Multiple Defendant Settlement in 10b-5: Good Faith Contribution Bar

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By

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Securities and Exchange Commission ("SEC") Rule 10b-5\(^1\) provides the dominant private remedy for securities fraud.\(^2\) Private actions under 10b-5 commonly involve multiple defendants who may be jointly and severally liable.\(^3\) In these situations, less culpable defendants generally possess a right to contribution from more culpable ones.\(^4\) If all the parties litigate the matter to a judgment, there are few problems in determining contribution rights among the defendants—standard rules of contribution will apply.\(^5\)

When one or more of the defendants settle with the plaintiff, however, problems arise in determining how the settlement affects the judgment and how to apportion the judgment among the remaining

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1. 17 C.F.R. § 240 10b-5 (1988). It provides:
Employment of Manipulative and Deceptive Devices
   It shall be unlawful for any person, directly or indirectly, by the use of any
means or instrumentality of interstate commerce, or of the mails, or of any facility of
any national securities exchange,
   (a) To employ any device, scheme, or artifice to defraud,
   (b) To make any untrue statement of a material fact or to omit to state a mate-
rial fact necessary in order to make the statements made, in the light of the circum-
stances under which they were made, not misleading, or
   (c) To engage in any act, practice, or course of business which operates or
would operate as a fraud or deceit upon any person, in connection with the purchase
or sale of any security. *Id.*


[1253]
defendants. In negotiating settlements, the parties need to know how a proposed settlement will affect the rights and duties of the nonsettling parties. Settling plaintiffs want to know the extent to which a settlement will decrease an eventual judgment. Settling defendants want a final determination of their liability. Nonsettling defendants need assurance that their liability is not disproportionate to their culpability. Finally, society has an interest in the fair and speedy disposition of potentially complex litigation.

Courts have expressed incongruent views on how settlements affect contribution rights. Although the issue remains unresolved, one may detect a trend in recent court decisions that settlement extinguishes the contribution rights of the remaining defendants against the settling defendant. If a partial settlement bars contribution claims by nonsettling defendants, it is necessary to determine how the settlement bar will affect the ultimate judgment.

This Note explores the issues surrounding settlements in 10b-5 actions, advocates that under certain conditions partial settlements should bar contribution and proposes a solution to the potential problems created by barring contribution. Section I briefly examines the development of the private cause of action and the right of contribution under Rule 10b-5. Section II elaborates on the circumstances that should bar contribution and describes an equitable standard for approving such settlements. Section III analyzes various methods of apportioning judgments among the defendants remaining after an approved settlement. This section proposes a solution to the settlement bar problem that is consistent with the goals of the federal securities laws. The Note concludes that settlements made in good faith should bar contribution claims and that the nonsettling defendants' liability should be reduced by the greater of either the settlement amount, or the settling defendant's financial culpa-

6. Otherwise, a defendant has little incentive to settle. If a defendant's settlement with the plaintiff does not sever liability to the nonsettling defendants, the settling defendant remains potentially liable for the entire judgment by virtue of a cross-claim for contribution. Therefore, because the settling defendant's potential liability vis-a-vis the ultimate judgment remains unchanged, there is little incentive to settle with the plaintiff.

7. See infra notes 45-48 and accompanying text.


9. The term "settlement bar" is used here to identify the situation in which a "settlement prevents nonsettling defendants from getting contribution from settling ones." Donovan v. Robbins, 752 F.2d 1170, 1180 (7th Cir. 1984).

10. "[T]he goal of the [federal] securities laws is . . . to compensate persons who have been defrauded [and] to deter violations of those laws." Tucker v. Arthur Andersen & Co., 646 F.2d 721, 727 n.7 (2d Cir. 1981).
bility. This approach ensures the fairness of 10b-5 settlements, and protects the interests of the parties.

I. Development of the Private Cause of Action and Contribution Under Rule 10b-5

To fully analyze settlement issues in the context of 10b-5 actions, the judicial origins of the 10b-5 private right of action and the history of contribution in 10b-5 suits should be considered. Although well-accepted today, a private citizen’s remedy under Rule 10b-5, was not always as assured; rather, the 10b-5 private cause of action is the result of judicial implication. This section briefly examines the origins of the private cause of action under Rule 10b-5 and the ramifications of these judicial beginnings.

A. The Private Cause of Action

Section 10(b) of the Securities Exchange Act of 1934 provides that it is unlawful “[t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [Securities and Exchange] Commission may prescribe.”11 Section 10(b) of the Act also grants rulemaking power to the SEC, which the agency used to fashion the broad anti-fraud prohibitions in Rule 10b-5.12

Unlike sections 9(e)13 and 18(a)14 of the Act, Rule 10b-5 does not expressly provide a private remedy.15 In 1946, however, a federal district court in Pennsylvania found an “implicit” private cause of action under Rule 10b-5 by applying tort analysis to the violation of the statute.16

12. See supra note 1 for the text of Rule 10b-5.
13. 15 U.S.C.A. § 78i(e) (West 1981) (providing a private cause of action against one who has engaged in market manipulation of securities subject to the 1934 Act’s registration and reporting mechanisms). See generally T. HAZEN, supra note 2, § 12.1 (discussing market manipulation and deceptive practices under sections 9, 10, 14(e), and 15(c) of the 1934 Act).
14. 15 U.S.C.A. § 78r(a) (West 1981) (providing a private cause of action for investors who have detrimentally relied on materially misleading statements or omissions of material facts in documents filed with the Securities and Exchange Commission). See generally T. HAZEN, supra note 2, § 12.8 (discussing section 18(a) of the 1934 Act).
16. Kardon v. National Gypsum Co., 69 F. Supp. 512 (E.D. Pa. 1946). The court stated: “The violation of a legislative enactment by doing a prohibited act, or by failing to do a required act, makes the actor liable for an invasion of an interest of another if; (a) the intent of the enactment is exclusively or in part to protect an interest of the other as an individual; and (b) the interest invaded is one which the enactment is intended to protect.” Id. at 513 (quoting the RESTATEMENT OF TORTS § 286 (1934)).
Twenty-five years later, the Supreme Court expressly adopted this view.\textsuperscript{17}

A private remedy for 10b-5 violations offers a valuable tool for injured investors.\textsuperscript{18} First, it is easy to establish federal jurisdiction; for example, it can attach from the mere use of a telephone in any part of a securities transaction.\textsuperscript{19} Thus, an injured investor almost always will be able to seek a remedy in federal court. Second, through pendent jurisdiction,\textsuperscript{20} a 10b-5 plaintiff may join related state claims to the 10b-5 claim and bring them in federal court.\textsuperscript{21} Finally, Rule 10b-5 provides a cause of action in many cases in which the common law offers no remedy, such as material corporate misstatements or nondisclosures,\textsuperscript{22} insider trading,\textsuperscript{23} and corporate mismanagement involving transactions in securities.\textsuperscript{24}

Having implied a private cause of action under 10b-5, courts have had to develop federal common law to deal with issues ordinarily provided for by statute.\textsuperscript{25} These issues include the question of what consti-

