Should Prejudgment Interest Be a Matter of Procedural or Substantive Law in Choice-of-Law Disputes?

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Prejudgment interest is interest a court awards to a plaintiff who receives money damages in excess of any settlement offer made by a defendant prior to trial.[1] Courts award prejudgment interest for two basic reasons: (1) to compensate the aggrieved plaintiff fully,[2] and (2) to alleviate congestion in the courts by encouraging prompt and equitable settlements.[3] Courts consider the former rationale substantive and the latter procedural.[4] States characterize their prejudgment interest rules according to whether they regard them as more substantive or procedural, that is, geared more toward plaintiff compensation or judicial economy.[5] For example, some statutes contain offer-counteroffer provisions and other procedural mechanisms, which suggests that the legislatures designed them and courts interpreted them mainly for purposes of judicial economy and control.[6] Conversely,

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1 *Laudenberger v Port Authority of Allegheny County*, 496 Pa 52, 436 A2d 147, 149 (1981).

2 See, for example, *Simeone v First Bank National Association*, 73 F3d 184, 190–91 (8th Cir 1996) (stating that prejudgment interest is an element of damages that courts "award to provide full compensation by converting time-of-demand damages into time-of-verdict damages"); *Marrazzo v Scranton Nehi Bottling Co*, 438 Pa 72, 263 A2d 336, 337 (1970) (stating that the award for the time delay is in the form of interest and is thus merely an extension of the compensatory damages necessary to make a plaintiff whole).

3 See, for example, *Laudenberger*, 436 A2d at 150–51 (explaining that the purposes of Pennsylvania's prejudgment interest rule were to "encourage pre-trial settlement" and "alleviate delay in the disposition of cases, thereby lessening congestion in the courts").

4 See, for example, id (comparing different courts' characterizations of their prejudgment interest rules and explaining that every rule or law has some procedural and substantive component, though a characterization is still useful to show the purpose for which a legislature or court enacted the rule or to show the area in which the rule has the greatest effect).

5 For example, compare *Yohannon v Keene Corp*, 924 F2d 1255, 1264–67 (3d Cir 1991) (arguing that even though courts can characterize prejudgment interest as substantive, the Pennsylvania Supreme Court structured the rule such that Pennsylvania courts could and should characterize it as procedural), with *Simeone*, 73 F3d at 190–91 (stating that Minnesota's prejudgment interest rule is an element of damages to provide full compensation "by converting time-of-demand damages into time-of-verdict damages" and is therefore substantive). See also *Morris v Watsco, Inc*, 385 Mass 672, 433 NE2d 886, 890 n 7 (1982) (explaining that prejudgment interest laws may be more procedural or substantive depending on whether the calculation is ministerial or discretionary).

6 See, for example, Ohio Rev Code Ann § 1343.03 (West 1994 & Supp 1999) (conditioning the interest award on a determination that the party required to pay failed to make a good faith effort to settle, and that the party who will receive the payment did not fail to do so); Tex Fin

other states have characterized their prejudgment interest rules primarily as additional victim compensation.[7]

Federal courts, however, unanimously construe prejudgment interest rules as substantive under *Erie Railroad Co v Tompkins*[8] because of their outcome-determinative nature. Thus, federal courts follow the characterizations of the states in which they sit.[9] This practice by the federal courts has led to heightened vertical uniformity within states.[10] The increased vertical uniformity, coupled with states' differing characterizations of prejudgment interest along procedural/substantive lines, exacerbates the lack of horizontal uniformity that might have existed among federal courts across state lines.[11] This lack of uniformity across state lines has led to forum shopping, unpredictability, and a lack of uniformity of outcomes in choice-of-law cases because damage awards from identical cases vary depending on the state.[12]

This Comment proposes a solution to these problems by challenging the assumption that when courts characterize prejudgment interest rules as procedural for choice-of-law purposes, they fulfill the stated purposes of "unclogging the judicial machinery," "encourag[ing] settlements," and "reducing the number of cases actually going to

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Code Ann §§ 304.101–304.108 (West 1998) (including suspended periods for the accrual of interest due to delays in the trial or during periods that an offer may be accepted). Thus, courts can penalize plaintiffs and defendants for refusing to accept, or failing to offer, a reasonable settlement offer. See also *Laudenberger*, 436 A2d at 150–55, in which the Pennsylvania Supreme Court firmly established that its prejudgment rule's main purpose—control over both plaintiffs and defendants—is procedural and thus courts should always construe it as a procedural rule, even though it involves some substantive rights.

7 See, for example, *Simeone*, 73 F3d at 190–91 (noting that "[p]rejudgment interest is an element of damages awarded to provide full compensation" to the plaintiff); *Star Technologies, Inc v Philips Medical Systems, NA, Inc*, 23 Va App Cir 267, 269 (1991) ("'The award of prejudgment interest is to compensate plaintiff for the loss sustained by not receiving the amount to which he was entitled at the time he was entitled to receive it.'"), quoting *Marks v Sanzo*, 231 Va 350, 345 SE2d 263, 267 (1986).

8 304 US 64 (1938).

9 *Laudenberger*, 436 A2d at 152. See also *Plantation Key Developers, Inc v Colonial Mortgage Co of Indiana, Inc*, 589 F2d 164, 170 (5th Cir 1979); *Clissold v St. Louis-San Francisco Railway Co*, 600 F2d 35, 38–39 (6th Cir 1979); *Glick v White Motor Co*, 458 F2d 1287, 1293 (3d Cir 1972) (stating that the unanimous federal rule regarding prejudgment interest is to follow the state rules in which the federal court sits); *In re Air Crash Disaster near Chicago, Illinois, on May 25, 1979*, 480 F Supp 1280, 1282 (N D Ill 1979), affd, 644 F2d 633 (7th Cir 1981).

10 Vertical uniformity refers to the uniform adjudication of cases within a particular state while horizontal uniformity refers to the uniform adjudication of cases by courts across state lines.

11 For example, federal law is said to be horizontally uniform because courts should apply federal law in the same way as other federal courts regardless of the state in which the parties brought the suit. Likewise, state criminal laws often lack horizontal uniformity because they differ from state to state. Therefore, because states characterize their laws differently and federal courts follow *Erie* and its progeny to enforce vertical uniformity strictly, together these conditions exacerbate horizontal uniformity.

12 See discussion in Parts II.C, III, and IV.A.

trial."[13] A procedural characterization, in the end, does just the opposite.

Part I of this Comment describes what prejudgment interest is and explains why different states characterize their prejudgment interest rules as either procedural or substantive. Part II delineates the current state of the law, showing how static interpretations of prejudgment interest statutes have led to differences between states.[14] Part III offers an example to demonstrate how the problem can actually play out in the real world. Part IV argues that the proper understanding of the purpose behind procedurally characterized prejudgment interest rules is dynamic judicial efficiency and case control. Part IV then argues that the only way to fulfill this purpose is to interpret prejudgment interest rules dynamically and thus to characterize them as substantive for choice-of-law determinations. In conclusion, in order to fulfill the procedural purposes of reducing forum shopping and increasing settlements and judicial economy, courts need to consider prejudgment interest effects dynamically.

I. PREJUDGMENT INTEREST AND THE CHOICE-OF-LAW REVOLUTION

A. Prejudgment Interest

If justice were immediate, there would never be a need for an award of prejudgment interest because the injured party would instantly receive an enforceable judgment. The injured party would not suffer time value of money losses due to delay of payment.[15] Yet because justice often takes many years to achieve, the laws of most

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13 *Zaretsky v Molecular Biosystems, Inc*, 464 NW2d 546, 550 (Minn App 1990) (explaining the reasons behind characterizing prejudgment interest as procedural). This Comment focuses solely on the use of prejudgment interest in choice-of-law situations where courts apply another state's substantive law rather than their own. It does not consider how effective prejudgment interest rules are or whether courts should consider them substantive or procedural for any other purpose.

14 A static interpretation refers to a court's interpreting a rule or statute only in light of the case at hand. A dynamic interpretation occurs when a court interprets a rule or statute in light of the effect the ruling will have on the entire system and its future. Some statutes seem uniquely static because their main effect is for plaintiff compensation or efficient discovery. Even these rules, however, have dynamic components. How judges rule today may dictate future plaintiff compensation and discovery because of its precedential value. Likewise, other statutes seem uniquely dynamic in that they aim to protect the integrity of the court system, as opposed to individual parties in a suit.

15 Time value of money refers to the general notion that money is worth more now than later. This is based on the idea that we either get more enjoyment out of a comparable present pleasure or that we can take current money and receive interest on it such that we will have more money in the future. If justice were immediate, there would be no time for interest to accrue. See, for example, *Perry Drug Stores, Inc v Department of Treasury*, 229 Mich App 453, 582 NW2d 533, 536 n 4 (1998) (stating that the time value of money refers to the concept that "a dollar received today is worth more than a dollar to be received in the future").

