

Executive Summary of the Settlement Panel

Judge D. Brock Hornby, Moderator and Reporter

Professor Richard Nagareda: Trial is no longer the endgame of civil litigation. The endgame today consists of settlement or resolution of the case on some sort of dispositive pretrial motion.

We are in a position quite similar to that of 1938 when the Rules were first adopted. Now, as then, there is a lingering sense that procedure *as procedure* may be exerting an undue influence on the pricing of civil claims. But now the procedures suspected of having this effect are not the kinds of formal code-pleading standards of the 19th century but, rather, features of the 1938 reforms themselves.

We should think about civil procedure as a regulatory regime – a regime that regulates the pricing of claims via *settlement*. A key goal is for regulation to achieve desired results without introducing distortions of its own that undermine its goals.

If we think about civil procedure – especially pretrial procedure – as a regulatory regime, two features stand out:

1. Since roughly the mid-1980s, the overarching trend in judicial decisions has been to push judicial scrutiny of claims ever earlier in the pretrial process. The process began with the 1986 trilogy of Court decisions on summary judgment. Then, in 1993, we received Daubert. Then, in the 2000s, we were handed a series of decisions like IPO Securities and Hydrogen Peroxide that seek to set out a distinctive law of class action certification. And now, we have the Twombly/Iqbal line of decisions that situate judicial scrutiny of pleadings at the very outset of the lawsuit. In pushing judicial scrutiny ever earlier in the pretrial process, we have now reached the endpoint.
2. These various dispositive (or nearly dispositive) pretrial motions all operate in basically the same way. They operate as a relatively blunt “stop” or “go” sign on the road to trial. Insofar as they shed light on the settlement endgame, they do so only opaquely and indirectly – as when a denial of summary judgment nonetheless signals the judge’s views about where the weaknesses on the merits might lie.

The great enterprise of the NEXT generation of civil procedure reform will be NOT to prop up the regulatory regime of the 1938 Rules. The great enterprise will be to think about how we might design procedural rules that broaden the regulatory tools available to courts. One possible direction: Pretrial rulings that don’t operate as on-or-off, stop-or-go signs on the road to trial but that, instead, seek to inform directly the pricing of claims via settlement.

Here, we can draw on the considerable outpouring of scholarship on civil litigation since 1938. The major move has been to shift away from a focus on appellate decisions and toward accounts of the fundamental decision to settle or to proceed further in the lawsuit; in other words, away from what judges *say* to what litigants (and their lawyers) *do*. This research draws

on a wide array of methods – economics, finance, psychology, and empirical analysis. What we need to do is draw on that body of knowledge – to design a sensible regulatory regime for the pricing of claims via settlement.

Professor Robert Bone: Procedural rules should consider settlement outcomes as well as trial outcomes. The best definition of an “optimal” settlement is a settlement that corresponds to the expected trial value of the case, defined as the value of the judgment (conditional on the defendant being held liable), discounted by the likelihood that the defendant will be held liable (or more loosely, discounted by the strength of the case). It is a mistake to focus exclusively on procedures that prepare cases well for trial and produce good trial results. It is also important to pay attention to how procedures affect settlement outcomes. This doesn’t mean that procedural rules or trial judges should aim to encourage or promote settlement. Rather it means that settlement effects should figure in any metric for evaluating whether a procedural system is operating well.

We need to confront three asymmetries that impair fair settlements:

Cost asymmetry: In complex cases where litigation is more costly for one side than the other, the side bearing the greater cost is usually at a disadvantage in settlement negotiations. When a procedure, such as broad discovery, gives one side an ability to impose asymmetric costs on the other, the resulting asymmetry is likely to distort settlement outcomes, and in a systematic way.

Risk asymmetry: Risk includes two components, each of which can be asymmetrically distributed: degree of risk and risk preference. The plaintiff and the defendant might face different degrees of risk from an adverse outcome. For example, the defendant in a large damages class action might face the risk of a crippling judgment if the class were to win, and this can give the plaintiff improper settlement leverage and encourage the filing of frivolous and weak cases. Furthermore, the plaintiff and the defendant might have different risk preferences. A risk-averse plaintiff, for example, facing a risk-neutral defendant is at a disadvantage in settlement negotiations. So too, many argue that in “bet the company” cases with very large stakes, corporate defendants act as if they were risk-averse and settle even weak and frivolous suits for large amounts.

