What Tax Law Has to Say About *Ortiz* v. *Fibreboard Corp.* and the Valuation of Contested Legal Rights: Loosening the Independent Valuation Requirement

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I– *ORTIZ* V. *FIBREBOARD* AND THE INDEPENDENT VALUATION REQUIREMENT FOR 23(B)(2) CLASSES

Ortiz v. *Fibreboard* is famous for overturning the certification of a Rule 23(b)(1)(B) limited fund class action settlement involving thousands of class members who were exposed to asbestos. In *Ortiz*, the claimants were supposed to be paid from a proposed limited fund, which consisted of a combination of Fibreboard's assets and Fibreboard insurance policies, with the company contributing $500,000 of its own funds. While the district court heard evidence and made findings with respect to Fibreboard's sale value, it assumed, without extensive factual showings, that the parties' proffered settlement accurately valued the insurance policies.[1]

For Justice Souter, one of the "essential premises of mandatory limited fund actions" is a demonstration that the fund is in fact limited.[2] The district court, however, did not make this required finding. It failed independently to verify the upper limit of the fund; it did not require evidence from the parties that would allow them to ascertain the limits of the fund; and it did not allow third parties to challenge the proposed limit of the fund.[3] Instead of requiring presentation of evidence and challenges from third parties, the lower courts blithely accepted the settlement of the parties as the actual amount of the fund. The primary problem, according to Justice Souter, was the lack of evidentiary presentation concerning the existence of a limited

1. *Ortiz* v. *Fibreboard Corp.*, 527 U.S. 815, 828, 851 (1999).
2. *Ibid.,* at 848.
3. *Ibid.,* at 849-850 ("Thus, in an action such as this the settling parties must present not only their agreement, but evidence on which the district court may ascertain the limit and the insufficiency of the fund, with support in findings of fact following a proceeding in which the evidence is subject to challenge.").

fund.[4] In sum, the lower courts failed because they uncritically adopted the parties' valuation of the limited fund.[5]

The independent valuation requirement in *Ortiz* has spurred courts in subsequent cases to see this requirement as an independent ground for denying certification. For example, in *In re Simon II*, the Second Circuit unwound a class certified under Rule 23(b)(1)(B) by Judge Jack Weinstein.[6] The limited fund class in *Simon II* was based on the idea of a constitutional cap on damages.[7] Because "substantive due process … limits punitive damages", Judge Weinstein certified the class based on a belief that the constitutional limit on punishment could provide the limited fund required for 23(b)(1)(B) classes.[8] Directly following *Ortiz*, however, the Second Circuit decertified the class based on traditional notions of the limited fund.[9] A lack of

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4. See, e.g., Elizabeth J. CABRASER and Thomas M. SOBOL, "Equity for the Victims, Equity for the Transgressor: The Classwide Treatment of Punitive Damages Claims", (2000) *Tul L. Rev.* 2005, 2021 ("As *Ortiz* demonstrates, the failure of cases to establish limited fund certification stems more from lack of evidentiary presentation than from unrealistic legal barriers. Often, the problem is not that the litigants have failed in their proof of the existence of a limited fund, but that the requisite proof was not undertaken.").
5. *Ortiz*, 527 U.S. at 848 ("The defect of certification going to the most characteristic feature of a limited fund action was the uncritical adoption by both the District Court and the Court of Appeals of figures agreed upon by the parties in defining the limits of the fund and demonstrating its inadequacy.").
6. *Simon II Litig.* v. *Philip Morris USA Inc. (In re Simon Litig.)*, 407 F.3d 125, 128 (2d Cir. 2005).
7. *In re Simon II*, 211 F.R.D. 86, 107-11 (E.D.N.Y. 2002); see also *In re Exxon Valdez*, No. A89-0095-CV (HRH), slip op. at 8 (D. Alaska Mar. 8, 1994) (certifying a limited fund class action on a limited punishment theory).
8. *In re Simon II*, 211 F.R.D. at 185 ("There must … be some limit, either as a matter of policy or as a matter of due process, to the amount of times defendants may be punished for a single transaction."); see also Elizabeth J. CABRASER and Thomas M. SOBOL, *supra*, note 4 ("At least in the mass tort context, therefore, where the number of claimants is large, the pool of available punitive damages dollars is a classic limited fund warranting 'limited punishment' through Rule 23(b)(1)(B) certification for a single punitive damages trial or a comprehensive settlement of punitive damages liability."); *In re School Asbestos Litigation*, 789 F.2d 996, 1005-06 (3d Cir. 1986) ("More precisely, "limited generosity" (or "punitive damages overkill," as some class members call it) is the functional equivalent of the limited fund in that, by operation of the limited generosity principle, only a limited amount of punitive damage funds will be available, regardless of the ability of the defendants to pay.").
9. *In re Simon Litig.*, 407 F.3d at 127-28 ("We hold that the order certifying this punitive damages class must be vacated because there is no evidence by which the district court could ascertain the limits of either the fund or the aggregate value of punitive claims against it, such that the postulated fund could be deemed inadequate to pay all legitimate claims, and thus plaintiffs have failed to satisfy one of the presumptively necessary conditions for limited fund treatment").

