Balancing Deterrence and Cost Using an Inverse Multiplier: A Modification of the Polinsky-Shavell Model for Punitive Damages.

John F Willems, Mr., Harvard University
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Abstract

States have been dividing punitive damage awards between the government and the plaintiff since the 1980s. However, there has been an academic debate over whether this method of preventing a windfall reduces costs at the expense of deterrence. Polinsky and Che have argued that dividing punitive damages reduces litigation costs by increasing deterrence while decreasing the incentive to bring a suit. Sanchirico and Choi have responded that reducing the recovery of the plaintiff reduces deterrence by discouraging plaintiffs from putting the same effort into lawsuits that defendants do. The effect observed by Sanchirico and Choi can be moderated combining a division of punitive damages between the plaintiff and the state with Polinsky and Shavell’s model of determining the amount of punitive damages based on the likelihood of the defendant escaping liability. After finding the multiplier under Polinsky and
Shavell’s model to determine the amount of punitive damages, we can then use an inverted multiplier to determine what percentage of the damages go to the state. The end result is that as the amount of punitive damages goes up, the take home award of the plaintiff increases while the percentage of the award the plaintiff wins actually decreases. This preserves deterrence while preventing a windfall for the plaintiff and reducing litigation costs.

This process is meant to apply to a class action lawsuit. I propose that it be used at the third stage of a trifurcated trial based on the trial proposed by Judge Jack Weinstein in the case In Re Simon. The first stage would use sampling to determine compensatory damages, which would be distributed according to severity of injury by an insurance fund. The second stage would determine whether a punitive damage award will be awarded based on the reprehensibility of the defendant’s actions. This stage exists to satisfy the substantive due process limits put on punitive damages outlined in BMW v. Gore. Attorney fees will be awarded pro-rata and multiple juries will be used in the course of a trial. A model jury instruction is attached at the end.

Introduction

Punitive damages have never been uncontroversial.¹ Today, the public has grown concerned over the size of punitive damages.² Some have asserted that punitive damages are completely unconstitutional.³ Still others have defended the use of punitive damages on the grounds that “punitive damages can be a useful tool for deterring the wrongdoer and others who are similarly situated from engaging in intentional or willful conduct that may injure others.”⁴ Some have argued that punitive damages serve to “redress the harms caused by defendants who

¹ See, e.g., Fay v. Parker, 1872 WL 4394, 41 (N. H. Dec. 1872) (“The idea is wrong. It is a monstrous heresy. It is an unsightly and unhealthy excrescence, deforming the symmetry of the body of the law.”); Spokane Truck & Dray Co. v. Hoefer, 25 P. 1072, 1075 (Wash. 1891) (“we believe that the doctrine of punitive damages is unsound in principle, and unfair and dangerous in practice.”); Murphy v. Hobbs, 5 P. 119, 122 (Colo. 1884) (“the reflecting lawyer is naturally curious to account for this ‘heresy’ or ‘deformity,’ as it has been termed. Able and searching investigations made by both jurist and writer disclose the following facts concerning it, viz: That it was entirely unknown to the civil law; that it never obtained a foothold in Scotland; that it finds no real sanction in the writings of Blackstone, Hammond, Comyns, or Rutherford; that it was not recognized in the earliest English cases; that the supreme courts of New Hampshire, Massachusetts, Indiana, Iowa, Nebraska, Michigan, and Georgia have rejected it in whole or in part; that of late other states have falteringly retained it because ‘committed’ so to do; that a few years ago it was correctly said, ‘at last accounts the court of the queen’s bench was still sitting hopelessly involved in the meshes of what Mr. Justice Quain declared to be ‘utterly inconsistent propositions;’” and that the rule is comparatively modern, resulting in all probability from a misconception of impassioned language and inaccurate expressions used by judges in some of the earlier English cases.”)
⁴ Shores, supra note 2, at 69.
injure persons beyond the individual plaintiffs in the particular case.”

Others have said that plaintiffs should be allowed to pursue punitive damages as a way to “fine” actors defying their rightful legal obligations, serving essentially on the public’s behalf.

The controversy has been waged on the Supreme Court level in this country. In Browning-Ferris Indus. of Vermont, Inc. v. Kelco Disposal, Inc., Justice O’Connor warned that “[a]wards of punitive damages are skyrocketing.” The Court later found that excessive punitive damages can violate the due process clause of the Fourteenth Amendment. The Court has most recently concluded that “the 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.” Even before this line of cases, Justice Rehnquist had opined that “even assuming a punitive ‘fine’ should be imposed after a civil trial, the penalty should go to the state, not to the plaintiff-who by hypothesis is fully compensated.”

Some states have followed Justice Rehnquist’s suggestion and have diverted part of punitive damage awards to the state by statute. The Ohio Supreme Court, without authorization from a statute, has allocated punitive damages away from a plaintiff and towards “a place that will achieve a societal good, a good that can rationally offset the harm done by the defendants in this case.” Some scholars have argued that punitive damage allocation is unconstitutional.

