

Reverse Sampling: Holding Lotteries to Allocate the Proceeds of Small-Claims Class Actions

Shay Lavie*

ABSTRACT

Small-claims class actions pose a unique dilemma: individual awards are small, and it is often not feasible to distribute them to each and every plaintiff. Courts have devised several alternative allocation procedures to cope with this problem, but none are satisfactory.

This Article proposes a different method: paying more money to fewer, randomly sampled claimants. As each individual award entails per-claim administrative costs, using lotteries to distribute the proceeds of small-claims class actions cuts these expenses. This Article demonstrates that the lottery method for dispersing small-claims class action proceeds is superior to all existing alternatives. It funnels the money back to the group of victims, achieves deterrence, and maintains administrative efficiency. Finally, the Article shows that randomization is a fair allocation mechanism, as all class members are equally treated, and that the use of lotteries in this context raises no legitimacy concerns.

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*[A random selection] is resorted to as the fairest mode, and, in some sort, as an appeal to God [W]e can conceive of no mode so consonant both to humanity and to justice In no other than this . . . way are those having equal rights put upon an equal footing, and in no other way is it possible to guard against partiality and oppression, violence and conflict.*¹

INTRODUCTION

In a recent antitrust class action, a number of fashion models filed a complaint against model agencies for price fixing.² The parties settled and the agreement created a settlement fund of approximately \$22,000,000 to be distributed among the members of the class.³ Following the creation of the settlement fund, letters were sent to thousands of potential class members, urging them to redeem their awards.⁴ Alas, numerous class members failed to show up. In fact, it turned out that a nontrivial portion of the settlement amount remained in the settlement fund's coffers.⁵ The presiding judge then "found himself with \$6 million of unclaimed money."⁶ The court had to distribute this money somewhere. And so it did. Among several

¹ United States v. Holmes, 26 F. Cas. 360, 367 (C.C.E.D. Pa. 1842) (No. 15,383).

² See *Masters v. Wilhelmina Model Agency, Inc.*, 473 F.3d 423, 426 (2d Cir. 2007).

³ *Id.* at 428.

⁴ *Id.* at 429.

⁵ See *Fears v. Wilhelmina Model Agency, Inc.*, No. 02-Civ.4911(HB), 2005 WL 1041134, at *10 (S.D.N.Y. May 5, 2005), *aff'd in part, vacated in part sub nom. Masters*, 473 F.3d 423.

⁶ Adam Liptak, *Doling Out Other People's Money*, N.Y. TIMES, Nov. 26, 2007, at A14.

alternatives, it decided to award the unclaimed funds to charities such as eating disorder and substance abuse programs.⁷ The distribution plan was based on the theory that these charities are likely to indirectly assist the fashion models who were involved as plaintiffs in the case.⁸ Not surprisingly, the court's solution led to strident disapproval, including an unflattering article in *The New York Times*⁹ and vacatur by an appellate court.¹⁰ Specifically, it seems that the unfettered judicial discretion to dole out money is bothersome because it presents "an invitation to wild corruption of the judicial process."¹¹ However, it is not clear that among existing solutions to the problem of unclaimed funds, the court had a better practical choice.

This story, the dilemma of unclaimed funds, and the solution implemented by the court are emblematic of many other class actions. A class action suit is a powerful enforcement tool. It forces the defendant to pay damages where the stakes are too low for individual litigation, and thereby achieves better deterrence.¹² However, especially in low-value claims, the per-claim administrative costs of awarding the money are often high relative to the value of each individual claim. It is often prohibitively expensive to locate and compensate each and every member of the class.¹³ Likewise, for many class members, it is not economically viable to redeem their meager awards.¹⁴ The result is unclaimed compensatory damages commonly in the range of millions of dollars.¹⁵ Obviously, these "pots of money"¹⁶ are not left intact.¹⁷ Courts, lawyers, and legislators have found creative destinations to transfer these leftover funds: to the defendant, the gov-

⁷ *See id.*

⁸ *See id.*

⁹ *Id.*

¹⁰ *Masters*, 473 F.3d 423, *aff'g in part, vacating in part Fears*, No. 02-Civ.4911(HB), 2005 WL 1041134.

¹¹ Liptak, *supra* note 6 (quoting Professor Samuel Issacharoff).

¹² Aggregating the plaintiffs into one class also avoids the inherent advantages the defendant has when he deals with a separated group of individual plaintiffs. *See* David Rosenberg, *Mass Tort Class Actions: What Defendants Have and Plaintiffs Don't*, 37 HARV. J. ON LEGIS. 393, 418 (2000).

¹³ *See* ALBA CONTE & HERBERT B. NEWBERG, *NEWBERG ON CLASS ACTIONS* § 10:14 (4th ed. 2002).

¹⁴ *See id.*; Deborah R. Hensler, *Revisiting the Monster: New Myths and Realities of Class Action and Other Large Scale Litigation*, 11 DUKE J. COMP. & INT'L L. 179, 200-01 (2001).

¹⁵ *See, e.g.*, Liptak, *supra* note 6.

¹⁶ *Id.*

¹⁷ As one attorney puts it, "it's in everyone's best interest to stipulate . . . that the residual money will go somewhere." S. Gale Dick, *Fluid Recovery: Flexible Ways to Settle Cases*, 13 ALTERNATIVES TO HIGH COSTS LITIG. 73, 82 (1995) (internal quotation marks omitted).

ernment, prospective consumers, charity organizations, and various legal aid societies, among others. “Judges all over the country have gotten into the business of doling out leftover class-action settlement money, sometimes to organizations only tangentially related to the subject of the lawsuit.”¹⁸

None of the existing solutions to the problem of unclaimed funds are satisfactory. Some fall short of achieving optimal deterrence, as the defendants are not bound to pay the complete price for their wrongdoing. Other distribution methods entail substantive administrative costs or fail to compensate the victims, and instead, award these large funds to a third party, thereby distorting its incentives. Finally, existing mechanisms provide judges with unfettered discretion to dole out sizeable funds, encouraging abuse of power.

This Article introduces a new method to allocate the proceeds of small-claims class actions that obviates the problem of unclaimed funds. Unlike most other existing methods, the proposed mechanism diverts the compensation money back to the place where it belongs: the class of plaintiffs. To cut the per-claim administrative costs of allocating the common fund, the proposal relies on a simple principle: instead of distributing the money to all class members, more money is paid to a random sample of the class. For instance, instead of paying five dollars to each member of the class, the court would randomly select one in every twenty plaintiffs, who is awarded one hundred dollars. The benefits of this simple method are straightforward. The proposed distribution scheme would result in saving substantial per-claim administrative costs (e.g., locating plaintiffs, handling each payment, and proving individual entitlements). Therefore, plaintiffs would receive, on average, a larger compensation. As low-value claimants are approximately risk neutral, it is plausible to believe that they would prefer allocation by lottery.

No previous literature has gone in this direction.¹⁹ Sampling was proposed²⁰ and used in several complex litigation contexts as a method to easily determine the defendant’s aggregate liability based

¹⁸ Liptak, *supra* note 6.

¹⁹ More generally, the literature tends to focus on deterrence (improving the process of imposing liability on the defendant) and ignore the compensation process. A recent article expresses this lack of interest in the distribution process: “As long as the transaction causes the defendant to internalize the social costs of its wrongdoing, . . . [the] court ought to approve.” Myriam Gilles & Gary B. Friedman, *Exploding the Class Action Agency Costs Myth: The Social Utility of Entrepreneurial Lawyers*, 155 U. PA. L. REV. 103, 153 (2006).

²⁰ See David Rosenberg & Steven M. Shavell, *A Simple Proposal to Halve Litigation Costs*, 91 VA. L. REV. 1721, 1721 (2006).

on randomly selected plaintiffs.²¹ This Article also suggests using a random sample, but of a different sort. The proposed “sampling,” i.e., random selection, does not aim at knowing more about the class of plaintiffs. Rather, its only goal is to return the money the defendant owes back to the plaintiffs. Hence the proposal is dubbed “reverse sampling.”

As this Article discusses in greater detail, the proposed reversed sampling method is superior to all existing distribution plans because it better fulfills the dual goals of compensating the class of plaintiffs and deterring defendants. Moreover, the use of randomization in this context does not infringe on the judiciary’s legitimacy. In many other procedural settings, judges use lotteries, which are generally perceived as a fair—indeed, the fairest—allocation mechanism. Finally, this proposal can easily be implemented. It requires no change in the law; rather, it borrows the equitable powers courts already employ in these contexts.

The Article is organized as follows: Part I presents the basic framework. It uses a numerical example to demonstrate the proposed solution, provides three paradigmatic applications, and elaborates on the main advantages and practical scope of reverse sampling. Part II discusses lotteries in the judicial setting. It argues that lotteries are widely perceived as a fair mode of decisionmaking. Although the judiciary does have some aversion to the use of lotteries in decisions on the merits, a closer look reveals that randomization is not per se illegitimate, and judges commonly employ lotteries in diverse settings. Part III surveys the existing alternatives to distributing the proceeds of small-claims class actions, and compares these methods to the proposed solution. It argues that the proposed mechanism, reverse sampling, fares better than any existing alternative.

I. BASIC FRAMEWORK: THE REVERSE SAMPLING METHOD

A. *Numerical Example*

This Article argues that courts should use lotteries to allocate the proceeds of small-claims class actions. To better illustrate this proposal, the following paragraphs provide a numerical example.

An Internet-based travel reservation website charged excessive fees, in the amount of five dollars, for each reservation. Its liability is

²¹ See Robert G. Bone, *Statistical Adjudication: Rights, Justice, and Utility in a World of Process Scarcity*, 46 VAND. L. REV. 561, 563–66 (1993). For a concrete example of the use of sampling to determine aggregate liability, see *Long v. Trans World Airlines, Inc.*, 761 F. Supp. 1320, 1329 (N.D. Ill. 1991).

not contested. It costs one dollar per claim to dole out the money (e.g., handling and mailing a check).²² There are 1,000,000 class members. Under the traditional approach, which mandates compensation for each class member,²³ administrative costs are \$1,000,000. The common fund, the total amount of money the defendant has to pay, is $\$5.00 \times 1,000,000 = \$5,000,000$. The net fund is the common fund, less administrative costs: $\$5,000,000 - \$1,000,000 = \$4,000,000$. The net fund is distributed to 1,000,000 class members such that each member gets \$4.00.²⁴

Using reverse sampling, the court randomly selects, say, one in every twenty class members so that five percent of the class is chosen. Hence, only 50,000—rather than 1,000,000—plaintiffs are actually awarded damages.²⁵ Administrative costs of distributing the money are only \$1.00 (per claim) \times 50,000 (members) = \$50,000, instead of \$1,000,000. Accordingly, the net value of the common fund is now \$4,950,000. This is a net gain of \$950,000 that can be shared among class members. Each of the 50,000 chosen members now gets \$99.00.²⁶ Therefore, each member of the class has a five percent probability of receiving ninety-nine dollars. The following table demonstrates the difference between traditional distribution and reverse sampling.

²² This amount is a rough estimate, which takes into account that a single stamp costs forty-four cents and a standard envelope costs around eight cents. See Jasmin Melvin, *Stamps for U.S. Letters to Rise to 44 Cents in May*, REUTERS, Feb. 10, 2009, available at <http://www.reuters.com/article/idUSTRE5197CQ20090210>; *Mead Press-It Seal-It #10 White Envelopes, 50 Count (75024)*, AMAZON.COM, http://www.amazon.com/Mead-Press-Seal-Envelopes-75024/dp/B000N4C1LO/ref=sr_1_1?ie=UTF8&s=office-products&qid=1274940735&sr=1-1 (last visited Apr. 15, 2011).

²³ See, e.g., PRINCIPLES OF THE LAW OF AGGREGATE LITIG. § 1.04(b)(2) (2010) (“[T]he objectives of an aggregation of claimants include . . . compensating each claimant appropriately.”); *id.* § 1.04 cmt. f (discussing the “normative importance” of individual compensation).