"evidence indicating [both] the upper limit [and] the insufficiency of the posited fund" led the Second Circuit to invalidate the limited fund class.[10] According to the Second Circuit, the class certification failed the independent valuation requirement.[11] The "constitutional cap" hypothesized by Judge Weinstein was "theoretical" and "not easily susceptible to … even estimation."[12] The primary issue with certification was that the "postulated" limited fund was "fundamentally unlike the classic limited funds of the historical antecedents of Rule 23."[13] Or as one scholar put it, "the most significant stumbling block to Judge Weinstein's innovative approach" sprang directly from the formalistic notions of 23(b)(1)(B) classes *Ortiz* promoted.[14]

Similarly, in *In re Telectronics Pacing Systems*, the Sixth Circuit unwound a class settlement agreement because the district court failed to verify that the defendant company, as well as its parent companies, had insufficient funds to pay all the outstanding claims.[15] Other courts have reached similar conclusions, overturning certified class action settlements under Rule 23(b)(1)(B) because the limits of the fund were not settled by the lower court.[16] As these cases

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Notably, the Second Circuit had reached the opposite conclusion in cases prior to *Ortiz*. See, e.g., *In re Diamond Shamrock Chems. Co.*, 725 F.2d 858, 861-62 (2d Cir. 1984) (footnote omitted) ("Chief Judge Weinstein … certified a class under Rule 23(b)(1)(B) for the award of punitive damages. Given the large number of potential claimants, estimated by the Special Master to be over 40,000 and given the fact that punitive damages ought in theory to be distributed among the individual plaintiffs on a basis other than date of trial, the argument against his ruling does not justify issuance of a writ of mandamus.").

10. *In re Simon Litig.*, 407 F.3d at 138.
11. *Ibid.,* at 137 (quoting *Ortiz* v. *Fibreboard Corp.*, 527 U.S. 815, 841 (1999)).
12. *Ibid.,* at 138 ("The proposed fund in this case … is a theoretical one, unlike any of those in the cases cited in *Ortiz*. … The fund here is—in essence—postulated, and for that reason it is not easily susceptible to proof, definition, or even estimation, by any precise figure.").
13. *Ibid.,* at 138.
14. Catherine M. SHARKEY, "The BP Oil Spill Settlements, Classwide Punitive Damages, and Societal Deterrence", (2015) 64 *DePaul L. Rev.* 681, 687-88.
15. *In re Telectronics Pacing Sys., Inc.*, 221 F.3d 870, 880 (6th Cir. 2000) ("As in *Ortiz,* the district court in the instant case did not undertake an independent risk analysis, but instead accepted the $10 million settlement figure as representing the maximum amount the Australian defendants could be required to pay claimants, which is plainly improper.").
16. *See e.g.*, *Zinser* v. *Accufix Research Institute, Inc.*, 253 F.3d 1180 (9th Cir. 2001) (holding that class certification was not warranted because the defendant's parent corporation, affiliated corporations, and insurance might have available funds); *Macedonia Church* v. *Lancaster Hotel Ltd. Partnership*, 270 F.R.D. 107 (D. Conn. 2010) (declining to certify a class because the defendants had not shown that they were insolvent or declaring bankruptcy); *Doe* v. *Karadzic*, 192 F.R.D. 133, 135

demonstrate, the independent valuation reasoning in *Ortiz* serves as an independent bar to class certification, unwinding otherwise valid class action settlements.

However, reasons stated in dicta of the *Ortiz* opinion suggest that the Court's independent valuation requirement should not be viewed as an independent reason to decertify a class settlement. First, the *Ortiz* class was riddled with problems, and the variety of flaws in the class's structure gave the Court a multitude of grounds on which to deny certification. As other commentators have noted, the decertification of the class in *Ortiz* was somewhat over-determined.[17] The proposed class excluded a vast amount of potential claimants[18] and lacked the required structural protections developed in *Amchem*