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12 Dardinger v. Anthem Blue Cross & Blue Shield, 781 N.E.2d 121, 146 (Ohio, 2002).
State supreme courts have struck down allocation statutes on the ground that they are unconstitutional takings.\textsuperscript{14} However, the only federal circuit to review such a law has upheld it.\textsuperscript{15}

While the traditional justification for allocating punitive damages to the state or charity has been to avoid giving a windfall to the plaintiff, Mitchell Polinsky and Yeon-Koo Che have argued that allocating punitive damages away from the plaintiff also has the benefit of lowering litigation costs.\textsuperscript{16} They reasoned that by increasing the amount of damages that defendants pay while lowering the recovery that plaintiffs receive, defendants would take more care while plaintiffs sued less often, leading to lower litigation costs.\textsuperscript{17} However, Choi and Sanchirico have argued that this model creates a risk of under deterrence.\textsuperscript{18} They claim that Polinsky and Che’s model, while reducing litigation costs, also reduces the plaintiff’s incentive to put effort into the litigation, which in turn reduces the probability that the defendant will be held liable.\textsuperscript{19}

My paper first proposes a way to cure Polinsky and Che’s model of such a defect by linking it with Polinsky and Shavell’s model of punitive damages. Mitchell Polinsky and Steven Shavell have argued that punitive damages should be imposed when there is a possibility that the defendant escape liability for committing the tort and that the size of the punitive damage award should depend on the compensatory damages and the probability of escaping liability.\textsuperscript{20} For instance, if there is a 10 percent chance of escaping liability, under Polinsky’s model the multiplier is 1.11. If the compensatory damages are $1 million, the punitive damages should be

\textsuperscript{15} See Engquist v. Oregon Dept. of Agric., 478 F.3d 985, 1002 (9th Cir. 2007) (“Engquist’s interest in her punitive damages award is not a property right cognizable under the Takings Clause, because punitive damages awards are necessarily contingent and discretionary.”)
\textsuperscript{16} Mitchell Polinsky & Yeon-Koo Che, Decoupling Liability: Optimal Incentives for Care and Litigation, 22.4 Rand J. of Econ. 562, 563 (1991)
\textsuperscript{17} Id.
\textsuperscript{19} Id. at 330.
$111,000. Under the scheme I am proposing, 90 percent would go to the plaintiff in this situation, which is approximately $100,000. Now if the chance of escaping liability goes up to 20 percent, the multiplier goes up to 1.25 and the punitive damages would go up to $250,000. The percentage that would go to the plaintiff would decrease to 80 percent, but the absolute amount that goes to the plaintiff actually increases to $200,000.

Next, I propose a trifurcated trial structure based on the model proposed by Judge Jack Weinstein in a class action against tobacco companies in the earlier part of the decade that divided the class action into three phases.21 In the first phase, compensatory damages would be decided by the jury.22 In the second phase, the jury would determine whether the defendants’ conduct warranted punitive damages.23 In the third phase, the jury would determine the amount of punitive damages to be awarded to the class and how they would be allocated.24 Judge Weinstein’s decision was overturned on appeal to the Second Circuit because the limited fund proposed by Weinstein did not meet the necessary criteria for a limited fund.25 The court also held that it was likely unconstitutional for Judge Weinstein to ask the jury to take into account harm done to non-parties when calculating the amount of punitive damages.26 However, the court did not decide on the validity of the trifurcated model. Under Rule 42(b), the court has the right to order separate trials for one or more separate issues, claims, cross claims, counterclaims, or third party claims.27 The basic trial structure laid out by Judge Weinstein is still valid.

The model I am proposing would have the same basic trial structure, but would differ from Weinstein’s model at the different stages. Like Weinstein’s model, my model has three

21 In Re Simon II Litigation, 211 F.R.D. 86, 100 (E.D.N.Y. 2002).
22 Id.
23 Id.
24 Id.
25 See In Re Simon II Litigation, 407 F.3d 125, 138 (2nd Cir. 2005).
26 Id. at 138–139.
phases: one to determine the class wide liability of the defendants to be used as a predicate for
determining punitive damages, another to determine if the defendant’s conduct warranted
punitive damages, and a final trial to determine the amount of punitive damages to be awarded to
the class and how they would be allocated. The first trial would use sampling to determine the
total liability of the defendant. Both sides could negotiate how many trials they would use to
determine this liability, and then multiply the average by the number of class members. The
result would be set aside in an insurance fund to compensate the class members. The second trial
would determine whether the defendant is deserving of punitive damages by considering the
“reprehensibility” of the defendant’s actions. Finally, the third stage would determine the amount
of punitive damages by measuring the likelihood of the defendant escaping liability for similar
actions. The punitive damage award would be allocated by the judge partially to the plaintiffs
and partially to the state based on an inverse multiplier system. All damages awarded for
punishment and not deterrence purposes would go to the state. Attorneys’ fees and other
litigation costs would be divided between the compensatory award and punitive damage award
on a pro rata basis. The percentage of the award to be given to the plaintiffs would be inversely
proportionally to the deterrence multiplier. The number of juries would be determined by the
number of sample trials selected by the parties at phase one. Also, there would be a separate jury
for stages two and three.

I. Calculating and Allocating the Punitive Damage Award

A. Basing the Amount of Punitive Damages on the Likelihood of Escaping Liability

The theory of punitive damages I will use at this stage was outlined by Professors
Polinsky and Shavell in their paper.28 Like them, I believe that punitive damages should

28 Polinsky & Shavell, supra note 20.
primarily serve the purpose of deterrence. They start with the belief that when a defendant will
definitely found liable for the harm for which he is responsible, damages should equal the harm
the defendant has caused.\textsuperscript{29} If damages are less than the harm caused, than firms might take too
few precautions, while if damages are more than the harm caused, than firms might take too
many precautions.\textsuperscript{30} However, sometimes the defendant will be able to escape liability, in which
case imposing damages equal to the harm may significantly under deter the defendant because
the liability the defendant expects is the total harm he or she has caused multiplied by the
probability of being held liable.\textsuperscript{31} To solve this problem, Polinsky and Shavell propose that the
total damages imposed on a defendant should equal the harm multiplied by the reciprocal of the
probability that the defendant will be found liable when he ought to be.\textsuperscript{32} The jury should first
award compensatory damages and then award punitive damages based on the multiplier.

To give an example, assume that total compensatory damages awarded in a lawsuit were
$1,000,000. Let us then assume that there is a 90 percent chance that the defendant will be held
liable. Under Polinsky and Shavell’s model, the damages multiplier is $1/0.9$ or $1.11$. The punitive
damage award in that situation would be $110,000, and the total award would be $1,110,000. If
the defendant has a 25 percent chance of being held liable, then the defendant’s multiplier is
$1/0.25$ or $4$. The total award would be $4,000,000 with punitive damages totaling $3,000,000.

