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February 15, 2017

Ms. Rebecca A. Womeldorf
Secretary of the Committee on Rules and Practice
and Procedure of the Administrative Office of the
United States Courts
One Columbus Circle, NE
Washington, D.C. 20544

Re: CEI Comments to Proposed Amendments to Federal Rule Civil Procedure 23

Ms. Womeldorf:

On behalf of the Competitive Enterprise Institute (CEI), we respectfully submit these comments regarding proposed amendments to Rule 23 of the Federal Rules of Civil Procedure presently under consideration by the Civil Rules Advisory Committee and its Rule 23 Subcommittee.

Please contact Mr. Frank at (202) 331-2263 or ted.frank@cei.org if you have any questions.

Sincerely,

/s/ Theodore H. Frank
Theodore H. Frank

/s/ Melissa A. Holyoak
Melissa A. Holyoak

COMPETITIVE ENTERPRISE INSTITUTE'S CENTER FOR CLASS ACTION FAIRNESS

COMMENTS
to the
CIVIL RULES ADVISORY COMMITTEE
AND ITS RULE 23 SUBCOMMITTEE

Competitive Enterprise Institute (CEI) respectfully submits these comments regarding the proposed amendments to Rule 23 of the Federal Rules of Civil Procedure presently under consideration by the Civil Rules Advisory Committee and its Rule 23 Subcommittee ("Proposed Amendments").[1] CEI is a nonprofit public interest organization dedicated to the principles of limited constitutional government and free enterprise. The authors of these comments are CEI Senior Attorney and Director of the Center for Class Action Fairness, Theodore H. Frank, and CEI Senior Attorney Melissa A. Holyoak.

Interest of the Commenters

CEI's Center for Class Action Fairness represents class members *pro bono* against unfair class action settlements and procedures. Since the Center's inception in 2009,[2] it has won numerous appellate landmark decisions protecting class members' rights, and has secured over $100 million for class members that otherwise might have gone to trial attorneys or unrelated third parties. The *New York Times* calls Mr. Frank the leading critic of abusive class-action settlements. *See* Adam Liptak, *When Lawyers Cut Their Clients Out of the Deal,* N.Y. TIMES, Aug. 13, 2013, at A12.

Summary

It is important to understand that, in practice, rules relating to class-action settlements will most often be litigated in *ex parte* circumstances where settling parties will seek interpretations favorable to themselves at the expense of absent class members. If rules do not explicitly bind settling parties, courts will tend to adopt interpretations and create precedents permitting abuse. The Proposed Amendments to Rule 23(e)(2) therefore do not adequately protect the class from self-dealing settlements where class counsel is the primary beneficiary. Settlements will continue to be approved where attorneys' fees are disproportionate to the relief *actually* received by the class. The

1 Proposed Amendments to the Federal Rules of Appellate, Bankruptcy, Civil, and Criminal Procedure ("Proposed Amendments"), available at http://www.uscourts.gov/sites/default/files/2016-08preliminary_draft_of_rules_forms_published_for_public_comment_0.pdf.

2 On October 1, 2015, the Center merged with the non-profit Competitive Enterprise Institute.

Advisory Committee tried to fix this problem in 2003 when Rule 23(h) was created, but Rule 23(h) failed to explicitly require courts to determine whether class counsel's fee request was proportionate to relief actually received and the Advisory Committee's intent went ignored. Now courts are split as to whether fees may be awarded based on actual relief and the Rules risk undoing the precedent that requires courts to determine whether fees are proportionate. To end the circuit split and avoid repeating the deficiency of the 2003 Amendments, the Rules should explicitly require that district courts consider the proportion of fees to relief actually received by class members, and explicitly reject the line of precedent that permits parties to value settlements based on the fiction of maximum possible relief, when in practice parties can predict with actuarial certainty the claims rate of a settlement structure. Indeed, the Rules should provide additional protections by requiring district courts to consider whether class counsel negotiated clear sailing, reversion, or *cy pres* awards that prioritize relief to third parties when assessing adequacy of class counsel.

The Proposed Amendments to Rule 23(e)(5) should be deleted. Proposed Paragraph (A) requiring specificity for objections is unnecessary because district courts and parties can already effectively manage non-specific objections and will instead create collateral litigation. Paragraph (A) will only serve as a mechanism for class counsel to eliminate objections that may derail their self-dealing settlements.

Proposed Paragraphs (B) and (C)—requiring court approval for settlement of objections—will, as conferences discussing the amendments have shown, be ineffective in ending objector blackmail (extortionate payments to objectors in exchange for dismissal of their appeals) because the Rules fail to adopt a standard that objectors must satisfy for approval of their settlement with class counsel. The Proposed Amendments do nothing to address the real problem: objectors are more motivated to bring bad-faith objections than good-faith objections because there is a greater chance of payment in objector blackmail than in successfully litigating an objection. The Rules need to eliminate the incentive for objector blackmail by eliminating the possibility of receiving consideration for dismissal of appeal and instead, create incentives for good faith objections by explicitly recognizing that objectors who realize a benefit for the class are entitled to attorneys' fees. Under current law, only non-profit organizations have the ability to consistently see through meritorious objections.

I. Amendments to Rule 23(e)(2) as Proposed Will Permit Approval of Unfair Class Action Settlements.

The Proposed Amendments to Rule 23(e)(2) incorporate factors a district court must consider in determining whether a proposed class action settlement is fair, reasonable and adequate:

> (A) the class representatives and class counsel have adequately represented the class;
>
> (B) the proposal was negotiated at arm's length;
>
> (C) the relief provided for the class is adequate, taking into account:
>
> > (i) the costs, risks, and delay of trial and appeal;
> >
> > (ii) the effectiveness of the proposed method of distributing relief to the class, including the method of processing class-member claims, if required;
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> > (iii) the terms of any proposed award of attorney's fees, including timing of payment; and
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> > (iv) any agreement required to be identified under Rule 23(e)(3); and
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> (D) class members are treated equitably relative to each other.

See Proposed Amendments at 213-214.

As the Committee Notes to the Proposed Amendments observe, circuit courts have developed lengthy, "distracting" lists of factors to consider in approving class action settlements. *See id.* at 224-225. The Proposed Amendments are intended to focus the court on the "core concerns" in deciding whether a class action settlement should be approved. *Id.* at 224. The Proposed Amendments correctly identify the adequacy of class counsel and the award of attorneys' fees as a core concern when assessing whether the settlement relief is fair. *See id.* at 214 (Paragraph 23(e)(2)(C)(iii)). As drafted, however, the Proposed Amendments are not explicit enough to protect the class from attorneys' fee requests that may be disproportionate to the relief *actually* received by the class as well as other unfair settlement provisions that often cost class members millions of dollars.

A. Because of the *ex parte* nature of the settlement approval process in most cases, if the Proposed Amendments do not explicitly require the court to consider whether the requested fees are disproportionate to actual class relief, then the future Rules will be distorted to promote self-dealing settlements.

When negotiating a class action settlement, class counsel and defendants are both incentivized to bargain effectively over the size of the settlement. But defendant only cares about the "bottom line" and will take the deal that drives down the total cost to defendant, with "no reason to care about the allocation of its cost of settlement between class counsel and class members." *See Pearson v. NBTY, Inc.*, 772 F.3d 778, 783 (7th Cir. 2014). Class counsel, on the other hand, are incentivized to seek as large a portion of the relief as possible for themselves, and may accept bargains that are worse for the class in exchange for a larger piece of the pie. *Id.* at 783-84.

