

STATE COURT CLASS ACTION SETTLEMENTS: A PATTERN OF ABUSE AND A PROPOSED SOLUTION

The U.S. Chamber Institute for Legal Reform respectfully submits the following comments to the Federal Trade Commission in conjunction with the FTC workshop entitled “Protecting Consumer Interests in Class Actions.”

I. INTRODUCTION

The Institute for Legal Reform (ILR) is a non-profit organization established by the Chamber of Commerce of the United States. Its purpose is to work toward making America’s civil justice system simpler, fairer and faster. ILR promotes legislative and judicial solutions to reduce excessive and frivolous litigation, to address vexing legal problems (such as the current class action crisis), and to restore sanity to the legal system.

ILR commends the FTC for its growing involvement in the important issues surrounding class actions and class action settlements. The FTC’s focus on the class action issue – most notably by filing amicus briefs objecting to improper settlements – has helped bring the issue of frivolous filings, collusive settlements, and exorbitant attorneys’ fees to the forefront of public attention.

Every year, thousands of class actions are filed in the United States – the vast majority in our state court system. The attorneys who file these lawsuits purport to represent thousands or even millions of allegedly injured individuals. But too frequently, the interests of the supposedly injured parties are not really represented at all. Instead of pursuing the interests of their supposed clients, the attorneys strike a deal under which the money ends up in their own pockets – rather than the hands of the supposedly injured parties they claim to represent. The result is more and more class action filings, concentrated in certain state courts, and a growing pattern of settlement abuse.¹

The Institute for Civil Justice/RAND, in a study jointly funded by the plaintiffs’ and defense bar, took a systematic look at where the money goes in class settlements. That study indicates that in state court consumer class action settlements (*i.e.*, non-personal injury monetary relief cases), the class counsel frequently receive more money than all class members combined.² Significantly, another study found that this phenomenon was not occurring in federal courts – “[i]n most [class actions handled by federal courts], net monetary distributions to the class

¹ See Deborah R. Hensler et al., PRELIMINARY RESULTS OF RAND STUDY OF CLASS ACTION LITIGATION 15 (1997) (observing a “doubling or tripling of the number of putative class actions” that was “concentrated in the state courts”); *Analysis: Class Action Litigation*, Class Action Watch, Spring 1999, at 3 (Figure 2), available at <http://www.fed-soc.org/publications/classactionwatch/classaction1-2.pdf>. (finding that while federal court class actions had increased somewhat over the past decade, the frequency of state court class action filings had increased 1,315 percent – with most of the cases seeking to certify nationwide or multi-state classes); Deborah R. Hensler et al., CLASS ACTION DILEMMAS: PURSUING PUBLIC GOALS FOR PRIVATE GAIN 15 (1999) (PRIVATE GAIN) (confirming the explosive growth in the number of state court class actions and concluding that class actions “were more prevalent” in certain state courts “than one would expect on the basis of population”).

² PRIVATE GAIN at 15.

exceeded attorneys' fees by substantial margins."³

Class action abuse is unjustifiably draining millions of dollars from our nation's economy by transferring large amounts of capital from companies to plaintiffs' lawyers with no commensurate benefit to society at large. It is also undermining public confidence in the law by suggesting to American citizens that our judicial system condones a distorted system of justice in which plaintiffs go without any real compensation, while their supposed lawyers walk away with millions in cash.

ILR has steadfastly supported legislation – The Class Action Fairness Act of 2004 – that would address many of these problems by allowing federal courts to hear more interstate class actions, by requiring heightened scrutiny before coupon settlements are approved, and by limiting attorneys' contingency fees in coupon settlements to the value of the coupons actually redeemed.⁴

II. STATE COURT CLASS ACTION SETTLEMENTS: A RECORD OF ABUSE

Class actions – when used properly – are a powerful tool for large groups of individuals who cannot seek justice individually. The problem is that in today's class actions, the individuals are typically left out of the picture. More often than not, the lawyers conceive of the lawsuit, the lawyers direct the lawsuit, and the lawyers get all the benefits from the lawsuit. The so-called “plaintiff” in the case is usually just a titular representative – an acquaintance recruited by the plaintiffs' lawyer because he or she lives near a “magnet” state court, reputed to be friendly to class actions.

As FTC Commissioner Leary has pointed out, class action lawyers have effectively appointed themselves as private cops and arrogated the responsibility for policing corporate behavior.⁵ What's wrong with this form of so-called “private law enforcement”? It's analogous to permitting self-appointed “cops” to go out on the streets, set up speed traps, pull drivers over (whether they were speeding or not), and give those drivers the option of either: (a) spending a few nights in jail, or (b) resolving the problem by paying the “cop” (for personal benefit) whatever he demands. No doubt, the “cops” would argue that this is a marvelous system – on the theory that it discourages speeding. But justifiably, the public would have no trust in – or respect for – such a system of law enforcement, since prosecutorial decisions would be driven (or at least have the appearance of being driven) by the overwhelming financial self-interest of the “cops” themselves.