²⁴ This example is motivated by *In re Expedia Hotel Taxes & Fees Litig.*, No. 05-2-02060-1 SEA (Wash. Super. Ct. Aug. 10, 2009), <http://www.kingcounty.gov/courts/SuperiorCourt/-/media/courts/SuperiorCourt/Docs/Expedia.ashx>, in which the author, as a class member, received a check in the amount of seventy-seven cents.

²⁵ The proposed use of reverse sampling is independent of notice requirements. If individual notice is cheap, notice can be sent to every member of the class; otherwise, the court may promulgate public notice. Either way, class members can be advised as to the class action and the use of reverse sampling, and be given the opportunity to opt out.

²⁶ Courts could also use reverse sampling when individual claims vary, in which case the chosen plaintiffs would receive compensation based on a multiplier of their actual claims (in the given example, the multiplier is twenty). For a more detailed discussion, see *infra* note 47 and accompanying text.

Table 1. Reverse Sampling Versus Traditional Approach

| | Traditional Distribution | Reverse Sampling |
|------------------------------------------------------------------|---------------------------------|-------------------------|
| Individual Claim | \$5.00 | \$5.00 |
| Class Size | 1,000,000 | 1,000,000 |
| The Common Fund | \$5,000,000 | \$5,000,000 |
| Proportion of Actual Beneficiaries to Total Class Members | 1:1 | 1:20 |
| Number of Actual Beneficiaries | 1,000,000 | 50,000 |
| Administrative Costs per Claim | \$1.00 | \$1.00 |
| Total Administrative Costs | \$1,000,000 | \$50,000 |
| Net Common Fund | \$4,000,000 | \$4,950,000 |
| Net Award per Actual Beneficiary | \$4.00 | \$99.00 |
| Expected Value per Claim²⁷ | \$4.00 | \$4.95 |

The defendant pays the same amount, \$5,000,000, under either the traditional allocation approach or the reverse sampling approach. The expected value of each claim, however, is \$4.95 under the reverse sampling mechanism and \$4.00 under the traditional allocation approach. Thus, under reverse sampling, plaintiffs get ninety-nine dollars with a five percent probability; under the traditional approach, plaintiffs receive four dollars with certainty.

The next paragraphs delineate the paradigmatic cases in which reverse sampling is beneficial. In all of these cases, the distribution of the money entails nontrivial per-claim administrative costs, which can be saved by giving more money to fewer plaintiffs.

B. Paradigmatic Applications

The reverse sampling method cuts the administrative costs of awarding money to the victims. There are three main sources of these costs: handling the payment, locating the victims, and claiming damages.

²⁷ The expected value per claim is an average in which each possible value is weighted by its probability. Under the traditional approach, there is 100% probability of receiving a value of \$4.00, and therefore the expected value per claim is \$4.00. In the case of lottery distribution, however, each plaintiff has a 5% probability of receiving \$99.00, and a 95% probability of getting nothing. The expected value per claim is therefore $0.05 \times \$99.00 + 0.95 \times \$0.00 = \$4.95$.

High Handling Costs. This paradigmatic case is similar to the aforementioned numerical example. All victims are known, but awarding them the money entails some constant costs per claim (e.g., handling forms and mailing a check). When these costs comprise a nontrivial portion of the individual awards—as is common in low-value claims—reverse sampling is useful.

High Search Costs. In this paradigmatic case, victims are not easily identified. Take the following example:

A small hotel chain charged each customer excessive fees in the amount of two dollars. Customers are not readily known. However, the hotel can identify them through a costly process (e.g., tracking the credit cards used to pay for the hotel). Normally, these per-claim identification costs surpass individual awards. Hence, courts should use reverse sampling, and they can do so, for example, by awarding damages only to customers from a randomly chosen day.²⁸

Similar to the first paradigmatic case, the high administrative costs relative to the individual awards prohibit a traditional compensation plan. In this second case the administrative costs stem from the need to identify class members rather than implementing the payment scheme. In both cases, as will be discussed in greater detail, reverse sampling is superior to the traditional distribution scheme and its alternatives.

High Claiming Costs. In this paradigmatic case, the victims have to bear high per-claim costs in order to receive compensation. Take the following case:

Plaintiffs filed a products liability class action against a manufacturer of orthopedic medical devices. The settlement agreement requires class members to prove their claims by signing an extensive Proof of Claim form that contains a detailed medical history questionnaire. Due to the low-value awards, some class members do not find it valuable to fill out the detailed form, and a large portion of the settlement fund remains unclaimed. Reverse sampling can rectify this state of affairs. By randomly choosing some victims, and awarding damages that are augmented by the appropriate multiplier, actual individual entitlements become sufficiently large so as to induce plaintiffs to cash their awards.²⁹

²⁸ This example draws on *In re Hotel Telephone Charges*, 500 F.2d 86 (9th Cir. 1974).

²⁹ This example is inspired by *In re Orthopedic Bone Screw Products Liability Litigation*, 246 F.3d 315 (3d Cir. 2001).

This paradigmatic case is similar to the previous ones, in the sense that there are high administrative per-claim costs relative to the individual awards. Unlike the two previous paradigmatic examples, however, the constant per-claim costs are borne by class members who have to prove their damages, whereas in previous examples, the administrative costs are borne by the fund itself.

Class members are required to expend some effort to receive compensation. First, plaintiffs have to actually cash their awards; this might be a demanding task relative to the low sums involved. Second, courts frequently ask class members to prove their claims.³⁰ Proof requirements range from merely filing a statement,³¹ to filing affidavits, purchase records, and so on.³² Oftentimes, many class members, particularly those with smaller claims, do not find it in their interest to bear the costs of proving their claims or even cashing their modest awards.³³ In those cases, some individual awards are left unclaimed. The reverse sampling method could solve this problem by paying more money to fewer claimants, thereby making it valuable for the low-award plaintiffs to prove and cash their claims as well.³⁴

The following Section summarizes the advantages of reverse sampling, which are equally relevant to all of the aforementioned paradigmatic applications.

C. *Advantages of the Reverse Sampling Method*

Reverse sampling economizes on administrative costs. It does so without frustrating class members' risk preferences.

³⁰ See CONTE & NEWBERG, *supra* note 13, § 10:14. Courts can determine total aggregate damages based on class-wide evidence while still requiring class members to prove their individual claims to receive compensation. See *id.* § 10:5 (citing cases).

³¹ *Id.* § 10:14.

³² *Id.* § 10:12.

³³ *Id.* § 8:41 (“Experience has demonstrated that persons with modest or nominal individual potential recoveries will not bother to file a proof of claim.”). Judge Posner has similarly asserted in one opinion that “many people won’t bother to do the paperwork necessary to obtain \$10, or even a somewhat larger amount.” *Mirfasihi v. Fleet Mortg. Corp.*, 356 F.3d 781, 783 (7th Cir. 2004).

³⁴ Similarly, the reverse sampling technique is valuable even when all class members find it economically viable to redeem their claims, e.g., when the costs of proving the claim and cashing the award are lower than the smallest claim. In that case, the fact that only a small, random sample of plaintiffs is entitled to come forward to redeem their claims raises the expected value of all individual awards.

1. *Economizing on Administrative Costs*

Economization of administrative costs is the main argument for implementing reverse sampling, as “[m]aximizing [the net] value is a central objective of aggregate litigation.”³⁵ Administrative costs per claim are, by and large, constant. By awarding more money to fewer members, administrative costs are saved—a pure gain to the class. Recall the numerical example: If courts use the traditional method, each member is awarded four dollars with certainty. Using reverse sampling, the expected value per claim is \$4.95, or \$99.00 with a five percent probability. This difference—a net gain—is the result of cutting administrative costs and distributing more money to fewer, randomly sampled plaintiffs. In the numerical example, the class-wide gain amounts to \$950,000.

2. *Class Members’ Risk Preferences*

A complementary argument for implementing reverse sampling is that it does not frustrate plaintiffs’ risk preferences.

The traditional distribution scheme guarantees small sums of monetary awards, while the reverse sampling method members are awarded larger sums with low probability. Discerning which method class members would prefer is an empirical question. Behavioral economists predict that, in this type of situation, individuals actually tend to prefer a fair gamble.³⁶ One need not go that far to justify dis-

³⁵ PRINCIPLES OF THE LAW OF AGGREGATE LITIG. § 1.04 cmt. e (2010); *see also id.* § 1.04(b)(1) (“[T]he objectives of an aggregation of claimants include . . . maximizing the net value of the group of claims.”).

³⁶ This prediction is supported by many experiments as part of a broader pattern of behavior under risky conditions. *See generally* Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 *ECONOMETRICA* 236 (1979). For instance, “Tversky and Kahneman found . . . that when they asked individuals to choose between . . . a 10 percent chance at \$500—and the expected value of that gain—i.e., a certain \$50—78 percent of decision makers preferred the gamble.” *See* Chris Guthrie, *Framing Frivolous Litigation: A Psychological Theory*, 67 *U. CHI. L. REV.* 163, 179–80 (2000) (citing Amos Tversky & Daniel Kahneman, *Advances in Prospect Theory: Cumulative Representation of Uncertainty*, 5 *J. RISK & UNCERTAINTY* 297, 308 (1992)). The preference for a risky award depends on the distinction between “gain” and “loss”: people prefer low-probability “gains” but dislike low-probability “losses.” *Cf.* Christine Jolls, *Behavioral Economics Analysis of Redistributive Legal Rules*, 51 *VAND. L. REV.* 1653, 1655–56 (1998) (discussing this differential framing in the context of the choice between redistributive legal rules and taxes). For previous legal literature applying the risk-seeking phenomenon, *see, for example*, Stephen J. Choi & A.C. Pritchard, *Behavioral Economics and the SEC*, 56 *STAN. L. REV.* 1, 15 (2003) (explaining the lottery-like investment behavior of middle-class individuals), Dennis D. Crouch, *The Patent Lottery: Exploiting Behavioral Economics for the Common Good*, 16 *GEO. MASON L. REV.* 141, 162–63 (2008) (applying low-probability risk-seeking to patent policy), and Guthrie, *supra*, at 187–92 (using the risk-seeking pattern to explain frivolous, low-probability lawsuits).

tribution by lotteries in small-claims class actions.³⁷ For low-value claims, plaintiffs can be taken as approximately risk neutral. As the reverse sampling mechanism results in nontrivial administrative savings, each class member can expect to receive more compensation on average. Because plaintiffs are approximately risk neutral with respect to these modest values, it is plausible that they will prefer the more efficient random distribution.

Of course, we can never know in advance the actual risk preferences of each and every class member. The best we can do is approximate what the expected preferences of most plaintiffs in the class are. To the extent that plaintiffs suffer extreme risk aversion, even with respect to low-value claims, this factor militates against the more efficient reverse sampling mechanism.

The combination, then, of administrative savings and risk neutrality suggests that class members would prefer monetary damages to be distributed by a lottery system in which they can expect to receive a higher award on average.

D. Additional Considerations

1. Practicability

In theory, each and every member of the class should receive exactly her individual entitlement. In reality, administrative constraints lead to “rough justice,” at best.³⁸ Some plaintiffs fail to receive their awards, and nontrivial undistributed funds are virtually certain.³⁹ Against this backdrop, judges have used broad, equitable powers to dole out class action funds.⁴⁰ Facing “administrative difficulties,”

³⁷ There are several difficulties with the risk-seeking argument and its application to the current context. First, one may wonder what explains this affinity for risk and whether these explanations are relevant to the proposed lottery distribution. For potential reasons why individuals prefer a risky gamble, see, for example, Guthrie, *supra* note 36, at 198–205, and Edward J. McCaffery, *Why People Play Lotteries and Why It Matters*, 1994 WIS. L. REV. 71, 93–96. Likewise, the bulk of the relevant evidence is experimental work conducted in the lab with students (though there are some real world manifestations of the risk-seeking phenomenon. See, e.g., Colin F. Camerer, *Prospect Theory in the Wild: Evidence from the Field*, in CHOICES, VALUES, AND FRAMES 296–97 (Daniel Kahneman & Amos Tversky eds., 2000)).

³⁸ As the American Law Institute’s *Principles of the Law of Aggregate Litigation* concedes, even when each plaintiff actually receives compensation, the amount is not likely to equal the victim’s damages. Rather, only “rough justice” can be achieved. PRINCIPLES OF THE LAW OF AGGREGATE LITIG. § 1.04 cmt. f (2010).