Together, class counsel and defendants have a mutual interest in creating the illusion of relief rather than actual relief to the class: the optimal settlement for class counsel maximizes attorneys' fees, while the defendant is seeking only to minimize its total expenditure with indifference to where the settlement money actually goes. *See Redman v. RadioShack Corp.*, 768 F.3d 622 (7th Cir. 2014) (Posner, J.); *Eubank v. Pella Corp.*, 753 F.3d 718, 720 (7th Cir. 2014) (Posner, J.) ("From the selfish standpoint of class counsel and the defendant, … the optimal settlement is one modest in overall amount but heavily tilted toward attorneys' fees."). *See generally*, Howard Erichson, *Aggregation As Disempowerment: Red Flags in Class Action Settlements*, 92 N.D. L. REV. 859 (2016); Erin L. Sheley & Theodore H. Frank, *Prospective Injunctive Relief and Class Settlements*, 39 HARV. J. L. & PUB. POL'Y 769 (2016).

The classic example of illusory relief is the coupon settlement, which "provides class counsel with the opportunity to puff the perceived value of the settlement so as to enhance their own compensation." *In re HP Inkjet Printer Litig.*, 716 F.3d 1173, 1179 (9th Cir. 2013). The Class Action Fairness Act (CAFA), 28 U.S.C. § 1712, sought to preclude parties from taking credit for 100% of the face value of coupons when the actual redemption rates are typically less than 1%. But even with this bright-line principle, district courts' application remains inconsistent because the settling parties often refuse to admit that a settlement is offering "coupons" to the class members. *E.g., Redman*, 768 F.3d at 635 (rejecting class counsel's argument that settlement "vouchers" were not coupons under CAFA).

The problem is that the settling parties' *ex parte* presentation of the class action settlement deprives the court of an adversarial system. As Judge Posner explained:

> A trial judge's instinct, in our adversarial system of legal justice, is to approve a settlement, trusting the parties to have negotiated to a just result as an alternative to bearing the risks and costs of litigation. But the law quite rightly requires more than a judicial rubber stamp when the lawsuit that the parties have agreed to settle is a class action. The reason is the built-in conflict of interest in class action suits.

See Redman, 768 F.3d at 629.[3] District courts depend on an adversary system, one that involves independent, unconflicted counsel. District courts have neither the time nor the resources to step into that adversarial role and unearth the illusory relief, the self-dealing settlement structure and provisions, and the self-interested interpretations of the Civil Rules and legal precedent.

When the district courts are presented with a settlement that will take a years-old case off their dockets, and both parties are telling the judge that the settlement is a good deal for their clients and complies with the Rules, district courts will bend over backwards to approve settlements, even when they are unfair for absent class members. Take for example, *In re EasySaver Rewards Litig.*, 921 F. Supp. 2d 1040 (S.D. Cal. 2013), *rev'd* No. 13-55373, 599 Fed. Appx. 274 (9th Cir. Mar. 19, 2015).

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3 *See also* Ted Frank, *Class Actions, Arbitration, and Consumer Rights*, Legal Policy Report No. 16 at 6-11 (Manhattan Institute 2013); Lester Brickman, LAWYER BARONS 335-72 (Cambridge U. Press 2011); John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 COLUM. L. REV. 1343, 1347-48 (1995); Coffee, 54 U. CHI. L. REV. at 883-84; Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 7-8 (1991).

Plaintiffs claimed that defendants' gift- and flower-delivery websites violated state and federal law by enrolling customers in rewards programs after luring them with the promise of worthless coupons. Class counsel negotiated a settlement where 0.2% of the class received cash ($225,000) and the remaining class members received low-value coupons, while $8.85 million went to plaintiffs' lawyers and $3 million to *cy pres* including class counsel's alma maters. The district court agreed with the parties that the settlement "e-credits" were not "coupons," and valued them at full face value for determining settlement fairness and fees—even though the "e-credits" were called coupons in the Rule 8 complaint, they expired in a year, could only be used to purchase flowers and other gifts, were neither transferable or usable in conjunction with other coupons, and could not be used in the weeks before or of Valentine's Day, Mother's Day, and Christmas. 921 F. Supp. 2d at 1048-49. The Ninth Circuit vacated the settlement approval and remanded for further consideration. 599 Fed. Appx. at 275. But even on remand, the district court repeated its finding. In 2016 U.S. Dist. LEXIS 105152 (S.D. Cal. Aug. 9, 2016). The Civil Rules must be explicit and drafted to limit district courts from adopting class counsel's self-interested interpretations.

Claims-made settlements are no different economically from coupon settlements. In both types of settlements, the defendant "makes available" a certain amount of relief, but can expect to pay only a fraction of that amount because of low claims rates. But like coupon settlements, class counsel exploit their conflict of interest by seeking fees based on the amount "available" and not what the class will *actually* receive. The circuit courts of appeals to have considered the issue are split. The Proposed Amendments do not resolve the split and worse, they may undo the progress some circuits have made in protecting absent class members. The Rules must be explicit regarding the valuing of settlement relief when assessing the attorneys' fee award.

1. The Proposed Amendments do not resolve the circuit split regarding valuation of settlement relief when assessing fairness and attorneys' fee awards but instead, the Amendments risk reversing the legal precedents that protect class members from self-dealing settlements.

Several courts have recognized the inherent conflict between class counsel and the class during settlement negotiations and have required an additional inquiry beyond the typical multi-factors tests for fairness: Have the class attorneys engaged in self-dealing to structure the settlement so that they are receiving preferential treatment vis-à-vis the clients to whom they have a fiduciary duty? *See In re Dry Max Pampers Litig.*, 724 F.3d 713, 718 (6th Cir. 2013) (looking beyond Sixth Circuit's seven-factor test to find settlement unfair when it constitutes "preferential treatment" for class counsel); *In re Baby Prods. Antitrust Litig.*, 708 F.3d 163, 174 (3d Cir. 2013) (failure to consider "the degree of direct benefit provided to the class" reversible error, though not in Third Circuit's nine-factor test). These appellate courts have employed doctrinal tests to correctly align the incentives of class counsel with those of the absent class members. Most notably, the Seventh Circuit has held that it will compare the attorney award only to the amount *actually* realized by the class: "the ratio that is relevant ... is the ratio of (1) the fee to (2) the fee plus what the class members received." *Pearson*, 772 F.3d at 781, *Redman*, 768 F.3d at 630.

Pearson involved claims regarding the marketing of glucosamine nutritional supplements. 772 F.3d at 779. While there were over 12 million class members, only 30,245 class members claimed $865,284; the settlement also provided a $1.13 million *cy pres* award and an injunction against certain marketing practices. *Id.* at 780, 784. Class counsel requested $4.5 million and the district court awarded $1.93 million in fees. *Id.* at 780. The Seventh Circuit reversed settlement approval, finding

that the "problem with the district judge's decision is not that it leans too far in favor of the objectors, as class counsel contend, but that it doesn't lean far enough." *Id.* The Seventh Circuit held that the district court correctly excluded the *cy pres* award in calculating the benefit to the class "for the obvious reason that the recipient of that award was not a member of the class" and that the court properly valued the injunction at zero. *Id.* at 781. Seventh Circuit held that the district court erred, however, in valuing the settlement with the "maximum *potential* payment" that class members could receive. *Id.* at 780.

The Third Circuit and the Ninth Circuit have reached similar conclusions. *Allen v. Bedolla*, 787 F.3d 1218, 1224 n.4 (9th Cir. 2015) (reversing approval because although $1.125 million was 25% of gross fund, "economic reality" was that fee request was three times more than what class would actually receive); *In re Baby Prods. Litig.*, 708 F.3d 163, 169-70, 179 (3d Cir. 2013) (rejecting settlement that gave $3 million to class, $14 million to attorneys' and $18.5 million to *cy pres* and administrative expenses because class members were not "foremost beneficiaries of the settlement").

