and that "[d]ue process does not permit courts, in the calculation of punitive damages, to adjudicate the merits of other parties' hypothetical claims against a defendant under the guise of the reprehensibility analysis."<sup>107</sup> Additionally, the Court stated that tying the permissible amount of punitive damages to the particular harm suffered by the plaintiff was necessary to prevent defendants from being subjected to "multiple punitive-damages awards for the same conduct."<sup>108</sup>

The Court further reinforced its view of the individualized nature of punitive damages by focusing on the ratio of punitive damages to the compensatory damages recovered by the plaintiff. While the Court refused to endorse any bright-line rule, it warned that "few awards

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102. *Id.* at 420.

103. *Id.* at 416, 419 ("It should be presumed a plaintiff has been made whole for his injuries by compensatory damages, so punitive damages should only be awarded if the defendant's culpability, after having paid compensatory damages, is so reprehensible as to warrant the imposition of further sanctions to achieve punishment or deterrence.").

104. *Id.* at 419–20.

105. *Id.* at 422.

106. *Id.* at 423.

107. *Id.*

108. *Id.* (citing *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 593 (1996) (Breyer, J., concurring) ("Larger damages might also 'double count' by including in the punitive damages award some of the compensatory, or punitive, damages that subsequent plaintiffs would also recover.")). The Court acknowledged that conduct directed toward others—if sufficiently similar to the conduct directed toward the plaintiff—could be considered in determining the defendant's reprehensibility, but found that there was no such similar conduct in the record. *Id.* at 423–24.

exceeding a single-digit ratio” will survive due process and suggested that a 4:1 ratio would be the maximum in most cases.<sup>109</sup>

Finally, in its most recent due process decision on punitive damages, *Philip Morris USA v. Williams*,<sup>110</sup> the Court cemented its view that punitive damages must be individually tailored so that they punish the defendant only for harm done to the plaintiff and not to non-parties to the proceeding.<sup>111</sup> Philip Morris appealed a \$79.5 million punitive damage award to Williams on the ground that the trial court erroneously refused to give a jury instruction saying that the jury could not punish Philip Morris for its misconduct toward others.<sup>112</sup> The Court agreed with Philip Morris, holding that due process prohibits punishing a defendant for harm inflicted on nonparties.<sup>113</sup> The Court held that while a jury can consider evidence of harm to non-parties to show “that the conduct that harmed the plaintiff also posed a substantial risk of harm to the general public, and so was particularly reprehensible,” it cannot use that evidence “to punish a defendant directly on account of harms it is alleged to have visited on nonparties.”<sup>114</sup> Similarly, the Court acknowledged that a jury could consider the potential harm the defendant’s actions may have caused, but stated that the jury is limited to the harm “potentially caused the plaintiff.”<sup>115</sup> Thus, the Court’s decisions have culminated in the principle that as a matter of due process, an individual punitive-damages award can go no further than punishing the defendant for the harm it inflicted on the individual plaintiff.

### *B. The Re-Emergence of the “Limited Punishment” Mandatory Class*

Once the Supreme Court declared that excessive punitive-damages awards violate due process, scholars and practitioners began renewing the call for non-opt-out limited-punishment punitive-damages classes. Even though each of the Supreme Court’s punitive-damages cases

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109. *Id.* at 425.

110. 549 U.S. 346 (2007).

111. *Id.* at 349 (“We are asked whether the Constitution’s Due Process Clause permits a jury to base [a punitive-damages] award in part upon its desire to *punish* the defendant for harming persons who are not before the court (*e.g.*, victims whom the parties do not represent). We hold that such an award would amount to a taking of ‘property’ from the defendant without due process.”).

112. *Id.* at 350–51.

113. *Id.* at 353 (“[T]he Constitution’s Due Process Clause forbids a State to use a punitive damages award to punish a defendant for injury that it inflicts upon nonparties or those whom they directly represent, *i.e.*, injury that it inflicts upon those who are, essentially, strangers to the litigation.”).

114. *Id.* at 355.

115. *Id.* at 354 (emphasis omitted).

involved an individual action, supporters of the limited-punishment class have argued that the Court's reasoning regarding individual awards also serves to prohibit multiple punitive damage awards for the same conduct. Supporters have argued that the restriction on multiple awards creates a limited fund of punitive damages that a defendant can be required to pay, thereby justifying a mandatory class.<sup>116</sup> Supporters

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116. See, e.g., Cabraser, *supra* note 12, at 1028; Cabraser & Sobol, *supra* note 5, at 2031 (arguing that the Supreme Court's punitive-damages decisions justify mandatory punitive-damages classes under Rule 23(b)(1)(B)); John C. Coffee, Jr., *The Tobacco Wars: Peace in Our Time?*, N.Y. L.J., July 20, 2000, at 1 (suggesting that a mandatory punitive-damages class might be a viable solution to tobacco litigation); Janutis, *supra* note 4, at 368 ("Thus, while purporting to impose limitations on individual awards, *Gore* and *Campbell* also seem to impose limitations on multiple punitive damages."); Nagareda, *supra* note 9, at 956 ("Advocates of the stand-alone, mandatory class read the Supreme Court's punitive damages decisions under the Due Process Clause to imply the existence of an outer limit on the punishment that may be imposed cumulatively for a single course of conduct."); Newman, *supra* note 49, at 257 (citing *State Farm* in asserting that punitive-damages classes can be certified under Rule 23(b)(1)(B) because the Constitution places a legal limit on total permissible punitive damages); Sharkey, *supra* note 1, at 411-12 (noting that advocates of punitive-damages class actions have relied on *State Farm* to support their view); Mesulam, *supra* note 12, at 1132 ("[T]he Supreme Court's punitive damages jurisprudence implicitly forbids multiple awards and thus requires claim aggregation [under Rule 23(b)(1)(B)]."); Aileen L. Nagy, Note, *Certifying Mandatory Punitive Damages Classes in a Post-Ortiz and State Farm World*, 58 VAND. L. REV. 599, 611 (2005) ("*State Farm* has reopened the door for proponents of mandatory punitive damage class certification to argue the need for such certification under [Rule] 23(b)(1)(B)."); Ryan Kathleen Roth, Note, *Mass Tort Malignancy: In the Search for a Cure, Courts Should Continue to Certify Mandatory, Settlement Only Class Actions*, 79 B.U. L. REV. 577, 623-29 (1999) (arguing in favor of mandatory, settlement-only class actions); see also *In re The Exxon Valdez*, 229 F.3d 790, 795-96 (9th Cir. 2000) (extolling mandatory classes for punitive damages and noting that "mandatory classes have been endorsed by many courts and commentators"); *Rahim v. Sheahan*, No. 99-C-0395, 2001 WL 1263493, at \*14 n.7 (N.D. Ill. Oct. 19, 2001) (stating that to the extent that due process places a limit on total punitive damages, Rule 23(b)(1)(B) is ideally suited to resolving mass punitive-damages claims).

Advocates also have argued that the Supreme Court's decisions in *Gore* and *State Farm* establish a substantive limit on punitive damages that justifies a mandatory class under Rule 23(b)(1)(B). See, e.g., Brief of Amici Curiae Center for Constitutional Rights et al. in Support of Plaintiffs/Appellees/Cross-Appellants Dukes et al. at 5, 13, *Dukes v. Wal-Mart Stores, Inc.*, 474 F.3d 1214 (9th Cir. 2007), *withdrawn*, 509 F.3d 1168 (9th Cir. 2007) (Nos. 04-16688, 04-16720), 2005 WL 513295 (arguing that *State Farm* is consistent with class-wide determination of punitive damages and supports including all affected parties in a single class proceeding for punitive damages); Defendant Exxon Mobil Corp.'s Memorandum of Law in Support of Its Motion to Certify Mandatory Punitive Damages Class Pursuant to the Due Process Clause and Maryland Rule 2-231(b)(1)(B) at 2-3, 6, *Alban v. ExxonMobil Corp.*, Nos. 03-C-06-010932 OT, 03-C-07-003809 (Md. Cir. Ct. Feb. 29, 2008), 2008 WL 5743596 (arguing for a mandatory class because "there is a finite limit to punitive damages that may be awarded against ExxonMobil under the Due Process Clause."); Defendants' Fairness Hearing Memorandum in Support of the Proposed Class Settlement at 2, *Light*

also have relied on the Court's statements that punitive damages are designed to punish defendants rather than to compensate plaintiffs in order to argue that plaintiffs have no right to punitive damages and therefore no right to opt out their punitive damages claims.<sup>117</sup>

In short, the Supreme Court's recent punitive-damages decisions have breathed new life into the mandatory punitive-damages class action. Although efforts to certify limited-punishment classes have not met with universal success, and were notably rejected in the *Simon II* tobacco litigation,<sup>118</sup> a number of courts recently have certified non-opt-out punitive-damages classes both for settlement and for litigation.<sup>119</sup> Moreover, these recent certification decisions demonstrate the expansive breadth of the limited-punishment theory and shows that it can apply to any class action for punitive damages.

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*v. SCI Funeral Servs. of Fla., Inc.*, No. 01-21376 CA 08 (Fla. Cir. Ct. Sept. 15, 2004), 2004 WL 5777703 [hereinafter Light Motion].

117. See, e.g., *Cabraser & Sobol*, *supra* note 5, at 2020–21 (“Without question, individuals do not have the same entitlement to punitive damages that they do to compensatory damages . . . .”); Newman, *supra* note 49, at 258 (arguing that preventing class members from opting out of “punitive damages claims does not deprive any class member of a vested right”); Mesulam, *supra* note 12, at 1148 (noting that the concern about taking away class members’ opt-out rights “is almost certainly less pressing in the case of punitive damages”); see also *In re Simon II Litig.*, 211 F.R.D. 86, 162–63 (E.D.N.Y. 2002) (“In the context of a punitive damages-only class, opt out is less necessary than it would be with a compensatory damages class since no injured party’s vested right would be affected.”), *vacated*, 407 F.3d 125 (2d Cir. 2005); Light Motion, *supra* note 116, at 17–20 (arguing that due process protections on the right to opt out do not apply to claims for punitive damages); *cf.* Nagareda, *supra* note 54, at 818 & n.287 (stating that because plaintiffs have no right to punitive damages, there is no due process concern with requiring them to give up punitive-damages claims in exchange for exercising a back end right to opt out).

118. *In re Simon II Litig.*, 407 F.3d 125, 127–28 (2d Cir. 2005).

119. See, e.g., *Baker v. Wash. Mut. Fin. Grp., L.L.C.*, No. 1:04-cv-00137-WJG-JMR (S.D. Miss. May 16, 2005), ECF No. 120, at 8–10, 21–22, *aff’d*, 193 F. App’x 294 (5th Cir. 2006); *In re the Exxon Valdez*, No. A89-0095-CV-HRH, at 7–13 (D. Alaska Mar. 8, 1994) (on file with author) (certifying mandatory class for punitive-damages claims arising from the Exxon Valdez oil spill); *Ferguson v. Lief, Cabraser, Heimann & Bernstein, L.L.P.*, 69 P.3d 965, 967 (Cal. 2003) (describing how the parties agreed to certification of a non-opt-out punitive-damages class as part of an \$80 million settlement to resolve a class action arising out of the release of toxic chemicals into the atmosphere); *Light v. SCI Funeral Servs. of Fla., Inc.*, No. 01-21376-08, 2003 WL 25573414, at \*29–32 (Fla. Cir. Ct. Aug. 19, 2003); *Nationwide Mut. Ins. Co. v. O’Dell*, No. 00-C-37, 2006 WL 6367367, at ¶¶ 63–64 (W. Va. Cir. Ct. June 3, 2006) (holding that “*Campbell, Gore* and their progeny” create limits on punitive damages that could be exhausted in conditionally certifying a mandatory class under Rule 23(b)(1)(B)); see also *Rahim*, 2001 WL 1263493, at \*14 n.7 (supporting the use of Rule 23(b)(1)(B) to resolving multiple punitive-damages claims). *But see In re Simon II Litig.*, 407 F.3d 125, 127–28 (2d Cir. 2005) (vacating certification of a mandatory punitive-damages class in a nationwide tobacco class action).

Notably, unlike the early cases that concerned billions of dollars in potential punitive damages, the punitive damages at stake in some recent cases have been much smaller—including one case that settled for only \$3.5 million in punitive damages.<sup>120</sup> As the next Part explains, despite the support for mandatory punitive-damages classes and despite increasing judicial willingness to certify such classes, mandatory punitive-damages classes deprive class members of valuable opt-out rights without justification, and give defendants a vehicle for artificially capping their punitive-damages liability at a level well below that necessary for punishment and deterrence.

### III. THE MANDATORY PUNITIVE-DAMAGES CLASS AS A DISTORTION OF THE SUPREME COURT'S PUNITIVE-DAMAGES JURISPRUDENCE

The reasoning underlying the limited-punishment theory of mandatory class certification is flawed. Rather than establishing a collective cap on punitive damages that requires a mandatory class to prevent opting-out plaintiffs from exhausting all available punitive damages and leaving other plaintiffs with nothing, the Supreme Court's decisions emphasizing the individualized nature of punitive damages demonstrate precisely why a limited-punishment class is not justified. First, the restrictions that the Court has established with respect to individual punitive-damages awards protect against the risk of duplicative punishment and therefore eliminate any risk that one plaintiff's punitive-damages recovery will take punitive damages away from another plaintiff. Second, because plaintiffs have the same right to pursue punitive-damages claims as they do for any other cause of action, there is no special justification for restricting class members' opt-out rights for punitive-damages claims simply because punitive damages are non-compensatory. As a result, limited-punishment classes provide plaintiffs with no additional benefit in exchange for sacrificing their right to opt out and bring their own litigation. Instead, the real winners are (a) defendants—who can settle a class action on the cheap and pay plaintiffs an artificially low level of punitive damages, and (b) class counsel—who can maximize their attorneys' fees by preventing individual class members from pursuing their claims outside of the class action.

