

## THE RELATIONAL CONTINGENCY OF RIGHTS

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## INTRODUCTION

CONTRARY to conventional wisdom, in this Article we contend that all rights are relationally contingent. As we demonstrate, whether a right—indeed, any legal entitlement—is realizable will always critically depend on the relationship between two variables: (1) the cost a rightsholder would need to incur to vindicate the right; and (2) the cost faced by a challenger who wishes to attack and ultimately eliminate the right. In the real world, rights are meaningful only when the cost of protecting them is lower than the cost of attacking them. When the converse is true, the right becomes ineffective: it ceases to protect the rightsholder’s underlying interest. The cost of challenging a right is not uniform for all potential challengers, but rather varies dramatically across the population. The rightsholder’s cost of defending a right, on the other hand, remains constant. Consequently, rights will avail against certain challengers, but not against others. Or, succinctly put: rights are always relationally contingent. Furthermore, we show that the relational contingency of rights dominates all other factors that determine whether a rightsholder will realize her entitlement. When an entitlement is cheaper to attack than to vindicate, its holder will not be able to realize it.

To illustrate, consider the following examples. Assume that Brutus Inc., the owner of a large residential building, violates Anne’s right of quiet enjoyment. Anne places a value of \$3000 on that right. However, it will cost her \$5000 to hire a lawyer and take legal action against the owner. Brutus Inc., by contrast, has a retainer agreement with a law firm. The firm is well versed in landlord-and-tenant law and can handle suits expeditiously. Consequently, Brutus Inc.’s expected cost of defense is only \$1000. Under these circumstances, Anne will choose to refrain from commencing legal action against Brutus Inc.

Diane suffers from ongoing discrimination by her employer. Unfortunately for Diane, employment discrimination suits are notoriously expensive to prosecute. The cost of the average suit is \$40,000. Diane’s harm exceeds that amount. Diane estimates the harm at \$50,000, which means that her claim has a net value of

\$10,000. Her employer, on account of various economies of scale and scope, can litigate the case at \$30,000. Taking advantage of Diane's much higher litigation expenditures, the employer can offer her to settle her claim for \$20,000. If Diane is rational, she will agree; settling the case will guarantee her a net payoff of \$20,000, as opposed to the \$10,000 she will get from litigation.

Finally, consider the case of Ian, who has just received an ominous letter from Proprietary Images Inc., accusing him of a copyright infringement. Proprietary Images further informs Ian that the Copyright Act entitles successful plaintiffs to statutory damages of up to \$150,000<sup>1</sup> and then proceeds to offer him to settle the case out-of-court for the modest amount of \$3000. Ian is outraged by what he believes to be a baseless accusation, as he has a valid fair-use defense that he can prove in court. To do so, however, Ian would have to expend \$10,000 on legal representation. Hence, acting rationally, he will elect to accept Proprietary Images's settlement offer and forego litigation.<sup>2</sup>

We can now formulate the conditions that allow a challenger who enjoys a litigation-cost advantage over the rightsholder to force the rightsholder into a settlement agreement that will surrender her entitlement or part thereof. The challenger will succeed at forcing out this surrender when the entitlement, net of the enforcement cost, yields the rightsholder a positive amount that exceeds the challenger's cost of attacking the entitlement. To illustrate, when Rita values her legal entitlement at \$10,000 and it costs her \$6000 to protect the entitlement in court, Carl will be able to challenge the entitlement and force Rita to give it up so long as he keeps his litigation expenses below \$4000. Notably, Carl would not

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<sup>1</sup> See 17 U.S.C. § 504(c) (2006) (providing that a successful plaintiff in a copyright suit can elect to recover an award in any amount between \$750 and \$150,000 per infringed work in a case where the copyright owner sustains the burden of proof and the court finds willful infringement).

<sup>2</sup> This example also shows how a rightsholder's calculus changes when her entitlement is an affirmative defense against liability. Then, as in Ian's case, the defense's value equals the defender's expected liability. If Ian's defense fails, he might have to pay statutory damages in excess of Proprietary Images's actual harm. As a result, Ian will rationally choose to litigate even when his litigation cost is higher than the company's cost. As far as settlement is concerned, Ian will accept any offer that will require him to pay the company any sum below his litigation expenditure. By agreeing not to sue Ian if it pays it \$3000, Proprietary Images therefore does not make full use of its extortionary power.

be able to extort a similar settlement if Rita were to expend \$12,000 on vindicating her entitlement in court, which would make the net value of the entitlement  $-\$2000$  (a negative sum). However, Carl would be able to violate Rita's entitlement with impunity, a much worse outcome for those who believe that rights are an important legal and social institution.

An interesting and counter-intuitive result that emerges from our core claim is that sometimes negative value entitlements—that is, entitlements that cost more to defend than the value they yield to their holder—will nonetheless afford effective protection to their holders. Consider a person who values a certain right at \$5000. Assume that it would cost her \$7000 to vindicate the right in court. The right thus has a value of  $-\$2000$ , which may lead one to conclude that this right is meaningless in the real world since it is not cost-effective for the entitlement holder to defend it in court.<sup>3</sup> Surprisingly, this cost structure on its own does not make the entitlement worthless or meaningless. The entitlement may prove both valuable and effective if the cost of challenging it is, say, \$10,000 and the expected return to the challenger is only \$6000. The net return from challenging the entitlement ( $-\$4000$ ) would fend off the challenger. Importantly, this negative sum also does not allow the challenger to pose a credible threat of litigation to the rightsholder.<sup>4</sup> The reason is simple: although the entitlement is costly to

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<sup>3</sup> For definition of negative-value suits, see, e.g., Samuel Issacharoff, Preclusion, Due Process, and the Right To Opt Out of Class Actions, 77 *Notre Dame L. Rev.* 1057, 1059–60 (2002) (defining a negative-value suit as a “claim . . . too small to justify the cost of prosecution.”).

<sup>4</sup> This observation holds true in most cases, but there are exceptions. See Lucian Arye Bebchuk, A New Theory Concerning the Credibility and Success of Threats to Sue, 25 *J. Legal Stud.* 1, 5–9 (1996) (demonstrating that multistage litigation with divisible costs often allows a plaintiff with a negative-value suit to extract settlement from a defendant by expending—and thereby sinking—some of her costs and credibly threatening to go to trial that promises her a positive net return from the remaining expenditure); Lucian A. Bebchuk & Alon Klement, Negative-Expected-Value Suits, in 8 *Encyclopedia of Law and Economics: Procedural Law and Economics* 341, 341–44 (Chris William Sanchirico ed., 2d ed. 2012) (specifying circumstances in which divisibility of costs and informational advantage allow a plaintiff with a negative-value suit to extract settlement from defendant, and surveying relevant literature); Lucian Arye Bebchuk, Suing Solely To Extract a Settlement Offer, 17 *J. Legal Stud.* 437, 448 (1988) (showing that a plaintiff with a negative-value suit can sometimes exploit asymmetrical information to extract settlement from the less informed defendant); Joseph A. Grundfest & Peter H. Huang, The Unexpected Value of Litigation: A Real

defend, it is even costlier to attack, and the challenger therefore cannot rationally deliver on his threat to litigate. Under such circumstances, the entitlement will stay unchallenged and its holder will be able to realize it.

At this point, it is important to emphasize that our thesis about the relational contingency of rights addresses a completely different set of issues than Wesley Newcomb Hohfeld's famous scheme of "jural relations."<sup>5</sup> Both schemes allude to relationality, but each of them addresses a jurisprudentially distinct phenomenon. Hohfeld's scheme lays out the analytics of jural relations with a view to achieve conceptual clarity of diverse entitlements, generically identified as "rights."<sup>6</sup> Elaborating on the distinction between rights in personam—those that avail against a specific person—and rights in rem—those that avail against the rest of the world—Hohfeld suggested that rights in rem can be understood as aggregations of the underlying in personam rights. This characterization suggests that all rights—whether in personam or in rem—define people's jural relations as individual units.<sup>7</sup>

Our core insight is very different. Unlike Hohfeld, we are not interested in rights as abstract legal concepts. Rather, we are interested in the way they operate in practice. Furthermore, Hohfeld's analysis was formal in nature in that it was confined to the legal specification of rights. We, by contrast, are not interested in the formal recognition of rights by the lawmaker, but rather in the ways rights and entitlements operate in real-world settings. For us, the act of formal recognition is a mere starting point. In fact, we show that formal legal recognition often falls short of affording meaningful protection to entitlement holders.

Our thesis also markedly differs from Marc Galanter's classic examination of how wealth disparities affect court decisions and, in particular, the formation of legal precedent. Galanter famously

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Options Perspective, 58 *Stan. L. Rev.* 1267, 1299–1315 (2006) (using option theory to demonstrate that negative-value suits can be viable in a regime that allows parties to make piecemeal investments in the litigation, gradually reveal information to each other, and negotiate a settlement at any given point in time).

<sup>5</sup> See Wesley Newcomb Hohfeld, *Some Fundamental Legal Conceptions as Applied in Judicial Reasoning*, 23 *Yale L.J.* 16, 19 (1913).

<sup>6</sup> *Id.* at 29–44.

<sup>7</sup> See Wesley Newcomb Hohfeld, *Fundamental Legal Conceptions as Applied in Judicial Reasoning*, 26 *Yale L.J.* 710, 718–20 (1917).

showed that well-to-do litigants are able to achieve favorable outcomes in court and take the law in their desired direction due to the fact that they can afford superior legal representation.<sup>8</sup> The focal point of our inquiry is different. We focus on vindication and loss of entitlements that occur outside the courtroom.

This pivotal difference is best illustrated by cases in which the entitlement's vindication requires no assistance from courts. In any such case, the entitlement holder will realize her entitlement unilaterally: when the entitlement allows her to build a house, she will go ahead and build the house; when the entitlement permits her to rescind her contractual obligation, she will go ahead and rescind the obligation; and when the entitlement authorizes her to use another person's copyrighted work, she will go ahead and use the work. The entitlement's potential challenger will not be able to counter the holder's unilateral action by taking the case to court when the cost of doing so exceeds his expected return.

Oftentimes, an entitlement will be cheap to attack but costly to vindicate. This cost asymmetry will turn the entitlement into a dead letter of the law, viable in theory but unrealizable in practice. Asymmetric litigation costs that make entitlements unrealizable will be present whenever one of the litigants benefits from economies of scale or scope. For any such litigant, the marginal expenditure on every lawsuit drops as the number of cases increases. This condition obtains for many large corporations, for the government, and for other repeat litigants. These litigants retain legal representation for a fixed amount that reflects the declining cost. When any of them confronts an opponent with no parallel ability to economize on the litigation costs, it will usually be able to eradicate the opponent's entitlement. The three examples with which we opened our discussion show how this deleterious dynamic unfolds. In each of those examples, a wealthy firm utilizes economies of scale and scope to destroy the legal entitlement of its weaker opponent.

In this Article, we seek to make four novel contributions to the theory of entitlements. Our first and least ambitious goal is to bring together two important threads in entitlement literature: economic analysis of entitlements and deontological accounts of rights. These

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<sup>8</sup> See Marc Galanter, *Why the "Haves" Come Out Ahead: Speculations on the Limits of Legal Change*, 9 *Law & Soc'y Rev.* 95 (1974).

two threads coexist alongside one another without meaningful interaction. Several leading scholars of Law and Economics have devised stylized models that analyze asymmetric litigation costs and their effect on settlements.<sup>9</sup> These models demonstrated that a party with lower litigation costs can extort a favorable settlement from his opponent—a consequence that sometimes does and sometimes does not erode society's welfare.<sup>10</sup> This economic analysis has been highly abstract, insular and divorced from the broader jurisprudential context of legal rights. Critically, it paid no attention to the special role that rights play in our society as protectors of individuals' worth and wellbeing.

Deontological accounts of rights likewise suffer from isolationism. These accounts examine the nature, content, and justifications of rights from different philosophical perspectives.<sup>11</sup> Collectively, they develop a broad and illuminating vision of rights as an important social institution.<sup>12</sup> This vision underscores rights' role as constraining society's utilitarian pursuits, trumpeting rights as trumps.<sup>13</sup> Yet, deontological accounts pay virtually no attention to the economics of rights' enforcement<sup>14</sup> and overlook the destructive effect of asymmetric litigation costs on entitlements. This oversight undermines these accounts' practical viability.

The holistic approach we adopt in this Article enables us to draw on the powerful insights of each of these bodies of literature and develop a more complete understanding of rights and their ability to promote social goals and values.

Our second contribution is conceptual. We demonstrate that, contrary to the conventional wisdom among rights theorists, all rights and entitlements are contingent in nature. Rights provide ef-

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<sup>9</sup> See *infra* note 29.

<sup>10</sup> See *infra* notes 29–32 and accompanying text.

<sup>11</sup> See generally *Theories of Rights* (Jeremy Waldron ed., 1984).

<sup>12</sup> See *infra* Section I.B.

<sup>13</sup> See Ronald Dworkin, *Rights as Trumps*, in *Theories of Rights*, *supra* note 11, at 153, 153; see also Joseph Raz, *Rights and Individual Well-Being*, in *Ethics in the Public Domain: Essays in the Morality of Law and Politics* 29, 30 (1994) (arguing that rights afford individuals' interests special protection that is more stringent than a requirement that state officials account for those interests in making decisions).

<sup>14</sup> For one exception, see Stephen Holmes & Cass R. Sunstein, *The Cost of Rights: Why Liberty Depends on Taxes* (1999) (factoring costs of enforcing rights into philosophy of entitlements). For specifics and shortcomings of this account, see *infra* notes 54–58 and accompanying text.

fective protection to their holders only when they are cheaper to defend than to attack. When a right's challenge costs less than its vindication, the right's promised protection fades away up to the point of non-existence. Consequently, legal recognition of rights and other entitlements will result in no protection in some extreme cases and in full protection against all potential takers in other rare cases, while in the majority of cases its effect will be an effective protection against some takers and no protection against others. This critical insight is analytically robust and independent of the way in which legislatures and courts define and construe rights and entitlements.

Third, and relatedly, we show that in certain types of cases, the effects of asymmetric litigation costs are not randomly distributed across the population. Rather, they are systemic, favoring certain categories of litigants and disfavoring others. In such cases, asymmetric litigation costs often result in unrealizable entitlements: entitlements that are recognized *de jure*, but cannot be vindicated *de facto*. As a consequence, certain entitlement holders will find themselves helpless in the face of meritless, and oftentimes downright extortionary, claims. Or, if one prefers to look at it from the point of view of potential takers, it can be said that certain entitlements can be expropriated without their holders' consent and for an under-compensatory price. Worse yet, this phenomenon has regressive distributional effects because wealth and litigation expenditures are negatively correlated.<sup>15</sup> In addition to uncovering this systemic bias, we identify certain legal areas, both civil and criminal, in which it is prevalent.

Our fourth and final contribution is normative in nature. We propose several potential remedies that will protect entitlements against unmeritorious attacks by parties who enjoy a litigation cost

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<sup>15</sup> Marc Galanter identified this negative correlation in his classic article *Why the "Haves" Come Out Ahead*. See *supra* note 8, at 103–04. As we already mentioned, this article does not address the entitlement destruction that occurs out of court. Instead, it focuses on the rule-making process in which wealthy “repeat players” use their cost advantage to defeat the unwealthy “one shotters” and shape legal precedent the way they want. See also Patricia Munch, *An Economic Analysis of Eminent Domain*, 84 *J. Pol. Econ.* 473, 495 (1976) (demonstrating that owners of high-valued properties, who spend more on eminent domain proceedings, receive compensation that exceeds their properties' market value, while owners of low-valued properties are undercompensated).



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advantage. These remedies include fee shifting, punitive damages and special procedural safeguards. We explain each remedy's potential to level the litigation playfield and thereby afford better protection to entitlements. We also evaluate the relative strengths and weaknesses of each remedy, both in terms of its efficacy and in terms of its potential to be implemented. We conclude that the most promising solution resides in the revival and widespread use of equitable doctrines—misuse of rights, unclean hands, and abuse of process—in combination with punitive damages. This set of remedies has the potential to deter strategic abuse of lower litigation costs and will go a long way toward restoring the integrity of rights.

Structurally, the Article unfolds as follows. In Part I, we review the economic and deontological accounts of rights and show how they both overlooked rights' intrinsic dependency on the cost of vindication as compared to the cost of challenge. In Part II, we present our core thesis that rights are relationally contingent and consequently prone to be taken over by expedient challengers. In Part III, we identify categories of cases in which this dynamic is pervasive as challengers with lower litigation costs can systematically force the weaker rightsholders into undeserved surrender of entitlements. In Part IV, we present several proposals for reform that aim at restoring the integrity of rights by weakening the power of parties with lower litigation costs. A short Conclusion follows.