American jurisdictions provide that prejudgment interest be calculated for the period between the time of the wrong and the date of the judgment.[16] This interest is then added to the damage award. Thus, prejudgment interest pressures a defendant to settle if the plaintiff has a strong case because if the defendant waits and the plaintiff wins at least as much as the defendant offered the plaintiff as a settlement then the defendant must pay interest on the full amount awarded.[17]

Prejudgment interest rules, which can be part of a state's civil procedure rules or general statutes, vary significantly between states.[18] Some prejudgment interest rules are mandatory, usually requiring the defendant to pay a percentage of the plaintiff's award, while others give a range and leave the exact percentage to the discretion of the trial judge.[19] The default percentage range is also quite large, beginning at 5 percent and extending to 20 percent, though most states defer to any contracted rate.[20] For example, Illinois's statutory rate is 5 percent,[21] whereas Texas's statutory rate is variable up to 20 percent.[22] With a $1 million verdict, this translates to a $150,000 difference per year, which could exert serious settlement pressure on the defendant. This creates a large incentive for the plaintiff to forum shop, especially given the fact that large civil trials rarely last less than a year.[23] Thus, prejudgment interest not only increases forum shopping and pressure to settle quickly, but plaintiffs may be able to request more for settlement because the extra burden of prejudgment interest is a credible threat.

Historically, courts and legislatures have viewed prejudgment interest as exploitative and thus an improper judicial remedy.[24] Recent trends in prejudgment interest law, however, suggest an increased willingness by state courts and legislatures to impose prejudgment interest.[25] Many states believe that courts need to be able to award prejudgment interest to expedite the resolution of disputes, help judges

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16 See *Prejudgment and Postjudgment Interest: A Fifty State Survey* § 1 (Vedder Price 1996) (comparing the prejudgment interest rules of all fifty states).

17 This is the general configuration of most states' prejudgment interest statutes. See id.

18 Interestingly, most prejudgment interest rules are statutes, not civil procedure rules. See id.

19 See id.

20 See id. Note that because most states enforce any contractual rates set by the parties these rates could theoretically be from 0 percent to 100 percent (or more), depending on the rate in the contract.

21 815 ILCS § 205/2 (West 1998).

22 Tex Rev Civ Stat Ann articles 5069-1.03, 5069-1.05 (West 2001).

23 See Theodore Eisenberg and Kevin M. Clermont, Federal District-Court Civil Trials Database, available online at <http://teddy.law.cornell.edu:8090/questtr2.htm> (visited Dec 7, 2001) (reporting average case duration, among other data).

24 See Charles L. Knapp, 1 *Commercial Damages* § 604[1] (Matthew Bender 1986).

25 See id at 6.04[2] (discussing the increased recognition of the importance of prejudgment interest by state courts and legislatures).

control their dockets, and compensate plaintiffs fully for their loss of use of the judgment money.[26]

B. Substantive/Procedural Distinction

Courts frequently provide two justifications for the additional liability of prejudgment interest: (1) the necessity to compensate ("make whole") the aggrieved plaintiff; and (2) the encouragement of prompt and equitable settlements.[27] Although state courts will often defer to choice-of-law provisions when adjudicating the substantive issues within a law,[28] the law of the forum usually governs matters of procedure.[29] The forum court decides whether to characterize given laws as substantive or procedural.[30] All courts recognize, however, that prejudgment interest rules have both substantive and procedural features, and that one rationale or the other may be more compelling depending on the legal context.[31] Rules granting prejudgment interest inherently serve both substantive and procedural purposes: promoting early settlement of claims and compensating the plaintiff for the inability to utilize funds that were rightly due earlier.[32]

This is true regardless of whether the legislature or courts officially list prejudgment interest rules as procedural or substantive.[33]

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26 Prejudgment interest easily serves all three purposes, and courts cite any or all of these purposes depending on the context. See, for example, *Paine Webber Jackson and Curtis, Inc v Winters*, 22 Conn App 640, 579 A2d 545, 553 (1990) (citing various purposes for prejudgment interest); *Laudenberger*, 436 A2d at 150–55 (same).

27 See, for example, *Royal Electric Construction Corp v Ohio State University*, 73 Ohio St 3d 110, 652 NE2d 687, 692 (1995) (noting that the state's prejudgment interest statute serves the dual purpose of providing compensation and promoting early settlements); *Rhode Island Turnpike & Bridge Authority v Bethlehem Steel Corp*, 446 A2d 752, 757 (RI 1982) (same).

28 See, for example, *Stonewall Insurance Co v Argonaut Insurance Co*, 75 F Supp 2d 893, 912 (N D Ill 1999) (looking first to the contract for a choice-of-law provision, but upon finding none looking to Illinois choice-of-law rules to determine which state's law governs prejudgment interest).

29 See, for example, *Zaretsky v Molecular Biosystems, Inc*, 464 NW2d 546, 548 (Minn App 1990) (stating the "well-settled rule . . . that matters of procedure . . . are governed by the law of the forum," even though the court may be adjudicating the case under the substantive law of another state).

30 Id, quoting Robert A. Leflar, Luther L. McDougal, III, and Robert L. Felix, *American Conflicts Law* § 121 at 333 (Michie 4th ed 1986) ("The court before which the question arises is the one that has to decide whether any rule of law, domestic or foreign, will be characterized as substantive or as procedural for choice-of-law purposes.").

31 See, for example, *Hanna v Plumer*, 380 US 460, 471 (1965) ("The line between 'substance' and 'procedure' shifts as the legal context changes. 'Each implies different variables depending upon the particular problem for which it is used.'"), quoting *Guaranty Trust Co v York*, 326 US 99, 108 (1945); *Zaretsky*, 464 NW2d at 548 (explaining that the substantive/procedural line is slippery).

32 See *Rhode Island Turnpike*, 446 A2d at 757 (delineating the potential substantive and procedural rationales for prejudgment interest statutes); *Laudenberger v Port Authority of Allegheny County*, 496 Pa 52, 436 A2d 147, 150–51 (1981) (same).

33 See, for example, *Zaretsky*, 464 NW2d at 550 (holding that although prejudgment inter-

Prejudgment interest does abridge, enlarge, or modify substantive rights by increasing damage awards, but it also promotes settlement and solves problems of congestion and delay, which are intrinsically procedural goals.[34]

The Second Restatement states that prejudgment interest is substantive for choice-of-law decisions, and thus that the law of the state under which the substantive legal issues are decided also "determines whether plaintiff can recover interest, and, if so, the rate" at which it may be recovered.[35] Courts, however, hotly contest the Second Restatement's substantive characterization.[36]

C. The Second Restatement and Governmental Interest Analysis

Earlier choice-of-law rules based on territorial analysis, including prejudgment interest, were relatively stable between 1834 (when Justice Story's treatise was published)[37] and 1962.[38] Territorial analysis meant determining the "rate of interest allowed as part of the damages . . . by the law of the place of performance."[39] Courts applied this rule by using the law where the parties performed (or were to perform) the contract, or where the tort occurred.[40] In response to critics and the multiple exceptions to the territorial rule,[41] the American Le-

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est is a substantive remedy, the payment of such damages is an effect of the procedural purposes of the statute, and therefore is procedural).

34 Compare *Laudenberger*, 436 A2d at 150–51 (stating that the state's prejudgment interest rule "clearly reflects a primary desire to encourage pre-trial settlement"), and *Zaretsky*, 464 NW2d at 548–50 (stating that the primary goal of the statute was "the procedural aim of unclogging the judicial machinery"), with *Morris v Watsco, Inc*, 385 Mass 672, 433 NE2d 886, 888–90 (1982) (describing these damages substantively as "a defendant's interest obligations," and a "plaintiff's right to interest as damages").

35 Restatement (Second) of Conflict of Laws § 207 comment e (1971). See also *Amoco Rocmount Co v Anschutz Corp*, 7 F3d 909, 920 (10th Cir 1993) (discussing comment e).

36 See note 5.

37 Joseph Story, *Commentaries on the Conflict of Laws* (Hilliard, Gray 1834).

38 See Patrick J. Borchers, *Courts and the Second Conflicts Restatement: Some Observations and an Empirical Note*, 56 Md L Rev 1232, 1232–33 (1997) (stating that the "conflicts revolution" began with the decision in *Babcock v Jackson*, 12 NY2d 473, 191 NE2d 279, 282 (1963)). Stability only indicates the lack of major changes, not that the policies were necessarily the best. A court first applied the Restatement (Second) in 1962, even though the ALI did not officially finish the Restatement (Second) until 1969. See *Babcock*, 191 NE2d at 282 (applying the Second Restatement's choice-of-law analysis).