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120. *Baker v. Wash. Mut.*, ECF No. 120, at 9 (holding that \$3.5 million in punitive damages was “within the constitutional limit for punitive damages”). Other settlements, however, have provided higher amounts. See *Ferguson*, 69 P.3d at 967 (\$80 million total settlement); *Light v. SCI Funeral Servs. of Fla., Inc.*, No. 01-21376-CA-08, 2004 WL 5771805 (Fla. Cir. Ct. Oct. 20, 2004) (approving settlement providing \$25 million in punitive damages).

*A. The Whole Is Determined by the Sum of Its Parts*

Allowing class members to opt out of a class action and pursue punitive-damages claims individually does not create a risk of subjecting defendants to multiple punishment or of breaching any constitutional cap on punitive damages because the Supreme Court's due process principles already guard against multiple, overlapping awards. Each individual award of punitive damages, even in cases involving multiple claimants, is a separate and distinct award for a separate and distinct legal wrong, and therefore one individual's punitive damage award does not limit the punitive damages available to subsequent claimants. In both *State Farm* and *Philip Morris*, the Supreme Court emphasized that a plaintiff can recover punitive damages only for the harm directed toward that plaintiff, even if the same conduct by the defendant also harmed others.<sup>121</sup> In fact, the Court specifically stated that such strict, individualized limits on punitive damages were necessary in order to prevent the defendant from facing multiple punishment for the same conduct.<sup>122</sup> Similarly, the Court's focus on the ratio of punitive damages to compensatory damages reinforces the plaintiff-specific function of punitive damages by tying punitive damages to the harm suffered by the plaintiff, regardless of whether other victims suffered substantially greater or lesser damages.

As long as the Court's due process principles are followed at the individual level, there is no risk of overlapping awards. If a class member opts out and pursues a separate punitive-damages claim, that class member cannot recover any punitive damages to which other plaintiffs would be entitled because she cannot recover for the defendant's wrongdoing toward others.<sup>123</sup> For the same reason, no other

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121. See *supra* notes 97–115 and accompanying text.

122. *State Farm Mut. Auto. Ins. Co.*, 538 U.S. 408, 423. A number of lower courts have relied on this reasoning to hold that punitive damages in an individual case must be limited to the harm directed at the individual plaintiff so that the award does not cover conduct that could be punished in a separate lawsuit. See, e.g., *Williams v. Conagra Poultry Co.*, 378 F.3d 790, 797 (8th Cir. 2004) (“Tying punitive damages to the harm actually suffered by the plaintiff prevents punishing defendants repeatedly for the same conduct: If a jury fails to confine its deliberations with respect to punitive damages to the specific harm suffered by the plaintiff and instead focuses on the conduct of the defendant in general, it may award exemplary damages for conduct that could be the subject of an independent lawsuit, resulting in a duplicative punitive damages award.”); *Bocci v. Key Pharm., Inc.*, 76 P.3d 669, 676 n.1 (Or. Ct. App. 2003) (vacating punitive-damages verdict that would have allowed one plaintiff to recover for harm done to another plaintiff).

123. Even before *Gore*, some courts addressing multiple punitive-damages claims against a single defendant held that a prior award of punitive damages in an individual case did not limit a punitive-damages award in a subsequent case precisely because the punitive-damages award in the prior case was only for harm caused to that

plaintiff would have a claim to her punitive damages because those damages are specific to the harm done to her. Thus, a punitive-damages award obtained by an opting-out plaintiff would not impair the punitive damage claims of any other class members.

The flaw in the limited-punishment theory is the tacit assumption that there is a collective cap on punitive damages that is fixed and independent of the number of people in the class. It is more accurate to characterize any overall limit on punitive damages (to the extent one exists) as a function of the size of the class, since the amount of punitive damages awardable depends on the number of individuals wrongly harmed. The collective limit therefore can be conceptualized as the sum of the individual constitutional limits on each plaintiff's separate and distinct claim for punitive damages.<sup>124</sup>

Under that conception, successive individual claims would not breach the punitive-damages cap for two reasons. First, reframing the cap as a total of each individual cap shows that there is no risk of one plaintiff taking punitive damages away from another plaintiff. Unlike a traditional limited fund, plaintiffs are not competing with each other for the same common pool of damages. Rather, the pool is one that can be divided into shares for each plaintiff, and each plaintiff is only entitled to his or her particular share, as if a common piece of land were divided into separate private plots. Because each plaintiff has no claim to anyone else's slice, there is no risk that an opting-out plaintiff will take someone else's punitive damages.

Second, there is no risk that successive claims will breach the punitive-damages cap because the cap is determined by the total number of individual claims. Thus, the limited-punishment theory operates

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particular plaintiff. *See, e.g., King v. Armstrong World Indus., Inc.*, 906 F.2d 1022, 1030 (5th Cir. 1990) (allowing plaintiff to collect punitive damages from defendant Celotex because "even though Celotex has paid punitive damages to other plaintiffs in other cases, the punitive damages awarded in those cases have reflected the harm inflicted upon only the plaintiffs in those suits"); *Neal v. Carey Canadian Mines, Ltd.*, 548 F. Supp. 357, 376-77 (E.D. Pa. 1982) (rejecting the argument that multiple punitive damage awards constitute excessive punishment because "[e]ach tort committed by the defendant is individual and peculiar to that particular plaintiff who . . . brought suit"). *But cf.* Colby, *supra* note 13, at 643 (suggesting that these decisions are atypical and "have been drowned out" by decisions assessing punitive damages to address the total harm caused by a defendant's misconduct).

124. Some criticisms of opt-out rights also assume a fixed limit of available funds that is independent of the size of the class. Professor Perino, for example, applies a game-theoretic analysis to a situation where the defendant has a fixed level of available assets and concludes that permitting opt-outs could undermine the equilibrium favoring settlement. Perino, *supra* note 38, at 119-31. Whether or not Perino's model holds sway in the "limited assets" context, it is not clear that the model applies in the "limited punishment" context, where the size of the fund rises and falls as the class size rises and falls.

differently than the original limited-fund example in which the defendant's assets were capped at \$100 but twenty plaintiffs had \$10 claims, which justified a mandatory class that gave every plaintiff \$5. The cap is determined by the number of people in the class: if twenty individuals have punitive-damages claims of \$10 against the defendant, then the constitutional cap is \$200, not \$100.<sup>125</sup> If one plaintiff opts out, that plaintiff will only be able to receive \$10 in punitive damages for the harm directed at her. Similarly, the nineteen plaintiffs who remain in the class will each be able to collect their \$10, because \$190 in punitive damages will remain in the fund.<sup>126</sup> Whether or not a plaintiff opts out, each plaintiff will be able to obtain \$10 in punitive damages.<sup>127</sup> In short, a mandatory class provides no benefit to plaintiffs.

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125. This reasoning presumes that there is no other limit on the amount of punitive damages that a defendant can pay. If a defendant harms a very large number of people, however, it is possible that it could be driven into bankruptcy if it has to pay all punitive-damages claims, even when constrained by the Constitution. But if that is the case, then mandatory certification might be permissible under the more traditional "limited assets" version of the limited-fund theory and there would be no need to try and separately justify a "limited punishment" class on due process grounds. The fact that litigants are seeking certification under a "limited punishment" theory rather than a "limited assets" theory suggests that this issue is arising in cases that do not present a risk of bankruptcy. In any event, if individual litigation threatens to exhaust a defendant's assets, bankruptcy may be a better alternative than a mandatory class. See Coffee, *supra* note 22, at 1383 (arguing that bankruptcy pools assets more effectively than the class action and that it prevents defendants from undervaluing their assets). Moreover, the risk of bankruptcy does not justify a limited-punishment class because such a class is mandatory for punitive damages only. It does not prevent plaintiffs from opting out their compensatory damages claims. See, e.g., *Baker v. Wash. Mut.*, No. 1:04-cv-00137-WJG-JMR, at 6 (noting that the settlement permitted class members to opt out compensatory damages claims but barred them from opting out punitive-damages claims); Coffee, *supra* note 116, at 1-2 (suggesting, in the tobacco context, a class action that permitted class members to opt out compensatory claims but barred them from opting out punitive claims). It would be difficult to justify a limited-punishment class on the ground that the defendant cannot afford to pay all claims while still allowing class members to opt out and seek compensatory damages awards in individual litigation.

126. In fairness, it is difficult to see how a jury can effectively compartmentalize a defendant's wrongdoing that affects a wide range of people, see Mesulam, *supra* note 12, at 1133, but that is what the Supreme Court requires, and that is how lower courts have been assessing individual punitive-damages awards. See, e.g., *Estate of Schwartz v. Philip Morris, Inc.*, 235 P.3d 668, 670 (Or. 2010) (vacating punitive-damages award where jury instructions did not warn the jury that it could not consider harm inflicted on non-parties). Additionally, jury awards of punitive damages tend to be individualized to some degree, as the strongest predictor of a punitive-damages award is the amount of compensatory damages awarded. See Theodore Eisenberg et al., *The Predictability of Punitive Damages*, 26 J. LEGAL STUD. 623, 637 (1997).

127. Several scholars have made the point that the Supreme Court's punitive-damages jurisprudence makes punitive damages individualized and therefore mitigates

Instead, its only consequence is that class members lose their right to opt out and pursue their own claims.

The only way a limited-punishment class could be justified would be if the Supreme Court's punitive-damages principles established a discrete collective cap on punitive damages that exists in addition to the constitutional limits on individual awards. But nothing in the Court's decisions supports that outcome. Rather, imposing a separate collective cap would allow defendants to engage in their own form of double counting, leading to too little punishment and deterrence. This reasoning would permit defendants to argue not only that the punitive damages each individual plaintiff can receive are limited by due process, but also that the amount of punitive damages that a class of plaintiffs can collectively recover is further reduced beyond the limits established for individual cases. In effect, this would mean that a class as a whole would be entitled to a lower level of punitive damages than would otherwise be available simply because the defendant happened to harm multiple people.<sup>128</sup> Not only is such a result illogical, but it would appear to violate the Court's holding in *Ortiz* that the total amount distributed to plaintiffs in a limited-fund class cannot fall below the totals that separate individual litigation would have provided.<sup>129</sup> Thus, rather than protecting plaintiffs, applying a collective ceiling simply

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the risk of multiple punishment. Thomas Colby, for example, argues that punitive damages traditionally were designed to punish defendants only for harm done to the individual plaintiff, and therefore the problem of multiple punishment "is essentially moot." Colby, *supra* note 13, at 589; *see also* Hines, *supra* note 3, at 811 ("If every mass tort punitive damages award is properly and constitutionally calculated to punish only the harm to a particular plaintiff, then it would seem every mass tort plaintiff could recover punitive damages awards for the same conduct – because prior plaintiffs would only have been awarded punitive damages based on their own harm."); Janutis, *supra* note 4, at 375–76 (identifying the debate over whether *State Farm* protects against multiple punishment or prohibits multiple punishment). These commentators either have not explicitly addressed how the individualized nature of punitive damages affects mandatory class certification under Rule 23(b)(1)(B) or address the issue only briefly. Colby concludes that limited-punishment classes may not be legitimate under a theory of individualized punitive damages, but assumes that after *Ortiz*, limited-fund classes are no longer viable. *See* Colby, *supra* note 13, at 664–65. However, this has turned out not to be the case. *See supra* note 119 and accompanying text. Professor Hines appears to believe that despite the Supreme Court's statements about the individualized nature of punitive damages, an "aggregate punishment problem" still exists, and that the Supreme Court one day will have to step in to resolve it. Hines, *supra* note 3, at 811.

128. *Cf.* Cabraser, *supra* note 12, at 982 ("While it is well established that no individual victim is entitled to punitive damages, it is equally true that no transgressor is entitled to be relieved of exposure to them.").

129. 527 U.S. 815, 839 (1999) ("The limited fund cases thus ensured that the class as a whole was given the best deal; they did not give the defendant a better deal than *seriatim* litigation would have produced.").

allows defendants to artificially cap their punitive-damages liability at a level that does not adequately safeguard society's interest in punishment and deterrence while at the same time eliminating the ability of class members to opt out and bring their own claims.

*B. A Plaintiff's Right to Punitive Damages*

Just as the Supreme Court's punitive-damages jurisprudence does not justify a limited-punishment mandatory class, the argument that plaintiffs lack a "right" to punitive damages also fails to justify a non-opt-out punitive-damages class. A number of courts and commentators have asserted that because punitive damages are designed to punish and deter rather than to compensate, they represent a windfall for plaintiffs, and that plaintiffs therefore lack any right to collect punitive damages.<sup>130</sup> Supporters of non-opt-out punitive-damages classes have relied on this line of reasoning to assert that because plaintiffs lack any right to punitive damages, there is no due process concern with taking away a class member's right to opt out punitive-damages claims.<sup>131</sup> That reasoning is flawed, however, because it conflates the question of whether punitive damages are compensatory with the question of whether a plaintiff has the right to seek them.