³⁹ See CONTE & NEWBERG, *supra* note 13, § 10:14.

⁴⁰ See Robert E. Draba, Note, *Motorsports Merchandise: A Cy Pres Distribution Not Quite “As Near As Possible,”* 16 LOY. CONSUMER L. REV. 121, 127–28 (2004) (“[T]he court . . . has discretion to adopt a distribution plan that is in the interests of the class as a whole, and it uses traditional principles of equity to resolve the disposition of unclaimed funds.”); see also Kevin M.

courts “are admonished to respond with flexibility and imagination [reflecting] the equitable origin of the class action device.”⁴¹ The same judicial powers can authorize the use of reverse sampling. No change in the law is required.

This Article adds another tool—reverse sampling—to the array of mechanisms already in use to cope with these administrative difficulties. It argues that the proposed method trumps, in principle, existing mechanisms. Hence, subject to the idiosyncrasies of each case, this Article calls for courts to commonly employ lotteries to distribute the proceeds of small-claims class actions. Nevertheless, courts can still benefit from a narrower application of this proposal, limiting its use to certain types of class actions. Courts might also limit the use of lotteries to distributing the unclaimed residuals rather than the entire fund. Although this version sacrifices administrative efficiency, it is still preferable to existing allocation mechanisms.⁴²

The following paragraphs raise several concerns regarding the use of reverse sampling, which are pertinent to delineating its practical limits.

2. *Low- and High-Value Claims*

One concern might be the applicability of reverse sampling to high-value claims. Would the proposal be limited to low-value claims? If so, how should courts define low-value claims?

The same logic applies to both low- and high-value claims: paying some plaintiffs more money is more efficient than paying all plaintiffs less money. However, high-value claims comprise a nontrivial portion of one’s wealth. Thus, a lottery distribution would leave many victims with sizeable uncompensated injuries. In these circumstances, and to the extent that victims have no prior insurance available, individual insurance considerations should be taken into account. Actual compensation to each victim with large damages might serve as an essential safety net. More generally, high-value claims implicate more directly risk-aversion concerns, which counter the appeal of lotteries

Forde, *What Can a Court Do with Leftover Class Action Funds? Almost Anything!*, 35 JUDGES J. 19, 19 (1996); Goutam U. Jois, *The Cy Pres Problem and the Role of Damages in Tort Law*, 16 VA. J. SOC. POL’Y & L. 258, 271–72 (2008); Natalie A. DeJarlais, Note, *The Consumer Trust Fund: A Cy Pres Solution to Undistributed Funds in Consumer Class Actions*, 38 HASTINGS L.J. 729, 742–43 (1987).

⁴¹ *In re Folding Carton Antitrust Litig.*, 557 F. Supp. 1091, 1104 (N.D. Ill. 1983), *aff’d*, 774 F.2d 1252 (7th Cir. 1984).

⁴² Another alternative is to employ both traditional and lottery distribution plans and give class members the choice between them.

as a method to distribute the common fund. Therefore, high-value claims are not always appropriate for the reverse sampling distribution. Low-value claims, however, have a meager effect on one's wealth. Claimants can be taken as approximately risk neutral, and insurance considerations should not prevent the use of reverse sampling. Courts can, and should, use their discretion to determine low-value claims. Indeed, courts already engage in equivalent decision-making in similar contexts. For example, courts are expected to determine whether small-claims class actions are "economically viable" for individual distribution.⁴³

3. *Decoupling Compensation and Deterrence?*

Another potential concern is related to a general argument for compensating victims to a lesser degree than their harm. There are two reasons for awarding reduced, or even zero, compensation. First, consumers prefer not to be insured against several risks such as pain and suffering.⁴⁴ Although, the argument goes, people would rather leave these potential damages uncompensated, the current tort system does compensate for them. The implication might be a tort system that exacts the entire damages from the defendant but pays a reduced sum to the victims. Second, reduced compensation improves victims' incentives to act properly: if they know they would not be fully compensated, victims are likely to take better care against the risks.⁴⁵ Where victims' precautions can easily avoid harm, it is important to induce potential plaintiffs to take these precautions. However, these considerations are generally irrelevant to small-claims class actions, which do not typically implicate pain and suffering awards, and in which victims' reasonable precautions usually have no bearing on the scope of damages.⁴⁶ To the extent that these considerations are relevant in some low-value cases, compensating class members, with or without lotteries, is less appealing. Judges should use their discretion to employ class lotteries accordingly.

⁴³ When individual distribution is not economically viable, alternative allocation mechanisms should be employed. *See, e.g.*, PRINCIPLES OF THE LAW OF AGGREGATE LITIG. § 3.07 *illus.* 2 (2010).

⁴⁴ *See* Robert Cooter, *Towards a Market in Unmatured Tort Claims*, 75 VA. L. REV. 383, 392 (1989). Another example of such risk is a death of a child. Consumers prefer to bear this risk themselves, as "[t]he death of a child does not ordinarily increase the family's need for wealth." *Id.* at 393–94.

⁴⁵ *See* Robert Cooter & Ariel Porat, *Anti-Insurance*, 31 J. LEGAL STUD. 203, 209–11 (2002).

⁴⁶ For additional discussion, see the text accompanying *infra* notes 185–86.

4. *Heterogeneous Claims*

Where all victims have similar claims, the application of reverse sampling is straightforward. However, even if victims' individual damages diverge, courts possess the tools to easily accommodate these cases within the reverse sampling framework.

Where victims' damages vary, courts should use a multiplier to calculate the postrandomization, actual individual awards. To illustrate, recall the numerical example set forth previously. There are 1,000,000 victims in the class, and the court randomly selects one in twenty (50,000 plaintiffs) who will actually receive the award. Assume, as before, that the common fund is \$5,000,000 and that the average individual damages are hence \$5.00. Now, however, there are two types of plaintiffs: half of the class has suffered three dollars in damages, and the others are entitled to seven dollars in damages. In this case, each chosen plaintiff should receive his individual award, multiplied by a factor of twenty. Hence, as before, the average actual individual entitlement is \$100.00. In this heterogeneous damages example, however, some plaintiffs are entitled to \$60.00 ($20 \times \3.00) and others, to \$140.00 ($20 \times \7.00).

The average individual harm in the sample is identical to the average individual damages in the class. In several cases, the total compensation using the multiplier can deviate slightly from the common fund (\$5,000,000). Where the sample of plaintiffs is large, these deviations are likely to be trivial. Where these deviations are more sizeable, courts can adjust the multiplier to exactly dispose of the common fund.⁴⁷

In sum, reverse sampling is a practical method that cuts nontrivial administrative costs to the benefit of the class. As plaintiffs are approximately risk neutral, and each can expect a larger gain on average, class members are better off. The concerns about the practical use of reverse sampling do not undermine its advantages, but rather delineate the proposal's limits.

The reverse sampling approach relies on a unique procedural device: lotteries. Notwithstanding the proposal's virtues, is the institutional use of lotteries normatively valid? The following section argues that employing lotteries in this context poses no institutional difficulties.

⁴⁷ To illustrate, assume that a 50,000 plaintiff sample results in an average individual entitlement of \$5.26. In that case, the adjusted multiplier is $100 \div 5.26 = 19$ (rather than 20). Accordingly, the low- and high-value entitlements are \$57.00 ($19 \times \3.00) and \$133.00 ($19 \times \7.00). Using this method, the total actual compensation is approximately identical to the common fund.

II. LOTTERIES?

Do we really want to cast lots in order to determine the allocation of the proceeds of small-claims class actions? Lotteries are widely perceived as a fair decisionmaking procedure. Furthermore, the institutional use of lotteries in this context should not infringe on the judiciary's legitimacy.

A. *Fairness*

Class lotteries create inequality in outcomes among plaintiffs: some plaintiffs gain more, while others receive nothing. Like plaintiffs, one might argue, are not treated alike. However, prior to casting the lots, plaintiffs are treated equally: they all expect to receive, on average, exactly the same award.⁴⁸ In fact, the very use of randomization creates equality—equality of chances (and expected values) rather than equality of outcomes. This generates procedural fairness: nonrigged lotteries represent a fair judicial decision process independent of the outcome.⁴⁹ Randomization can also avoid unfairness.⁵⁰ As one article has stated: “None of the personal characteristics that typically interfere with decision processes . . . enter procedures based on chance The rich and the powerful do not have any better chances than the poor and the humble.”⁵¹

Lotteries are indeed widely associated with procedural justice.⁵²

⁴⁸ See Adam M. Samaha, *Randomization in Adjudication*, 51 WM. & MARY L. REV. 1, 38–39 (2009).

⁴⁹ This is “pure procedural justice” in John Rawls’ terminology. JOHN RAWLS, *A THEORY OF JUSTICE* 85–86 (1971) (“If a number of persons engage in a series of fair bets, the distribution of cash after the last bet is fair, or at least not unfair, whatever this distribution is.”).

⁵⁰ This is true with respect to unfairness in outcomes between silent and informed plaintiffs. See *infra* notes 115–18 and accompanying text. Another example is partitioning jointly owned land. Using lotteries to allocate the plots might be more desirable than consensual allocation, as it avoids inequalities among owners, who are often family members. See, e.g., *Rhodes v. Cooper*, 42 So. 943, 944 (La. 1907) (“[S]ince [casting lots] is the greatest safeguard the law has thrown around partitions, it cannot be departed from where minors are interested.”).

⁵¹ Felix Oberholzer-Gee, Iris Bohnet & Bruno S. Frey, *Fairness and Competence in Democratic Decisions*, 91 PUB. CHOICE 89, 89 (1997).

⁵² The potential use of lotteries to achieve justice has produced much literature. Jens Timmermann, for example, suggests using a weighted lottery as a fair and nonconsequentialist solution to a longstanding philosophical question: whether to save the many or the few from dying. See Jens Timmermann, *The Individualist Lottery: How People Count, but Not Their Numbers*, 64 ANALYSIS 106, 110–12 (2004). Akhil Amar proposes choosing representatives by lottery voting to create “a richer democracy” in which each person truly has one vote. Akhil Reed Amar, Note, *Choosing Representatives by Lottery Voting*, 93 YALE L.J. 1283, 1283 (1984). Lotteries have also been proposed as a means to achieve colorblind admission decisions. See, e.g., Pauline T. Kim, *The Colorblind Lottery*, 72 FORDHAM L. REV. 9 (2003) (discussing the fairness of such

In a famous decision, *United States v. Holmes*,⁵³ the court convicted a crewman for not using a lottery to determine which passengers would be sacrificed to save a ship:

When . . . sacrifice of one person is necessary to appease the hunger of others, the selection is by lot. This mode is resorted to as the fairest mode, and, in some sort, as an appeal to God, for selection of the victim [W]e can conceive of no mode so consonant both to humanity and to justice In no other than this or some like way are those having equal rights put upon an equal footing, and in no other way is it possible to guard against partiality and oppression, violence and conflict.⁵⁴

Not only are lotteries generally conceived of as the fairest allocation mode, alternatives used to distribute the proceeds of small-claims class actions are not fairer.

Randomization Versus Alternatives. The use of lotteries to allocate the proceeds of small-claims class actions is fair compared to the alternatives. Jon Elster surveys alternative modes of decisionmaking where a good cannot be divided without a loss of value. His typology is illustrative of small-claims class actions in which a comprehensive distribution plan is expensive relative to individual claims. One distributional approach is “absolute equality,” i.e., dividing the good in equal shares to all beneficiaries.⁵⁵ Alas, the division process is costly, and formal equality comes at the expense of efficiency.⁵⁶ Where the equal distribution process reduces the value of the goods in question, each member should prefer a random decisionmaking process, “substituting equality of chance for equality of outcomes.”⁵⁷ The absolute equality method, which exalts formal equality among class members, forms the theoretical basis of the traditional distribution approach.⁵⁸ Given that low-value claimants are approximately risk neutral,⁵⁹ it is plausible to believe that class members would prefer lotteries to for-

lotteries). Another example is employing a lottery system to award permanent residency visas. See *infra* notes 86–87 and accompanying text.