39 Restatement of Conflict of Laws § 418 (1934).

40 See, for example, *Burlington Northern and Santa Fe Railway Co v Kansas City Southern Railway Co*, 73 F Supp 2d 1274, 1283 & n 3 (D Kan 1999) (analyzing and comparing the different outcomes possible under the First and Second Restatements' applications of prejudgment interest, but following the First Restatement's approach).

41 See David F. Cavers, *A Critique of the Choice-of-Law Problem*, 47 Harv L Rev 173, 180 (1933) (comparing the traditional methodology to a slot-machine that was programmed to select the applicable law in a "blindfold" fashion, based solely on territorial contacts and without regard to the content of the implicated laws). But see Erin A. O'Hara and Larry E. Ribstein, *From Politics to Efficiency in Choice of Law*, 67 U Chi L Rev 1151, 1184 (2000) (arguing that the First

gal Institute began drafting its Second Restatement of Conflict of Laws in 1952 and finished it in 1969.[42]

The ALI based the Second Restatement more on governmental interest than territorial contacts. Governmental interest analysis leads courts to interpret statutes and procedural rules in light of the governmental need they are supposed to fill. Though the Second Restatement specifically characterizes prejudgment interest as substantive,[43] governmental analysis has led many states to characterize their prejudgment interest statutes as procedural because of a focus on the settlement and judicial economy aspects of prejudgment interest.[44] At least half of the states follow the Second Restatement's view that prejudgment interest is substantive,[45] even if their rules originated from different sources.[46] Therefore, the Second Restatement's addition of interest analysis to states' decisionmaking arsenals, coupled with its determination that prejudgment interest be considered substantive, has led to a divergence among the states in the characterization of prejudgment interest.

Restatement's territorial analysis is "most likely to lead to efficient results because its clear rules promote predictability").

42 See W. Noel Keyes, *The Restatement (Second): Its Misleading Quality and a Proposal for Its Amelioration*, 13 Pepperdine L Rev 23, 37–41 (1985) (laying out the history of the Second Restatement); Willis L. M. Reese, *Conflict of Laws and the Restatement Second*, 28 L & Contemp Probs 679, 680–81 (1963) (same).

43 Restatement (Second) of Conflict of Laws § 207 comment e.

44 See, for example, *Laudenberger v Port Authority of Allegheny County*, 496 Pa 52, 436 A2d 147, 150–51 (1981) (focusing solely on the procedural aspects of Pennsylvania's prejudgment interest rule while admitting that it has substantive aspects).

45 See Symeon C. Symeonides, *The Judicial Acceptance of the Second Conflicts Restatement: A Mixed Blessing*, 56 Md L Rev 1248, 1264–69 (1997) (listing twenty-one jurisdictions that follow the Second Restatement in tort conflicts, twenty-five jurisdictions that follow it in contracts conflicts, twenty-eight jurisdictions that follow a "significant contacts" approach to conflicts in torts, and thirty that do so in contracts, and still additional jurisdictions that follow a "mixed" approach, relying partly on the Second Restatement in torts (six states) and contracts (ten states)). See also *Cooper v Ross & Roberts, Inc*, 505 A2d 1305, 1307 (Del Super 1986) (stating that the majority view among states is that "prejudgment interest, like the issue of damages, is substantive, and the state whose laws govern the substantive legal questions also governs the question of prejudgment interest").

46 See, for example, *Sorrels Steel Co, Inc v Great Southwest Corp*, 906 F2d 158, 167–68 (5th Cir 1990) (stating that the law chosen in the contract should govern prejudgment interest, provided that "the state law selected bears a reasonable relation to the transaction"), quoting *FMC Finance Corp v Murphree*, 632 F2d 413, 418 (5th Cir 1980). Only a handful of courts have fully endorsed the Second Restatement. See, for example, *Emerson Electric Co v Crawford & Co*, 963 SW2d 268, 272 (Mo App 1997); *Wang Laboratories, Inc v Lee*, 1989 Del Super LEXIS 173, *14–15; *Morris v Watsco, Inc*, 385 Mass 672, 433 NE2d 886, 889–90 (1982). But see *Schulhof v Northeast Cellulose, Inc*, 545 F Supp 1200, 1211 (D Mass 1982) (noting that although cases have fully endorsed the Second Restatement in transportation contracts, "it is not clear whether the law governing prejudgment interest automatically would follow that governing substantive issues under *Morris v Watsco, Inc*").

II. CURRENT STATE OF PREJUDGMENT INTEREST LAW

A. Federal Courts

Federal courts sitting in diversity and applying state law have resolved the procedural/substantive debate by choosing to use the prejudgment interest rule of the state in which they sit, not any federal rule.[47] These federal courts reason that, under the *Erie* doctrine,[48] state prejudgment interest rules concern substantive rights of the parties, and thus the state prejudgment interest law applies.[49] Federal courts usually rely on the Supreme Court's ruling in *Klaxon Co v Stentor Electric Manufacturing Co, Inc*[50] for the proposition that a "federal court sitting in diversity must apply the substantive law of the state in which it sits, including that state's choice-of-law rules."[51] The *Klaxon* Court, ruling that on issues of pre- and postjudgment interest state and federal courts should be in harmony, disallowed federal courts

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47 See *American Anodco, Inc v Reynolds Metals Co*, 743 F2d 417, 425 (6th Cir 1984) ("In diversity cases, federal courts follow state law on the question of prejudgment interest."). See also *Klaxon Co v Stentor Electric Manufacturing Co, Inc*, 313 US 487, 496 (1941) (holding that a federal court sitting in diversity must apply the substantive law of the state in which it sits, including that state's choice-of-law rules). Accordingly, federal courts have few rules regarding the conflict of laws, and those are used in federal jurisdiction cases only. See *Maddox v American Airlines, Inc*, 115 F Supp 2d 993, 995–96 (E D Ark 2000) (holding that since Arkansas was the forum in which the case was brought, the court must look to Arkansas's rules, which point to applying Oklahoma's prejudgment interest laws, but since Oklahoma characterizes prejudgment interest as procedural, Arkansas's choice-of-law rules dictate that the court should award no prejudgment interest). The *Maddox* court applied no form of federal prejudgment interest. Id. But when a district court sits in federal question jurisdiction, prejudgment interest has been determined by federal common law. See, for example, *Robinson v Watts Detective Agency, Inc*, 685 F2d 729, 741 (1st Cir 1982) (applying the federal prejudgment interest rule because the case involved no state law). Notwithstanding, if the underlying federal law is silent as to awarding prejudgment interest, a court may look to state law. See *Colon Velez v Puerto Rico Marine Management, Inc*, 957 F2d 933, 941 (1st Cir 1992) (applying the state prejudgment interest rule in a purely federal case).

48 See 304 US at 71–79 (holding that a federal court sitting under diversity jurisdiction must apply the law of the forum state to questions that are "substantive" but should use federal rules to govern questions that are "procedural"); *Simmons v Allstate Insurance Co*, 1997 US Dist LEXIS 10793, *3 (E D Pa) (applying *Erie* in prejudgment interest context). In *Klaxon*, 313 US at 487, the Supreme Court held that rules for ascertaining damages are "matters of substance" for *Erie* purposes. Likewise, in *Yohannon v Keene Corp*, 924 F2d 1255, 1267 (3d Cir 1991), the Third Circuit determined that prejudgment interest rules were "matters of substance" as far as *Erie* is concerned, following *Klaxon*'s damage ruling. Thus, federal courts sitting in diversity must examine prejudgment interest according to the state's laws in which they sit. See *Klaxon*, 313 US at 496. As with many issues, the problem is that prejudgment interest is somewhat "substantive" in that it is outcome-determinative. On choice-of-law issues, "all of the labels in *Erie* and its progeny seem to become logically non-determinative." *Yohannon*, 924 F2d at 1265.

49 See note 62.

50 313 US 487 (1941).

51 Id at 495–97. See also, *Burlington Northern and Santa Fe Railway Co v Kansas City Southern Railway Co*, 73 F Supp 2d 1274, 1283 (D Kan 1999) (applying Kansas's choice-of-law rules because that is where the court sits, even though the contract had a choice-of-law provision for Missouri law).

from making choice-of-law determinations that were independent of rulings from the states in which they sit.[52] The Supreme Court based its ruling on *Erie* concerns: "Otherwise, the accident of diversity of citizenship would constantly disturb equal administration of justice in coordinate state and federal courts sitting side by side."[53] *Klaxon* and *Erie* thus created vertical uniformity between federal and state courts within each state for choice-of-law and pre- and postjudgment interest decisions.[54] The Supreme Court in *Klaxon* recognized, however, that its decision might exacerbate the lack of horizontal uniformity that had resulted from differing administration of justice between states.[55]

B. State Courts

Not all states have authoritatively established whether their prejudgment interest rules are procedural or substantive.[56] In those "undecided" states, federal courts guess how they think state supreme courts will rule or certify the question directly to the state supreme courts.[57]

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52 313 US at 495–97.