Informational asymmetry: Informational asymmetry interacts with the other two asymmetries to exacerbate settlement problems. A party who possesses critical private information unknown to its opponent ordinarily has a strategic advantage and can negotiate a settlement out of proportion to its substantive entitlement. There is much discussion today of the effect of Twombly and Iqbal on cases where the defendant has private information. But informational asymmetry is also an important determinant of settlement dynamics and bargaining throughout the litigation.

Professor Bone supports Professor Nagareda’s suggestion of asking trial judges to give parties preliminary evaluations of the merits, perhaps tied to phased discovery. He suggests that the judge could even make an evaluation based on the discovery results after each stage (and perhaps use the evaluation to decide how much additional discovery to allow). Discovery results could inform the judge’s merits analysis, and staging the process could reduce the risk

that high discovery costs will pressure parties to settle before the judge has a chance to offer an evaluation. This approach could reduce informational and risk asymmetries without exacerbating cost asymmetry, thereby facilitating good settlements.

The Legitimacy Critique of Settlement: Professor Bone says that we must distinguish between two types of legitimacy. One type, “perceived legitimacy,” is concerned with whether the public will lose faith in the legitimacy of the courts. The other type, “normative legitimacy,” is concerned with whether it is in fact legitimate for courts to focus on settlement (entirely apart from what the public might think). Professor Bone is not persuaded by arguments from perceived legitimacy, but believes that arguments from normative legitimacy must be taken very seriously, because they raise complex and subtle issues that implicate the fundamental nature of adjudication. Focusing excessively on promoting settlement could lead judges and lawyers, over the long run, to view their responsibilities primarily in settlement terms. If this were to happen, we would have lost something crucial about adjudication as a social institution. Civil adjudication is, and should be, committed at its core to reasoned decisions based on principle. Settlements are not inconsistent with this commitment insofar as they reflect what a reasoned decision would produce. But adjudication demands more than merely consensual resolutions acceptable to the parties. At times it demands great courage from a judge in the face of sharp public dissent. It would be a tragedy if we were to lose sight of these vital truths in the midst of trying to save litigation costs and to reduce delays by promoting settlements.

Attorney Loren Kieve: A major point (if not *the* major point) that a broad group of Duke Conference participants have stressed is making sure that the trial court moves the case forward by promptly hearing and deciding issues, including motions to dismiss, for discovery and for summary judgment. Another key point is having firm, fixed dates, including the date for a final pretrial conference, followed shortly by a trial.

Cases settle when the participants do not want to risk having someone else – a judge or a jury – decide it for them. The shorter the time period before that happens, the sooner the case will settle (or be tried). Attorney Kieve believes that the rules and procedures of United States District Court for the Eastern District of Virginia (the “rocket docket”) already accomplish this.

Attorney Kieve says that the E.D. Va.’s procedures comport with the ABA Section of Litigation 2009 survey of its members, 3,300 of whom responded. Although plaintiffs’ and defendants’ lawyers did not always agree, there seemed to be a consensus that:

- Early case management by judges helps to narrow the issues and limit discovery.
- Shortening the time to final disposition reduces costs.

Attorney Kieve says that the E.D. Va. Procedures also track the ABA Standards for Final Pretrial Submissions and Orders (August 2008).

The E.D. Va. remains by a fair margin one of the most efficient and effectively managed federal district courts in the nation. According to Attorney Kieve, everyone who practices in that court – on both sides of the “v.”, including government lawyers as well as civil practitioners – likes the system.

Motions are heard and decided promptly. Discovery proceeds efficiently. Extensions of time are honored only if approved by the court and are sparingly given. Perhaps the most important factor, however, is that the court sets firm deadlines for completing discovery, having the final pretrial conference and then setting a trial date shortly thereafter. Attorney Kieve says that assuming that the adage “time is money” is true, this practice saves the parties considerable amounts of both.