⁵³ *United States v. Holmes*, 26 F. Cas. 360 (C.C.E.D. Pa. 1842) (No. 15,383).

⁵⁴ *Id.* at 367.

⁵⁵ JON ELSTER, SOLOMONIC JUDGMENTS 69–70 (1989).

⁵⁶ An extreme example of an inefficient equal-allocation distribution is King Solomon’s proposal to cut a child in half. *Id.* at 70.

⁵⁷ *Id.* at 69.

⁵⁸ The American Law Institute’s *Principles of the Law of Aggregate Litigation* reflect this traditional approach. See *supra* note 23 and accompanying text.

⁵⁹ See *supra* notes 36–37 and accompanying text.

mal equal distribution of the total damages, as they are not risk averse and they can expect to gain a larger award on average.

Another approach to the distribution of the common fund to its beneficiaries is queuing, where the goods are distributed on a first-come, first-served basis.⁶⁰ In the context of small-claims class actions, as will be discussed below, this approach resembles pro rata distribution—a method that is sometimes implemented when the court is able to locate only a portion of the class. This group, then, receives the entire fund at the expense of other, silent class members.⁶¹ Queuing can be perceived as a fair mode of decisionmaking where the order of the queue is based on some reasonable, substantive policy considerations or where the queue is close to a “natural lottery,” i.e., when the order reflects a random process.⁶² However, in the reality of small-claims class actions, this method generates a bias for informed, proactive class members at the expense of less informed and silent ones.⁶³ If anything, it seems that a more random process might be more publicly acceptable.⁶⁴

As lotteries are a fair allocation mode compared to the alternatives, what can be argued against their use in distributing the proceeds of small-claims class actions? Lotteries do have several drawbacks, and criticism can be raised against the very use of lotteries in judicial decisionmaking.

B. Institutional Use of Lotteries

Lotteries have been used throughout history in various legal, political, and social contexts. Cellular telephone and oil drilling licenses, the military draft, jury duty,⁶⁵ breaking ties in mayoral elections,⁶⁶ al-

⁶⁰ See ELSTER, *supra* note 55, at 70–72.

⁶¹ The pro rata approach is discussed in more detail below. See *infra* notes 105–20 and accompanying text.

⁶² See ELSTER, *supra* note 55, at 71 (“For a queue to be assimilable to a natural lottery, it must be organized in a way that does not waste resources, and the order in which people enter the queue should reflect a truly random process.”); cf. Jeremy Waldron, *One Law for All? The Logic of Cultural Accommodation*, 59 WASH. & LEE L. REV. 3, 18 (2002) (“Fairness requires some procedure—such as a lottery—or some criterion—such as greater need, for example—to determine who should get the special privilege.”).

⁶³ For a more detailed discussion, see *infra* notes 115–18 and accompanying text.

⁶⁴ There are other allocation mechanisms: rotating the goods in question among class members, ELSTER, *supra* note 55, at 72–73, looking for the neediest members and awarding them the scarce goods, *id.* at 73–74, finding the most productive members and awarding them the goods, *id.* at 75–76, awarding the goods based on previous contribution, *id.* at 76–77, or auctioning the goods, *id.* at 77–78. These methods appear irrelevant, too expensive, or practically infeasible in the context of small-claims class action proceeds distribution.

⁶⁵ See, e.g., Oberholzer-Gee, Bohnet & Frey, *supra* note 51, at 89.

location of scarce medical resources, inheritance rights, admission to schools, entitlement to public housing⁶⁷—each of these is an example of institutional use of lotteries.⁶⁸

In particular, there is an inclination to use lotteries where equal division—“absolute equality”—reduces the value of the goods and there is no alternative distribution criterion.⁶⁹ Not only is it a fair and efficient mode of allotting scarce resources, a lottery also reduces potential beneficiaries’ incentives to change their behavior. Randomization mitigates the risk of corruption⁷⁰ and discourages participants’ dishonesty.⁷¹

Notwithstanding the benefits, the use of lotteries in these contexts has several drawbacks. The following are traditional arguments against randomization. First, the use of lotteries might imply that a certain decision is not amenable to a reasoned determination.⁷² The perception of unreasoned decisionmaking might harm judicial legitimacy.⁷³ Second, the use of lotteries creates an appearance of impar-

⁶⁶ In one California town, for example, a lottery determined the winner of a tied 2002 election. Gary E. Bolton, Jordi Brandts & Axel Ockenfels, *Fair Procedures: Evidence from Games Involving Lotteries*, 115 *ECON. J.* 1054, 1055 n.5 (2005) (“No costly run-off elections, no appeals to the courts, just a cut of the cards. What could be fairer?” (quoting Lloyd de Vries, *Real Election Reform Is in the Cards*, CBSNEWS (Dec. 11, 2002), <http://www.cbsnews.com/stories/2002/12/11/opinion/garver/main532631.shtml>) (internal quotation marks omitted)).

⁶⁷ See, e.g., ELSTER, *supra* note 55, at 62–63.

⁶⁸ Other notable examples include: using lotteries to appoint officials to governmental positions in past republics such as Athens and Venice, Amar, *supra* note 52, at 1289–90, and using lotteries in law enforcement decisionmaking (e.g., baggage inspection at the Mexican border), Oberholzer-Gee, Bohnet & Frey, *supra* note 51, at 89.

⁶⁹ See Samaha, *supra* note 48, at 20–21 (“[I]f a decision is unavoidable, and particularly in cases of indivisibility, statistical randomization gains ground when sound reasons for choosing run short.”); see also Bolton, Brandts & Ockenfels, *supra* note 66, at 1055.

⁷⁰ See ELSTER, *supra* note 55, at 111 (“Random selection prevents officials from using their discretionary power to play favourites, punish enemies, enrich themselves or simply bask in the arbitrary exercise of power [and] prevents potential appointees or recipients from bribing and threatening officials.”); BARBARA GOODWIN, *JUSTICE BY LOTTERY* 169 (1992) (“[A] lottery principle might be introduced . . . in order to improve the workings of the free market [e.g., in the context of broadcasting licenses and oil drilling franchises] by preventing graft, kickbacks and other forms of underhand dealing.”); see also Samaha, *supra* note 48, at 21.

⁷¹ See, e.g., ELSTER, *supra* note 55, at 87 (“Perhaps the main argument for lottery voting is that it reconciles honesty with self-interest [Without lottery voting,] an individual may be able to ensure a social decision which is better—according to his true preferences—than the decision which would be made if he reported them correctly.”).

⁷² See *id.* at 38 (“[T]he use of lotteries to resolve decision problems under uncertainty presupposes an unusual willingness to admit the insufficiency of reason. Usually, we do not want to cope with indeterminacy, but to avoid it.”).

⁷³ See *id.* at 102 (“In legal contexts . . . ‘random’ is often synonymous with ‘whimsical’, ‘capricious’ and ‘arbitrary.’”). Whether people oppose random decisionmaking on these grounds is an empirical question. There are good reasons to believe that accurate, well-

ality, and enables decisionmakers to abdicate their responsibility to make difficult substantive decisions.⁷⁴ A related factor is accountability: it is hard to monitor random determinations and haphazardly assigned decisionmakers.⁷⁵ Third, lotteries might be an inefficient mechanism of allocating resources: they infringe upon the principle that entitlements should be distributed to those who value them the most.⁷⁶

In the context of reverse sampling, i.e., distributing the proceeds of small-claims class actions, the arguments against randomization appear weak. First, as mentioned above, lotteries are widely perceived as a fair allocation procedure, and can even substitute for a fair outcome.⁷⁷ Hence, the use of a lottery to allocate the proceeds of small-claims class actions can enhance fairness perceptions. Second, as will be discussed in detail below, the use of lotteries to allocate the proceeds of small-claims class actions masks no substantive decisionmaking and poses no legitimacy difficulties. On the contrary, it fulfills the very principle that the money belongs to the members of the class.⁷⁸ Courts are fully responsible for their substantive decision to impose liability, and the use of lotteries to distribute the money among the plaintiffs replaces no tough substantive decisionmaking. Hence, reverse sampling does not make courts unaccountable. Rather, the use of lotteries guarantees a fair and equal decisionmaking procedure,

pondered judicial decisionmaking is not that highly valued (e.g., the fact that litigants almost always prefer to settle). See LOUIS KAPLOW & STEVEN SHAVELL, *FAIRNESS VERSUS WELFARE* 248–75 (2002).

⁷⁴ See ELSTER, *supra* note 55, at 99 (noting that due to the use of lotteries, “each case might be less carefully considered [by judges and jurors]”); Carol Nicole Brown, *Casting Lots: The Illusion of Justice and Accountability in Property Allocation*, 53 *BUFF. L. REV.* 65, 73 (2005) (“Essentially, casting lots obscures the decision to avoid making difficult choices.”).

⁷⁵ See ELSTER, *supra* note 55, at 92.

⁷⁶ See *id.* at 117 (noting that lotteries serve as a cheap and readily available substitute for optimal, but more expensive, decisionmaking). A notable example is the random military draft, which fails to consider allocative efficiency—persons who place a high value on not being drafted are as likely to end up in the military as those who place a low value on not being drafted. See John R. Boyce, *Allocation of Goods by Lottery*, 32 *ECON. INQUIRY* 457, 459 (1994). An anecdotal example of allocative inefficiency from the seventeenth century is the random appointment of professors to various subjects, which “resulted in the great mathematician Jakob Bernoulli teaching medicine instead of mathematics for quite some time.” Oberholzer-Gee, Bohnet & Frey, *supra* note 51, at 89–90. However, when the randomly distributed entitlements can be costlessly traded, “there is not even a loss in allocative efficiency.” *Id.* at 89.

⁷⁷ See Bolton, Brandts & Ockenfels, *supra* note 66, at 1054 (describing an experiment which found that lotteries are perceived as fair procedures).

⁷⁸ See *PRINCIPLES OF THE LAW OF AGGREGATE LITIG.* § 3.07(b) (2010). Reverse sampling cuts administrative costs and hence also fulfills another principle: “maximizing the net value of the group of claims.” *Id.* § 1.04(b)(1).

free of biases and favoritism.⁷⁹ Finally, lotteries, in this context, do not interfere with allocative efficiency, as the class action's awards—money damages—are fungible.

These arguments notwithstanding, it seems that the judiciary has a unique aversion to the use of randomization. While this intuition is correct in some contexts, it is wrong in others. In the following paragraphs, this Article distinguishes between using lotteries where nuanced substantive decisionmaking is required and where there is no underlying consensual legal criterion for decisionmaking. While there is a reluctance to use judicial lotteries in nuanced decisionmaking on the merits, the judiciary commonly uses lotteries where there is no conclusive substantive decision rule in the background. The allocation of class action proceeds, this Article argues, requires no nuanced decision on the merits, and thus the use of reverse sampling is normatively valid.

Aversion to Lotteries Only Where Nuanced Decisionmaking Is Required. On several occasions when officials have employed lotteries, they faced harsh criticism. However, the aversion to using lotteries is not the fear of randomization in and of itself; rather, it is the use of lotteries instead of required nuanced decisionmaking that bothers us. Furthermore, the hostility toward lotteries dissipates in other contexts, where well-reasoned decisionmaking is not expected. Courts widely use lotteries in several contexts, most of them procedural, where there is no clear legal rule that should be taken into account.

The most telling evidence of the aversion to lotteries in merit decisionmaking is the fact that judges who cast lots to decide the merits of a case are castigated.⁸⁰ In one divorce case, for example, the judge had to decide where the parties' children should spend Christmas Eve.⁸¹ Upon finding that each side's arguments were equally compelling, the judge flipped a coin to decide the matter.⁸² She was publicly censured.⁸³ In another illustrative case, a judge was disciplined for tossing a coin to determine whether the defendant had committed a traffic infraction.⁸⁴ What is the source of the opposition toward tossing coins? Lotteries are not per se unethical. Rather, it is

⁷⁹ For similar biases in the context of small-claims class actions, see *infra* notes 154–62.

⁸⁰ See ELSTER, *supra* note 55, at 99; Samaha, *supra* note 48, at 27–30.