This is precisely what is occurring in class actions, and it has spawned a troubling pattern of abuse. Over the last several years, there have been 100 editorials in major newspapers – and

³ Federal Judicial Center, *EMPIRICAL STUDY OF CLASS ACTIONS IN FOUR FEDERAL DISTRICT COURTS 68-69* (1996).

⁴ The U.S. House of Representatives passed H.R. 1115 on June 12, 2003. Although more than 60 Senators have expressed support for the Senate version of the bill, S. 2062, the Senate has not yet voted on the legislation because of a disagreement between Democrats and Republicans regarding non-germane amendments that led to a filibuster. *See Senate Abandons Class Action Lawsuit Bill*, Associated Press, July 8, 2004.

⁵ Thomas B. Leary, *The FTC and Class Actions*, available at www.ftc.gov/speeches/leary/classactionsummit.htm.

countless more news stories – highlighting the problems of frivolous class actions, abusive coupon settlements, and excessive attorneys’ fees, nearly all of which are occurring in state courts.⁶ In the words of the *Washington Post*, class actions have become a “high-stakes extortion racket . . . in which truly crazy rules permit trial lawyers to cash in at the expense of businesses.”⁷ Or, as the *Wall Street Journal* put it, “[t]he lawyers who bring the suits make a mint, while the court approved settlements award the actual victims only pennies or coupons.”⁸

Numerous examples of abusive class action settlements abound. A list can be found in a compilation on our website, at www.legalreformnow.com/issues. Some other recent examples of abusive state court settlements include:

- *Shields, et al. v. Bridgestone/Firestone Inc. et al.* (No. E-0167637, Jefferson County, Texas, 2003) – This suit involves customers who had Firestone tires that were among those that the National Highway Traffic Safety Administration investigated or recalled, but who did not suffer any personal injury or property damage. After a federal appeals court rejected class certification, plaintiffs’ counsel and Firestone negotiated a settlement, which has now been approved by a Texas state court. Under the settlement, the company has agreed to redesign certain tires (a move already underway irrespective of the suit) and to develop a three-year consumer education and awareness campaign, but the *members of the class received nothing*. The lawyers? They will get **\$19 million**.⁹
- *Premier Cruise Lines* (No. 96-06932 CA-FN, Fla. Cir. Ct., Brevard County, Florida, 2003) – This class action alleged that a cruise line collected “port charges” that exceeded the amount actually paid by the defendant. Under the settlement, plaintiffs will receive **\$30 to \$40 discounts** from *another cruise line* on its two- and three-night cruises out of Port Canaveral, Florida.¹⁰ (Premier is no longer in business.) In other words, a company that had not even been sued and had absolutely no risk of liability agreed to offer coupons – no doubt because they recognize that such coupons are a *promotional* opportunity and not a *penalty*. Attorney for the plaintiffs received **\$887,000** in fees, costs, and expenses.¹¹
- *In Re Microsoft Litigation Settlement* (No. 99 CV 17089, Johnson County, Kansas, 2003) – Microsoft has settled antitrust class actions in ten states in which plaintiffs alleged that Microsoft used its monopoly to gouge consumers. Based on the terms of the settlement, consumers who bought Microsoft software will receive a **\$5 to \$10 voucher** good for future purchases of particular computer hardware or software products. To receive the

⁶ See www.legalreformnow.com/Favorable%20Editorials.pdf (listing editorials).

⁷ *Reforming Class Actions*, Wash. Post, June 14, 2003.

⁸ *Mayhem in Madison County*, Wall Street Journal, Dec. 6, 2002.

⁹ See Miles Moore, *BFS Settles Nationwide Class Action Suit; Tire Maker to Modify Certain Models, Launch Education Program*, Rubber & Plastics News, August 4, 2003.

¹⁰ *The Law Offices of Douglas Bowdoin, for Plaintiffs, and Todd Pittenger of Lowndes, Drosdick, Doster, Kantor & Reed, P.A., for Defendant, Announce a Proposed Class Action Settlement*, Business Wire, Inc., July 2, 2003.

¹¹ *Premier Cruise Line Reaches Settlement*, Mealey’s Litigation Report: Class Actions, July 17, 2003.

voucher, consumers must download a form from www.microsoftproductsettlement.com/kansas and then mail it in. To redeem the voucher, consumers must mail in the voucher, a photocopy of an original receipt, and an original UPC code. Half of the unclaimed settlement money will be used to donate Microsoft products to schools. A federal judge rejected a similar settlement in part on the ground that the school donations were intended to inflict further injury on Apple. Attorneys in these cases have sought *hundreds of millions of dollars* in fees.¹²