#### I. ECONOMIC AND DEONTOLOGICAL THEORIES OF RIGHTS: A CRITICAL REVIEW

The principal difference between economic and deontological theories of rights can be summed in one sentence: deontological theories allocate entitlements to persons to protect intrinsic values of importance to the person, whereas economic theories match persons to entitlements in a way that maximizes aggregate wealth at any given time. Deontological theories are morality-driven en-

dowers,<sup>16</sup> while economic theories are welfare-oriented matchmakers.<sup>17</sup>

For deontological theories, the key question is whether an individual deserves the entitlement in question. For economic theories, the key question is who is the entitlement's best user from a social welfare perspective. Deontological theories use moral desert as a sole criterion for determining entitlements and granting them to people. For economic theories, the sole criterion for identifying an entitlement's best user—an individual whose use of the entitlement will improve society's welfare—is utility.

As we will show, each theoretical approach, albeit for a different reason, overlooks the core insight that we identify in this Article as the relational contingency of rights. Deontological theories miss this insight because they end at the point at which the law recognizes legal entitlements. Deontologists do not look beyond this point and, consequently, do not consider the operation of entitlement-enforcing mechanisms. As a result, they fail to appreciate that a rightsholder will not be able to realize her entitlement against a challenger whose litigation costs are lower than hers.

Economic theories, by contrast, have no pre-set endpoint: for them, any entitlement is a fair game and a tradable unit in society's continual pursuit of welfare. For these theories, entitlements play no special role in cost-benefit tradeoffs carried out by policymakers and courts.<sup>18</sup> These theories consequently do not necessarily see special harm in the dissipation of legal entitlements whose owners cannot afford the cost of litigation against thrift challengers. We

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<sup>16</sup> See Robert Nozick, *Anarchy, State, and Utopia*, at ix–xi, 28–30 (1974) (favoring a strong deontological format of rights as unbending endowments).

<sup>17</sup> See Richard A. Posner, *Economic Analysis of Law* 40 (8th ed. 2011) (“The proper incentives are created by parceling out mutually exclusive rights to the use of particular resources among the members of society. If every piece of land is owned by someone—if there is always someone who can exclude all others from access to any given area—then individuals will endeavor by cultivation or other improvements to maximize the value of land. Land is just an example. The principle applies to all valuable resources.”); see also Joe Mintoff, *Can Utilitarianism Justify Legal Rights with Moral Force?*, 151 *U. Pa. L. Rev.* 887, 901, 905–09 (2003) (justifying a utilitarian theory under which individuals are given rights in order to maximize human welfare); cf. David Lyons, *Utility and Rights*, in *Theories of Rights*, supra note 11, at 110, 111, 113–20 (arguing that utilitarian justifications of rights have no moral force).

<sup>18</sup> See generally Matthew D. Adler & Eric A. Posner, *New Foundations of Cost-Benefit Analysis* (2006).

posit, however, that dissipation of entitlements should not be a readily acceptable outcome even to efficiency scholars, as it brings about socially deleterious consequences. Economically minded scholars and policymakers should care about the relational contingency of rights.

In the following analysis, we develop these arguments in more detail. We first examine the relevant Law and Economics literature and then move to discuss the jurisprudential theories of rights.

#### *A. Economic Literature*

Economic theory, being amoral,<sup>19</sup> attributes no independent importance to rights as such. Economic literature uses the terms “rights” and “entitlements” interchangeably and does not define them with any particular degree of precision. For writers in the Law and Economics school of thought, legal entitlements are no more than bargaining “chips”: legal commodities that can be bought or sold in the marketplace. The entitlements’ content and meaning are of no consequence either. The only thing that matters is for entitlements to be clearly defined so as to make them fit for voluntary exchange.<sup>20</sup> Indeed, voluntary exchange is the paramount value from an economic perspective, as it promotes allocative efficiency. More precisely, voluntary exchange ensures that entitlements gravitate to their highest-value users in a process that is welfare enhancing.<sup>21</sup>

With voluntary exchange being the norm, Law and Economics scholars view usurpations or takings of others’ entitlements with disfavor. The reason is obvious: nonconsensual transfers can move entitlements to highest-value users only accidentally, rather than by design. More often than not, such transfers erode society’s wel-

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<sup>19</sup> This feature looms large in Kaplow and Shavell’s seminal juxtaposition of fairness against social welfare. See Louis Kaplow & Steven Shavell, *Fairness Versus Welfare* 11–12 (2002) (attesting that for purposes of economic theory, individuals’ “taste for fairness is no different . . . from a taste for a tangible good or for anything else”).

<sup>20</sup> Another purpose of entitlements’ clear demarcation is strengthening of ownership that incentivizes owners of valuable assets to put those assets to their best use. See generally Henry E. Smith, *Exclusion Versus Governance: Two Strategies for Delineating Property Rights*, 31 *J. Legal Stud.* S453 (2002).

<sup>21</sup> See R.H. Coase, *The Problem of Social Cost*, 3 *J.L. & Econ.* 1 (1960) (famously demonstrating that law can unlock movement of assets and entitlements to their most efficient users by reducing transaction costs that impede voluntary exchange).

fare by benefiting encroachers who bypass the market. Thus, when *X* forcibly appropriates one of *Y*'s rights, we cannot assume that the right is worth more to *X* than it is to *Y*. The only inference one can draw from these facts is that the net value of the right to *X* is positive, since otherwise he would not have appropriated it. But it is impossible to know whether *X* values the right more than *Y*, or vice versa. Voluntary transfers reveal information about the value the transacting parties ascribe to legal entitlements; involuntary transfers do not.<sup>22</sup>

Nonconsensual transfers not only suppress information about the value of entitlements; they also inflict substantive harm: the deprivation suffered by the rightsholder. Such deprivations would occur even in a world with perfect information about the entitlement's valuation by relevant actors. Self-interest maximizers will not hesitate to violate other peoples' entitlements when doing so improves their own utility. The rightsholders' deprivation would not affect the encroachers' decisions so long as they do not have to redress the loss or face criminal liability. Economically minded scholars consequently favor a legal regime that fends off nonconsensual transfers.

That said, legal entitlements make little difference for Law and Economics scholars. Consider the Coase Theorem, the progenitor of economic analysis of the law.<sup>23</sup> In its strong form, this theorem stands for the proposition that entitlements do not matter. Under a more nuanced interpretation, it shows that in a world with perfect information and zero transaction costs, the efficient outcome will be reached irrespectively of the law's initial allocation of entitlements.<sup>24</sup> Voluntary exchange will navigate entitlements to their most efficient users.<sup>25</sup>

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<sup>22</sup> See, e.g., Munch, *supra* note 15, at 477 (showing that under the voluntary exchange system "[c]ompetition among buyers . . . will lead to the development of techniques to discover true seller reservation prices.").

<sup>23</sup> See Coase, *supra* note 21. For an insightful analysis of the theorem, see Robert Cooter, *The Cost of Coase*, 11 *J. Legal Stud.* 1 (1982).

<sup>24</sup> As explained by Cooter, *supra* note 23, at 14, "The [theorem's] basic idea . . . is that the structure of the law which assigns property rights and liability does not matter so long as transaction costs are nil; bargaining will result in an efficient outcome no matter who bears the burden of liability."

<sup>25</sup> See *id.*

The mechanism envisioned by Coase en route to this economically happy end is voluntary exchange. Involuntary transfers, however, are capable of producing the same result. If there were a way to ensure that all involuntary transfers enhance welfare, Law and Economics champions would see no reason to oppose them. This worldview underlies the economic theory of efficient breach.<sup>26</sup> Adherents of this theory see no harm in a breach of contract when it improves social welfare.<sup>27</sup> As Professor Daniel Friedman astutely observed, it is but a small step from supporting efficient breaches to advocating efficient theft.<sup>28</sup>

Efficiency-minded scholars did not overlook the litigation cost asymmetry. Lucian Bebchuk, Steven Shavell, and other Law and Economics scholars have analyzed this phenomenon.<sup>29</sup> Their analy-

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<sup>26</sup> For a both critical and comprehensive review of existing efficient-breach theories, see Daniel Markovits & Alan Schwartz, *The Myth of Efficient Breach: New Defenses of the Expectation Interest*, 97 Va. L. Rev. 1939, 1977–2005 (2011).

<sup>27</sup> *Id.* at 1943–45 (summarizing Law and Economics scholars' justification for efficient breach).

<sup>28</sup> See Daniel Friedmann, *The Efficient Breach Fallacy*, 18 J. Legal Stud. 1, 4 (1989). Theft, of course, is never efficient. See Richard L. Hasen & Richard H. McAdams, *The Surprisingly Complex Case Against Theft*, 17 Int'l Rev. L. & Econ. 367, 370–74 (1997) (explaining that society's unnecessary costs from theft include owners' defensive measures and thieves' operational investments that include expenditures on transactions with stolen goods); Gil Lahav, *A Principle of Justified Promise-Breaking and Its Application to Contract Law*, 57 N.Y.U. Ann. Surv. Am. L. 163, 184–85 (2000) (“[T]heft undermines the tremendous utility of certain intangible benefits associated with a theft-free society, such as: the ability to rely on the future presence of one’s possessions; the ability to trust strangers not to steal one’s personal property; and the ability to enjoy the privacy of a domicile that will not be invaded by thieves.”).

<sup>29</sup> See Janet Cooper Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 Stan. L. Rev. 497, 548–50 (1991) (attesting that plaintiffs in securities class actions extort favorable settlements from defendants because defendants' costs are much higher than theirs); Lucian Arye Bebchuk & Howard F. Chang, *The Effect of Offer-of-Settlement Rules on the Terms of Settlement*, 28 J. Legal Stud. 489, 510–12 (1999) (noting that settlement terms as compared with expected judgment tend to favor the party with lower litigation costs and explaining how fee-shifting rules can ameliorate this problem); John C. Coffee, Jr., *New Myths and Old Realities: The American Law Institute Faces the Derivative Action*, 48 Bus. Law. 1407, 1415 n.39 (1993) (“[T]he existence of asymmetric litigation costs could allow some plaintiffs to exploit this cost differential to obtain a settlement unrelated to the merits.”); James D. Hurwitz, *Abuse of Governmental Processes, the First Amendment, and the Boundaries of Noerr*, 74 Geo. L.J. 65, 71 (1985) (noting that predatory litigation can be successful when it imposes disproportionate legal costs on a rival); D. Rosenberg & S. Shavell, *A Model in Which Suits Are Brought for Their Nuisance Value*, 5 Int'l Rev. L. & Econ. 3, 3 (1985) (demonstrating that strike suits with nega-

ses demonstrated with rigor and precision that a party with lower litigation costs can secure a settlement more favorable than the one he would obtain under symmetrical costs.<sup>30</sup> If that party is the plaintiff, the settlement amount he will recover from the opponent will exceed the expected value of the suit. If that party is the defendant, his settlement payment to the opponent will fall below the suit's expected value.<sup>31</sup> This outcome, however, is not inefficient in and of itself, as the savings in the trial costs may offset the overpayments and underpayments occasioned by extortionary settlements.<sup>32</sup>

Unfortunately, these important works have stopped short of analyzing the broader economic consequences of this phenomenon. An actor with a litigation cost advantage may abridge or altogether obliterate other people's entitlements when doing so is detrimental to welfare. Self-interest maximizers will tend to take advantage of rightsholders who cannot protect their entitlements in court at a comparable cost. Ex ante, therefore, asymmetrical litigation costs have a profoundly undesirable effect on society: they prompt actors with low litigation costs to bypass voluntary exchange, encroach on, or otherwise violate other people's entitlements and subsequently force these people—who must expend

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tive-expected value are possible when plaintiff can exploit asymmetric litigation costs to extort settlement); see also William H. Wagener, Note, Modeling the Effect of One-Way Fee Shifting on Discovery Abuse in Private Antitrust Litigation, 78 N.Y.U. L. Rev. 1887, 1902–04 (2003) (summarizing literature that analyzes the effects of litigation cost asymmetries).

<sup>30</sup> See, e.g., Bebchuk & Chang, *supra* note 29, at 510–11.

<sup>31</sup> See *id.*

<sup>32</sup> Consider again the conflict between Brutus Inc. and Anne, but assume this time that Anne has found an incredibly inexpensive and capable attorney who can vindicate her entitlement to quiet enjoyment for a \$1000 fee. Aware of this circumstance, Brutus makes a proposal to recognize the entitlement if Anne pays it \$1000 in return. The parties' conflict, of course, would be best resolved if Brutus were to recognize Anne's entitlement for free. The company's extortion of that payment, however, still leads to the economically second-best state of affairs, vastly superior to the otherwise probable scenario in which the parties go to court to litigate quiet enjoyment. Under that scenario, Anne's entitlement will be redeemed at a much steeper price. Brutus' extortion of \$1000 consequently can be viewed as an efficient transaction that saves the parties and society at large the expense of the trial and opens up the possibility for Anne's attorney to apply his talent elsewhere. As the famous adage goes, "A bad settlement is better than a good trial." See, e.g., *Strong v. BellSouth Telecomm., Inc.*, 173 F.R.D. 167, 172 (W.D. La. 1997) ("In this case, I could hold my nose and accept the [suspicious class-action] settlement, after all, it is said that a bad settlement is better than a good trial.").

more on litigation—into a full or partial surrender of their rights. This effect is far more severe than extortionary settlements.

Failure to attend to this broader issue is not the only shortcoming of the asymmetric-cost literature. This literature is highly abstract, insular and divorced from the broader jurisprudential context of legal rights. As a result, it pays no attention to the special role that rights play in our society as protectors of individuals' worth and wellbeing. This neglect is not surprising: rights and other rudiments of analytical jurisprudence carry no weight in the Law and Economics literature. The economists' declination to take rights seriously<sup>33</sup> may well be the logical consequence of their all-encompassing cost-benefit tradeoffs.<sup>34</sup> Yet, it puts the Law and Economics literature in tension with prevalent understanding of rights among jurists, courts, and laypeople as well.

The tension, or even disconnect, between the Law and Economics approach to rights and the prevalent conception thereof makes the former vastly incomplete, if not socially irrelevant. Our legal system is entitlement-based, and not accidentally so.<sup>35</sup> The law grants people entitlements to protect their personhood,<sup>36</sup> to secure their freedom to choose among different courses of action,<sup>37</sup> to im-

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<sup>33</sup> This declination separates mainstream economists from rights deontologists. See Ronald Dworkin, *Taking Rights Seriously* 92–97, 200 (1978) (asserting and justifying rights' immunity from utilitarian trade-offs).

<sup>34</sup> See generally Kaplow & Shavell, *supra* note 19, at 5 (underscoring normative superiority of cost-benefit analysis).

<sup>35</sup> See Jack N. Rakove & Elizabeth Beaumont, *Rights Talk in the Past Tense*, 52 *Stan. L. Rev.* 1865, 1865 (2000) (reviewing Richard A. Primus, *The American Language of Rights* (1999)) (“Rights have been a staple of Anglo-American law and politics since at least the seventeenth century.”); see also J. Harvie Wilkinson III, *The Dual Lives of Rights: The Rhetoric and Practice of Rights in America*, 98 *Calif. L. Rev.* 277, 281 (2010) (observing that rights “help[] to shape our most important legal institutions,” while arguing that rights are absolute only in speech, but defeasible in practice when special circumstances call for their removal, and describing this duality as an example of “our nation’s most admirable qualities”).

<sup>36</sup> See James Griffin, *On Human Rights* (2008) (unfolding a comprehensive personhood-based account of human rights); Margaret Jane Radin, *Property and Personhood*, 34 *Stan L. Rev.* 957, 957 (1982) (developing a personhood account of entitlements that includes protection of property rights upon recognition that a person cannot properly develop herself without having some control over resources in the external environment).

<sup>37</sup> See Gerald Dworkin, *The Theory and Practice of Autonomy* (1988) (laying out autonomy theory); H.L.A. Hart, *Legal Rights*, *in* *Essays on Bentham: Studies in Jurisprudence and Political Theory* 162, 183–84 (1982) (advancing an autonomy-based

prove their wellbeing,<sup>38</sup> and to motivate their engagement in activities that benefit our society as a whole.<sup>39</sup> Hence, when a person's entitlement cannot be actualized on account of high litigation costs, the underlying purpose of the entitlement is defeated as well. When an entitlement protects personhood and free choice, its unenforceability will make the person less autonomous, force her into insecurity, and might even cause her to experience unworthiness as a human being. When an entitlement protects its holders' wellbeing, its unavailability will erode the quality of the person's life. Finally, when an entitlement is designed to reward individuals who engage in a particular socially beneficial activity, its unavailability will deny individuals the benefit they labored to obtain and thereby compromise society's interest in encouraging individuals to pursue that activity. Furthermore, society's failure to redress the plight of the entitlement holder will incentivize encroachers who can litigate at a low cost to misappropriate others' entitlements instead of pursuing more productive activities.