53 Id at 496. See also *Erie*, 304 US at 74–77.

54 *Curran v Kwon*, 153 F3d 481, 488 (7th Cir 1998) ("A district court exercising jurisdiction because of the diversity of citizenship of the parties must apply the choice of law rules of the state in which it sits."). See also Restatement (Second) of Conflict of Laws § 207 comment e (stating that the issue of prejudgment interest is substantive, and thus the law of the state under which the substantive legal issues were decided also "determines whether plaintiff can recover interest, and, if so, the rate"). Federal courts first look to how the state in which they sit would rule when faced with a choice-of-law provision. See, for example, *Burlington Northern*, 73 F Supp 2d at 1283 (stating that since the court sits in Kansas, it "looks to Kansas choice of law rules to determine which state's law governs"); *Maddox*, 115 F Supp 2d at 994–95 (stating that since the plaintiff commenced the case in Arkansas, Arkansas was the forum and its choice-of-law rules would govern).

55 313 US at 496 (acknowledging that its ruling would hurt uniformity among federal courts by stating that "[w]hatever lack of uniformity this may produce between federal courts in different states is attributable to our federal system, which leaves to a state, within the limits permitted by the Constitution, the right to pursue local policies diverging from those of its neighbors"). Apparently, this is the price we pay for the benefits of our federal system. See also *International Insurance Co v Stonewall Insurance Co*, 86 F3d 601, 604–07 (6th Cir 1996) (discussing the dramatic differences in liability and prejudgment interest damages when adjudicating a tort claim under Ohio versus Louisiana law).

56 See, for example, *Contract Lodging Corp v Union Pacific Railroad*, 1991 US Dist LEXIS 18663, *8 (D Kan) (stating that "it is not clear whether Kansas considers prejudgment interest to be a matter of substantive or procedural law").

57 See, for example, *Alaska Airlines, Inc v United Airlines, Inc*, 902 F2d 1400, 1404–05 (9th Cir 1990) (certifying to the state supreme court the question of whether prejudgment interest is of such vital public policy importance that it can override a choice of law provision); *Burlington Northern and Santa Fe Railway Co v Kansas City Southern Railway Co*, 73 F Supp 2d 1274, 1283 (D Kan 1999) (determining that there was no authority in the Kansas court "resolving the issue as to what law governs the allowance of prejudgment interest as an element of damages for the breach of a contract" and thus trying to divine what Kansas courts would do based on other precedents).

1. Substantive prejudgment interest and the Restatement (Second) of Conflict of Laws.

The Restatement has embraced contractual choice-of-law clauses as a method for determining the substantive law to be applied to disputes between two parties.[58] The Restatement's position on interest as applied to a judgment for damages is straightforward and likely to promote certainty among parties to a contract: "The local law of the state selected by application of the rule of this Section determines whether plaintiff can recover interest, and, if so, the rate, upon damages awarded him for the period between the breach of contract and the rendition of judgment."[59] Thus, the Restatement argues that the substantive law which the parties to a contract chose or which the court applies to the parties under the "most significant relationship" test determines if prejudgment interest will be awarded in the case, and if so, how much.[60] Many states follow this reasoning and apply the chosen state's prejudgment interest rules because the law significantly affects the parties' substantive rights.[61] These states generally reason along *Erie* grounds: substantive prejudgment interest results in uniform outcomes for uniform cases, reduces forum shopping, and fulfills

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58 See Restatement (Second) of Conflict of Laws § 187 (stating that a court should rely on the law chosen by parties to adjudicate disputes sounding in contract; carving out two exceptions related to offensiveness to public policy and the minimum contacts with the selected jurisdiction).

59 Id at § 207 comment e.

60 See *Johnson v Continental Airlines Corp*, 964 F2d 1059, 1063–64 (10th Cir 1992) (holding that prejudgment interest is "an integral element of compensatory damages [and] is not subject to an independent choice-of-law analysis"); *Morris v Watsco, Inc*, 385 Mass 672, 433 NE2d 886, 890 (1982) (holding that "even where the parties have not agreed on the law which governs their rights, the better rule may be in all instances to turn to the law governing rights and duties under the contract to determine the interest payable for breach of contract"). But see *Burlington Northern*, 73 F Supp 2d at 1283 (applying Kansas's choice-of-law rules because that is where the court sits, even though the contract had a choice-of-law provision for Missouri law, on the grounds that "[a] federal court sitting in diversity must apply the substantive law of the state in which it sits, including that state's choice-of-law rules"); *Yohannon v Keene Corp*, 924 F2d 1255, 1264 (3d Cir 1991) (applying Pennsylvania's prejudgment interest rule because it is procedural even though the court decided the case under New Jersey law).

61 See, for example, *International Insurance Co v Stonewall Insurance Co*, 86 F3d 601, 604 (6th Cir 1996) ("Ohio has adopted the test set forth in the Restatement Second."); *Sorrels Steel Co, Inc v Great Southwest Corp*, 906 F2d 158, 167–68 (5th Cir 1990) ("Under Mississippi choice of law principles, a choice of law provision in a contract will govern the issue of prejudgment interest."); *Star Technologies v Philips Medical Systems, NA, Inc*, 23 Va App Cir 267, 269 (1991) (noting that, in Virginia, prejudgment interest serves to compensate the plaintiff and is therefore substantive); *Cooper v Ross & Roberts, Inc*, 505 A2d 1305, 1307 (Del Super 1986) (holding that "the state whose laws govern the substantive legal questions also govern the questions of prejudgment interest"). The majority view among states is that "prejudgment interest, like the issue of damages, is substantive, and the state whose laws govern the substantive legal questions also governs the question of prejudgment interest." Id. See also Restatement (Second) of Conflict of Laws § 207 comment e; note 51.

the parties' expectations.[62] Thus, these states think that the Second Restatement's position will "result in uniform interest payments, without regard to the [state or federal] forum selected."[63] The Massachusetts Supreme Court in *Morris v Watsco, Inc*[64] gave another reason for applying a substantive prejudgment interest rule to parties in contract: it accords with the parties' intent.[65] Some courts, however, are reluctant to follow the reasoning in *Morris*,[66] especially because Comment C to § 207 of the Restatement states that protecting the justified expectations of the parties "has little role to play with respect to the measure of damages."[67]

The courts that characterize prejudgment interest as substantive also generally defer to the state law chosen by the parties if they have specifically detailed prejudgment interest in the contract; otherwise they will look to the choice-of-law rules in the forum state to determine the availability of prejudgment interest.[68] This accords with parties' intentions and should not disrupt the adjudicating court.[69]

2. Procedural prejudgment interest.

At the other end of the spectrum are states that characterize their prejudgment interest laws as procedural, regardless of whether they are civil procedure rules (generally promulgated by the supreme court of the respective state) or substantive laws.[70] Although state courts will

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62 See, for example, *Morris*, 433 NE2d at 889–90 (noting that adjudicating all rights according to the substantive law chosen by the parties would decrease forum shopping and would result in uniform treatment regardless of the court or state chosen).

63 Id at 890 (arguing that "the better rule . . . in all instances [is] to turn to the law governing rights and duties under the contract to determine the interest payable for breach of contract").

64 385 Mass 672, 433 NE2d 886 (1982).

65 Id at 889 (stating that "the parties to the contract involved . . . intended that their rights should be determined by Florida law and that those rights include the determination of the damages, including interest, to be paid as a consequence of a breach of contract").

66 See, for example, *Schulhof v Northeast Cellulose, Inc*, 545 F Supp 1200, 1211 (D Mass 1982) (asking the parties to brief the court regarding "the law governing prejudgment interest" for later judgment because keeping with the parties' intentions was not sufficient justification for using the laws from the state which supplied the substantive law).

67 Restatement (Second) of Conflict of Laws § 207 comment c.

68 See, for example, *Mobilificio San Giacomo SpA v Stoffi*, 1998 WL 125536, *11 (D Del) (looking to the "law of the forum state for determining the availability of prejudgment interest" in a diversity case because the parties' agreement did not provide for prejudgment interest).

