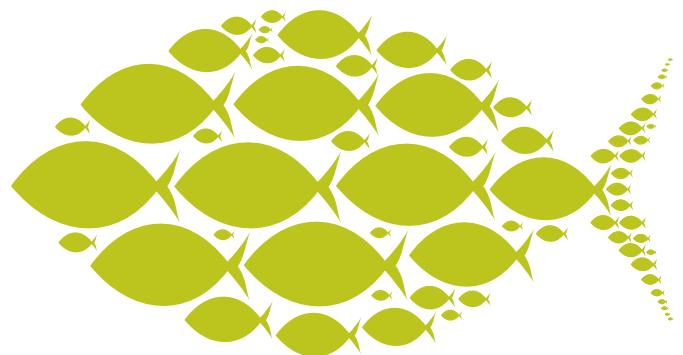
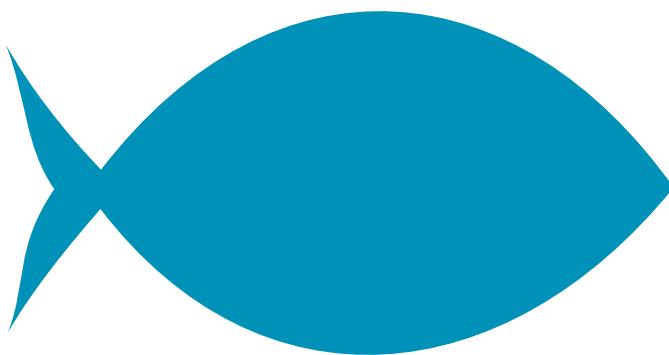


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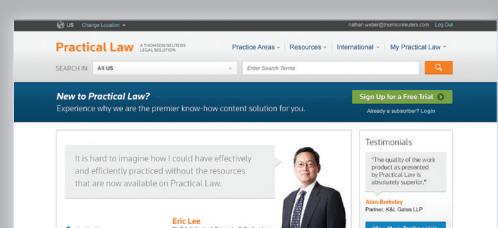
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Settling Class Actions

Process and Procedure

Parties to a class action settlement and their counsel must observe certain procedures to gain court approval and withstand heightened public scrutiny.

“**C**lass-action settlements are different from other settlements.” With these words, the US Court of Appeals for the Sixth Circuit began an August 2013 opinion in which it rejected a class action settlement that had been approved by the district court. (*Greenberg v. Procter & Gamble Co. (In re Dry Max Pampers Litig.)*, No. 11-4156, 2013 WL 3957060, at *1 (6th Cir. Aug. 2, 2013)).

The Sixth Circuit explained that, in contrast to ordinary settlements, class action settlements affect not only the interests of the parties and counsel who negotiate them, but also the interests of unnamed class members who are not present during the negotiations. Therefore, there is a danger that the parties and counsel will bargain away the interests of unnamed class members to maximize their own. (*In re Dry*

Max Pampers Litig., 2013 WL 3957060, at *1.) It is for these reasons that, unlike settlements in ordinary suits, the court must approve a class action settlement to ensure that the proposed settlement is fair, reasonable and adequate (*Federal Rule of Civil Procedure (FRCP) 23(e)*).

In making the required fairness determination, a court considers not only the terms of the proposed settlement agreement, but also the negotiating process leading up to the settlement. These negotiations frequently involve multiple parties and law firms struggling to satisfy competing interests. A fair settlement takes into account both the defendant’s incentive to minimize total settlement compensation and the plaintiffs’ inherent conflict when facing a limited amount of compensation available for class members that must be further diminished by contingent attorneys’ fees.

Author

GREGORY A. MARKEL

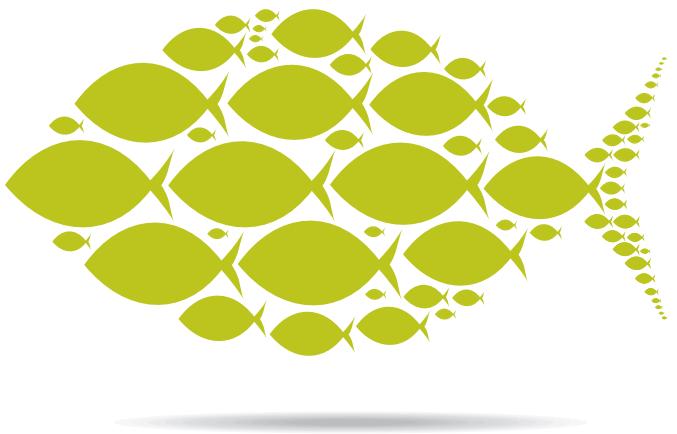
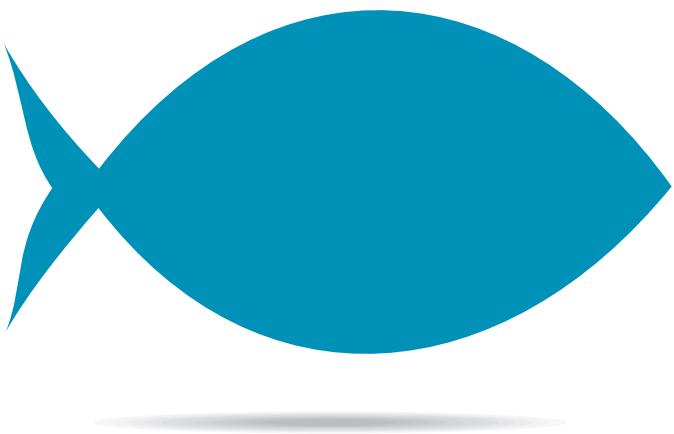