One of the advantages of this model is that punitive damages will rarely exceed
compensatory damages by a 9 to 1 ratio. One of the guideposts the Court has used to determine
whether a punitive damages award meets due process is the ratio between harm to the plaintiff

\textsuperscript{29} \textit{Id.} at 878.
\textsuperscript{30} \textit{Id.} at 879.
\textsuperscript{31} \textit{Id.} at 888–889.
\textsuperscript{32} \textit{Id.} at 889.
and the punitive damages award.\(^{33}\) While the Court has never imposed a bright-line rule, it has said that “in practice, few awards exceeding a single-digit ratio between punitive and compensatory damages, to a significant degree, will satisfy due process.”\(^{34}\) If a defendant under Polinsky and Shavell’s model has a 10 percent chance of being held liable, then the multiplier is 10, meaning that for $1,000,000 of compensatory damages there will be $9,000,000 in punitive damages. In order to get beyond a 10 to 1 ratio, the defendant would have to have less than a 10 percent chance of being held liable. Situations like that may actually be considered an exception to the general rule. The Court has allowed punitive damages awards that exceeded that ratio by quite a bit.\(^{35}\)

**B. Allocating the Punitive Damage Award**

After the jury decides the amount of damages, the court will decide how they will be allocated. Punitive damages can be an undeserved windfall to the plaintiff, particularly if the damages are extremely high. As a result, many states have passed statutes saying that in the event of a punitive damage award only part of the award will go to the plaintiff while the rest will be allocated to the state.\(^{36}\) State supreme courts have allocated punitive damages to the state and non-profit organizations.\(^{37}\) Furthermore, Polinsky and Che have argued that allocating damages in such a way may decrease litigation costs by encouraging more care by defendants while discouraging lawsuits by plaintiffs.\(^{38}\) Pursuant to these arguments, in my model, after the


\(^{34}\) *State Farm*, 538 U.S. at 425.


\(^{37}\) E.g., *Dardinger v. Anthem Blue Cross & Blue Shield*, 781 N.E.2d 121, 146 (Ohio, 2002); *Life Ins. Co. of Georgia v. Johnson*, 684 So.2d 685, 698 (Ala. 1996).

\(^{38}\) Polinsky & Che, *supra* note 16, at 563.
jury has determined the amount of the punitive damage award, the court would allocate part of the award to the state.

Some scholars have disputed Polinsky and Che’s assertions, but my model is different from theirs in an important way. Sanchirico and Choi have argued that Polinsky and Che’s model, while reducing litigation costs, also causes under deterrence because reducing the recovery of the plaintiff gives the plaintiff less incentive to put effort into the litigation, which in turn reduces the probability that the defendant will be held liable.39 My model is different in that the recovery of the plaintiffs actually increases while the percentage of the plaintiffs’ recovery of the punitive damage award decreases. The percentage of the punitive damage award going to the plaintiff has an inverse relation to the damages multiplier determined by the jury. For instance, if the compensatory damage award is $1,000,000 and the jury find that the defendant had a 90 percent chance of being held liable, than the damages multiplier will be 1.11 and the punitive damage award will be $110,000. In that situation, the plaintiffs would receive 90 percent of the punitive damage award, which is $99,000. If the jury found that the defendant had an 80 percent chance of being held liable, than the multiplier would be 1.25 and the punitive damage award would be $250,000. Of that award, 80 percent would go to the plaintiffs, which would be $200,000. The percentage of the punitive damage award going to the plaintiffs mirrors the likelihood of the defendant being held liable.

39 Sanchirico & Choi, supra note 18, at 330.
<table>
<thead>
<tr>
<th>Chance of escaping liability</th>
<th>Multiplier</th>
<th>Punitive Damages</th>
<th>Percentage going to plaintiff</th>
<th>Amount going to plaintiff</th>
</tr>
</thead>
<tbody>
<tr>
<td>10%</td>
<td>1.11</td>
<td>$111,000</td>
<td>90%</td>
<td>$100,000</td>
</tr>
<tr>
<td>20%</td>
<td>1.25</td>
<td>$250,000</td>
<td>80%</td>
<td>$200,000</td>
</tr>
<tr>
<td>30%</td>
<td>1.43</td>
<td>$428,571</td>
<td>70%</td>
<td>$300,000</td>
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<tr>
<td>40%</td>
<td>1.66</td>
<td>$666,000</td>
<td>60%</td>
<td>$400,000</td>
</tr>
<tr>
<td>50%</td>
<td>2</td>
<td>$1,000,000</td>
<td>50%</td>
<td>$500,000</td>
</tr>
<tr>
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<td>2.5</td>
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<td>40%</td>
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</tr>
<tr>
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<td>3.33</td>
<td>$2,330,000</td>
<td>30%</td>
<td>$700,000</td>
</tr>
<tr>
<td>80%</td>
<td>5</td>
<td>$4,000,000</td>
<td>20%</td>
<td>$800,000</td>
</tr>
<tr>
<td>90%</td>
<td>10</td>
<td>$9,000,000</td>
<td>10%</td>
<td>$900,000</td>
</tr>
</tbody>
</table>
It could be argued that there is still a problem of under deterrence, although it is a smaller one. Because the plaintiff is not eligible for a windfall, the plaintiff will still not invest as much to secure the judgment as the defendant does to avoid it. This may be true, but deterrence has to be balanced against other objectives such as lowering litigation costs and preventing a windfall to the plaintiff. As I said earlier, these factors must be balanced against each other.

