

## Summary of Remarks of Professor Christopher R. Leslie, Chicago-Kent College of Law

Private causes of action generally exist to achieve two goals: (1) compensation for the victims, and (2) disgorgement of the ill-gotten gains of wrongdoers in order to make their misdeeds not cost-beneficial, in the hopes of deterring such conduct in the future.

Class action litigation exists to allow individuals with small claims to aggregate their causes of action. But the class action vehicle does not change the two underlying purposes of private suits, compensation and disgorgement. Instead, it seeks to allow those with small claims the opportunity to achieve those same goals, even when the ordinary costs of litigation would lead individuals not to pursue their small claims.

Like most private litigation, most class action lawsuits settle. In general, any settlement's merits should be evaluated based on the settlement's likelihood of achieving the twin goals of compensation and deterrence. However, unlike traditional litigation, the plaintiffs in a class action (i.e. the class members) have little say in the actual conduct of the litigation, including how it is settled. This has led to many class actions being settled by the defendant paying the class members in coupons. The anecdotal evidence suggests that such coupon-based settlements often fail to achieve either the compensation or deterrence goals of litigation.

When class members are paid in coupons, each class member will have one of four outcomes. First, the class member might not use coupon at all. Second, she could use the coupon because it induced her to make a purchase that she otherwise would not have made. Third, she could use her coupon for a purchase that she was planning to make anyway. Fourth, she could transfer (e.g., sell) the settlement coupon to a third-party who uses it.

The first outcome, the Non-Use Outcome, results in the class member receiving nothing of value from the settlement. There is no compensation. Similarly, the defendant pays out nothing to the class member. There is no disgorgement.

The second outcome, the Induced-Purchase Outcome, occurs when the class member makes a purchase with her settlement coupon simply to avoid the feeling of getting nothing from the settlement. The defendant is actually in a better position in this scenario because it makes a sale and some marginal profit. The settlement coupon operates as a promotional coupon.

The third outcome, the Non-Induced-Purchase Outcome, shows that settlement coupons are not inherently worthless. The class member who uses the coupon for planned purchase receives in essence a payment worth the face value of the coupon. The defendant loses money if that purchase would have taken place without the use of any coupons (settlement or promotion).

The fourth outcome, the Transferred-Use Outcome, is a variant of the third, only someone other than the class member is making the non-induced purchase. The class

member receives value if she sells the settlement coupon to the person who eventually uses it, although such sale is likely to take place at a price below the coupon's face value.

Because defendants prefer outcomes where the class member either does not use the coupon (and the defendant thus pays nothing) or uses the coupon to make an induced purchase (and the defendant actually earns additional revenues), defendants often structure settlement coupons to increase the probability of achieving one of these two outcomes. They do this by imposing transfer restrictions, short expiration dates, aggregation limits, and product restrictions. Such restrictions increase the probability of the coupon either not being used at all or inducing a purchase right before the coupon expires. The success of such tactics is demonstrated by the fact that it appears that in many class actions, the Non-Use Outcome is the most common result. Most of the coupons are simply not used. Most class members receive nothing. Such a result must be considered a failure, measured against the purposes of allowing litigation in the first place.

How can this result occur, given that in the litigation process the class members have both their own attorneys and the judge (who must approve the proposed settlement) to protect the class members' interests? Evidence and theory suggest that the class counsel may permit defendants to pay class members with settlement coupons laden with restrictions in exchange for a higher payment in attorneys' fees. In recognition of the risk of class counsel selling out the class, Rule 23(e) requires the judge to approve any proposed settlement to a class action lawsuit. But judges frequently, though not always, approve coupon-based settlements that are inadequate. Part of the problem is that coupons create noise. The restrictions make it difficult for a judge to predict whether class members will use the coupons. Furthermore, during the judge's consideration of the proposed settlement, both the defendant and class counsel are informing the court that the coupons are valuable.