PARTNER

CADWALADER,
WICKERSHAM & TAFT LLP

Greg is the Co-Chairman of the firm's Litigation Department and a member of the Management Committee. He has extensive experience in class action

litigation, including securities, merger and acquisition, antitrust, ERISA and consumer class actions. He also has been involved in many other types of complex cases, including contract, corporate governance, corporate control, director and officer liability, RICO, antitrust, accounting and banking litigation.



Adding to the complexities surrounding class action settlements is the recent emergence of "professional" or "serial" objectors, who can delay and jeopardize settlements. In particular, these objectors (often represented by outside attorneys or public interest groups) have been scrutinizing the amount and proportion of attorneys' fees and the use of *cy pres* awards, in which unclaimed funds are directed to a charitable organization.

Despite these complications and differing interests, a very high percentage of class actions do ultimately settle. This article examines:

- The rules governing class action settlements.
- The timing of a class action settlement and significance of class certification.

- The settlement approval process.
- The confidentiality concerns involved in filing a proposed settlement agreement.
- The court's discretion to grant an additional opt-out period.
- The common grounds for objecting to a settlement and strategies for dealing with objectors.
- The use of *cy pres* awards.
- The distribution of settlement funds to claimants.



Search [Class Actions](#) for additional resources on class action litigation.

RULES GOVERNING CLASS ACTION SETTLEMENTS

FRCP 23 governs class actions generally and subsection (e) governs class action settlements. FRCP 23(e) was amended in 2003 to strengthen the process of reviewing proposed class action settlements. While recognizing that these settlements are desirable, the amendment reflects the view that court review and approval are essential to assure adequate representation of absent class members who have not participated in shaping the settlement (*FRCP 23(e) 2003 advisory committee's note*).

In considering whether a class action settlement is fair, reasonable and adequate, a trial judge must apprise herself of all facts necessary for an intelligent and objective opinion of the probabilities of ultimate success should the class action be fully litigated. The court should not go so far as to effectively conduct a trial on the merits, but should make findings of fact and conclusions of law whenever the propriety of the settlement is seriously in dispute. (*In re Initial Pub. Offering Sec. Litig.*, 226 F.R.D. 186, 189-90 (S.D.N.Y. 2005).)

In addition to requiring court approval of a class action settlement, FRCP 23(e) sets out five subsections crafted to:

- Assure notice to class members of a proposed settlement.
- Avoid collusion.
- Allow for class members to opt out.

(See *FRCP 23(e)(1)-(5)*.)

The Class Action Fairness Act of 2005 (CAFA) also contains provisions related to class action settlements. These include certain notice requirements and rules concerning the calculation of attorneys' fees in connection with coupon settlements. (See 28 U.S.C. §§ 1712-1715.)



Search [Class Action Fairness Act of 2005](#) for more on CAFA's effect on class action settlements.

TIMING OF A CLASS ACTION SETTLEMENT

A settlement can occur before or after the court has certified the case as a class action. The timing of a settlement has important implications for whether the court has to approve the settlement and who will be bound by its terms.

PRE-CERTIFICATION SETTLEMENTS

Prior to formal class certification, a class action can be settled as an individual action or, most commonly, by using a class certified for settlement purposes.

Individual Action

A complaint purporting to be a class action complaint can be settled as an individual action between the named plaintiff

and the defendant, before class certification. This approach avoids the need for court approval because the lead plaintiff is in effect agreeing to convert the case from a class action to an individual action. However, any release in an individual settlement would not be binding on a class or anyone not a party to the settlement.



Search [Genesis Healthcare Corp. v. Symczyk](#) for more on settlement offers of full relief to a lead plaintiff.

Settlement Class

If the parties agree on a settlement amount, they may ask a court to certify a specified settlement class and postpone formal class certification until after settlement negotiations have ended. In this case, the court must approve the fairness of the settlement terms because the settlement would bind absent class members.

The use of a settlement class allows the parties to concede, for purposes of settlement negotiations only, the propriety of bringing the suit as a class action. A settlement class must meet all the requirements of FRCP 23, with one important exception. Because the case will never go to trial, the court does not need to consider the manageability of class action proceedings. Therefore, a court may approve a settlement class that is broader than the class it would approve if there were no settlement.



Search [How Defendants Can Use Class Certification to Their Advantage](#) for more on the class certification process.