⁸¹ See *In re Brown*, 662 N.W.2d 733, 736 (Mich. 2003).

⁸² See *id.* at 737. For a discussion and a survey of several similar cases, see Samaha, *supra* note 48, at 28–29.

⁸³ *Brown*, 662 N.W.2d at 733.

⁸⁴ Turco, No. 97-2451-F-66, 1998 WL 101560, at *1 (Wash. Comm'n on Judicial Conduct Mar. 5, 1998) (advisory order of censure and admonishment).

the overt substitution of luck for reason. The judge in the first case should have considered the best interests of the children, and the judge in the second case should have evaluated the witness's credibility; instead, they both just tossed a coin. As one judicial commission explained in another case: "The public has every right to expect that a jurist will carefully weigh the matters at issue and . . . render reasoned rulings and decisions."⁸⁵

Another illustrative example of this logic is the debated diversity visa lottery. Since 1986, the United States has used a lottery to award permanent residency visas.⁸⁶ This selection process is criticized: "[A] visa to the United States is the most valuable resource that mobile foreigners can ever hope to obtain No convincing conception of justice demands . . . that this precious asset should simply be given away at random and without reference to any benefits for American society."⁸⁷ In a similar vein, other scholars argue that the random process masks, rather than ignores, substantive considerations.⁸⁸ The aversion to the diversity lottery, then, rests on the underlying substantive considerations that should have been considered, rather than the random process itself.

The Supreme Court expressed the very same logic with regard to law school admission lotteries. The Court frowned upon the idea of using lotteries to make race-neutral admission decisions, as randomization "would make that kind of [required] nuanced judgment impossible."⁸⁹ Again, what bothered the Court was the use of lotteries where "nuanced judgment" ought to be applied.⁹⁰

⁸⁵ N.Y. COMM'N ON JUDICIAL CONDUCT, ANNUAL REPORT OF THE NEW YORK STATE COMMISSION ON JUDICIAL CONDUCT 88 (1984) (removing a judge from office for tossing a coin to determine a defendant's jail term). The commission also held that "[j]udicial judgment is a non-delegable duty. For a judge to abdicate this judicial judgment to the flipping of a coin gives the appearance of reckless dispensation of justice." *Id.* at 87; *see also* Samaha, *supra* note 48, at 28.

⁸⁶ Liav Orgad & Theodore Ruthizer, *Race, Religion and Nationality in Immigration Selection: 120 Years After the Chinese Exclusion Case*, 26 CONST. COMMENT. 237, 289-90 (2010).

⁸⁷ PETER H. SCHUCK, *DIVERSITY IN AMERICA: KEEPING GOVERNMENT AT A SAFE DISTANCE* 128 (2003).

⁸⁸ *See* Stephen H. Legomsky, *Immigration, Equality and Diversity*, 31 COLUM. J. TRANSNAT'L L. 319, 321, 326 (1993) ("the diversity [lottery] is merely the latest in a series of congressional attempts, spanning more than a century, to influence the ethnic composition of the United States immigrant stream [It] is new in form but not in spirit."); Liav Orgad & Theodore Ruthizer, *supra* note 86, at 290 ("Lottery visas look neutral. Nevertheless, a closer look reveals a fiery debate on their motivation and impact.").

⁸⁹ *Grutter v. Bollinger*, 539 U.S. 306, 340 (2003).

⁹⁰ Other examples of institutional contexts that seem innately inappropriate for randomized decisionmaking are death penalty commutations and exercises of prosecutorial discretion.

Perhaps the best evidence for the proposition that the institutional use of randomization may be normatively valid is the prevalent use of lotteries by the judiciary itself. Lotteries are common in several judicial contexts, most of which are procedural questions incidental to the merits of the case. One such example is the random selection of jurors—a widely practiced phenomenon.⁹¹ And, even more so, judges are often assigned to cases by lotteries.⁹² Random sampling has been used in complex litigation contexts to determine the defendant's aggregate liability.⁹³ Judges employ their equitable powers to hold lotteries where they have to partition jointly owned land and allocate the particular plots.⁹⁴

As these examples show, lotteries in judicial decisionmaking are by no means proscribed per se. Lotteries are condemned where nuanced judicial decisionmaking on the merits is required, but are widely used where they do not replace consensual legal considerations judges ought to take into account.⁹⁵ Of course, the exact boundary between merit-based, nuanced decisionmaking, and other contexts

See Daniel T. Kobil, *Due Process in Death Penalty Commutations: Life, Liberty, and the Pursuit of Clemency*, 27 U. RICH. L. REV. 201, 216 (1993).

⁹¹ See ELSTER, *supra* note 55, at 90.

⁹² See Samaha, *supra* note 48, at 47 (“Today the process of assigning cases to judges is pervaded with lotteries”). The Southern District of New York is one notable example of a court that uses a randomized case assignment process. *Id.* at 48–49.

⁹³ See *supra* note 21; see also Alexandra D. Lahav, *Bellwether Trials*, 76 GEO. WASH. L. REV. 576, 581 (2008) (noting that in binding bellwether trials, “the court will choose a random sample of cases to try to a jury”); Samaha, *supra* note 48, at 30 (arguing that courts are more prone to resort to randomly selected bellwether trials, but less inclined to use random sampling to resolve similar issues for all plaintiffs).

⁹⁴ See Samaha, *supra* note 48, at 33. In one illustrative decision, the court approved the use of lotteries in the following terms:

The procedure for the partitioning of real property is governed by . . . Article 1 of Chapter 46 of our General Statutes. No section in that Article makes provision for a drawing to determine by lot or chance the manner in which the separate parcels of partitioned real property should be allotted Nevertheless, in this state partition proceedings have been consistently held to be equitable in nature Therefore, there can be no question . . . as to the validity of . . . conduct[ing] a lottery [in this context].

Dunn v. Dunn, 245 S.E.2d 580, 582 (N.C. Ct. App. 1978) (internal quotation marks and citation omitted).

⁹⁵ Professor Samaha, who focuses on lotteries in assigning judges to cases, identifies a similar distinction between the use of lotteries in decisionmaking on the merits and elsewhere. He concludes that “we are left with an especially awkward combination: judges habitually randomize case assignments while they routinely punish merits randomization.” Samaha, *supra* note 48, at 53. One explanation for this differential treatment to merits lotteries, which Professor Samaha does not find completely convincing, is that “overt merits lotteries have a uniquely insulting quality that gives rise to a justified feeling of disrespect.” *Id.* at 58.

may be murky. But the general pattern is clear: lotteries are a normatively valid procedure to determine controversies for which a consensual substantive decision rule does not exist.

The proposed lottery, dispersing the proceeds of small-claims class actions, does not substitute for merit-based decisionmaking. Holding a lottery to divide the entire compensation among class members is not akin to tossing a coin to decide with which parent a child should spend Christmas Eve. Once class-wide damages are determined, the precise allocation of monies—how much each member receives from the common fund—is not a nondelegable duty that directs judges to apply a nuanced decision rule and carefully weigh the matters.

Can there even be any workable criterion, apart from randomization, to award money to some plaintiffs at the expense of others? As the next Part demonstrates, there is no consensual legal decision rule that controls the allocation of the proceeds of small-claims class actions. The traditional rule mandates compensation for each and every claimant. In actuality, however, this rule is infeasible where individual awards are small.⁹⁶ Hence, residual funds are a virtually certain phenomenon in small-claims class actions. And where there are residual funds, broad equitable powers substitute for the traditional distribution approach.⁹⁷ The leftover money can go, at the court's discretion, to one of the following entities: the defendant, already-compensated plaintiffs, the government, future consumers, or charities. Because judges already have wide discretion to choose among these alternative distribution schemes, they should not be prohibited from holding lotteries to allocate the money among the members of the class. As the next Part shows, there are very good reasons to use lotteries in this context: the proposed sampling is a superior distribution mechanism to all current alternatives.

III. REVERSE SAMPLING AND EXISTING MECHANISMS

A. *Current Solutions to the Problem of Small-Claims Class Actions*

Individual claims are often very low relative to the efforts required to process the payment, search for the beneficiaries, or redeem the money. Sometimes, individual claims are so small that no individ-

⁹⁶ See *supra* notes 38–39 and accompanying text.

⁹⁷ See Jois, *supra* note 40, at 271–72 (“When it is no longer cost effective to redistribute money, the court has the power to somewhat arbitrarily decide where the leftover money should be allocated.”); see also *Van Gemert v. Boeing Co.*, 739 F.2d 730, 737 (2d Cir. 1984); *supra* note 40 and accompanying text.

ual distribution scheme is feasible.⁹⁸ In other cases, not all class members can be located, and the small individual claims prohibit other members from filing the required statement and cashing their awards.⁹⁹ Either way, the prospect of some residual unclaimed funds is “virtually certain.”¹⁰⁰ “The problem . . . is not rare and often involves significant amounts of money.”¹⁰¹

The academic literature on class actions is rich, but it tends to focus on the process of imposing liability on defendants.¹⁰² While there has been some discussion on distributing unclaimed funds, usually the literature either supports or criticizes existing mechanisms courts use rather than propose new ones.¹⁰³ As will be demonstrated below, courts have been employing five main alternative methods for allocating money in small-claims class actions; reverse sampling—the new method proposed here—is superior to each of these solutions. Current distribution mechanisms are inefficient. They invite abuse of

⁹⁸ See CONTE & NEWBERG, *supra* note 13, § 10:14.

⁹⁹ See *id.*; Hensler, *supra* note 14, at 202 (“In damage class actions, not all class members come forward to claim the full amount defendants make available for compensation”); see also Forde, *supra* note 40, at 19.

¹⁰⁰ CONTE & NEWBERG, *supra* note 13, § 10:14. For examples of actual leftovers in consumer class actions, see Hensler, *supra* note 14, at 201.

¹⁰¹ Jois, *supra* note 40, at 264–65 (surveying class actions in which unclaimed monies were left, ranging from \$1 million to \$32 million); see also SEC v. Bear, Stearns & Co., 626 F. Supp. 2d 402, 403 (S.D.N.Y. 2009) (“The quandary of what to do with undisbursable funds presents cautionary lessons for regulators, courts, and all other participants in securities fraud litigation.”).

¹⁰² For examples of innovative mechanisms to improve the deterrent potential of class actions, see Pamela H. Bucy, *Private Justice*, 76 S. CAL. L. REV. 1 (2002) (extending *qui tam* actions); John C. Coffee, Jr., *Rethinking the Class Action: A Policy Primer on Reform*, 62 IND. L.J. 625, 658–64 (1986) (restricting opt-outs); Alon Klement, *Who Should Guard the Guardians?: A New Approach for Monitoring Class Action Lawyers*, 21 REV. LITIG. 25 (2002) (third party monitoring); Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs’ Attorney’s Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 105–16 (1991) (auctions); David Rosenberg, *Mandatory-Litigation Class Action: The Only Option for Mass Tort Cases*, 115 HARV. L. REV. 831 (2002) (mandatory class actions); 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, 2105 (1995) (empowered lead plaintiff).

¹⁰³ See, e.g., Gail Hillebrand & Daniel Torrence, *Claims Procedures in Large Consumer Class Actions and Equitable Distribution of Benefits*, 28 SANTA CLARA L. REV. 747 (1988); Jois, *supra* note 40; Martin H. Redish, Peter Julian & Samantha Zyontz, *Cy Pres Relief and the Pathologies of the Modern Class Action: A Normative and Empirical Analysis*, 62 FLA. L. REV. 617 (2010); Kerry Barnett, Note, *Equitable Trusts: An Effective Remedy in Consumer Class Actions*, 96 YALE L.J. 1591 (1987); DeJarlais, *supra* note 40; Draba, *supra* note 40; Anna L. Durand, Note, *An Economic Analysis of Fluid Class Recovery Mechanisms*, 34 STAN. L. REV. 173 (1981); Stewart R. Shepard, Comment, *Damage Distribution in Class Actions: The Cy Pres Remedy*, 39 U. CHI. L. REV. 448 (1972); Sam Yospe, Note, *Cy Pres Distributions in Class Action Settlements*, 2009 COLUM. BUS. L. REV. 1014.

power and they cannot meet the dual goals of deterring defendants and compensating victims.