By contrast, a settlement nearly identical to *Pearson* (but with even *worse* results) was upheld in the Eleventh Circuit. In *Poertner v. Gillette Co.*, the Eleventh Circuit affirmed a settlement involving claims regarding marketing of a line of Duracell batteries. 618 Fed. Appx. 624, 625 (11th Cir. July 16, 2015) (unpublished). Under the settlement, class members received less than $345,000 (and over 99 percent of the class got zero), defendant would give $6 million in batteries to a third-party charity (*cy pres* award) and defendant agreed to an injunction preventing marketing of a discontinued line of batteries. *Id.* at 626. Class counsel requested over $5 million in fees based on an estimated settlement value of $50 million. *Id.* But class counsel based it on the assumption that *every* class member would file a claim, even though they were fully aware that only a tiny fraction would. *Id.* at 626 n.1. The Eleventh Circuit upheld the settlement—even though the attorneys received ***nearly 15 times more*** than their "putative clients"—because its Rule 23(e) precedents allowed vague notions of the settlement's overall value in direct conflict with other circuits' rules. *Id.* at 630. Predictably, similarly structured settlements are flowing into Eleventh Circuit courts relying on the *Poertner* decision. *See, e.g., Braynen v. Nationstar Mortg.*, LLC, No. 14-CV-20726, 2015 WL 6872519, 2015 U.S. Dist. LEXIS 151744, *55-57 (S.D. Fla. Nov. 9, 2015) (approving claims-made settlement and $5 million fee without claim-rate or actual recovery information); *Marty v. Anheuser-Busch Cos.*, No. 13-cv-23656-JJO, 2015 WL 6391185, 2015 U.S. Dist. LEXIS 144290, *4-*5 (S.D. Fla. Oct. 22, 2015) (approving $3.5 million fee and rejecting objection that court should consider the actual amount of claims paid).

Like the Eleventh Circuit, the Sixth Circuit upheld a settlement where class counsel received a disproportionate fee award. Though the settling parties had the addresses of the class members and knew precisely what each class member was entitled to under the terms of the settlement, the settlement was structured as a claims-made settlement, with the settlement administrator testifying under oath that this structure could be expected to pay less than ten percent of the class's claims. The class received less than $1.6 million (49,808 claims of the 600,000 class members) but class counsel sought to justify their $2.39 million fee request by arguing to the district court that the settlement value was $15.5 million because that was the total *available benefit* to the class. *Gascho v. Global Fitness Holdings, LLC*, 822 F.3d 269, 277 (6th Cir. 2016). The district court decided to split the difference—without any economic explanation why an unclaimed award is worth anything to a class member, much less 50% of its unclaimed value—and held that the class benefit should be valued at $8.5 million. *Id.* at 288. The Sixth Circuit affirmed in a split decision, with the majority opinion citing

a law-review article suggesting there was nothing problematic if 100% of settlement benefit went to class counsel. *Id.*[4]

That class counsel should be given credit for making the entire maximum available—because they somehow have "no control" over the amount that is claimed—is one of the greatest fictions presented by class counsel. When class counsel structures a claims-made settlement, they are fully aware that 99% of the class will go uncompensated because those class members will not submit claims. In *Poertner,* class counsel attempted to defend the low number of claims by presenting a study of hundreds of class-action settlements that showed that the median settlement pays only 0.23% of the class. *See* Daniel Fisher, *Odds of a Payoff in Consumer Class Action? Less Than a Straight Flush*, FORBES (May 8, 2014) (discussing evidence presented in *Poertner*); Alison Frankel, *A Smoking Gun in Debate over Consumer Class Actions?*, REUTERS (May 9, 2014) (noting that median claims rate in such cases is "1 claim per 4,350 class members").

Not only can class counsel accurately predict the claims rates, they can manipulate them with actuarial certainty. Risk Settlements, a company that offers post-lawsuit insurance for class action settlements, market their services to prospective clients by explaining that class-action defendants can save millions of dollars if they use claims-made settlements instead of common funds. *See* http://risksettlements.com/case-studies/case-study-a (saving client $7.5 million by restricting from common fund to claims-made settlement). But as Risk Settlements explains, each claims-made settlement can be "individually design[ed]" to reduce cost by using "historical database and risk assessment predictive system." *See* http://risksettlements.com/case-studies/case-study-a; *see generally* Theodore H. Frank, *Settlement Insurance Shows Need for Court Skepticism in Class Actions*, OpenMarket blog (Aug. 31, 2016), available at https://cei.org/blog/settlement-insurance-shows-need-court-skepticism-class-actions; *cf. also* Brian T. Fitzpatrick & Robert C. Gilbert, *An Empirical Look at Compensation in Consumer Class Actions,* 11 N.Y.U. J. OF LAW AND BUSINESS 767, 783 (2015) (empirical data showed that a higher percentage of class members received compensation in settlements with direct payments compared to settlements with a claims process and that class members negotiated postcard-sized checks less often than standard-sized checks). Parties can structure the claims process to ensure that very little money actually reaches the class. *E.g., Dry Max Pampers,* 724 F.3d at 718; *Eubank v. Pella Corp.*, 753 F.3d 718 (7th Cir. 2014); *Pearson v. NBTY*, 772 F.3d 778 (7th Cir. 2014).

When class counsel's fee award is compared to the amount *actually* received by the class, the comparison "gives class counsel an incentive to design the claims process in such a way as will maximize the settlement benefits actually received by the class, rather than to connive with the defendant in formulating claims-filing procedures that discourage filing and so reduce the benefit to the class." *Pearson*, 772 F.3d at 781. Conversely, "[w]hen the parties to a class action expect that the reasonableness of the attorneys' fees allowed to class counsel will be judged against the potential rather than actual or at least reasonably foreseeable benefits to the class, class counsel lack any incentive to push back against the defendant's creating a burdensome claims process in order to minimize the number of claims." *Id.* at 783.

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4 CCAF has petitioned for writ of certiorari. *See Blackman v. Gascho*, No 16-364 (U.S.). Attorneys General from seventeen states filed an *amici* brief in support of CCAF's position that fees must be awarded and settlements must be judged based on the actual relief received. *Id.*

The idea that class counsel will respond to these incentives by more carefully working to ensure settlement money gets to class members is more than theoretical, and has been borne out by the Center's experience. On remand from the *Baby Products* reversal, the parties determined that they had access to a list of class members, arranged for direct distribution of settlement proceeds, and paid an additional $14.45 million to over one million class members—money the parties initially directed to *cy pres* before the successful objection led to an "exponential increase" in class recovery. *McDonough v. Toys "R" Us, Inc.*, 80 F. Supp. 3d 626, 660 (E.D. Pa. 2015). After the Center objected to a claims-made settlement in a settlement over alleged false advertising of aspirin, the parties used subpoenaed third-party retailer data to identify over a million class members (instead of the 18,938 who would have been paid $5 each in the original claims-made structure), and paid an additional $5.84 million to the class. Order at 4, *In re Bayer Corp. Litig.,* No. 09-md-2023, Doc. 254 (E.D.N.Y. Nov. 8, 2013). And on remand in *Pearson*, the parties renegotiated to give class members at least $4 million more in cash, with any reduction in attorneys' fees now going to class members rather than back to defendants. Settlement ¶¶ 7-8, No. 11-cv-07972, Doc. 213-1 (N.D. Ill. May 14, 2015). In short, as *Pearson* predicted, if courts require lawyers get money to clients in order to get paid, that is *exactly* what happens.

The Proposed Amendments should resolve the circuit split and adopt the Seventh Circuit's requirement that fees be compared to what the class *actually* receives and the Committee Notes should specifically reject the approach adopted by the Eleventh and Sixth Circuits. The Seventh Circuit approach aligns the interests of class counsel and the class: class counsel will be incentivized to get as much money as possible in the class members' pockets.[5] As currently drafted, the Proposed Amendments do not resolve the split. Instead, class counsel will argue that Paragraph (e)(2)(C)(iii)—requiring the court to simply "take into account" the fees in considering the adequacy of class relief—does not affect the circuit split and courts may employ the Eleventh and Sixth Circuit's approach to consider the relief made *available* in awarding fees.