First, the fact that punitive damages do not serve a compensatory purpose does not mean that plaintiffs do not have the right to seek them in appropriate circumstances. Whether or not plaintiffs are entitled to punitive damages as of right, they are entitled to have a fact-finder determine whether or not they will receive punitive damages. If plaintiffs have individual claims for punitive damages that would be potentially addressed by a limited-punishment class, that means that either state or federal law has provided them with a cause of action that permits recovery of punitive damages, and that gives them a right to present their punitive-damages claims to a jury.<sup>132</sup> That cause of action

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130. See, e.g., *City of Newport v. Fact Concerts, Inc.*, 453 U.S. 247, 266–67 (1981) ("Punitive damages . . . are not intended to compensate the injured party, but rather to punish the tortfeasor . . . [they] are in effect a windfall to a fully compensated plaintiff."); Nagareda, *supra* note 54, at 818 ("Plaintiffs are entitled to compensatory damages upon proof that a tort has been committed upon them, but they have no entitlement to punitive damages."); Newman, *supra* note 49, at 258 (citing cases); Malcolm E. Wheeler, *The Constitutional Case for Reforming Punitive Damages Procedures*, 69 VA. L. REV. 269, 292 (1983) ("As courts have uniformly held, no plaintiff has a right to punitive damages: the purpose of punitive damages is to vindicate the public interest, not that of a particular plaintiff.").

131. See *supra* note 115 and accompanying text.

132. See, e.g., *Wallace v. Thornton*, 672 So. 2d 724, 728 (Miss. 1996) ("A plaintiff is entitled to punitive damages only if he has demonstrated a willful or malicious wrong or the gross, reckless disregard for the rights of others." (quoting

is a property interest protected by the Due Process Clause.<sup>133</sup> Thus, in other contexts, the Supreme Court has treated the right to seek punitive damages (as opposed to an automatic right to the punitive damages themselves) as an “important substantive right.”<sup>134</sup> In fact, several states have purposely decided to allow plaintiffs to recover punitive damages in order to provide an incentive to bring lawsuits that keep defendants accountable for their misconduct.<sup>135</sup> Once state or federal

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*Valley Forge Ins. Co. v. Strickland*, 620 So. 2d 535, 540 (Miss. 1993))). Some federal causes of action also permit plaintiffs to recover punitive damages. *See, e.g.*, 42 U.S.C. § 1981a(a)-(b) (2006) (permitting plaintiffs to recover both compensatory and punitive damages against private defendants in employment discrimination cases if the defendant acted with “malice or with reckless indifference to the federally protected rights of an aggrieved individual”); *Smith v. Wade*, 461 U.S. 30, 52 (1983) (holding that punitive damages are recoverable under 42 U.S.C. § 1983 and stating that while plaintiffs cannot receive punitive damages as of right, they are entitled to have a jury decide whether to award punitive damages upon a showing of “sufficiently serious misconduct on the defendant’s part”).

In a similar vein, if plaintiffs have no right to seek punitive damages, then it seems strange that the law places the decision to seek punitive damages in the hands of the plaintiff, as opposed to the state or some other party. If plaintiffs lack a right to punitive damages because punitive damages are designed to punish the defendant rather than to reward the plaintiff, then, as other scholars have noted, the defendant’s obligation to pay punitive damages should not depend, as it does now, on the plaintiff’s decision to seek punitive damages, or whether the plaintiff actually succeeds in the litigation. *See, e.g.*, Colby, *supra* note 13, at 607–13; Anthony J. Sebok, *Punitive Damages: From Myth to Theory*, 92 IOWA L. REV. 957, 1023–29 (2007). For example, if a plaintiff’s claim fails on procedural grounds, say because the statute of limitations has run, that does not change the degree of the defendant’s wrongdoing, but it does bar the plaintiff from collecting punitive damages. Under a theory where punitive damages do not belong to the plaintiff, a defendant should still be held accountable for its wrongdoing whether or not the particular individual who suffered harm has pursued a timely claim. Alternatively, if there is no right to punitive damages, then there is no reason why only the plaintiff should be able to seek punitive damages. Arguably, if punitive damages are designed to fulfill the social functions of punishment and deterrence, then the State, or perhaps any individual, should be authorized to pursue punitive damages to ensure that those goals are satisfied, even if the injured plaintiff decides not to bring a lawsuit.

133. *Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 428 (1982) (“[A] cause of action is a species of property protected by the Fourteenth Amendment’s Due Process Clause.” (discussing *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 313 (1950))).

134. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 63 (1995) (interpreting an arbitration clause not to restrict the arbitrator’s authority to award punitive damages because it was unlikely that the parties would have agreed to give up such an “important substantive right.”).

135. *See, e.g.*, *Johns-Manville Sales Corp. v. Janssens*, 463 So. 2d 242, 247 (Fla. Dist. Ct. App. 1984) (“The incentive to bring actions for punitive damages is favored because it has been determined to be the most satisfactory way to correct evil-doing in areas not covered by the criminal law.”); *Sudeen v. Castleberry*, 794 So. 2d 237, 249 (Miss. Ct. App. 2001) (“What is otherwise a windfall is deemed necessarily

law creates a cause of action that permits recovery of punitive damages, a court should not be able to use class certification procedures to take away a plaintiff's cause of action for punitive damages simply because punitive damages are not compensatory.

Second, plaintiffs have a right to seek other non-compensatory remedies, and there is no reason to treat punitive damages any differently. Several federal statutes, for example, provide for relief in the form of statutory damages, where defendants, if found liable, must pay minimum penalties regardless of whether those damages match the harm suffered by the plaintiff.<sup>136</sup> Other state and federal statutes provide that plaintiffs can receive treble damages for a statutory violation.<sup>137</sup> Although such damages are extra-compensatory, plaintiffs are entitled to collect those damages when violations occur.

Third, nothing in either Rule 23 or the Due Process Clause provides that punitive-damages claims are somehow exempt from the general right to opt-out claims for money damages. In describing the constitutional foundations of the right to opt out, the Supreme Court stated that due process protects plaintiffs' rights to opt out of class actions that are "wholly or predominately for money judgments."<sup>138</sup> It did not speak of compensatory damages only, or say that punitive damages would not constitute a "money judgment." Similarly, the limited-fund class settlement that the Supreme Court rejected in *Ortiz* encompassed claims for both compensatory and punitive damages, and the Court nowhere distinguished between the two in rejecting certification of a non-opt-out class or suggested that the punitive-damages claims could be certified on a mandatory basis even if the compensatory claims could not.<sup>139</sup> Nor would there be a legitimate basis for distinguishing compensatory-damages claims from punitive-damages

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granted to the plaintiff as his reward for public service in bringing the wrongdoer to account."); *Walker v. Sheldon*, 179 N.E.2d 497, 498 (N.Y. 1961) (indicating that "the principal advantage" of punitive damages is that it induces wronged plaintiffs to hold defendants to account (quoting CHARLES T. MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES 276 (1935))).

136. *See, e.g.*, 5 U.S.C. § 552a(g)(4)(A) (2006) (stating that any plaintiff suffering damages shall receive no less than \$1,000); 15 U.S.C. § 1640(a) (authorizing statutory damages in varying amounts); § 1681n(a)(1)(B) (stating that for certain violations, a plaintiff shall receive actual damages or \$1,000, whichever is greater); § 1692k(a)(2)(A) (permitting judge to award up to \$1,000 to prevailing plaintiffs irrespective of actual damages).

137. *See, e.g.*, § 15(a); 18 U.S.C. § 1964(c); N.C. GEN. STAT. § 75-16 (2009).

138. *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 811-12 & n.3 (1985).

139. 527 U.S. 815, 827 (1999) (describing how the parties' global asbestos settlement barred plaintiffs from receiving punitive damages if they brought claims against the settlement trust).

claims, as the right to opt out is predicated in large part on the principle that no person should be bound by *res judicata* to a judgment to which that person is not a party.<sup>140</sup> Because principles of *res judicata* apply to punitive-damages claims as well as compensatory-damages claims,<sup>141</sup> a class member's right to opt out is just as strong for punitive-damages claims as it is for compensatory-damages claims.

Finally, and perhaps most importantly, if plaintiffs truly lack a right to punitive damages, then the entire justification for a mandatory class under Rule 23(b)(1)(B) disappears. The purpose of Rule 23(b)(1)(B) is to protect plaintiffs, not defendants, by ensuring that the proceeds of a limited fund are distributed equitably among all claimants. But if plaintiffs have no right to punitive damages, then how punitive damages are distributed among class members is irrelevant. The punishment and deterrence functions of punitive damages are fulfilled simply by making the defendant pay them, regardless of how they are paid. Giving some plaintiffs all the available punitive damages and others none satisfies the function of punitive damages just as well as distributing punitive damages on a pro-rata basis.<sup>142</sup> Thus, the argument that limited-punishment classes are appropriate under Rule 23(b)(1)(B) because plaintiffs lack a right to punitive damages more likely reflects a defendant's interest in undermining a plaintiff's claim for punitive damages than a concern about treating plaintiffs equitably.

In short, both arguments that proponents of the limited-punishment theory use to justify mandatory punitive-damages classes—(a) that the Due Process Clause creates a collective limit on punitive damages awardable against a defendant, and (b) that plaintiffs have no right to punitive damages—actually eliminate the rationale for taking away class members' right to opt out. Instead of protecting plaintiffs, mandatory limited-punishment classes unnecessarily deprive plaintiffs of their right to opt out and hinder them from recovering an appropriate level of punitive damages. They also allow defendants to erect additional limits to their punitive-damages liability beyond the limits already set by the Supreme Court, which could result in under-punishment and under-deterrence of serious wrongdoing. But even if such arguments could

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140. See *id.* at 846 (quoting *Hansberry v. Lee*, 311 U.S. 32, 40 (1940)).

141. See, e.g., *Brown & Williamson Tobacco Corp. v. Gault*, 627 S.E.2d 549, 553–54 (Ga. 2006) (holding that a state settlement of tobacco-related claims was *res judicata* as to private plaintiffs' subsequent claims for punitive damages against the same defendants).

142. See, e.g., Denmark, *supra* note 5, at 945 n.72 (noting that punitive damages could just as easily be burned as given to the plaintiff and that each would equally serve the deterrence and punishment goals of punitive damages); Sharkey, *supra* note 1, at 370–71 & nn.65–66 (“[C]onventional economic opinion has traditionally remained completely agnostic with respect to the distribution of punitive damages.”).

justify a limited-fund class in a litigation context, as the next Part discusses, the problems with mandatory punitive-damages classes are exacerbated when, as is commonly the case, class actions are resolved by settlement rather than by litigation.

#### IV. PUNITIVE DAMAGES AND SETTLEMENT

Many of the arguments favoring limited-punishment classes assume a class action that will be litigated to judgment.<sup>143</sup> The limited-punishment theory may seem appealing in a trial setting. There, a jury can make findings regarding liability, assess the level of wrongdoing of the defendant with respect to all affected individuals, award punitive damages that fully account for the total harm inflicted by the defendant, and fully punish the defendant up to the limits provided by the Constitution.

Most class actions, however, are resolved by settlement rather than by trial.<sup>144</sup> In a settlement, there is no jury determination of the

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143. See, e.g., *In re "Agent Orange" Prod. Liab. Litig.*, 100 F.R.D. 718, 728 (E.D.N.Y. 1983) (describing how a mandatory class would ensure an equitable distribution of punitive damages awarded by a jury), *mandamus denied sub nom. In re Diamond Shamrock Chems. Co.*, 725 F.2d 858 (2d Cir. 1984); 2 ALI, ENTERPRISE RESPONSIBILITY FOR PERSONAL INJURY: APPROACHES TO LEGAL AND INSTITUTIONAL CHANGE 262 (1991) (describing and supporting an American Bar Association proposal for federal legislation that would create a single class action in which there would be "one mass trial on the punitive damages component" of the class claims (citing ABA, SPECIAL COMM. ON PUNITIVE DAMAGES SECTION OF LITIG., PUNITIVE DAMAGES: A CONSTRUCTIVE EXAMINATION 71-85 (1986))); Mesulam, *supra* note 12, at 1146-47 (describing trial procedures for determining punitive damages and distributing them to class members). *But see* Cabraser & Sobol, *supra* note 5, at 2005-06 (discussing how "[p]unitive damages class action settlements" can resolve multiple punishment concerns); Newman, *supra* note 49, at 255 ("Mandatory punitive damages classes may be beneficial to defendants either in the context of litigation or settlement . . .").

144. See, e.g., Elliott J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*, 104 YALE L.J. 2053, 2098 (1995) ("Defendants' and plaintiffs' attorneys agree to settle virtually all class actions that survive motions to dismiss and motions for summary judgment."); Wolfman & Morrison, *supra* note 44, at 739 ("The vast majority of class actions settle."). Although empirical data is limited, one study of four federal district courts found that a "substantial majority" of certified class actions were resolved by settlement. See THOMAS E. WILLGING, LAURAL L. HOOPER & ROBERT J. NIEMIC, FED. JUD. CTR., EMPIRICAL STUDY OF CLASS ACTIONS IN FOUR FEDERAL DISTRICT COURTS: FINAL REPORT TO THE ADVISORY COMMITTEE ON CIVIL RULES 60 (1996). Settlement rates for certified classes in the four districts ranged from 62 percent to 100 percent. See *id.*; Bryant G. Garth, *Studying Civil Litigation Through the Class Action*, 62 IND. L.J. 497, 501 (1987) (finding that certified classes settled at a 78 percent rate). One study of state-court civil trials in large counties found that only one of the 11,908 trials covered in the study was a class action. THOMAS H. COHEN & STEVEN K. SMITH, U.S. DEP'T OF JUSTICE, BUREAU OF JUSTICE STATISTICS, CIVIL TRIAL

defendant's wrongdoing and no jury award of punitive damages. Instead, the amount of the settlement, including the amount of the settlement allocated as punitive damages, is determined by the parties. Resolving class members' punitive-damages claims through a non-opt-out limited-punishment settlement class starkly illustrates how such classes reward defendants and class counsel at the expense of class plaintiffs. Specifically, limited-punishment settlement classes are not justified for three reasons.