### *B. Jurisprudential Literature*

Theories of rights provide a useful vantage point for analyzing the effects of unrealizable entitlements. Theoretical writings on rights illuminate the importance of legal entitlements and the social benefits arising from their existence.<sup>40</sup> Naturally, once an entitlement becomes unrealizable, the benefit it was supposed to generate is lost. Entitlements bring about diverse benefits, but the meth-

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account of rights); see also Charles Fried, *Modern Liberty and the Limits of Government* (2007) (offering an account of rights that underscores the primacy of individuals' autonomy over the government's vision of the good); Matthew D. Adler, *Rights Against Rules: The Moral Structure of American Constitutional Law*, 97 *Mich. L. Rev.* 1, 2-3 (1998) (recommending "moral reading" of the Constitution that perceives rights as limitations on the government's power to set up rules regulating individuals' conduct).

<sup>38</sup> See, e.g., Neil MacCormick, *Legal Right and Social Democracy: Essays in Legal and Political Philosophy* 143 (1982) ("[R]ights always and necessarily concern human goods, that is, concern what it is, at least in normal circumstances, good for a person to have.").

<sup>39</sup> See, e.g., John H. Garvey, *What Are Freedoms For?* (1996) (offering an account of freedoms consisting of rights that serve societal good).

<sup>40</sup> For a superb exposition of existing theories of rights, see Alon Harel, *Theories of Rights*, in *The Blackwell Guide to the Philosophy of Law and Legal Theory* (Martin P. Golding & William A. Edmundson eds., 2005).



odology by which entitlements are identified stays invariant across different theories of rights and the ideologies they represent. Rights theorists compare a regime that recognizes and respects individuals' entitlements with one that does not. Theories associating entitlements with personhood, for example, emphasize the perniciousness of a rightless regime that exposes every individual to the omnipresent prospect of being used as a tool for promoting other people's goals.<sup>41</sup> Any such instrumentalization violates personhood by eroding the individual's intrinsic value as a human being. To forestall this erosion, the state must set up entitlements that will protect personhood.<sup>42</sup>

From another angle, autonomy-based theories of rights underscore the effect of entitlements on actors' freedom to choose the right course of action for themselves.<sup>43</sup> In a world without legal rights, an actor's ability to form and act upon autonomous choices will crucially depend on the balance of power between her and other people whose interests clash with her endeavors. Other people may attempt to thwart the actor's endeavors or even coerce her into acting according to their will. Whether they will succeed in doing so will depend on how much power they have relative to the actor. The dependency on others and their decisions undermines the actor's self-governance and ability to live as a free individual. To free individuals of this dependency and grant them true freedom of choice, the state must grant individuals entitlements that will protect their autonomy.<sup>44</sup>

Another influential thread in the rights literature associates entitlements with their holders' wellbeing.<sup>45</sup> The wellbeing theories of rights maintain that the state's allocation of freedoms and prop-

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<sup>41</sup> For an early statement of this idea, see 2 John Stuart Mill, *Principles of Political Economy with Some of Their Applications to Social Philosophy* 560 (D. Appleton & Co. 1909) (1848) ("Whatever theory we adopt respecting the foundation of the social union, and under whatever political institutions we live, there is a circle around every individual human being, which no government, be it that of one, of a few, or of the many, ought to be permitted to overstep . . . [T]here is, or ought to be, some space in human existence thus entrenched around, and sacred from authoritative intrusion . . .").

<sup>42</sup> See Griffin, *supra* note 36, at 33–37; Radin, *supra* note 36, at 1014–15.

<sup>43</sup> See Dworkin, *supra* note 37; Hart, *supra* note 37.

<sup>44</sup> See, e.g., Matthew H. Kramer, *Rights Without Trimmings*, in *A Debate Over Rights: Philosophical Enquiries* 7, 75 (Matthew H. Kramer et al. eds., 1998).

<sup>45</sup> See MacCormick, *supra* note 38, at 143.

erty-related entitlements across individuals determines what those individuals can and cannot enjoy as they go about their lives. When rights are not recognized, an individual's ability to enjoy her freedoms and possessions will be severely compromised by the continual threat of their violation. Other individuals, and the state itself, may harbor interests and desires that conflict with the individual's freedoms and possessions and hence jeopardize her enjoyment of her freedom and property. If the threat is carried out, it will be damaging—sometimes even devastating—to the individual's well-being. To fend off this threat to the individual, the state must grant her entitlements that she can use as a shield against encroachments.

Finally, instrumental or consequentialist theories of rights emphasize the benefit of the rights' correlatives—namely, the duties they impose on other people to act or avoid acting in a particular way.<sup>46</sup> Under these theories, the state sets up entitlements to force or motivate the entitlements' subordinates (or duty bearers) to behave in a socially beneficial way.<sup>47</sup> To this end, the state grants entitlements to its agencies and to private individuals. Those individuals are not the entitlements' ultimate beneficiaries. Rather, they receive their entitlements and the underlying proprietary and monetary rewards as an inducement to enforce the correlative duties of other people.<sup>48</sup> Those individuals thus function as the state's agents and get their rewards in return.<sup>49</sup> They are granted entitlements when private enforcement of the law is more cost-effective than public enforcement.<sup>50</sup>

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<sup>46</sup> The correlativity concept originates from Hohfeld, *supra* note 5, at 30 (introducing the concept of “jural correlatives” and explaining duties as correlatives of rights).

<sup>47</sup> Not all consequentialist theories of rights are utilitarian. See, e.g., Garvey, *supra* note 39, at 2 (arguing that rights exist to enable individuals to make virtuous choices and to impose corresponding moral duties on government).

<sup>48</sup> See Harel, *supra* note 40, at 197 (underscoring that, in some cases, “it is utilitarian or quasi-utilitarian considerations that determine who controls a duty”).

<sup>49</sup> See Gary S. Becker & George J. Stigler, *Law Enforcement, Malfeasance, and Compensation of Enforcers*, 3 *J. Legal Stud.* 1, 13–16 (1974) (identifying conditions under which private enforcement of the law economically dominates public enforcement).

<sup>50</sup> See William M. Landes & Richard A. Posner, *The Private Enforcement of Law*, 4 *J. Legal Stud.* 1, 14–15 (1975) (arguing that private enforcement is economically suboptimal when government can intensify deterrence by increasing penalties without

To illustrate the differences between these theories, consider a person who owns a house in which she lives. Assume that a trespasser takes over her house, drives her away and denies her the ability to use it. Under personhood-based theories of rights, when the state does not prevent the trespasser from encroaching and fails to remedy the wrong after its occurrence, it allows the trespasser to devalue the homeowner as a human being.

Autonomy-based theories highlight a different aspect of the homeowner's harm. By acting against the homeowner's will, the trespasser deprived her of the ability to make autonomous choices with regard to her property. The state's failure to redress the wrong further undermines the homeowner's self-governance.

Rights theories that put the premium on individual wellbeing will be concerned about the value the homeowner lost as a result of the deprivation she suffered. The state's failure to make her whole and reinstate her former status condones the erosion of her wellbeing.

Finally, consequentialist theories of rights would denounce the state's failure to intervene on the ground that it creates perverse economic incentives. The state's failure to protect property rights encourages intrusions of private property and induces excessive investment in private protection of property as well as suboptimal development of assets. This failure also dilutes the value of individuals' productive efforts and may even breed violence.<sup>51</sup>

Our goal in this Article is not to determine which of the theories is normatively or descriptively superior.<sup>52</sup> Nor do we need to decide

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making expensive enforcement efforts, while self-interested private enforcers will make efforts to realize their entitlements).

<sup>51</sup> See, e.g., Jonathan R. Hay et al., *Privatization in Transition Economies: Toward a Theory of Legal Reform*, 40 *Eur. Econ. Rev.* 559, 562–64 (1996) (demonstrating that efficient enforcement of entitlements crowds out enforcement by mafia and vice versa).

<sup>52</sup> The four groups of theories described in the preceding paragraphs track the analytical divide between the “will” or “choice” theory of rights and the “interest” theory of rights. See Harel, *supra* note 40, at 194–95. Another important aspect of rights theories is whether rights should function as “trumps” that defeat competing interests even when those interests outscore the rights on the utility scale. The rights-as-trumps approach characterizes the personhood- and the autonomy-based theories of rights. *Id.* at 197–98. Some of the wellbeing theories of entitlements adopt this approach as well. See Dworkin, *supra* note 33, at 91–93, 199, 204–05 (arguing that violating one's right means “treating a man as less than a man, or as less worthy of concern than

which theory does a better job of capturing the harm occasioned by the denial of rights and entitlements. The only thing that is important for our purposes is the recognition that *some* distinct harm is inflicted whenever a person is denied her entitlement. Whether the main harm from the entitlement's denial comes from the erosion of the holder's personhood, autonomy, or wellbeing, or from the loss to society at large, is a question that need not be resolved here. All rights theorists agree that denial of rights invariably leads to harm, and we proceed from this premise as well.

The case of denial of a right, however, is not identical to the case of unrealizable entitlements. In the latter case, a person's entitlement is not denied. In fact, the legal system is ready to enforce it, but the person cannot afford to vindicate it in court. One might argue that although this result is unquestionably regrettable, it is morally and economically different from a deliberate denial or suppression of a person's right. Both analytically and as a matter of substance, unrealizability of entitlements presents a distinct problem that calls for independent analysis. In the case of unrealizable entitlements, the core problem is not the state's refusal to recognize a certain entitlement but rather the cost of enforcement. Yet from the vantage point of the entitlement holder, inability to enforce the entitlement will in many cases have the same effect as not having the entitlement to begin with.

Unrealizability of entitlements may not present a problem that calls for legal intervention when it happens accidentally in a small number of cases. Such cases, while unfortunate, do not threaten to unravel our entitlements-based system. However, when an entitlement is systematically turned into a dead letter of the law, policymakers have serious cause for concern. Accepting this state of affairs may bring about socially devastating consequences. This can be most readily seen in the case of criminal prosecutions. Consider the case of an unscrupulous prosecutor who files misdemeanor

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other men" and that rights constitute "the majority's promise to the minorities that their dignity and equality will be respected."). Under the prevalent—welfare-oriented—consequentialist accounts, rights are defeasible in the sense that a cost-benefit analysis can justify their removal. See, e.g., Richard A. Posner, *Overcoming Law* 387–405 (1995). These differences do not affect our discussion of entitlements' unrealizability.

charges against multiple defendants to induce guilty pleas.<sup>53</sup> While the charges are baseless, defending oneself against them is expensive—indeed, costlier than pleading guilty to and getting punished for a relatively minor misdemeanor charge. Under these circumstances, all rational defendants—both guilty and innocent—will likely plead guilty.

The same might happen in other areas of the law. Individuals and corporations may systematically use their relative cost advantages to erode entitlements that arise out of property and contractual arrangements, and even constitutional rights. In Part III, we illustrate this deleterious potential by providing examples that involved the entitlements of insurance holders, intellectual property users, and criminal defendants. But, of course, systematic asymmetries in litigation costs pervade other areas of the law as well. Taxpayers often face a similar problem in their dealings with the tax authorities.

Loss of entitlements on account of high enforcement costs should alarm policymakers for several reasons. First, and most obviously, it harms the entitlement holder. Rights theorists may disagree whether the harm is to her personhood, autonomy, or well-being, but none will contest the fact that she suffered some serious harm. Second, entitlement erosion undermines the goals of society at large since it upsets the balance of powers and freedoms within society. After all, entitlements are granted for a reason and their systematic non-enforcement therefore impairs policymaking. Third, the possibility of entitlements' erosion creates a perverse incentive for third parties to deliberately intrude on others' entitlements. Correspondingly, it induces inefficient changes in the behavior of entitlement holders who foresee the possibility that they will not be able to enforce their legal rights and privileges.

With one important exception, existing theories of rights have overlooked the cost of enforcing rights almost completely and have paid no heed to the social cost of enforcing rights. The exception is Professors Stephen Holmes and Cass Sunstein's analysis of rights that centers on the cost of enforcement.<sup>54</sup> Specifically, Holmes and Sunstein demonstrated how the social cost of enforcing rights alters

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<sup>53</sup> See *infra* Section III.C.

<sup>54</sup> See Holmes & Sunstein, *supra* note 14, at 18–22.

our conventional understanding of rights. Their account begins with a simple observation that rights cannot vindicate themselves: they always require enforcement and are often contested. Society, therefore, needs to set up adjudicative procedures and other costly mechanisms for enforcing rights, and it will have to pay for those mechanisms with its taxpayers' money. Society's need to subsidize rights thus unravels the classic distinction between the so-called "negative rights" that fend off interference with the rights' holders and the so-called "positive rights" to welfare.<sup>55</sup> Because society must (and does) subsidize the protection of negative rights, the enforcement of which is often costly,<sup>56</sup> negative rights too are grounded in welfare.<sup>57</sup> If society were to remove its welfare protection from negative rights, it would doom many of them to extinction.<sup>58</sup>

Holmes and Sunstein's account of rights is important both analytically and practically. It provides guidance as to real-world policies. However, it fails to notice a crucial dynamic that determines the effect of entitlements' enforcement cost on their holders' ability to realize them. Whether an entitlement holder will choose to protect an entitlement does not only depend on how much it costs her to vindicate it *in court* but also—indeed, primarily—on an attacker's cost of challenging the entitlement. When the cost of challenging an entitlement is prohibitive, the entitlement will not be challenged and its holder will be able to enjoy it for free. Hence, the fact that an entitlement is costly to enforce does not by itself imply that it will not be realized in the absence of a subsidy from the government. A state subsidy is required only when a third party is willing to expend money and effort to challenge the entitlement. As we showed, this will often happen when the challenger enjoys a significant cost advantage over the entitlement holder.

Contrariwise, when the cost of challenging (or taking over) an entitlement is systematically lower than the cost of defending it, the entitlement may become unrealizable. The entitlement holders will choose to forego its enforcement, effectively relinquishing it. This

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<sup>55</sup> Id. at 218–22.

<sup>56</sup> Id. at 43–44.

<sup>57</sup> Id. at 222.

<sup>58</sup> Id. at 44 (“[A]ll rights presuppose taxpayer funding of effective supervisory machinery for monitoring and enforcement.”).

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insight has profound implications for law enforcement. The government must not rush to expend taxpayers' money on subsidizing the defense of entitlements. Instead, it can tax attacks on entitlements by imposing special procedural and evidentiary burdens upon anyone who deliberately seeks to deprive others of their entitlements by utilizing economies of scale or scope. In Part IV below, we make a number of proposals that follow this approach.

## II. THE RELATIONAL CONTINGENCY THESIS

In this Part, we present the core thesis of the Article, which holds that all entitlements are relationally contingent. Accordingly, legal formalization of rights and entitlements does not guarantee their effectiveness against all intended duty holders. In the real world, rights will oftentimes fail to protect the underlying value they were enacted to defend, and, worse yet, may expose the rightsholder to predation by others. As we will show, this insight has far-reaching implications for the way policymakers and scholars think about rights and entitlements. However, before proceeding to analyze these implications, we will first position our core thesis within the larger framework of the rights literature and explain what causes rights and entitlements to be relationally contingent in the real world.

The conceptual literature on rights and entitlements is too vast to be summarized in a single article. At a risk of a mild overgeneralization, the literature may be divided into two categories. The first may be termed as "rights idealism."<sup>59</sup> It consists of analytical examination of rights and entitlements as ideal legal concepts operating in a constraint-free world. The main contributions to this genre were made by legal philosophers seeking to understand and illuminate the concept of rights. This body of scholarship is largely divorced from real-world constraints and pragmatic concerns, such as cost and how rights and entitlements operate in reality. Scholars who work in this tradition see their mission as elucidating the essential characteristics of legal entitlements, offering typologies of entitlements, and positioning entitlements within the greater framework of legal concepts. These scholars are by and large

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<sup>59</sup> For an important critique of rights idealism in constitutional law, see Daryl J. Levinson, *Rights Essentialism and Remedial Equilibration*, 99 *Colum. L. Rev.* 857 (1999).

avowed deontologists, who proceed on the assumption that entitlements, once formalized, are readily capable of performing the tasks assigned to them by lawmakers.

Ronald Dworkin's highly influential work<sup>60</sup> provides a useful illustration. Characterizing rights as "trumps," Dworkin advances a powerful argument for why rights should prevail over utilitarian considerations. This argument develops a purist and highly abstracted conception of rights, unaffected by institutional constraints and real-world interactions. Dworkin postulates that rights have independent existence and viability and are also equipped with the special power to fend off utilitarian challenges.<sup>61</sup> Understandably, he does not even consider the possibility that the same utilitarian factors he dismisses may render rights ineffective on the ground in such a way that courts will not be able to salvage them. The cost of enforcing legal rights is the most significant of those factors. In other words, Dworkin and other rights idealists have ignored the basic fact that rights are not self-enforcing and hence inherently vulnerable to cost constraints.