1. *Reversion to Defendant*

Defendants sometimes argue that any unclaimed, residual funds should be returned to them. This distribution mechanism, of course, reduces the deterrent power of class actions, as the defendant pays less than the full harm it inflicted on the victims. Indeed, this solution is rejected by most courts.¹⁰⁴

2. *Distributing Remaining Funds Pro Rata to Class Members*

A second mechanism is pro rata distribution to some class members. Where some plaintiffs claimed the money and others did not, courts can distribute the residual to the first group. This is the method the American Law Institute (“ALI”) endorses when “funds remain after distributions.”¹⁰⁵ Conceptually, this distribution scheme envisions several stages.¹⁰⁶ In the first stage, after the notice of class action, class members are expected to show up and cash their awards. In the intermediate stages, after finding out that many plaintiffs remained silent, a broader search might be conducted to induce more class members to claim their money. In the final stage, the court distributes whatever money is left to those who did file a claim in the previous stages.¹⁰⁷

The ALI’s support notwithstanding, some courts dislike the pro rata mechanism.¹⁰⁸ Allegedly, it provides an unfair windfall to the

¹⁰⁴ See, e.g., Forde, *supra* note 40, at 23; Yospe, *supra* note 103, at 1042–44. Some courts, however, have approved this distribution mechanism. See, e.g., Van Gemert v. Boeing Co., 739 F.2d 730, 730 (2d Cir. 1984); Jois, *supra* note 40, at 271–72.

¹⁰⁵ PRINCIPLES OF THE LAW OF AGGREGATE LITIG. § 3.07(b) (2010).

¹⁰⁶ See *Id.* § 3.07(b) (“If . . . funds remain after distributions . . . the settlement should . . . provide for further distributions to participating class members unless the amounts involved are too small . . .”). One court describes its pro rata distribution plan as follows:

The plan calls for the continued re-distribution of unclaimed funds to class members according to their pro rata shares, until the costs of such re-distributions make it economically unfeasible to continue doing so This approach is consistent with the latest draft of the American Law Institute’s Principles of the Law of Aggregate Litigation.

In re Tyco Int’l, Ltd. Multidist. Litig., 535 F. Supp. 2d 249, 262 (D.N.H. 2007). For another illustrative example of the multiple phases involved, see *SEC. v. Bear, Stearns & Co.*, 626 F. Supp. 2d 402, 417 (S.D.N.Y. 2009), and the text accompanying note 114, *infra*.

¹⁰⁷ See PRINCIPLES OF THE LAW OF AGGREGATE LITIG. § 3.07 illus. 2 (2010) (“[A]t the end of the claims period, [the first-best solution is] additional payments to identified class members [unless these additional payments] would not be economically viable.”).

¹⁰⁸ See Yospe, *supra* note 103, at 1045.

claiming plaintiffs¹⁰⁹ at the expense of silent class members, who “will not receive any compensation, even indirectly.”¹¹⁰ In addition to fairness, another concern is “the adequacy of representation where the interests of the named plaintiffs lie in keeping the other class members uninformed.”¹¹¹

The pro rata solution bears some resemblance to the reverse sampling approach, as some members of the class are overcompensated at the expense of others. However, as will be further discussed, the two solutions represent distinct perspectives that lead to different distribution processes. In particular, the pro rata mechanism requires additional administrative costs of reaching out to as many plaintiffs as possible, and holding multiple stages of distribution.

The Differences Between Reverse Sampling and Pro Rata Distribution. At first blush, the two distribution schemes might look similar: some class members receive the entire fund, while others get nothing. In both, one might argue that some lucky class members receive an unfair windfall. However, the two methods diverge, conceptually and practically.

The purpose of the pro rata mechanism is to distribute individual awards to as many class members as possible. The search for class members is not random; rather, it should be based on cost effectiveness: how to locate the largest number of plaintiffs with the cheapest expenses. The purpose of reverse sampling, in contrast, is to distribute more money to fewer randomly selected members. In fact, reverse sampling repudiates extensive distributions; when too many class members receive compensation, more money is spent on per-award administrative costs.

Practically, a court that adheres to the ALI’s instructions and implements the pro rata approach should take all economically viable measures to locate and compensate as many class members as possible. Typically, letters are sent first. If participation is low, courts can use “publication, posting, public service announcements, or other means, apart from individual mailed notices.”¹¹² To further identify

¹⁰⁹ See *In re Folding Carton Antitrust Litig.*, 557 F. Supp. 1091, 1107 (N.D. Ill. 1983), *aff’d*, 774 F.2d 1252 (7th Cir. 1984); see also Yospe, *supra* note 103, at 1045. In one illustrative decision, the lower court declined a pro rata distribution to already-compensated class members as this plan would allow existing claimants to “recover 116% of their single damages.” *Fears v. Wilhelmina Model Agency, Inc.*, No. 02 Civ. 4911(HB), 2007 WL 1944343, at *8 (S.D.N.Y. July 5, 2007), *vacated*, 315 Fed. App’x. 333 (2d Cir. 2009).

¹¹⁰ Shepard, *supra* note 103, at 453.

¹¹¹ *Id.*

¹¹² CONTE & NEWBERG, *supra* note 13, § 10:14.

silent plaintiffs, courts may attempt to locate class members “by referring to public records such as driver registrations or Social Security records, by checking telephone directories, by hiring professional locator services, or by other means.”¹¹³ These efforts are costly. Often, they also tend to be useless. One court describes this process in the following terms:

Consistent with the premise articulated by the American Law Institute, this Court and the Fund Administrator exhausted every possible avenue to distribute funds to aggrieved [plaintiffs]. While the first distribution phase resulted in a significant response rate—44%—and the Fund Administrator distributed \$284,919,173 . . . this Court determined that more could be done. As a result, a second distribution phase employed targeted outreach aimed at increasing the number of [plaintiffs] filing claims. This additional effort yielded 10,299 additional claims, leading to the distribution of another \$92,956,548 to aggrieved [plaintiffs]. In everyone’s estimation, the law of diminishing returns suggests the game is no longer worth the candle.¹¹⁴

Reverse sampling envisions a different process. The number of identified class members is irrelevant and these costly recurrent search and distribution efforts are avoided. Rather, reverse sampling strives for randomness: it is preferable to locate a small, random sample of class members, to which the entire fund is funneled.

In addition to administrative savings, the use of reverse sampling in lieu of pro rata distribution potentially mitigates another concern. As mentioned, the pro rata distribution is sometimes perceived as unfair, as it leaves the plaintiffs that were located with a windfall and leaves silent plaintiffs with nothing.¹¹⁵ This perception of unfairness makes some sense, as courts essentially prefer class members who are easier to locate—perhaps the more informed ones, who read the right newspapers and websites—at the expense of the hard-to-reach and uninformed members.¹¹⁶ Likewise, even where all plaintiffs are advised, pro rata distribution might still favor knowledgeable plaintiffs who find it easier to prove their claims.¹¹⁷ Purely randomized distribu-

¹¹³ *Id.*

¹¹⁴ *SEC v. Bear, Stearns & Co.*, 626 F. Supp. 2d 402, 417 (S.D.N.Y. 2009).

¹¹⁵ *See supra* notes 109–10 and accompanying text.

¹¹⁶ *See, e.g.*, *Barnett*, *supra* note 103, at 1596 (“From the perspectives of both the victims and society as a whole, the losses of absentees are no less serious than the losses of . . . readily identifiable plaintiffs. All injuries deserve the same equitable resolution.”).

¹¹⁷ Some class members find even the mere filing of a statement complicated. *See CONTE*

tion does not discriminate between class members on the basis of their access to information about the action.¹¹⁸ Hence, lottery allocation is likely to raise fewer concerns about an unfair windfall to proactive and knowledgeable class members.

Certainly, a purely random sample is an idealization, and cannot always be achieved. In some small-claims class actions, most plaintiffs can easily be found; these cases are more amenable to lottery distribution.¹¹⁹ In other cases, it is more difficult to locate plaintiffs. Courts can attempt, then, to randomly search for plaintiffs (e.g., all the consumers in a certain month, all purchasers in a certain store, etc.).¹²⁰ In yet other cases, however, a random search may be too complicated to carry out.

The distinction between pro rata distribution and reverse sampling, then, is not clear cut. The choice of allocation mechanism in actual cases is more likely to reflect a continuum between lotteries and pro rata distribution. And, on the margin, there might be distribution schemes that resemble both: few actual beneficiaries, one-shot search for plaintiffs, etc. Moreover, courts that do take the pro rata approach should acknowledge its lottery-like nature and take into account the implications. The search for class members, for example, should not strive to reach maximum numbers, contrary to the dictates of the pro rata approach. Furthermore, the search should be based, to the extent possible, on random characteristics. Where random allocation is impossible, courts should encourage a small, nonrandom fraction of the group of plaintiffs to step forward, thereby acknowledging that some beneficiaries remain silent, and that the efforts required to locate those plaintiffs are counterproductive.

3. *Escheat to the State*

The third distribution mechanism allows the court to turn over the residual funds to the Federal Treasury or to the state. This method envisions two stages: first, money is distributed to some plaintiffs, and

& NEWBERG, *supra* note 13, § 10:14 (noting that for some plaintiffs, “the notice language may be unintelligible . . . or misunderstood”); Barnett, *supra* note 103, at 1596 (“Often, absenteeism is simply a result of . . . lack of understanding of one’s legal rights . . .”).

¹¹⁸ See Oberholzer-Gee, Bohnet & Frey, *supra* note 51, at 89 (“Random decision mechanisms are the embodiment of fair allocation procedures”). For more on the fairness of lotteries, see *supra* notes 48–54 and accompanying text.

¹¹⁹ For one such example see *supra* note 24.

¹²⁰ When the pool of targeted class members is smaller, the court can employ more sophisticated and costly search efforts. For examples of these more extensive search efforts, see *supra* text accompanying note 113.

second, the remainder goes to the state.¹²¹ An extended version of this approach skips the first stage and funnels the entire fund directly to the government.¹²² Those who praise this mechanism assert that this is actually what all plaintiffs want. Ex ante, the argument goes, victims want to be compensated equally.¹²³ Where such compensation is impossible, what can be better than diverting the money to the government? Allegedly, “all individuals expect to share equally in the provision of benefits by the state.”¹²⁴

This method has its own problems. First, it fails to compensate the victims and instead rewards the state.¹²⁵ This might raise separation of powers concerns.¹²⁶ The argument that all victims obtain an equal benefit from a richer government is also questionable. Similarly, it is by no means self-evident that victims want, ex ante, the money to be escheated to the state. Moreover, this mechanism creates a trilateral process, as it implicates another party in the litigation: the government,¹²⁷ and the prospect of a large award might distort the government’s incentives.

The escheat mechanism transfers the plaintiffs’ awards to the state treasury to be used at the government’s discretion.¹²⁸ Hence, escheat to the state is essentially akin to a tax levied on the group of

¹²¹ Redish, Julian & Zyontz, *supra* note 103, at 619.

¹²² For this suggestion, see Jois, *supra* note 40, at 259–60.

¹²³ *See id.* at 282.

¹²⁴ *Id.* at 282–83.

¹²⁵ The term “escheat” is illustrative. Originally, the concept referred to the reversion of property to the state when there was no individual to claim or inherit it. *See BLACK’S LAW DICTIONARY* 623 (9th ed. 2009). When the group of claimants is known, there is no reason to transfer the claimants’ entitlement to the state.

¹²⁶ Redish, Julian, and Zyontz argue that compensating not-for-profit organizations in lieu of class members creates constitutional concerns: “the practice [of compensating a third party rather than class members] violates separation of powers because through the wholly improper mechanism of a purely procedural device, the substantive law is effectively transformed from a compensatory remedial structure to the equivalent of a civil fine.” Redish, Julian & Zyontz, *supra* note 103, at 641. The argument is even more potent when the third-party beneficiary is the government.

¹²⁷ See Forde, *supra* note 40, at 21, for an actual example of governmental intervention in the litigation over the appropriate distribution plan. As Redish, Julian, and Zyontz argue, trilateral process, which substitutes traditional adversary adjudication, might raise constitutional concerns. *See* Redish, Julian & Zyontz, *supra* note 103, at 641 (“[The] less-than-fully-adversary trilateral process [is] wholly unknown to the adjudicatory structure contemplated by Article III.”).