(S.D.N.Y. 2000) (declining to certify a class action because it was not adequately shown that the defendant's funds were insufficient to pay all claims); *but see Baker* v. *Washington Mut. Fin. Grp., LLC*, 193 F. App'x 294, 298 (5th Cir. 2006) (upholding the certification of a 23(b)(1)(B) class based on a limited punishment rationale). For cases coming before *Ortiz*, see *In re Dennis Greenman Secs. Litigation*, 829 F.2d 1539 (11th Cir. 1987) (holding that certification of a class on the basis that some plaintiffs might bankrupt potential sources of recovery if allowed to proceed individually was improper, absent specific findings of defendants' financial status); *In re Northern Dist. of California Dalkon Shield IUD Prods. Liability Litigation*, 693 F.2d 847 (9th Cir. 1982), *cert. denied* 459 U.S. 1171 (same); *In re Telectronics Pacing Sys., Inc*., 172 F.R.D. 271, 286 (S.D. Ohio 1997) (failure to present evidence on cost of medical monitoring prevented court from finding defendant threatened by insolvency if no class action); *Listle* v. *Milwaukee Cty.*, 170 F.R.D. 17, 19 (E.D. Wis. 1996) (refusing to certify a class on behalf of 200 persons who had received implants of artificial ligaments when records did not clearly establish that the physician and insurers would be unable to pay damages and there were other prospective defendants); *Hum* v. *Dericks*, 162 F.R.D. 628 (D. Haw. 1995); *Fogie* v. *Rent-A-Center, Inc*., 867 F. Supp. 1398 (D. Minn. 1993); *Langley* v. *Coughlin*, 715 F. Supp. 522, 564 (S.D.N.Y. 1989); *In re Bendectin Products Liability Litigation,* 749 F.2d 300, 306 (6th Cir. 1984) ("[T]he district court, as a matter of law, must have a fact-finding inquiry on this question and allow the opponents of class certification to present evidence that a limited fund does not exist"); *see also In re Temple,* 851 F.2d 1269, 1272 (11th Cir. 1988) ("Without a finding as to the net worth of the defendant, it is difficult to see how the fact of a limited fund could have been established given that all of [the defendant's] assets are potentially available to suitors"); *In re Dennis Greenman Securities Litigation,* 829 F.2d 1539, 1546 (11th Cir. 1987) (discussing factual findings necessary for certification of a limited fund class action).

17. See, e.g., Samuel L. ISSACHAROFF, "Governance and Legitimacy in the Law of Class Actions", (1999) *Sup. Ct. Rev.* 337, 350 (describing the *Ortiz* class as "hopelessly riven by internal divisions between present and future claimants" and concluding that "[t]his alone should have sufficed for the Court's holding").
18. *Ortiz*, 527 U.S. at 854 ("[T]here can be no question that such a mandatory settlement class will not qualify when in the very negotiations aimed at a class settlement, class counsel agree to exclude what could turn out to be as much as a third of the claimants").

Prods., Inc. v. *Windsor*.[19] Based on these flaws, decertification was correct regardless of whether the fund was truly limited.

Second, the Court seemed to acknowledge that the independent valuation requirement might not be an independent bar to class certification if these problems were cured. Justice Souter recognized that "settlement amount" can serve as "good evidence of the maximum available if one can assume that parties of equal knowledge and negotiating skill agreed upon the figure through arms-length bargaining."[20] He did not go so far as to say, however, that settlement amount is sufficient evidence to unwind class certification. He also noted that potential savings in transaction costs from settlement could allow a court to certify the class without forcing the defendant into insolvency or bankruptcy.[21] In other words, Justice Souter recognized that settlements come with savings that might be passed on to the class, and these savings might outweigh the additional funds gained from pushing the defendant to give up all available funds. These benefits could not be realized in *Ortiz*, however, because of the multitude of flaws in the class making it unlikely that the settlement was "the best that [could] be provided for class members."[22]

Beyond reasoning internal to the opinion, a larger question unaddressed by the Court is whether the parties in *Ortiz* should have been allowed to value the settlement on their own, assuming the other structural flaws in the class were cured. Differently put, assuming that all of the Rule 23(a) factors were met, would the district court have been justified in relying on the parties' settlement agreement as a demonstration of the fund's upper limit? Should courts accept the value that arm's length bargainers give to a limited fund? In order to demonstrate the potential functional shortcomings of the Court's independent valuation requirement, particularly as an independent bar to certification, I will look to another legal context, in which courts regularly address problems with valuation in situations of contested legal liability: tax law.

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19. *Ibid.,* at 856-57 ("[T]he conflict [between present and future claimants] was as contrary to the equitable obligation entailed by the limited fund rationale as it was to the requirements of structural protection applicable to all class actions under Rule 23(a)(4)." (citing *Amchem Prods., Inc.* v. *Windsor*, 521 U.S. 591 (1997)).
20. *Ibid.,* at 852.
21. *Ibid.,* at 861 ("If a settlement thus saves transaction costs that would never have gone into a class member's pocket in the absence of settlement, may credit for some of the savings be recognized in a mandatory class action as an incentive to settle? It is at least a legitimate question. …").
22. *Ibid.,* at 860

II– TAX LAW AND THE VALUATION OF CONTESTED LEGAL RIGHTS

Courts assessing tax law issues have developed precedent that suggests arm's length party valuations should be respected by courts.[23] In numerous areas within the tax law, courts refuse to independently verify settlements between parties for tax purposes.[24] Two areas in particular are relevant to analysis of the *Ortiz* independent valuation requirement. The first is contested discharge of indebtedness, and the second involves transfers related to marriage.