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\item\textsuperscript{17} Superintendent of Ins. v. Bankers Life & Casualty Co., 404 U.S. 6, 13 n.9 (1971).
\item\textsuperscript{18} See T. HAZEN, supra note 2, at 449 (discussing the importance of a private action under 10b-5).
\item\textsuperscript{19} E.g., Loveridge v. Dreagoux, 678 F.2d 870, 874 (10th Cir. 1982) ("proof of intra state telephonic messages in connection with the employment of deceptive devices or contrivances is sufficient to confer jurisdiction in a § 10(b) and Rule 10b-5 action"); Kerbs v. Fall River Indus., 502 F.2d 731, 737 (10th Cir. 1974) ("It is not required ... that the manipulative or deceptive ... be a part of or actually transmitted in the mails or instrumentality of interstate commerce; it is sufficient that such device or contrivance be employed \textit{in connection with the use of instruments of interstate commerce or the mails.}") (emphasis in the original).
\item\textsuperscript{20} United Mine Workers of Am. v. Gibbs, 383 U.S. 715, 725 (1966) (quoting U.S. Const. art. III, § 2) ("Pendent jurisdiction ... exists whenever there is a claim 'arising under [the] Constitution, the Laws of the United States, and Treaties ...' and the relationship between that claim and the state claim permits the conclusion that the entire action before the court comprises but one constitutional 'case.'").
\item\textsuperscript{23} The idea that insider trading might violate rule 10b-5 was expressed in \textit{In re Cady Roberts & Co.}, 40 S.E.C. 907 (1961). This doctrine was first applied in SEC v. Texas Gulf Sulphur Corp., 401 F.2d 833 (2d Cir. 1968). See also Wang, \textit{Trading on Material Nonpublic Information on Impersonal Stock Markets: Who is Harmed, and Who Can Sue Whom Under SEC Rule 10b-5?}, 54 S. CAL. L. REV. 1217 (1981) (analyzing the application of Rule 10b-5 to insider trading on the basis of nonpublic information).
\item\textsuperscript{24} See, e.g., Superintendent of Ins. v. Bankers Life & Casualty Co., 404 U.S. 6, 12-13 (1971) (Rule 10b-5 is violated when there is deception touching the purchase or sale of a security even if the acts complained of amount to no more than corporate mismanagement).
\item\textsuperscript{25} It has been argued that Congress should enact procedures to fill gaps created by the private cause of action under 10b-5. See, e.g., Adamski, supra note 8, at 572 ("A more satisfactory solution to the problem of contribution and settlement under the securities laws would be
tutes a "material fact" under 10b-5, whether the plaintiff must prove reliance on the misstatement or omission, how to measure damages, and which statute of limitations to apply. Thus, judicial recognition of a private cause of action under 10b-5 represents both a useful means of administering justice and a source of unanswered questions. As the next section describes, the absence of legislative guidance in the area of contribution in 10b-5 situations has been particularly troublesome.

B. Contribution Under Rule 10b-5

The doctrine of contribution provides a positive effect by ensuring fairness to named defendants and a deterrent effect by placing unnamed defendants at risk of being joined in the litigation. Contribution causes problems, however, in settlements of multiple defendant 10b-5 actions. This section examines the doctrine of contribution, its effect on settling multiple defendant suits, and judicial approaches to the problems caused by contribution and settlement in 10b-5 actions.

(1) Contribution in General

Under the equitable doctrine of contribution "a person who discharges a liability shared with another should not bear the sole burden of payment." The doctrine allows defendants to require other tortfeasors, even those not named by the plaintiff, to bear their fair portion of the plaintiff's damage award.

Historically, intentional joint tortfeasors were not able to seek contribution from one another. Recent court decisions, however, have al-federal legislation.


28. Id. § 13.7 (discussing the measurement of damages in private 10b-5 actions).

29. Id. § 13.8 (selection of statute of limitations in private 10b-5 actions).


32. See RESTATEMENT (SECOND) OF TORTS § 886A(3) (1977) ("There is no right of contribution in favor of any tortfeasor who has intentionally caused the harm."). The intentional tort analogy is appropriate in private 10b-5 actions. The U.S. Supreme Court in Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976), required that the defendant act with "intentional or willful conduct."
owed contribution in this context. These decisions are particularly relevant in the 10b-5 area, since securities fraud, unlike negligent torts, involves intentional wrongdoing. As one court has commented on this new development:

[This] trend... has been motivated primarily by two policy objectives: fairness to defendants and deterrence. First, and probably most importantly, contribution achieves a more fair and equal distribution of justice by spreading plaintiffs' losses proportionally among all wrongdoers. Otherwise, under the traditional common law rule, plaintiffs could unilaterally force one of many wrongdoers to bear the entire loss, even though others may be equally or more to blame. Second, contribution ensures that the deterrent effect of the law will be felt by all persons contemplating liability, rather than just those persons most likely to be named as defendants by the plaintiffs.

Although there is no express provision for contribution included in section 10(b) of the Securities Exchange Act, a right to contribution has been implied by the courts. Significantly, the same sections of the 1934 Act that created express private causes of action also provide for a statutory right of contribution among persons liable. The first court to examine the problem of contribution in 10b-5 actions noted the express statutory provisions for contribution under 9(e) and 18(b) of the Act and reasoned that because "the specific liability provisions of the Act provide for contribution, it appears that contribution should be permitted when liability is implied under Section 10(b)." Subsequent decisions have followed this rationale. Moreover, as another court has noted, the implied

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33. Globus Inc. v. Law Research Serv. Inc., 318 F. Supp. 955, 957 (S.D.N.Y. 1970) ("[T]he general drift of the law today is toward the allowance of contribution among joint tortfeasors."). See also Heizer Corp. v. Ross, 601 F.2d 330, 334 (7th Cir. 1979) (contribution is available in securities cases); Nelson, 662 F. Supp. at 1328 (defendants have implied rights of contribution under the federal securities laws). See generally Brodsky & Adamski, Corp. Officers & Dir. § 12:32 (1984) (examining contribution under § 10(b)).

34. Nelson, 662 F. Supp. at 1328 (citations omitted).

35. 15 U.S.C.A. §§ 78i(e), 78r(b) (West 1981).


contribution right serves the twin purposes of the securities laws: fairness to defendants and deterrence of violations. 38

(2) Effect of Contribution on Settlement of 10b-5 Claims

There are several reasons why settlement is desirable in private 10b-5 actions. Partial settlements in multiple defendant actions can promote judicial economy by creating pressure on the remaining defendants to settle also. In addition, settlements may allow immediate compensation for plaintiffs. Settlements may also benefit the settling parties by permitting them to drop out of the lawsuit and devote their time and money to other matters. 40

Allowing contribution claims may hinder settlement. In Nelson v. Bennett the court observed:

[Even if an individual defendant is willing to settle with plaintiffs, that defendant would nevertheless remain subject to liability on the cross-claims for contribution asserted by the non-settling defendants. In other words, a settling defendant does not reduce its financial exposure by entering into a partial settlement with plaintiffs and, therefore, has little incentive to do so. 41