First, the portion of the settlement fund that the parties designate as punitive damages is an arbitrary number, and is unlikely to represent the upper constitutional limit on permissible punitive damages. Second, it is far from clear that funds designated by the parties as punitive damages can truly be considered punitive within the meaning of due process. Punitive damages constitute a state-sanctioned penalty that reflects the community's sense of moral outrage, and it is difficult to see how punitive damages that are agreed to and set by the parties themselves can represent state-sponsored punishment. Third, the due process limits on punitive damages apply only to state action, such as a jury award made at trial. Settlements, by contrast, generally do not qualify as state action. If a class settlement is not state action, then the Due Process Clause does not come into play, and a settlement's allocation of punitive damages does not implicate the constitutional constraints on punitive damages.

To be sure, these arguments apply to all settlements, not just class actions. But in individual cases, the allocation of damages as compensatory or punitive in a settlement will hold little significance for the parties involved. In the class action context, by contrast, considering whether settlements can constitute punitive damages is critically important because the parties' designation of a portion of a settlement as punitive damages becomes the basis for resolving the rights of third-party class members, and resolving them in a way that deprives those class members of the ability to control their own fate by opting out of the settlement. Settlement enables defendants and class counsel to game the system in order to certify a mandatory class. They can label an arbitrary portion of the settlement as punitive damages and call it the constitutional limit on punitive damages, regardless of whether the amount they designate actually serves the function of punitive damages. Instead of exposing defendants to the maximum

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CASES AND VERDICTS IN LARGE COUNTIES, 2001, at 4 (2004). Moreover, not all cases that are not settled are necessarily tried, as some may be resolved by dispositive motion. The federal study, for example, found that a trial began in only 18 of 407 class actions (4 percent), and that 5 of those 18 cases ended up settling. *See* WILLING, *supra*, at 10-11.

allowable punishment, settlement allows defendants to help set their own punitive-damages liability at a level that may fall well short of that necessary to punish and deter. Permitting limited-punishment settlement classes therefore sacrifices the interests of class plaintiffs for those of defendants and class counsel. Ultimately, it threatens to leave plaintiffs worse off than if no settlement had been reached.

#### *A. Meaningless Numbers*

One of the requirements of a limited-fund class is that the entire fund must be devoted to satisfying the class members' claims in order to ensure that the defendant does not get a better deal than it would through individual litigation.<sup>145</sup> A pre-requisite of a mandatory punitive-damages settlement class is that the amount the settlement provides as punitive damages must represent the upper threshold of constitutionally permissible punitive damages. For several reasons, however, it is unlikely that the amount of the settlement that the parties label as punitive damages will constitute that limit, meaning that the settlement threatens to leave plaintiffs with fewer punitive damages than they might obtain in the absence of settlement.

First, the parties' allocation of a settlement fund between compensatory and punitive damages is necessarily arbitrary. A defendant deciding whether to settle a case typically cares only about the total amount of money that it has to pay.<sup>146</sup> It does not care whether that money is called compensatory damages, punitive damages, or something else. From the defendant's perspective, there is no difference between (a) a \$10 million settlement that labels \$5 million as compensatory damages and \$5 million as punitive damages, (b) a settlement that labels \$2 million as compensatory damages and \$8 million as punitive damages, or (c) a settlement that labels \$8 million as compensatory damages and \$2 million as punitive damages. The division that the parties settle upon is essentially meaningless. At a minimum, it is highly unlikely that the parties are engaging in a detailed examination of the defendant's wrongdoing in deciding how to allocate the settlement fund between compensatory and punitive damages. Settlement allows parties who want a mandatory class to manipulate the settlement by shrinking the amount of compensatory damages and

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145. See *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 838–39 (1999).

146. See, e.g., *Strong v. Bellsouth Telecomm., Inc.*, 137 F.3d 844, 849 (5th Cir. 1998) (recognizing “the economic reality that a settling defendant is concerned only with its total liability”); Coffee, *supra* note 22, at 1376 (noting that defendants are “largely indifferent” to how settlement funds are allocated); Leslie, *supra* note 21, at 79–80 (“The defendant merely wants to eliminate liability while minimizing its overall payout, however distributed.”).

increasing the amount of punitive damages to create the appearance of a limited fund. The result is that class plaintiffs who think that the total settlement is too low will find themselves unable to pursue their own claims because the parties will be able to point to their inflated punitive-damages allocation as representing the maximum permitted by due process.

To be sure, a plaintiff may have some incentive to try and decrease the percentage of the settlement devoted to punitive damages for tax reasons. Punitive damages are taxable as income while some types of compensatory damages are not.<sup>147</sup> But for many class actions involving punitive damages, this tax incentive will not apply. Only compensatory damages obtained “on account of personal physical injuries or physical sickness” are excluded from gross income.<sup>148</sup> Compensatory and punitive damages are equally taxable with respect to claims of discrimination, financial impropriety, deceptive trade practices, and other non-physical injuries.<sup>149</sup>

But even in cases that do involve personal physical injuries, the fact that plaintiffs may want to minimize punitive damages and maximize compensatory damages does not justify a mandatory class. It merely shows that the plaintiffs’ preferred allocation of compensatory and punitive damages rests on tax considerations, and not on factors related to the extent of the defendant’s wrongdoing or society’s interest in punishment and deterrence. Thus, even if the amount devoted to

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147. See 26 U.S.C. § 104(a)(2) (2006) (excluding from the definition of gross income “the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness”).

148. *Id.*

149. See *Comm’r v. Schleier*, 515 U.S. 323, 330–31 (1995) (finding that damages plaintiff received for his age discrimination claim were taxable, and implying that economic injuries are not personal physical injuries within the meaning of the statute). Several recent cases in which courts approved mandatory punitive-damages settlement classes involved injuries where both compensatory and punitive damages likely were taxable. In *Baker v. Washington Mutual Finance Group*, the plaintiffs’ claims were for financial fraud, deceptive trade practices, and breach of fiduciary duty regarding the purchase of loans and credit disability and personal property insurance. 193 F. App’x 294, 295–96 (5th Cir. 2006). In *Light v. SCI Funeral Services of Florida*, relatives of persons who had bought plots at a cemetery alleged that the cemetery had desecrated remains and brought claims for deceptive trade practices, tortious interference with dead bodies, and failure to maintain cemeteries in a reasonable and dignified condition. 2003 WL 25573414, at 3 (Fla. Cir. Ct. Aug. 19, 2003). Similarly, some studies have shown that a significant portion of punitive-damages verdicts occur in cases involving non-physical injuries such as financial fraud, discrimination, libel and slander, and other employment cases. See CAROL J. DEFRAnces & MARIKA F.X. LITRAS, U.S. DEP’T OF JUSTICE, BUREAU OF JUSTICE STATISTICS, CIVIL JUSTICE SURVEY OF STATE COURTS, 1996: CIVIL TRIAL CASES AND VERDICTS IN LARGE COUNTIES 9 tbl.8 (1999).

punitive damages is determined by arms-length negotiations, there is little reason to think that the number bears any meaningful relationship to the constitutional guideposts for assessing punitive damages.<sup>150</sup>

Second, even if the amount devoted to punitive damages was not arbitrarily chosen, it is fanciful to think that a defendant would agree to settle for the maximum amount of permissible punitive damages. Settlements are by their nature compromises, and they inevitably occur at a discount. Plaintiffs agree to accept less than one hundred cents on the dollar to avoid the uncertainty of litigation while defendants agree to pay more than they claim they owe in order to obtain closure.<sup>151</sup> Thus, a settlement will neither inflict the maximum amount of punishment necessary to achieve the retribution goal of punitive damages, nor require a defendant to internalize the full costs of its misconduct as necessary to achieve the deterrence goal of punitive damages.

Past experience with more traditional limited-fund settlements confirms that defendants will settle at a discount rather than at the fund's upper limit. In the limited-fund global asbestos settlement addressed in *Ortiz*, for example, the defendant Fibreboard's insurers paid most of the settlement funds while Fibreboard itself contributed

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150. With respect to settlements, the Internal Revenue Service (IRS) conducts its own investigation based upon the pleadings if it believes that the parties have allocated too much of the settlement to compensatory damages in order to minimize tax obligations. *See, e.g., Bagley v. Comm'r*, 105 T.C. 396, 417–18 (1995) (finding that the IRS was not bound by a settlement allocating the entire \$1.5 million settlement to compensatory damages); *Robinson v. Comm'r*, 102 T.C. 116, 133–34 (1994) (refusing to follow the parties' settlement allocations); *see also* Denmark, *supra* note 5, at 973 (“The IRS makes its own allocation [of compensatory and punitive damages] when parties suggest an allocation that does not reflect the reality of the suit.”). In theory, trial judges deciding whether to approve a class action settlement could evaluate the settlement allocations and decide whether the allocations seem fair. But in many cases, judges will lack both the capacity and the incentive to rigorously investigate the fairness of the parties' proposed distribution of compensatory and punitive damages. *See infra* notes 191–203 and accompanying text. Moreover, unlike the IRS, which can re-allocate the punitive-compensatory breakdown for purposes of calculating tax obligations, a judge presiding over a class action settlement can only approve or reject the settlement. *See* Leslie, *supra* note 21, at 124 (stating that judges “cannot modify the proposed settlement” (citing *In re Domestic Air Transp. Antitrust Litig.*, 148 F.R.D. 297, 305 (N.D. Ga. 1993) (“[The] Court may not rewrite the settlement as requested by numerous objectors.”))). The judge lacks the authority to alter the settlement's terms. *See Becker v. Warner Commc'ns, Inc. (In re Warner Commc'ns Sec. Litig.)*, 798 F.2d 35, 37 (2d Cir. 1986) (holding that district courts should not modify the terms of settlement agreed to by the parties).

151. *See, e.g., Eubanks v. Billington*, 110 F.3d 87, 98 (D.C. Cir. 1997) (“[N]o party can reasonably expect to receive in a settlement precisely what it would receive if it prevailed on the merits.”); *cf. Owens-Corning Fiberglass Corp. v. Malone*, 972 S.W.2d 35, 42 (Tex. 1998) (recognizing that many punitive-damages awards are subsequently settled at a discount during the pendency of an appeal).

only an estimated 4 percent of its post-liability net worth.<sup>152</sup> Similarly, the Liggett tobacco company sought approval of a non-opt-out nationwide class action settlement under the limited-fund theory of Rule 23(b)(1)(B), even though the settlement required Liggett to devote only 7.5 percent of its pre-tax income to the settlement fund.<sup>153</sup> While settling parties seeking certification of a limited-punishment mandatory class may claim that their arms-length negotiations resulted in a settlement that just happened to reach the constitutional limit on punitive damages, the reality is that defendants are not going to settle for the maximum amount of their potential obligations, including their maximum exposure to punitive damages.

Additionally, the fact that settlements occur at a discount makes it difficult to determine whether the funds the parties label as punitive damages can truly be considered punitive. The constitutional constraints on punitive-damages awards are predicated on the assumption that an injured plaintiff has received full compensation through compensatory damages and that punitive damages represent punishment, or exemplary damages, that are imposed over and above compensatory damages.<sup>154</sup> The Supreme Court has explicitly stated that punitive-damages limits

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152. See Coffee, *supra* note 22, at 1402 (describing how Fibreboard was required to contribute only \$10 million even though its post-liability net worth was estimated at \$230 to \$300 million (citing *Ahearn v. Fibreboard Corp.*, 162 F.R.D. 505, 517 (E.D. Tex. 1995))).

153. See Objections of Kenneth Rowe to the Proposed Settlement and Class Certification at 7–10, *Fletcher v. Brooke Group Ltd.*, No. 97-913, (Ala. Cir. Ct. Mar. 1, 1999), available at <http://www.publicjustice.net/Repository/Files/032-Fletcher.pdf>. Similarly, Professor Nagareda describes the *Sulzer Hip Implant Class Action* settlement, which while ostensibly an opt-out settlement, strongly disincentivized class members from opting out by giving opt-out claimants a lower priority than individuals who remained in the class. See Nagareda, *supra* note 76, at 159–60. While the original settlement required Sulzer to make substantial contributions to the settlement fund, those contributions “fell glaringly short of Sulzer’s net worth.” *Id.* at 162.