The second thread in the rights literature is best described as "court-centered theories of entitlements." By contrast to "rights idealism," this body of scholarship focuses exclusively on how entitlements are implemented by courts. Contributors to this scholarship are predominantly pragmatists, who take an avowedly practical approach that seeks to explain how rights affect litigation outcomes. This approach to entitlements is taken by virtually all Law and Economics specialists and by a smaller number of Law and Society scholars. The celebrated "Cathedral" article by Guido Calabresi and Douglas Melamed<sup>62</sup> vividly illustrates the Law and Economics scholars' approach. This article offers a fascinating account of how courts should protect legal entitlements—the Law and Economics equivalent of rights. Alas, as Carol Rose correctly observes, "Cathedral" at its core is an article about remedies rather than about entitlements as such.<sup>63</sup> The article enumerates three re-

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<sup>60</sup> Dworkin, *supra* note 33.

<sup>61</sup> *Id.*

<sup>62</sup> Guido Calabresi & A. Douglas Melamed, Property Rules, Liability Rules, and Inalienability: One View of the Cathedral, 85 *Harv. L. Rev.* 1089 (1972).

<sup>63</sup> See Carol M. Rose, The Shadow of the Cathedral, 106 *Yale L.J.* 2175, 2177–82 (1997).



medial modes of entitlements' protection—property rules, liability rules, and inalienability—and then moves on to tell readers how to choose the right mode of protection in order to maximize social welfare.<sup>64</sup>

Law and Society scholars, for their part, focus on the legal process more broadly. Specifically, they explore how inequalities in wealth distribution might distort legal processes and lead to socially inequitable results irrespective of the initial allocation of rights. This line of scholarly work builds on Marc Galanter's seminal essay "Why the 'Haves' Come Out Ahead," which demonstrates how affluent litigants can obtain more favorable outcomes in courts on account of superior legal representation.<sup>65</sup>

Surprisingly, scant attention has been paid to the role of entitlements *outside* the courts. Neither trend has consistently examined this important aspect of legal entitlements. Our analysis seeks to redress this omission. We would like to emphasize at this point that we do not intend to challenge any of the existing accounts of legal entitlements. Rather, our aspiration is to complement these accounts. We readily acknowledge the importance of legal formalization of entitlements. Formalization of entitlements lowers information costs for holders and duty bearers, economizes on individuals' compliance costs, facilitates adjudication and dispute resolution expenses, and enables voluntary exchange. It also makes entitlements more valuable to their holders by giving them effect vis-à-vis the largest possible number of individuals and by putting the coercive powers of the state at the rightsholders' disposal.<sup>66</sup> We likewise recognize the important role of courts and legal processes in protecting rights. Indeed, the fact that entitlements must be vindicated via legal process is what makes them relationally contingent.

Our account differs from the previous accounts of rights in that it focuses on the role that legal entitlements play in real-world interactions between actors. Accordingly, the discussion in the pages ahead aims to bridge the gap between rights idealism and the court-centered theories of entitlements. Temporally, we are interested in the period after an entitlement's formalization but before

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<sup>64</sup> Calabresi & Melamed, *supra* note 62, at 1092–93, 1096–98.

<sup>65</sup> See Galanter, *supra* note 8, at 103–04, 114.

<sup>66</sup> See Abraham Bell & Gideon Parchomovsky, *Property Lost in Translation* (May 8, 2012) (unpublished manuscript, on file with the Virginia Law Review Association).

it becomes the subject of litigation. To paraphrase a famous legal metaphor,<sup>67</sup> we focus primarily on the unmaking of entitlements in the shadow of the litigation costs and on how to prevent this.

To illustrate, consider the famous jurisprudential distinction between rights in rem and rights in personam. As any person trained in the law knows, rights in rem avail against the rest of the world, while rights in personam are effective vis-à-vis a certain individual or a specified group of individuals. The accepted lore holds that an entitlement's formal recognition as a right in rem or a right in personam determines the group of individuals against whom the entitlement is effective. Rights and entitlements are not self-enforcing, however. Most of the time, their subordinates—the duty holders—will respect them. But there will be cases in which duty holders will fail to respect entitlements and may even violate them deliberately. In such cases, the entitlement holder will have to rely on the legal process to protect her entitlement. The legal process is not cost free. Litigation requires investment of resources—in many cases, a substantial investment. When an entitlement holder does not have the financial wherewithal to vindicate the entitlement in court, the entitlement will fail to protect her regardless of its classification as a right in personam or a right in rem. In reality, the group against which the right avails may be a null set.

This observation about the effectiveness of rights and legal entitlements is not confined to extreme cases. On the contrary, it can be generalized. Rightsholders who have the financial means to protect their entitlements may rationally choose not to do so as well when the cost of vindicating the entitlement in court exceeds the benefit thereof. One might think that this is not too troubling; after all, the owner should decide whether to vindicate her right and at what cost. However, this narrow view ignores the incentive effect of the cost-driven desertion of entitlements on their subordinates. Opportunists with low litigation costs can violate others' entitlements, thereby compromising the values that the entitlements are set to protect.

In reality, therefore, the effectiveness of a legal entitlement depends on two factors: (1) the cost of defending the entitlement in

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<sup>67</sup> See Robert H. Mnookin & Lewis Kornhauser, *Bargaining in the Shadow of the Law: The Case of Divorce*, 88 *Yale L.J.* 950, 997 (1979).

court; and (2) the cost of challenging it. Consequently, actors with low litigation costs are able to force rightsholders to forfeit their entitlements. They can achieve this result by violating or misappropriating those entitlements and then offering the rightsholders an unconscionable settlement that the rightsholders have no choice but to accept.

Condoning misappropriation of others' entitlements on account of asymmetric litigation costs is neither fair nor efficient. From a moral standpoint, such misappropriations are akin to extortion or, at best, to unconscionable transactions. From an economic standpoint, they represent opportunistic transfers that are welfare diminishing. The existing state of affairs creates an incentive for actors to forego productive activities and search, instead, for entitlements that are prone for the taking. Social resources will systematically be wasted in this way. Worse yet, when any such wasteful predation endeavor compromises an entitlement originating from a productive endeavor of its holder (or the holder's predecessor), it breeds opportunism and extortion. By forcing transfers of wealth from the productive sector to opportunists, such endeavors will bring about a socially perverse regrouping of occupations and talent.<sup>68</sup>

Importantly, the relational contingency of entitlements cuts across wealth lines. The phenomenon is not confined to poor rightsholders, and can also strike the rich. The wealthy, too, may rationally elect to forfeit their rights in order to avoid litigation. To see one such scenario, consider again the fair-use dispute between Ian and Proprietary Images.<sup>69</sup> Assume now that Ian is incredibly wealthy, indeed, wealthier than Proprietary Images. Proprietary Images, however, can litigate the dispute at a much lower cost owing to economies of scale that Ian does not enjoy. These economies accrue to Proprietary Images by dint of the fact that it has litigated multiple similar cases in the past and has ready access to all the legal resources—physical and human—necessary to litigate the case against Ian at a negligible cost. The law firm representing Proprietary Images has developed a standard method of prosecuting the

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<sup>68</sup> Cf. Daron Acemoglu, *Reward Structures and the Allocation of Talent*, 39 *Eur. Econ. Rev.* 17, 18, 20, 27, 32 (1995) (identifying similar dynamics in societies that tolerate corruption).

<sup>69</sup> See *supra* text accompanying note 1.

client's copyright suits against alleged infringers like Ian. Ian, by contrast, will incur a much greater expense if he decides to defend against Proprietary Images's claim. He will have to retain an attorney solely for the purpose of dealing with the infringement allegation. His attorney will then have to educate herself about the facts of the case and applicable legal rules without being able to reuse this knowledge in future cases and spread the cost of its acquisition across multiple clients. Ian's bill for attorney services therefore will not be discounted by economies of scale and scope. Importantly, the gap between the parties' expenses will only widen if the case goes to court, as the preparation time for Ian's attorney is likely to be more substantial than that for Proprietary Images's lawyers. Worse yet, Ian may be subject to hourly billing, which will further drive his cost up.

Being incredibly wealthy (by hypothesis), Ian can pay virtually any legal bill. Unlike most defendants in his position, he can afford sticking to his guns and fighting Proprietary Images in court even at the cost of \$10,000. This course of action, however, would only be rational if Ian valued his psychological satisfaction from the victory as worth \$7000 or more. Otherwise, it would still be most rational for him to surrender to Proprietary Images's demand and pay the company \$3000.

Our relational-contingency thesis has an interesting and counter-intuitive implication that we mentioned in the Introduction. This implication concerns negative-value entitlements—ones that cost more to vindicate than the value they yield to their holders. According to widely held intuition, such entitlements are tantamount to a dead letter of the law unless they are sufficiently similar to each other to be consolidated into a class action—a proceeding that utilizes economies of scale and transforms many negative-value suits into a single action with a positive net value. However, this intuition is inaccurate as it ignores the relational contingency of entitlements. When the cost of an entitlement's vindication exceeds its value to the holder, she will not expend resources and effort on vindicating the entitlement in court. The entitlement, however, may nevertheless provide her with effective protection if the cost faced by potential challengers is higher still. To illustrate, assume that Anne values her entitlement to live in a nuisance-free environment at \$1000. However, Anne's expected cost of vindicat-

ing this entitlement in court is \$1500. Thus, the entitlement has a net value of  $-\$500$ . Nonetheless, it will afford Anne effective protection against her neighbor Ben if Ben's expected value from playing loud music is \$500 while his cost of defending himself, if sued, is \$3000. If Ben causes Anne a nuisance, she can credibly threaten litigation and offer Ben to settle for \$2000. Anticipating this result, Ben will abstain from violating Anne's entitlement *ab initio*.

This happy outcome, however, is far from typical. As we have shown, the relational contingency of rights will oftentimes lead to the opposite scenario: an individual or, more realistically, a large corporation will use its cost advantage in litigation to force out the surrender of a weaker opponent's entitlement. We now turn to identify and discuss the most recurrent of those scenarios.

### III. THE DESTRUCTIVE CONSEQUENCE OF RELATIONAL CONTINGENCY FOR CATEGORIES OF RIGHTS

Not all litigants are created equal—at least, not as far as litigation costs are concerned. While courts treat everyone equally in principle, some litigants enjoy a cost advantage over others. Two things need to be clarified at the outset in connection with this observation. First, cost advantage in litigation does not always positively correlate with wealth. Wealth allows people and firms to secure good legal representation for a price. But it does not, on its own, give a litigant a cost advantage. Cost advantage exists only when a party can litigate at a lower cost than her adversary. Second, cost advantage does not guarantee a victory in court. The actual outcome of a dispute depends on the merits of one's claims. The significance of lower litigation costs lies elsewhere: it enables a party who can litigate more cost-effectively to extract favorable settlements from its opponents. Or, to put it in contractual parlance, lower litigation costs improve a party's bargaining power. This is especially true under the American legal system under which each litigant normally bears her own costs.

Asymmetry in litigation costs may arise by dint of the design of legal rules—substantive, procedural, or evidentiary. For example, the law can interpose heightened pleading and proof requirements in order to make it hard for plaintiffs to file and prosecute certain suits. Consider the legal rules governing securities fraud. Under the

Private Securities Litigation Reform Act of 1995 (“PSLRA”),<sup>70</sup> a securities fraud action cannot survive motion to dismiss when the plaintiff does not provide a detailed account of the defendant’s “scienter” or fails to substantiate his allegations of “scienter” by evidence.<sup>71</sup> This rule blocks potentially unmeritorious class actions that may unjustifiably erode the firm’s stock value and reputation on the market.<sup>72</sup> At the same time, the rule makes it difficult for plaintiffs to commence securities fraud actions.<sup>73</sup>

Conversely, the law can make it easier for plaintiffs to prove their case. To this end, it may adopt various presumptions that favor plaintiffs (such as *res ipsa loquitur*) or employ procedural and evidentiary rules that economize on plaintiffs’ costs. Similarly, the law can increase the relative cost of litigation for defendants by fashioning complex multifactor defenses that can only be proved at a significant cost. For example, Section 11(e) of the Securities Act of 1933 allows a defendant who made “any [false or misleading] statement [with respect to any material fact] in any application, report, or document filed pursuant to [the Act]”<sup>74</sup> to avoid liability by proving that the alleged securities’ drop in market price would have occurred anyway.<sup>75</sup> This “negative causation” defense is complicated and very hard to establish. Courts have decided that “Congress’ desire to allocate the risk of uncertainty to the defendants”<sup>76</sup> calls for the imposition of stringent proof requirements upon defendants who invoke this defense.<sup>77</sup> Specifically, any such defendant must prove by a preponderance of the evidence that the

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<sup>70</sup> Pub. L. No. 104–67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

<sup>71</sup> For discussion of this rule and the relevant case law and literature, see Richard A. Bierschbach & Alex Stein, *Overenforcement*, 93 *Geo. L.J.* 1743, 1762–65 (2005).

<sup>72</sup> *Id.*

<sup>73</sup> See Stephen J. Choi, *Do the Merits Matter Less After the Private Securities Litigation Reform Act?*, 23 *J.L. Econ. & Org.* 598, 622–23 (2007) (demonstrating empirically that alongside their discouragement of frivolous suits, the PSLRA’s heightened pleading and proof requirements have discouraged many meritorious suits by making them unprofitable).

<sup>74</sup> See 15 U.S.C. § 78r (2006) (codified version).

<sup>75</sup> Pub. L. No. 73–22, ch. 38, 48 Stat. 74, 83 (1933) (codified as amended at 15 U.S.C. § 77k(e) (2006)).

<sup>76</sup> *Akerman v. Oryx Commc’ns*, 810 F.2d 336, 341 (2d. Cir. 1987).

<sup>77</sup> *Alaska Elec. Pension Fund v. Flowserve Corp.*, 572 F.3d 221, 234 (5th Cir. 2009) (citing and quoting *Akerman*, 810 F.2d at 341).

decline in the stock's value "resulted 'solely' from factors other than the material omissions [or misstatements]." <sup>78</sup> To establish the requisite disassociation, the defendant must furnish expert testimony that carries out an event study or other economic analysis of the affected stock's fluctuations. <sup>79</sup> The cost of this testimony and the underlying expert work will usually be high. <sup>80</sup> The prospect of

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<sup>78</sup> *Akerman v. Oryx Commc'ns*, 609 F. Supp. 363, 371 (S.D.N.Y. 1984) (quoting *Collins v. Signetics Corp.*, 605 F.2d 110, 115–16 (3d Cir. 1979) (emphasis added)). The *Akerman* trial court further observed that "[t]he influence of general market factors . . . entitles defendants only to an appropriate reduction of damages" and that "[t]he legislative choice to impose the burden of proof on defendants under section 11(e) represents a judgment that the risk of any uncertainty as to causality must fall upon defendants in order to insure the full disclosure that is the primary goal of the Act." *Id.* at 371–72. The court referred in this connection to the Supreme Court's vision of burdens of proof as "[serving] to allocate the risk of error between the litigants and [indicating] the relative importance attached to the ultimate decision." *Id.* at 371 (quoting *Herman & MacLean v. Huddleston*, 459 U.S. 375, 389 (1983)). For similar interpretations of Section 11(e) of the Securities Act, see *In re Adams Golf, Inc., Sec. Litig.*, 618 F. Supp. 2d 343, 347 (D. Del. 2009) (requiring defendant asserting Section 11(e) defense to prove "negative causation" (citing *Akerman*, 810 F.2d at 340, and *Collins*, 605 F.2d at 114)); see also *In re DDI Corp. Sec. Litig.*, No. CV 03-7063 NM, 2005 WL 3090882, at \*14 (C.D. Cal. July 21, 2005) (attesting that defendant's proof burden under Section 11(e) is "heavy" (citing *In re Dynegey, Inc. Sec. Litig.*, 339 F. Supp. 2d 804, 867–68 (S.D. Tex. 2004))).