- *Ross and Lambert v. Portillo's Restaurant Group, Inc.* (00 Ch 13612, Circuit Court of Cook County, Illinois, Chancery Division, 2003) – In this case, consumers alleged that the beer goblets served at a Chicago restaurant chain were misrepresented to be 12 ounces, when they held only 10.6 ounces. In settlement, the company will give away 50,000 *coupons for \$1 off every subsequent \$5 purchase* at its 22 Chicago-area restaurants.¹³ All cash from the settlement goes to the lawyers.
- *DeGradi v. KB Holdings, Inc.* (No. 02 CH 15838, Circuit Court of Cook County, Illinois, Chancery Division, 2003) – In this case, consumers alleged that the KB Toys engaged in deceptive pricing practices on certain products. Under the settlement agreement, the toy retailer offered a *30 percent discount* on selected products between October 8 and October 14, 2003. In other words, the retailer agreed to hold a sale. According to an independent analyst, “KB Toys will benefit from the settlement,” because “they’re driving traffic.”¹⁴ The attorneys benefited too: they received all the cash – fees and costs of *\$1 million*.¹⁵
- *Dorel Juvenile Group, Inc.* (2003) – In this lawsuit, consumers alleged that the company was selling cribs unsafe for use by infants. The class members received either a crib *repair kit or a coupon for \$55*, which could be used toward the future purchase of a Dorel Juvenile Group Product.¹⁶ Of course, the coupon is only valuable for consumers who plan to have another baby and still trust the company.
- *Ramsey v. Nestle Waters North America, Inc. d/b/a Poland Spring Water Co.* (No. 03 CHK 817, Kane County, Illinois, 2003) – This suit involved allegations that Poland Spring water does not really come from a spring deep in the woods of Maine. The settlement calls for *discounts or free water* to Poland Spring customers over five years

¹² Dan Voorhis, *Here's How to Claim Your Share of Microsoft Settlement*, The Wichita Eagle, December 28, 2003.

¹³ *Judge Approves Portillo's Class Action Settlement Over Mislabeled Beer*, PR Newswire, Nov. 26, 2003.

¹⁴ Betty Lin-Fisher, *Shoppers Win In Suit; Customers Get a Jump on Holidays*, Akron Beacon Journal, Oct. 14, 2003.

¹⁵ Stephanie Zimmerman, *KB Toys Settles Lawsuit Over “Low” Prices By Offering Discount*, Chicago Sun-Times, Oct. 11, 2003.

¹⁶ *Dorel Juvenile Group Settles Class Action Lawsuit*, PR Newswire, Oct. 6, 2003.

and contributions of \$2.75 million to charities. In addition, the named plaintiff will receive \$12,000. Plaintiffs' lawyers received **\$1.35 million**.¹⁷

- *Chavez v. GameStop Corp.* (No. CGC-02-406658, San Francisco Superior Court, California, 2003) – In this class action, plaintiffs alleged that GameStop Corp. misrepresented some of the video games it was selling as new, when they had actually been previously purchased and returned. Under the settlement, GameStop agreed to post notices in stores stating: “All software for video game consoles may have been used and returned in accordance with (the store’s) return policy.” Further, anyone who bought a game from particular stores on specified dates, and can produce their receipt, will receive a **coupon for 5 percent off** the price of any one game. In other words, customers would receive \$1.25 off a \$25 dollar game – as long as they kept receipts. The coupon can be redeemed at retail locations, but not on the defendant’s website.¹⁸ Lawyers for the plaintiffs were paid **\$125,000** in fees and costs.¹⁹
- *Zurakov v. Register.com, Inc.* (No. 2301, N.Y. Sup. Ct., App. Div., 2003) – Plaintiffs alleged that Register.com delayed in switching purchased domains over to their customers and continued to display the company’s “Coming Soon” page which promotes the company and its advertisers. Under this settlement, class members receive **\$5 coupons** to use with Register.com (assuming they ever plan to register one of the company’s domains again). The lawyers for the class get **\$642,500**.²⁰

In short, a small number of state courts have amassed a troubling record of approving class action settlements in which all the benefits go to the lawyers – and the consumers are left holding the bag. And the problem is self-perpetuating. The lure of six- and seven-figure attorneys’ fees for little or no work has led to more and more class actions being filed in plaintiffs’ attorney-friendly magnet state courts. In one of the most notorious, Madison County, Illinois, class action filings have increased **more than 5,000 percent** since 1998.²¹

III. THE FEDERAL COURT RECORD: CLOSER SCRUTINY OF COUPON SETTLEMENTS

For the most part, federal courts have been far more consistent than their state court counterparts about scrutinizing coupon settlements. The reason for that stretches back more than

¹⁷ Edward D. Murphy, et al., *Conflict and Change; Maine’s Employment and Price Levels Remained Stable Last Year, but its Economy Experienced Plenty of Turmoil*, Portland Press Herald, January 4, 2004; see also www.noticeclass.com/springwatersettlement/LongFormNoticev2.pdf.

¹⁸ *Big Class Action: Settlements and Verdicts: Consumer Goods*, available at <http://www.bigclassaction.com/settlements/consumer.html>.

¹⁹ <http://www.gamestop.com/gs/help/classaction.asp>.

²⁰ Tom Perrotta, *Panel Revives Case Over Domain Name Registry*, Internet Newsletter, May 14, 2003.

²¹ See John H. Beisner and Jessica Davidson Miller, *They’re Making A Federal Case Out Of It . . . In State Court*, 25 HARV. J. L. & PUB. POL’Y 1 (Fall 2001); John H. Beisner and Jessica Davidson Miller, *Class Action Magnet Courts: The Allure Intensifies*, *Civil Justice Report* (Center for Legal Policy, July 2002); Trisha L. Howard, *Class Actions Set Record Last Year In Madison County/ Possible Change In Law Prompted Rush In Filing*, St. Louis Post Dispatch, Jan. 11, 2004.