154. See *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 419 (2003) (“It should be presumed a plaintiff has been made whole for his injuries by compensatory damages, so punitive damages should only be awarded if the defendant’s culpability, after having paid compensatory damages, is so reprehensible as to warrant the imposition of further sanctions to achieve punishment or deterrence.”); *In re Sch. Asbestos Litig.*, 789 F.2d 996, 1003 (3d Cir. 1986) (“[P]unitive damages form no part of the compensatory award—in theory the plaintiff’s losses are fully redressed before consideration is given to exemplary damages.”); A. Mitchell Polinsky & Steven Shavell, *Punitive Damages: An Economic Analysis*, 111 HARV. L. REV. 869, 878 n.15 (1998) (“[P]unitive damages are generally extracompensatory; thus, whether or not they are paid typically does not affect fulfillment of the compensation objective.”); see also *Cooper Indus., Inc. v. Leatherman Tool Grp., Inc.*, 532 U.S. 424, 432 (2001) (explaining that compensatory and punitive damages serve distinct purposes and that compensatory damages are designed to make a plaintiff whole while punitive damages are “private fines” designed to punish and deter) (quoting *Gertz v. Robert Welch, Inc.*, 418 U.S. 323, 350 (1974))).

are based on “a conception of punitive damages awarded entirely for a punitive, not quasi-compensatory, purpose.”<sup>155</sup> But in a settlement where the plaintiff receives less than one hundred cents on the dollar in compensatory damages, the plaintiff will not be made whole by compensatory damages alone, and some portion of the settlement devoted to punitive damages will actually serve a compensatory function rather than a punitive function. If a plaintiff suffers a \$200 injury, and settles a case for \$100 in compensatory damages and \$100 in punitive damages, from the plaintiff’s perspective, the punitive-damages portion of the settlement will go toward making the plaintiff whole just as if that plaintiff received \$200 in compensatory damages and zero punitive damages—the labels themselves are irrelevant.<sup>156</sup> To the extent that the full settlement fund represents less than the full amount of compensatory damages sought, the punitive-damages portion of the fund serves no punitive function at all, but instead is simply a mislabeled pot of additional compensatory damages.<sup>157</sup> The fact that the parties call part of the settlement fund “punitive damages” does not make them so.

The arbitrary nature of a settlement fund’s allocation of compensatory and punitive damages means that the punitive damages that class members receive do not necessarily reflect the full measure of punishment that a defendant deserves for its misconduct. Many class members may still find the settlement to be a good deal, and are certainly entitled to stay in the class and reap the settlement’s benefits. But class members should not find themselves barred from opting out on the ground that the settlement provides the maximum level of

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155. *Exxon Shipping Co. v. Baker*, 554 U.S. 471, 513 n.27 (2008); see Allen, *supra* note 13, at 8–9 (stating that under the Supreme Court’s punitive-damages jurisprudence, “there is no compensatory role for punitive damages”).

156. To be sure, parties could settle a case with claims for both compensatory and punitive damages for an amount greater than full compensation because of the possibility of punitive damages. Even if that were the case, though, only the portion of the fund that exceeds full compensation, rather than the amount of the fund designated by the parties as punitive damages, could be considered punitive damages. Additionally, as explained later, in most cases, it is unlikely that the risk of punitive damages has a significant effect on settlement decisions. See *infra* notes 207–12 and accompanying text.

157. Of course, plaintiffs who receive favorable jury verdicts also do not get full compensation because an attorney working on a contingent fee basis will receive some portion of the recovery. See, e.g., *Helfend v. S. Cal. Rapid Transit Dist.*, 465 P.2d 61, 68 (Cal. 1970); Denmark, *supra* note 5, at 944 n.70. But the jury reaching the verdict is not informed of that fact and is choosing a number that is designed to represent full compensation. In a settlement, by contrast, there is no pretense that the settling amount constitutes full compensation. Moreover, attorneys’ fees also reduce the plaintiff’s recovery in a settlement. A settlement for fifty cents on the dollar is really less if some portion of that settlement goes to the plaintiff’s attorney.

permissible punitive damages. Some class members may reasonably believe—especially given the arbitrary nature of compensatory- and punitive-damages allocations—that they can get a better deal through individual actions. To bar them from doing so is to force them to accept a payment of punitive damages chosen and agreed to by the parties themselves, and one that is likely to be lower than whatever constitutional limit may apply to those individual cases.

### *B. Settlement and Punishment*

Limited-punishment settlement classes also are inappropriate because settlements do not constitute punishment for purposes of assessing punitive damages. A primary goal of punitive damages is to impose punishment on the defendant and provide retribution to society for the defendant's misbehavior.<sup>158</sup> When a jury awards punitive damages after finding that a defendant engaged in serious wrongdoing, its award represents punishment. By contrast, an agreement by private parties to settle a lawsuit does not constitute punishment in any meaningful sense, regardless of whether the parties label a portion of the settlement as punitive damages. The Supreme Court has described punitive damages as a jury's "expression of moral . . . condemnation,"<sup>159</sup> and a number of commentators have emphasized that punitive damages represent a statement by society as a whole regarding the wrongfulness of the defendant's conduct and the appropriate punishment to be meted out.<sup>160</sup> Thus, punitive damages are not just

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158. See, e.g., *State Farm*, 538 U.S. at 416 (describing the goals of punitive damages as deterrence, retribution, and punishment); Gash, *supra* note 9, at 1669 ("The retribution function is what is commonly referred to as punishment and is a core function of punitive damages." (footnote omitted)); David Luban, *A Flawed Case Against Punitive Damages*, 87 GEO. L.J. 359, 359 (1998) (arguing that the punishment and retribution goals of punitive damages are just as important as deterrence goals).

159. *Cooper*, 532 U.S. at 432; see *IBEW v. Foust*, 442 U.S. 42, 48 (1979) (stating that punitive damages represent community condemnation of "reprehensible conduct" (quoting *Gertz*, 418 U.S. at 350)); see also *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 600 (1996) (Scalia, J., dissenting) ("At the time of the adoption of the Fourteenth Amendment, it was well understood that punitive damages represent the assessment by the jury, as the voice of the community, of the measure of punishment the defendant deserved.").

160. See, e.g., DAVID G. OWEN, PRODUCTS LIABILITY LAW § 18.2, at 1135–36 (2005) (describing punitive damages as a "form of judicial punishment [that] serves to publicize the community's condemnation of flagrant breaches of the rules of proper behavior which reaffirms society's commitment to its moral and legal standards"); Gash, *supra* note 9, at 1669 ("Punitive damages also serve to express the community's sense of outrage, and force the defendant to disgorge much or all of the advantage gained from such conduct."); Sharkey, *supra* note 1, at 380–81 (quoting *Dardinger v. Anthem Blue Cross & Blue Shield*, 781 N.E.2d 121, 145 (Ohio 2002)); Cass R.

punishment; they represent state-imposed punishment that expresses society's rejection and condemnation of the defendant's conduct. According to philosopher Jean Hampton, moral injuries worthy of punishment or retribution—such as the kinds of reprehensible injuries that authorize punitive damages—occur because the transgressor believes that it has greater worth than the victim and that it is entitled to denigrate the victim.<sup>161</sup> Under Hampton's theory, retribution must impose an expressive punishment on the transgressor that elevates the moral worth of the victim and demonstrates that the transgressor has no greater value than the victim.<sup>162</sup>

Settlements do not fulfill these retributive functions. Unlike jury awards, settlements are private agreements.<sup>163</sup> They are not expressions of community outrage. Indeed, a settlement, by its nature, is designed to avoid having an impartial body make a finding of wrongdoing. Moreover, in a settlement, the party purportedly being punished actually helps determine the amount of punishment it will receive. It is one thing for an impartial jury, as a spokesperson for the community, to make findings regarding the defendant's wrongdoing and to render an award of punitive damages that expresses its sense of outrage.<sup>164</sup> It is

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Sunstein, Daniel Kahneman & David Schkade, *Assessing Punitive Damages (with Notes on Cognition and Valuation in Law)*, 107 YALE L.J. 2071, 2075 (1998) (“[P]unitive damages may have a retributive or expressive function, designed to embody social outrage at the actions of serious wrongdoers.”).

161. See Jean Hampton, *Correcting Harms Versus Righting Wrongs: The Goal of Retribution*, 39 UCLA L. REV. 1659, 1677 (1992). For more expanded discussions of Hampton's theory of retribution as it relates to the imposition of punitive damages, see, for example, Marc Galanter & David Luban, *Poetic Justice: Punitive Damages and Legal Pluralism*, 42 AM. U. L. REV. 1393, 1432–35 (1993), Luban, *supra* note 158, at 378–79, and Sebok, *supra* note 132, at 1015–20.

162. Hampton, *supra* note 161, at 1686; see also Luban, *supra* note 158, at 378 (applying Hampton's theory to punitive damages and stating that punishment must inflict “a publicly visible defeat—an *expressive defeat*—on the wrongdoer”); Sebok, *supra* note 132, at 1019 (stating that under Hampton's theory, the punishment component of punitive damages must “establish not only that the victim has value, but that the value judgment contained in the wrongdoer's act was wrong”).

163. Arguably, one could say the same thing about guilty pleas or no contest pleas in the criminal context. Society allows the state to impose punishment on defendants who plead guilty or who plead no contest and do not expressly admit wrongdoing. However, it may be that criminal law simply presents qualitatively different circumstances than a punitive-damages settlement because the state remains intimately involved in the process of carrying out a guilty plea. See *infra* note 185.

164. See Philip Borowsky & Jay Nicolaisen, *Punitive Damages in California: The Integrity of Jury Verdicts*, 17 U.S.F. L. REV. 147, 152 (1983) (“As a group, the jury is in the best possible position to function as the community's conscience. A jury's reactions of shock and outrage presumably mirror those of the community as a whole.”); Hampton, *supra* note 161, at 1694 (“[T]he state is the only institution that can speak and act on behalf of the community . . .”).

quite another to suggest that a settlement agreement devised by private parties, and expressly agreed to by the very defendant against whom punishment is sought, expresses the community's condemnation at all, much less at a level that represents the constitutional upper limit of permissible punitive damages.<sup>165</sup> Because settlement decisions are made by the parties themselves, there is no opportunity for the community to express its disapproval and determine what the appropriate sanction should be.<sup>166</sup>

Nor do settlements typically constitute an expressive defeat of the defendant that equalizes the worth of the defendant and the victim. A settlement is little more than a truce between the parties, that is, an agreement to resolve a dispute rather than any statement about the defendant's wrongdoing. In individual cases, settlements are often confidential, so there is no opportunity for any public expression of wrongdoing. While class action settlements are public documents, in that they must be made available to class members and presented to the court for approval, they also fail to send a public message of wrongdoing. Indeed, in many class action settlements, the defendant will expressly disclaim any wrongdoing and state that it is settling purely to avoid the expenses of litigation.<sup>167</sup> Because the primary factor

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165. There is no question that settlements impose costs on defendants, particularly where they have to make monetary payouts or change their practices. Additionally, the negative publicity accompanying a class action settlement can adversely affect a defendant. See Nagareda, *supra* note 54, at 810–11. *But see* Janet Cooper Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 532 (1991) (suggesting that business defendants see settlement as a way of avoiding the negative publicity of a trial, in part because a settlement will probably not result in any finding of wrongdoing). But suffering adverse collateral consequences is not necessarily the same as suffering punishment for the purposes of punitive damages. Suffering harm is not equivalent to an admission of wrongdoing or of diminished moral worth, nor is it a societal expression of reprehensibility.

166. Not all punishment necessarily must be public punishment. Hampton concludes that “retribution is neither the exclusive, nor perhaps even the primary, responsibility of the state.” Hampton, *supra* note 161, at 1693. Private parties can privately admit wrongdoing and they can make payments to the wronged individual that penalize themselves and elevate the victim. But where punishment is supposed to represent community outrage rather than the personal outrage of the victim, it is not clear that a private agreement fulfills that function, or can fulfill it as effectively as a jury. See *supra* note 164 and accompanying text. And while perhaps a private agreement can constitute punishment where the defendant expresses genuine contrition, that often is not the case as defendants routinely disclaim wrongdoing in class action settlement agreements. See *infra* notes 167–68 and accompanying text.

167. One typical example is the *In re Classmates.com Consolidated Litigation* class action. No. C09-45RAJ, 2011 U.S. Dist. LEXIS 17761 (W.D. Wash., Feb. 23, 2011). The defendants agreed to pay \$9.5 million to settle claims of false advertising and deceptive practices, but stated in the settlement that they “have expressly denied

for assessing the constitutionality of a punitive-damages award is the reprehensibility of the defendant's conduct,<sup>168</sup> it is difficult to see how a settlement can be punitive if the defendant continues to maintain that it did nothing wrong. Moreover, some settlements contain "reverter" clauses in which unclaimed settlement funds are returned to the defendant.<sup>169</sup> Thus, not only can a defendant deny any wrongdoing, but it also may ultimately be able to keep some of the money it agreed to pay as punitive damages. Allowing defendants both to deny wrongdoing and potentially to retain settlement funds further attenuates any connection between a class action settlement and the concept of punishment.<sup>170</sup>

Finally, the manner in which some states have regulated punitive damages reinforces the notion that settlements do not constitute punitive damages. Several states regulate punitive damages either by requiring some portion of punitive damages to be paid to the state rather than to the plaintiff, or by restricting the number of times punitive damages can be awarded against a defendant for a single course of conduct. Many of those statutes, however, apply only to a punitive-damages "award."<sup>171</sup> An "award" implies a judgment by an impartial decision-maker based

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and continue to deny any wrongdoing or legal liability arising out of any of the facts or conduct alleged" in the lawsuit. Class Action Settlement Agreement at ¶ G, I, § 4.1.1, *In re Classmates.com Consol. Litig.*, 2011 U.S. Dist. LEXIS, available at <http://www.cmemailsettlement.com/sa.pdf>.

168. See *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 575 (1996) ("Perhaps the most important indicium of the reasonableness of a punitive damages award is the degree of reprehensibility of the defendant's conduct.").

169. See, e.g., Leslie, *supra* note 21, at 83.

170. This is not to say that defendants cannot disclaim wrongdoing or negotiate reverter clauses. They are certainly entitled to do both. The point here is simply that if they do so, they should not at the same time be able to claim that the settlement constitutes punitive damages for purposes of certifying a non-opt-out class.