[Attorney Kieve also described many of the E.D. Va. Procedures, which are omitted in this Executive Summary.]

Attorney James Batson: In Attorney Batson’s practice, he finds that litigation is structured for summary judgment. He believes that it should be structured for trial. Settlements are good only when they are reached for the right reasons: i.e., risk assessment of trial prospects, not exhaustion by the process and procedures.

Now, defendants are exhausted by cost, disruption to their affairs, and bad public relations. Plaintiffs are exhausted by cost and delay, false hopes for resolution, and embarrassment.

Attorney Batson finds that many plaintiffs who lose after trial and their “day in court” are nevertheless far more satisfied with the process than those who settle.

On discovery problems, there is no need for rules changes. (Attorney Batson does support rules re: preservation and sanctions.)

But Attorney Batson is in favor of best practices. Here are his:

- Require parties to raise discovery issues with the court immediately. The longer a party waits, the less likely that party should be able to get relief
- Judges should be available and should rule promptly
- Bring the parties to court
- Have iterative discovery
- Make initial document requests almost immediately

Make trials seem inevitable!

Attorney Peter Keisler: The Rules were principally designed to create a structure for adjudication (whether trial or summary judgment), not for settlement, but settlement has become a dominant outcome because parties prefer it to the alternative of going to trial under the system the Rules have created. The system depends upon that preference because of limited resources. But even when cases settle, the Rules create a mechanism that people invoke to establish the threats, deadlines, forced sharing of information, etc., that establish the backdrop and incentives for resolving cases.

Whatever the misalignment between the Rules’ purpose and the outcomes they generate, amending them to influence the settlement process more directly is the wrong path. The focus

of the Rules should be on making the litigation process the best it can be at securing the just, speedy, and inexpensive determination of every action and proceeding, and the better the Rules are at doing that, the better the outcomes will be, in both litigated and settled cases.

We could perhaps write rules that would force more settlements by, for example, imposing more draconian consequences on parties that decline to settle and then lose their cases, but quite properly there would be very little support for such rules – they would probably encourage undesirable and desirable settlements indiscriminately, and in all events there shouldn't be a penalty for wanting to have a serious claim or defense adjudicated in court.

A “desirable settlement” is one that reflects a process in which the parties come to a similar enough view of the merits of the case and the likely outcome of litigation that they can shortcut that process and save themselves, and the system, the time and expense of trying the case to judgment while achieving a roughly parallel end result (or a result that delivers benefits to the parties that are different from what could be achieved in litigation but which they regard as equivalent or better). An “undesirable settlement” is one in which a party is forced to buckle under because of the costs imposed by the system or its randomness and unpredictability, and to abandon or heavily discount meritorious claims or defenses – such as the plaintiff who needs relief in the short-term and is afraid the defendant will engage in a protracted war of attrition, or the defendant who faces a non-meritorious case where the discovery costs will exceed the settlement costs or who fears a small possibility of a wrong but cataclysmic outcome.

While rules of general applicability can't be discriminating enough to successfully encourage desirable settlements while discouraging undesirable ones, case-specific judicial practices can. The focus should be more on best practices than on rules. Judicial practices that clarify sooner rather than later the applicable law—prompt rulings on dispositive motions, or even periodic status conferences where the judge can provisionally indicate how he or she is seeing key issues—judicial actions that help the parties know sooner rather than later what counts are in and what counts are out, what categories and measures of damages and other relief will be available and what categories will not be—those can really move the parties' positions to the point where they are in shouting distance of one another and can close the gap.

Instead, judges sometimes adopt other strategies:

Prolonging the uncertainty—declining to resolve issues on which wild swings in the outcome could turn until the last possible moment, precisely because judges believe that settlements will happen if one or more parties fear an extreme and unpredictable result. As a predictive matter, that's an accurate assessment of how many parties respond to uncertainty. But that fosters undesirable settlements in which the costs of traversing the system and the unpredictability in its result drive the outcome.