<sup>79</sup> See *In re Enron Corp. Sec. Derivative & "ERISA" Litig.*, 529 F. Supp. 2d 644, 720 (S.D. Tex. 2006) (noting that "[o]ne method increasingly recognized by courts and mandated by some of them is an event study, a statistical method of measuring the effect of a particular event such as a press release . . . or a prospectus, on the price of a company's stock" and citing court decisions (footnote omitted)); *In re N. Telecom Ltd. Sec. Litig.*, 116 F. Supp. 2d 446, 460, 468 (S.D.N.Y. 2000) (granting summary judgment for defendants where their expert's event study, uncontroverted by the plaintiffs, showed that none of the challenged statements caused increases in the stock price); see also Michael J. Kaufman & John M. Wunderlich, *Regressing: The Troubling Dispositive Role of Event Studies in Securities Fraud Litigation*, 15 *Stan. J.L. Bus. & Fin.* 183, 187–88, 260 (2009) (documenting and criticizing the prevalence of event studies in securities fraud litigation); Marc I. Steinberg & Brent A. Kirby, *The Assault on Section 11 of the Securities Act: A Study in Judicial Activism*, 63 *Rutgers L. Rev.* 1, 36–37 (2010) (documenting defendants' frequent resort to event studies in establishing "negative causation" under Section 11(e) of the Securities Act).

<sup>80</sup> See, e.g., *New Eng. Health Care Emp. Pension Fund v. Fruit of the Loom*, 234 F.R.D. 627, 634–35 (W.D. Ky. 2006) (finding that a "significant component" in plaintiffs' reimbursable expenses of more than two million dollars (not including attorneys' fees) "was the cost of experts and consultants"); Merritt B. Fox, *Why Civil Liability for Disclosure Violations When Issuers Do Not Trade?*, 2009 *Wis. L. Rev.* 297, 306–07 (including the high cost of experts among the factors that raise the social cost of securities fraud litigation).

incurring this cost will exert deterrent effects on the primary behavior of affected parties.<sup>81</sup>

A second source of the litigation-cost asymmetry concerns access to legal counsel and representation. Certain litigants have cheaper access to legal representation than others. Corporations and repeat litigants often pay retainer fees or employ in-house lawyers. Their adversaries, on the other hand, especially when they are private individuals, must expend considerably higher amounts of money and effort to secure adequate legal representation. First, they have to incur search and verification costs to ensure adequate representation. Second, they will be subject to hourly billing.

The cost advantage of repeat litigants is not based on volume alone, however. Such parties can often take advantage of economies of scale and scope that further lower their cost. A firm that faces multiple legal disputes can hire attorneys who will specialize in representing it after acquiring expertise in the relevant litigation areas. These attorneys will develop standard litigation methods that will maximize the firm's chances to prevail in court. Those methods may include repeated engagement of experts, document reviewers, and other specialists. These specialists, too, will set up working protocols that will apply in every case and help the firm achieve the best possible results. This litigation machinery will spread the firm's one-time investment in the dispute resolution across many cases. Consequently, the firm's expenditure on every individual case will steadily decline.

To illustrate, consider a company that holds a large portfolio of patents like IBM or an insurance company like AIG. Many of the legal disputes in which such companies are involved will share numerous common characteristics. Those commonalities allow such companies to rely on past cases in litigating new ones. The presence of recurring elements considerably lowers learning and draft-

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<sup>81</sup> See generally Gideon Parchomovsky & Alex Stein, *The Distortionary Effect of Evidence on Primary Behavior*, 124 *Harv. L. Rev.* 518 (2010) (describing how the quest for favorable evidence affects—and oftentimes distorts—a party's primary behavior); see also Chris William Sanchirico, *A Primary-Activity Approach to Proof Burdens*, 37 *J. Legal Stud.* 273, 276–80 (2008) (showing how allocation of proof burdens can affect the cost and direction of underlying primary activity); Robert E. Scott & George G. Triantis, *Anticipating Litigation in Contract Design*, 115 *Yale L.J.* 814, 858–70 (2006) (showing how default and contractual allocations-of-proof burdens can improve performance of contractual obligations).



ing costs, as well as the cost of legal research. First-time litigants and their representatives must, of course, do everything from scratch.

Asymmetry in the parties' litigation costs is not a rare spectacle in our legal system. In fact, such cases are ubiquitous. When asymmetrical litigation costs occur randomly in our legal system, they do not present a serious cause for concern. However, when they systematically favor one group of litigants over another, they can result in erosion of entitlements. The reason is simple and disturbing at once: the party who holds a cost advantage can always induce her adversary to forego litigation and succumb to a settlement offer even when the law is on her side. A simple numerical example can demonstrate this point. Take a firm whose litigation cost is \$1000 per case and pit it against an individual entitlement holder whose parallel expenditure is \$5000. Under this recurrent scenario, the entitlement holder will be willing to avoid litigation—no matter how successful it promises to be, as far as merits are concerned—by paying the firm any sum up to \$5000. And if the entitlement holder values her entitlement below \$5000, she will surrender to the firm's pressure and forfeit her entitlement altogether, as did Anne in our introductory example.<sup>82</sup>

This decision of the entitlement holder is rational. Indeed, it is the only rational decision she can make. The firm's threat of going to court, given its low litigation cost, is credible. As a consequence of this threat, the entitlement holder stands to lose \$5000. Hence, it is only rational for her to remove the threat by paying the firm any ransom amount below \$5000.<sup>83</sup>

In the remainder of this Part, we discuss three representative cases. We extract those cases from three diverse areas: intellectual property, insurance, and criminal law.

### *A. Intellectual Property*

The field of intellectual property is rife with examples of how asymmetrical litigation costs can lead to the erosion of entitle-

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<sup>82</sup> See supra note 32.

<sup>83</sup> From the entitlement holder's point of view, going to court will only be rational in a rather unusual scenario in which she values her satisfaction from vindicating her entitlement at more than \$5000.

ments. Begin with copyright law. Many creative industries are highly centralized. The rights to the vast majority of musical works and films are held by a relatively small number of corporations. Furthermore, the field is characterized by central enforcement agencies—such as the American Society of Composers, Authors and Publishers (“ASCAP”), the Recording Industry Association of America (“RIAA”), and the Motion Picture Association of America (“MPAA”)—that represent all relevant rightsholders and carry out their litigation initiatives.<sup>84</sup>

Although copyright law is supposed to balance the interests of copyright holders against those of users, numerous scholars have noted that the design of copyright law is slanted in favor of copyright holders.<sup>85</sup> The Copyright Act bestows very broad rights and powers on copyright holders, while making painstaking efforts to define privileges very narrowly and carefully.<sup>86</sup> The most important privilege, or defense, the Act grants to users is fair use. Fair use is supposed to be the bastion of users’ rights and the most important counterweight to the broad powers of copyright owners. Unfortunately, fair use, on account of its complex design, has won itself the

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<sup>84</sup> Recently, a private company made itself an assignee of multiple copyrights solely for the purpose of filing suits against alleged infringers and profiting from those suits by utilizing economies of scale. The company had no standing to file those suits, as only the legal or beneficial copyright owner can sue for infringement. See 17 U.S.C. §§ 106, 501(b) (2006); *Silvers v. Sony Pictures Entm’t*, 402 F.3d 881, 884 (9th Cir. 2005) (en banc). For that reason, presumably, the company did not disclose its assignee status and the copyright owner’s identity in two hundred actions for copyright infringement. The court dismissed the company from the case and ordered it to show cause why it should not be sanctioned for egregious litigation behavior. *Righthaven LLC v. Democratic Underground, LLC*, 791 F. Supp. 2d 968, 978–79 (D. Nev. 2011).

<sup>85</sup> See Gideon Parchomovsky & Alex Stein, *Originality*, 95 Va. L. Rev. 1505, 1509–16 (2009) and sources cited therein.

<sup>86</sup> See, e.g., Neil Weinstock Netanel, *Copyright’s Paradox* 54–80 (2008) (criticizing “copyright’s ungainly expansion”); Yochai Benkler, *Free as the Air to Common Use: First Amendment Constraints on Enclosure of the Public Domain*, 74 N.Y.U. L. Rev. 354, 354–60 (1999) (criticizing the “enclosure movement” in copyright law: the current tendency to outlaw uses of expressive works that were previously considered legitimate); Jessica Litman, *Billowing White Goo*, 31 Colum. J.L. & Arts 587, 587 (2008) (attesting that rights granted by copyright law underwent extraordinary expansion over the past fifty years); John Tehranian, *Infringement Nation: Copyright Reform and the Law/Norm Gap*, 3 Utah L. Rev. 537, 543–48 (2007) (observing that copyright protection and liability for copyright infringement are excessive); Pamela Samuelson, *The Copyright Grab, Wired*, Jan. 1996, at 134, 134 (describing the enclosure dynamic as “the copyright grab”). See generally Siva Vaidhyanathan, *Copyrights and Copywrongs: The Rise of Intellectual Property and How It Threatens Creativity* (2001).

dubious distinction of being the “most troublesome [doctrine] in the whole law of copyright.”<sup>87</sup> As one of us, together with Professor Philip Weiser, observed, fair use’s ability to shield unauthorized users of works is greatly undermined by the uncertainty that has become the hallmark of the doctrine.<sup>88</sup> Furthermore, as Professor James Gibson pointed out, the design of our copyright system allows copyright holders to expand their dominion at users’ expense.<sup>89</sup> Specifically, the vagueness and consequent uncertainty of fair use and other defenses prompt users to pay copyright owners license fees rather than risk litigation.<sup>90</sup> This dynamic leads to accretion of rights by copyright owners.<sup>91</sup>

But the vagueness of the fair use doctrine is only the beginning of the story. All copyright infringement actions share many basic characteristics. To succeed in an infringement suit, a copyright holder essentially needs to show ownership of a valid copyright and infringement by the alleged defendant. She then has to specify the remedies she requests. This is a common pattern in most copyright infringement suits. As a result, plaintiffs’ attorneys who represent clients with large copyright portfolios face a downward sloping cost curve. This means that up to a certain number of cases, the cost of instituting each additional infringement suit will be lower than the cost of bringing the previous suit. Ultimately, the cost curve will flatten out, but even then the relative cost of litigation for plaintiffs’ attorneys will be much lower than it is for defendants’ attorneys.

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<sup>87</sup> *Dellar v. Samuel Goldwyn, Inc.*, 104 F.2d 661, 662 (2d Cir. 1939).

<sup>88</sup> Gideon Parchomovsky & Philip J. Weiser, *Beyond Fair Use*, 96 *Cornell L. Rev.* 91, 100 (2010) (“The standard’s vagueness prevents actors from discerning the optimal behavior that the law requires of them.”).

<sup>89</sup> See James Gibson, *Risk Aversion and Rights Accretion in Intellectual Property Law*, 116 *Yale L.J.* 882, 884 (2007).

<sup>90</sup> *Id.* at 884, 887.

<sup>91</sup> *Id.* at 884. But see Steven J. Horowitz, *Copyright’s Asymmetric Uncertainty*, 79 *U. Chi. L. Rev.* 333, 360–61 (2012) (arguing based on the prospect theory that uncertainty of users’ liability stimulates use of copyrighted works as people generally prefer uncertain losses over certain ones).

The use of central enforcement organizations not only lowers the infringement-detection cost for copyright owners;<sup>92</sup> it also guarantees them an inherent advantage in court. Enforcement organizations are repeat players in the copyright arena. As such, they can produce “cease and desist” letters and court briefs at a much lower cost than their adversaries, and then leverage this advantage into a favorable settlement. These settlements economize on litigation costs, but they also stunt the development of fair-use, misuse, and other copyright defenses, as courts are increasingly denied the opportunity to consider these defenses. A corollary cost of this dynamic is that it sweeps problems under the rug and thereby prevents policymakers from adopting corrective measures. After all, disputes that have been settled privately between the parties rarely make policymakers’ “to do” list.

Importantly, the cost advantage enjoyed by owners of large copyright portfolios has a profound effect on their primary behavior. First, it induces owners to create and acquire large portfolios of copyrighted works. For instance, Getty Images, Inc. recently acquired Flickr’s entire collection of images. Following this acquisition, Getty established an international network of enforcement agencies and started asserting its rights against users of digital photos all over the world.<sup>93</sup> This strategic move is consistent with our analysis, but it is not necessarily disconcerting. Second and much more troubling, certain corporations and individual actors reportedly adopted a “business model” under which they wait for certain works to become “viral,” or in ordinary parlance, enjoy wide distribution over the Internet. Works typically attain this status due to the fact that they are initially distributed freely, often under permission from the original creators. At this point, profit-driven actors, typically corporations, acquire the rights to the works and launch an aggressive enforcement attack against unsuspecting

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<sup>92</sup> See Stanley M. Besen, Sheila N. Kirby & Steven C. Salop, *An Economic Analysis of Copyright Collectives*, 78 Va. L. Rev. 383, 390 (1992) (explaining how copyright collectives economize on monitoring and collection costs).

<sup>93</sup> See Wendy M. Grossman, *Is a Picture Really Worth £1,000?*, *The Guardian*, Nov. 27, 2008, at 1, available at <http://www.guardian.co.uk/technology/2008/nov/27/internet-photography> (same strategy used by a large picture company).

Internet users.<sup>94</sup> The companies' cost advantage in litigation secures the attack's success in virtually every case.<sup>95</sup>

Strategic abuse of intellectual property rights is by no means restricted to the area of copyright. Holders of large patent portfolios enjoy the same cost advantage in litigation, as do owners of sizable copyright pools. In the world of patents, the advantage may be even more pronounced. A patent portfolio will often contain multiple individual patents that cover different aspects of the given technology or product. Due to this fact, a portfolio holder will often be able to make several infringement claims against its rival. Each additional claim will widen the parties' litigation cost differential, thereby dramatically increasing the defendants' motivation to settle.

In the patent context, large portfolios can help their owners avoid costly litigation, "serving to dissuade litigation (and threats thereof) by others in the field, because of the threat (real or implied) of retaliatory litigation."<sup>96</sup> As Professor Polk Wagner and one of us pointed out, "the scale-effects of a portfolio mean that the broader array of possible infringement claims (and the concomitant greater net likelihood of success) allow significant patent portfolios to serve as important defensive mechanisms in a highly litigious environment."<sup>97</sup> This dynamic has an important implication: inventors whose patents are infringed by holders of large

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<sup>94</sup> See, e.g., Michelle Castillo, Law Firm Finds Success Targeting Those Who Post Copyrighted Images, *Time Techland*, Feb. 9, 2011, <http://techland.time.com/2011/02/09/law-firm-finds-success-targeting-those-who-post-copyrighted-images/> (describing a law firm whose strategy is to "[b]uy out the copyrights for viral content and then sue bloggers and other people who violate copyright by reposting those images" and reporting that the firm's annual profits from these suits exceed \$300,000); Alison Frankel, Porn Copyright Troll Targets Strike Back in New Class Action, *Reuters*, July 6, 2012, <http://blogs.reuters.com/alison-frankel/2012/07/06/porn-copyright-troll-targets-strike-back-in-new-class-action/> (reporting that a company pressured thousands of users of the Internet into settlement payments after accusing them of unpermitted downloading of its copyrighted porn materials and that a class action was filed to fend off this practice and reimburse victims).

<sup>95</sup> Indeed, as Professor Jason Mazzone recently demonstrated, copyright owners oftentimes exploit their strategic advantage by filing suits for remedies they do not lawfully deserve. See Jason Mazzone, *Copyfraud and Other Abuses of Intellectual Property Law* (2011).

<sup>96</sup> Gideon Parchomovsky & R. Polk Wagner, Patent Portfolios, 154 *U. Pa. L. Rev.* 1, 36 (2005).

<sup>97</sup> *Id.*

portfolios will choose not to sue them at all in order not to expose themselves to the risk of a retaliatory counter-suit which they can ill-afford.<sup>98</sup>

The abuse of cost advantages is not confined to large corporations. Consider the phenomenon of “patent trolling,” the practice of holding patents solely for the purpose of extracting payments from others, without ever intending to commercialize the underlying invention. Jerome Lemelson, whose name is often mentioned in this context, amassed about six hundred patents during his lifetime and frequently asserted them against various corporations. He became famous in part for suing Japanese and European corporations for infringing his machine-vision patents. The merits of these suits are subject to a heated debate to this day.<sup>99</sup> Yet the foreign corporations chose to settle the suits for \$100 million. Their decision to settle was driven in part by the fear of an unfavorable outcome in court.<sup>100</sup> But Lemelson also enjoyed a substantial cost advantage over his opponents, as he could litigate more cheaply, and this advantage also helped him to extract the settlements.

Strategic litigation threats also pervade the domain of trademark law. The relative advantage in litigation costs enjoyed by large corporations enables them continuously to expand the scope of trademark protection at the expense of small businesses that can ill-afford to protect their rights in lengthy court battles. For example, Adidas, who owns the famous three-stripe mark, can assert its rights against smaller competitors who produce shoes whose designs incorporate two or four stripes, demanding that they cease producing and marketing their shoes even when the shoes’ overall design is different and consumer confusion is highly unlikely. Over

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<sup>98</sup> See Daniel L. Rubinfeld & Robert Maness, *The Strategic Use of Patents: Implications for Antitrust*, in *Antitrust, Patents and Copyright: EU and US Perspectives* 85, 90 (François Lévêque & Howard Shelanski eds., 2005) (observing that large patent holders pay reduced legal fees, which allows them to use litigation warfare to their advantage).