If partial settlement does not extinguish the nonsettling defendant's rights to contribution from the settling defendant, defendants will have little reason to settle. 42 In fact, if a settling defendant must continue to protect his position against contribution claims from nonsettling defendants, there may be a significant disincentive to settlement. 43

Consequently, barring contribution claims should encourage settlements. Under such a system, a partial settlement would "bar the nonsettling defendants from asserting cross-claims for contribution against the settling defendant. A defendant contemplating settlement with plaintiff

39. The term "partial settlement" is used here to indicate the situation when, in a multiple defendant action, there is a settlement with the plaintiff by fewer than all of the defendants.
40. Adamski, supra note 8, at 543.
41. Nelson, 662 F. Supp. at 1328-29. The court also stated, "While financial exposure can, of course, be terminated by a full settlement between plaintiffs and all defendants, as a practical matter a single, comprehensive settlement agreement is exceedingly difficult to orchestrate in complex actions." Id. at 1329.
43. E.g., McLean v. Alexander, 449 F. Supp. 1251, 1266 (D. Del. 1978), rev'd on other grounds, 599 F.2d 1190 (3d Cir. 1979); Sabre Shipping Corp. v. American President Lines, Ltd., 298 F. Supp. 1339, 1346 (S.D.N.Y. 1969) ("No defendant would settle with [a plaintiff] if he was to find himself back in the suit as a third party defendant."); see also In re Corrugated Container Antitrust Litig., 84 F.R.D. 40, 41 (S.D. Tex.) aff'd per curiam, 606 F.2d 319 (5th Cir. 1979) (stating that in settling antitrust claims, "[d]efendants have little incentive to buy peace from plaintiffs if they may be obligated to litigate the same claim against other defendants.").
is thereby granted assurance that . . . it may fully 'buy its peace' through such a settlement."\textsuperscript{44}

Several courts have considered barring contribution claims against settling defendants in private 10b-5 actions. These courts disagree, however, as to the circumstances that justify imposing such a bar.\textsuperscript{45} Case law suggests that courts will allow a partial settlement to bar contribution, subject to certain conditions.\textsuperscript{46} The courts have not, however, clearly set out their preferred criteria for this determination. As one court has recognized, "the caselaw does not forge a clear path to follow, but merely provides a variety of alternatives."\textsuperscript{47} The following section examines the conditions under which courts are willing to bar contribution and the resulting effect on settlement.

II. Barring Contribution Claims After Partial Settlement in 10b-5 Actions

Since barring contribution claims is likely to promote settlements and the benefits derived from them, it is useful to examine the means by which this goal can be achieved. Primarily, this analysis requires examination of state settlement bar statutes and their application in 10b-5 actions.

\textsuperscript{44} Nelson, 662 F. Supp. at 1329.
\textsuperscript{45} The courts have advanced the following views:


(3) Partial settlement might bar contribution when settlement represents a "proper share of damages." Laventhal, Krekstein, Horwath & Horwath v. Horwitch, 637 F.2d 672, 675 (9th Cir. 1980); see also In re Nucorp Energy Sec. Litig., 661 F. Supp. 1403, 1408 (S.D. Cal. 1987) (non-settling defendants' rights of contribution are barred "so long as the settlement represents the settling defendant's 'fair' or 'proper' share of the damages sought"). This vague language has caused problems because the court provided no guidance regarding what is meant by "fair" or "proper." Indeed, the central question is how to encourage settlement while ensuring equity.

(4) Partial settlement should bar contribution as prescribed by a new principle of federal common law announced by court. Nelson, 662 F. Supp. at 1338-39. The Nelson court, recognizing the anomalous results that would occur without a uniform federal standard, took it on themselves to proclaim what that standard would be.

\textsuperscript{46} Harrison v. Sheats, 608 F. Supp. 502 (E.D. Cal. 1985), in which the court refused to bar contribution, appears to be an anomaly. First, subsequent cases in the district have held that, under the right circumstances, partial settlement will bar contribution. See, e.g., Nelson, 662 F. Supp. at 1338. Second, the Harrison court merely considered that Congress intended to allow a right to contribution. In view of this implied statutory right, the court refused to bar contribution. Harrison, 608 F. Supp. at 506. Finally, the court recognized that, depending on the outcome of the trial, the non-settling defendants might be entitled to contribution. Id. at 507.

\textsuperscript{47} Nelson, 662 F. Supp. at 1333.
A. State Settlement Bar Statutes

The absence of a federal statute governing a partial settlement’s effect on contribution under 10b-5 requires courts to look to other sources of law. One of the most helpful sources of law is state tort settlement bar statutes.

(1) The Three Types of Settlement Bar Statutes

General tort settlement bar statutes have been enacted by twenty-four states.48 These statutes fall into three categories: those based on the 1939 Uniform Contribution Among Tortfeasors Act, those founded on the 1975 version of that Act, and those enacted by California and New York, which do not precisely follow either version of the Act, but which are substantially similar to them.

In states with statutes based on the 1939 version of the Uniform Contribution Among Tortfeasors Act,49 partial settlement bars contribution if the amount of the settlement reduces the nonsettling defendant’s ultimate liability.50 These statutes bar contribution only if the settling defendant receives a release before the nonsettling defendant receives the right to secure a monetary judgment. Also, the contribution bar requires that the settlement reduce the plaintiff’s award in any subsequent judgment by the settling defendant’s pro rata share.51


49. UNIF. CONTRIBUTION AMONG TORTFEASORS ACT § 5, 12 U.L.A. 98 (1939). A typical provision reads:

A release by the injured of one (1) joint tortfeasor does not relieve him from liability to make contribution to another joint tortfeasor unless the release is given before the right of the other tortfeasor to secure a money judgment for contribution has accrued, and provides for a reduction, to the extent of the pro rata share of the released tortfeasor, of the injured person’s damages recoverable against all the other tortfeasors.


In providing that reduction is available only "to the extent of the pro rata share of the released tortfeasor," these statutes actually may have "discourage[d] settlements in joint tort cases by making it impossible for one tortfeasor alone to take a release and close the file." Since the "pro rata share" cannot be determined in advance of a judgment against the other defendants, the plaintiffs cannot appreciate the effect a settlement might have on their total recovery.

A second category of settlement bar statutes, based on the later version of the Uniform Contribution Among Tortfeasors Act, were enacted in response to these deficiencies. Under these statutes, a partial settlement made in "good faith" completely bars contribution from the settling defendant. The Commissioners' comments accompanying the Uniform Act state that "[t]he requirement that the release or covenant be given in good faith gives the court occasion to determine whether the transaction was collusive, and if so there is no discharge." Under this scheme, so long as the settlement is made in good faith, the judgment is reduced by the dollar amount of the settlement and further claims for contribution against the settling defendants are barred.

