

Settling Fraud Cases under the Class Action Fairness Act of 2005

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Settlements Generally

Even more so than with individual cases, most class actions settle. This is due in part to the fact that the risks of proceeding to judgment post-certification are very significant to all parties. However, many settlements are often negotiated prior to certification. In those cases, the settlement is contingent on the court certifying a class for settlement purposes only.

When making the determination, several factors are considered by the court including the lack of collusion, a comparison of the strengths of the case against the amount of the settlement and the possible range of recovery at trial, defendant's ability or inability to pay a greater amount, the complexity, length and expense of the litigation, the amount of opposition to the settlement from affected parties, the opinion of counsel, the stage of the proceedings and the amount of discovery undertaken at the time of the settlement.

The court's involvement in the approval of a class action settlement and the notice requirements provide a measure of assurance that the interest of the members of the class have been fully considered and class members are afforded an opportunity to object or voice their views on the settlement.

The Class Action Fairness Act ("CAFA") was passed and enacted as of February 18, 2005. Section 3, Consumer Class Action Bill of Rights and Improved Procedures for Interstate Class Actions, defines "proposed settlement" as an agreement regarding a class action that is subject to court approval and that, if approved, would be binding on some or all class members. (See attached Exhibit "A" hereto).

Section 3 includes a provision limiting the power of a court to approve a settlement which imposes a “net financial loss” on class members. CAFA states that a court may only approve a proposed settlement whereby class members are obligated to pay class counsel and the result would be a “net loss” to the class members, only after the court makes a written finding that the non-monetary benefits to the class members substantially outweigh the financial loss suffered by the class members. This provision obviously places a check on settlements where the overall monetary benefit to class members is less than the total amount of attorney fees owed by class members to plaintiff’s counsel.

Coupon Settlements

The pros of non-cash settlements are that it cost less for the defendant out-of-pocket to settle a case and is usually easier to sell to a defendant. Whether in the form of coupons or vouchers, the settlement can be an effective public relations campaign for the defendant, who can also use the coupons or vouchers to encourage consumers to buy another one of its products. If the coupons or vouchers are used in the case where a plaintiff class is very likely in the position to *have* to buy another product (e.g., mandated insurance from a settling insurance company or coupons from a drug manufacturer for patients who have prescriptions for a particular drug), the settlement will also be quite valuable to the plaintiffs. Situations where the settlement may not be valuable could be where coupons are offered to receive, for example, \$150.00 off any new Ford vehicle purchase when the class member would not otherwise be buying a new Ford vehicle.

There are several factors to be considered by the court in non-cash settlements:

- (a) What is the maturity date of the particular coupon or voucher?
- (b) What is the likelihood that the settling class member may actually use the coupon?

- (c) Is the coupon transferable to another party so that if the class member does not want it, the class member can sell it for cash to someone else who may want it?
- (d) Is there a claims process for the plaintiff class so that they have to apply for the coupon to receive it or is it automatically sent out to all class members?

The problem with non-cash settlements is the argument that they do not have any value to the class. This will affect court approval of the settlement and the approval of any award of attorney fees. The real issue is: Will the class use the coupon? Which boils down to whether the consumer *needs* the particular product? The fact that the consumer ultimately does not use the coupon should not be the problem of the plaintiff or defendant because the settlement involves making the product available. After all, even in cash settlements, some plaintiffs do not cash settlement checks.

Section 3 of CAFA increases the level of judicial scrutiny applied to coupon and other non-cash settlements. Prior to granting settlement approval, district courts will now be required to conduct a hearing and publish a written finding that a proposed coupon settlement is fair, reasonable, and adequate to class members. 114 U.S.C. §1712(e).

CAFA allows *cy pres* distributions of unclaimed coupons, “to one or more charitable or governmental organizations, as agreed to by the parties,” but the proceeds of such relief, “shall not be used to calculate attorney fees under this section.” *Id.*

This section also limits the recovery of attorney’s fees in these type settlements by mandating that contingency fee awards be, “based on the value to class members of the coupons that are redeemed.” 114 U.S.C. §1712(a). When not awarded on a contingent basis, such fees must be based on, “the amount of time class counsel reasonably expended working on the action.” 114 U.S.C. §1712(b)(1). When fees are awarded on a “mixed” basis, the courts must apply these guidelines proportionately. *Id.*, setting forth 114 U.S.C. §1712(c). Of course, CAFA sets forth that nothing shall be

construed to prohibit the application of a lodestar with a multiplier method of determining attorney fees. *Id.*

There are several key factors which should involve setting of attorney fees and the review conducted by court:

1. Negotiations. Fees should not be negotiated at the same time as any other issues affecting class members.
2. Pre-litigation Pricing. The court may require potential class counsel to price their services in advance of litigation.
3. Sharing Agreement. It must bear some relationship to services rendered and must be revealed to the court when formulated.
4. Hours. Describing to the court the type and amount of work plaintiff's counsel have performed is the key to convincing the court that the fee is reasonable under the circumstances. Try to convince the court that it is a fair and reasonable settlement for the class and that you worked hard to craft a good settlement for the class and that your fee is based on a reasonable percentage in light of the work created.

The court may receive expert testimony, upon the motion of a party, regarding settlement valuation. 114 U.S.C. §1712(d).

Opt-Out Rights

The passage of CAFA does not appear to directly affect class member opt-out rights. In Alabama, Rule 23(b)(3) is primarily a damages class, allowing opt-out and requiring notice to class members. In the typical class action, one seeking damages under Rule 23(b)(3), class members must be given an opportunity to opt-out of the class. The opt-out procedure should be simple and should afford class members a reasonable time in which to exercise their option. Courts usually establish a period of 30 to 60 days (or longer if appropriate) following mailing or publication of the notice for class members to opt-out. A form for members of the proposed class who wish to opt-out might be included with the notice; it should clearly and concisely explain the available alternatives and their consequences. Typically, opt-out forms are filed with the clerk, although in large class actions the court can arrange for a special mailing address and designate an administrator retained by counsel and accountable to the court to

assume responsibility for receiving, time-stamping, tabulating, and entering into a database the information from responses (such as name, address, and Social Security number, etc.).

Usually, the defendant requires a maximum number of opt-outs before they can void an overall settlement. This opt-out percentage can be negotiated by way of a side letter so that it is not in the actual settlement agreement so that the objectors will not know how many opt-outs they have to void a settlement.

Opt-outs generally have no ground to object to a settlement. The more problematic issue is class members who move to intervene in the settlement and appeal the settlement in order to hold up funds and relief of the settlement. Counsel for the plaintiff class is wise to negotiate interest on their attorney fees which will be paid to them pending any appeal by an objector.

Class Settlement Notice Issues

There are a number of factors involved in designing, formulating and implementing notice to class members. Cost is a factor and especially in large class actions becomes a sometimes hotly negotiated issue. Although typically defendants are taxed with the cost of notifying class members, some courts have held differently. In the case of *In re. Victor Technologies Securities Litigation*, 792 F. 2d 862 (9th Cir. 1986), the plaintiffs were required to offer to reimburse record owners for costs of forwarding notice to beneficial owners. The failure to provide notice to any class members may very well mean that the non-notified class members can pursue their own subsequent lawsuits against the Defendants. *Besinga v. U.S.*, 923 F. 2d 133 (9th Cir. 1991). Typically, first-class mail will suffice as a proper mailing method. *Peters v. National R. R. Passenger Corp.*, 966 F. 2d 1483 (D.C. Cir. 1992).