69 See id (implying that the court was simply following the parties' ex-ante intentions).

70 If a law is in the civil rules of procedure, rather than among substantive statutes, it may be telling for an analysis of whether it is procedural or substantive, but it is not determinative. See *Busik v Levine*, 63 NJ 351, 307 A2d 571, 577–79 (1973). As the New Jersey Supreme Court noted in *Busik*, "[I]t is simplistic to assume that all law is divided neatly between 'substance' and 'procedure.' A rule of procedure may have an impact upon the substantive result and be no less a rule of procedure on that account." Id at 578. Compare *Zaretsky v Molecular Biosystems, Inc*, 464 NW2d 546, 550 (Minn App 1990) (holding the Minnesota prejudgment interest statute proce-

often defer to contractual choice-of-law clauses when adjudicating the substantive issues within a law, courts have an incentive to make the prejudgment interest rule procedural because the law of the forum state usually governs matters of procedure.[71] Likewise, all courts recognize that prejudgment interest rules have both substantive and procedural features, and one rationale or the other may be more compelling depending on the legal context.[72]

Emphasis on the settlement and judicial economy functions of prejudgment interest, coupled with governmental interest analysis, has caused some state courts to characterize prejudgment interest as a component of procedural law.[73] For example, in *Paine Webber Jackson and Curtis, Inc v Winters*,[74] a Connecticut appellate court explicitly rejected the Second Restatement as applied to the state statute on prejudgment interest, ruling that "interest awarded under § 52-192a is unrelated to the underlying debt."[75] The court stated that prejudgment interest in Connecticut "is solely related to a defendant's rejection of an advantageous offer to settle before trial and his subsequent waste

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dural because it "is a substantive remedy for a new, litigant's wrong"), with *Maddox v American Airlines, Inc*, 115 F Supp 2d 993, 995 (E D Ark 2000) (holding in a diversity case brought in Arkansas that since Oklahoma's prejudgment interest statute is procedural, the court would apply no prejudgment interest), and *Paine Webber Jackson and Curtis, Inc v Winters*, 22 Conn App 640, 579 A2d 545, 551 (1990) (noting that New York has two prejudgment interest rules: one New York courts regard as substantive, and another they regard as procedural). Compare also *Yohannon v Keene Corp*, 924 F2d 1255, 1265–67 (3d Cir 1991) (holding that the Pennsylvania Supreme Court created Rule 238 of the Pennsylvania Rules of Civil Procedure, which provides for the award of prejudgment interest or "delay damages" in tort cases, to "encourage settlements and reduce a severe backlog of civil cases sounding in tort"; therefore it is procedural and courts should apply it in tort cases, even if the court applies another state's law on issues of liability and basic damages).

71 See, for example, *Zaretsky*, 464 NW2d at 548 ("[T]he well-settled rule is that matters of procedure and remedies are governed by the law of the forum.").

72 See, for example, id ("[T]he line between 'substance' and 'procedure' shifts as the legal context changes. Each implies different variables depending upon the particular problem for which it is used."), quoting *Hanna v Plumer*, 380 US 460, 471 (1965).

73 See, for example, *Zaretsky*, 464 NW2d at 550–51 (claiming that a prejudgment interest award is a substantive remedy for a new, litigant's wrong, which is inherently a matter for the state in which the parties are litigating the contract dispute); *Laudenberger v Port Authority of Allegheny County*, 496 Pa 52, 436 A2d 147, 150–51 (claiming that the Pennsylvania prejudgment interest rule was more procedural than substantive in response to a state constitutional claim that the prejudgment interest rule promulgated by the Pennsylvania Supreme Court under their authority to make procedural rules was unconstitutional because it was really a rule of substance in disguise). Both courts noted the possibly substantive nature of prejudgment interest rules. Because the Pennsylvania Supreme Court itself promulgates procedural rules, it amended the Pennsylvania prejudgment rule (Rule 238) to correct any potential constitutional problems that could possibly be found in the original version because the original version had a strict application against defendants whose actions had no relation to any delay in payment. See *Craig v Magee Memorial Rehabilitation Center*, 512 Pa 60, 515 A2d 1350, 1352–53 (1986) (discussing the changes that the Pennsylvania Supreme Court made to Rule 238).

74 579 A2d 545 (1990).

75 Id at 552.

of judicial resources."[76] The *Paine Webber* court also rejected an earlier ruling by a federal district court in Connecticut that the same statute was substantive.[77] According to the *Paine Webber* court, an analysis of the substantive/procedural distinction can vary depending on whether the two jurisdictions are state and federal as opposed to state and state, implying that more things are substantive for *Erie* purposes than for the forum state's procedural purposes.[78]

C. Summary: Horizontal Disuniformity

The combination of all these factors—state courts' differing characterizations of prejudgment interest, the different amounts and reasons for which courts award prejudgment interest in different states, and *Klaxon*'s further whittling away of any horizontal uniformity among federal courts in different states—has led to drastic differences in the outcomes available to plaintiffs depending on the state in which they bring their suits.[79] These are similar problems to those that the Supreme Court in *Erie* tried to avoid: forum shopping and different outcomes depending on the court in which the case is brought.[80] In all fairness, the Supreme Court minimized these concerns vertically between state and federal courts within the same state by mandating that the "substantive" law be the same.[81] But the United States's econ-

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[76] Id. See also *Zaretsky*, 464 NW2d at 549–50 (agreeing with the lower court's determination that features of prejudgment interest law were "more procedural than substantive"); *Fields v Volkswagen of America, Inc*, 1976 Okla 106, 555 P2d 48, 63 (1976) (ruling that a statute pertaining to interest on judgments is "procedural rather than substantive" and therefore courts can apply it retroactively).

[77] 579 A2d at 552–53 (holding that Connecticut's prejudgment interest statute "clearly creates a substantive statutory right in persons suing in the Connecticut courts"), distinguishing *Frenette v Vickery*, 522 F Supp 1098, 1099 (D Conn 1981). See also *Laudenberger*, 436 A2d at 154–55 (ruling that the prejudgment interest rule is procedural enough to justify the Pennsylvania Supreme Court's propagating it under its delegated authority to establish procedural rules).

[78] 579 A2d at 552–53 (noting that the court in *Frenette* clearly limited its ruling to the "*Erie* context"). Thus, federal courts in these contexts generally do two analyses: first, they decide whether a certain rule is "substantive" for *Erie* purposes, and then they decide whether the rule is "substantive" for choice-of-law purposes according to how the state in which they sit would decide the issue. See *Simmons v Allstate Insurance Co*, 1997 US Dist LEXIS 10793, *3–5 (E D Pa) (holding that even though prejudgment interest is substantive for *Erie* purposes, it is a procedural rule in Pennsylvania, so a federal court should apply Pennsylvania prejudgment interest even though the parties are adjudicating the case under New Jersey law).

[79] Compare, for example, the outcomes in *Maddox v American Airlines, Inc*, 115 F Supp 2d 993, 996 (E D Ark 2000), in which the plaintiff received no prejudgment interest (because of a combination of prejudgment interest rules, states' characterization of such, and the court's interpretation of its duty to look to state law under *Klaxon*), with the possibility of two different applicable state rules in *Paine Webber*, 579 A2d at 551–52 (stating that if prejudgment interest is not discretionary under either statute or for discretionary reasons "both statutes could apply").

[80] 304 US at 75–76.

[81] See *Klaxon*, 313 US at 496 (stating that federal courts should apply state law for anything that "would constantly disturb equal administration of justice in coordinate state and fed-

omy and mobility are such that the cost of bringing a lawsuit in another state may not be too much greater, and with possibilities of a much greater recovery or a quicker settlement, the benefits may easily outweigh the inconvenience and cost. The Supreme Court in *Klaxon* did not solve the game of forum shopping or different outcomes; it just changed the rules of the game.[82] In creating this vertical uniformity, the Supreme Court disrupted any horizontal uniformity that might have existed among federal courts and simply switched forums for forum shopping: plaintiffs now decide between states.[83] Because state laws differ, whenever the Supreme Court forces federal courts into being more like state courts (vertical uniformity), courts across state boundaries become more divergent (horizontal uniformity).[84]

Choice-of-law clauses in contracts and conflict of laws rules in states do not bring certainty as to how a case will be decided. The *Klaxon* rule forcing federal courts to follow the choice-of-law rules of the states in which they sit may have added some certainty between state and federal courts in the same state, but this certainty came at the cost of shifting the uncertainty to another forum. Plaintiffs still have roughly the same opportunity to choose favorable prejudgment interest law between different states (either state or federal courts) as they did between federal and state courts in the same state before *Erie*.[85] Because prejudgment interest can comprise large sums of

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eral courts sitting side by side"). Later holdings were not this strong and have somewhat whittled down this principle. See, for example, *Stewart Organization, Inc v Ricoh Corp*, 487 US 22, 28–32 (1988) (allowing some differences in quasi-substantive laws between state and federal courts sitting in the same state); *Burlington Northern Railroad Co v Woods*, 480 US 1, 8 (1987) (holding that a federal rule controlled the manner of imposing penalties because the procedural rule "affects only the process of enforcing litigants rights and not the rights themselves"); *Walker v Armco Steel Corp*, 446 US 740, 751–52 (1980) (stating that "there is no direct conflict between the Federal Rule and the state law," and therefore each rule controls "its own intended sphere of coverage"); *Hanna v Plumer*, 380 US 460, 473–74 (1965) (holding that a Federal Rule of Civil Procedure was valid and controlling when in conflict with a state rule).