Worse yet, settling parties may argue that the newly adopted Rule 23(e) (and factors set forth in Rule 23(e)(2)(C)) supersede the legal precedent in the Third, Seventh, and Ninth Circuits requiring district courts to consider what the class *actually* receives in awarding fees.[6] **If the Proposed Amendments do not explicitly require courts to consider the actual relief awarded, the legal**

5 This would also solve many of the problems associated with *cy pres* awards. "A *cy pres* award is supposed to be limited to money that can't feasibly be awarded to the intended beneficiaries, here consisting of the class members." *Pearson*, 772 F.3d at 784 (rejecting $1.13 million *cy pres* award because distribution was possible to class members); *In re BankAmerica Corp. Sec. Litig.*, 775 F.3d 1060, 1063-64 (8th Cir. 2015) (rejecting $2.7 million *cy pres* award where third distribution to class members was possible). If class counsel is only paid for money delivered to the class (and not third parties), class counsel is incentivized to negotiate settlements that prioritize payments to class members rather than third-party *cy pres* recipients. *See, e.g., Pearson,* 772 F.3d at 781 (comparing class counsel's fee award only to amounts delivered to class and not the $1.13 million *cy pres* distribution when assessing settlement fairness).

6 The Committee Notes to the Proposed Amendments explain that the "goal" of 23(e)(2)(C) is not to "displace" the factors contained in the various multi-factor tests. *See* Proposed Amendments at 224. Although this would support an argument that the legal precedents in the Third, Seventh, and Ninth Circuits are not superseded by the future adopted Rules, as further explained below, the Committee Notes have largely been ignored and may not prevent the reversal of those precedents that protect absent class members.

precedents protecting class members may be reversed. In the future, during the settling parties' *ex parte* presentation of a class action settlement, class counsel will replace the "superseded" precedent with a self-interested interpretation of the newly adopted Rules that follows the Eleventh and Sixth Circuit approach.

2. Just as the Committee Notes to the 2003 Amendments to the Civil Procedure Rules did not effectively stop disproportionate 23(h) awards, the Committee Notes to the Proposed Amendments will also be ignored when unfavorable to settling parties.

The guidance contained in the Committee Notes to the Proposed Amendments are not sufficient to address the concerns regarding self-dealing settlements. Consistent with the Seventh Circuit's approach, the Committee Notes to the Proposed Amendments observe that "the ***relief actually delivered*** to the class can be an important factor in determining the appropriate fee award." *See* Proposed Amendments at 227 (emphasis added). Mr. Frank has had conversations with Federal Judiciary Center members who were surprised that this guidance did not resolve the controversy in favor of requiring consideration of actual recovery. But like the Committee Notes to the 2003 Amendments, the guidance in the Notes to the Proposed Amendments will be ignored.

In 2003, the Rules were amended to include Rule 23(h), which permits a court to award "reasonable attorney's fees" in connection with a class action settlement. *See* Fed. R. Civ. P. 23(h). The Committee Notes to the 2003 Amendments directed courts to consider the relief *actually* received by the class in determining the reasonableness of class counsel's fee award:

> Courts discharging this responsibility have looked to a variety of factors. **One fundamental focus is the result actually achieved for class members, a basic consideration in any case in which fees are sought on the basis of a benefit achieved for class members**. The Private Securities Litigation Reform Act of 1995 explicitly makes this factor a cap for a fee award in actions to which it applies. See 15 U.S.C. §§77z–1(a)(6); 78u–4(a)(6) (fee award should not exceed a "reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class"). For a percentage approach to fee measurement, **results achieved is the basic starting point**.
>
> In many instances, the court may need to proceed with care in assessing the value conferred on class members. Settlement regimes that provide for future payments, for example, may not result in significant actual payments to class members. In this connection, the court may need to scrutinize the manner and operation of any applicable claims procedure. **In some cases, it may be appropriate to defer some portion of the fee award until actual payouts to class members are known. Settlements involving nonmonetary provisions for class members also deserve careful scrutiny to ensure that these provisions have actual value to the class**. On occasion the court's Rule 23(e) review will provide a solid basis for this sort of evaluation, but in any event it is also important to assessing the fee award for the class.

See Notes of Advisory Committee on 2003 Amendments to Rule 23 (emphasis added).

The Federal Judicial Center (FJC) expected the parties to adhere to the Committee Notes to the Rule 23(h) amendments: "In cases involving a claims procedure…, the court should not base the attorney fee award on the amount of money set aside to satisfy potential claims. Rather, the fee awards should be based only on the benefits actually delivered." Federal Judicial Center, Manual for Complex Litigation (Fourth) § 21.71 (2004).

The Advisory Committee and the FJC anticipated the district courts to follow the Notes, but unfair class action settlements that awarded attorney fee awards disproportionate to class relief were consistently approved for over a decade after 23(h)'s adoption. The landmark appellate rulings recognizing that district courts must look at the results *actually* achieved—the same approach the Committee advocated in 2003—were not decided until CCAF challenged the misapplication of the Rules a decade after they were adopted. *See Baby Prods*, 708 F.3d 163 (3d Cir. 2013); *Pearson* 772 F.3d 778 (7th Cir. 2014). (Unfair results persisted for so long based in part on the fact that the Rules do not provide incentives for good faith objectors to challenge settlements. *See* § II.B below.)

The problem was that the language in Rule 23(h) did not *expressly* include the requirement that fees be awarded based on relief actually delivered. The Committee Notes were ignored because the settling parties' *ex parte* presentation misapplied the Rules and in turn created precedent for future settlements to be rubber-stamped that endorse that same abuse of the Rules.

For example, in *Masters v. Wilhelmina Model Agency, Inc*., the Second Circuit held that the district court should have computed class counsel's attorneys' fees based on the amount made available and not the amount actually delivered to the class. 473 F.3d 423, 436-37 (2d Cir. 2007). In reaching its decision, the Second Circuit distinguished the Advisory Committee Notes to Rule 23(h) and held that the fee restrictions described in the 2003 Committee Notes only applied to securities class actions. *Id.* at 437-38.

The 2003 Committee Notes state that the Private Securities Litigation Reform Act (PSLRA) requires a fee award to not exceed a "reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class." *See* Notes of Advisory Committee on 2003 Amendments to Rule 23 (quoting 15 U.S.C. §§77z–1(a)(6)). But the 2003 Committee Notes used the PSLRA as an *example* of why fees should be based on actual relief delivered. The Second Circuit's limitation of the 2003 Notes to securities cases makes no sense because (1) there would be no need for the Notes to provide guidance on fees in securities class actions when the PSLRA statute expressly requires fees to be based on amounts "actually paid;" and (2) it contradicts a plain reading of the 2003 Notes.

The same thing will happen again. Even if the Committee Notes to the Proposed Amendments direct district courts to consider the amounts class members actually receive when assessing the relief provided and class counsel's fee award, those Notes will once again be ignored or distorted to promote class counsel's self-interest.

* * *

To protect class members from unfair settlements with disproportionate fee awards, Proposed Rule 23(e)(2)(C) should adopt the Seventh Circuit approach and include the additional bolded, underlined language:

> (C) the relief provided for the class is adequate, taking into account:
>
> (i) the costs, risks, and delay of trial and appeal;

(ii) the effectiveness of the proposed method of distributing relief to the class, including the method of processing class-member claims, if required;

(iii) the terms of any proposed award of attorney's fees, including timing of payment, **and, if class members are being required to compromise their claims, the ratio of (a) attorneys' fees to (b) the amount of relief actually delivered to class members**; and

(iv) any agreement required to be identified under Rule 23(e)(3); ….