Some objections have been made to allocation on the basis that they violate the Constitution. State supreme courts have struck down such laws as unconstitutional takings of property.\(^{40}\) Bethany Rabe has argued that turning punitive damages over to the state converts them into civil fines subject to the Excessive Fines Clause.\(^ {41}\) Rabe has also argued that punitive damages are “essentially criminal in nature” and that due process is offended when they are handed out without the procedural safeguards of the criminal system.\(^ {42}\)

The Utah Supreme Court in Smith v. Price Development Co. did not strike down allocation of punitive damages as unconstitutional in itself. The court distinguished the provision at issue from those upheld in other states that gave the state an interest in the judgments.\(^ {43}\) Other courts have upheld allocation statutes even if they do not give the state an interest in the judgment on the basis that a punitive damage award does not become property until it accrues to the plaintiff.\(^ {44}\) The Ninth Circuit, the only federal circuit to consider this question, found that an interest in a punitive damage award is “not a property right cognizable under the Takings Clause,

\(^{41}\) Rabe, supra note 13, at 346.
\(^{42}\) Id. at 350.
\(^{43}\) Price Development Co., 125 P.3d at 951.
\(^{44}\) See e.g. State v. Carpenter, 171 P.3d 41, 68 (Alaska, 2007) (“an unlitigated claim does not have ‘property’ until after it accrues”); DeMendoza v. Huffman, 51 P.3d 1232, 1246 (Or., 2002) (“We therefore hold that plaintiffs do not have a vested prejudgment property right in punitive damages.”)
because punitive damage awards are necessarily contingent and discretionary.”\textsuperscript{45} The plaintiff does not have a property interest in the punitive damage award until final judgment is entered. In this model, the allocation is part of the final judgment. A plaintiff objecting to this allocation cannot claim a property interest because at that time it has not been vested in the plaintiff.

The court also decided that the allocation statute did not turn the punitive damages into fines reviewable under the Excessive Fines Clause.\textsuperscript{46} The court found that the Clause “applies only to government acts that are intended to punish, and the split-remedy scheme is not intended to punish Engquist.”\textsuperscript{47} It is true that the Supreme Court in \textit{Browning-Ferris Indus. of Vermont, Inc. v. Kelco Disposal, Inc.} did not decide whether the Excessive Fines Clause applies just to criminal cases, limiting its ruling to punitive damages in a civil suit where the government does not prosecute the action and has no share in the damages.\textsuperscript{48} The Court, however, reviewed history and concluded that “the primary focus of the Eighth Amendment was the potential governmental abuse of its ‘prosecutorial’ power, not concern with the extent or purposes of civil damages.”\textsuperscript{49} The Excessive Fines Clause applies to money taken from a defendant pursuant to government’s prosecutorial role, not in private suits.

It could be argued that a court does not have the right allocate funds like this unless authorized to do so by the statute. While the court in \textit{Dardinger v. Anthem Blue Cross & Blue Shield} allocated punitive damages on its own accord to a charitable organization,\textsuperscript{50} Justice Moyer, dissenting in part, wrote that “every American court that engages in the alternative

\textsuperscript{45} \textit{Engquist}, 478 F.3d at 1002.
\textsuperscript{46} \textit{Id.} at 1006.
\textsuperscript{47} \textit{Id.}
\textsuperscript{49} \textit{Id.} at 266.
\textsuperscript{50} 781 N.E.2d at 146
distribution of punitive damages awards has acted pursuant to statutory authorization.”

Allowing courts to redistribute damages without legislative authorization gives judges too much discretion and is best left to the legislative branch of government, he said.

However, courts should be able to institute this allocation without legislative authorization because the “broad power to shape and effectuate remedies is deeply rooted in the common law system.” Punitive damages are themselves an outgrowth of the common law system. As such, courts have “the inherent authority to allocate punitive damages awards without legislation directing such allocation.” Recently, federal courts have created remedies such as supervising mental institutions, prisons, and school systems, so the power of courts to shape remedies in the area of public law litigation is “no longer seriously questioned.” Even the dissenter in Dardinger admitted that the court had the power of remitter over the amount of awards.

Federal courts have used this power to shape remedies in similar ways before. The court in Bebchick v. Public Utilities Commissioner decided that a fare increase by the D.C. Transit System was unwarranted, but decided it was “not feasible to require refunds to be made to individuals who paid the increase.” Instead, the extra money that was collected would be set aside in a fund to be used by the public utilities commission. The Eleventh Circuit in Nelson v. Greater Gadsden Housing Authority upheld a district court order that directed any unclaimed

52 See id. at 147–148.
54 See Shores, supra note 2, at 63–64.
55 Id. at 90.
56 Id. at 91.
59 Id. at 203–204.
compensatory damages to be used by the defendant to increase the energy efficiency of their apartment units or improved the appliances within the apartment.60

C. Damages Awarded for Punishment

Polinsky and Shavell also allow, in their model, for juries to award punitive damages in order to fulfill the “punishment objective.”61 They leave open the possibility for the jury to award damages purely for the sake of punishment. I would like to leave this option open for the jury, but I am nervous about the incentives it would have on the plaintiff. Given the reverse multiplier I outlined earlier, I have the concern that the plaintiff may wish to emphasize punishment while deemphasizing the likelihood of escaping liability. In doing so, the plaintiff would increase the total punitive damage award while keeping his or her share of the award constant. Therefore, if the jury decides to award addition punitive damages purely for punishment, then all of those damages should go to the state. Ideally, no such damages would be given at all because the combined compensatory and punitive damages should be sufficient to punish a firm that has committed a mass tort.

II. The Trifurcated Trial Structure

As stated earlier, I will situate this system of punitive damages in the middle of a trifurcated trial structure. The model for punitive damages will be used at Phase III when the amount of punitive damages will be decided. At Phase I a sampling system will be used to determine the aggregate punitive damage award and then distribute it. At Phase II, the jury will decide whether the defendant’s behavior is sufficiently reprehensible to merit punitive damages.