82 Instead of choosing between federal or state courts within the same states, plaintiffs and defendants now choose between states. See Joseph W. Glannon, *Civil Procedure* 187–89 (Aspen 3d ed 1997) (giving examples to show how plaintiffs can still forum shop between states).

83 See text accompanying note 55 for the Supreme Court's acknowledgment that *Erie* and *Klaxon* would lead to horizontal disuniformity.

84 As long as state laws regarding prejudgment interest are different, forcing vertical uniformity must exacerbate the lack of horizontal uniformity between federal courts because they will essentially be applying the law of the state in which they sit. The only way to really combat this problem is to allow a uniform federal prejudgment interest rule or a uniform state prejudgment interest rule, such as that proposed by the Restatement (Second) of Conflict of Laws § 207 comment e, which would have all courts decide prejudgment interest according to the state's law under which the parties are adjudicating the contract or dispute.

85 The main point of *Erie* and *Klaxon* was to rid our system of forum shopping and different outcomes among courts sitting right next to each other in the same state. The Supreme Court in *Klaxon*, 313 US at 496, argued that the prohibition in *Erie* "against such independent determinations by the federal courts, extends to the field of conflicts of laws . . . [o]therwise, the accident of diversity of citizenship would constantly disturb equal administration of justice in coordinate

money,[86] differences between how states apply prejudgment interest rules may have a large impact on where many plaintiffs take their cases.[87] Plaintiffs trying to maximize their damages and settlement pressure logically will choose a state with a procedural prejudgment interest rule, and hope that the substantive law comes from a state with a substantive prejudgment interest rule.[88]

Note that this outcome may actually hurt those states that rely on their procedural rules, such as prejudgment interest, to decrease the demand on their court system: plaintiffs, when possible, will choose these states over their substantive sisters.[89] Thus, even though courts in their own states should be able to set the rules that promote early settlement of claims and make for more efficient courthouses, it appears that differences in prejudgment interest characterization may bring more uncertainty into our system, subvert parties' expectations, allow forum shopping and disparate outcomes, and end up hurting those states that are trying to protect themselves.

III. HORIZONTAL DISUNIFORMITY AND FORUM SHOPPING ILLUSTRATED

The following example shows how different characterizations of prejudgment interest encourage forum shopping and other problems that *Erie* tried to avoid: Two businesses, Π and Δ, make a contract with

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state and federal courts sitting side by side." This will inevitably eliminate some forum shopping and make it a bit more costly. Notwithstanding, many people and businesses have sufficient contacts in many states for jurisdiction and many major cities are located near state borders. Likewise, courts still give dramatically different rulings even though they sit "side by side" just because they are in different states. The Northeast and cities such as Kansas City are most susceptible to the "easy" forum shopping that *Erie* and its progeny tried to rid from our system. See also examples in Glannon, *Civil Procedure* at 189–202 (cited in note 82).

86 A brief survey of the variability of prejudgment interest statutes on the state level strongly suggests that calculations of this additional liability, holding the substantive law constant, can vary significantly. See *Prejudgment and Postjudgment Interest* § 1 (cited in note 16). When the parties or the court prolong the pretrial phase and the monetary stakes are high, a sophisticated defendant could rely on a declaratory judgment action to secure a forum that could ultimately limit the defendant's liability. Likewise, plaintiffs would certainly be interested in selecting a forum that can augment or preserve the value of a favorable judgment, assuming the issue of prejudgment interest was not a factor in the original choice-of-law clause.

87 See text accompanying notes 21–24.

88 This strategy could backfire, however, due to courts' general dislike for exploitation of the court system. See, for example, *Portwood v Ford Motor Co*, 183 Ill 2d 459, 701 NE2d 1102, 1104 (1998) (rejecting a rule of crossjurisdictional class action tolling because of the potential for exploitation of the Illinois court system).

89 The court in *Laudenberger v Port Authority of Allegheny County*, 496 Pa 52, 436 A2d 147, 150–51 (1981), explicitly held that Pennsylvania's prejudgment interest rule is procedural because the court intended it to "encourage pre-trial settlement" and "alleviate delay in the disposition of cases, thereby lessening congestion in the courts." Nonetheless, this policy may backfire if plaintiffs disproportionately choose Pennsylvania when the benefits of doing so outweigh the costs of adjudication in a more convenient state.

a choice-of-law provision stating that any adjudication will be done under Connecticut law regardless of who brings the case and where. Both businesses have sufficient contacts in at least three states for jurisdictional purposes: New York, Connecticut, and New Jersey. Nevertheless, the state courts differ in their characterizations of prejudgment interest: Connecticut's is procedural, New York has both a substantive and procedural prejudgment interest rule (though the procedural prejudgment rule is discretionary and courts generally do not apply it when they utilize the substantive rule), and New Jersey's is substantive.[90]

A year after the parties form the contract, Π thinks that Δ is not fulfilling the obligations of the bargain, so Π desires to take Δ to court for breach of contract. The outcome probably will be different in each state. If Π believes that there is a good chance that a prejudgment interest rule will either force early settlement or provide additional compensation if Π wins, in which state should Π bring the case? If Π brings the case in Connecticut, the state or federal court will, of course, use Connecticut law to adjudicate everything, including its procedural prejudgment interest rule. This is the normal, but uninteresting, case that the parties intended.[91]

If Π brings the case in New Jersey, however, Π loses the benefit of any prejudgment interest rule. New Jersey will apply the substantive law chosen by the contract (Connecticut's) and its own procedural rules, which do not include prejudgment interest. New Jersey would look to Connecticut's laws for a prejudgment interest rule, but would most likely not award any prejudgment interest upon finding that Connecticut courts characterize their prejudgment interest rule as procedural.[92] This hurts Π, helps Δ, and most likely subverts the inten-

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[90] Though simplified, this example roughly follows Connecticut, New York, and New Jersey's prejudgment interest rules. Compare *Paine Webber*, 579 A2d at 550–52 (ruling that Connecticut's offer of judgment rule is procedural and courts should apply it despite a determination that another state's law governs substantive issues; also noting that New York has two prejudgment interest rules: 52-192a, which New York regards as procedural because it provides an economic incentive for parties to settle disputes before trial, and CPLR § 5001, which New York regards as substantive), with *Busik v Levine*, 63 NJ 351, 307 A2d 571, 580 (1973) (stating in a plurality opinion that "in the context of conflict of laws, . . . 'damages' go to the substance" in New Jersey). *Paine Webber*, 579 A2d at 552, noted that in appropriate cases both Connecticut and New York's prejudgment rules could apply: "The defendant could owe interest as damages on the debt and then owe interest on the total amount based on his refusal to settle."

[91] If our goal as a society is to maximize social utility, we should construct a rule under which the intended outcome will occur most often. See O'Hara and Ribstein, 67 U Chi L Rev at 1152 (cited in note 41) (arguing that the most efficient choice-of-law system would fulfill parties' intents, thus maximizing parties' joint welfare).

[92] For an example of this result, see *Maddox v American Airlines, Inc*, 115 F Supp 2d 993, 995–96 (E D Ark 2000) (ruling that no prejudgment interest would apply to the damage award because Oklahoma characterizes its prejudgment interest rule as procedural and Arkansas does not have an applicable procedural rule).

tions of the contract in favor of Δ. Thus, if prejudgment interest is significant enough to make a difference in the case,[93] Π will not rationally choose New Jersey. It is possible that Δ may be able to move the case to New Jersey by way of venue and thus thwart any possibility of prejudgment interest, depending on whether the referring court considered prejudgment interest "outcome determinative."[94]

Finally, if Π brings the suit in New York, Π will have the benefit of that state's procedural prejudgment interest rule. Nonetheless, bringing the case in New York may still subvert the intentions of the parties because the rate of interest and the date from which it accrues often differ dramatically between states.[95] To summarize, if the case is brought in Connecticut, the court will adhere to the parties' expectations, in New Jersey, it will thwart the parties' expectations, and in New York, the court will fulfill or thwart the parties' intentions depending on how similar New York's prejudgment interest rule is to Connecticut's.[96]

Changing the hypothetical slightly, however, can easily cause a windfall for Π. Assume the same facts as above, except that this time the contract lists New Jersey's as the state law under which the contract should be decided. If Π brings the suit in a New Jersey court, the court will apply New Jersey law, corresponding to the parties' expectations. On the other hand, if Π brings the case in Connecticut, Δ may feel the pressure of both New Jersey's substantive prejudgment rule

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93 Prejudgment interest is important for at least two reasons. First, plaintiffs' potential upside on 5–20 percent interest on any sizeable judgment will be quite large. Second, states and courts obviously believe that the imposition of prejudgment interest will serve as a sufficient economic incentive to settle early. See note 3.