171. See, e.g., ALASKA STAT. § 09.17.020(j) (2010) ("If a person receives an award of punitive damages, the court shall require that 50 percent of the award be deposited into the general fund of the state."); FLA. STAT. ANN. § 768.73(2)(a) (West 2005) ("[P]unitive damages may not be awarded against a defendant in a civil action if that defendant establishes, before trial, that punitive damages have previously been awarded against that defendant in any state or federal court in any action alleging harm from the same act or single course of conduct for which the claimant seeks compensatory damages."); GA. CODE ANN. § 51-12-5.1(e)(1) (2000) ("Only one award of punitive damages may be recovered in a court in this state from a defendant for any act or omission if the cause of action arises from product liability, regardless of the number of causes of action which may arise from such act or omission." (emphasis added)); IND. CODE ANN. § 34-51-3-6(b)-(c) (LexisNexis Supp. 2008) (stating that when "a punitive damage award is paid," 75 percent of the award shall be paid to the state); IOWA CODE ANN. § 668A.1(2)(b) (West 1998) (stating that under certain circumstances no more than 25 percent of "punitive or exemplary damages awarded" shall go to the plaintiff, with the rest going to the state).

on evidence and facts, rather than a privately negotiated agreement.<sup>172</sup> In fact, some of these state statutes distinguish awards from settlements.<sup>173</sup>

Although the parties may label a portion of a settlement as punitive damages, it is not clear that those damages serve any punitive function at all. Because settlements do not represent society's condemnation of the defendant's conduct and do not require the defendant to admit wrongdoing, they should not qualify as punitive damages for purposes of binding class members to a settlement and taking away their right to opt out.

### *C. State Action*

A third problem with treating settlement funds as punitive damages for purposes of certifying a mandatory class under Rule 23(b)(1)(B) is that class action settlements for money damages, even though they must be approved by a court, may not constitute state action. The Constitution's limits on punitive damages derive from the Due Process Clause, and the Due Process Clause applies only to state action.<sup>174</sup> Thus, if a settlement is not state action, then any part of the settlement labeled as punitive damages would not count toward the due process limit on punitive damages and could not justify certification of a mandatory limited-punishment class.

Settlements and other private forms of dispute resolution typically do not constitute state action. For example, when parties resolve a dispute through private arbitration rather than through the judicial system, the arbitrator's decision is not state action.<sup>175</sup> Consequently,

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172. See BLACK'S LAW DICTIONARY 157 (9th ed. 2009) (defining "award" as "[a] final judgment or decision, esp. one by an arbitrator or by a jury assessing damages").

173. See, e.g., FLA. STAT. ANN. § 768.28(4) (2005) (providing, in a statute waiving sovereign immunity, that "any state agency or subdivision shall have the right to appeal any award, compromise, settlement, or determination to the court of appropriate jurisdiction"); FLA. STAT. ANN. § 381.785(2) (2007) (allowing third-party subrogation from any "contract, settlement, or award").

174. See *United States v. Morrison*, 529 U.S. 598, 620–21 (2000) (stating that the Fourteenth Amendment applies only to state conduct).

175. See, e.g., *Perpetual Sec., Inc. v. Tang*, 290 F.3d 132, 137–39 (2d Cir. 2002); *Koveleskie v. SBC Capital Mkts., Inc.*, 167 F.3d 361, 368–69 (7th Cir. 1999); *Duffield v. Robertson Stephens & Co.*, 144 F.3d 1182, 1200–02 (9th Cir. 1998); *Davis v. Prudential Sec., Inc.*, 59 F.3d 1186, 1190–92 (11th Cir. 1995); *Dluhos v. Strasberg*, No. 00-CV-3163, 2001 WL 1720272, at \*5, \*11, (D.N.J. Aug. 31, 2001), *aff'd in part*, 321 F.3d 365 (3d Cir. 2003); *Brannon v. Mass. Mut. Life Ins. Co.*, No. 99-3497, 2000 WL 122241, at \*5 (E.D. La. Jan. 31, 2000); *MedValUSA Health Programs, Inc. v. Memberworks, Inc.*, 872 A.2d 423, 428 (Conn. 2005). Additionally, "[n]o state courts have found state action in contractual arbitration." Sarah Rudolph Cole,

when arbitrators have awarded punitive damages and parties have challenged those awards as violating due process, courts have rejected the challenges on the ground that the arbitrator's decision was not state action and therefore could not run afoul of due process.<sup>176</sup>

Although class action settlements are different from individual settlements in that they require judicial approval,<sup>177</sup> judicial review of the settlement is unlikely to convert the settlement into state action. Arbitration awards must be confirmed by a court to become judicially enforceable,<sup>178</sup> yet it is well settled that judicial confirmation of an arbitration award does not turn an otherwise private arbitration award into state action.<sup>179</sup> Outside of the Supreme Court's holding in *Shelley v. Kraemer*<sup>180</sup> that judicial enforcement of a racially restrictive covenant was state action,<sup>181</sup> a holding that has been regarded as an

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*Arbitration and State Action*, 2005 B.Y.U. L. REV. 1, 4 & n.11. By contrast, several scholars have argued that arbitration, particularly court-ordered arbitration, should qualify as state action. *See, e.g.*, Edward Brunet, *Arbitration and Constitutional Rights*, 71 N.C. L. REV. 81, 109–13 (1992); Cole, *supra*, at 5 (arguing that court-ordered arbitration and agency-initiated arbitration is state action while other arbitration is not state action); Richard C. Reuben, *Constitutional Gravity: A Unitary Theory of Alternative Dispute Resolution and Public Civil Justice*, 47 UCLA L. REV. 949, 989–1017 (2000); Jean R. Sternlight, *Rethinking the Constitutionality of the Supreme Court's Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers, and Due Process Concerns*, 72 TUL. L. REV. 1, 40–47 (1997). *But see* Stephen J. Ware, *Punitive Damages in Arbitration: Contracting Out of Government's Role in Punishment and Federal Preemption of State Law*, 63 FORDHAM L. REV. 529, 559–67 (1994).

176. *See, e.g.*, *Davis*, 59 F.3d at 1190–94 (holding that arbitrator's decision was not state action and therefore the arbitrator's punitive-damages award did not violate due process); *MedValUSA*, 872 A.2d at 428 (“We conclude that, because an arbitration award does not constitute state action and is not converted into state action by the trial court's confirmation of that award, an arbitration panel's award of punitive damages does not implicate the due process clause, regardless of how excessive the award may be.”); F. PAUL BLAND, JR. ET AL., CONSUMER ARBITRATION AGREEMENTS: ENFORCEABILITY AND OTHER TOPICS § 11.7.6, at 252 (5th ed. 2007) (collecting cases).

177. *See* FED. R. CIV. P. 23(e).

178. *See* 9 U.S.C. § 9 (2006) (allowing parties to arbitration proceedings to seek judicial confirmation of an arbitration award).

179. *See Davis*, 59 F.3d at 1191–92; *McDaniels v. City of Philadelphia*, 56 F.2d 578, 580 (E.D. Pa. 1999) (“Private actions of an arbitrator are not undertaken under color of state law because the arbitration has been conducted pursuant to a state statute or the arbitrator's award is enforced by a state court.”); *MedValUSA*, 872 A.2d at 429; BLAND ET AL., *supra* note 176, § 11.7.6, at 252 (“Courts generally also find that court confirmation of a private arbitration proceeding is not sufficient state action to trigger due process considerations.”).

180. 334 U.S. 1 (1948).

181. *Id.* at 20.

outlier and as generally confined to its facts,<sup>182</sup> the general rule is that judicial enforcement of neutral private agreements is not state action.<sup>183</sup> A class action settlement is designed by the parties, and although the court must review the agreement under Rule 23(e) to ensure that it is fair, reasonable, and adequate, the court's only job is to accept or reject it.<sup>184</sup> The court's limited role in either approving or striking down a settlement is more akin to "providing contractual agreements with the imprimatur of 'judgments'" than it is to state action.<sup>185</sup> This tenuous connection between settlements and state action reinforces how punitive-damages settlements do not effectively approximate the type of state-imposed punishment that comes from a jury award of punitive damages.

Moreover, even if judicial approval of a class settlement could constitute state action, the fact that individual settlements are not state action may still undermine the justification for a limited-punishment

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182. See Brunet, *supra* note 175, at 111 ("Characterizing a *Shelley*-type court enforcement as state action could be criticized because the case has been interpreted as limited to its facts."); Cole, *supra* note 175, at 11 (describing *Shelley* as "an unusual case that will not likely be repeated"); see also LAURENCE H. TRIBE, *AMERICAN CONSTITUTIONAL LAW* 1711–12 (2d ed. 1988) ("[C]ourts and commentators have characteristically viewed *Shelley* with suspicion.").

183. See, e.g., Cole, *supra* note 175, at 14 (arguing that the Supreme Court has repeatedly rejected the argument that "a court's involvement in enforcing neutral private arrangements is state action"); see also *Miles v. Funk*, 259 F. App'x 335, 336–37 (1st Cir. 2008) (finding that a state court's enforcement of an allegedly unconstitutional settlement agreement was not state action).

184. See *supra* note 150.

185. Judith Resnik, *Money Matters: Judicial Market Interventions Creating Subsidies and Awarding Fees and Costs in Individual and Aggregate Litigation*, 148 U. PA. L. REV. 2119, 2159 (2000). A natural counter-example is plea bargaining in criminal prosecutions. There, the government and the defendant reach an agreement for the defendant to plead guilty, and courts have analogized plea bargains to contracts. See, e.g., *United States v. Garcia*, 606 F.3d 209, 215 (5th Cir. 2010) ("Plea bargain agreements are contractual in nature, and are to be construed accordingly." (quoting *Hentz v. Hargett*, 71 F.3d 1169, 1173 (5th Cir. 1996))). Like in class action settlements, where a judge must determine if the settlement is fair, a judge must approve the plea and must determine that the defendant is pleading guilty voluntarily and that a factual basis exists for the plea. See FED. R. CRIM. P. 11(b). Criminal law differs, however, in that it inherently involves state action. Criminal cases are prosecuted by the state and only the state. There is no private criminal law. Thus, whether a criminal action is resolved by trial or by plea, the state is a party to the case and inextricably involved in it. Cf. *Sanders v. Brown*, 504 F.3d 903, 915 (9th Cir. 2007) (holding that a settlement with a government entity is state action for purposes of the *Parker* antitrust immunity doctrine). Moreover, the punishment imposed through a plea bargain—such as imprisonment or a fine—is necessarily public in nature, as it derives from the state's exclusive authority to define and prosecute crimes, and to restrain the liberty of convicts through incarceration.

mandatory class.<sup>186</sup> To justify a non-opt-out class, there must be a substantial risk that allowing class members to opt out and pursue individual cases would exhaust the constitutional limit on punitive damages.<sup>187</sup> But just as class actions are unlikely to go to trial, individual actions are unlikely to go to trial.<sup>188</sup> A plaintiff who receives a favorable result in a case therefore is much more likely to do so through non-state-action, such as settlement or private adjudication, than through trial. Given these probabilities, it is doubtful that the risk that individual litigation will exhaust the fund of constitutionally permissible punitive damages is high enough to justify joining all plaintiffs in a mandatory class.

Finally, treating class action settlements as state action but individual settlements as private action would create anomalous results. Doing so would mean that the parties could use the class device to manufacture a justification for restricting an individual's ability to pursue his or her own action that would not otherwise exist simply by aggregating individual actions (which are not state action if resolved by settlement or private adjudication) into a single collective settlement (which would be state action). But for the class device, state action would not be present, and no basis would exist for barring individual actions. This approach would appear to violate (a) the requirement that the limit on the fund must exist independently of the class action

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186. Just as judges are not required to review settlements in individual cases, they are not required to review individual side settlements involving class members who object to a class settlement or who otherwise negotiate their own settlement with the defendants. See Katherine Ikeda, Note, *Silencing the Objectors*, 15 GEO. J. LEGAL ETHICS 177, 178 (2001) (citing *Duhaime v. John Hancock Mut. Life Ins. Co.*, 183 F.3d 1, 4 (1st Cir. 1999)).

187. See *In re N. Dist. Cal., Dalkon Shield IUD Prods. Liab. Litig.*, 693 F.2d 847, 852 (9th Cir. 1982) (“Rule 23(b)(1)(B) certification is proper only when separate punitive damages claims necessarily will affect later claims.”); *In re “Agent Orange” Prod. Liab. Litig.*, 100 F.R.D. 718, 726 (E.D.N.Y. 1983) (requiring a “substantial probability—that is less than a preponderance but more than a mere possibility” that individual claims would exhaust the fund), *mandamus denied sub nom. In re Diamond Shamrock Chems. Co.*, 725 F.2d 858 (2d Cir. 1984).

188. See, e.g., Gash, *supra* note 9, at 1665 (“[T]he vast majority of cases filed in American courts are settled before trial.”); Lahav, *supra* note 31, at 389–90 (describing the declining rate of trials and attributing part of the decline to settlements). Statistics from state courts show that only about 3 percent of filed cases go to trial. See COHEN & SMITH, *supra* note 144, at 2; LYNN LANGTON & THOMAS H. COHEN, U.S. DEP’T OF JUSTICE, BUREAU OF JUSTICE STATISTICS, CIVIL JUSTICE SURVEY OF STATE COURTS, 2005: CIVIL BENCH AND JURY TRIALS IN STATE COURTS, 2005, at 9 (2008). See generally Marc Galanter, *The Vanishing Trial: An Examination of Trials and Related Matters in Federal and State Courts*, 1 J. EMPIRICAL LEGAL STUD. 459 (2004) (describing how trial rates have declined over time and how alternative forms of dispute resolution, such as settlement and private adjudication, have increased).

process itself;<sup>189</sup> and (b) the Rules Enabling Act, which states that the federal procedural rules cannot alter a party's substantive rights.<sup>190</sup> Parties should not be able to use the class device to transform private individual lawsuits into state action and then argue that because a class settlement is state action, those individual lawsuits cannot proceed. Because settlements are not state action, and because the due process limits on punitive damages apply only to state action, there is no basis for certifying a class action settlement on a mandatory basis under a limited-punishment theory.