Finally, two states chose not to follow either version of the Uniform Contribution Among Tortfeasors Act, but enacted statutes of their own design. Both of these statutes, however, contain a requirement of "good
faith," and otherwise operate in the same manner as statutes based on the 1975 Uniform Act.\(^{59}\)

(2) **Application of State Settlement Bar Statutes to Private 10b-5 Actions—**

**Should State or Federal Law Govern?**

The focus will now turn to the mechanism the courts must use in adopting state settlement bar statutes as the rule of law, or alternatively, pronouncing federal common law. Typically, contribution claims arise under state law. It might appear, then, that state substantive rules regarding the effect of settlements on contribution in 10b-5 actions would apply.\(^{60}\) Certain "areas of judicial decision," however, "[are]... so dominated by the sweep of federal statutes that legal relations which they affect must be deemed governed by federal law."\(^{61}\) Applying this principle, the court in *Globus v. Law Research Service Inc.*\(^{62}\) determined that since the sections of the Securities Exchange Act that provided express civil remedies also contain express provisions for contribution, there must be contribution under 10b-5. Thus, the court found an implied right of contribution just as a previous court had found an implied private cause of action under 10b-5.

Furthermore, the court held that contribution under Rule 10b-5 is governed by federal law.\(^{63}\) Contribution in these cases does not involve federal pendent jurisdiction over a state common law claim. Rather, these cases present an independent cause of action implied from the Se-

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58. Any party to an action wherein it is alleged that two or more parties are joint tortfeasors . . . shall be entitled to a hearing on the issue of the good faith of a settlement entered into by the plaintiff . . . and one or more alleged tortfeasors. . . . A determination by the court that the settlement was made in good faith shall bar any other joint tortfeasor . . . from any further claims against the settling tortfeasor. CAL. CIV. PROC. CODE § 877.6 (West Supp. 1989).


60. California's statute differs by providing the right to a hearing on the issue of good faith. CAL. CIV. PROC. CODE § 877.6 (West Supp. 1989).

61. "Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State. . . . There is no federal general common law." Erie R.R. Co. v. Tompkins, 304 U.S. 64, 78 (1938).

62. Sola Elec. Co. v. Jefferson Elec. Co. 317 U.S. 173, 176 (1942). In *Sola*, a patent dispute was brought in federal court based on diversity of citizenship. The court held that federal, rather than state, law governs whether the licensee is estopped from raising the defenses that the patent was invalid or that the license agreement violated the federal antitrust laws.


64. *Id.* at 958 n.2. ("There is no basis for doubting that the subject of contribution . . . is governed here by federal law [under § 10(b)].")
It is helpful to examine the rationale for applying a uniform federal rule of contribution, however, because the issue has not been definitively resolved.

The federal court first created a rule of federal common law in *Clearfield Trust*. *Clearfield* involved a suit by the United States against a Pennsylvania bank for the bank’s guaranty of a forged endorsement. Under Pennsylvania law, the government’s claim was estopped. The court held that the government was not subject to Pennsylvania law. Justice Douglas, writing for the majority, found that the federal government’s authority to issue checks was grounded in the Constitution and not dependent on the law of any state. Therefore, “[t]he duties imposed upon the United States and the rights acquired by it as a result of the issuance [must] find their roots in the same federal sources.”

Thus, when a rule of law is required to resolve rights and duties arising under federal law, the federal courts may fashion the necessary rule of decision by pronouncing federal common law.

Courts are not compelled to ignore state law, however, when issues require application of federal common law. Federal courts may decide that state law on a particular matter is a more appropriate choice and may adopt it as a federal rule of decision. In *United States v. Kimbell Foods, Inc.* the Supreme Court provided a test for lower courts to use in determining whether to formulate uniform federal common law under *Clearfield* or to adopt state law as the federal rule of decision. The test states that, “federal programs that ‘by their nature are and must be uni-

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64. Huddleston v. Herman & MacLean, 640 F.2d 534, 557 (5th Cir. 1981) aff’d in part, rev’d in part on other grounds, 459 U.S. 375 (1983) (“Because the Rule 10b-5 action is implied in a federal statute, the right to contribution under Rule 10b-5 is determined by federal law.”). See generally Note, Globus: A Prolific Generator of Nice Questions, 33 Ohio St. L.J. 898 (authored by Tom H. Connolly) (examining the development and application of federal common law to securities litigation, and exploring the implications of a federal common law right to contribution).

65. Clearfield Trust Co. v. United States, 318 U.S. 363, 367 (1943) (“In the absence of an applicable Act of Congress it is for the federal courts to fashion the governing rule of law according to their own standards.”).

66. Id. at 366.

67. While *Clearfield* involved an action on a federal contract, the principle has been applied in tort cases as well. E.g., United States v. Standard Oil Co., 332 U.S. 301, 305-11 (1947) (suit for injury to U.S. serviceman); Urie v. Thompson, 337 U.S. 163, 173-87 (1949) (the meaning of the word “negligence” in the Federal Employers Liability Act is determined by federal law even though the act itself does not define the word). At the extreme, the Supreme Court held in Textile Workers v. Lincoln Mills, 353 U.S. 448, 456-57 (1957), that a statute that gave federal jurisdiction over suits by unions involving collective bargaining agreements required the federal courts to formulate an entire body of substantive federal law. See generally Mishkin, The Variousness of “Federal Law”: Competence and Discretion in the Choice of National and State Rules for Decision, 105 U. Pa. L. Rev. 797 (1957) (analyzing the application of the rule in *Clearfield*).

form in character throughout the Nation' necessitate formulation of controlling federal rules. . . . Conversely, when there is little need for a nationally uniform body of law, state law may be incorporated as the federal rule of decision."69

In First Federal Savings & Loan v. Oppenheim Appel, Dixon & Co.,70 the Southern District Court of New York applied the Kimbell test to a 10b-5 situation and determined that each district court should apply the local forum's law in 10b-5 actions. The court stated that it could "think of no compelling reason why a uniform national rule would be necessary to effectuate the federal regulatory program."71 Additionally, the court observed that state statutes of limitations are often incorporated as the rule of decision for federal securities claims.72 Finally, the court noted the uncertainty of a situation in which there are both federal and state claims at stake. The application of federal law to the 10b-5 claim and state law to the state action could create difficulty in sorting out a jury's damage award.73 The court concluded that the forum state settlement bar statute74 should be applied in 10b-5 actions.75

The Central District Court of California, however, took a contrary position in Nelson v. Bennett.76 In Nelson, a group of 10b-5 defendants offered to settle with the plaintiffs, subject to the condition that the court would dismiss all contribution claims against the settling defendants. As in First Federal, a key issue was whether the court should use the state settlement bar statute or recognize federal common law. Applying the Kimbell test, the Nelson court determined that the First Federal reliance on the forum state settlement bar statute was inappropriate. The Nelson court held that there were "at least three compelling reasons why a uniform national [settlement bar] rule would be necessary."77 First, contri-