When a settlement class is proposed, the specifications of FRCP 23 demand undiluted, even heightened, attention by the court (see *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 620 (1997); accord *Rodriguez v. Nat'l City Bank*, No. 11-cv-8079, 2013 WL 4046385, at *4 (3d Cir. Aug. 12, 2013)). Several circuits have held that when the settlement for the entire class takes place before formal class certification, approval requires a higher standard of fairness, in addition to the baseline judicial finding that the settlement is fair, reasonable and adequate (see *Lane v. Facebook, Inc.*, 696 F.3d 811, 819 (9th Cir. 2012) (citing *Hanlon v. Chrysler Corp.*, 150 F.3d 1011, 1026 (9th Cir. 1998))).

Certain types of inequities under these circumstances would make the settlement unfair and subject to objection, and may cause the settlement to be rejected. Acting as a protector of the class, the court should:

- Monitor for collusion, improper buy-offs and the like (*In re Gen. Motors Corp. Pick-Up Truck Fuel Tank Prods. Liab. Litig.*, 55 F.3d 768, 787 (3d Cir. 1995)).
- Determine if the settlement gives "preferential treatment to the named plaintiffs while only perfunctory relief to unnamed class members" (*In re Dry Max Pampers Litig.*, 2013 WL 3957060, at *3).

- Ensure that class counsel does not receive a disproportionate benefit compared to unnamed class members (*In re Dry Max Pampers Litig.*, 2013 WL 3957060, at *3).

The court should also ensure that the definition of “settlement class” is reasonable. The more encompassing the class, the greater the total compensation must be to qualify as adequate. Additionally, broad class definitions can raise practical issues concerning notice (see below *Notice to the Class*).

POST-CERTIFICATION SETTLEMENTS

Post-certification settlements face far fewer unknowns because the size and scope of the class are already established. Because the size of the class is not conditional, the negotiation of the settlement is done with one less variable. As a result, post-certification settlements are somewhat more likely to obtain court approval, particularly where a class is certified long before a settlement is reached (see *In re PaineWebber Ltd. P'ships Litig.*, 171 F.R.D. 104, 122 (S.D.N.Y.), aff'd, 117 F.3d 721 (2d Cir. 1997)).

After class certification, the plaintiffs' bargaining position for settlement purposes may be improved because both the likelihood of a trial and the defendant's exposure to potential liability are greater. Notably, after class certification, a settlement with an individual plaintiff may be permitted by the court, but ultimately would not diminish the defendant's exposure to the rest of the class (*In re Shell Oil Refinery*, 152 F.R.D. 526, 535-36 (E.D. La. 1989)).

SETTLEMENT APPROVAL PROCESS

The process for obtaining court approval of a settlement can be broken down into three key stages:

- The preliminary approval hearing.
- The notice period.
- The final approval and fairness hearing.

PRELIMINARY APPROVAL HEARING

Once a class action settlement is negotiated and agreed on, the parties must make a motion to the court asking for preliminary approval of the settlement. In some cases, the settlement class certification hearing and preliminary approval hearing can be combined. At the preliminary approval hearing, the court reviews the proposed settlement terms and makes an initial determination as to whether they are fair, reasonable and adequate. (See *Manual for Complex Litig.* (Fourth) § 21.632 (2004).)

Preliminary approval is granted where the proposed settlement:

- Appears to be the product of serious, informed and non-collusive negotiations.
- Has no obvious deficiencies.

- Does not improperly grant preferential treatment to class representatives or segments of the class.
- Falls within the range of possible approval.

(*In re Nasdaq Market-Makers Antitrust Litig.*, 176 F.R.D. 99, 102 (S.D.N.Y. 1997) (citing *Manual for Complex Litig.* (Third) § 30.41 (1995)).)

If the court grants preliminary approval, it will direct the preparation of notice to proposed class members. Requiring preliminary approval before notice avoids providing unnecessary notice to the class of a settlement which the court may find unacceptable.

NOTICE TO THE CLASS

FRCP 23(e)(1) requires notice in a reasonable manner to all class members who would be bound by a proposed settlement. Additionally, CAFA requires notice to certain government officials (see 28 U.S.C. § 1715).



Search [Class Action Fairness Act of 2005](#) for more on CAFA's settlement requirements.

Depending on the size of the class and the information available about potential members, providing notice can be quite complex and expensive. The parties usually specify in the settlement agreement how they will allocate the cost of settlement notices. Costs are often assessed to the defendant or against a fund created by the defendant. The court usually directs class counsel or their agents (claims administrators, notice agents or both) to distribute the notice to the class members and help ensure informed election of, or exclusion from, class membership.

Reasonableness Standard

The standard for reasonable notice has been interpreted to include efforts that:

- Are calculated to reach class members.
- Convey all required information.
- Permit a reasonable amount of time to respond.

(*Mullane v. Cent. Hanover Bank & Trust Co.*, 339 U.S. 306, 314 (1950).)