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The fact that class actions typically settle rather than proceed to a jury verdict dramatically transforms the nature of a limited-punishment class action. In the settlement context, where the value of a plaintiff's opt-out right is at its height, it is easy for the parties to manipulate the settlement terms to justify a mandatory class. Settlement enables the parties to self-servingly allocate whatever portion of the settlement they desire as punitive damages without requiring any connection between that allocation and the deterrence and punishment functions of punitive damages. Additionally, although the parties may label some portion of the settlement as punitive damages, that portion does not constitute state-sponsored punishment. It is not punishment because it is not a determination of wrongdoing and in fact typically involves a denial by the defendant of any wrongdoing at all. It is not state action because the settlement is a private agreement among private parties that neither represents a community's sense of outrage at wrongful conduct nor bears the imprimatur of the state. As a result, plaintiffs in limited-punishment settlement classes end up shortchanged because the parties not only control the amount of punitive damages that the class receives, but they do so in a setting where the members of the class cannot opt-out if they are dissatisfied with the result.

## V. OBJECTIONS

Even assuming that the limited-punishment theory has flaws, one might raise several objections to the argument that such classes are improper. First, one might object that the argument against them overlooks the role of the settlement fairness hearing and the fact that

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189. *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 864 (1999) (holding that the limit of the fund must exist independently of the agreement of the parties).

190. 28 U.S.C. § 2072(b) (2006) (stating that federal rules "shall not abridge, enlarge or modify any substantive right").

judges must review class action settlements to ensure that they are fair to class members. According to this objection, a judge reviewing a class action settlement can scrutinize the record to evaluate the degree of the defendant's wrongdoing and to evaluate whether the amount of the settlement fund devoted to punitive damages is fair and is likely to approach the constitutional limit on punitive damages. Second, one could argue that settlements do contain punitive damages because a settlement involving claims for punitive damages will be higher than if the action lacked any punitive-damages claim. A third objection is that eliminating the option of a limited-punishment class ultimately would harm plaintiffs by causing proposed settlements to unravel, which would leave many class plaintiffs with no recovery at all and would keep the multiple-punishment problem intact.

#### *A. Judicial Review of Class Action Settlements*

Class action settlements, unlike individual settlements, do not automatically go into effect and result in dismissal of the underlying action. Rather, the settlement requires the court's approval, and the court can approve the settlement only if the court finds that the requirements of Rule 23 are satisfied and that the settlement is fair, reasonable, and adequate.<sup>191</sup> In evaluating the fairness of a settlement, courts consider a number of factors, including the possibility of fraud or collusion between class counsel and the defendants, the likelihood and range of the potential recovery, the opinions of class counsel, the defendants and the individual class members, the complexity and expense of the case, the chances of success on the merits, and the stage of proceedings at the time of settlement.<sup>192</sup> Given that courts are supposed to scrutinize proposed settlements, one argument in favor of limited-punishment classes is that courts should be able to ensure that the amount the parties designate in a settlement as punitive damages reflects society's interest in punishment and deterrence and bears a reasonable relationship to the defendant's wrongdoing. If a court believes that the parties have settled on an arbitrary number for punitive damages, then it can reject the settlement or refuse to certify it as a mandatory class under Rule 23(b)(1)(B).

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191. See FED. R. CIV. P. 23(e) (requiring court approval of class action settlements); *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 620–21 (1997) (holding that a class settlement must still satisfy the requirements of Rule 23); *Ayers v. Thompson*, 358 F.3d 356, 368 (5th Cir. 2004) (requiring that class settlements be fair, reasonable, and adequate).

192. See, e.g., *Ayers*, 358 F.3d at 369.

Whether or not courts may be able to rigorously review class action settlements in theory, as a practical matter they often lack both the incentive and the capacity to rigorously evaluate the fairness of the settlement and of the parties' allocation of punitive damages. Consequently, courts often will approve questionable settlements and cannot be relied upon to protect class members' rights.<sup>193</sup>

First, no matter how well-intentioned judges may be, they have a strong incentive to approve class action settlements and little incentive to subject them to rigorous review. Judges have crowded dockets and busy schedules, and the opportunity to remove a large and complex case from the docket by approving a settlement is a tempting one.<sup>194</sup> Class actions require a significant investment of judicial time and resources. One study by the Federal Judicial Center found that class actions required anywhere from five to eleven times the work of a non-class action, and that a judge on average spends more than thirty-four hours on a certified class action but less than three hours on a class action settlement.<sup>195</sup> Furthermore, notwithstanding the requirement that class settlements be fair, reasonable, and adequate, courts have created and relied upon a strong judicial policy favoring settlement to support

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193. A number of scholars have described the limitations facing courts reviewing class action settlements. *See, e.g.*, Edward Brunet, *Class Action Objectors: Extortionist Free Riders or Fairness Guarantors*, 2003 U. CHI. LEGAL F. 403, 405–06; Geoffrey C. Hazard, Jr., Lecture, *The Settlement Black Box*, 75 B.U. L. REV. 1257, 1265 (1995); Issacharoff, *supra* note 33, at 808, 829; Alon Klement, *Who Should Guard the Guardians? A New Approach for Monitoring Class Action Lawyers*, 21 REV. LITIG. 25, 45–47 (2002); G. Donald Puckett, *Peering Into a Black Box: Discovery and Adequate Attorney Representation for Class Action Settlements*, 77 TEX. L. REV. 1271, 1279–83 (1999); William B. Rubenstein, *The Fairness Hearing: Adversarial and Regulatory Approaches*, 53 UCLA L. REV. 1435, 1444–45 (2006); Rhonda Wasserman, *Dueling Class Actions*, 80 B.U. L. REV. 461, 474 (2000); John C. Coffee, Jr. & Susan P. Koniak, *Rule of Law: The Latest Class Action Scam*, WALL ST. J., Dec. 27, 1995, at 11 (pointing out that in class actions “[i]ndividual trial judges simply have inadequate incentives to resist parties who want to settle and too little information to recognize when the settlement is collusive”).

194. Alexander, *supra* note 161, at 566 (noting that judges “typically display a strong interest” in seeing large class actions reach settlement); James A. Henderson, Jr., *Comment: Settlement Class Actions and the Limits of Adjudication*, 80 CORNELL L. REV. 1014, 1020 (1995); Leslie, *supra* note 21, at 124 (“[J]udges feel pressure to approve settlements in order to clear their dockets.”); Rubenstein, *supra* note 193, at 1445 (“Judges are also unlikely to police class action attorneys for a third, independent reason: They often have their own vested interest in seeing cases settle. Settlement removes the matter for the judge’s docket, not an unimportant factor in a time of onerous caseloads.”); Ikeda, *supra* note 186, at 190–91 (describing the docket pressures on courts and arguing that they have pushed courts to “accept tainted settlements”).

195. *See WILLGING ET AL.*, *supra* note 144, at 7, 61, 169.

approval of class settlements.<sup>196</sup> Additionally, the trial court may have helped broker the settlement and may have previously granted preliminary approval, giving it a vested interest in seeing the settlement go through.<sup>197</sup>

Thus, courts often give class settlements little scrutiny and are unlikely to reject them, even when they recognize that the settlements are imperfect or even tainted.<sup>198</sup> The Federal Judicial Center study found that twenty-four of twenty-eight settlement-only class actions were approved without changes, and that the other four were approved after the parties made only minor changes.<sup>199</sup> The same study also found that the median length of fairness hearings on class settlements was thirty-eight to forty minutes.<sup>200</sup> Such short hearings suggest that courts are not engaging in exacting scrutiny of proposed settlements.

In addition to lacking the incentive to rigorously scrutinize class settlements, courts also lack the capacity to do so. In the settlement context, courts stand at a significant informational deficit in relation to the parties. Unlike litigation, settlement hearings are non-adversarial. Both the plaintiffs and the defendants want to win settlement approval, and so they will present information to the judge that puts the settlement

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196. See, e.g., *Wal-Mart Stores, Inc. v. Visa U.S.A., Inc.*, 396 F.3d 96, 116 (2d Cir. 2005) (“We are mindful of the ‘strong judicial policy in favor of settlements, particularly in the class action context.’” (quoting *In re PaineWebber Ltd. P’ships Litig.*, 147 F.3d 132, 138 (2d Cir. 1998))); John C. Coffee, Jr., *Understanding the Plaintiff’s Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 714 n.121 (1986) (“Although the case law may require full and elaborate judicial review before a settlement is approved, it is doubtful that courts have much incentive to be very demanding. Their deferential attitude is probably best expressed by one recent decision which acknowledged that: ‘In deciding whether to approve this settlement proposal, the court starts from the familiar axiom that a bad settlement is almost always better than a good trial.’” (quoting *In re Warner Commc’ns Sec. Litig.*, 618 F. Supp. 735, 740 (S.D.N.Y. 1985))).

197. See Alexander, *supra* note 165, at 566; Leslie, *supra* note 21, at 124 (“Because the judge has already preliminarily approved the proposed settlement, she is predisposed to granting final approval of the settlement.”).

198. See, e.g., Susan P. Koniak, *Feasting While the Widow Weeps: Georgine v. Amchem Prods., Inc.*, 80 CORNELL L. REV. 1045, 1056 (1995) (asserting that the district court approved the *Georgine* asbestos settlement, even though it was “tainted,” because it would reduce the docket pressures on the court system); Leslie, *supra* note 21, at 105 (noting that courts routinely approve class settlements over class members’ objections); Richard A. Nagareda, *Turning from Tort to Administration*, 94 MICH. L. REV. 899, 968 (1996) (“[A] court . . . may have an incentive to rubber stamp a mass tort settlement simply to rid itself of such meddlesome claims.”).

199. See WILLGING ET AL., *supra* note 144, at 35.

200. See Coffee, *supra* note 22, at 1348 n.14.

in the best possible light.<sup>201</sup> Judges are not privy to the discovery the parties obtained or to the substance of the parties' settlement negotiations. Nor are they equipped to conduct their own investigation into the facts of the case.<sup>202</sup> In the punitive-damages context, this means that courts have little information that would permit them to independently assess the defendant's wrongdoing and determine an appropriate level of punitive damages, or to question the basis for the parties' allocation of compensatory and punitive damages. The court's limitations are especially glaring in settlement-only actions where the case may have settled at an early stage and the parties may only have engaged in limited discovery. Indeed, courts even have certified limited-punishment settlement classes where the defendants have denied any wrongdoing whatsoever.<sup>203</sup>

Although class members wishing to opt-out of a limited-punishment class can object to the settlement and help create an adversarial atmosphere at the fairness hearing,<sup>204</sup> objectors may not provide a sufficient check against approval of improper settlements. Objectors suffer from the same informational deficits as judges. Objectors often are denied the opportunity to take discovery or access the parties' discovery,<sup>205</sup> and so they may be unable to present evidence demonstrating the unfairness of the settlement. Consequently, while courts sometimes refuse to approve class settlements on the basis of objectors' complaints, in the vast majority of cases they approve class

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201. Brunet, *supra* note 193, at 405–06 (“[A] district judge lacks the incentive, information, and practical ability to effectively monitor class counsel. Under these conditions, the trial court alone cannot realistically be an effective check on the potential abuse that can arise in the class action settlement process.” (footnote omitted)); Leslie, *supra* note 21, at 86 (noting that the settling parties will not want to present negative information to the judge); Judith Resnik, *Judging Consent*, 1987 U. CHI. LEGAL. F. 43, 101 (“[J]udges are ill-equipped to do much other than nod when the litigants join together and seek court approval.”); Rubenstein, *supra* note 193, at 1445; Wolfman & Morrison, *supra* note 44, at 745 (arguing that the non-adversarial nature of fairness hearings makes it difficult for the court to assess the validity of a settlement).

202. Leslie, *supra* note 21, at 86–87 (“In our adversarial system, judges are ill-equipped to investigate and discover evidence against a proposed settlement on their own initiative.”); Nagareda, *supra* note 54, at 782 (“[Fairness] hearings allow the attorneys who engineered the deal to exploit their informational advantage relative to the court through the presentation of witnesses and documentary evidence on the fairness of the settlement.”).

203. See, e.g., *Baker v. Wash. Mut. Fin. Grp., L.L.C.*, No. 1:04-cv-00137-WJG-JMR (S.D. Miss. May 16, 2005), ECF No. 120, at 8, *aff'd*, 193 F. App'x 294 (5th Cir. 2006). In *Baker*, the defendants denied all wrongdoing in the settlement agreement. Opening Brief of Appellants at 8, *Baker v. Washington Mut. Fin. Group, et al.*, No. 05-60572 (5th Cir. Oct. 25, 2005).

204. See, e.g., Brunet, *supra* note 193, at 439–42 (describing how objectors have succeeded in derailing faulty settlements).

205. See *id.* at 408.

settlements over the objections of dissatisfied class members.<sup>206</sup> In short, courts cannot be relied upon to protect absent class members by acting as a check against arbitrary allocations of punitive damages or the risk that the parties will select a punitive-damages amount that falls well below the constitutional limit.