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69. Id. at 728 (citations omitted).
71. Id. at 1036.
72. Id. at 1036 n.11. The Supreme Court in Ernst & Ernst v. Hochfelder, 425 U.S. 185, 210 n.29 (1976), stated that since no statute of limitations is provided for in § 10(b) actions, the statute of limitations of the forum state should be followed.
73. 631 F. Supp. at 1036 (S.D. N.Y. 1986) ("Where a federal securities law and a state law claim are based on the same tortious conduct . . . it is not clear how disparate rules of contribution . . . would be applied to a jury's verdict awarding identical damages on both claims.").
75. The court also observed that other courts in the second circuit had applied the New York settlement bar statute. See, e.g., Stratton Group, Ltd. v. Sprayregen, 466 F. Supp. 1180, 1189 n.11 (S.D.N.Y. 1979) ("On balance . . . the better approach for a federal court would be to look to state law concerning contribution and its underlying principles. If these principles sufficiently vindicate the federal policy concerning contribution, they should be adopted. Indeed, absent a federal statute the parameters of contribution in relation to settling tortfeasors should not be defined in a vacuum.").
77. Id. at 1336.
bution bar rules "affect[ ] key substantive rights of the defendants under the federal securities laws." 78 Second, the Nelson court felt that application of state settlement bar statutes would lead to disparate results. The court observed that some states do not have any law barring contribution from settling defendants. 79 Thus, if federal courts sitting in those states tried to apply the forum's law, any federal right of contribution would be destroyed. Finally, the court found that a state-by-state rule would encourage forum shopping and generate "wasteful conflicts of law litigation . . . to determine which state's settlement bar statute applies." 80

The Nelson court makes a more persuasive argument. 81 If contribution is to serve its federal purposes of assuring fairness and deterring 10b-5 violations, 82 it should be enforced without regard to the locus of the 10b-5 violation. In light of the potential for inconsistent verdicts and forum shopping, either the courts or Congress must declare a uniform rule on the settlement bar question, and not rely on the settlement bar scheme set out in the forum state's statute. The next section will demonstrate that, in spite of conflicting directions, common themes emerge that may guide the development of such a rule.

B. The Good Faith Requirement

(1) Good Faith and State Settlement Bar Statutes

There is agreement among the courts, the Uniform Contribution Among Tortfeasors Act, and the state settlement bar statutes, that, subject to a condition of "rightness," a partial settlement will release the settling defendant from further liability both to the plaintiff and to the nonsettling defendants. 83 For all practical purposes, "rightness" entails that a settlement must be entered into in "good faith." 84 In fact, the 1975 Uniform Contribution Among Tortfeasors Act and the state settle-

78. Id.
79. Id. The court also noted that at the time of the decision only twenty-two states had some form of settlement bar statute. Id. at n.20.
80. Id. at 1337. The court took special note of the fact that adoption of local statutes of limitations have resulted in such problems, citing several commentators. See, e.g., Committee on Federal Regulation of Securities, Report on the Task Force on Statute of Limitations for Implied Actions, 41 Bus. LAW. 65, 647 (1986) ("The uncertainty and lack of uniformity promote forum shopping by plaintiffs and result in wholly unjustified disparities in the rights of parties litigating identical claims in different states.").
81. This position was acknowledged by In re Sunrise Sec. Litig., 698 F. Supp. 1256, 1257 (E.D. Pa. 1988) ("a uniform federal rule is desirable here").
82. See supra note 10.
83. See supra notes 45-47, 48-59 and accompanying text.
84. Unfortunately, there is no uniform standard for "good faith." This section will examine how the general concept is found throughout the acts, and will later establish a model standard for the determination of good faith in private 10b-5 actions. See infra notes 96-99 and accompanying text.
ment bar statutes that follow its scheme, explicitly require good faith. Likewise, California and New York, which have chosen to draft their own settlement bar statutes, expressly require settlements to be in good faith.

State settlement bar statutes based on the 1939 Uniform Contribution Among Tortfeasors Act, however, do not require good faith as a specific prerequisite to barring contribution claims. The commissioners on Uniform State Law lessened the likelihood of a bad faith settlement by reducing any judgment according to the relative culpability of the settling defendant instead of the dollar amount of the settlement. As the commissioners for the 1975 Uniform Contribution Among Tortfeasors Act explained this part of the 1939 scheme:

The idea underlying the 1939 provision was that the plaintiff should not be permitted to release one tortfeasor from his fair share of liability and mulct another instead, from motives of sympathy or spite, or because it might be easier to collect from one than from the other; and that the release from contribution affords too much opportunity for collusion between plaintiff and the released tortfeasor against the one not released.

In short, the framers of the 1939 Uniform Act sought to ensure good faith settlements by placing the plaintiff at risk of not receiving full collection of the judgment.

Although California's settlement bar statute does not follow either of the Uniform Acts, the California Supreme Court has enunciated a valuable method for determining good faith under any scheme. In *Tech-Bilt v. Woodward-Clyde & Assoc.*, the court reasoned that to determine the presence of good faith, it must first decide "whether the amount of the settlement is within the reasonable range of the settling tortfeasor's proportional share of comparative liability for the plaintiff's injuries." The court observed that a showing of "good faith" is not merely the opposite of a showing of "bad faith." On the contrary, even an apparently low settlement might be in good faith because the task of quantifying damages is often difficult because a disproportionately low sum may be reasonable if the tortfeasor is insolvent or uninsured.

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85. See supra note 57.
86. See supra note 58.
87. UNIF. CONTRIBUTION AMONG TORTFEASORS ACT § 4, 12 U.L.A. 98, 99 (commissioners' comment (1975)).
88. But see Foley, *Settling Out of a Multiparty Case: Tech-Bilt Leaves the 'Good Faith Standard' as Vague as Ever*, 5 CAL. L. W., Oct. 1985, at 25 (arguing that the court's standard does not improve the understanding of good faith).
90. *Tech-Bilt*, 38 Cal. 3d at 499, 698 P.2d at 166, 213 Cal. Rptr. at 263.
91. Id.
92. Id., 213 Cal. Rptr. at 263, 698 P.2d at 167 (quoting Stambach v. Superior Court, 62 Cal. App. 3d 231, 238 (1976)).
The court cautioned, however, that the amount of the settlement is relevant to a determination of good faith,93 stating that, "[a] defendant's settlement figure must not be grossly disproportionate to what a reasonable person, at the time of the settlement, would estimate the settling defendant's liability to be."94 The court also imposed a requirement that a decision regarding good faith be made solely on the basis of the information available at the time of the determination.95

Like the 1939 and 1975 versions of the Uniform Contribution Among Tortfeasors Act and the state statutes based upon them, the federal common law settlement bar rule should bar contribution in multiple defendant 10b-5 actions when a defendant wishes to settle with the plaintiff, subject to a judicial determination of good faith. The Tech-Bilt standard for determining good faith is a logical and flexible rule appropriate for application in the context of 10b-5 settlements.