Direct notice to class members (for example, through the mail) is generally required, where practicable. Posting notices on the internet or publishing attention-grabbing notices in newspapers and other media may be acceptable substitutes where individualized, direct notice is not practicable.

In the event that notice is deemed insufficient, a court can order the appointment of a class action notification expert to advise the court on the sufficiency of the proposed method of notice and recommend improvements (see, for example, *Kaufman v. Am. Express Travel Related Servs., Inc.*, 283 F.R.D. 404, 408 (N.D. Ill. 2012)).

Courts are increasingly relying on reach calculations to determine the adequacy of a notice's dissemination. Current guidelines published by the Federal Judicial Center state that it is reasonable to reach between 70% and 95% of class members.

Reach Calculations

"Reach" refers to the number of non-identical class members reached by a class action settlement notice. Reach calculations help predict the percentage of class members among the whole class universe who will likely receive notice. Courts are increasingly relying on reach calculations to determine the adequacy of a notice's dissemination. Current guidelines published by the Federal Judicial Center (available at fjc.gov) state that it is reasonable to reach between 70% and 95% of class members.

Where notice is provided through publications, reach calculations attempt to get to the net number of class members who would receive any publication containing the notice, that is, distinct subscribers with no overlap across publications targeted for notice. Placing print ads in a variety of publications that likely do not have great subscriber overlap, such as *USA Today* in conjunction with *Sports Illustrated*, can aid in maximizing the net number of class members reached. Claims administrators often lack the training to conduct reach analyses, so parties more frequently turn to advertising or marketing consultants for commonly practiced methodology.

Although the internet and e-mail provide convenient means for direct notice, the accuracy of e-mail lists is an important factor in determining successful reach (see *Schlesinger v. Ticketmaster*, No. BC304565, 2012 WL 4739283, at *4-5 (Cal. Super. Sept. 26, 2012) (e-mail notice to class members was not effective where 20% of the e-mails "bounced")). Facebook and other social media outlets also offer a large universe of users, but notice via social media is likely to be successful only after determining which class members are consistent social media users.

Contents of the Notice

There is an opportunity to opt out of certain types of settlement classes (see *FRCP 23(b)(3), (c)(2)(B)*), and one of the main goals of a class action settlement notice is to aid class members in making informed decisions about whether to opt out. Where

certification of a settlement class and preliminary approval of a settlement agreement occur simultaneously, a single meaningful notice can inform absent class members of the existence of the class action, the settlement agreement and the potential for opting out (see *FRCP 23(e)(3) 2003 advisory committee's note*).

Additionally, notice may provide absent class members with the information needed to decide whether to object.

The contents of the notice should include:

- The terms of the proposed settlement and a statement that the proposed settlement will bind all class members if approved.
- The definition of the class.
- The names of class members, if feasible, and an estimate of the proportionate share of the claims, or a reasonable estimate of the number of class members in each state and an estimate of the proportionate share of the claims.
- A disclosure stating if the class was certified for settlement purposes only.
- The proposed or final notification to class members of their rights to opt out of the class action or, if opt-out rights are not available, a statement to that effect.
- An outline of the original claims, relief sought and defenses, or a copy of the complaint and materials filed with the complaint.
- A schedule of judicial hearings related to the class action.
- The settlements or agreements made between class counsel and defendant's counsel.
- The final judgment or notice of dismissal.
- Any judicial opinions related to the settlement proceedings.

(See *Manual for Complex Litig. (Fourth)* § 21.633 (2004); see also 28 U.S.C. § 1715(b).)

FINAL APPROVAL HEARING

A court may approve a class action settlement proposal only after a hearing and on finding that it is fair, reasonable and adequate (*FRCP 23(e)(2)*). The court must evaluate the settlement as a whole, rather than assessing its individual components (*Facebook*, 696 F.3d at 819). Moreover, the settlement does not need to be the fairest possible resolution, but the compromises reflected in the agreement must be fair, reasonable and adequate when considered from the perspective of the class as a whole (*In re Baby Prods. Antitrust Litig.*, 708 F.3d 163, 174 (3d Cir. 2013)).

The US Court of Appeals for the Ninth Circuit recently analyzed the fairness of a settlement plan through consideration of the following factors:

- The strength of the plaintiffs' case.
- The risk, expense, complexity and likely duration of further litigation.
- The risk of maintaining class action status throughout the trial.
- The amount offered in the settlement.
- The extent of discovery completed and the stage of the proceedings.
- The experience and views of counsel.
- The presence of a governmental participant.
- The reaction of the class members to the proposed settlement.

(*Facebook*, 696 F.3d at 819 (citing *Hanlon*, 150 F.3d at 1026).)

While these factors are not exhaustive, many courts follow similar guidelines (see, for example, *In re Prudential Ins. Co. Am. Sales Practice Litig. Agent Actions*, 148 F.3d 283, 323-24 (3d Cir. 1998); *In re Thornburg Mortgage, Inc. Sec. Litig.*, 912 F. Supp. 2d 1178, 1205 (D.N.M. 2012) (citing *Jones v. Nuclear Pharm., Inc.*, 741 F.2d 322, 324 (10th Cir. 1984)); see also *Manual for Complex Litig. (Fourth)* § 21.62 (2004)).