### *B. Settlements Do Contain Punitive Damages*

A second critique of the argument that settlement funds do not constitute punitive damages for purposes of due process is that settlements do account for punitive-damages claims. As one judge stated in discussing the issue of multiple punitive-damages awards in the asbestos context, “the potential for punitive awards is a weighty factor in settlement negotiations and inevitably results in a larger settlement agreement than would ordinarily be obtained.”<sup>207</sup> If it is the case that settlements are larger by virtue of punitive-damages claims, then it may be unfair to ignore the extra payout that class members receive because of the punitive-damages claim. This critique, however, also fails to justify limited-punishment classes.

First, while the notion that settlements resolving punitive-damages claims are larger than they would be if there were no punitive-damages claim is intuitively appealing, it lacks empirical support. Juries award punitive damages in only a very small percentage of cases in which plaintiffs prevail.<sup>208</sup> Additionally, class plaintiffs who litigate to

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206. See Leslie, *supra* note 21, at 105 (stating that “courts consistently approve proposed class settlements over the objections of class members” and that “[c]ourts have approved proposed settlements in over 90% of the cases in which class members filed objections”).

207. *Dunn v. HOVIC*, 1 F.3d 1371, 1398 (3d Cir. 1993) (en banc) (Weis, J., dissenting); see Eisenberg et al., *supra* note 126, at 625 (“The possibility of punitive damages likely shapes the settlement process in which the bulk of cases terminate. Perhaps uncounted thousands of cases settle on terms different than those on which they would otherwise settle because of the possibility of punitive damages.”); Galanter & Luban, *supra* note 161, at 1414 (“[I]n the litigation arising from the Buffalo Creek mine dam disaster, the possibility of punitive damages loomed large in the plaintiff’s investigatory strategy and in the settlement negotiations.”); George L. Priest, *Punitive Damages Reform: The Case of Alabama*, 56 LA. L. REV. 825, 830 (1996) (arguing that it is “obvious and indisputable that a punitive damages claim increases the magnitude of the ultimate settlement” and that it may affect whether or not settlement is achieved at all).

208. Various studies estimate that juries award punitive damages in only two percent to nine percent of pro-plaintiff verdicts. See, e.g., COHEN & SMITH, *supra* note 144, at 6 (finding that juries awarded punitive damages in 6 percent of cases in which the plaintiff won damages); DEFRANCES & LITRAS, *supra* note 149, at 1 (5 percent); LANGTON & COHEN, *supra* note 188, at 1 (5 percent); Denemark, *supra* note 5, at 939 & n.40 (arguing that punitive damages are awarded only rarely); Sebok, *supra* note 132, at 964 (collecting studies and concluding that “factfinders have awarded punitive

judgment seldom receive a favorable verdict.<sup>209</sup> Because of the small risk of a jury award of punitive damages, available data suggests that the potential risk of punitive damages does not induce defendants to settle cases that they would otherwise litigate.<sup>210</sup>

These data do not indicate whether, in cases that do settle, the overall settlement is higher because of punitive-damages claims. Empirical support for this latter proposition, however, also is weak. Although data are limited, one study found that punitive damages provided in settlements were on average just 17 percent of the average punitive damage jury award and that the median punitive damage settlement amount was zero, meaning that many cases settled for no punitive damages at all.<sup>211</sup> The authors of that study concluded that one possible explanation (among several) for this difference is that “[p]unitive awards may not be important in cases that settle.”<sup>212</sup>

Additionally, a statistical regression analysis of punitive-damages awards in states that cap punitive damages versus those that do not failed to show materially different settlement rates.<sup>213</sup> If punitive damages influenced either the likelihood of settlement or the amount of settlement, then one would expect fewer settlements in states that cap punitive damages because defendants in those states face reduced exposure to punitive damages. The fact that the study found no material difference between capping and non-capping states undermines the assertion that punitive damages significantly affect settlement amounts.

Second, even if settlements do include a premium for punitive damages, paying punitive damages via settlement is not the same as imposing punitive damages via a jury verdict. A private agreement to

damages in 2%–9% of all cases where plaintiffs won, and an average of the studies suggests a rate on the low end of the range.”).

209. See WILLGING ET AL., *supra* note 144, at 66 (finding that “no trial resulted in a final judgment for a plaintiff class” in a study of class actions in four federal districts).

210. See, e.g., *Exxon Shipping Co. v. Baker*, 554 U.S. 471, 498 n.15 (2008) (collecting studies showing that the existence of punitive-damages claims does not affect whether or not a case settles); Theodore Eisenberg et al., *Juries, Judges, and Punitive Damages: An Empirical Study*, 87 CORNELL L. REV. 743, 768 (2002) (suggesting that available data does not provide strong support for the proposition that punitive-damages claims induce settlement). *But see* A. Mitchell Polinsky, *Are Punitive Damages Really Insignificant, Predictable, and Rational? A Comment on Eisenberg et al.*, 26 J. LEGAL STUD. 663, 666–69 (1997) (arguing that the risk of punitive damages induces settlement).

211. See Jonathan M. Karpoff & John R. Lott, Jr., *On the Determinants and Importance of Punitive Damage Awards*, 42 J.L. & ECON. 527, 537–40 (1999). Some commentators caution that this data may not be representative and that “further study of this issue is warranted.” Eisenberg et al., *supra* note 210, at 768 n.91.

212. Karpoff & Lott, *supra* note 211, at 540.

213. See Eisenberg et al., *supra* note 210, at 769–70.

forego litigation, including litigation of punitive-damages claims is not equivalent to community-sanctioned punishment. Settlement is merely an expression of the parties' views that a certain resolution for a fixed payment is preferable to the expense and uncertainty of taking a case to trial. It is not a finding of wrongdoing or an expression of the community's distaste with the defendant. A party's decision to settle may be based on other factors, including the time and expense of litigation, the estimated success on the merits, and the makeup of the jury that might hear the case. Settlements reflect the cost-benefit judgments of the parties, not the moral judgments of the community.

Third, concluding that settlements can constitute punitive damages within the meaning of the Due Process Clause is different from concluding that the parties' allocation of compensatory and punitive damages should be dispositive. Because settlements are compromises and generally will not provide full compensation to plaintiffs, the parties' allocation of punitive damages will usually be too high. A settlement fund should constitute punitive damages only where the plaintiff receives greater than full compensation, and even then only the portion of punitive damages that exceeds the compensatory damages sought, rather than the amount labeled by the parties themselves, should qualify as punitive damages.

This does not mean that a class action settlement fund could never qualify as punitive damages. But to do so, the settlement process likely would have to look very different than it does currently, and probably would have to incorporate trial-type procedures. For example, there would have to be something approaching a full evidentiary hearing resulting in a neutral, adjudicatory determination of the defendant's wrongdoing that would provide a basis for assessing the proper level of punitive damages.<sup>214</sup> Such a determination also would require the plaintiffs to conduct sufficient discovery to develop evidence supporting punitive damages. Moreover, defendants would not be able to disclaim wrongdoing in their settlement agreements and still contend that their settlements require them to pay punitive damages. But given that many settlements do not satisfy these criteria, current practices do not support

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214. For example, in the Agent Orange mass tort litigation, in which the district court certified a mandatory punitive-damages class under Rule 23(b)(1)(B), the court appointed a special master to conduct an evidentiary hearing regarding the defendant's assets, the number of likely plaintiff claims and the plaintiffs' possible recoveries to determine the risk that the defendant's assets would be insufficient to pay out all claims. *In re "Agent Orange" Prod. Liab. Litig.*, 100 F.R.D. 718, 727 (E.D.N.Y. 1983), *mandamus denied sub nom. In re Diamond Shamrock Chems. Co.*, 725 F.2d 858 (2d Cir. 1984). Courts could use a similar process to attempt to assess a defendant's wrongdoing and to determine an appropriate amount of permissible punitive damages.

settling punitive-damages claims in a manner that deprives class members of their right to opt out.

*C. A Flawed Settlement Is Better Than Nothing at All*

A third criticism is that restricting or prohibiting the use of mandatory classes for punitive damages will cause potential settlements to unravel. This will leave many plaintiffs who do not wish to bring individual actions without any recovery at all, and will leave the multiple-punishment problem intact by allowing some plaintiffs to obtain windfall awards at the expense of other plaintiffs.<sup>215</sup> According to this view, even if the limited-punishment class may be an imperfect solution, it is better than leaving the multiple-punishment problem untamed.

First, although it is true that parties like mandatory classes, the argument that settlements will fall apart in the absence of mandatory certification is more speculative than real. In fact, in several cases where courts rejected mandatory class certification, the parties ended up settling on an opt-out basis with relief that was as good as or better than the relief provided in the original settlement.<sup>216</sup> Similarly, while defendants often write reservations into settlement agreements that allow them to walk away from the settlement if a certain percentage of class members opt out, they “rarely, if ever,” exercise that right.<sup>217</sup> Instead of destroying settlements, the effect of refusing to certify mandatory punitive-damages classes may be to force the parties to

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215. See, e.g., Perino, *supra* note 38, at 104 (“Like the courts, class action scholars recognize that the ability to opt out may destroy the viability of a class action if the prospect of obtaining large compensatory or punitive awards from sympathetic juries drives large-stakes claimants from the class.”).

216. For example, following the court’s rejection of a mandatory settlement class in *In re Telectronics Pacing Systems, Inc.*, 221 F.3d 870 (6th Cir. 2000), the parties simply entered into an opt-out settlement that still provided class members with valuable relief. See *In re Telectronics Pacing Sys., Inc.*, 137 F. Supp. 2d 985 (S.D. Ohio 2001); see also Wolfman & Morrison, *supra* note 44, at 732 n.19 (citing *Telectronics* to argue that “when a court strikes down a mandatory settlement, the parties may still negotiate an opt-out settlement that provides class members with substantial relief”). Similarly, after the Eighth Circuit rejected certification of a mandatory punitive-damages class in *In re Federal Skywalk Cases*, 680 F.2d 1175 (8th Cir. 1982), the parties settled on an opt-out basis that, according to Judge Scott O. Wright, the district court judge presiding in the case, “permitted the claims of all litigants to be resolved in the same equitable and efficient manner that would have resulted if the mandatory class action had not been vacated.” Scott O. Wright & Joseph A. Colussi, *The Successful Use of the Class Action Device in the Management of the Skywalks Mass Tort Litigation*, 52 UMKC L. REV. 141, 142 (1984).

217. Coffee, *supra* note 70, at 421.

provide better relief to class members so that they choose to stay in the settlement rather than exercise their opt-out rights.<sup>218</sup>

Second, even if eliminating mandatory classes leaves the multiple-punishment problem intact, the limited-punishment cure may be worse than the multiple-punishment disease. If courts take the Supreme Court's punitive-damages jurisprudence seriously and limit individual punitive-damages awards to harm directed toward the individual plaintiffs, then the multiple-punishment problem goes away. Additionally, there are other solutions besides the limited-punishment class that may be fairer to plaintiffs and that do not artificially limit punitive-damages recoveries through arbitrary caps. For example, Professor Jim Gash has proposed a national punitive-damages registry where defendants can report punitive-damages verdicts and settlements, which can then be used as a set-off against subsequent punitive-damages awards to later-suing plaintiffs if the subsequent cases involve the same conduct.<sup>219</sup> While Gash's proposal may still encourage a race to the courthouse, and while Gash may be more willing than I am to treat settlements as containing punitive damages,<sup>220</sup> his proposal would at least require the defendant to identify the wrongful conduct giving rise to punitive damages rather than simply allowing the parties to determine the defendant's punitive-damages liability through agreement and use the number they generate to eliminate class members' opt-out rights. Even if the risk of multiple punishment is a problem, that does not mean that taking away class members' opt-out rights through a limited-punishment class is the right solution.

#### CONCLUSION

Mandatory punitive-damages classes do not serve the purposes of either punitive damages or class actions. Rather, they provide a telling example of how class counsel and class defendants have manipulated class action procedures to restrict class members' opt-out rights. Both

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218. Allowing opt outs may create the risk of "greenmailers" who will threaten to opt out as a way of holding up the settlement and obtaining leverage to exact a favorable side settlement from the parties. But threatening to opt out is unlikely to create effective leverage. Presumably, greenmailers do not want to actually litigate a case on their own; they just want an easy payoff. Thus, the parties could call their bluff and allow them to opt out rather than give in to their demands. It is much more likely that greenmailers will stay in the settlement and object to it—whether or not the settlement allows opt outs—than opt out.

219. See Gash, *supra* note 9, at 1617–18; see also Denmark, *supra* note 5, at 933–34 (proposing a dollar-for-dollar setoff of punitive damages already paid by the defendant in earlier cases arising out of the same course of conduct).

220. See Gash, *supra* note 9, at 1650–53 (proposing that settlements involving punitive damages could be included in the registry).

the Supreme Court's jurisprudence on punitive damages and the realities of class action settlement practice suggest that it is unnecessary to deprive class members of their opt-out rights in order to ensure a fair distribution of punitive damages and protect defendants from excessive punishment. Instead, limited-punishment mandatory classes threaten to impose too little punishment on defendants and to leave plaintiffs not only with fewer punitive damages than they would receive in the absence of a class action but also with an inability to opt out if they feel that they are being shortchanged. Rather than receiving punitive damages that reflect the constitutional upper limit on permissible punitive damages, limited-punishment class members are stuck with an amount of punitive damages chosen by the parties, a number that often carries no meaning and cannot be considered punitive in any true sense. While mandatory punitive-damages classes may serve the interests of defendants and class counsel, they do not serve the interests of the class plaintiffs who have been injured by a defendant's wrongdoing. Since it is those interests that class actions are intended to protect, courts should not certify mandatory punitive-damages classes that deprive class members of their right to opt out.