Under case law developed in tax cases, loans are not taxed, even though the recipient of the loan experiences an immediate accession to wealth. The reason loans are not taxed is that the accession to wealth carries a corresponding obligation to repay.[25] When this obligation goes unfulfilled, however, and the debtor does not repay the full amount of the loan, the debtor must pay taxes on the windfall, and the creditor may write off the bad debt, because the recipient of the loan experienced a lasting increase in wealth as a result of the transaction.[26] Contested discharge of indebtedness falls into a grey area between these two precepts of tax law. While it is clear that the debtor has received assets without fully repaying them, sometimes the amount of the debt is not fixed with accuracy, or liability for the debt might be unclear. Importantly, in response to the inability clearly to show the amount of the shortfall and legal liability, tax courts have placed increased reliance on settlement agreements reached by the parties.

For example, in *Zarin* v. *Commissioner*, the court addressed a casino patron's unpaid line of credit. The casino patron, Zarin,

23. See, e.g., *Zarin* v. *C.I.R.*, 916 F.2d 110, 111 (3d Cir. 1990); *United States* v. *Davis*, 370 U.S. 65 (1962).
24. *Ibid.*
25. See, e.g., *United States* v. *Kirby Lumber Co.*, 284 U.S. 1, 3 (1931) (holding that a taxpayer realizes income and should be taxed on it when she is able to discharge a debt for less than its face value).
26. See Boris I. BITTKER and Barton H. THOMPSON, "Income from the Discharge of Indebtedness: The Progeny of *United States* v. *Kirby Lumber Co.*", (1978) 66 *Calif. L. Rev.* 1159, 1166 ("Income results from the discharge of indebtedness because the taxpayer received (and excluded from income) funds that he is no longer required to pay back, not because assets are freed of off-setting liabilities on the balance sheet. Debtors who ultimately pay back less than they received enjoy a financial benefit. …").

had run up a large debt of $3,435,000, which he refused to repay.[27] Instead of demanding full repayment, the casino settled with him for $500,000.[28] Under normal tax principles, courts would find that Zarin profited from the transaction with the casino. He effectively took out a loan from the casino, which he did not fully repay. As a result, the amount by which he gained should be treated as income. He experienced an accession to wealth and should be required to pay taxes on his gains.[29] But the court in *Zarin* took a different position. According to the court, Zarin's transaction with the casino did not involve mere discharge of indebtedness. Instead, the case involved discharge of *contested* debt liability.

Confounding the court's evaluation of Zarin's debt was a law making it illegal for casinos to extend lines of credit.[30] This law made it unclear that the casino chips were actually worth their face value. Casino chips were not legally enforceable, which made it unclear (a) whether Zarin was liable for the debt at all and (b) how to determine the value of legally contested items. Because the value of the chips was unclear, as was Zarin's legal liability for those chips, the case presented difficult questions of valuation.[31] Rather than ascertaining the amount of the debt liability, and assessing taxes based on that amount, the court deferred to the parties' settlement as the amount of debt cognizable for tax purposes.[32] In other words, the

27. *Zarin* v. *C.I.R.*, 916 F.2d 110, 111 (3d Cir. 1990).
28. *Ibid.,* at 111-12.
29. Before being reversed, the Tax Court below applied traditional tax concepts and found that Zarin profited and should pay taxes on the unrepaid amount of the debt. See *Zarin* v. *C.I.R.*, 92 T.C. 1084, 1087 (1989), *rev'd*, 916 F.2d 110 (3d Cir. 1990).
30. *Zarin*, 916 F.2d at 112.
31. See, e.g., Daniel SHAVIRO, "The Man Who Lost Too Much: *Zarin* v. *Commissioner* and the Measurement of Taxable Consumption", (1990) 45 *Tax L. Rev.* 215, 256 ("[Zarin and the casino] settled at a discount, because Zarin had a legal challenge going to the validity of the entire debt. The Third Circuit reasoned, however, that a dispute about the validity of a debt necessarily implies dispute about its amount.").
32. *Zarin*, 916 F.2d at 116 ("To summarize, the transaction between Zarin and [the casino] can best be characterized as a disputed debt, or contested liability. Zarin owed an unenforceable debt of $3,435,000 to [the casino]. After Zarin in good faith disputed his obligation to repay the debt, the parties settled for $500,000, which Zarin paid. That $500,000 settlement fixed the amount of loss and the amount of debt cognizable for tax purposes."); *id.* at 115 ("Under the contested liability doctrine, if a taxpayer, in good faith, disputed the amount of a debt, a subsequent settlement of the dispute would be treated as the amount of debt cognizable for tax purposes.").