In sum, despite the safeguards in place to protect the class members, the problem remains that class action litigation is often settled with coupons that are largely worthless to many class members. Courts and the FTC should consider ways to address the issues associated with coupon-based settlements. This forum is a huge step in the right direction. In my scholarship, I have discussed possible approaches, such as banning coupon settlements, restructuring settlement coupons, imposing or encouraging minimum redemption rates, and requiring that class counsel be paid in the same currency as the class. In this forum, I would like to consider two new potential solutions: greater data collection and FTC intervention in fairness hearings to evaluate coupon-based settlements.

As an academic, I think that the next step is data collection. The evidence that we have on redemption rates is largely anecdotal because information on redemption is not generally public; there is no requirement that defendants and/or class counsel collect and report data on what happens after the settlement coupons are distributed. It is hard to know the full extent of the problem because we do not have accurate data on how many

coupon-based settlements there are, what restrictions the coupons contain, what the redemption rates are, what the class counsel actually received as attorneys' fees, etc.

Because it is difficult for academics, public interest organizations, and government officials (such as the FTC) to diagnose the problem if we are never allowed to see the patient, I recommend that after every coupon-based settlement, class counsel and defendants be required to file in a central public repository disclosure statements that include the number of coupons distributed and ultimately redeemed, as well as all of the coupon terms and copies of the actual coupons themselves and all instructions distributed to the class. Researchers should also have access to defendants' sales data for a meaningful period of time before the issuance of the coupons, during the redemption period, and afterwards. This will allow researchers to estimate how many redemptions of settlement coupons reflect the Induced-Purchase Outcome.

Over time, greater openness about redemption rates would yield two advantages. First, it is too difficult to determine after the fact whether coupon-based settlements do provide meaningful compensation or are routinely inadequate if scholars, public interest attorneys, and government officials are denied access to the necessary data. Making this data available will help researchers determine what coupon terms are associated with low redemption rates so that we can better predict whether future coupon-based settlements will be likely to compensate class members.

Second, accurate public knowledge about coupon structure and redemption rates helps the market for class counsel work more efficiently. When class counsel are competing for the right to represent the class, a judge should look at their previous performance. If the law firm has negotiated coupon-based settlements with low redemption rates, this is strong evidence that these attorneys may be ineffective class counsel, the types of attorneys who would sell out the class in order to pursue their own interests and who should not be permitted to represent the class in future class action litigation (whenever the judge is in a position to select the class counsel). Knowing that their negotiation of inadequate coupon-based settlements in class action litigation in the past could affect their ability to serve as class counsel in the future should provide a strong incentive for class counsel not to negotiate coupon-based settlements that confer little or no value on the class.

In addition to facilitating greater access to data on coupon-based settlements, the FTC should consider becoming more involved in individual cases. The collective action problem that necessitates class action litigation in the first place replicates itself at the settlement stage: for each individual class member, the costs of objecting to an adequate settlement – whether based on coupons or not – outweighs the expected benefits of objecting. This is especially true given that courts generally ignore the objections of individual class members. Thus, no matter how inadequate a proposed settlement is, it is generally rational for class members to not object.

The FTC can help solve this collective action problem by objecting to suspect settlements. After understanding the underlying data on coupon-based settlements, the

FTC will be a good position to inform courts as to whether a particular proposed coupon-based settlement will likely prove inadequate and, thus, should be rejected. If the FTC were to begin objecting, objections would be taken seriously.

Of course, some will find greater government involvement in private litigation controversial. The most likely criticism is that without the ability to negotiate coupon-based settlements, much class action litigation might not settle. My response is simple: if the only settlement that you can structure neither disgorges the ill-gotten gains nor compensates the class (despite eliminating their ability to bring individual actions), you should not settle the case at all. If eliminating the possibility of such settlements means that class action attorneys will not initiate a class action lawsuit, then the suit should not be brought. The class action vehicle does not exist to serve the interests of the class counsel; it is there primary to compensate the class. If the result will not compensate the class, then class action litigation should not be initiated.