A. Using Sampling to Determine Compensatory Damages At Phase I

60 802 F.2d 405, 409 (11th Cir. 1986).
61 See Polinsky & Shavell, supra note 20, at 949–950 (“Notwithstanding these reservations, it is possible that individuals do want to personify firms and punish them as entities, and the reader can make up his or her mind about the importance of this way of defining the punishment objective. To the extent that it is important, the imposition of punitive damages on a blameworthy firm directly promotes the punishment objective, much as it does when the defendant is a culpable individual.”).
Sampling has been used by courts to deal with class actions with a large number of class members in order to reduce the time and cost of determining liability. It involves trying a few cases within the class, using them to find an average liability, and then extrapolating the liability to the other members of the class. Appellate courts are divided on its permissibility. Using traditional trials to process these claims entails great expense in terms of litigation costs, insurance deductibles, and time.

Sampling produces a more accurate outcome because the average represents the true worth of a lawsuit more than any given award by a jury. Any given award in a traditional trial is likely to be an over or under-award relative to the true worth of the suit as shown in the average award, and individual awards can vary due to “random noise in decision making” as much as legally relevant distinctions. Sampling also meets the requirements of due process because the liability imposed by sampling is not significantly more than traditional trials would impose and there is little or no risk of erroneous deprivation of the defendants’ property. Sampling may also serve such non-instrumental values such as equality before the law, predictability, transparency, rationality, and revelation, though other non-instrumental values such as the right of the plaintiff to communicate his or her own views may be compromised. However, plaintiffs and their lawyers in mass tort cases communicate very little to begin with.

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63 Compare Hilao, 103 F.3d at 786 with Cimino v. Raymark Indus., 151 F.3d 297, 321 (5th Cir., 1998).
66 Id. at 836.
67 Id. at 828.
68 Id. at 832.
and plaintiffs have very little control to begin with.69 Put simply, “the goals of corrective justice are better achieved” through sampling than through traditional trials.70

Sampling has the added benefit, however, of reducing litigation costs by reducing the number of trials used to determine liability. In my model, the court in the first stage would utilize a sampling method proposed by Prof. David Rosenberg called “average claim sampling.”71 Under Rosenberg’s method, the parties negotiate on the number of claims that are part of the sample and then choose a number.72 If the two sides cannot agree on a number, both sides would file their respective ideal number claims for sampling with the court, and the court would select the higher number.73 After a number is chosen, “the court randomly selects the party-designated number of claims from among the relevant pool of claims and resolves each selected claim by judgment or settlement as it normally would be resolved.”74 The defendant’s aggregate liability and damages are then determined according to the average of the resulting outcomes.75 The defendant’s aggregate liability and damages “results directly from multiplying the average of the sample claim outcomes by the total number of claims in the relevant pool.”76 To put the idea in practice, in a hypothetical class action of thousands of class claimants, the defendants and the plaintiffs agree to a sample size of three. The court selects three class members representing the high, low, and moderate sized claims. The trials are held and the three claims are found to be worth $300, $200, and $100. The liability would be added up and averaged to create an average liability of $200. This average liability would be then be multiplied by the number of class members to determine the total liability of the defendant.

69 Id. at 840.
70 Id. at 836.
71 Rosenberg, A New Sampling Method, supra note 64.
72 Id. at 3.
73 Id. at 3, fn. 7.
74 Id. at 3.
75 Id.
76 Id.
The chief virtue of this system is that it saves litigation expenses “while preserving the deterrence, compensation, and other functions of a civil liability regime.”\textsuperscript{77} While some courts have complained that sampling should not be used if it cannot approximate the result that would be determined in separate trials in order to implement the proper deterrence, Rosenberg argues that it is the ex ante probable liability that matters in deterrence.\textsuperscript{78} This system only affects the defendant’s aggregate liability and damages and does not affect the compensation of the plaintiffs, which will be decided in separate proceedings.\textsuperscript{79} If compensation is decoupled from aggregate liability, as is being proposed here, the defendant should not care how compensation occurs. In addition to reducing costs, average claim sampling also has the advantage of being a simple model that is easy to understand so the total liability can be determined by courts quickly. Whatever the benefits of average claim sampling, in order to apply it the court must accept the legal reasoning behind sampling, which, as noted earlier, the courts are divided on. The Fifth Circuit, when deciding \textit{Cimino v. Raymark Industries},\textsuperscript{80} decided that the case before them was distinguishable from \textit{Hilao} because the suit in \textit{Hilao} was a suit under the Alien Tort Claims Act and did not operate under the restraint of the Rules of Decision Act or \textit{Erie}.\textsuperscript{81} \textit{Cimino} involved a sampling scheme divided into three phases where there would be a complete jury trial for ten class representatives and a class-wide determination of issues such as product defectiveness, warning, and punitive damages in the first phase, the exposure on a craft and job site basis was stipulated to in the second phase, and 160 different sample cases would be tried to determine an average which would then be extrapolated to the rest of the class.\textsuperscript{82} Because there

\textsuperscript{77} \textit{Id.} at 4.  
\textsuperscript{78} See \textit{id.} at 7–10.  
\textsuperscript{79} \textit{Id.} at 4.  
\textsuperscript{80} 151 F.3d 297  
\textsuperscript{81} \textit{Id.} at 319.  
\textsuperscript{82} \textit{Id.} at 299–300.
was no attempt to prove causation in the phase three judgments or the extrapolation cases, the court found that the judgments were “fatally flawed.”