FILING THE PROPOSED SETTLEMENT AGREEMENT

Any class action settlement agreement that is reached between the parties must be filed with the court, and any related side agreements or undertakings must be identified to the court (*FRCP 23(e)(3)*). The parties may petition the court to keep certain terms of the settlement agreement confidential, including side agreements. Courts typically balance confidentiality concerns against the rights of, or consideration to, the proposed settlement classes.

Further, some agreements may include information that merits protection against general disclosures. The court may direct the parties to provide a copy or summary of such an agreement to resolve the issue (see *In re Initial Pub. Offering Sec. Litig.*, 226 F.R.D. at 205; see also *FRCP 23(e)(2) 2003 advisory committee's note*). For example:

■ The US Court of Appeals for the Eleventh Circuit examined a "blow provision" granting the defendant the opportunity to withdraw from the class action settlement if an undisclosed number of class members opted out of the settlement. The court found that the number of opt outs required to trigger the blow provision could be kept confidential to encourage settlement and discourage third parties from soliciting class members to opt out. (*HealthSouth Corp. Sec. Litig.*, 334 Fed. Appx. 248, 250 & n.4 (11th Cir. 2009).)

■ The US District Court for the Northern District of Georgia preserved the confidentiality of certain side "termination" agreements that allowed the defendant to terminate its settlement if opt outs by settlement class members reached certain levels. After conducting an *in camera* review, the court found that the plaintiff had not bargained away any of the rights of class members in return for advantages of others. (*Columbus Drywall & Insulation, Inc. v. Masco Corp.*, 258 F.R.D. 545, 560 (N.D. Ga. 2007).)

ADDITIONAL OPT-OUT PERIOD

If a settlement occurs after formal class certification, the court may refuse to approve it unless the settlement affords a new opportunity for the individual class members who had not previously opted out to request exclusion (*FRCP 23(e)(4)*). The decision to create a second opt-out period is entirely within the court's discretion based on the particular case (*Manual for Complex Litig. (Fourth)* § 22.611 (2004)). Although second opt-out periods are not commonly granted, factors that courts may consider include:

- Changes in information available to class members after expiration of the first opportunity to opt out.
- The nature of the individual claims.

It would be rare for courts to grant second opt-out periods in commercial class actions involving antitrust or securities claims. However, second opt-out options may be somewhat more common in personal injury cases. In any situation, a court may exercise caution in granting a second opt-out period because it has the potential to create uncertainty for the potential settlement and disrupt the settlement itself.

To deal with the risks of a second opt-out period, a defendant may insist on a "blow-up" provision in the class action settlement agreement, which allows the defendant to terminate the settlement based on a specific set of circumstances.

OBJECTIONS TO CLASS ACTION SETTLEMENTS

Any class member may object to a proposed settlement if the settlement requires court approval under FRCP 23(e) (*FRCP 23(e)(5)*). Generally, only class members have standing to object to a proposed class action settlement (see *In re Sunrise Sec. Litig.*,

131 F.R.D. 450, 459 (E.D. Pa. 1990)). Besides class membership, there do not appear to be any other requirements or standards that must be met to file an objection to a proposed settlement. However, courts allow parties to draft basic rules regarding the submission of objections (see, for example, *Trombley v. Bank of Am. Corp.*, No. 08-cv-456-JD, 2011 WL 3740488 (D.R.I. Aug. 24, 2011)).

COMMON GROUNDS FOR OBJECTIONS

Objections typically address either defects in process or any matter that would result in the settlement failing to meet the fair, reasonable and adequate test. Common grounds for objections include:

- Defective notice (see *Union Asset Mgmt. Holding A.G. v. Dell, Inc.*, 669 F.3d 632, 641 (5th Cir. 2012)).
- An unreasonable *cy pres* provision (see *In re Lupron Mktg. & Sales Practices Litig.*, 677 F.3d 21, 24 (1st Cir. 2012)).
- Unreasonable fees and expenses of counsel (see *Union Asset Mgmt. Holding A.G.*, 669 F.3d at 642-45).
- Improper allocation of settlement funds among subclasses (see *In re Baby Prods.*, 708 F.3d at 175-76).
- Conflicts of interest (see *Radcliffe v. Experian Info. Solutions Inc.*, 715 F.3d 1157, 1163-68 (9th Cir. 2013); *Rodriguez v. West Publ'g Corp.*, 563 F.3d 948, 960-61 (9th Cir. 2001)).

DEALING WITH PROFESSIONAL OBJECTORS

A group of objectors has recently emerged who repeatedly object to class action settlements. There are two primary types of these “professional” objectors:

- Those who object to try to get more money.
- Those who take on the role of class action watchdogs, such as the Center for Class Action Fairness, and object on policy grounds.