The above provision would alert the district court to the most fundamental problem of fairness in class actions: class counsel structuring the settlement so that they receive the lion's share of the actual relief obtained.

B. The Proposed Amendments should also explicitly require district courts to consider whether class counsel failed to adequately represent the class by negotiating self-dealing settlement structures.

In assessing the fairness of a class action settlement, Proposed Amendment Rule 23(e)(2)(A) requires a district court to consider "the class representatives and class counsel have adequately represented the class." *See* Proposed Amendments at 213. This inquiry should not just ask whether the attorneys have zealously prosecuted the litigation, but whether they have disregarded their fiduciary duties by negotiating a settlement that provides preferential treatment to class counsel. *Dry Max Pampers*, 724 F.3d at 717-18; *Pearson*, 772 F.3d 778.

Although a disproportionate fee award is the most fundamental problem of fairness in class action settlements, there are other problematic features of class settlements that "benefit defendants and plaintiffs' lawyers without providing value to class members" including "spurious injunctive relief, nontransferable or non-stackable coupons, unjustified *cy pres* remedies, burdensome or unnecessary claims procedures, reversions, excessively broad releases, expanded class definitions, class representative bonuses, revertible fee funds, and clear sailing agreements." *See* Erichson, *supra*.

Some of these features were identified by the Ninth Circuit in its partial list of warning signs that class counsel had engaged in self-dealing. *In re Bluetooth Headset Prod. Liab. Litig.,* 654 F.3d 935, 947-49 (9th Cir. 2011) (recognizing disproportionate fee awards, clear-sailing and reversion as warning signs of self-dealing settlements). Unfortunately, many courts interpret this list narrowly to hold that these factors are irrelevant if there is no actual collusion or if they are otherwise satisfied with the size of the settlement—even though "clear sailing" clauses, reversion provisions and the other problematic features are inherently tacitly collusive and prejudicial to the class.

1. The Proposed Amendments should explicitly prohibit inclusion of clear-sailing and reversion clauses.

The Proposed Amendments should prohibit, or at the very least warn district courts, against inclusion of clear-sailing and reversion clauses.

Class actions may be negotiated as a common fund structure (where the parties negotiate a single pot of money from which class counsel would later seek fees) or a segregated fee structure

(where the parties negotiate the class benefit first and negotiate the fees later). The segregated fee structure is often sold to the district courts as a "good deal" for the class because defendant is "responsible" for the fees and the payment won't affect class compensation. Courts have debunked the myth that a segregated fee agreement benefits the class:

> Class counsel claim that often they negotiate for the benefits to the members of the class first, selflessly leaving for later any consideration of or negotiation for their award of attorneys' fees. That claim is not realistic. For we know that an economically rational defendant will be indifferent to the allocation of dollars between class members and class counsel. Caring only about his total liability, the defendant will not agree to class benefits so generous that when added to a reasonable attorneys' fee award for class counsel they will render the total cost of settlement unacceptable to the defendant. We invited class counsel to explain how, therefore, negotiating first for class benefits could actually benefit a class, and were left without an answer.

Pearson, 772 F. 3d 778, 786-87 (7th Cir. 2014) (Posner, J.); *cf Bluetooth*, 654 F.3d at 948 (separation of fee negotiations from other settlement negotiations does not demonstrate that a settlement with disproportionate fee proposal is fair).

Where plaintiffs' counsel and defendants are negotiating fees separate from recovery, "[l]awyers might urge a class settlement at a low figure or on a less-than-optimal basis in exchange for red-carpet treatment on fees." *Bluetooth*, 654 F.3 at 847 (quoting *Weinberger v. Great N. Nekoosa Corp.*, 925 F.2d 518, 524 (1st Cir. 1991)); "Clear-sailing" clauses (where the defendant agrees not to challenge the fee) and "kicker" clauses (where any reduction in the fee award reverts to defendants rather than the class) combine together to insulate fee requests from scrutiny.

Courts have repeatedly held that the reversion to defendant is part of a constructive common fund and reflects money that a defendant would have been willing to pay class members to settle, whether it was negotiated separately or not. *Pearson*, 772 F.3d at 786-87; *Redman v. RadioShack Corp.*, 768 F.3d 622, 637 (7th Cir. 2014); *Bluetooth*, 654 F.3d at 948-49; *Johnston*, 83 F.3d at 245-46. "It is the duty of attorneys under fiduciary principles, the law of agency, and the rules of ethics to achieve the best possible results for their clients." *See* Letter to Standing Committee on Ethics and Professional Responsibility from Lester Brickman, et al. (Sept. 17, 2007) at 10-11 ("Ethics Committee Letter");[7] *see also* Lester Brickman, *Lawyer Barons* 522-25 (2011). By structuring a segregated fee structure, class counsel may sacrifice the best possible result and breach their fiduciary duty because of the potential reversion or "kicker" to the defendant if the district court awards less than what the parties had agreed (clear-sailing agreement). *Cf. Lobatz v. U.S. West Cellular of Cal., Inc.*, 222 F.3d 1142, 1147 (9th Cir. 2000) ("If … class counsel agreed to accept excessive fees and costs to the detriment of class plaintiffs, then class counsel breached their fiduciary duty to the class.").

For example, if the settling parties agree to $10 million in fees, but the district court awards only $5 million, the unawarded difference ($5 million) would revert back to the defendant. If the

[7] *Available at* http://is.gd/BrickmanLetter or https://cardozo.yu.edu/sites/default/files/ABA%20Ethics%20Letter%20September%2017%202007%20Edited(1).pdf.

defendant is willing to pay $10 million, then class counsel—as fiduciaries for the class—should have structured the settlement to capture the unawarded fees for their clients rather than returning to defendant. Negotiating a settlement structure with a reversion is a breach of class counsel's fiduciary duty. As Judge Posner explained, the *Pearson* panel could not "think of a justification for a kicker clause; at the very least there should be a ***strong presumption of its invalidity***." 772 F.3d at 786-87 (emphasis added); *see also* Lester Brickman, LAWYER BARONS 522-25 (2011) (reversionary kicker should be considered *per se* unethical).

When class counsel negotiate settlements with these provisions, they breach their fiduciary duty to the class. These provisions are costing class members millions of dollars, but if they are not explicitly included in the Proposed Amendments, district courts will not appreciate the dangers they pose. As explained above, settling parties' *ex parte* presentation will argue that any previous legal precedents warning of these provisions (e.g., *Bluetooth*, *Pearson*) are superseded by the "core concerns" set forth in Paragraph 23(e)(2)(C). *See* § I.A above.

2. In considering class counsel's adequacy for purposes of assessing settlement fairness, the Proposed Amendments should expressly require district court's to consider class counsel's use of *cy pres* awards.

Class counsel or representatives do not adequately represent the class when class counsel structures a settlement to include *cy pres* awards that prioritize benefits to third parties (including third parties related to class counsel!) over payments to the class. Two appellate courts have endorsed the approach set forth in Section 3.07 of the ALI Principles regarding *cy pres* awards: "A *cy pres* award is supposed to be limited to money that can't feasibly be awarded to the intended beneficiaries, here consisting of the class members." *Pearson*, 772 F.3d at 784 (rejecting $1.13 million cy pres residual when distribution possible to 4.7 million class members); *accord BankAmerica*, 775 F.3d at 1063-64 (rejecting cy pres of $2.7 million residual in lieu of third distribution to class members) (explicitly adopting ALI Principles § 3.07); *Klier v. Elf Atochem N. Am., Inc.*, 658 F.3d 468, 475 (5th Cir. 2011).