200 years and is a testament to the foresight of the Framers. Under Article III of the Constitution, federal judges are appointed for life.²² They do not stand for re-election. They do not need to fill their campaign coffers with attorney contributions. They are confirmed by the U.S. Senate, which means their credentials are subject to substantial public scrutiny by congressional staffs, the national legal community, and the national media.

The results speak for themselves. Federal courts are far more likely than state courts to question coupon settlements and exorbitant attorneys' fees, and consumers in federal courts are much more likely to receive the same type of currency as their attorneys – *i.e.*, cash.

The most egregious examples of the disparity between federal and state courts are cases in which federal courts have rejected settlements that were later approved by state courts. The most notorious is the GM fuel tank litigation where the plaintiffs' counsel were able to obtain state court approval of a settlement that was harshly criticized by a federal court is inadequate.²³ Other examples of cases in which federal courts have rejected inadequate settlements include:

- *In Re Microsoft Corp. Antitrust Litigation*²⁴ – Consumers and entities who acquired licenses for Microsoft operating system or applications, brought a class action against Microsoft asserting that they were overcharged for Microsoft's software products. The court rejected a proposed settlement releasing all claims in return for a \$400 million contribution by Microsoft to a national "learning foundation" that would be established for the purpose of providing computer technology to schools in economically depressed areas. The court questioned whether the settlement agreement was adequately funded – particularly whether funding for technical support for schools was adequate. Furthermore, the court found that the proposed settlement would actually have anti-competitive effects because it allowed Microsoft to flood the kindergarten through high school market with PCs running its operating system and software products, at the expense of competitors like Apple. (As discussed above, a substantially similar settlement was later approved in state court.)
- *Schwartz v. Dallas Cowboys Football Club, Ltd.*²⁵ – In this antitrust case, the 1.8 million-member plaintiff class (people in the U.S. who had purchased NFL Sunday Ticket satellite television program since 1994), challenged the NFL's requirement that satellite television viewers purchase all regular Sunday afternoon games. The parties proposed a settlement agreement that required defendants to: (1) provide an additional weekly satellite television package for one season which allows consumers to purchase all NFL regular season Sunday afternoon games for any one Sunday; (2) establish a \$7.5 settlement fund to pay damages to class members; (3) provide class members with merchandise discounts at the NFL's Internet store (10 percent discount on one purchase of up to \$75); (4) pay \$2.3 million in administration and notification costs; and (5) pay \$3.7 million attorneys' fees and expenses. In return, plaintiffs agreed to release defendants from all claims regarding past broadcasting

²² See U.S. Const. art. III, § 1.

²³ See *In re General Motors Corp. Pick-Up Truck Fuel Tank Prods. Liab. Litig.*, 55 F.3d 768, 803-11 (3rd Cir. 1995).

²⁴ 185 F. Supp. 2d 519 (D. Md. 2002).

²⁵ 157 F. Supp. 2d 561 (E.D. Pa. 2001).

of NFL football games. The district court rejected the settlement because: (1) the relief provided through the sale of a single Sunday ticket was limited because consumers still could not purchase a single game of their choice and because the defendants were only required to offer the package for one season; (2) merchandise discounts offered as a part of consideration for settlement were insufficient; (3) monetary value of settlement was too low; (4) release required from viewers was overbroad; and (5) attorneys' fees were too high in light of the limited relief obtained.

- *Levell v. Monsanto Research Corp.*²⁶ – In this case which involved alleged radiation exposure, the court rejected a proposed settlement that provided occupational disease insurance for current and former employees, but did not provide benefits for class members who received Medicare, retiree medical insurance or alternative coverage and only guaranteed insurance for three years – the length of time that federal agencies contracting to spend money that has not yet been appropriated may do so under the Anti-Deficiency Act. The court rejected the proposed settlement because it benefited current employees at the expense of former employees and because much of the relief was contingent upon the Department of Energy's receipt of federal funding. For example, only current employees were eligible for payment from the settlement fund, which was \$926,000, and only current employees would benefit from enhanced workplace radiation protection and expert review of workplace safety practices. The court also found that an award of more than \$200,000 in attorneys' fees adversely affected the class members' recovery.
- *Sheppard v. Consolidated Edison Co.*²⁷ – The court rejected the proposed settlement in this employment discrimination case brought against Consolidated Edison Company of New York, finding that it was unfair to absent class members. The court concluded that the settlement, which proposed to pay seven named class members \$400,000 each and 2,400 unnamed class members awards ranging from \$566 to \$3,502, disproportionately benefited the named class members. In addition, the court questioned the award of almost \$2 million (more than 40 percent of the \$4.5 million settlement fund) to plaintiffs' attorneys for fees and costs.
- *Polar International Brokerage Corp. v. John Reeve*²⁸ – Calling the proposed settlement “virtually worthless” to shareholders, U.S. District Judge Shira Scheindlin rejected a settlement in a securities fraud class action under which plaintiffs received no money and had to waive all future claims. According to her decision, “The settlement puts no additional money in class members' pockets; what it offers is reassurance that the price they received is ‘not unfair.’ This benefit is of little value.”
- *Martens v. Smith Barney, Inc.*²⁹ – Court rejected settlement in gender discrimination case that would have established a new dispute resolution process, required Smith Barney to spend \$15 million over four years on new diversity programs and paid up to \$13.2 million in

²⁶ 191 F.R.D. 543 (S.D. Ohio 2000).