¹²⁸ Theoretically, the court can direct the government to use the funds for specific purposes (“earmarked escheat”). Practically, the government retains complete discretion to do whatever it wants with these funds, as “nothing prevents the government from diverting the earmarked funds away from the intended purpose [or reducing] existing budget allocations proportionately.” DeJarlais, *supra* note 40, at 752; *see also* Barnett, *supra* note 103, at 1599 (“[T]here is

plaintiffs.¹²⁹ As it is equally levied on all members of the class, escheat is a regressive tax.¹³⁰ Even more bothersome, the prospective award might create perverse incentives for the government,¹³¹ especially in highly regulated areas of the law and where public enforcement complements private enforcement.¹³² When a state is likely to gain a sizeable share of the proceeds of consumer class actions, for instance, it might be driven to impose a laxer regulation on standard form contracts. Similarly, where the government's investigations can stimulate private litigation, the looming escheat might induce it to encourage private enforcement, thus creating overdeterrence.¹³³ Escheat to the state, then, might lead to inefficient governmental intervention that eases the levying of taxes and their collection.

In sum, not only does escheat to the government fail to compensate victims, it also distorts its ex ante incentives for optimal regulation. Indeed, courts do not often employ this distribution method¹³⁴—“it is usually regarded as a last resort.”¹³⁵

4. *Fluid Fund—Price Reduction*

Under this distribution alternative, rather than compensating the victims, courts can compensate other prospective consumers, e.g., through a price reduction. An illustrative case is *Daar v Yellow Cab Co.*,¹³⁶ in which the defendants set the meter rates in excess of those

nothing to prevent the legislature from scaling back its own allocations in an amount equal to the escheat.”); Durand, *supra* note 103, at 180.

¹²⁹ Cf. Martha A. Churchill, *Fluid Recovery: Not a Class Act*, 72 MICH. B.J. 1184, 1185 (1993); Hillebrand & Torrence, *supra* note 103, at 765; David C. Auten, Note, *Modern Rationales of Escheat*, 112 U. PA. L. REV. 95, 133 (1963); DeJarlais, *supra* note 40, at 751.

¹³⁰ Moreover, oftentimes the victims of the class are poorer than average, and taxing them is particularly unjust.

¹³¹ For a similar argument, see Leon E. Trakman, *David Meets Goliath: Consumers Unite Against Big Business*, 25 SETON HALL L. REV. 617, 642 (1994).

¹³² Jois, who praises the escheat mechanism, notes that when the state is a party to the proceedings (defendant, in his example), the escheat proposal should be qualified. See Jois, *supra* note 40, at 298. He fails to observe, however, that in many areas—even when the state is not a formal party—it does directly influence the legal background either by regulation or public enforcement.

¹³³ See Howard M. Erichson, *Coattail Class Actions: Reflection on Microsoft, Tobacco, and the Mixing of Public and Private Lawyering in Mass Litigation*, 34 U.C. DAVIS L. REV. 1, 30–35 (2000), for a discussion on the governments' conflicting interests in similar situations. Notable areas of the law in which public regulation interweaves with private enforcement are securities and antitrust.

¹³⁴ See Jois, *supra* note 40, at 273; Yospe, *supra* note 103, at 1047.

¹³⁵ State v. Levi Strauss & Co., 715 P.2d 564, 572 (Cal. 1986).

¹³⁶ Daar v. Yellow Cab Co., 433 P.2d 732 (Cal. 1967).

approved by the utility commission.¹³⁷ The settlement fund was to be returned to the class by reducing cab fares in future years.¹³⁸

One drawback of this method is obvious: the original victims are rarely compensated. But there are even deeper problems with the price reduction approach: ironically, price reduction can be a boon for the defendant, who now enjoys a competitive advantage.¹³⁹ Hence, price reduction for prospective clients will generally fail to achieve optimal deterrence.¹⁴⁰ Finally, the price reduction mechanism entails “substantial operating costs” and its implementation requires “sophisticated skills of economic analysis.”¹⁴¹

5. *Cy Pres Distribution*

This distribution mechanism has become increasingly popular,¹⁴² as well as increasingly controversial.¹⁴³ Instead of compensating the victims, the cy pres method diverts the money to “its next best compensation use.”¹⁴⁴ The idea is simple and appealing: channeling the funds to a third party, such as a charity, whose goals indirectly benefit the victims.¹⁴⁵

In actuality, however, things are not as rosy as they may seem at first blush. The cy pres mechanism is fraught with problems. First, class members are not compensated;¹⁴⁶ rather, a trilateral adjudication

¹³⁷ *Id.* at 737.

¹³⁸ See CONTE & NEWBERG, *supra* note 13, § 10:18.

¹³⁹ See *id.*

¹⁴⁰ The price reduction system can work where the defendant has a monopoly or “where the reduced prices are not likely to attract purchasers at the expense of substitute products.” *Id.* § 10:18 (quoting II ONTARIO LAW REFORM COMM’N, REPORT ON CLASS ACTIONS 579 (1982) (internal quotation marks omitted)); see also Durand, *supra* note 103, at 201 (“[T]he price mechanism effectively meets the goal of compensating the injured plaintiff only when the defendant is a monopolist and the reduced price is greater than the cost of producing the good.”).

¹⁴¹ Durand, *supra* note 103, at 201.

¹⁴² See Redish, Julian & Zyontz, *supra* note 103, at 661. Based on a dataset of federal cy pres class actions between 1974 and 2008, the authors suggest that there is a “trend in the growth of [cy pres] awards over time.” *Id.* at 652–53.

¹⁴³ See, e.g., Jois, *supra* note 40, at 260, 270–71; Redish, Julian & Zyontz, *supra* note 103, at 621–23; Yospe, *supra* note 103, at 1021–36; Liptak, *supra* note 6.

¹⁴⁴ CONTE & NEWBERG, *supra* note 13, § 10:17.

¹⁴⁵ Another version of the cy pres mechanism is establishing an ongoing equitable trust that is supervised by the court and designed to the broad benefits of the group of plaintiffs. See Barnett, *supra* note 103, at 1600–09. Of course, administering such a trust is more costly than directly transferring the money to charities. See, e.g., Forde, *supra* note 40, at 21.

¹⁴⁶ For this reason, the ALI advises a parsimonious use of the cy pres doctrine: it should only be used when class members cannot be easily identified or when the individual distributions are small. See PRINCIPLES OF THE LAW OF AGGREGATE LITIG. § 3.07(a) (2010) (“If individual class members can be identified through reasonable effort, and the distributions are sufficiently

process distributes a windfall to a third-party beneficiary. These features might raise constitutional concerns.¹⁴⁷ Moreover, transferring the money to charity is supposed to fulfill class members' preferences, but who knows what class members want? Attorneys and courts do not survey the class before deciding where to funnel the money on its behalf.¹⁴⁸

While "there must be a 'nexus' between the injury sustained by the class and the prospective benefit that the class obtains through the distribution of residual funds to cy pres beneficiaries,"¹⁴⁹ such a nexus hardly exists in many cases,¹⁵⁰ and the cy pres practice seems to be "getting out of hand."¹⁵¹ In one case, for example, \$700,000 was distributed to the American Red Cross for Hurricane Katrina Relief, allegedly remedying price fixing of infant formula.¹⁵² In another case, the court approved cy pres grants to fifteen beneficiaries, ranging from schools, to the Legal Aid Bureau, to an art museum.¹⁵³

The unfettered judicial discretion to dole out money through the cy pres mechanism is troubling.¹⁵⁴ As Professor Samuel Issacharoff—

large to make individual distributions economically viable, settlement proceeds should be distributed directly to individual class members."). Similarly, when some class members are easily identified and others are not, the ALI advises doling out the remaining money pro rata to the already-identified class members. *See id.* § 3.07(b).

¹⁴⁷ *See supra* notes 126–27.

¹⁴⁸ *Cf.* Churchill, *supra* note 129, at 1187 (asserting that no class counsels "are known to have surveyed the consuming public they 'represent[]'" and that "[i]n [one case,] an intervenor suggested a poll of class preferences, but that request was denied").

¹⁴⁹ Yospe, *supra* note 103, at 1018–19.

¹⁵⁰ For examples and a more detailed discussion, *see id.* at 1023–26.

¹⁵¹ *See* Liptak, *supra* note 6 (quoting Professor Samuel Issacharoff).

¹⁵² *In re* Infant Formula Multidist. Litig., No. 4:91-CV-00878-MP, 2005 WL 2211312, at *2–3 (N.D. Fla. Sept. 8, 2005).

¹⁵³ *Superior Beverage Co. v. Owens-Ill., Inc.*, 827 F. Supp. 477, 480–86 (N.D. Ill. 1993). A number of other examples exist. In one price-fixing cy pres case, the benefiting organizations included civil legal services and a medical center. *See Fears v. Wilhelmina Model Agency, Inc.*, 02-Civ.4911(HB), 2005 WL 1041134, at *11 (S.D.N.Y. May 5, 2005), *aff'd in part, vacated in part sub nom.* *Masters v. Wilhelmina Model Agency, Inc.*, 473 F.3d 423 (2d Cir. 2007). In a securities fraud case, the cy pres award went to a securities class action research center at Stanford Law School. *See In re Wells Fargo Sec. Litig.*, 991 F. Supp. 1193, 1197–98 (N.D. Cal. 1998). In yet another securities fraud suit, the court awarded the cy pres grant to a legal aid society. *See Jones v. Nat'l Distillers*, 56 F. Supp. 2d 355, 360 (S.D.N.Y. 1999). In one consumer class action, several legal aid organizations received cy pres awards. *See* DEBORAH R. HENSLER ET AL., CLASS ACTION DILEMMAS: PURSUING PUBLIC GOALS FOR PRIVATE GAIN 211–23 (2000) (discussing *Selnick v. Sacramento Cable*, No. 541,907 (Cal. Super. Ct. 1996)). For a survey of other cases that demonstrate the "attenuated connection between the direct interests of the class members and the charity receiving the cy pres award," *see* Redish, Julian & Zyontz, *supra* note 103, at 635–37.

¹⁵⁴ However, judges and counsel seem to support the cy pres doctrine and oppose competing solutions. *See* Liptak, *supra* note 6 ("Lawyers and judges have grown used to controlling

the reporter for the ALI's *Principles of the Law of Aggregate Litigation* project—warns, “[i]t is . . . an invitation to wild corruption of the judicial process.”¹⁵⁵ Apparently, the selection of the winning charity is biased toward the personal preferences of the presiding judge and the attorneys.¹⁵⁶ Many cy pres grants are made to legal aid societies or charitable arms of bar associations,¹⁵⁷ in which plaintiffs’ attorneys are heavily involved.¹⁵⁸ An illustrative example is an antitrust case in which the class attorney proposed a cy pres distribution to The George Washington University Law School, his alma mater;¹⁵⁹ the court approved.¹⁶⁰ Another problem is localism bias.¹⁶¹ In a national class action that was adjudicated in Georgia, for example, the main beneficiaries were Georgia charities.¹⁶²

these pots of money, and they enjoy distributing them to favored charities, alma maters and the like.”).

¹⁵⁵ *Id.*

¹⁵⁶ For a more detailed discussion, see Yospe, *supra* note 103, at 1027–31. Settlement agreements, in particular, allow attorneys to divert the unclaimed funds according to their personal preferences. See CONTE & NEWBERG, *supra* note 13, § 10:15 (“In a settlement context, subject to court approval, counsel for the parties have great flexibility in negotiating an agreement concerning how any unclaimed balance of an aggregate class recovery should be distributed.”).

¹⁵⁷ See Amy Sings in the Timber, *Legal Aid Is Paid a Visit by an Old Friend*, MONT. LAW., Dec. 2007–Jan. 2008, at 26, 26 (“Since the early 1990s, the cy pres doctrine has been revived as a means for distributing residual funds in class-action lawsuits to legal aid and address-to-justice programs.”); see also Forde, *supra* note 40, at 44 (“[M]any [cy pres charitable purposes] are devoted to improvements in the administration of justice.”); Yospe, *supra* note 103, at 1027. In addition to legal aid societies, law schools and hospitals are also popular targets for cy pres awards. See Liptak, *supra* note 6.