(2) Good Faith in 10b-5 Actions

Although the Nelson v. Bennett court denounced the wisdom of applying the California settlement bar statute in 10b-5 cases,96 its solution paralleled that of Tech-Bilt. The similarity is apparent in the Nelson court's expression of the factors to consider in determining good faith: "the possible uncollectibility of any larger judgment which might be entered against the settling defendants, the adequacy of the settlement amount in light of the comparative culpability of the settling defendants and the uncertainties of establishing such liability."97

In antitrust cases, federal courts have reached similar conclusions regarding the propriety of settlements. For example, the Fifth Circuit, in In re Corrugated Container Antitrust Litigation,98 examined the settlement problem and established a standard of good faith for antitrust settlements similar to the standard expressed in Tech-Bilt and Nelson:

First the district court must evaluate the likelihood that plaintiffs would prevail at trial. Second, the district court must establish a range

93. Id., 213 Cal. Rptr. at 263, 698 P.2d at 166-67.
95. Id., 213 Cal. Rptr. at 263, 698 P.2d at 167. See also City of Detroit v. Grinnell Corp., 495 F.2d 448, 456 (2d Cir. 1974) (citations omitted):
   It cannot be overemphasized that neither the trial court in approving the settlement nor this Court in reviewing that approval have the right or the duty to reach any ultimate conclusions on the issues of fact and law which underlie the merits of the dispute. It is well settled that in the judicial consideration of proposed settlement, 'the [trial] judge does not try out or attempt to decide the merits of the controversy' . . . and the appellate court 'need not and should not reach any dispositive conclusions on the admittedly unsettled legal issues.'
97. Id.
98. 643 F.2d 195 (5th Cir. 1981).
of possible recovery that plaintiffs would realize if they prevailed at trial. And third, guided by its findings on plaintiffs’ likelihood of prevailing on the merits and such other factors as may be relevant, the district court must establish, in effect, the point on, or if appropriate, below, the range of possible recovery at which a settlement is fair and adequate.\(^9\)

Thus, *Tech-Bilt*, *Nelson*, and *Corrugated* developed a standard that looks to the plaintiff’s potential trial recovery and then establishes the point of good faith settlement. This “good faith point” is determined by a variety of factors: (1) an examination of the likelihood and degree of culpability of the settling defendant to protect the interests of the non-settling defendants by avoiding disproportionately low settlements; (2) an examination of the settling defendant’s financial ability to ensure that the settlement amount adequately compensates the plaintiff and has a sufficient deterrent effect; and (3) an evaluation of the circumstances surrounding the settlement to avoid the possibility of collusion, fraud, or other tortious conduct.

The emerging federal common law settlement bar determination of good faith should adopt these factors for application in 10b-5 cases. The court first should determine the range of the plaintiff’s possible trial recovery. The court then should compare the proposed settlement amount to the range of fair and adequate settlements. Such a determination should consider several factors, including: the settlor’s likely proportionate liability; the settlement amount; the financial conditions and insurance policy limits of settling defendants; and the existence of collusion, fraud or other tortious conduct.

### III. Apportioning the Judgment Among Nonsettling Defendants

If the remaining defendants’ rights to contribution are barred, a mechanism for equitably adjusting the plaintiffs’ ultimate judgment must be created. This device is necessary to protect the non-settling defendants from having to pay more than their fair share of the judgment. In this section three methods of apportioning 10b-5 judgments are described. The discussion then focuses on the two most commonly applied methods and their effects on the litigation process. The section concludes with a proposal for the correct allocation of risks and benefits.

#### A. Methods of Apportioning 10b-5 Judgments

Three approaches to apportioning responsibility for paying a plaintiff’s damage award have been used by the courts in 10b-5 actions. A pro rata approach divides the judgment equally among settling and nonsettling defendants. Relative culpability divides the award according to the fault of each defendant. A pro tanto approach reduces the judgment by

\(^9\) Id. at 212.
the settlement amount, then apportions it among the nonsettling defendants. Each approach involves a different "price" paid by the settling plaintiff. The plaintiff either will give up the settling defendant's pro rata liability, the settling defendant's relative culpability, or the portion of his claim precisely equal to the dollar amount of the settlement.

(1) Pro Rata Allocation

In early 10b-5 cases, liability among defendants often was determined by the pro rata method.100 Under this scheme, the judgment is divided evenly among all culpable defendants whether they have settled or not. If a partial settlement is reached, the total liability of any remaining defendants is reduced by the pro rata share of any settling defendants. For example, in a suit by $P$ against $D_1$ and $D_2$, if $D_1$ settles for $100,000$, and then $P$ receives a judgment for $500,000$, $D_2$'s liability will be $250,000$ and $P$ will recover $350,000.101 The framers of the 1939 Uniform Contribution Among Tortfeasors Act adopted the pro rata approach.102 Although pro rata is administered easily, it has been widely criticized as unfair, since it places equal liability on parties who are not necessarily equally culpable.103

One commentator has suggested that the use of the pro rata approach in 10b-5 settlement cases is the result of three factors: its wide use at common law, its ease of administration, and the use of the phrase "as in cases of contract" by sections 9(e) and 18(b) of the Securities Exchange Act, which expressly provide for contribution.104 As these sections state, "Every person who becomes liable to make payment under this section may recover contribution as in cases of contract from any person who, if joined in the original suit, would have been liable to make the same payment."105

Courts initially understood the phrase to mean that the pro rata method used in common law contract cases should be applied to securities cases as well.106 In Gould v. American Hawaiian Steamship Co.,

101. The $500,000 judgment is divided evenly between the two original defendants. See Adamski, supra note 8, at 555.
102. See supra note 50 and accompanying text.
105. 15 U.S.C.A. §§ 78i(e), 78r(b) (West 1981) (emphasis added).
however, the court held that the phrase did not necessarily mandate pro rata allocation. In Gould, a defendant who was required to surrender profits acquired in violation of the securities laws cross-claimed against settling defendants. In rejecting a strict application of the pro rata rule, the court first observed that multiple defendants to a common law contract action need not always receive pro rata contribution. Second, the court determined that the phrase "in case of contract" was intended to exclude tort law from the contribution analysis. Instead of the common law tort rule that intentional joint tortfeasors are not entitled to contribution, the Gould court believed the phrase mandates use of the common law contract rule that allows for contribution. Thus, the Gould court held that the phrase was not intended to establish a method of allocation, but rather to establish contribution in the first instance. The court thus refused to blindly apply the pro rata method. One commentator has stated, "[t]he teaching of Gould is that federal courts will not be bound inflexibly to a pro rata measure of contribution."

(2) Relative Culpability

In view of more recent developments regarding the apportionment of a partial settlement, the pro rata method no longer presents a viable solution to apportioning liability among nonsettling defendants. Starting with McLean v. Alexander, courts began to develop the policy of relative culpability. In McLean, all of the defendants who had sold stock to the plaintiff settled. The sole remaining defendant was an accountant who had audited the books. A judgment was entered that far exceeded the amount the other defendants had paid in settlement. The court found the accountant only ten percent culpable and refused to use the pro rata allocation of fifty percent, recognizing a "vast difference" in the relative culpability of the defendants. The court maintained that damages should be apportioned on the basis of relative fault, viewing this method as the "modern approach," and criticizing the pro rata standard as having "more mathematical than judicial integrity."