Class counsel and district courts employ various strategies to counter professional objectors whose motives may often be either to obstruct the settlement process in the hopes of being paid to go away or to express idiosyncratic ideological points of view.

One strategy is to move forward briskly with the settlement approval process and force objectors to demonstrate the merits of their objections. Weak objections are often dealt with quickly by the court. Of course, legitimate objections are entitled to be fully considered. Sometimes, but rarely, settlements have to be revised or they fall apart as a result of objections.

A second approach is for defendant’s counsel to tell class counsel that they have the responsibility to work out an arrangement with objectors, particularly economic objectors, given the risk of diminishing the total settlement compensation.

A third method, used at the appeal stage, is to ask the court to require objectors to post an appeal bond (also known as a cost bond) pursuant to Federal Rule of Appellate Procedure

(FRAP) 7. In deciding whether to require an appeal bond under FRAP 7, courts often consider:

- The appellant’s financial resources available to post a bond.
- The risk of paying the appellee’s costs in an unsuccessful appeal.
- The merits of the appeal.
- Whether the appellant has shown bad faith in filing the appeal.

(See *In re Initial Pub. Offering Sec. Litig.*, 728 F.Supp. 2d 289, 292 (S.D.N.Y. 2010).)

There are generally three approaches courts take with respect to the types of costs that may be included in appeal bonds:

- Only the costs found in FRAP 39 and 28 U.S.C. § 1920 (see *In re AOL TimeWarner, Inc., Sec. & “ERISA” Litig.*, No. 02-cv-5575, 2007 WL 2741033, at *5 (S.D.N.Y. Sept. 20, 2007)).
- The costs found in FRAP 39 and 28 U.S.C. § 1920, plus any costs that the appellees are entitled to under the relevant substantive statutory authorities (see *In re AOL TimeWarner, Inc.*, 2007 WL 2741033, at *5).
- All costs resulting from a frivolous appeal under FRAP 38 (see *Sckolnick v. Harlow*, 820 F.2d 13, 15 (1st Cir. 1987)).

Circuit courts are split on the issue of including attorneys’ fees in FRAP 7 appeal bonds. The majority rule is that attorneys’ fees may be included if they would be treated as recoverable costs under an applicable fee-shifting statute (see *Azizian v. Federated Dep’t Stores, Inc.*, 499 F.3d 950, 955 (9th Cir. 2007) (collecting cases)). The minority rule does not allow attorneys’ fees to be included in FRAP 7 appeal bonds and instead requires security for only those costs identified in FRAP 39 and 28 U.S.C. § 1920 (see *Hirschensohn v. Lawyers Title Ins. Corp.*, No. 96-cv-7312, 1997 WL 307777, at *2,*3 (3d Cir. June 10, 1997); *In re Am. President Lines, Inc.*, 779 F.2d 714, 716 (D.C. Cir. 1985)).

A final strategy is to include “quick pay” provisions in class action settlement agreements. These provisions allow class counsel to receive fees approved by the district court upon approval of the settlement irrespective of an appeal, providing that class counsel agrees to refund these fees if the fees or the settlement is reversed on appeal.

DISCOVERY FROM OBJECTORS

Although the FRCP does not provide for discovery from absent or unnamed class members or objectors, courts have carved out circumstances in which parties can seek this discovery. However, both the types and purposes of this discovery are limited (see, for example, *勞工第17號健康及福利基金 v. Philip Morris, Inc.*, No. 97-cv-4550, 1998 WL 241279, at *1 (S.D.N.Y. May 12, 1998) (taking discovery of absent class members is not per se unavailable, although it is generally disfavored)). Defendants generally must:

- Demonstrate a clear need for the information.
- Narrowly tailor the requests to their purpose.
- Avoid unduly burdensome requests.

(*Philip Morris, Inc.*, 1998 WL 241279, at *1.)

The requirement to narrowly tailor discovery requests has resulted in a preference toward written discovery, such as document requests and interrogatories, over depositions.

There is limited case law on taking discovery of class objectors. However, some courts are skeptical of class objectors and the motivations of their counsel and occasionally have allowed this discovery. For example, a court permitted deposition and written discovery from an objector to a class action settlement on topics concerning:

- The objector's alleged standing as a class member.
- The underlying bases for the objection.
- The objector's relationships with professional objector's counsel.

(See *In re Cathode Ray Tube (CRT) Antitrust Litig.*, 281 F.R.D. 531, 532-33 (N.D. Cal. 2012) (basing authority to compel discovery from the class objector on FRCP 45, to the extent the objector can be considered a non-party); see also *In re TFT-LCD (Flat Panel) Antitrust Litig.*, 289 F.R.D. 548, 554 (N.D. Cal. 2013) (ordering deposition and document production, and sanctioning the objectors for failing to appear for the depositions); but see *Corpac v. Rubin & Rothman, LLC*, No. 10-CV-4165, 2012 WL 2923514, at *2, *3 (E.D.N.Y. July 19, 2012) (denying request to depose an objector where the primary purpose for the discovery was to determine the motivation of the objector's counsel in opposing the settlement, as well as settlements in other similar class actions).)