court did not independently value the debt at issue. Other courts have reached similar conclusions.[33]

When dealing with transfers related to marriage, as well, courts refuse independently to evaluate the bargains made between future and former spouses. In *United States* v. *Davis*, the court addressed a divorce settlement agreement in which the husband settled with the wife, exchanging 1000 shares of stock for her signing away her right to sue for half of his wealth.[34] Similarly, in *Farid-Es-Sultaneh* v. *Commissioner*, the court addressed a prenuptial agreement in which the future husband transferred stock to the future wife in exchange for her marital rights.[35] In both of these cases, the husbands transferred stock—commodities that are easy to value—for inchoate legal rights—commodities that are virtually impossible to value. Also in both cases, the court accepted the valuation of the legal rights set forth by the parties.

The courts in these cases confronted two difficult, related questions. First, how much did the wife effectively pay for the stock (i.e., what were her inchoate marital rights worth)? And second, did the husband profit from the sale of stock?[36] Normally, the most accurate way to determine how much she paid for the shares would be to value her inchoate legal rights. Technically, the price she paid for the shares should be equal to what she gave up for them. But the court did not attempt this independent valuation. Instead, both courts took the fair market value of the stock as the value of the wives' legal rights. Differently put, the courts assumed that the wives had contracted at arm's length, accurately valued their rights, and exchanged them for stock of equal value. In essence, the courts accepted the parties' own valuation of their legal claims.[37] As a result of this determination,

33. See, e.g., *United States* v. *Hall,* 307 F.2d 238 (10th Cir. 1962) (applying the contested liability doctrine to a situation involving a taxpayer who incurred gambling losses at a Las Vegas club in an estimated range of $145,000 to $478,000 when one of the club owners agreed to forgive the debt in return for a one-half interest in the taxpayer's cattle); *N. Sobel, Inc.* v. *Comm'r*, 40 B.T.A. 1263 (1939) ("There is question whether the taxpayer bought property in 1929 and question as to its liability *and the amount thereof.*").
34. *United States* v. *Davis*, 370 U.S. 65 (1962).
35. *Farid-Es-Sultaneh* v. *C.I.R.*, 160 F.2d 812, 815 (2d Cir. 1947).
36. The first question is important from a tax law perspective because taxes would later be assessed from the wife when she sold her stock, and the assessment of those taxes would be based on the price at which she bought the shares.
37. See *Davis*, 370 U.S. at 72 ("It must be assumed, we think, that the parties acted at arm's length and that they judged the marital rights to be equal in value to the property for which they were exchanged."); *Farid-Es-Sultaneh*, 160 F.2d at 815

the husband's profit was also set. His profit was equal to the difference between the original purchase price of the shares and the fair market value of the shares when sold to the wife.

The law surrounding contested discharge of indebtedness and transfers related to marriage contains two important insights that bear on the independent valuation requirement developed in *Ortiz*. First, tax courts are wary of appraising the value of unliquidated legal claims. In *Davis* and *Farid-Es-Sultaneh*, the courts avoided assigning value the inchoate marital rights at issue. Similarly, in *Zarin*, the Court considered the face value of the casino chips not to be a necessarily accurate estimation of their worth.[38] Other courts have applied similar reasoning. For example, one court distinguished between contested liability in cases where the face value of debt is definitively ascertainable—a determination that courts are capable of making—and cases in which the debt is not liquidated (i.e., the amount is not definitively ascertainable).[39] The latter types of cases are the ones that present problems for judges, who are incapable of accurately valuing an unliquidated debt. As one court put it, courts in contested discharge of debt cases are "unaware of the exact consideration initially exchanged in a transaction."[40]

This first point leads to the second important point: If the court cannot determine the amount of the unliquidated debt, then the court rightly defers to the valuations of parties negotiating at arms' length. In both areas of law discussed above, courts gave weight to the fact that parties were arm's length bargainers. In *Zarin*, the court presumed that the casino drove as hard a bargain as it could, and that it had squeezed as much money as possible out of Zarin.[41]

("Her inchoate interest in the property of her affianced husband greatly exceeded the value of the stock transferred to her. … She performed the contract under the terms of which the stock was transferred to her and held the shares not as a donee but as a purchaser for a fair consideration.").