In the recent case of Smith v. Mulvaney, the Ninth Circuit examined pro rata allocation of liability, but determined that the proper

108. Id. at 171.
109. Id. at 170.
111. Fischer, supra note 103, at 1830.
113. Id. at 1272.
114. Id. at 1274.
115. Id. at 1273.
116. 827 F.2d 558 (9th Cir. 1987).
measure should be relative culpability.\textsuperscript{117} The court stated that the Mc-
Lean court's criticism of the pro rata method "[A]ppears especially ap-
propriate in securities fraud cases which include numerous defendants
with potentially vast differences in culpability. Contribution is an equi-
table doctrine. To apportion damages without regard to fault reduces, to
an extent, the equity which the doctrine was intended to provide."\textsuperscript{118}

Applying the relative culpability rule to the previous example in
which $D1$ settles for $100,000 and $P$ receives a judgment for $500,000, if
$D1$ were determined to be 40% culpable, $D2$ would be liable to $P$ for
$300,000 (60\% of the judgment) without regard for the amount of $D1$'s
settlement. Determination of the ultimate relative culpability is made at
trial, not at the time of the settlement. To effectuate a settlement, the
court only need determine that the settlement is in good faith and that
the amount is within the range of reasonable, expected settlements.\textsuperscript{119}

(3) \textit{Pro Tanto Allocation}

The potential difficulty of determining a settling defendant's liability
gives rise to a third method of allocating the effects of a settlement. The
1975 Uniform Contribution Among Tortfeasors Act\textsuperscript{120} presents an ap-
proach that simply reduces the nonsettling defendant's liability by the
dollar amount of the settlement. "Any judgment against the remaining
defendant is reduced \textit{pro tanto}, that is, by the amount actually paid in
settlement."\textsuperscript{121} Thus, in the above example, a $100,000 settlement by
$D1$ would reduce $D2$'s liability by $100,000 to $400,000. If there is more
than one nonsettling defendant, the reduced judgment is divided among
them after trial.

Although pro tanto does not expressly consider each defendant's in-
dividual liability, as does relative culpability, it has been argued that a
pro tanto rule would produce more equitable settlements. According to
this view, the pro tanto rule "provides an inducement to fair settlements,
yet at the same time allows for sufficient judicial supervision of the terms
of the settlement that the rights of nonsettling defendants are not
prejudiced or diminished.... It would appear that a 'good faith' require-
ment [for settlement] would adequately safeguard the interest of the non-
settling defendants."\textsuperscript{122}

Since the developing federal common law settlement bar rule seems
to be moving towards a good faith requirement, including a judicial de-

\begin{footnotes}
\item 117. \textit{Id.} at 561.
\item 118. \textit{Id.}
\item 119. This is the direct application of the good faith standard. \textit{See supra} notes 96-99 and
accompanying text.
\item 121. Adamski, \textit{supra} note 8, at 548-49.
\item 122. Fischer, \textit{supra} note 103, at 1834.
\end{footnotes}
termination that the settlement is within the range of reasonable settlement amounts, pro tanto appears to be a reasonable and fair means of apportionment in 10b-5 cases. Several cases have taken this approach. Nevertheless, from the nonsettling defendant's vantage, a pretrial decision of a settlement's reasonableness may not be a satisfactory solution. Essentially, the pro tanto approach requires her to rely on the other parties to protect her interests during the settlement process. The next section describes how the allocation of the settlement amount to the final judgment can have a substantial effect on the nonsettling defendants' liability to the plaintiff.

B. The Effect of Apportionment on the Remaining Parties

Both the relative culpability and the pro tanto methods of apportioning settlements significantly affect the character of the litigation. The risk that the settlement is correct shifts among the parties, depending on which method of allocation is used. This section examines the effect each of the currently predominant methods, relative culpability and pro tanto, have on the parties.

(1) Effect of Relative Culpability

If the relative culpability of a settling defendant reduces a nonsettling defendant's ultimate liability the nonsettling defendant will be no worse off than if no settlement had occurred. "This approach has the advantage of preventing the unfairness to the nonsettlor inherent in the pro tanto approach, since the nonsettling defendant will not be required to bear a disproportionately large share of plaintiff's total damages." Under this system, the plaintiff will not necessarily receive the full value of any ultimate judgment. If the settlement amount is less than the relative culpability of the settling defendant, the plaintiff's recovery will be that much less. In short, the relative culpability approach allocates to the plaintiff the risk that the settlement amount is less than the settling defendant's culpability. On the other hand, blind application of the relative culpability approach could result in a windfall to the plaintiff should the settlement amount exceed the settling defendant's relative culpability.

123. See notes 96-99 and accompanying text.

124. See, e.g., U.S. Indus., Inc. v. Touche Ross & Co., 854 F.2d 1223, 1263 (10th Cir. 1988) (holding that lower court's awarding of setoff of settlement amount was not clearly erroneous); Knox v. County of Los Angeles, 109 Cal. App. 3d 825, 836, 167 Cal. Rptr. 463, 469 (1980) (absent good faith allocation of settlement amounts, defendants were entitled to setoff of entire settlement); Dionese v. City of West Palm Beach, 500 So. 2d 1347, 1349 (Fla. 1987) (in absence of specific allocations in settlement agreement, the total amount of the settlement must be set off from the entire verdict).

125. Adamski, supra note 8, at 551-52.
share of the judgment. In *Doyle v. United States*, a wrongful death action involving contribution and settlement issues, the court stated:

The better rule, this court feels, is to respect the aleatory nature of the settlement process and to hold both the plaintiff and settling defendant to their gamble. The plaintiff gambles that the amount he receives in settlement plus the amount recoverable from the non-settling defendant will be greater than he could have recovered if he pursued both actions to a judgment (i.e., the plaintiff hopes the settling defendant will pay more than what is eventually determined to be his proportional share of the damages). The settling defendant gambles that the amount he pays in settlement is less than he ultimately would be liable to pay, had he gone to judgment.

There are three significant problems with the relative culpability system. First, the plaintiff does not know precisely what she is bargaining for, since she does not know the parties' relative culpabilities until a judgment is received. Second, relative culpability requires the court eventually to determine the actual culpability of the settling defendant, thus negating some of the judicial economy benefits of settlement. Third, the settling defendant will not be a party to the determination of relative culpability. Thus, to obtain the lowest possible liability, the nonsettling defendants will argue that the settling defendant is more culpable than the amount indicated by the settlement. As a result, the plaintiff is forced to take the position of the settling defendant, effectively, switching sides. In order to obtain the largest possible recovery from the now settling defendants, the plaintiff must minimize the settling defendant's culpability by arguing that the settlement was at least an adequate representation of the settling defendant's relative culpability.

A benefit of the relative culpability method is that it "is unlikely that a plaintiff will voluntarily settle for an intentionally low amount with one wrongdoer, knowing that any judgment against the remaining defendants will be reduced by the settling defendant's share of total damages." In other words, the mechanics of relative culpability make fraud and collusion between the plaintiff and the defendant unlikely.

While the court's determination of relative culpability of an absent party may be burdensome and lead to administrative inefficiency, this problem may not be significant. The district court in *McLean v. Alexan-

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127. Id. at 711 n.5.
129. See Pieringer v. Hoger, 21 Wis. 2d 182, 192, 124 N.W.2d 106, 112 (1963) (the relative culpability of the settling defendant can be determined without requiring the settlor to be a party to the litigation).
130. Adamski, *supra* note 8, at 553.
found that determining relative culpability was "only minimally more difficult" than applying a pro rata approach. The court need not be concerned with the good faith or reasonableness of the settlement, since the settlors will protect their own interests, and the nonsettlers will not be affected by the settlement. Any inefficiencies in determining the culpability of the settlor will be balanced by the efficiency of a less rigorous, pretrial hearing for good faith.