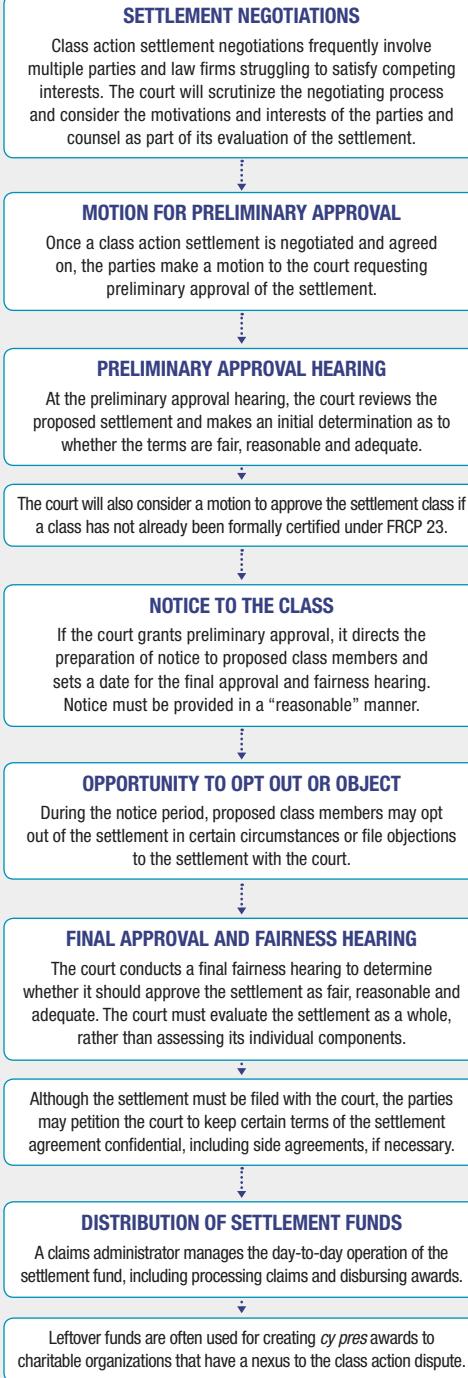
CY PRES PROVISIONS IN SETTLEMENT AGREEMENTS

Cy pres provisions are commonly used in class action settlement agreements to address the issue of unclaimed funds that are not distributed to class members for a variety of reasons. "*Cy pres*" originates from the French expression "cy pres comme possible," meaning as near as possible.

Leftover funds are often used for creating *cy pres* awards to charitable organizations that have a nexus to the class action dispute, rather than having those funds revert to the defendant, escheat to the state or increase the share pro rata to the remaining claimants (*In re Baby Prods.*, 708 F.3d at 172). *Cy pres* provisions allow the court to direct the proceeds to the next best class of beneficiaries (*Nachshin v. AOL, LLC*, 663 F.3d 1034, 1036 (9th Cir. 2011)).

Courts and critics have been looking closely at *cy pres* awards, including their effect on attorneys' fees, and there are a growing number of cases where courts have rejected them.

KEY STAGES OF A TYPICAL CLASS ACTION SETTLEMENT



Courts closely scrutinize *cy pres* awards. They often view these arrangements with skepticism because of the risks to the named class members and because the award adds a totally new beneficiary that has no involvement in the dispute.

GUIDELINES FOR USING CY PRES AWARDS

The American Law Institute (ALI) and the National Association of Consumer Advocates (NACA) have each issued guidelines on the appropriate use of *cy pres* awards in class action settlements.

The ALI guidelines describe two circumstances in which *cy pres* awards are appropriate:

- When funds are left over after all claims are satisfied or when distribution of funds to all class members is not feasible (for example, because recipients cannot be located).
- When the identified or administrative costs for distribution are too large and the interests of the recipients reasonably approximate the interests of the class members.

(*ALI, Principles of the Law of Aggregate Litig.*, § 3.07 (2010).)

The NACA guidelines, on the other hand, provide for *cy pres* awards only for unclaimed portions of the settlement. The guidelines state that unclaimed portions of the settlement should be used to either:

- Protect the interests of persons injured by illegal conduct and thus indirectly benefit absent class members.
- Promote the purposes of the statutory prohibitions sought to be enforced in the underlying litigation.

(*NACA, Standards & Guidelines for Litig. & Settling Consumer Class Actions, Revised*, 255 F.R.D. 215, 244 (2009).)

COURT APPROVAL OF CY PRES AWARDS

A court's power to approve a *cy pres* award derives from FRCP 23(e). Approval is warranted if the court finds that the settlement, taken as a whole, is fair, reasonable and adequate (*In re Baby Prods.*, 708 F.3d at 173-74).