94 Change of venue only could occur if the case were in federal court and then only under the rules prescribed in 28 USC § 1404(a) (1994). See, for example, *Van Dusen v Barrack*, 376 US 612, 616–24 (1964) (discussing ways in which a party may move a case due to improper venue). Whether a court transfers a case under 28 USC § 1404(a) depends on many issues, generally practical, such as where the parties prepared the contract, where the contracted duties took place (or should have taken place), where evidence in the case is located, where the witnesses reside, etc. 28 USC § 1391 (1994).

95 See *Prejudgment and Postjudgment Interest* § 1 (cited in note 16). Though the difference between New York's prejudgment interest rate (9 percent) and Connecticut's prejudgment interest rate (up to 12 percent) is not large, it is significant. Furthermore, the difference could be as high as 15 percent, depending on the states involved. See text accompanying notes 21 and 22.

96 Applying another state's prejudgment interest rule may not subvert parties' intentions because if they truly relied on a state's prejudgment interest rule, they would probably put it in the contract. This assumption is true, however, only if the parties know that Connecticut courts may not apply its prejudgment interest rule and the other potential possibilities, such as the courts applying no prejudgment interest. It seems somewhat implausible that even sophisticated parties will know the intricacies and possibilities of all the rules of the state they choose and the potential pitfalls from differing prejudgment interest rules. The parties may not have contemplated that a court would not apply all of Connecticut's rules that would have a substantial bearing to the outcome of a lawsuit.

and Connecticut's procedural prejudgment rule.[97] This pressure may be very substantial if both Connecticut's procedural and New Jersey's substantive rules are mandatory. This could lead to greater than optimal settlement pressure, as well as to too much compensation for Π. The outcome also would thwart the intentions of the parties who, by choosing New Jersey as the state under which the contract should be decided, knew exactly what substantive statute (they thought) would be applied to any possible case.[98] Of course, Δ could still try to change the venue back to New Jersey.[99]

Finally, if Π chose to bring the case in New York, uncertainty exists as to which forum would be superior. New York may choose to apply only New Jersey's prejudgment rule because applying only one prejudgment rule is what it normally does in its own cases. It may also apply both prejudgment interest rules for many reasons: it thinks New Jersey's interest rate is too low, or the case was too long, or the parties should have settled, and so on. Regardless, Δ probably will feel more pressure from the beginning of the case to settle because of this uncertainty, which may very well change the outcome of the case.[100]

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97 For a discussion of the possibility of two different state prejudgment interest rules applying to a single case, see *Paine Webber*, 579 A2d at 550–52 (explaining that if a court is applying another state's law with a nondiscretionary substantive prejudgment interest rule and the court also has a nondiscretionary procedural prejudgment interest rule, then "both [states'] statutes could apply"). This could conceivably occur even if one or both rules were discretionary if the court thought it had good cause. As *Paine Webber* notes, the application of two prejudgment statutes is very possible. Id. Thus, there is a real possibility that a defendant will pay both a substantive and a procedural prejudgment interest, if a state with a procedural prejudgment interest rule decides a case based on the substantive laws of a state with a substantive prejudgment interest rule.

98 This seems like an even stronger case for disrupted intentions because the prejudgment rule is substantive. Granted, if the parties were sophisticated businesses and knew of the prejudgment interest laws' state of disarray, then they may have taken into consideration the fact that a court may adjudicate their case in a state that characterized their prejudgment interest as procedural, which could lead to the defendant having to pay double interest or feeling excessive settlement pressure. Nonetheless, it seems unlikely that even two sophisticated businesses could consider all the different states in which a suit could be brought against them and all the different laws which may be different or differently applied. This bad result is exactly why parties include a choice-of-law provision.

99 See note 95 for change of venue rules.

100 As shown in this example, legislatures and courts intend prejudgment interest rules to enhance settlement pressure and be "outcome-determinative," even though they are often considered procedural. As the Pennsylvania Supreme Court explained, quoting the Civil Procedure Rules Committee, "Statistics show that . . . [t]hirty-eight percent [of cases] are settled without going to trial . . . but in too many cases meaningful negotiations commence only after a trial date is fixed or on the courthouse steps or in the courtroom, thus leading to delay in the disposition of cases and congestion in the courts. [A system without prejudgment interest] provides no incentive for early settlement. [There is currently] no compensation to the successful plaintiff and no sanction against the defendant for the long delay between commencement of the action and the trial." *Laudenberger v Port Authority of Allegheny County*, 496 Pa 52, 436 A2d 147, 150–51 (1981), citing 8 Pa Bulletin 2668 (1978).

IV. SOLUTION: DYNAMIC EFFICIENCY TO HORIZONTAL UNIFORMITY

Governmental interest analysis, coupled with a focused, static view of prejudgment interest, has not only led to horizontal disuniformity—it has not fulfilled its own procedural aims. A dynamic approach, by contrast, however, would both fulfill the procedural purposes of prejudgment interest and create more horizontal uniformity, leading to less forum shopping.

A. The Traditional Approach: Static Reading of Purpose and the Procedural Conundrum

Ever since Brainerd Currie introduced governmental interest analysis into choice-of-law situations,[101] state legislatures and courts have deemphasized predictability and forum shopping prevention goals in favor of the more important policy objectives of state governments.[102] However, if governmental interest analysis undermines predictability and introduces arbitrariness and inconsistency into the legal system, then it also undermines the rule of law itself, for the rule of law is based on nonarbitrariness.[103]

A static view of governmental interest and a focus on the specific case at hand have led state courts to characterize their prejudgment interest rules as procedural.[104] The stated purposes of states that characterize their prejudgment interest rules as procedural include "unclogging the judicial machinery," "encourag[ing] settlement," and "reducing the number of cases actually going to trial."[105] These statutes usually have features of prejudgment interest law that distinctively advance the interests of judicial economy rather than victim compensation. This static view of prejudgment interest, intended for judicial efficiency or to decrease the caseload, is likely to have just the opposite effect in a multistate system where parties can choose the most advantageous forum.[106] Returning to the first example,[107] since the con-

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101 See Brainerd Currie, *Survival of Actions: Adjudication versus Automation in the Conflict of Laws*, in *Selected Essays in the Conflict of Laws* 128, 168 (Duke 1963) (proposing that forum shopping may be "too broadly condemned" because if parties had more freedom to forum shop then this may in fact lead to fewer conflicts of interest between states).

102 Id at 169 (suggesting that this approach would induce plaintiffs to minimize conflict and "avoid the necessity of one state's striking down the interest of another").

103 See Ralph U. Whitten, *Commentary: Curing the Deficiencies of the Conflicts Revolution: A Proposal for National Legislation on Choice of Law, Jurisdiction, and Judgments*, 37 Willamette L Rev 259, 263–64 (2001) (discussing how governmental interest analysis has undermined the rule of law and proposing a national solution to choice-of-law issues).

104 See note 71.

105 See, for example, *Zaretsky v Molecular Biosystems, Inc*, 464 NW2d 546, 550 (Minn App 1990).

106 It is increasingly probable that many states will have jurisdiction over most parties be-

tract lists Connecticut as the state law under which the contract should be adjudicated, Π rationally will choose Connecticut in which to sue, unless New York's procedural prejudgment interest rule is stronger. In the modified example,[108] in which the contract lists New Jersey as the state law under which the contract should be adjudicated, Π rationally will choose to sue in Connecticut, unless New York's procedural prejudgment interest rule is stronger.

Finally, if we add one more iteration and assume that the parties wrote the contract to be adjudicated under New York law, then Π rationally will choose either New York or Connecticut, depending on which prejudgment interest statute provides more incentive to settle.[109] Thus, procedural prejudgment interest rules such as those in Connecticut and New York, whose purpose is to reduce the number of cases in the system, may actually increase the number of cases because these states become magnets to plaintiffs. States that characterize their prejudgment interest statutes as substantive, such as New Jersey, should receive fewer cases and thus lower their caseloads—the exact scenario that states with procedural prejudgment interest characterizations were trying to create.