It is particularly problematic when class counsel has a preexisting relationship with the recipients of the *cy pres* award. One Academic recently classified "the ugliest *cy pres* settlements" as "those that direct funds to organizations with which class counsel or the judge is affiliated." Erichson, *supra*; *see also Nachshin*, 663 F.3d at 1039 (criticizing *cy pres* where "the selection process may answer to the whims and self interests of the parties [or] their counsel"). For example, in one class settlement where class counsel was scheduled to receive $27 million, *cy pres* was designated to a charity run by class counsel's ex-wife; the conflict was never disclosed to the district court, which approved the settlement. *See In re Chase Bank USA NA "Check Loan" Contract Lit*g., No. 09-md-02032 (N.D. Cal.)). Defendants' pre-existing relationships with *cy pres* recipients present additional problems. When the defendant is already a regular contributor to the proposed *cy pres* recipients, there is no demonstrable value added by the defendant's agreement to give money to that institution. *See Dennis v. Kellogg*, 697 F.3d 858, 867-68 (9th Cir. 2012), 697 F.3d at 867-68. The settling parties will hide such conflicts in their *ex parte* presentation of the settlement unless the Proposed Rules expressly require disclosure of such conflicts and pre-existing relationships.

* * *

The Proposed Amendments should prohibit clear sailing and reversion provisions in class action settlements. At a minimum, however, the Proposed Amendments to Rule 23(e)(2)(A) regarding class counsel's adequacy in analyzing the fairness of a proposed settlement should explicitly consider whether class counsel negotiated some of the problematic self-dealing features and insert the following bolded, underlined language:

> (A) the class representatives and class counsel have adequately represented the class **or whether they negotiated settlement provisions or structures intended to benefit class counsel and not the class including, but not limited to, disproportionate fee awards, clear-sailing and reversion, *cy pres* awards that prioritize relief to third parties rather than class members, and *cy pres* recipients that have preexisting relationships with the parties or their attorneys**;

II. Amendments to Rule 23(e)(5) Will Continue to Permit Settling Parties to Improperly Insulate Self-Dealing Settlements and Will Continue to Permit Bad-Faith Objectors to Receive Objector Blackmail.

Proposed Rule 23(e)(5)(A) requires greater specificity of objections but the new requirements will only create unnecessary collateral litigation over whether objections are "specific" enough and lead to the technical rejection of meritorious objections. And while Proposed Rule 23(e)(5)(B) and (C) are intended to eliminate payments to bad-faith objectors (those who seek only personal gain, i.e., payment in exchange for dismissal of the objection or appeal), these paragraphs will not eliminate payments to bad-faith objectors but could potentially *increase* the practice of extorting money from the settling parties and worse, be used to insulate class counsel's self-dealing settlements.

A. The proposed changes to Paragraph (A) requiring specificity should be deleted because they are unnecessary and will be abused to protect bad settlements, but at a minimum, Paragraph (A) should be revised to require notification, prevent technical rejection of objections, and ensure preservation of objectors' appellate rights.

Proposed Paragraph 23(e)(5)(A) inserts the following (bolded) language:

> **In General**. Any class member may object to the proposal if it requires court approval under this subdivision (e)~~the objection may be withdrawn only with the court's approval.~~ **The objection must state whether it applies only to the objector, to a specific subset of the class, or to the entire class, and also state with specificity the grounds for the objection**.

See Proposed Amendments at 215-16. This change is unnecessary because district courts and parties already effectively manage non-specific objections. Instead, Paragraph (A) will create unnecessary collateral litigation and will serve as a mechanism for class counsel to eliminate legitimate objections.

1. Paragraph (A) as proposed creates unnecessary collateral litigation that will be abused to protect self-dealing settlements.

The Comments to the Proposed Amendments indicate that the specificity requirement of Paragraph (A) was added "to clarify that objections must provide sufficient specifics to **enable the parties to respond to them and the court to evaluate them**." *See id.* at 228 (emphasis added). Although the supposed reason for the change is to assist the parties and the court, there is no evidence that parties or courts suffer any costs from non-specific objections.

No settlement has ever been derailed by a non-specific objection; courts invariably dismiss them out of hand. District courts can require objectors at the fairness hearing to clarify their objections, or, if the objector cannot provide sufficient specificity beyond "general unfairness," district courts can approve the proposed settlement over the objections. *Int'l Union v. GMC,* 2008 U.S. Dist. LEXIS 92590, *83-84 (E.D. Mich. July 31, 2008) ("In sum, the objections that do not specify any grounds beyond general unfairness provide no basis for rejecting the settlement.") (citing 7B Wright, et al., Fed. Prac. & Proc. § 1797. 1 ("Only clearly presented objections…will be considered.")); *Sunrise Toyota, Ltd. v. Toyota Motor Co.*, No. 71-1335, 1973 U.S. Dist. LEXIS 14862, at *6 (S.D.N.Y. Feb. 20, 1973) (rejecting objections based on "conclusory allegations" of "general unfairness"); *cf. Dennis v. Kellogg*, 697 F.3d 858 (9th Cir. 2012) (holding that district court "must give 'a reasoned response' to all non-frivolous objections").

Because the proposed Paragraph (A) is unnecessary, the only thing the Rules will realize is additional collateral litigation regarding whether objections are sufficiently "specific." The Comments to the Proposed Amendments indicate that "[f]ailure to provide needed specificity may be a basis for rejecting an objection." *See* Proposed Amendments at 229. Rejection of objections—where objectors lose appellate rights—is a draconian measure if the purpose of Proposed Paragraph (A) is to simply help the court and parties discover the actual concerns of vague objections. In practice, Paragraph (A) will be used to provide a means for eliminating objections that get in the way of settling parties' settlements. Settling parties will argue that objections are waived based on failure to satisfy Paragraph (A). Thus, setting aside the underlying merits of the objections, the settling parties and objectors will engage in additional litigation over what level of specificity is required to satisfy Paragraph (A).

Indeed, faced with this new specificity standard, settling parties will interpret the Rules to unduly burden objectors. Settling parties will point to other similar Federal Civil Rules and argue that the specificity requirement is akin to Rule 9's "heightened pleading" requirement of a "specific allegation." *Swanson v. Citibank, N.A.*, 614 F.3d 400, 410 (7th Cir. Ill. 2010) ("The basic requirement for a complaint ('a short and plain statement of the claim showing that the pleader is entitled to relief') is set forth in Rule 8(a)(2) of the Federal Rules of Civil Procedure. Rule 9 requires heightened pleading (that is, a specific allegation) of certain elements in particular cases, such as fraud and special damages."). While it is fundamentally unfair to place a higher burden on absent class members than placed on the named plaintiffs, settling parties will endorse such an interpretation to eliminate objections that potentially block settlement approval. Just as the parties will present a self-interested interpretation of the Rules for approval of a settlement, *see* § I.A above, the settling parties will present a self-interested interpretation of the Rules to protect that settlement.

Rather than taking away the carrot, the Proposed Amendments are giving class counsel a stick to fight against bad-faith objectors. But this stick will also be used against good-faith objectors.

Unlike professional objectors, CCAF does not settle appeals for *quid pro quo* payments and brings objections in good faith to overturn unlawful settlements. While CCAF has won over a dozen landmark decisions, the vast majority of the time, settling parties file briefs in response to CCAF's objections that attempt to lump CCAF in with decisions criticizing so-called "professional objectors," and/or accuse us of filing "boilerplate" because there was overlap in precedents we cited in previous objections.