However, average claim sampling is different from the model imposed in *Cimino* because the plan in *Cimino* involved the court choosing the sample size of 160 based on information provided by the plaintiffs. In average claim sampling, the two parties would negotiate the size of the sample or, if they could not reach an agreement, submit the desired sample size to the court and allow the court to pick the bigger sample. In reaching an agreement, both parties would be waiving their right to challenge the other cases on the basis of causation or damages because they did so voluntarily. If one party utterly refuses to allow any sampling, then it can simply submit to the court that the desired number of trials is the same as the number of class members, and under this model the court would be obligated to try each of those cases. If the parties cannot agree and one party submits a higher number to the judge that is lower than the total class size, than both sides have waived their legal rights to challenge the results based on the untried cases. One party could insist on trying every case, but given the accuracy of a good sample at determining liability and the high litigation costs that would come with doing this, it is unlikely that either party would view that as a rational option.

**B. Setting Aside Compensatory Damages into an Insurance Fund Judgment**

After the total compensatory damages award against the defendant has been determined, the damages would be set aside into an insurance fund by order of the court. The court would, in order to advance the goal of optimal insurance, distribute damages to class members according

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83 *Id.* at 321.
84 *Id.* at 303.
85 This idea has also been proposed by David Rosenberg in *Decoupling Deterrence and Compensation Functions in Mass Tort Class Actions for Future Loss*, 88 Va. L. Rev. 1871 (2002).
to the relative severity of their loss rather than the relative strength of their legal claims.\textsuperscript{86} This is preferable to how plaintiffs are typically compensated because “ex ante, the risk-averse individual in need of tort insurance rationally prefers that the legal system award damages according to severity of harm.”\textsuperscript{87} Plaintiffs rationally do not want compensation to reflect the defendant’s causal responsibility, governing law, and competence of counsel.\textsuperscript{88} Defendants should not care how the liability is distributed after it is established because it does not affect them if the total number stays the same. Each insurance fund judgment will likely vary from case to case, and there are several options for adapting the insurance funds on a case by case basis.\textsuperscript{89}

This may offend the law in the Second Circuit on the basis that it is considered “fluid recovery” which the Second Circuit has found to be “to be illegal, inadmissible as a solution of the manageability problems of class actions and wholly improper.”\textsuperscript{90} The concept of “fluid recovery” is that when the court decides that there is no conceivable way in which many of the individual claimants can be paid, the class as a whole is substituted for the claimants and claims for compensation are filed after liability is determined.\textsuperscript{91} Any leftover funds in the Eisen case were to be used for the benefit of all odd-lot traders by reducing the odd-lot differential (Eisen was an antitrust case brought by an odd-lot investor against two brokerage firms and the New York Stock Exchange).\textsuperscript{92} The court found that this concept was not permitted by Rule 23, and even if it was, it violated due process.\textsuperscript{93}

\begin{itemize}
\item \textsuperscript{86} Id. at 1876.
\item \textsuperscript{87} Id. at 1885.
\item \textsuperscript{88} Id.
\item \textsuperscript{89} See Id. at 1896–1900.
\item \textsuperscript{90} Eisen v. Carlisle & Jacquelin, 479 F.2d 1005, 1018 (2\textsuperscript{nd} Cir. 1973).
\item \textsuperscript{91} Id. at 1010.
\item \textsuperscript{92} Id. at 1011.
\item \textsuperscript{93} Id. at 1018.
\end{itemize}
However, other courts have addressed fluid recovery schemes and come to opposite conclusions.\textsuperscript{94} The court in \textit{Nelson v. Greater Gadsden Housing Authority} found it proper that any compensatory damages that were not claimed to be used by the Greater Gadsden Housing Authority to increase the energy efficiency of their apartment units or to improve the defendant-supplied appliances within the units.\textsuperscript{95} The court noted that “objections to fluid recovery appear to relate to the use of this system to relieve plaintiff classes of the burden of proving individual damages or to avoid the dismissal of unmanageable class actions.”\textsuperscript{96} Someone could object that because of the presence of sampling, individual damages are not being proven here, but once again the sampling is voluntary so any objection either the plaintiff or defendant might have against it has been waived. Furthermore, the defendant has no reason to object to the distribution of the money because it has no effect on the defendant’s total liability. The Second Circuit has allowed fluid recovery when it was part of a voluntary settlement.\textsuperscript{97} The court in \textit{Windham v. American Brands Inc.}, rejected fluid recovery, but only because the suit was Sherman Act anti-trust suit and the court could not find such recovery contemplated in the statute.\textsuperscript{98}

\textbf{C. Deciding Whether to Award Punitive Damages at Phase II}

In the second phase of the litigation the jury will decide whether the defendant’s actions are worthy of punitive damages. The standard that the jury will use to make this determination is “reprehensibility.” To determine reprehensibility, the jury will be allowed to use any number of factors they would not be allowed to or should not use when determining the amount of damages. This stage serves the dual purpose of satisfying due process while at the same time

\textsuperscript{95} 802 F.2d at 409.
\textsuperscript{96} \textit{Id.}
\textsuperscript{97} \textit{State of West Virginia v. Chas. Pfizer Co.}, 440 F.2d 1079, 1092 (2nd Cir. 1971).
\textsuperscript{98} 565 F.2d 59, 66 (4th Cir, 1977).
satisfying corrective justice concerns about the use of punitive damages. If the jury finds at this stage that punitive damages are not warranted, then the trial ends here.