Becoming too calculating in structuring timing, sequence, and substance of rulings in ways they think will best promote settlement. Judges rarely have the insight into the parties' incentives that would be necessary for such a strategy to be effective, and it

often backfires. (Attorney Keisler is not talking here about class actions or certain types of mass torts where settlement is itself adjudicated, and must be subjected to a formal and obviously conscious process; nor is it wrong, he says, for a judge to stay decisions when parties jointly, or their mediator, specifically request because they are close to settling. But in other situations, it is generally better for the judge to act without regard to settlement prospects than to act out of excessive consciousness of settlement effects.)

Mandatory Mediation: This is the one explicitly settlement-focused judicial practice – as opposed to the more general practice of issuing prompt rulings and moving the case efficiently to trial—that Attorney Keisler has seen work, sometimes quite unexpectedly from the perspective of the parties. Part of its advantage is that it lifts from the parties the burden of suggesting mediation, which some might worry conveys over-eagerness to the other side, but part of it is that a skillfully run mediation process can bring a party to a willingness to agree to something it would have earlier said (sincerely) was completely out of the question and not worth even discussing. The psychology of this has something to do with the ways in which mental baselines start changing once you get into serious discussions and the fact that discussions can make the prospect of actually resolving and closing out litigation that’s become a headache seem more concrete and therefore more motivating. Sometimes forcing parties into those discussions even when they say it would be fruitless can be helpful.

The parties and lawyers in a lawsuit generally need help to avoid their worst tendencies and incentives, and there’s no substitute for smart, skilled, experienced judges who actively manage their cases throughout the pre-trial process. The Rules already do what the Rules need to do, which is to empower them. The judge who actively moves the case along, decides issues promptly, manages discovery effectively, etc., promotes constructive settlement even (perhaps especially) when he or she is oblivious to the settlement side.

Judge Paul Friedman: We can lament the demise of the trial, but we cannot do anything about it; there will continue to be lots of settlements. We should encourage settlements and discussions in appropriate cases, and assure as best we can that settlements are made for the right reasons. There are a lot of coerced settlements because the system wears parties down, not because that is the best strategic decision. We must manage pre-trial better so as to prevent exhaustion from being the main reason for settlements. A good settlement involves an economic risk analysis.

There is a certainty to settlement. As much as you can admire juries, there is an inherent unpredictability to juries. “You can’t always get what you want.” Take what you need. This is good pre-trial strategy, which Judge Friedman tells lawyers all the time. There is neither a clearly defined nor valuable public interest in all cases, as to settlement v. trial. Many are just disputes, and it doesn’t really matter if there is consistency with prior decisions, case law, etc.

In 97% of cases, lawyers who collaborate/talk cause costs to go down. Lawyers should not be enemies—leave that to the clients.

Judges and lawyers approach discovery as if there is going to be a trial, even though, as is clear from the statistics, there usually is not going to be one; this approach is a waste of money.

Rule change recommendations:

- (1) Eliminate initial disclosures
- (2) Phased/staged discovery
- (3) If a defendant files a motion, its discovery ends – the opponent may still pursue discovery
- (4) Consider employing phased/staged discovery to **get** to the next stage
- (5) Mandatory ADR in every case; not just at trial, but also in pre-trial practice.

Consensus (perhaps):

1. Cases settle in the shadow of the Rules; the Rules do affect settlement, but they should not coerce settlement. Settlement of the vast majority of case is inevitable and not to be decried or avoided.
2. There are good and bad settlements; coerced settlements (whether by judges or excessive risk or excessive cost of litigation) are not good settlements; a desirable settlement is generally one that corresponds to the expected trial value of the case, discounted according to the strength/weakness of the case, and not distorted by great asymmetries of risk, information or cost between the parties.
3. Judges should not themselves be intimately involved in settlement.
4. Court-ordered mediation should perhaps be considered in all cases.
5. The parties need better information, at lower cost, sooner, to help them assess the settlement value of a case. Some of that information could come from judges through earlier (and prompter) rulings; maybe we also should look for new ways to achieve this goal.