Courts closely scrutinize *cy pres* awards. They often view these arrangements with skepticism because of the risks to the named class members and because the award adds a totally

new beneficiary, such as a charitable organization, that has no involvement in the dispute. Courts look to a variety of indicators to determine whether a *cy pres* award is appropriate, including:

- **The adequacy of the nexus between the alleged class injury and the *cy pres* recipient.** The beneficiaries must be closely tied to the lawsuit and the interests of the class members to avoid the specter of self-interest of other parties, their counsel or the court. If there is no sufficient nexus between the two, the award may be rejected. (*Dennis v. Kellogg Co.*, 697 F.3d 858, 865 (9th Cir. 2012).)
- **Whether the award to the class is non-distributable.** That is, whether the proof of individual claims would be burdensome or the distribution of damages costly. (*Nachshin*, 663 F.3d at 1038; *Six (6) Mexican Workers v. Arizona Citrus Growers*, 904 F.2d 1301, 1305 (9th Cir. 1990).)
- **The compensation to class members as compared to the *cy pres* award.** The settlement, taken as a whole, must be fair, reasonable and adequate. (*In re Baby Prods.*, 708 F.3d at 173-74.)
- **Whether counsel or the court faces criticism or a conflict of interest.** Attorneys and judges may tarnish their reputations and create the appearance of impropriety by choosing self-serving organizations to receive *cy pres* awards. (See *SEC v. Bear, Stearns & Co.*, 626 F. Supp. 2d 402, 415 (S.D.N.Y. 2009); see also *In re Thornburg Mortgage, Inc. Sec. Litig.*, 885 F. Supp. 2d 1097, 1106, 1109 (D.N.M. 2012).)

RECENT CY PRES CASES

Two recent federal appellate court cases address the adequacy of *cy pres* awards in class action settlement agreements.

In *In re Baby Products Antitrust Litigation*, the US Court of Appeals for the Third Circuit held that a settlement, whether or not incorporating a *cy pres* award, should provide sufficient compensation to class members. The Third Circuit

rejected the *cy pres* award of approximately \$18 million, less administrative costs, because it was too large in comparison to the compensation to the class recipients, which was approximately \$3 million. The Third Circuit held that “barring sufficient justification, *cy pres* awards should generally represent a small percentage of total settlement funds.” (708 F.3d at 173-76.)

In contrast, in *Lane v. Facebook, Inc.*, the Ninth Circuit approved a settlement where the aggrieved class received no relief at all, while \$6.5 million of the \$9.5 million total award was used to establish a new foundation controlled, in part, by the lead defendant, Facebook, and class counsel. The bulk of the remainder of the settlement (about \$3 million) went to class counsel’s fees. Notably, only four class members objected to the settlement and just over 100 of the more than 3.6 million class members opted out of the settlement. (696 F.3d at 835.) A petition for writ of certiorari currently before the US Supreme Court seeks to overturn the settlement agreement.

CY PRES AWARDS AND ATTORNEYS’ FEES

A *cy pres* award may increase a settlement fund and the attorneys’ fees without increasing the benefit to the class. The Third Circuit’s recent decision noted that while it may be appropriate to include a *cy pres* award in the calculation of attorneys’ fees, it is within the district court’s discretion to decrease attorneys’ fees, if necessary, where a portion of a settlement would be distributed *cy pres*, especially in cases where the foremost beneficiary of the settlement is counsel, not the class members (*In re Baby Prods.*, 708 F.3d at 173-76).

Similarly, there is a real risk that a large fee to attorneys in comparison to the settlement as a whole may cause a court to reject a settlement (*In re Dry Max Pampers Litig.*, 2013 WL 3957060, at *3-4).



Search [Class Action Fairness Act of 2005](#) for information on CAFA’s provisions on attorneys’ fees and *cy pres* awards in connection with coupon settlements of class actions.

DISTRIBUTION OF SETTLEMENT FUNDS

The strategies and logistics involved in the distribution of settlement funds are inherently complicated, but can be simplified with orderly planning and the retention of an experienced claims administrator. The distribution plan will depend on several factors, including the value of the settlement, size of the class and style of settlement that is agreed on by the parties and approved by the court.

Well before settlement, a claims administrator can prepare counsel by creating an effective notice and distribution plan, identifying potential issues and uncovering cost savings. This will help mitigate potential objections by the court and opposing counsel. The claims administrator or a settlement

consultant can also assist with planning critical steps, such as setting timelines for notices and claims, anticipating potential claims rates, staffing call centers and handling unredeemed settlement funds.

Many pitfalls can occur in each step of the process, especially with the use of e-mail and social media to notify class members. A strong claims administrator is essential for an effective notice and distribution plan. The claims administrator manages the day-to-day operation of the settlement fund, including:

- Holding and distributing funds on behalf of the class, including handling escrow issues.
- Managing class member data.
- Providing legal notification to class members, including individual and media notices.
- Providing call center support.
- Processing claims via postal, electronic and telephonic filings.
- Calculating and disbursing awards.
- Handling tax reporting and filings.

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