<sup>99</sup> See Adam Goldman, *Some Claim Inventor Lemelson a Fraud*, *USA Today*, Aug. 21, 2005, available at [http://www.usatoday.com/tech/science/discoveries/2005-08-21-lemelson-fraud\\_x.htm](http://www.usatoday.com/tech/science/discoveries/2005-08-21-lemelson-fraud_x.htm).

<sup>100</sup> *Id.*; see also Ashby Jones, *Patent ‘Troll’ Tactics Spread*, *Wall St. J.*, July 8, 2012, <http://online.wsj.com/article/SB10001424052702303292204577514782932390996.html> (reporting proliferation of a business model that involves large corporations acquiring hefty patent portfolios and aggressively suing ostensible infringers in order to extort licensing fees).

time, this strategy can yield Adidas a near monopoly over the incorporation of stripes into the design of shoes and apparel.<sup>101</sup>

Strategic assertion of trademarks is a broad phenomenon that encompasses all industries. This strategy characterizes large corporations and its typical victims are smaller businesses that dare to compete with the corporation. In a recent article, Professor Leah Chan Grinvald aptly called this practice “trademark bullying.”<sup>102</sup> Based on empirical evidence, she reported that

Large corporations send out multitudes of letters demanding small businesses or individuals cease and desist in their use of a trademark that has some resemblance to a large corporation’s trademark(s). On many occasions, these letters appear to be sent out without any analysis of the purported infringement. These letters seem intended to simply intimidate the small business or individual into forgoing the use and/or registration of their trademark.<sup>103</sup>

These letters are so effective that recipients often choose to surrender their trademark entitlements or alter their marks without legal battle. These surrenders are particularly troubling in view of the high costs of a business’s rebranding and readvertising. Professor Grinvald suggests that the source of the problem is that “victims do not have the wherewithal to fight legal battles.”<sup>104</sup> While we do not mean to underestimate the effect of wealth constraints on actors’ decisions, we posit that asymmetrical litigation costs are

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<sup>101</sup> Professor Kevin Greene was the first to note this problem in the context of the entertainment industry. K.J. Greene, *Abusive Trademark Litigation and the Incredible Shrinking Confusion Doctrine—Trademark Abuse in the Context of Entertainment Media and Cyberspace*, 27 *Harv. J.L. & Pub. Pol’y* 609 (2004). He expressed concern about corporations’ abusive litigation strategies, while underscoring that the “effectiveness of lawsuits to silence corporate critics derives in part from the disparity of resources between the plaintiff corporation and the defendant parody artist.” *Id.* at 632–33 (quoting Sarah Mayhew Schlosser, Note, *The High Price of (Criticizing) Coffee: The Chilling Effect of the Federal Trademark Dilution Act on Corporate Parody*, 43 *Ariz. L. Rev.* 931, 948 (2001)).

<sup>102</sup> Leah Chan Grinvald, *Shaming Trademark Bullies*, 2011 *Wis. L. Rev.* 625, 625–26.

<sup>103</sup> *Id.* at 628. Professor Grinvald further reports that the threatening letters are extremely effective: their recipients are business owners who are not trained in the law; the letters are often “written in legalese” and cite “court cases that may or may not be relevant”; and they also give their recipients an “extremely short time-frame for a response.” *Id.* at 628–29.

<sup>104</sup> *Id.* at 629.

equally responsible for the loss of the trademark rights of small businesses. As we explained in Part II, an entitlement's vitality does not depend solely on the cost of defending it in court, but also on how much it will cost the denier to attack it.

### *B. Insurance*

Insurance companies enjoy substantial economies of scale and scope in litigation. These economies stem from the companies' business organization and litigation setup. As far as the former is concerned, the companies systematically assemble and pool together information concerning the probability and the magnitude of the damages they insure against. The companies also elicit relevant personal data from the insured and develop standardized ways of juxtaposing the two sets of information—statistical and personal—against each other. This juxtaposition enables the companies to formulate and price the different policies they offer to individuals and organizations seeking to buy insurance and, subsequently, to assess the validity of policyholders' indemnification claims.<sup>105</sup>

The companies' litigation setup is equally standardized. By and large, it features policyholders who sue the company in court for failure to indemnify. Each of those plaintiffs complains that the company refuses to pay her for the damage that the policy she bought from it is supposed to cover. Some of those suits have merit, while others are unmeritorious or downright fraudulent. To defend against these multiple suits that have a virtually identical pattern, the companies retain (or employ) attorneys specializing in insurance law. To provide insurance companies with proper representation, those attorneys need to make a one-time investment: they need to study the standard terms of the relevant insurance policies and the information already assembled by the company. The attorneys also need to set up routine methods and protocols

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<sup>105</sup> See Emmett J. Vaughan & Therese Vaughan, *Fundamentals of Risk and Insurance* 35–40, 87–90, 130–38 (10th ed. 2008) (explaining how insurance companies gather, pool, and evaluate information pertaining to risks they insure against).



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for working with actuaries, private investigators and other experts.<sup>106</sup>

The resulting economies of scale and scope are enormous. They allow the company not only to take advantage of being a coveted client on an intensely competitive market for attorney services, but also to spread the cost of its representation and all other legal expenses across a very large number of cases. This cost-saving capacity gives the company litigation power that their policyholders cannot match. Any such policyholder, either rich or poor, will have to pay her attorney considerably more than what the company will expend on defending against the suit. The cost differential separating the two parties is vast, and so is the company's opportunity to drive the policyholder into an unfavorable settlement that will effectively obliterate her entitlements under the policy and insurance law. By seizing upon this opportunity, the company will systematically underpay its insured and profit at their expense.

Insurance companies also have a potentially legitimate reason for underpaying policyholders' indemnification claims. Many policyholders falsely exaggerate their losses, and it is not always easy for the company to detect such frauds. The company will consequently do well to factor in the possibility of fraud into its claim decisions and subsequent settlement offers. Under this framework, any indemnification claim that fits into the company's "suspicious" profile will be marked out as potentially fraudulent in calculating the company's claim-resolution proposal. By doing so, the company will reduce its payout to policyholders and deter fraudulent claims. Hence, systematic underpayment of claims might also be an economically optimal strategy for insurance companies.<sup>107</sup>

For good or bad reasons, insurance companies take advantage of their superior cost-differential by underpaying policyholders'

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<sup>106</sup> See, e.g., Stephen J. Choi, *Motions for Lead Plaintiff in Securities Class Actions*, 40 *J. Legal Stud.* 205, 221 (2011) (noting that "the very largest attorney firms . . . enjoy the greatest expertise and economies of scale in bringing a securities class action"); Steven L. Schwarcz, *Explaining the Value of Transactional Lawyering*, 12 *Stan. J.L. Bus. & Fin.* 486, 494 (2007) (specifying economies of scale and scope of transactional lawyers).

<sup>107</sup> See Keith J. Crocker & Sharon Tennyson, *Insurance Fraud and Optimal Claims Settlement Strategies*, 45 *J.L. & Econ.* 469, 469 (2002) (identifying optimality conditions for insurers' underpayments and furnishing empirical proof of systematic underpayments of injury claims arising from car accidents).

claims. This practice is well-documented in academic literature<sup>108</sup> and has given rise to suits filed by the government and consumer protection groups.<sup>109</sup> The New Mexico Supreme Court decision in *Truong v. Allstate Insurance Co.*<sup>110</sup> provides both a recent and a remarkable illustration of those suits.<sup>111</sup> This decision examined Allstate's use of a claim-processing computer software, programmed to undervalue and underpay policyholders' claims below their true value, against the state's prohibition of "[u]nfair or deceptive and unconscionable trade practices."<sup>112</sup> The court rejected Allstate's claim that its software fell under the "market conduct examination" permitted by a supervising agency (the Public Regulation Commission's Superintendent of Insurance). The court reasoned that such permission can only be granted expressly and formally, rather than implicitly, and reinstated the policyholders' class action.<sup>113</sup>

Another good example is Louisiana's *parens patriae* action against Allstate, its provider of statistical, actuarial, and underwriting information, and the manufacturers of computer programs manipulated to reduce the value of policyholders' claims.<sup>114</sup> The

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<sup>108</sup> See Tom Baker, Constructing the Insurance Relationship: Sales Stories, Claims Stories, and Insurance Contract Damages, 72 Tex. L. Rev. 1395, 1430–31 (1994) (arguing on empirical grounds that "insurance companies . . . engage in strategic behavior with claimants" and systematically underpay claims); Leon E. Trakman, David Meets Goliath: Consumers Unite Against Big Business, 25 Seton Hall L. Rev. 617, 623 (1994) ("Insurance companies consistently underpay valid insurance claims to horde the difference between the amount due to each insured and the amount actually paid.").

<sup>109</sup> This form of subsidized litigation is among our proposed solutions of the unrealizability problem. See *infra* Section IV.C.

<sup>110</sup> 227 P.3d 73 (N.M. 2010).

<sup>111</sup> For additional examples, see, e.g., Kelsey D. Dulin, Comment, The Disaster After the Disaster: Insurance Companies' Post-Catastrophe Claims Handling Practices, 61 Okla. L. Rev. 189, 191–92, 196–206 (2008) (explaining and illustrating how insurance companies take advantage of catastrophe victims and underpay claims); see also *Bradshaw v. State Farm Mut. Auto. Ins. Co.*, 758 P.2d 1313, 1322–23 (Ariz. 1988) (admitting into evidence an insurer's statements in settlement negotiations to show that it attempted to strong-arm the policyholder into a cheap settlement).

<sup>112</sup> See N.M. Stat. Ann. § 57-12-3 to -10 (2011) (prohibiting and making actionable "[u]nfair or deceptive trade practices and unconscionable trade practices in the conduct of any trade or commerce").

<sup>113</sup> *Truong*, 227 P.3d at 84–89.

<sup>114</sup> *Louisiana ex rel. Caldwell v. Allstate Ins. Co.*, 536 F.3d 418, 421–22 (5th Cir. 2008).

United States Court of Appeals for the Fifth Circuit categorized this action as an equivalent of a “class” or “mass” action<sup>115</sup> for purposes of the Class Action Fairness Act of 2005.<sup>116</sup> Based on this categorization, the court found “minimal diversity” between Allstate and the individuals represented by Louisiana’s Attorney General<sup>117</sup> and removed the action to federal court pursuant to the Act’s provisions.<sup>118</sup>

These decisions raise both important and interesting questions of law that merit an independent discussion.<sup>119</sup> However, they are discussed here for a different reason. These decisions show how prevalent the insurance companies’ underpayment strategies are and how hard it is for an individual policyholder facing those strategies to stand her ground.<sup>120</sup> Indeed, it is no coincidence that one of those decisions involved a class action and another a *parens patriae* suit. Absent proactive mechanisms that level the playfield between insurance companies and insured,<sup>121</sup> the companies will use their cost advantage to force the insured to forego the vindication of their rights in court and accept instead a cheap out-of-court settlement. The contractual rights of policyholders will consequently become mute.

### *C. Criminal Law*

Asymmetrical litigation costs can foil criminal justice as well. Consider a prosecutor who accuses numerous defendants of unlicensed work as contractors—a misdemeanor punishable by a fine not exceeding \$5000.<sup>122</sup> The prosecutor is one of several attorneys

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<sup>115</sup> Id. at 430.

<sup>116</sup> Pub. L. No. 109-2, 119 Stat. 4 (codified at 28 U.S.C. § 1332(d) (2006)).

<sup>117</sup> *Caldwell*, 536 F.3d at 430.

<sup>118</sup> Id. at 423, 430.

<sup>119</sup> See, e.g., Dwight R. Carswell, Comment, CAFA and Parens Patriae Actions, 78 U. Chi. L. Rev. 345, 353–57 (2011) (discussing the *Caldwell* decision).

<sup>120</sup> See, e.g., David Dietz & Darrell Preston, Home Insurers’ Secret Tactics Cheat Fire Victims, Hike Profits, Bloomberg, Aug. 3, 2007, <http://www.bloomberg.com/apps/news?pid=21070001&sid=aIOpZROwhvNI> (observing that insurance companies systematically underpay claims and providing examples).

<sup>121</sup> We discuss these mechanisms in Part IV below.

<sup>122</sup> See, e.g., Cal. Bus. & Prof. Code § 7028(a), (b) (West 2012) (providing that unlicensed work as a contractor is a misdemeanor punishable upon first conviction “by a fine not exceeding five thousand dollars (\$5,000) or by imprisonment in a county jail not exceeding six months, or by both that fine and imprisonment”).

on the government's payroll who specialize in prosecuting licensing violations. To be able to perform her job properly, the prosecutor had acquired the requisite legal and technical knowledge, which she employs in all cases she handles. The state can, consequently, prosecute contractors suspected of doing unlicensed work at a relatively low cost. For reasons we already explained, the state's cost of prosecuting every additional contractor gets lower relative to the cost of previous prosecutions. Any addition to the prosecutors' caseload spreads their effort across greater numbers of cases. Up to a certain point, it also helps prosecutors acquire experience and improve their efficiency, thus driving the state's costs further down.<sup>123</sup>

These economies of scale are one-sided. The prosecutor, for example, does not have to put much effort into prosecuting a general contractor for doing unlicensed electrical work. She knows from her and her colleagues' experience what electrical work is included in the general contractors' license. The contractor's attorney, on the other hand, will normally have to investigate this issue anew. The attorney will also have to familiarize himself with the relevant statutory and regulatory provisions, some of which are complex and not easy to understand. Consequently, in this and many other criminal cases, the gap between the cost of defense and the cost of prosecution is substantial.

Assume that the state's cost of prosecuting a contractor for doing unlicensed work is \$2000, while the cost of defense is typically \$10,000 per case. The prosecutor offers each defendant to plead guilty and receive a \$3000 fine. Under these circumstances, all defendants, including those who are innocent, will do well to accept the prosecutor's offer.

Why would an innocent defendant accept this offer? The reason is simple: the defendant's conviction and punishment are costly but still cheaper than the defense. Even when the defendant's trial is completely risk-free—so that his acquittal at the end of the trial is guaranteed—he is still better off paying the state a fine of \$3000

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<sup>123</sup> See, e.g., Brandon L. Garrett, *Aggregation in Criminal Law*, 95 *Calif. L. Rev.* 383, 393 (2007) (noting that prosecutors, as repeat players, "can achieve economies of scale . . . by coordinating, channeling and settling cases . . . in the shadow of strict sentencing rules that routinize outcomes").

than paying an attorney a \$10,000 fee.<sup>124</sup> The innocent defendant will consequently choose to accept the plea bargain. Contrary to some scholars' belief,<sup>125</sup> the defendant's gain from the plea bargain does not fully account for this decision. His additional—and, indeed, dominant—reason for accepting the bargain is the prosecutor's cost advantage that lends credibility to her threat to litigate the case.<sup>126</sup> Had the prosecutor's litigation cost been equal to the

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<sup>124</sup> Cf. Gabriel J. Chin & Richard W. Holmes, Jr., Effective Assistance of Counsel and the Consequences of Guilty Pleas, 87 *Cornell L. Rev.* 697, 703 (2002) (“[I]n some cases defendants who might be acquitted after trial plead guilty to relatively minor offenses because the cost of defense exceeds seemingly minimal penalties and consequences.”).