²⁷ 2000 WL 33313540 (E.D.N.Y. 2000).

²⁸ 187 F.R.D. 108 (S.D.N.Y. 1999).

²⁹ 181 F.R.D. 243 (S.D.N.Y. 1998).

attorneys' fees and expense reimbursement, as well as up to \$1.9 million in incentive payments to class representatives. The court found that the diversity programs were not sufficiently spelled out in the proposed agreement: "So long as the settlement's touted diversity programs and initiatives remain admirable but amorphous aspirations rather than reasonably defined plans of action, the court's fiduciary duty to the class remains unfinished business." Because the court did not approve the settlement, it did not analyze the request for fees.

- *Clarke v. Advanced Private Networks*³⁰ – The court rejected a proposed settlement in this securities action because the proposed settlement released the defendants from all damages claims even though unnamed class members did not have an opt-out right. The court concluded that unnamed class members' interests were not adequately represented in the settlement.
- *Clement v. American Honda Fin. Corp.*³¹ – This case rejected as a marketing scheme a settlement in which class members would have received nontransferable \$75 or \$150 coupons as a credit against their next financed purchase or lease of a vehicle through the defendant.
- *Free v. Abbott Laboratories*³² – In this infant formula antitrust action, the district court concluded that the proposed settlement was neither fair, nor adequate, nor reasonable, because members of the class would receive no more than four to six dollars (a tiny fraction of the \$4.3 million dollar settlement) each, while their attorneys would receive \$1.5 million dollars. "Although a cash settlement amounting to only a fraction of the potential recovery does not in itself render a settlement unfair or inadequate, the court finds that the members of this class would literally be no worse off if their case were tried to an adverse verdict."
- *Land v. United Telephone-Southeast, Inc.*³³ – This case involved monopoly allegations in the area of telephone wire maintenance services. Under the proposed settlement, there was no refund for any alleged overcharge; rather, customers who elected to discontinue the maintenance services at issue would receive a \$20 calling card for each affected access line and a reduction in their phone bill by the amount of present and future charges for the optional maintenance services. At the same time, plaintiff's counsel would have received \$1.1 million in fees, and the defendant was released from all causes of action and future injuries. In rejecting the proposed settlement, the court held: "Based on the *de minimis* recovery by class members, in comparison to the large fee to be received by plaintiff's counsel, and in comparison to the extensive, far-reaching release from liability obtained by the defendant, the Court does not find that the proposed settlement is fair, adequate, or reasonable.

These federal court cases rejecting abusive settlements tell only part of the story. Not

³⁰ 173 F.R.D. 521 (D. Nev. 1997).

³¹ 176 F.R.D. 15 (E.D. Conn. 1997).

³² 953 F. Supp. 751 (M.D. La. 1997).

³³ 1997 WL 599506 (E.D. Tenn. 1997).

enough attention is paid in the class action debate to the numerous *federal court*-approved class action settlements in which the class members received real benefits and their lawyers secured a reasonable return for their litigation efforts. Put simply, these are cases where the class action device worked. The following are examples of recent federal court-approved class action settlements in which the allegedly injured class members obtained real relief, *and* their attorneys were compensated fairly:

- *In re Linerboard Antitrust Litigation*³⁴ – In this antitrust action plaintiffs alleged that a number of U.S. manufacturers of linerboard (corrugated paperboard) engaged in a continuing combination and conspiracy restraining trade. The court approved settlements totaling \$202.5 million – the sixth largest reported antitrust settlement.
- *Parks v. Portnoff Law Associates*³⁵ – Property owners sued a law office that mailed letters that violated the Fair Debt Collection Practices Act and Pennsylvania law by threatening that the plaintiffs’ town would place liens on recipients’ homes unless they paid overdue trash, sewer, and water bills, possibly resulting in the sale of their properties. The collection letters failed to include notices that the defendant was a debt collector. The fifty-two class members agreed to a settlement in which each class member received real cash payments, and the plaintiffs’ attorneys were awarded \$56,000 for fees and expenses.
- *In re Sterling Foster & Co., Inc., Securities Litigation*³⁶ – Defendants were sued for making misstatements and omissions regarding their public stock and for engaging in market manipulation. The court approved the proposed settlement of \$2,200,000, ensuring that each class member would have access to real cash payments. However, the court rejected the plaintiffs’ counsel’s request for a fee of 30% of the fund. The court awarded the plaintiffs’ lawyers 25% of the settlement, stating that, although attorneys are entitled to a reasonable fee taken from the fund, courts should consider the overarching concern for moderation when approving the portion of the settlement to be taken by plaintiffs’ counsel.
- *Oslan v. Law Offices of Mitchell N. Kay*³⁷ – In this action, class members were sent letters by the defendant attorney, who knew that recipients would wrongly believe that the law firm and lawyers were participating in the collection of debts. The plaintiff class also alleged that the letters contained deceptive and false statements. The court approved a settlement of \$20,000 for each class member, noting the amount far exceeded the Fair Debt Collection Practices Act statutory award, which is limited to \$290.00 per plaintiff.
- *In re First Databank Antitrust Litigation*³⁸ – The class alleged that the defendant illegally monopolized and increased prices in the drug information database market after it acquired its principal competitor. The approved settlement consisted of a payment of \$23.25 million