For example, in *In re Target Corporation Customer Data Security Breach Litigation*, CCAF objected on behalf of an absent class member, arguing that our client was part of an uncertified subclass that had been frozen out of recovery. *Target I,* 14-md-2522, Dkt. 513 (D. Minn.) ("*Target I*"), remanded and vacated in part with appeal pending, No. 15-3912 (8th Cir. Feb. 1, 2017) ("*Target II*"). Despite CCAF's thorough analysis of the claims process and settlement structure, the district court adopted class counsel's characterization that CCAF's objection was "boilerplate" and CCAF was a "professional objector" (though CCAF submitted a declaration proving otherwise), and sanctioned CCAF with an unlawful appeal bond. *Target,* 14-md-2522, Dkts. 645, 701, 713; *Target II*. Good-faith objectors will suffer similar results with increasing frequency if class counsel is armed with the new requirements under Paragraph (A); if nothing else, the rule will raise costs to good-faith objectors faced with collateral litigation over whether the objection was "specific" enough—with the class counsel then using the time on the frivolous motion to strike the objection to burnish their lodestar.

Class counsel will use any means available to insulate their bad settlements on appeal. For example, in *In re Magsafe Apple Power Adapter Litigation*, CCAF objected to a settlement where class counsel received $3 million, but the value of the class relief was unknown. 571 Fed. Appx. 560, 565 (9th Cir. 2014). Class counsel sought appeal bonds of $200,000 per objector and the district court awarded $15,000 per objector. *Id.* at 563. The Ninth Circuit reversed and remanded for consideration under the appropriate legal standards, and was especially critical of the abusive appeal bond. Just like abusive appeal bonds, the Proposed Amendments give class counsel an additional mechanism for blocking appellate review. **Class counsel will utilize Paragraph (A)'s specificity requirements to insulate bad settlements on appeal**.

If class counsel can eliminate objections for technical reasons under Paragraph (A), there is a risk that the merits of those objections will not be considered by the district court or on appeal. Class counsel's self-dealing settlements that are approved at the expense of the class will go unchecked because objectors are divested of their essential role. As Judge Posner recognized when striking down the "selfish deal" the settling parties had negotiated, because of the "acute conflict of interest" between the class and class counsel, "objectors play an essential role in judicial review of proposed settlements of class actions and why judges must be both vigilant and realistic in that review." *Pearson*, 772 F.3d at 787. Preventing review of the merits punishes the class because the class members benefit when the settlement is corrected on review. (Even some of the most-frequently criticized "professional objectors" have obtained success for the class in appeals courts. *E.g., In re Groupon Mktg. & Sales Practices Litigation*, 593 Fed. Appx. 699 (9th Cir. 2015); *Eubank v. Pella Corp.*, 753 F.3d 718 (7th Cir. 2014); *Dennis v. Kellogg*, 697 F.3d 858 (9th Cir. 2012).)

In sum, district courts and parties are already equipped to handle non-specific objections. Rules that require objections to be "specific" will be abused to create an unfair level of burden on legitimate objectors as settling parties encourage courts to shift the goalposts through collateral litigation. Paragraph (A) does nothing to help district courts because it will only burden the district courts with this additional litigation. The Rules will also be used to deprive good- and bad-faith

objectors of their appellate rights and insulate self-dealing settlements from correction on appeal. Accordingly, the proposed Paragraph (A) amendments should be rejected.

2. If Paragraph (A) is adopted as proposed, additional language should be inserted to protect class members including notifying absent class members of the new requirements, preventing technical rejection of objections, and preservation of objector's appellate rights.

If the proposed changed to Paragraph (A) are adopted, at a minimum, additional language should be inserted to protect class members. *First*, the Rules should be amended to require that absent class members be notified in the class notice of the new requirements. Most class members are unaware of the Federal Rules. Requiring class members to comply (or risk rejection of their objections) is fundamentally unfair if absent class members are not notified of the requirements.

Second, Paragraph (A) should be amended to instruct courts not to reject objections for technical failures. The Committee Notes instruct district courts "to recognize that a class member who is not represented by counsel may present objections that do not adhere to technical legal standards." *See* Proposed Amendments at 229. As explained above, this instruction will likely be ignored as district courts disregard the Committee Notes when class counsel present a self-interested interpretation of the Rules. *See* § I.A above. Thus, Paragraph (A) must explicitly direct courts that objections should not be rejected for technical deficiencies.

Third, Paragraph (A) should be amended to recognize that failure to satisfy the requirements of Paragraph (A) does not constitute waiver so that objectors may still appeal the district court's order approving the settlement. If a district court finds that the objection was waived (even if the "waiver" was because of an unduly burdensome procedure established for objecting), some courts of appeal hold that the class member lacks standing to appeal without a formal motion to intervene, notwithstanding the Supreme Court's command in *Devlin v. Scardelletti*. *See, e.g., In re Deepwater Horizon*, 739 F.3d 790, 809 (5th Cir. 2014) (dismissing appeal because objector had "forfeited and waived" objections by failing to comply with preliminary approval order); *In re UnitedHealth Group S'holder Derivative Litig.*, 631 F.3d 913, 917 (8th Cir. 2011) (dismissing appeal because objector failed to "file a timely objection pursuant to district court procedure"); *In re Integra Realty Res., Inc.*, 354 F.3d 1246, 1257-58 (10th Cir. 2004) (dismissing appeal where objector failed to follow proper procedure for filing objection).

* * *

The Proposed Amendments to Rule 23(e)(5)(A) should be deleted, but at a minimum, Paragraph (A) should be revised to protect absent class members by inserting the additional bolded, underlined language:

> (A) **In General**. Any class member may object to the proposal if it requires court approval under this subdivision (e)~~the objection may be withdrawn only with the court's approval.~~ The objection must state whether it applies only to the objector, to a specific subset of the class, or to the entire class, and also state with specificity the grounds for the objection. **The notice to the class must notify class members of the requirements contained in this paragraph. An objector's failure to**

satisfy technical standards is not a basis for dismissal of an objection. An objector does not waive an objection nor any rights to proceed on appeal for failure to meet the requirements of this paragraph.

In the alternative, language requiring that the class notice inform class members of Paragraph (A) could be added to Federal Rule 23(c)(2) regarding notice to the class.

B. Proposed Paragraphs (B) and (C) should be deleted because they will not effectively end extortionate payments to bad-faith objectors; the Rules should be revised to acknowledge that objectors are entitled to attorneys' fees if they demonstrate that the class realized a benefit; and the Rules should be further revised to provide an enforcement mechanism to recover the extortionate payments.

The Proposed Amendments insert the following paragraphs to Rule 23(e)(5):

> (B) Court Approval Required For Payment to an Objector or Objector's Counsel. Unless approved by the court after a hearing, no payment or other consideration may be provided to an objector or objector's counsel in connection with:
>
> (i) forgoing or withdrawing an objection, or
>
> (ii) forgoing, dismissing, or abandoning an appeal from a judgment approving the proposal.
>
> (C) Procedure For Approval After an Appeal. If approval under Rule 23(e)(5)(B) has not been obtained before an appeal is docketed in the court of appeals, the procedure of Rule 62.1 applies while the appeal remains pending.

See Proposed Amendments at 216-17. These additional changes will not effectively address the problem of extortionate payments to bad-faith objectors but will make the matters worse by increasing unlawful payments, increasing litigation, and permitting class counsel to insulate self-dealing settlements from correction on appeal. Proposed Paragraphs (B) and (C) should be removed. Instead, the Rules should be revised to encourage good faith objections by explicitly recognizing an objector's entitlement to attorneys' fees if an objector can demonstrate that their objection resulted in a benefit to the class.

1. Paragraphs (B) and (C) should be deleted because rather than effectively ending objector blackmail, the Proposed Amendments will only increase extortionate payments to bad-faith objectors.

Paragraphs (B) and (C) were added to address bad-faith or professional objectors: those who file objections, appeal the settlement approval and then seek extortionate payments from the settling parties in exchange for dismissal of their appeals. The problem is that the status quo of the class action system actually *encourages* professional objectors. The threat of an appeal can be a valuable weapon and objector blackmail can be quite lucrative. Fitzpatrick, Brian T., *The End of Objector Blackmail?*, 62 VAND. L. REV. 1623, 1634, 1637 n.67 (2009). On the other hand, when objectors are

successful and achieve a benefit for the class, their efforts often go uncompensated. *See* § II.B.2 below. Losing an objection and settling on appeal is a much more profitable business model than successfully litigating an objection.