<sup>125</sup> See, e.g., *id.*

<sup>126</sup> Importantly, the defendant in our example cannot obtain legal representation at the state's expense. Because he is not poor, he is not entitled to a state-funded attorney under *Gideon v. Wainwright*, 372 U.S. 335 (1963). More crucially, *Gideon* entitles an indigent defendant to be represented by counsel at the government's expense only when he stands to receive prison sentence upon conviction. Hence, even if our defendant were poor, he would still be ineligible for *Gideon*'s protection as in the event of conviction he will only be fined rather than go to jail. See *Scott v. Illinois*, 440 U.S. 367, 373–74 (1979) (holding that only actual imprisonment prospect makes an indigent defendant eligible for *Gideon* protection). Note that a defendant's eligibility for a state-funded counsel under *Gideon* does not level the playfield. Criminal defense requires expert assistance and testimony in a variety of areas ranging from DNA and forensics to corporate accounting. See Paul C. Giannelli, *Ake v. Oklahoma: The Right to Expert Assistance in a Post-Daubert, Post-DNA World*, 89 *Cornell L. Rev.* 1305, 1307–10 (2004). Under extant doctrine, an indigent defendant can receive expert assistance at the government's expense only upon showing of necessity. See Criminal Justice Act of 1964, 18 U.S.C. § 3006A(e)(1) (2006) (entitling an indigent defendant to government-funded expert assistance when “necessary for adequate representation”); *Medina v. California*, 505 U.S. 437, 444–45 (1992) (interpreting *Ake v. Oklahoma* as “an expansion of earlier due process cases holding that an indigent criminal defendant is entitled to the minimum assistance necessary to assure him ‘a fair opportunity to present his defense’ and ‘to participate meaningfully in [the] judicial proceeding.’” (quoting *Ake v. Oklahoma*, 470 U.S. 68, 76 (1985)); *Ake*, 470 U.S. at 76, 79–85; see also Giannelli, *supra*, at 1336, 1380–81 (attesting that courts use “necessity” and “particularized need” as governing standards and that “[i]t is not clear that these two formulations differ in result.”); David Alan Sklansky, *Hearsay's Last Hurrah*, 2009 *Sup. Ct. Rev.* 1, 7, 75–77 (proposing to expand the Sixth Amendment confrontation right to enable defendants to challenge prosecution's forensic evidence with the help of court-appointed experts); cf. *Commonwealth v. Serge*, 896 A.2d 1170, 1185 (Pa. 2006) (noting, in relation to expensive computer-generated animation that prosecution adduced as evidence of guilt, that defendant's financial inability to acquire computer-generated animation for exculpatory purposes weighs against admissibility).

defendant's, it would be much harder for her to threaten the defendant that she would take the case to court.<sup>127</sup>

Another factor that widens the gap between prosecutors' and defendants' litigation costs is the parties' unequal access to expert assistance. As attested by Professor Paul Giannelli in his comprehensive study of this area, "prosecutors . . . have an overwhelming advantage when compared to defense counsel."<sup>128</sup> Prosecutors can obtain expert assistance in virtually every case from government crime laboratories, both state and federal, and by relying on experts working in coroner and medical examiner offices, as well as federal agencies such as the Drug Enforcement Administration, Food and Drug Administration, Internal Revenue Service, and Bureau of Alcohol, Tobacco and Firearms.<sup>129</sup> The enormous pool of government-employed experts is a perfect combination of scale and scope economies. This pool allows prosecutors to obtain expert assistance both cheaply and easily. Defendants have no free access to this, or a comparable pool, of experts.<sup>130</sup> Consequently, they have to shop for their own experts and pay full market prices for expert services—something that only wealthy defendants can afford.<sup>131</sup>

In our illustration, the prosecutor's cost advantage enabled her to force an innocent defendant into a guilty plea followed by fine. Unscrupulous prosecutors, however, can go much further by abusing their cost advantage. They can put financial pressure on defendants to extort guilty pleas that will lead to a prison sentence. For example, a prosecutor can inflate the indictment by accusing the defendant of multiple crimes that include conspiracy and other inchoate offences.<sup>132</sup> The high cost of defending against multiple ac-

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<sup>127</sup> The defendant's difficulty is compounded by an agency problem. If the prosecutor were to spend her own money on prosecuting the case, she would likely not prosecute the defendant. However, since she is an agent of the state that uses public money under imperfect oversight of her superiors, she can afford prosecuting cases even when doing so is not cost-efficient.

<sup>128</sup> See Giannelli, *supra* note 126, at 1331.

<sup>129</sup> *Id.* at 1327–31.

<sup>130</sup> *Id.* at 1332.

<sup>131</sup> *Id.*

<sup>132</sup> See Russell D. Covey, *Fixed Justice: Reforming Plea Bargaining with Plea-Based Ceilings*, 82 *Tul. L. Rev.* 1237, 1254 (2008) (discussing strategic "horizontal overcharging," the widespread prosecutorial practice of charging defendants with multiple counts of the same or similar offense(s) when a criminal can be properly penalized by

cusations and the credibility of the prosecutor's threat to go to trial may force innocent defendants to plead guilty. To be sure, prosecutors' cost advantage is not the only factor that gives them the upper hand in plea bargain negotiations. Other factors contributing to this imbalance are defendants' aversion to risk and uncertainty,<sup>133</sup> financial constraints,<sup>134</sup> bounded rationality,<sup>135</sup> and prosecutors and defense attorneys' self-seeking motivations.<sup>136</sup> Yet, prosecutors' cost advantage is a key element in their ability to extract guilty pleas from defendants. Unlike other factors that drive plea bargaining, the prosecution's cost advantage may lead to the silencing of entire categories of defendants who are accused of relatively minor violations in the sense that their voices will not be heard in the courtroom and their defense claims will never be given full consideration.

#### IV. POTENTIAL SOLUTIONS

In this Part of the Article, we propose several approaches that can potentially ameliorate the deleterious effect of asymmetrical litigation costs on entitlement. In theory, the solution is quite simple: it is necessary to level the legal playfield. This can be achieved either by raising litigation costs for parties who currently enjoy a cost advantage or by lowering litigation costs for disadvantaged parties.<sup>137</sup> However, this is easier said than done. As is often the case, the devil is in the details<sup>138</sup> and there are no simple prophylactic solutions.

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a single count); see also Frank O. Bowman, III, *Debate: How the Supreme Court Has Mangled American Sentencing Law and How It Might Yet Be Mended*, 77 U. Chi. L. Rev. 367, 464 (2010) (attesting that prosecutors file multiple-count charges to achieve higher sentences).

<sup>133</sup> See generally Uzi Segal & Alex Stein, *Ambiguity Aversion and the Criminal Process*, 81 Notre Dame L. Rev. 1495 (2006) (explaining and illustrating criminal defendants' aversion toward risk and ambiguity).

<sup>134</sup> See Chin & Holmes, *supra* note 124, at 703.

<sup>135</sup> See Stephanos Bibas, *Plea Bargaining Outside the Shadow of Trial*, 117 Harv. L. Rev. 2464, 2496–527 (2004).

<sup>136</sup> *Id.* at 2470–86.

<sup>137</sup> Cf. Alan Wertheimer, *The Equalization of Legal Resources*, 17 Phil. & Pub. Aff. 303, 306–07 (1988) (advocating imposition of limits on parties' ability to litigate as a means for achieving equal distribution of legal resources).

<sup>138</sup> Cf. Margaret H. Lemos, *Special Incentives to Sue*, 95 Minn. L. Rev. 782, 782–83 (2011) (analyzing one-way attorneys' fee shifts and damage multipliers that function

Not every case in which one of the parties enjoys a cost advantage calls for leveling the playfield.<sup>139</sup> In almost all cases, one of the parties has this advantage and the adoption of broad policies that seek to negate it would be both wasteful and futile. The cost of the fix may far outweigh the benefit. What is more, the fact that one of the parties enjoys a cost advantage is not a real concern as long as she does not seek to use it strategically. This can be most easily seen in the context of criminal prosecution. When the government prosecutes a person who clearly committed a crime, making the process more costly for the government only for the sake of leveling the playfield would work to society's detriment without producing any offsetting benefits.

The main challenge, therefore, is to fashion legal mechanisms that are capable of distinguishing strategic litigants from non-strategic ones. In the following paragraphs, we will discuss a num-

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as special incentives to file suits in federal courts and expressing doubts about their efficacy on the ground as judges react negatively to increased caseload).

<sup>139</sup> In appropriate cases, pooling rightsholders into a class action will allow them to realize their entitlements. This pooling, however, is only possible when the rightsholders' suits exhibit commonality. Fed. R. Civ. P. 23(a)(2). Even then, the class attorney's self-seeking conduct (e.g., a collusive settlement with the defendant) might lead to the entitlements' erosion. See generally John C. Coffee, Jr., *Class Action Accountability: Reconciling Exit, Voice, and Loyalty in Representative Litigation*, 100 *Colum. L. Rev.* 370 (2000) (analyzing agency costs in class actions and ways to reduce those costs). Under certain conditions, state attorneys general and federal regulatory agencies may decide to seek legal redress for aggrieved citizens. These conditions typically include commonality of suits and presence of a strong public interest in prosecuting those suits. See Myriam Gilles & Gary Friedman, *After Class: Aggregate Litigation in the Wake of AT&T Mobility v. Concepcion*, 79 *U. Chi. L. Rev.* 623 (2012); Adam S. Zimmerman, *Distributing Justice*, 86 *N.Y.U. L. Rev.* 500, 518–39 (2011). Even then, there will be no alignment between the agencies' and the attorneys' general goals and the interests of the citizens they represent. For a superb analysis of this misalignment and its policy implications, see Margaret H. Lemos, *Aggregate Litigation Goes Public: Representative Suits by State Attorneys General*, 126 *Harv. L. Rev.* (forthcoming 2012) (unpublished manuscript, on file with the Virginia Law Review Association); see also Zimmerman, *supra*, at 541–53 (identifying agencies' limitations as protectors of individual rights). A class action still appears to be an economically superior solution for common question suits. See David Rosenberg & Kathryn E. Spier, *On Structural Bias in the Litigation of Common Question Claims* (June 20, 2012) (unpublished manuscript, available at <http://ssrn.com/abstract=1950196>) (identifying a structural bias in non-unified common question litigation: while each plaintiff invests in the litigation to promote his own case, the defendant spends to defeat all plaintiffs); see also David Rosenberg, *Mandatory-Litigation Class Action: The Only Option for Mass Tort Cases*, 115 *Harv. L. Rev.* 831, 831–33 (2002) (arguing that mandatory class action enhances social welfare).



ber of mechanisms that may be used to accomplish this task. Specifically, we will consider the options of increased court fees, fee-shifting rules, subsidization of disadvantaged litigants, and the intensified use of punitive damages, “bad faith,” “unclean hands” and other equitable doctrines. We will assess these mechanisms’ strengths and weaknesses and will try to rank them on the basis of this assessment.

#### *A. Increasing Court Fees*

The first remedial option we wish to consider is stricter *ex ante* screens that would make it more difficult for strategic litigants to file suits against disadvantaged defendants. The most conventional mechanism that may be employed toward this end is differential court fees that correlate with the number of suits one files. Under this mechanism, court fees will increase progressively with every additional lawsuit filed by a litigant suspected of being strategic. Serial litigants consequently will have to pay an increasingly high fee for each additional suit they file.

Rising court fees will increase litigation costs for serial litigants (both strategic and honest). The fee increments will gradually eliminate the serial litigants’ cost advantage, which, in turn, will take away their ability to threaten potential defendants with suits. Note that strategic plaintiffs’ capacity to extort settlements critically depends on their ability to make a credible threat to sue the defendant. Properly calibrated fee increases will gradually erode the credibility of those threats. Over time, those threats will become non-credible and the litigation playfield will be leveled.

But herein lies the main problem with the proposed mechanism. It takes time for it to take effect. This may appear to be a fairly inconsequential problem at first blush. But, in fact, the opposite is true. The time problem dooms the mechanism. To illustrate, assume that a five percent increase in court fees allows a strategic plaintiff to enjoy her cost advantage in the first ten suits she files, but not thereafter. Under the assumed rate, the plaintiff’s cost advantage disappears at the eleventh suit. Seemingly, after winning ten suits in a row, the plaintiff will no longer be able to destroy her opponents’ entitlements, and the unrealizability problem will fade away.

In fact, it will not. The reason is simple: defendants one through ten will not litigate their cases. No reasonable person will agree to be among the first ten defendants to go to court. Instead, a reasonable person will prefer to settle the case by giving up her entitlement (or part of it). The next defendants will follow suit, thereby completely exempting the plaintiff from the duty to pay court fees. The fee-increase mechanism is therefore unlikely to remedy the problem.

The increased fees solution also raises fairness and efficiency concerns. As we already noted, not all serial litigants are strategic. Some of them are honest rightsholders who suffered multiple infringements of their rights, as is often the case with owners of copyright in musical works. Raising court fees for those litigants up the point of unaffordability would block their access to courts and allow infringers to misappropriate their works. This outcome is neither fair nor efficient.

The increased fees solution is also partial by design. This solution only works with strategic plaintiffs, but not with strategic defendants, as defendants pay no court fees. Moreover, a strategic litigant can often choose between being a plaintiff and being a defendant. Consider a landowner who tries to void her neighbor's right-to-way easement. Instead of filing a suit to void the easement, the landowner can conveniently turn herself into a fee-exempted defendant by destroying and occupying the pathway in question. If this action triggers the neighbor's suit, the landowner will realize her cost-advantage and obliterate the neighbor's entitlement without paying court fees. If the neighbor decides not to sue, the landowner will prevail without a fight.

Finally, the increased-fee mechanism can only work in civil litigation. In the context of criminal prosecutions, this mechanism is inapplicable. Once it becomes effective, it will stop the criminal justice system dead in its tracks, as it will prevent the government from prosecuting offenders.

### *B. Fee Shifting*

Fee shifting is a second option that policymakers may adopt in order to combat strategic litigants. Across the United States, each civil litigant pays her own court costs and attorney's fees. This general principle is widely known as the "American rule." Most other

countries follow the so-called “English rule” that empowers the prevailing party to collect her court costs and attorney’s fees from the losing party. Critics of the American rule claim that it promotes “wasteful litigation expenditures, implausible claims, strike suits, onerous discovery demands, and spurious defenses.”<sup>140</sup> Champions of the American rule respond to this accusation by underscoring access to justice. They argue in this connection that the English rule “deters risk-averse plaintiffs from pursuing meritorious claims, especially against rich defendants who can afford expensive counsel.”<sup>141</sup> Law and Economics scholars who have weighed in on the debate tend to favor the American rule on the ground that it best promotes out-of-court settlements.<sup>142</sup>

But not all settlements are equally desirable from a social perspective.<sup>143</sup> While we do not challenge the conventional wisdom among Law and Economics scholars as to the incentive effect of the American rule on settlements, our analysis casts doubt on the assumption that maximizing the number of out-of-court settlements is necessarily a laudable goal. If our analysis is correct, not all settlements are socially desirable: some settlements, as Bentham

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<sup>140</sup> Bradley L. Smith, Note, Three Attorney Fee-Shifting Rules and Contingency Fees: Their Impact on Settlement Incentives, 90 Mich. L. Rev. 2154, 2154 (1992).

<sup>141</sup> *Id.* at 2155.

<sup>142</sup> See Richard A. Posner, Comment on Donohue, 22 Law & Soc’y Rev. 927, 928 (1988) (claiming that “making the losing party pay the winning party’s attorney’s fees would reduce, not increase, the settlement rate”); Steven Shavell, Suit, Settlement, and Trial: A Theoretical Analysis Under Alternative Methods for the Allocation of Legal Costs, 11 J. Legal Stud. 55, 65–66 (1982) (arguing that there will be fewer settlements under a fee-shifting regime when parties’ expected judgments are the same). But see John J. Donohue III, Opting for the British Rule, or If Posner and Shavell Can’t Remember the Coase Theorem, Who Will?, 104 Harv. L. Rev. 1093 (1991). Full discussion of the “English Rule or American Rule?” debate is beyond the ken of this Article.

<sup>143</sup> See, e.g., Jules Coleman & Charles Silver, Justice in Settlements, 4 Soc. Phil. & Pol’y 102, 114–19 (1986) (arguing that the private and often secret character of settlements deprives society of the valuable information and public goods generated by adjudication); Ben Depoorter, Law in the Shadow of Bargaining: The Feedback Effect of Civil Settlements, 95 Cornell L. Rev. 957, 960 (2010) (demonstrating that some settlements create socially undesirable benchmarks for primary behavior); Owen M. Fiss, Against Settlement, 93 Yale L.J. 1073, 1075–76 (1984) (underscoring distortionary effects of settlements and describing settlement as a “capitulation to the conditions of mass society [that] should be neither encouraged nor praised”).

put it, are “repugnant to justice.”<sup>144</sup> As we have shown, out-of-court settlements lead to the effacement of entitlements in certain contexts. After all, it is precisely the ability of parties with a cost advantage to craft settlements in a way that induces their adversaries to forego trial that causes the problem. Hence, the English rule may be desirable in the present context.

Forcing the losing party to pay the winner her court expenses and attorney’s fees has the same effect as increasing court fees: it raises total litigation costs for strategic litigants. The two remedial mechanisms, however, differ from each other in four important respects. First, unlike the increased court fees that acquire their remedial power over time, the English rule takes effect immediately as of the very first case. The English rule thus avoids the main shortcoming of the increased court fees solution. Second, while under the increased court fees regime the money goes to the courts system, the English fee-shifting rule channels the money to successful defendants. This difference increases the incentive of potential defendants to defend their entitlements in court. Third, a fee-shifting mechanism is a more precise measure than increased court fees, as it reimburses defendants for their actual—or under most legal systems, reasonable—expenses. Lastly, the increased court-fees mechanism, as we already noted, can only affect the strategic filing of suits. The fee-shifting mechanism is universal: its adoption will affect not only plaintiffs in civil cases, but also defendants and criminal prosecutors. For all these reasons, the English rule clearly outperforms increased court fees as a mechanism for combating strategic lawsuits.