¹⁵⁸ See Dick, *supra* note 17, at 82–83 (“[C]y pres grants in several recent cases have gone to advocacy groups that count among their board members the same plaintiffs’ attorneys who negotiated the fluid recovery settlement.”). No wonder, then, that these groups have been lobbying legislatures to institutionalize the cy pres mechanism, and some states have indeed enacted new statutes accordingly. See Liptak, *supra* note 6.

¹⁵⁹ *Diamond Chem. Co., v. Akzo Nobel Chems.*, No. 01-2118(CKK), 2007 WL 2007447, at *1 (D.D.C. July 10, 2007). The cy pres grant was aimed at developing a Center for Competition Law at The George Washington University Law School. See Yospe, *supra* note 103, at 1028.

¹⁶⁰ *Diamond Chem.*, No. 01-2118(CKK), 2007 WL 2007447, at *5. For a similar example in which plaintiffs’ counsels, alumni of Vanderbilt Law School, recommended a cy pres award to their alma mater to establish a dispute resolution program, see Jois, *supra* note 40, at 266.

¹⁶¹ Yospe, *supra* note 103, at 1030 (“[T]here is a tendency for charities located near the district in which the class action was filed to benefit disproportionately from cy pres distributions.”).

¹⁶² See *In re Motorsports Merch. Antitrust Litig.*, 160 F. Supp. 2d 1392, 1396–98 (N.D. Ga. 2001). In a Southern District of New York decision, the cy pres awards were distributed to New York City organizations even though most of the members in the class were not from the New York City metropolitan area. See Jois, *supra* note 40, at 267 n.32 (discussing *Fears v. Wilhelmina Model Agency, Inc.*, 02-Civ.4911(HB), 2005 WL 1041134 (S.D.N.Y. May 5, 2005), *aff’d in part, vacated in part sub nom. Masters v. Wilhelmina Model Agency, Inc.*, 473 F.3d 423 (2d Cir. 2007)).

Unfettered judicial discretion leads to yet another problem with the cy pres doctrine. The lucrative awards induce organizations, particularly charitable arms of bar associations, to lobby for themselves as potential beneficiaries of cy pres grants.¹⁶³ Such efforts made to publicize legal aid societies might be cost effective from the organization's perspective, as they increase the odds of winning a cy pres grant. However, from a social perspective, this race is a pure waste.¹⁶⁴

Moreover, even the seemingly greatest virtue of cy pres grants—the ease of administering them—is not wholly fulfilled. First, careful judges do not choose beneficiaries at their whim. Rather, they invite charitable associations to apply and hold hearings in which the most appropriate organizations have the opportunity to be heard.¹⁶⁵ Alternatively, cautious courts can delegate the task of sorting beneficiaries to appointed committees.¹⁶⁶ Second, administrative inefficiency can stem from ongoing supervision: courts sometimes want to make sure that the chosen organization uses the money for the broad benefit of class members.¹⁶⁷

B. *The Superiority of Reverse Sampling*

Reverse sampling is superior to all these existing mechanisms to distribute the proceeds of small-claims class actions.¹⁶⁸ It achieves de-

¹⁶³ See Yospe, *supra* note 103, at 1035–36 (giving several examples of such lobbying behavior).

¹⁶⁴ Cf. Jack Hirshleifer, *The Private and Social Value of Information and the Reward to Inventive Activity*, 61 AM. ECON. REV. 561, 561, 573 (1971).

¹⁶⁵ The cy pres process in *Superior Beverage Co. v. Owens-Illinois, Inc.*, 827 F. Supp. 477, 478 (N.D. Ill. 1993), followed this prescription. First, notice was published (including in *The Wall Street Journal*). See *id.* Then, upon receiving applications, the court held hearings for an entire day. See *id.*

¹⁶⁶ See, e.g., *In re Folding Carton Antitrust Litig.*, 744 F.2d 1252, 1253 (7th Cir. 1984) (appointing an “Administrative Committee” composed of counsels for the parties as well as an independent member). For a more detailed discussion, see Yospe, *supra* note 103, at 1055.

¹⁶⁷ In one cy pres case, for example, the court divided the money between several charitable organizations, holding that “[a]fter the initial distribution, additional distributions will be contingent upon achievement. Each entity will provide the Court in an annual report, with information detailing what the project has accomplished and the Court will retain jurisdiction over this aspect of the lawsuit.” *Fears*, 02-Civ.4911(HB), 2005 WL 1041134, at *11. Ongoing supervision is particularly costly when courts use the cy pres approach to establish a new trust. See *Dick*, *supra* note 17, at 82–83; *supra* note 145.

¹⁶⁸ Another possible distribution mechanism is awarding the entire fund to the plaintiffs' lawyer. See Brian T. Fitzpatrick, *Do Class Action Lawyers Make Too Little?*, 158 U. PA. L. REV. 2043, 2055, 2082–83 (2010) (arguing that incentivizing class action lawyers to bring suits by awarding them the entire class recovery would maximize deterrence). While this method certainly has several advantages, it is not perfect. In particular, this method makes the choice of the representative lawyer difficult. It is hard to conceive of a bidding process to select the class counsel in which the winning lawyer pays nothing for the right to pursue the action. In any

terrence, as the defendant has to fully bear the results of his wrongdoing; other proposals—reverting the money to the defendant and forcing price reduction—leave the defendant with some gain. Reverse sampling also performs better than the pro rata distribution option. It achieves greater administrative efficiency by cutting the number of victims to whom money is transferred as well as the efforts to locate these victims.

Furthermore, reverse sampling equally compensates the victims, as each member of the class is entitled to an expected sum that is similar to his or her loss. Other mechanisms, notably cy pres and escheat to the state, fail to do so. One might argue that compensation is not an important goal in low-value claims. This argument might very well be true, but even if compensation is not an important goal in itself, compensating the victims has important instrumental advantages: it allocates the money impartially and avoids perverse incentives. When a third party—be it the government or a charity—sees a large windfall, it is likely to change its behavior accordingly.¹⁶⁹ These distortions do not occur when the money is distributed to where it belongs: the group of victims. The following table sketches the superiority of reverse sampling vis-à-vis existing mechanisms:

Table 2. The Superiority of Reverse Sampling

| | Deterrence | Administrative Efficiency | Judicial Decision Making | Third-Party Beneficiary | Compensating the Victims |
|-------------------------------|---------------------------|----------------------------------|---------------------------------|--------------------------------|-------------------------------------|
| Reversion to Defendant | Incomplete ¹⁷⁰ | Very High | Mechanical | No | No |
| Pro Rata Distribution | Yes | Moderate-High ¹⁷¹ | Some discretion ¹⁷² | No | Yes (expected award) ¹⁷³ |
| Escheat to the State | Yes | Very High | Mechanical | Yes | No |

event, because this mechanism is not currently employed, and because it substantially deviates from existing practices, this Article does not discuss it.

¹⁶⁹ See *supra* notes 131–33 and accompanying text (discussing government); see also *supra* notes 163–64 and accompanying text (discussing charities).

¹⁷⁰ See *supra* note 104 and accompanying text.

¹⁷¹ See text accompanying *supra* notes 112–14.

¹⁷² There is some discretion in the pro rata distribution regime as to the number and depth of distribution phases. Cf. *supra* text accompanying note 114.

¹⁷³ See *supra* notes 109–10 and accompanying text.

| | Deterrence | Administrative Efficiency | Judicial Decision Making | Third-Party Beneficiary | Compensating the Victims |
|-------------------------|------------------------|----------------------------------|-----------------------------------|--------------------------------|-------------------------------------|
| Price Reduction | Depends ¹⁷⁴ | High ¹⁷⁵ | Requires expertise ¹⁷⁶ | No | Partially ¹⁷⁷ |
| Cy Pres | Yes | High ¹⁷⁸ | Unfettered ¹⁷⁹ | Yes | No ¹⁸⁰ |
| Reverse Sampling | Yes ¹⁸¹ | High ¹⁸² | Mechanical ¹⁸³ | No | Yes (expected award) ¹⁸⁴ |

Compared to the increasingly popular cy pres method, the superiority of reverse sampling is particularly salient. Where the cy pres doctrine fails to remunerate class members and creates unfettered judicial discretion, the reverse sampling method mandates courts to transfer the proceeds to the victims. Where the cy pres doctrine wastes judicial time and encourages charities to compete for windfalls, reverse sampling avoids beneficiaries' perverse incentives.

* * *

As this Article has shown, reverse sampling is superior to existing distribution methods, as it doles out the money to the victims and maintains administrative efficiency. The backdrop for the comparison between reverse sampling and existing alternatives is the notion that the first-best solution should be compensating the victims. As previously discussed, there might be independent reasons for not paying damages to plaintiffs, and the compensation principle can hence be inefficient in some instances.¹⁸⁵ These considerations might push toward more radical solutions that do not even attempt to award the members of the class.

¹⁷⁴ See *supra* note 140 and accompanying text.

¹⁷⁵ This method requires some judicial effort to calculate and administer the price reduction. See *supra* note 141 and accompanying text.

¹⁷⁶ See *supra* note 141 and accompanying text.

¹⁷⁷ This depends on prospective customers: to the extent they are likely to be the same previously injured plaintiffs, the price reduction scheme is more compensatory.

¹⁷⁸ There is some judicial effort required to determine the cy pres beneficiaries and monitor them thereafter. See *supra* notes 165–67 and accompanying text.

¹⁷⁹ See *supra* text accompanying notes 154–58.

¹⁸⁰ See *supra* text accompanying notes 146–53.

¹⁸¹ See *supra* Part III.B.

¹⁸² There are some administrative costs associated with holding a lottery and distributing the money to the chosen plaintiffs.

¹⁸³ See *supra* Part III.B.

¹⁸⁴ See *supra* Part III.B.

¹⁸⁵ See *supra* notes 44–45 and accompanying text.

If plaintiffs are not compensated, the money ought to be allocated elsewhere. It is not obvious that the distortions made by awarding the proceeds to the victims are greater than the inefficiencies from funneling the money to a third party. In fact, at least in small-claims class actions, a presumption in favor of compensating the victims seems more appropriate. This presumption rests on instrumental reasons. First, in typical small-claims class actions it is plausible to believe that victims cannot reasonably affect harm—damages are the defendant’s fault, not the victims’. Hence, class members’ *ex ante* incentives are irrelevant. By contrast, granting the money to the government distorts its incentives to optimally enforce the law. In addition, compensating the victims restrains the court’s unfettered freedom to dole out the money to third parties.¹⁸⁶ In short, at least in the context of low-value claims, the members of the injured class are the truly disinterested parties. Awarding them the money is the most neutral and impartial distribution which is the least likely to distort behavior. Therefore, compensating low-value plaintiffs in these contexts seems instrumentally superior to other, more radical alternatives.

CONCLUSION

The normative prescriptions of this Article are clear and simple: when individual payments are sufficiently low with respect to the efforts needed to award them, courts should distribute the proceeds to a randomly selected small fraction of the class—what this Article refers to as “reverse sampling.” This lottery allocation, this Article argues, is what class members would prefer, as they can expect to receive higher awards on average. The proposal is practical and does not require any legislative change. Rather, it uses the equitable powers courts already employ when they distribute the proceeds of small-claims class actions. Furthermore, the use of lotteries in similar contexts is not unknown to the judicial system.

The thrust of the reverse sampling argument is that it reduces the high per-claim costs required to distribute the money back to all victims. It might be that with sufficiently good technology, per-claim administrative costs will be virtually zero. In that case, the proposed lottery distribution loses its appeal. Alas, oftentimes per-claim administrative costs are prohibitively high. In these situations, as this Arti-

¹⁸⁶ This also prevents a wasteful race to the court. *See supra* note 164 and accompanying text.

cle demonstrates, reverse sampling performs better than any existing solution to the problem of small-claims class actions: it directs the money to the group of plaintiffs and cuts administrative costs.