38. See Joseph M. DODGE, "*Zarin* v. *Commissioner*: Musings About Debt Cancellations and 'Consumption' in an Income Tax Base", (1990) 45 *Tax L. Rev.* 677, 679 ("[O]ne cannot simply assume that Zarin received $3.4 million in money or money's worth from the gambling transactions because $3.4 million was the face amount of the liability.").
39. *Preslar* v. *C.I.R.*, 167 F.3d 1323, 1328-29 (10th Cir. 1999) ("The court maintained that only where a good faith dispute arises over the amount of a debt (i.e., the debt is unliquidated) will the contested liability doctrine be applicable.").
40. *Ibid.,* at 1328.
41. James L. MUSSELMAN, "Is Income from Discharge of Indebtedness Really Income at All?", (2004) 34 *U. Mem. L. Rev.* 607, 655 ("[T]he law presumes that, in ordinary arm's length purchases of property, the value of the property received by

The court in *Davis* assumed that spouses going through a divorce were arm's length bargainers.[42] More aggressively, the Court presumed that spouses signing a prenuptial agreement were rational, arm's length bargainers. And because these courts considered the two parties to be bargaining in their own self-interest, the courts saw little they could add to the valuation of the contested legal rights. Parties with more information and greater interest in the outcome were better at valuing the rights at stake.

III– *ORTIZ* FROM A TAX LAW PERSPECTIVE

The points drawn from these tax cases bear directly on *Ortiz*'s independent valuation requirement. In tax courts, judges have accepted that their own valuation of contested legal rights is of limited usefulness. It would be a waste of resources and counterproductive for courts to challenge the determinations made by parties who have more information and better incentives. Contested valuations are better left to arm's length bargainers who have incentives to both acquire an optimal amount of information and aggressively pursue their self-interest.

These concerns apply with even greater force to class action settlements.[43] When assessing class settlements, not only must the court determine the amount of the defendant's potential liability, it must determine the total amount of funds that the defendant can put towards the settlement fund.[44] The two points of value are difficult to pin down in a definitive manner. In the tax cases, the value of one

the taxpayer is equal to the amount the taxpayer paid or agreed to pay for it."); Joseph M. DODGE, *supra*, note 38, 677, 680 (arguing that *Zarin* can be seen as an "arm's length bargain purchase" of consumption rights, which would not be treated as income for tax purposes).

42. See Comment, "Federal Tax Consequences of Antenuptial Contracts", (1977) 53 *Wash. L. Rev.* 105, 116-117 n. 57 ("The Supreme Court rejected this reasoning and held that because the parties had acted at arm's length, the values of the properties exchanged were presumed to be equal.").
43. At least one scholar has noted the potential applicability of contested discharge of debt concepts to tort liability. See James L. MUSSELMAN, *supra*, note 41, 607, 655 (2004) ("In contrast, what if a judgment is obtained against a taxpayer in a tort action based upon his negligent or intentional conduct, and the judgment is subsequently forgiven or extinguished in whole or in part? Does the taxpayer have income from discharge of indebtedness?").
44. See, e.g., 14. Charles Alan WRIGHT, Arthur R. MILLER and Edward H. COOPER, Federal Practice and Procedure § 1774 (3d ed. 1998) ("[T]he Court found that the lower court had uncritically adopted the 'figures agreed upon by the parties in defining the limits of the fund and demonstrating its inadequacy' so that there

side of the bargain is fixed and easily ascertainable. For example, the value of the stock exchanged for the wife's marital rights in *Davis* was equal to its fair market value. In *Ortiz*, however, the value of the insurance funds available was not clear. Neither was the value of Fibreboard as a going concern, especially considering the effects a settlement would have on its stock prices.[45] Of even less certain value was Fibreboard's unliquidated tort liability to the class members. Indeed, the value of each individual class member's legal claims was of uncertain value. Lumping all of those class members together, with their differing levels and types of injury, created valuation problems that a court could not plausibly overcome.

Assuming that structural flaws in class actions are not present, and class agents are faithful, the tax law principles discussed above should lead courts to question what their own valuation of contested legal rights and limited funds can add.[46] Remedying these informational asymmetries between the litigants and the district court also takes extraordinary effort and entails high administrative costs.[47]

Rather than attempting an independent valuation of available funds, courts should focus on other issues that more directly bear on the more fundamental problem: whether the parties are in fact adversarial bargainers. This dynamic between the parties is not captured by valuing claims and the limited fund; it is more appropriately captured by the 23(a) factors of typicality, commonality, and adequate representation. If parties are typical, with common claims, and adequately represented by the named plaintiff and lead counsel,

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was no adequate finding of fact to support the first characteristic." (internal citation omitted)).

45. See John C. COFFEE, Jr., "The Corruption of the Class Action: The New Technology of Collusion", (1995) 80 *Cornell L. Rev.* 851, 856 n. 9 (noting that "the stock price of Fibreboard has soared following the announcement of the class action settlement").

46. See, e.g., Janet C. ALEXANDER, "Do the Merits Matter? A Study of Settlements in Securities Class Actions", 43 *Stan. L. Rev.* 497, 499 n. 5 ("Judicial approval is required for the settlement of class actions. … However, the judge's ability to provide meaningful review of a settlement's adequacy is questionable."); Judith Resnik, *Judging Consent*, 1987 U. Chi. Legal F. 43, 101 ("[J]udges are ill-equipped to do much other than nod when the litigants join together and seek court approval").