When the Supreme Court first held a punitive damage award unconstitutional in *BMW v. Gore*, the Court found that “elementary notions of fairness enshrined in our constitutional jurisprudence dictate that a person receive fair notice not only of the conduct that will subject him to punishment, but also of the severity of the penalty that a State may impose.”99 The Court outlined three “guideposts” to determine when a punitive damage award exceeds what the defendant had adequate notice to expect: the degree of reprehensibility, the disparity between the harm or potential harm suffered by the plaintiff and the punitive damage award, and the difference between this remedy and the civil penalties authorized.100 Of these factors, the Court found that the degree of reprehensibility was “perhaps the most important indicium of the reasonableness of a punitive damages award.”101

Phase II presents the opportunity to consider multiple theories about punitive damages because the main factor at Phase III will be the likelihood of the defendant escaping liability. The Court has said elsewhere that “it is appropriate to consider the magnitude of the potential harm that the defendant’s conduct would have caused to its intended victim if the wrongful plan had succeeded, as well as the possible harm to other victims that might have resulted if similar future behavior were not deterred.”102 Potential harm could be a factor considered at Phase II because it would have no influence on Phase III. In *Pacific Mutual Life Ins. Co. v. Haslip*, the Court approved a test by the Alabama Supreme Court that allowed the jury to consider “the profitability of the defendant of the wrongful conduct,” “the ‘financial position’ of the

100 *Id.*.
101 *Id.* at 575.
102 *TXO*, 509 U.S. at 460.
defendant,” “all the costs of litigation,” “the imposition of criminal sanctions on the defendant for its conduct,” and “the existence of other civil awards taken against the defendant for the same conduct.”103 All of these factors could be considered by the jury at Phase II.

In previous cases, the Court has held firmly that juries may not punish defendants for harms done to non-parties of the suit.104 However, while the jury may not punish defendants for harming nonparties directly, they are allowed to consider harms done to nonparties when determining reprehensibility.105 This creates a bit of a paradox because the jury is allowed to consider harms to nonparties when determining reprehensibility, which is the most important factor when reviewing the propriety of a punitive damages award. However, they are not allowed to base the amount of punitive damages off of harms done to other parties. It appears as if the Court is trying to have it both ways. However, by separating the reprehensibility analysis from the amount of the award by trifurcating the trial, this danger of confusing the jury is greatly reduced. Because the amount of punitive damages will not be decided at this stage, the jury can consider harms done to nonparties without invalidating the award.

III. Miscellaneous Concerns-Attorneys Fees and the Number of Juries

I have laid out the basic outline of the trial format along the lines similar to Judge Weinstein’s model. However, there are several overarching areas that need to be addressed. Namely, the payment of attorneys’ fees, the use of juries, and the review of the final punitive damage award by the judge will be addressed in this next section. Attorneys’ fees will be paid pro rata from the entire award both compensatory and punitive regardless of the ultimate

104 See e.g., Philip Morris USA v. Williams, 549 U.S. 346, 355 (2007) (“a jury may not ... use a punitive damages verdict to punish a defendant directly on account of harms it is alleged to have visited on nonparties.”); State Farm, 538 U.S. at 422 (“A defendant’s dissimilar acts, independent from the acts upon which liability was premised, may not serve as the basis for punitive damages.”).
105 Philip Morris USA, 549 U.S. at 355
recipient. Multiple juries will be used at the different phases of the trial both to keep the purpose of each phase distinct from the next and to reduce the workload for each jury.

A. Attorneys’ Fees to Be Paid Pro-Rata Across the Award

To prevent counsel from emphasizing one phase over another, attorneys’ fees will be paid pro-rata from the compensatory damages. The fees will be taken both from the government’s and the plaintiffs’ share of the punitive damage award. The Court has found that “a litigant or a lawyer who recovers a common fund for the benefit of persons other than himself or his client is entitled to a reasonable attorney’s fee from the fund as a whole.”106 Attorneys who secure such a common fund may take an award from it as long as the benefits of the class recovery have been traced with some accuracy and the costs of recovery have been shifted with some exactitude to those benefiting, the common-fund doctrine will allow an attorney’s fee to be taken from the whole fund.107 The Alaska Supreme Court has approved taking money from the state’s share of a punitive damage award without while simultaneously upholding the allocation statute.108 There is no contradiction in allocating money to the state while allowing the attorney to take money from that portion for his or her fee. The benefits of the state’s recovery can be traced to the work of the attorney, so this should fit under the common-fund doctrine.

B. Multiple Juries Will Be Used with Different Juries at Each Phase

While juries may be more reliable in determining damages than conventional wisdom commonly assumes,109 it is not advisable to use the same jury to try all cases in case a particular jury has a tendency to give too high or too low of awards.110 Furthermore, in a sampling situation it may be difficult for a single jury to hear all cases, particularly since it would be better to try

107 Id. at 480–481.
108 Carpenter, 171 P.3d at 69.
110 Id.
several cases at once in the interest of timeliness. For example, in Hilao the sample size was 131. For a single jury to try 131 cases is likely to both exhaust the jury and skew the results in the direction of that jury’s particularities. Furthermore, having separate juries at the second and third phases of the trial further serves the purpose of separating the distinct purposes of each phase. Certain factors the jury is allowed to consider at Phase II are forbidden at Phase III, and if the same jury decided both issues then there might be some bleeding of one phase into another.

It has been argued that having multiple juries violates the Seventh Amendment right to a jury trial because all interrelated issues must be tried before one jury in case one jury re-examines the finding of another. The Seventh Circuit has found that “the judge must not divide issues between separate trials in such a way that the same issue is reexamined by different juries.” In the Rhone-Poulenc Rorer case, the court found that the use of multiple juries was inappropriate because the first jury would be used to decide whether the defendant was negligent and subsequent juries would decide issues that pertained to the negligence of the defendant such as comparative negligence of the plaintiff and proximate causation.

The multiple juries here would not be considering the same question, however. The juries finding fact at Phase I would only be deciding questions pertaining to the individual trials they are adjudging. The juries in Phases II and Phases III would not reconsider the size of the compensatory damage award. The jury at Phase II will consider the reprehensibility of the defendant’s actions and the other factors I have mentioned while the jury at Phase III will only consider the likelihood of the defendant escaping liability. Different issues will be decided at each stage, and each jury in the sampling stage will not reconsider the findings of another jury.