³⁴ 321 F. Supp. 2d 619 (E.D. Pa. 2004).

³⁵ 243 F. Supp. 2d 244 (E.D. Pa. 2003).

³⁶ 238 F. Supp. 2d 480 (E.D.N.Y. 2002).

³⁷ 232 F. Supp. 2d 436 (E.D. Pa. 2002).

³⁸ 205 F.R.D 408 (D.D.C. 2002).

plus interest to members of the class, which was distributed based on “overcharges” that the members of plaintiff class had made to the defendant.

- *Roessler v. Nationwide Mutual Insurance Co.*³⁹ – Homeowners sued an insurance company that refused to pay claims for water or steam damage caused by an appliance. Under the settlement, Nationwide paid \$6.15 million to plaintiffs, an amount greater than the unpaid repair costs at issue. Individual recovery was estimated to be between \$2,200 and \$4,300. The federal court also granted incentive awards of \$10,000 to each class representative, contingent upon a demonstration that the awards were based on the time and money the class representatives had spent on the litigation.
- *In re Lorazepam & Clorazepate Antitrust Litigation*⁴⁰ – In this case, a plaintiff class alleged that defendant pharmaceutical companies entered into illegal agreements to monopolize markets for generic anti-anxiety drugs. Under the terms of the settlement, the defendants paid \$100 million into a settlement fund, \$71 million of which was used to pay consumer claims, and \$28.2 million of which was designated to pay claims by state governments. The federal court awarded an additional \$6.8 million for attorneys’ fees. Thus, the class members got real cash benefits, and counsel received substantial payment for their work.
- *In re Twinlab Corp. Securities Litigation*⁴¹ – In a case involving allegedly fraudulent accounting and business practices, the federal court approved a settlement under which \$26.5 million in cash was paid to approximately 15,000 purchasers of Twinlab Corp. stock. The court reduced plaintiffs’ counsel’s requested fees from \$8.8 million (33 percent) to \$3.2 million (12 percent). The court stated: “True, counsel undertook a risk in taking the case. However, the determination that 12 percent is a reasonable fee follows the emerging trend within the Second Circuit of awarding attorneys considerably less than 30 percent of the common funds... even where there is considerable contingency risk.”
- *In re Telectronics Pacing Systems*⁴² – A nationwide class of 25,000 plaintiffs alleged that defendants distributed defective pacemaker leads that could fracture from metal fatigue. After a court of appeals rejected an initial settlement, the district court approved a revised settlement, which established a \$58.2 million patient benefit fund. Patients who had properly functioning leads received small monetary awards (\$500) and were eligible to participate in a medical monitoring program that provided ongoing screening. Patients who had undergone lead extraction were eligible for \$6,500 in damages. Patients who had suffered complications were eligible for damages ranging from \$11,500-\$200,000, depending on the severity of the complications they experienced. Nothing in the settlement prevented class members from seeking adjustments in their remedies if their condition worsened. In addition, the second settlement allowed class members to exclude themselves from the settlement and pursue individual litigation.

³⁹ 2002 U.S. Dist. LEXIS 11288 (E.D. Pa. 2002).

⁴⁰ 205 F.R.D. 369 (D.D.C. 2002).

⁴¹ 187 F. Supp. 2d 80 (E.D.N.Y. 2002).

⁴² 137 F. Supp. 2d 985 (S.D. Ohio 2001).