47. See, e.g., Alvin K. HELLERSTEIN, James A. HENDERSON, Jr. and Aaron D. TWERSKI, "The 9/11 Litigation Database", (2013) 90 *Wash. U. L. Rev.* 653; Alvin K. HELLERSTEIN, James A. HENDERSON, Jr. and Aaron D. TWERSKI, "Managerial Judging: The 9/11 Responders' Tort Litigation", (2012) 98 *Cornell L. Rev.* 127.

then independent valuation of the limited fund by the Court is more likely to produce an inaccurate result than an accurate one. What's more, valuation is unlikely to directly target what we truly want to know when assessing a class settlement, whether the agent is a faithful representative of the class.

Moving forward, the independent valuation requirement developed in *Ortiz* should be modified to take account of the real goal of class settlement certification. Instead of independently valuing assets available for the plaintiff class to determine the upper limit of the fund, courts should view this valuation inquiry as relevant to determining whether the parties are bargaining at arm's length. Just as courts evaluate other factual evidence when assessing the relationship of parties at class certification, valuation can be another piece of evidence used to ensure that parties are in fact at arm's length in their bargaining. If claims seem radically undervalued, or if it is clear that companies are holding back a large amount of readily available assets without explanation, then reasons exist to doubt whether the class is being adequately represented.

Indeed, the Court in *Ortiz* seemed to use the value of the company in exactly this way.[48] But, importantly, these are not independent reasons to unwind class settlements—they are reasons to doubt that the Rule 23(a) requirements have been met at all. Differently stated, potential valuation problems are not a sufficient reason to refuse a class certification; instead, they are another piece of evidence relevant to assessing whether the class was proper to begin with.

This approach to the independent valuation requirement has particular ability to aid in the enforcement of settlements involving complex corporate arrangements between parents and subsidiaries. 23(b)(1)(B) settlement classes have been blocked in the past because the resources of subsidiaries and parents were possibly available to enlarge the fund.[49] Showing that these funds are available will

48. *Ortiz*, 527 U.S. at 860 ("With Fibreboard retaining nearly all its net worth, it hardly appears that such a regime is the best that can be provided for class members.")
49. See, e.g., *In re Telectronics Pacing Sys., Inc.*, 221 F.3d 870, 880 (6th Cir. 2000) ("As in *Ortiz,* the district court in the instant case did not undertake an independent risk analysis, but instead accepted the $10 million settlement figure as representing the maximum amount the Australian defendants could be required to pay claimants, which is plainly improper."); *Zinser* v. *Accufix Research Institute, Inc.*,

require complex rulings on state law governing piercing of the corporate veil—showings that are notoriously difficult to make and involve significant litigation costs. If properly driven class attorneys do not believe that those funds are readily available, or worth the effort to obtain, a court should not place itself in the role of advocate. The transaction costs that come with making these complex showings are better valued by the parties.

Loosening the independent valuation requirement could also ease the certification of classes formed solely for punitive damages. Punitive damages classes involve complex valuation problems, and the claims for punitive damages have no inherent worth. It is unclear that punitive classes can be accurately valued even when plaintiff claims have been liquidated—punitive damages only possess a constitutional limit somewhere around ten times each individual plaintiff's recovery.[50] Between this upper limit and a point below, punitive damages classes should not be blocked based on a desire precisely to pin down the exact amount of the class's claims and the upper limit of the fund. So long as the parties have negotiated in an adversarial manner, courts should avoid independent evaluation of the fund.

More broadly, the unique characteristics of 23(b)(1)(B) settlements could induce defendants to settle more readily in order to achieve greater finality. This enlarged finality would increase the payout available to potential claimants.[51] In addition, making certification of 23(b)(1)(B) classes more flexible could prevent the first-in-time problem, which results from earlier litigants effectively precluding the ability of later litigants to recover for their damages.[52] Adjudicating claims together could create a more equitable distribution, which could prevent some class members from recovering the bulk of the available funds while leaving others to pick up the scraps.

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253 F.3d 1180 (9th Cir. 2001) (holding that class certification was not warranted because the defendant's parent corporation, affiliated corporations, and insurance might have available funds).

50. See *State Farm Mut. Auto. Ins. Co.* v. *Campbell*, 538 U.S. 408 (2003).

51. *Cf.* Samuel L. ISSACHAROFF and D. Theodore RAVE, "The BP Oil Spill Settlement and the Paradox of Public Litigation", (2014) 74 *La. L. Rev.* 397 (documenting the increased payouts that stem from class action settlements due to the class being able to offer greater finality to the defendant).