111 103 F.3d at 783.
113 In the Matter of Rhone-Poulenc Rorer Inc., 51 F.3d 1293, 1303 (7th Cir. 1995).
114 Id.
It could be argued that there is a signaling problem here in that the jury at Phase III could take the positive result at Phase II as evidence that non-parties were harmed and inflate the amount of the award at Phase III. The solution is to keep the juries ignorant about the overall structure of the trial. The jury at Phase III will not see the jury instructions the jury at Phase II received and will not know what factors that jury was allowed to consider. The Court in *Phillip Morris* found that the judge’s refusal to instruct the jury not to punish the defendant for harm done to non-parties was what violated due process.115 Here the jury is being instructed not to consider harms done to non-parties, so this should satisfy that court that improper considerations are not being made.

**Conclusion**

In summation, each phase of the litigation works to achieve specific goals in the class action suit. Phase I exists to determine the required compensation and to set the compensatory award that will serve as the basis of any future punitive awards. Sampling will be used at this level to lower litigation costs. Phase II will be used to establish a base level of reprehensibility to satisfy due process and corrective justice views of punitive damages. Without establishing a basis of reprehensible behavior or “societal damage” the law suit will likely never reach Phase III. Phase III will then be used to enforce optimal deterrence and allocate the windfall in a way to create the proper incentives to pursue the suit.

Providing proper deterrence, maintaining due process, and reducing litigation costs is a balancing act. However, there is a way to do all three, as I have outlined here. There may be, at times, a need to balance one objective against the other. For instance, it may not comport with optimal deterrence to force the plaintiff to prove reprehensibility at Phase II before employing Polinsky and Shavell’s model at Phase III. However, Phase II is necessary to ensure that the

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115 *Phillip Morris*, 549 U.S. at 350–351.
punitive damage award is on solid constitutional ground. Furthermore, the balance between reducing litigation costs and ensuring optimal deterrence can be struck by ensuring that recovery goes up but not to the same extent as the punitive damage award overall. It could be argued that ensuring that the plaintiff puts in the optimal effort into the suit requires giving the plaintiff the full award, but this concern must be balanced against other concerns of giving the plaintiff and underserved windfall and encouraging speculative litigation. At the same time, some of the punitive award must be given to the plaintiff to encourage the plaintiff to through with this model. The model I have outlined assumes the structure of a class action and is not applicable to traditional individualized trials.

Appendix

Sample Jury Instructions

Phase I

These instructions will determine the amount of compensatory damages suffered by the plaintiff. In considering the imposition of compensatory damages, you should only consider the damages needed to fully compensate the plaintiff as a whole. This determination will be made by averaging out the claims made by individual class members in the trials you have witnessed. The compensatory damages should not be based on

1. The reprehensibility of the defendant’s conduct;
2. The net income or worth of the defendant;
3. The potential harm that might have been caused by the defendant;
4. The litigation costs that have been born by the plaintiff;
5. The gain or profit the defendant might have obtained from the harmful conduct, whether the harm included your personal injury;
6. The harm done to non-class members.
In assessing the damages to which the plaintiffs are entitled you may take into account any of the following that you believe from the evidence have resulted from the defendant’s action.

1. Any bodily injuries sustained and the extent and duration thereof;
2. Any effect of such injuries upon the health of the plaintiffs according to its degree and probable duration;
3. Any physical pain and mental anguish suffered by the plaintiffs in the past, and any that may be reasonably expected to be suffered by them in the future;
4. Any disfigurement or deformity resulting to them and any humiliation or embarrassment associated therewith;
5. Any inconvenience and discomfort caused in the past and any that will probably be caused in the future;
6. Any doctors, hospitals, nursing, and medical expenses incurred in the past and that may reasonably be expected to occur in the future;
7. Any loss of earning in the past by reason of being unable to work at his calling;
8. Any loss of earnings or lessening of earning capacity he may reasonably be expected to sustain in the future;
9. Damage to the property of the plaintiff as a result of the defendant’s actions.

From these as proven by the evidence your verdict should be for such sum as will fully and fairly compensate the plaintiffs for the damages sustained by them.

Plaintiff 1

The amount necessary to compensate plaintiff 1_________

Plaintiff 2
The amount necessary to compensate plaintiff 2________

(This will continue for as many trials as the plaintiffs and defendants agree on.)

Plaintiff X

The amount necessary to compensate plaintiff X________

Add the damages due to all plaintiffs together and then divide by X to determine the average liability of the defendant. Then, multiple the average liability by the total number of class members to determine the aggregate liability.

Average liability________

Aggregate liability________

Phase 2

Damages are of two types: compensatory damages, which are awarded as compensation for pecuniary loss and recompense for the injury suffered, and punitive damages, which are something in addition to full compensation, not given as the plaintiff’s due, but as punishment to the defendant and as a warning and example to deter him and others from committing like wrongs. At this stage, you will determine whether the defendant’s conduct is deserving of punitive damages. You will determine whether the defendant’s actions can rightly be called reprehensible. Among the things you may consider are whether the defendant harmed the plaintiffs intentionally, the harm done to nonparties to the suit by the defendant’s actions, and the potential harm the defendant could have caused by his actions. If you find the defendant’s conduct to be reprehensible, then the defendant will be eligible for punitive damages.

Was the defendant’s conduct reprehensible? Yes____  No_______

Phase 3
At this stage you will determine the amount of punitive damages. The damages should be based on two factors: the amount needed to deter the defendant and other similar actors and the amount needed to fully punish the defendant for his actions. Your calculation of deterrence should be based on the likelihood that the defendant might have escaped having to pay for the harm for which he or she is responsible. You should estimate the probability of escaping liability, find the reciprocal, and then multiply the compensatory damage award determined at Phase 1 by the resulting number. When determining additional amounts needed to fully punish the defendant for his reprehensible act, you should remember that other damages also punish the defendant. After having determined this amount, add the damages necessary for deterrence and the damages necessary for punishment together to determine the total punitive damage award. You are not to consider the harms possibly done to non-class members when calculating this award.

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