- *Brotherton v. Cleveland*⁴³ – This class action, which settled after ten years of litigation, arose from an Ohio law that permitted county coroners to harvest corneas for medical use under certain conditions, even where family member objected. The lead plaintiff sued after her deceased husband’s corneas were removed against her wishes. The court approved a settlement requiring the defendant to pay \$5.2 million into a settlement fund and to agree to cease harvesting corneas of autopsy subjects without consent by next of kin. A special master was appointed to distribute the settlement funds among class members. Class members received real cash.
- *Diamond Chemical Co. v. Azko Nobel Chemicals*⁴⁴ – Customers brought a class action against chemical companies alleging conspiracies to fix and raise prices of monochloroacetic acid and sodium monochloroacetate. The federal court approved a settlement that required cash payment equal to twenty percent of the sales of the two products to be made available to all persons or entities who purchased either product between 1995 and 1999. The bottom line: class members are receiving real cash.
- *Ingram v. Coca-Cola Company*⁴⁵ – The federal district court approved a settlement of a class action alleging race discrimination in promotions, compensation and performance evaluations. Under the settlement, Coca-Cola was required to make payments to class members from a Back Pay Fund of over \$24 million and a Compensatory Damages Fund of approximately \$59 million (guaranteeing each class member recovery averaging approximately \$38,000), and Coca-Cola was required to create a \$10 million Promotional Achievement Award Fund to pay bonuses to class members and to make pay equity adjustments to correct existing race-based inequities. In addition, Coca-Cola’s board was required to review and remain informed of the company’s progress toward achieving diversity goals, and the company had to create an outside, independent task force to evaluate existing human resources practices and policies, making recommendations for necessary reforms, investigating complaints and issuing written reports. The settlement also provided that class members could decline their share of the determined back pay amount, opting to obtain an individual hearing before a magistrate judge. Finally, the settlement provided for attorneys’ fees and expenses of \$20.7 million (approximately 20 percent of the total cash settlement fund). The class members received real money, and the class counsel received compensation for their efforts proportionate with what they achieved for the class.
- *Cullen v. Whitman Medical Corp.*⁴⁶ – The federal district court approved the settlement of a class action alleging fraudulent misrepresentation by a vocational school that taught sonography. The settlement provided \$5.97 million in cash and approximately \$1.3 million in loan forgiveness for delinquent obligations owed by students to the school. The settlement also included prospective relief that would be enforced by a court-appointed ombudsman, such as screening of faculty and a cooling-off period for admitted students to withdraw. The court approved class counsel’s request for an award of about 30% of the class compensation.

⁴³ 141 F. Supp. 2d 894 (S.D. Ohio 2001).

⁴⁴ 205 F.R.D. 33 (D.D.C. 2001).

⁴⁵ 200 F.R.D. 685 (N.D. Ga. 2001).

⁴⁶ 197 F.R.D. 136 (E.D. Pa. 2000).

The class received real monetary benefits, and counsel were adequately compensated for their efforts.

- *In re American Family Enterprises*⁴⁷ – In this case alleging fraud in sweepstakes mailings, a federal multidistrict litigation court approved a limited fund settlement of \$32 million, from which eligible class members would receive, on average, more than \$500 in refunds.
- *In re Motorsports Merchandise Antitrust Litigation*⁴⁸ – In this case, a 50,000-member class of purchasers of souvenirs and merchandise sold by defendants alleged that defendants engaged in a combination and conspiracy to fix and maintain prices for merchandise sold at professional stock car races. After extensive discovery, the parties reached settlement agreements proposing to pay class members in **both** cash (\$5.6 million) and coupons (valued at \$5.7 million). The federal district court concluded that the settlement was in the best interest of the class because establishing a class was difficult insofar as the items purchased were small and many class members did not retain proof of purchase. In addition, the court concluded that the coupon award was beneficial because: (1) the coupons were fully transferable to others; (2) defendants agreed to continue issuing coupons until the face value of each of the settlements was reached in redemptions; (3) the coupons were for small, frequently purchased items and would be redeemable for a year; (4) the coupons represented a sizeable discount on small, fungible items; and (5) coupons could be aggregated for higher discounts on items. In addition, the court determined that class members could not easily prove that they had suffered an injury as a result of defendants' conduct. "It is the Court's belief that the coupon program combined with the cash settlement and taking into account the risks and expenses of proceeding to trial with the possibility of no recovery, is well within the range of a fair, adequate and reasonable recovery." Furthermore, the court authorized an award of attorneys' fees based on the percentage of the cash recovery only so that class members would receive the full value of the coupon portion of the settlement.
- *Varljen v. H.J. Meyers & Co*⁴⁹ – A federal district court approved a settlement of \$4.04 million in cash and \$1 million in stock in this securities class action. The class of 24,461 plaintiffs alleged that the defendants artificially inflated and manipulated prices and spread false and misleading reports about the company. The court carefully considered attorneys' fees and costs and reduced the plaintiffs' counsel's request from \$1.6 million to \$800,000. Furthermore, the court reduced the request of additional law firms beyond lead counsel from \$240,454 to \$60,000, after reviewing the firms' descriptions of their work. "This amount reflects an amount between an unexamined lodestar figure for principal counsel – albeit one without any enhancement – and the 33 percent fee requested and, I believe, adequately recognizes the efforts of counsel and the risks and complexities of this litigation while ensuring sufficient remaining funds for distribution to class members."

In short, the federal court record speaks for itself. Federal courts do not reject coupon settlements *a priori*; however, they do engage in closer scrutiny of coupon settlements, are more

⁴⁷ 256 B.R. 377 (D. N.J. 2000).

⁴⁸ 112 F. Supp. 2d 1329 (N.D. Ga. 2000).

⁴⁹ 2000 U.S. Dist. LEXIS 16205 (S.D.N.Y. 2000).

likely to question attorneys' fees, and produce settlements in which the consumers get cash far more frequently than their state court counterparts.