(2) Effect of Pro Tanto

The most appealing aspect of the pro tanto approach to settlement allocation is its ease of administration. The court need not determine the exact relative culpability of the settling defendant. Rather, the court need only find that the settlement is within the range of reasonable settlement amounts, and thus in good faith. Additionally, because the plaintiff's total recovery equals the judgment amount, the plaintiff will not receive any more than a single satisfaction. Application of the pro tanto rule thus provides for an efficient allocation of the effects of settlement, and also ensures that the plaintiff receives a full, fair, and single satisfaction.

On the other hand, if a nonsettling defendant's liability is reduced by the pro tanto dollar amount of the settlement, that defendant could be worse off than if there had been no settlement at all. The nonsettling defendant would be forced to depend on the court's pretrial determination of good faith to protect her interests. Thus, the pro tanto system "may lead to collusion between the plaintiff and settling defendant, since the plaintiff—who will be able to collect total damages less the settlement amount from the remaining defendants—theoretically has nothing to

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132. Id. at 1276. The court considered the following factors in determining relative culpability: "the defendant's extent of involvement, duration of involvement, knowledge of entire scheme to defraud, intent, extent of his contribution toward causation of the losses and benefit received." Id. at n.84.
133. "The settlement payment is merely deducted from any judgment against the nonsettlor without regard to the culpability of the settlor." Adamski, supra note 8, at 549 n.105.
134. As required in the good faith hearing. A determination of good faith in the pro tanto approach not only protects less culpable nonsettling defendants, but also ensures the deterrent effect of the laws.
135. The "single satisfaction" rule is a common law doctrine which holds that a plaintiff is entitled to only one satisfaction for the joint wrongs of others. See generally PROSSER AND KEETON, supra note 30, at § 48. Thus, any amount received from one joint tortfeasor will reduce the liability of any other tortfeasors, such that the plaintiff will receive only a single compensation for the wrong. "The effect of this rule is that, unless further adjustment is made, the nonsettlor benefits by having to pay proportionately less whenever the settlor has paid more than his subsequently adjudged share of plaintiff's damages." Adamski, supra note 8, at 564 (footnote omitted).
lose by accepting an inadequate sum in settlement.”

In addition, “the pro tanto approach would allow the plaintiff [rather than the jury] to select, subject only to meeting the good faith test, which of several wrongdoers should bear the major burden of payment for the violation.”

In short, the pro tanto approach provides an easily administered system favorable to the plaintiff. Under the pro tanto approach, the plaintiff does no worse in settlement than in trial, and the risk of a bad settlement is shifted to the nonsettling defendants. Note, however, that this rule appears unfair to the nonsettling defendants. As each defendant settles, each of the remaining defendants potentially becomes liable for a larger and larger share of the final judgment.

(3) Allocation of Risk and Benefits

The primary difference between the relative culpability and pro tanto methods lies in the allocation of risk between the plaintiff and the nonsettling defendants. In a relative culpability allocation scheme, the risk of an inadequate settlement falls on the plaintiff. Under this scheme, it is in the plaintiff’s interest to make a settlement close to the settling defendant’s liability so that the plaintiff’s total recovery is not overly reduced. Conversely, the pro tanto scheme places this risk on the nonsettling defendants because an inadequate settlement increases their own liability.

Another perspective on the distinctions between the two methods focuses on their comparative benefits. Thus, under the relative culpability system, the possibility of collusion between plaintiff and settling defendant is virtually nonexistent, and the nonsettling defendants’ interests are completely protected. The pro tanto system has appeal in its simplicity of administration and in its guarantee that the plaintiff will receive neither more nor less than the amount of the judgment.

In light of the above analysis, a hybrid system that maximizes the benefits, yet minimizes the shortcomings appears to be the best solution.

136. Adamski, supra note 8, at 549.
137. Id. at 551.
138. There are three possible scenarios in a pro tanto allocation of settlement: First, the settlement could be an amount that is equal to or less than the ultimate judgment. Second, the settlement could be an amount in excess of the ultimate judgment. Finally, a settlement may be made and the court may find against the plaintiff at trial. In the first case, the plaintiff will receive exactly the amount of the judgment, either entirely from the settling defendant, or collectively from the settling and nonsettling defendants. In the second situation, the plaintiff will recover more via the settlement than at trial, and the nonsettlor is not obligated to pay anything. In the last case, the plaintiff will have recovered the entire settlement amount in excess of what would have been received at trial. Thus, the worst the plaintiff can do in settling, under a pro tanto allocation, is to receive exactly what he would be entitled to had the matter gone to a judgment.
139. See supra note 138.
In the emerging federal common law, the nonsettling defendant's liability should be reduced by the greater of either the settlement amount or the degree of culpability of the settling defendant. To apply the proposed standard to the example set out previously, assume $D1$ settles for $\$100,000$, and then $P$ receives a judgment for $\$500,000$. If it is determined that $D1$ is forty percent culpable, $D2$'s liability will be $\$300,000 ($500,000 less forty percent). On the other hand, if $D1$ is determined to be only five percent culpable, $D2$'s liability will be $\$400,000 ($500,000 less $\$100,000, since $\$100,000 is greater than five percent of $\$500,000$). This allocation ensures that the nonsettling defendant will be liable, at worst, for the same amount as in the absence of a settlement. At the same time, this allocation abides by the single satisfaction rule and provides the plaintiff receives no more than she would receive at trial.

Conclusion

Courts should develop federal common law to ensure that a partial settlement made in good faith will bar contribution. Good faith should be judicially determined, with primary emphasis on the anticipated relative culpability of the settling defendant. Determination of relative culpability vis-a-vis the proposed settlement should be based on a three-part test: (1) The likelihood plaintiff will prevail at trial, (2) the range of expected recovery, and (3) the point on this range where settlement by the defendant is fair and adequate, and thus made in good faith.

The nonsettling defendant's liability should be reduced by the greater of (1) the actual settlement amount, or (2) the degree of culpability of the settling defendant. This allocation will ensure that the nonsettling defendant will, at worst, be liable for the amount she would have incurred had there been no settlement. Although this method will shift to the plaintiff the risk of incorrectly estimating the value of a settlement, the plaintiff's knowledge of the risk will encourage a carefully negotiated settlement. This careful analysis by the plaintiff will further encourage a...
good faith settlement because she will bear the risk that the settlement amount is too small. Furthermore, the court must actively review the proposed settlement to ensure that it is adequate, in good faith, and not the result of undue influence or overreaching.

This proposal is consistent with the goals of the federal securities laws: compensation of defrauded persons and the deterrence of securities law violations.\textsuperscript{143} Such a proposal adequately compensates the plaintiff, subject only to the risk that the determination of settlement value by both the plaintiff and the court was incorrect. Furthermore, this proposal promotes deterrence by assuring, through the tools of contribution and the allocation of settlement amounts, that a person contemplating a violation of Rule 10b-5 will be reachable via contribution and therefore ultimately liable to potential plaintiffs.

\textsuperscript{143} See \textit{supra} note 10.