The total number of cases in states with procedural prejudgment interest rules may not increase due to forum shopping if all of the "extra" cases settle. This, however, seems unrealistic. Even if the cases did settle, procedural states may still face a dramatic increase in lower courts' workloads because judges or other administrative staff are often involved in settlement agreements.

Defendants have just as much interest in selecting the proper forum and thus may try to locate the trial in a similarly favorable state. The rules governing venue changes, however, are much stricter and permission for such switches is much more difficult to obtain. Further, our court system has a history of and preference for allowing a plaintiff to choose whatever forum best suits her, as long as the forum has personal jurisdiction.

If state courts take a static view when they interpret the purposes of their prejudgment interest statutes and only apply the governmental interest analysis to the case at hand, they are likely to miss the true effects of prejudgment interest. This static view of prejudgment interest may undermine the stated procedural purposes for prejudgment interest. Different state characterizations of prejudgment interest lead

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cause of the mobility of today's society and the interstate, if not international, nature of many businesses.

107 See text accompanying notes 90–96.

108 See text accompanying notes 97–99.

109 In fact, Π probably will choose Connecticut because of the possibility of receiving both a procedural and substantive prejudgment interest award.

to disuniformity among the states and exacerbate both unpredictability and forum shopping,[110] which may in turn lead to an increase in a state's caseload and a decrease in judicial efficiency. Thus, a state trying to protect itself by characterizing its prejudgment interest rule as procedural may impede its own purposes.[111]

B. Dynamic Reading of Purpose: Prejudgment Interest Rule as a Substantive Rule in Choice-of-Law Situations

The solution to this conundrum is not for a judge to defy the purposes of her state's prejudgment interest rule, but to recognize its procedural purpose statically *and* dynamically. A judge must realize that legislatures and courts established prejudgment interest for the dynamic efficiency and case control of the whole system, not solely for the case at hand.

If the purposes of prejudgment interest is to decrease caseloads, then this purpose is by its nature applicable to the whole system (that is, dynamic) and not just the case at hand. Courts cannot fulfill these purposes by detaching themselves from the judicial system and focusing on the case before them. Thus, when a judge looks at one case and decides whether prejudgment interest attaches, the judge must consider the implications of the decision for the entire judicial system. A court can best realize the dynamic purposes of procedural prejudgment interest by (1) applying its own prejudgment interest rule, whether procedural or substantive, in domestically controlled cases, (2) applying the prejudgment interest rule of the state law selected in a contract, and (3) applying the prejudgment interest rule of the state chosen by the state's choice-of-law determination in all other cases. This is especially true when there is a large discrepancy in states' prejudgment interest rules, because a party has more incentive to forum shop when there is a significant discrepancy between the forum state's own prejudgment interest rule and the prejudgment interest rule of the state under whose law the case is being adjudicated.

Once a state that characterizes its prejudgment rules as procedural has established a reputation for applying prejudgment interest as if it were substantive, plaintiffs and defendants will not have incentives to forum shop that state, and the caseload subsequently should

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[110] See Whitten, 37 Willamette L Rev at 263–78 (cited in note 103) (discussing the various approaches states have taken to conflict of laws and concluding that every approach allowed enough manipulation by states so as to create disuniformity even though states appeared to adopt the rule uniformly).

[111] States impede their own procedural purposes due to the dynamic effects of prejudgment interest only in choice-of-law situations. A state with a procedural prejudgment interest statute very well may lower its total caseload and increase judicial efficiency in the domestic realm. This would only occur if the effect on domestic cases is larger than the increase from forum shopping.

fall. This solution does not just acknowledge governmental interest analysis, but actually exalts it by furthering the state's interest while also having a beneficial effect on uniformity, predictability, and forum shopping. It accomplishes both a state's goal of limiting its caseload and the *Erie* goals of limiting forum shopping and uncertainty. The solution should also not upset parties' expectations and will make contracting more efficient.[112]

Additionally, a dynamic reading of prejudgment interest also would not infringe excessively on states' prerogative to make their own procedural rules and it should have favorable judicial efficiency effects on state court systems. First, this solution would leave intact our federalist system, allowing states to promulgate whatever prejudgment interest rules they desire. A judicial determination that prejudgment interest rules are substantive for choice-of-law decisions will not disrupt a state's flexibility to classify prejudgment interest rules as procedural or substantive for domestic cases. Divergence among states as to rates and the situations in which prejudgment interest applies will still exist, but this type of diversity is either the benefit of or the price to be paid for our multi-state system. Second, this judicial gap-filling in choice-of-law situations would only limit the application of prejudgment interest rules in cases in which another state law applies, thus decreasing judicial caseload by limiting forum shopping. This solution would not, of course, prevent all forum shopping, but it would eliminate one of the sources. Third, parties will still feel some settlement pressure from prejudgment interest in cases adjudicated under another state's laws, because all states have prejudgment interest rules. Finally, this solution would remove any need for national legislative solutions, which have been proposed.[113]

One may worry that this proposal would lessen defendants' pressure to settle and limit a state's choice to characterize its prejudgment rules as procedural. This proposal admittedly would lessen a defendant's settlement pressure, but generally only in those situations in which a plaintiff forum shopped into a state that characterizes its prejudgment interest rule as procedural. If the state held that its prejudgment interest rule should follow the substantive law in choice-of-law cases, then the plaintiff would not have forum shopped into that state initially and the state need not worry about any extra settlement pressure. The second concern is not necessarily true. A holding that prejudgment interest follows the substantive law in choice-of-law

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112 See the related discussion in O'Hara and Ribstein, 67 U Chi L Rev at 1184–97 (cited in note 41) (discussing how choice-of-law decisions in courts should promote efficiency by upholding parties' expectations).

113 See, for example, Whitten, 37 Willamette L Rev at 285–90 (cited in note 103) (discussing proposals for "uniform national conflicts rules in the multistate commercial context").

situations could be limited to the choice-of-law subset of situations. Moreover, simply because procedural matters generally are governed by the law of the forum state does not mean that they all must be.[114] A state could determine that procedural prejudgment interest follows the substantive state in choice-of-law cases, but remains a procedural rule. This characterization is within the state's prerogative,[115] and it would allow courts to keep the benefits from characterizing their rules as procedural, such as retroactivity or Supreme Court authorship.[116]

CONCLUSION

States enact prejudgment interest statutes for both substantive and procedural justifications: (1) achieving full compensation of the aggrieved plaintiff and (2) improving judicial efficiency by encouraging settlements and thereby reducing a court's caseload. In the choice-of-law context, however, state courts differ as to which rationale dominates. This leads to horizontal disuniformity and forum shopping between states. In addition, the Supreme Court's ruling in *Klaxon* held that federal courts must use choice-of-law decisions from the states in which they sit, which increased vertical uniformity but simply switched forum shopping between state and federal courts sitting in the same state to shopping between courts in different states. The potentially large awards courts give under prejudgment interest rules generate increased pressure on defendants to settle. Ironically, the forum shopping created by the divergence in interpretation of prejudgment interest ends up hurting those states that focus on the procedural aspects of caseload control and judicial efficiency because plaintiffs forum shop into their court system.

This Comment offers a consistent way to end forum shopping and unequal treatment, while maintaining a state's control over its procedural rules. Courts should interpret prejudgment interest rules dynamically, as opposed to statically, or on a case-by-case basis. A dynamic interpretation and the subsequent ruling that prejudgment interest follow the substantive law, if only for choice-of-law decisions, will further the procedural goal of increasing judicial efficiency by

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114 *Zaretsky v Molecular Biosystems, Inc*, 464 NW2d 546, 548 (Minn App 1990) (stating that choice-of-law determinations are made on an issue-by-issue basis depending on whether the law is more procedural or substantive).

115 See, for example, *Davis v Furlong*, 328 NW2d 150, 153 (Minn 1983) ("In Minnesota, the well-settled rule is that matters of procedure and remedies are governed by the law of the forum.").

116 State supreme courts generally can only prescribe procedural rules. See, for example Pa Const Art V, § 10(c) (stating that the Supreme Court of Pennsylvania is empowered to "prescribe general rules governing practice, procedure and the conduct of all courts . . . if such rules are consistent with this Constitution and neither abridge, enlarge nor modify the substantive rights of any litigant").

lessening the caseload. Plaintiffs then will have no prejudgment interest incentive to forum shop into any particular state. For potential parties, this proposal will add more certainty to cases and fulfill parties' expectations. For the state, this dynamic characterization of procedural prejudgment interest rules will lead to less forum shipping and less horizontal disuniformity, and will also fulfill the governmental interest in having the prejudgment interest rule.