IV. THE CLASS ACTION FAIRNESS ACT OF 2004

ILR supports the Class Action Fairness Act of 2004 and believes that this bipartisan compromise legislation would go a long way to resolving much of the class action abuse occurring throughout the country.⁵⁰ The Class Action Fairness Act would achieve this goal in a number of ways. First, it would allow federal courts to adjudicate more class actions in order to ensure that a small number of magnet state courts do not continue their abusive practice of simply rubber-stamping coupon settlements in which the vast majority of recovery goes to the lawyers as opposed to the plaintiffs. Second, it includes a "Class Action Consumer Bill of Rights" that would address many of the concerns that have been raised about coupon settlements. Among other things, the "bill of rights" would:

- ***Limit Attorneys' Fees In Coupon Settlements.*** One of the troubling phenomena that the FTC has noted in its amicus briefs is the growing number of class actions in which all the relief goes to the lawyers. The Class Action Fairness Act addresses this problem by requiring, in cases where the contingency fees in coupon settlements are based on the value of the coupons awarded to class members, that the fees be based on the value of coupons actually *redeemed*.⁵¹ Thus, if a settlement agreement promises \$5 million in coupons but only 1/5 of potential class members actually redeem the coupons at issue, then the lawyer's contingency fee should be based on a recovery of \$1 million – not a recovery of \$5 million. The provision also allows a court to hear expert testimony on the actual value of redeemed coupons to assist the court in determining the proper contingent fee. This provision addresses the situation where the actual value of the coupons differs from their face value. For example, a coupon for \$250 off a vehicle purchase may not really be worth \$250. The provision also allows for the attorneys to be paid based on an hourly rate (with a multiplier) and for achieving equitable relief in addition to any coupons.
- ***Require Adequate Review of Coupon Settlements.*** Under the bill, a federal judge may not approve a coupon or other similar noncash settlement without first conducting a hearing and determining that the settlement terms are fair, reasonable, and adequate for class members. In making that determination, the judge should consider, among other things, the real monetary value and likely utilization rate of the coupons provided by the settlement. A federal court may, in its discretion, require that a proposed settlement provide for the distribution of a portion of the value of unclaimed coupons to a charitable organization or government entity; however, any such distribution shall not be used as the basis for the award of any attorneys' fees.⁵²

⁵⁰ The U.S. House of Representatives passed H.R. 1115 on June 12, 2003. Although more than 60 Senators have expressed support for the Senate version of the bill, S. 2062, the Senate has not yet voted on the legislation because of a disagreement between Democrats and Republicans regarding non-germane amendments that led to a filibuster. See *Senate Abandons Class Action Lawsuit Bill*, Associated Press, July 8, 2004.

⁵¹ See S. 2062, 108th Cong. § 3 (2004).

⁵² *Id.* The House bill has a similar provision but does not include the provision regarding charitable organizations. See H.R. 1115, 108th Cong. § 3 (2003).

- ***Protect Consumers Against Net Loss Settlements.*** One of the most notorious class action settlements in history was the Bank of Boston in which the settlement provided that class members (many of whom had no actual knowledge of the suit) would receive credits of up to \$8.76 to their bank accounts – while the accounts were debited up to \$90 to pay their attorneys’ fees. The bill addresses this concern by providing that a federal judge may not approve a class action settlement in which a class member will be required to pay attorneys’ fees that would result in a net loss to the class members unless the judge makes a written finding that the benefits to the class members “substantially outweigh” the monetary loss.⁵³
- ***Protect Against Discrimination Based On Geographic Location.*** This provision states that a federal court settlement may not award some class members a larger recovery than others simply because the favored members of the class live closer to the courthouse in which the settlement is filed than do the disfavored class members. The provision, which responds to cases in which settlements have discriminated on the basis of geography, provides assurance that out-of-state class members are not disadvantaged by the parochialism of local judges.⁵⁴
- ***Require Notice Of Proposed Settlements To Appropriate Federal And State Officials.*** The notification provision of the Class Action Fairness Act is designed to ensure that a responsible state and/or federal official receives information about proposed class action settlements and is in a position to react if the settlement appears unfair to some or all class members or inconsistent with applicable regulatory policies. Section 1715 requires each defendant, within 10 days after a proposed class action settlement is filed in federal court, to provide notice of the proposed settlement to: (1) the U.S. Attorney General (or for banks and thrifts, the entity with primary regulatory or supervisory responsibility over the defendant); and (2) the state official that has primary regulatory or supervisory responsibility over the defendant or who licenses or otherwise authorizes the defendant to conduct business in the state (or for state depository institutions, the state bank supervisor in the state in which the defendant is incorporated or chartered).⁵⁵

V. CONCLUSION

The Institute for Legal Reform is pleased to have the opportunity to participate in the important debate about how to reform the class action system and ensure that class actions are a tool to redress legitimate consumer grievances rather than a vehicle for the enrichment of lawyers. The FTC’s efforts to date – both through the filing of amicus briefs and in sponsoring this important workshop – demonstrate a strong commitment to addressing a problem that is hurting consumers, dragging the American economy and undermining confidence in the judicial system.

⁵³ See S. 2062, § 3; H.R. 1115 § 3.

⁵⁴ *Id.*

⁵⁵ See S. 2062, § 3. The House bill does not have a parallel provision.