52. See, e.g., Catherine M. SHARKEY, *supra*, note 24, 681, 687 (discussing the limited fund class action as a solution to the potential first-in-time problem where the first plaintiffs may recover vast sums while others who arrive later are left with a depleted fund against which they cannot recover." (citing *In re Simon II*, 211 F.R.D. at 190))

IV– CONCLUSION

Numerous courts and influential judges have seemingly backed off overly restrictive application of the Rule 23(a) requirements.[53] The independent valuation requirement is another overly formalistic requirement that has been read into Rule 23(b)(1)(B) in a manner that is too restrictive. As discussed above, this formalism is at odds with concepts developed and employed by courts assessing complex valuation problems in the tax law. This excessive formalism also conflicts with principles in other areas of the law. When appraising real estate for property tax purposes[54] and securities,[55] assessing the corporate business decisions,[56] and valuing assets in bankruptcy proceedings,[57] courts regularly defer to the agreements of adversarial

53. See, e.g., *McReynolds* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 672 F.3d 482, 483 (7th Cir. 2012) (Posner, J.); *Mejdrech* v. *Met-Coil Sys. Corp.*, 319 F.3d 910, 911 (7th Cir. 2003) (Posner, J.); *Sullivan* v. *DB Investments, Inc.*, 667 F.3d 273, 334 (3d Cir. 2011) (Scirica, J., concurring) ("Despite initial uncertainty [*Amchem* and *Ortiz*] might pose formidable obstacles for settling massive, complex cases, this has not, for the most part, proved to be the case.").

54. See Jerome R. HELLERSTEIN, "Judicial Review of Property Tax Assessments", (1959) 14 *Tax L. Rev.* 327, 349 (collecting cases and concluding that "[i]f the taxpayer is given a fair hearing to review the action of the assessor before a competent, impartial, and independent review board, where he is given adequate opportunity to present his evidence and make his arguments, then it is hard to see why the courts should do more than consider what are typically regarded as problems of law, errors of method, and impropriety in procedure.").

55. See, e.g., Saul LEVMORE, "Self-Assessed Valuation Systems for Tort and Other Law", (1982) 68 *Va. L. Rev.* 771, 837-858.

56. See, e.g., Marcel KAHAN and Edward B. ROCK, "When the Government is Controlling the Shareholder: Implications for Delaware", (2010) 35 *Del. J. Corp. L.* 409, 415 ("Likewise, a conclusion that a transaction is protected by the business judgment rule is analogous to a conclusion that the company should not bring a lawsuit: in both instances, the court does not review the substance of the underlying decision or transaction."); Hillary A. SALE, "Delaware's Good Faith", (2004) 89 *Cornell L. Rev*. 456, 465 ("Essentially, the premise is that good procedure leads to good substance."); Wells M. ENGELDOW, "Handicapping the Corporate Law Race", (2002) 28 *J. Corp. L*. 143, 156 ("Entire cases hinge on the presence or absence of certain facts and, perhaps more importantly, on the processes involved in arriving at the decision in question. In other words, the courts have decided to examine the processes leading to the decision with greater scrutiny than the decision that is reached itself (assuming there is no waste or patent conflict of interest)"); Jay W. EISENHOFFER and John L. REED, "Valuation Litigation", (1997) 22 *Del. Corp. L.J*. 37, 62 ("When scrutinizing these and other corporate transactions, the courts distinguish between disinterested or arm's-length transactions and interested transactions.").

57. Donald S. BERNSTEIN and Douglas S. BAIRD, "Absolute Priority, Value Uncertainty, and Reorganization Bargain", (1930) 115 *Yale L.J.* 47 ("The settlement negotiations that take place in the context of these uncertainties are

bargainers, recognizing the inaccuracy and transaction costs of judicial valuation.[58]

In contradistinction to these other areas of law, however, the Court has forced lower courts addressing 23(b)(1)(B) class actions into a position of policing the substance of these arrangements regardless of whether the parties are adversarial or not. But the wisdom of placing such complex valuation requirements on courts seems dubious at best, especially where parties possess greater information and incentives to bargain aggressively. While there are reasons to be concerned about the potential for collusion in class action settlements, these concerns are better policed through (a) rigorous application of the 23(a) factors and (b) using the independent valuation requirement as a manner to smoke out a lack of true bargaining.

like any other litigation settlement negotiations. They will cut short litigation only if a bargaining range exists.").

58. For example, in the Chapter 11 proceedings of Mirant Corporation, the valuation hearing lasted for twenty-seven days over an eleven-week period, with separate experts testifying for the debtors, various creditor constituencies, and equity holders. *In re Mirant Corp.*, 334 B.R. 800, 809 (Bankr. N.D. Tex. 2005). The judge in *Mirant* also recognized the shortcomings of the adversarial process for determining value, calling it at best "an exercise in educated guesswork" and at worst "not much more than crystal ball gazing." *Ibid.,* at 848.