That said, the English rule is not a foolproof solution. This rule works best when the plaintiff’s case is completely without merit. When the plaintiff has absolutely no chance of winning the case, adoption of the English rule will take away the plaintiff’s ability to utilize her cost advantage as a means for extorting a favorable set-

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<sup>144</sup> See Jeremy Bentham, *Scotch Reform; Considered, with Reference to the Plan, Proposed in the Late Parliament, for the Regulation of the Courts, and the Administration of Justice, in Scotland* 75–76 (London, R. Taylor & Co. 1808) (describing settlements as “repugnant to” and a “denial of” justice); see also Amalia D. Kessler, *Deciding Against Conciliation: The Nineteenth-Century Rejection of a European Transplant and the Rise of a Distinctively American Ideal of Adversarial Adjudication*, 10 *Theoretical Inquiries L.* 423, 438–41 (2009) (laying out an insightful historical account of Bentham’s opposition to settlements).

tlement from the defendant—at least when the defendant also evaluates the plaintiff’s probability of winning the case at zero. Under this scenario, it does not matter how significant the plaintiff’s cost advantage is since the defendant knows that at the end of the process she will be fully reimbursed for her expenses. And the plaintiff knows it too. The English rule thus takes away the plaintiff’s threat point.

The analysis changes, however, when a strategic plaintiff’s chance of winning the case is not zero, but rather a small positive, say, thirty percent. In any such case, a strategic plaintiff will still be able to utilize her cost advantage to extract favorable out-of-court settlements from defendants. Naturally, the pool of potential targets will be smaller and the plaintiff’s settlement gains will correspondingly shrink. Yet, with respect to certain defendants who must pay a steep price for legal representation, the cost advantage will be substantial enough to extort ransom payments.<sup>145</sup>

Importantly, we do not argue that the English rule should be applied across the board simply because it does a better job of deterring strategic litigation that threatens to erode entitlements. The position we take is far less ambitious. What we did in this Section is to identify a previously-unnoticed factor that weighs in favor of the

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<sup>145</sup> Allowing defendants to file early motions to dismiss the suit and requiring courts to decide those motions promptly may provide a partial solution to this problem. This approach is followed by the Anti-SLAPP (Strategic Lawsuit Against Public Participation) statutes, enacted by numerous states to protect citizens who petition the government against suits aiming to suppress their petitioning activities. Anti-SLAPP statutes allow aggrieved citizens to file an early motion to dismiss the suit. This motion will be granted and the plaintiff will be obligated to pay the citizen’s legal fees if the court finds that the plaintiff sued the citizen because of her potentially meritorious petition to the government. See Paul D. Wilson & Noah C. Shaw, *Robber Barons, Back-Stabbers and Extortionists: How Far Does Anti-SLAPP Protection Go?*, 43 *Urb. Law.* 745, 745 (2011). Notably, courts recognize the cost advantage of SLAPP plaintiffs as one of the main reasons for granting early dismissal and cost-shifting remedies. See, e.g., *United States ex rel. Newsham v. Lockheed Missiles & Space Co.*, 190 F.3d 963, 970–71 (9th Cir. 1999) (“The hallmark of a SLAPP suit is that it lacks merit, and is brought with the goals of obtaining an economic advantage over a citizen party by increasing the cost of litigation to the point that the citizen party’s case will be weakened or abandoned, and of deterring future litigation.” (citing *Wilcox v. Superior Court*, 33 Cal. Rptr. 2d 446, 450 (Ct. App. 1994))); see also *Liberty Synergistics, Inc. v. Microflo Ltd.*, No. CV 11-0523, 2011 WL 4974832, at \*10 (E.D.N.Y. Oct. 26, 2011) (acknowledging that “California has an interest in protecting its citizens from malicious [SLAPP], even when the only damage they suffer is the costs of litigating the underlying lawsuit”).

English rule. This factor may not be weighty enough to warrant the English rule's adoption in *all* cases, but it certainly supports the rule's application under appropriate circumstances that courts can determine on a case-by-case basis. We therefore recommend that courts be given a broad discretion to apply the English rule to lawsuits that have little merit and were brought by plaintiffs with an inherent cost advantage over the defendant.

### *C. Subsidization*

The first two solutions we discussed are analogous to a tax: their goal is to increase litigation costs for strategic litigants. Another way to level the playfield is subsidization. Specifically, lawmakers may lower litigation costs for strategic litigants' targets by subsidizing the latter's litigation efforts. This result can be achieved either directly or indirectly. Direct subsidization consists of giving money to the litigants themselves. Indirect subsidization involves setting up legal aid organizations to represent the targets of strategic litigants.

Real world examples of direct subsidization are hard to find. In fact, we are not aware of any. The reason is straightforward. Direct subsidization presents a formidable challenge for the state in two respects. First, subsidizing all litigants is both impractical and inefficient. Any mechanism of direct subsidization will consequently require the state to set up a screening mechanism for identifying litigants who are eligible for subsidization. The cost of operating such a mechanism will likely be enormous, which calls into question the cost-effectiveness of the entire enterprise. Second, and equally important, a system of direct subsidization will create an acute moral hazard problem.<sup>146</sup> Litigants who know that their legal bills would be paid by the state—in part or in full—will invest excessively in legal representation. Ex ante screening, careful though it may be, will not eliminate this problem since it is impossible to estimate upfront the precise cost of legal processes.

In light of the inherent problems with direct subsidization, it is not surprising that most jurisdictions prefer the indirect subsidiza-

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<sup>146</sup> See generally Steven Shavell, *The Fundamental Divergence Between the Private and the Social Motive to Use the Legal System*, 26 *J. Legal Stud.* 575 (1997) (discussing misalignments between private and social incentives in litigation).

tion route. Instead of channeling public money directly to litigants, states by and large prefer to institute public agencies that represent eligible litigants. The most common agency of this sort is the public defender's office that provides legal representation to criminal defendants who cannot afford an attorney.<sup>147</sup>

The state may also set up legal aid agencies to help civil litigants. Importantly, numerous private organizations help litigants in civil cases. These organizations include the Legal Services Corporation, National Consumer Law Center, Electronic Frontier Foundation, law school clinics, and many other institutions and centers (including law firms providing pro bono services). Legal aid organizations—both private and public—screen out applicants and determine their appropriate level of involvement in each individual case. By doing so, they solve most of the problems that arise in the context of direct subsidization.

Alas, the current demand for services offered by legal aid organizations far exceeds supply. The state can bridge the gap between supply and demand by setting up additional legal aid agencies or by funneling more taxpayers' money into existing ones. However, provision of the optimal amount of legal aid is a tricky task for the state. First, the state will be hard-pressed to determine the aggregate demand for legal aid as well as the particular areas of need. This challenge will be compounded by the fact that any attempt at estimating the overall demand for legal services must factor in the price (or co-pay) at which they will be offered. For example, if legal aid were to be given for free, there will be much greater demand for it than if it were offered for a price. Second, the state will have to supervise the quality of the services provided by legal aid institutions. As the number of institutions and employees grows, the task will become more complex. Third, and finally, the level of funding for legal aid is a function of political priorities. In the current economic environment, it would be difficult to convince politicians to commit considerable amounts of money to litigation subsidies. Any fair-minded person would agree that there are far more pressing needs at this time.

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<sup>147</sup> See generally Barbara Allen Babcock, *Inventing the Public Defender*, 43 *Am. Crim. L. Rev.* 1267 (2006) (describing the history and the role of public defenders' offices across the United States).

*D. Equitable Measures and Punitive Damages*

Another possible approach to the challenge posed by strategic litigants involves the use of various equitable doctrines, such as bad faith, misuse, and unclean hands. Equity constitutes a rich depository of various flexible doctrines that enabled judges to achieve just results in individual cases. Indeed, as Professor Henry Smith recently put it, the point and purpose of the law of equity was to combat opportunism.<sup>148</sup> Strategic litigation falls squarely in this category. As we explained, strategic litigants take advantage of differential cost structures to extort unmeritorious payments from entitlement holders. This dynamic leads to results that are neither socially efficient nor equitable.

While the previous measures we discussed focus either on the litigants themselves or on their representatives (legal aid organizations), the current solution puts the premium on the courts—more precisely, on the courts *and* the legislature. We propose that courts be given broad discretion to rule in appropriate cases that litigants have acted in bad faith or misused their legal rights. In addition, courts will be empowered to order strategic litigants to pay their victims not just court and attorney's fees, but also punitive damages.<sup>149</sup> We submit that courts should be able to exercise this power not only against private actors, but also against state and federal prosecutors and other governmental agents.

Giving judges broad discretion to counter strategic litigation with punitive damages will not only deter strategic litigants, but will also motivate the innocent party to take her case to court. The introduction of punitive damages will radically reshape the payoff structure faced by innocent entitlements' holders. Currently, they have no financial incentive to go to court. For the reasons we explained, from a pure financial standpoint, settling the case out-of-court always dominates litigation. However, once the possibility of

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<sup>148</sup> Henry E. Smith, *An Economic Analysis of Law Versus Equity* 17 (Oct. 22, 2010) (unpublished manuscript, available at [http://www.law.yale.edu/documents/pdf/LEO/HSmith\\_LawVersusEquity7.pdf](http://www.law.yale.edu/documents/pdf/LEO/HSmith_LawVersusEquity7.pdf)); see also Mark P. Gergen, John M. Golden & Henry E. Smith, *The Supreme Court's Accidental Revolution? The Test for Permanent Injunctions*, 112 *Colum. L. Rev.* 203, 242–49 (2012) (stating and illustrating equity's rule in counteracting opportunistic behavior).

<sup>149</sup> For the goals and mechanics of punitive damages, see Dan Markel, *How Should Punitive Damages Work?*, 157 *U. Pa. L. Rev.* 1383 (2009).



collecting punitive damages is introduced, it will make sense for many innocent litigants to defend their entitlements in court.

This measure should be applied with caution because an increase in the level of compensation normally triggers a parallel increase in the litigation's costs. As the stakes get higher, the parties' motivation to invest in litigation increases as well. Oftentimes, however, the parties' combined investment in litigation will fail to produce a matching social benefit. As Professors Mitchell Polinsky and Steven Shavell have recently demonstrated, the marginal improvement in deterrence (and other social benefits) brought about by increased compensation may fall way short of the increase in the parties' litigation costs.<sup>150</sup> For that reason, courts should be sure to award punitive damages only in special cases. As Polinsky and Shavell have argued in their earlier work, these special cases include ones in which under-enforcement of the law creates a shortfall in deterrence.<sup>151</sup> Punitive damages can reduce, or even eliminate, this shortfall at a low social cost.<sup>152</sup> By the same token, punitive damages can also efficiently minimize the strategic abuse of rights when their use is limited to this goal.<sup>153</sup>

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<sup>150</sup> See A. Mitchell Polinsky & Steven Shavell, *Costly Litigation and Optimal Damages* (Jan. 24, 2012) (unpublished manuscript, available at <http://ssrn.com/abstract=1990786>). Tort litigation that consumes \$46 billion per year in litigation costs, *id.* at 2, vividly illustrates this point. Empirical evidence shows that for every dollar retained by the victim, the parties collectively expend one dollar on the litigation process. *Id.* Assume that litigation costs vary in proportion to damages and grant, for simplicity's sake, that plaintiffs and defendants expend on the litigation the same amount,  $\lambda d$ , that represents the relevant fraction ( $\lambda$ ) of the plaintiff's damage ( $d$ ). Because the parties' joint litigation expenditure,  $2\lambda d$ , equals the plaintiff's net recovery amount,  $(1-\lambda)d$ , then  $\lambda=1/3$ . Hence, for every dollar retained by the plaintiff, the parties collectively expend on the litigation 67 cents ( $2/3$ ). *Id.* at 10 & n.7. If so, every dollar that the torts system awards the victim must generate at least 67 cents in the marginal gain in deterrence. With every additional dollar that the system moves from defendants to plaintiffs, this condition becomes increasingly difficult to satisfy. *Id.*

<sup>151</sup> A. Mitchell Polinsky & Steven Shavell, *Punitive Damages: An Economic Analysis*, 111 *Harv. L. Rev.* 869, 896–97 (1998) (arguing that courts should take defendants' probability of escaping liability into account when calculating punitive damages).

<sup>152</sup> *Id.*

<sup>153</sup> *Cf.* *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 416–18, 425 (2003) (voiding on due process grounds award of \$145 million in punitive damages as an addition to \$1 million in compensatory damages against an insurance company that used strategic litigation to put unfair pressure on the insured, while indicating that a single-digit ratio between punitive and compensatory damages will pass constitutional muster).

Unlike the introduction of litigation subsidies, authorizing courts to award punitive damages is politically tenable. The concern that courts will award excessive punitive damages is not strong enough to block the introduction of this measure. This concern can only provide a reason for capping the amounts that courts will be authorized to award in punitive damages.<sup>154</sup>

That said, some might still criticize our proposal on the ground that it will lead to inconsistent court decisions. Some courts will routinely order strategic litigants to pay punitive damages, while others will not. Worse yet, some courts may overuse their power to penalize non-strategic litigants. We will deal with these objections in reverse order.

We believe that the second concern is greatly exaggerated. We are not aware of any empirical basis for raising it. In fact, we actually believe that courts will tend to be reluctant to rule that parties acted in bad faith and subject them to punitive damages. In an adversarial system, judges are generally predisposed to exercise restraint and hence are likely to use discretionary powers sparingly.

As for the first concern, while we agree that consistent application of the law is desirable, we do not share the view that fear of inconsistency should bar the introduction of discretionary powers. The issue at hand provides a useful illustration. Opportunism presents a challenge to lawmakers because it is largely impervious to broad generalizations and calls for the crafting of policies that rely on ad hoc determinations. Strategic litigation shares this characteristic. Judges are best positioned to identify opportunistic litigants. Their knowledge of the law and experience on the job enables them to detect opportunism. No other institution is equally qualified to perform this task. Any legal doctrine that relies on case-by-case application will inevitably engender inconsistencies. But is there a viable alternative that will guarantee uniformity in the

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<sup>154</sup> The Supreme Court has imposed constitutional limitations on state courts' power to award punitive damages. See *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559 (1996). Specifically, the Court ruled that the Due Process Clause of the Fourteenth Amendment prohibits the imposition of punitive damages that are grossly excessive or arbitrary. *Id.* at 585–86. The Court explained that the amount of punitive damages must reflect the reprehensibility of the defendant's conduct. *Id.* at 575. The Court also set up a "single-digit ratio" benchmark for punitive damages: it held that due process normally prohibits any award of punitive damages that exceeds the plaintiff's compensatory damage award by ten times or more. *Id.* at 581–83.

courts' applications of legal rules without giving opportunism free reign and accepting the inequities it brings about? We believe there is no such alternative. Inconsistent application of the law is a small price to pay in order to preserve the integrity of legal entitlements.

At the end of the day, we posit that giving courts broader discretion and equipping them with the right doctrinal and remedial tools will go a long way toward remedying the problem of erosion of entitlements via strategic litigation. Admittedly, the judicial mechanism we propose is imperfect, but its virtues clearly outweigh its vices. Furthermore, based on our analysis, this mechanism outperforms all the other solutions we considered. Finally, it is the only solution that may be acceptable to judges, politicians, and the bar.

#### CONCLUSION

Theodore Roosevelt famously captured the fundamental tenet of our free society by saying that “[n]o man is above the law and no man is below it . . . .”<sup>155</sup> By making rights relationally contingent, asymmetrical litigation costs call into question our ability to attain this ideal. As we showed, a party who enjoys a cost advantage in litigation can effectively prevent her opponent from realizing her entitlement. When litigation costs favor one *category* of litigants over another, as we proved to be the case in multiple legal areas, it will gradually lead to erosion of entitlements. Existing accounts of legal rights largely overlooked the fact that entitlements are not self-enforcing. To actualize them in the real world, their holders must be able to enforce them cost-effectively. When this condition is not met, entitlements become dead letter of the law: they exist in theory, but not in practice. As a result, they may be ignored, taken, or compromised by strategic parties. The surrender of entitlements without legal battle impairs the legal equilibrium contemplated by policymakers. Our goal in this Article was to draw attention to the effect of asymmetrical litigation costs on legal entitlements. We also proposed several institutional responses to this problem. We

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<sup>155</sup> Theodore Roosevelt, President's Message at the Opening of the Second Session of the Fifty-Eight [sic] Congress, Dec. 7, 1903, *in* 1 *The Roosevelt Policy: Speeches, Letters and State Papers, Relating to Corporate Wealth and Closely Allied Topics* 191, 196 (William Griffith ed., 1919).

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believe that of the various institutions that can effectively remedy the problem, courts are best suited for the task. Endowing courts with broad equitable discretion to penalize strategic litigants will go a long way toward alleviating the problem.