Traditionally, commentators and courts have wrongly focused on creating sticks to combat objector blackmail. *See, e.g.,* Lopatka, John E. & D. Brooks Smith, *Class Action Objectors: What to do About Them?*, 39 Fl. Law Rev. 865, 890-906 (discussing sanctions, prohibiting appeals, and appeal bonds as means for eliminating objector blackmail). But the focus should shift to the carrots. The Rules should eliminate the carrot of bad faith objections (remove the possibility of blackmail on appeal) and establish the carrot for good-faith objections (explicitly require attorneys' fee awards for objections that improve class settlements). The only way to truly end objector blackmail is by taking away the possibility of an extortionate payment on appeal.

While the proposed Rules may be intended to eliminate extortionate payments by requiring court approval, the Rules as drafted will serve only to *legitimize* objector blackmail. After proposed Paragraph (B) is adopted, the motivations of class counsel and the objectors will remain unchanged: class counsel want to eliminate the threat of appeal and the objectors want a payday. (Even if the objection has merit, objectors know that they have a better chance of being paid by settling than by successfully litigating the objection.) Proposed Paragraph (B) requiring court approval does not contain a standard that objectors must satisfy to receive a payment. Without any explicit standard for approval of such a settlement, class counsel and the settling objector need not demonstrate anything beyond the fact that they have settled. Like a class action settlement, class counsel and the settling objector will submit an *ex parte* presentation of their settlement with no adversarial response. *See* § I.A above. Objector blackmail will not change but simply transformed from an undisclosed settlement to a rubber-stamped order. Just as meritless M&A class actions justify attorney fees for $0 settlements with immaterial supplemental disclosures (*In re Walgreen Co. Shareholder Litig.*, 832 F.3d 718 (7th Cir. 2016)), bad-faith objectors colluding with class counsel will claim entitlement to fees for immaterial changes to the settlement website, a modest *cy pres* payment, or even for the right of the objector to opt out and negotiate a separate settlement of his claim. (Though it smacks of a joke about *chutzpah*, we have even seen class counsel claim that a shareholder class benefits simply from the settlement of litigation brought by the class counsel against the defendant corporation. *E.g., Gordon v. Verizon*, 2017 NY Slip Op 742 (N.Y.A.D. 1st Dept. Feb. 2, 2017) (agreeing that this was a benefit meriting settlement approval); *Robert F. Booth Trust v. Crowley*, 687 F.3d 314 (7th Cir. 2012) (rejecting argument).

Further, the proposed Paragraph (B) will actually *expand* the cottage industry of professional objectors. Currently objector blackmail is not disclosed to the court. But when a settlement between an objector and class counsel or defendants is on the docket and publicly disclosed, other entrepreneurial attorneys will soon catch on. Newcomers to the objector blackmail market will see that they too can file a boilerplate objection with conclusory allegations and be paid to go away.

And worse, class counsel can utilize Paragraph (B) as a mechanism to insulate their self-dealing settlements. While objector blackmail can be costly for class counsel, objector blackmail can *save* class counsel money by preventing their self-dealing settlements from being corrected on appeal. Appellate courts have rejected selfish settlements, knocking down millions of dollars in fees. *See, e.g., In re Baby Products Antitrust Lit.*, 708 F.3d 163 (3d Cir. 2013)(rejecting settlement that paid $14 million attorneys' fees and $3 million to class). Class counsel can protect their settlements by paying off objectors at a fraction of the millions they risk losing. *Cf.* Schmitt, Richard B., *Objecting to Class-Action*

Pacts Can be Lucrative for Attorneys, WALL ST. J., Jan.10, 1997 at B1. If class counsel utilizes proposed Paragraph (B) to insulate their settlements from appeal, class members are robbed of the benefit they would receive from correction on appeal.

The Rules should be revised to eliminate any payments or consideration to an objectors for dismissal of their appeal.

2. The Rules should be revised to explicitly recognize that objectors are entitled to attorneys' fees if they can demonstrate that their objection realized a benefit to the class.

In addition to removing the carrot motivating objector blackmail, the Rules should create a carrot for good faith objections by explicitly recognizing that objectors who realize a benefit for the class are entitled to attorneys' fees. The Comments to Rule 23(h) direct that fees may be awarded to those "whose work produced a beneficial result" including "attorneys who represented objectors." *See* Notes of Advisory Committee on 2003 Amendments to Rule 23. But too often, even when objectors realize a substantial benefit, objectors go uncompensated.

For example, in *Fraley v. Facebook, Inc.*, the district court denied CCAF's request for attorneys' fees where CCAF's objection realized $300,000 for the class. 638 Fed. Appx. 594, 600 (9th Cir. 2016). The district court claimed that it was "commonsense" that fees should be awarded based on net settlement value rather than gross settlement value *Id.* Of course it was not "commonsense" to class counsel who requested fees based on gross settlement value and class counsel suffered no consequence for presenting a fee request that contradicted the "commonsense" approach. In his dissenting opinion, Judge Bea explained: "[O]bjectors must decide whether to object without knowing what objections may be moot because they have already occurred to the judge." *Id.* (quoting *Reynolds v. Beneficial Nat'l Bank*, 288 F.3d 277, 288 (7th Cir. 2002)).

Another way objectors are shortchanged is when the judge argues that an objector's time should be sliced apart to award fees for arguments adopted by the court. For example, in *In re Transpacific Passenger Air Transportation Antitrust Litigation*, the district court reduced class counsel's request for attorneys' fees and expenses by over $5.1 million, for the benefit of the class. 2015 U.S. Dist. LEXIS 106943, *13-14, No. 3:07-cv-05634-CRB (N.D. Cal.), *pending appeal*, No. 15-16280 (9th Cir.). Despite the benefit CCAF's objection created, class counsel argued that the district court should reduce CCAF's fee request to solely the lodestar CCAF spent on the issues adopted by the court. Such a reduction is arbitrary as it is unreasonable to allocate time spent to various issues. Much of the time of objection is spent analyzing the settlement, engaging in the compliance costs of confirming and documenting class membership to have standing to object, and preparing for the fairness hearing; to say that only a page of the objection made a difference to the class and the attorneys should only be compensated for the time spent on that page misunderstands the nature of proximate cause. It is also inequitable to hold objectors to a different standard than class counsel. Courts do not dissect class counsel's lodestar to assign values to their success in litigating the separate claims or issues. If class counsel is concerned that "obvious" objections may result in disproportionate payout to successful objectors, the solution is to avoid settlements and fee requests that have obviously objectionable issues.

While CCAF does not bring objections to earn fees, CCAF's fee requests are often denied or reduced; despite CCAF's unprecedented success in improving class-action settlements in dozens of

cases, and despite CCAF paying non-profit level salaries a fraction of what our attorneys could be making in private practice, fee awards fund only a small fraction of CCAF's expenses. Under the status quo, no objector is incentivized to litigate a good-faith objection because they risk receiving nothing (or being nickel-and-dimed) when they could simply receive a payment to dismiss an appeal with a fraction of the work. The Rules should be revised to explicitly recognize that objectors are entitled to attorneys' fees when they realize a material benefit for the class.

Further, requiring objectors to demonstrate a material benefit also prevents objectors and class counsel from settling objections based on illusory relief, e.g., that objector is providing a benefit to the class by "getting out of the way" or that objector somehow created a benefit by a 10-word immaterial change to the class notice.

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The Proposed Amendments to Rule 23(e)(5)(B) & (C) should be revised to eliminate the ability of objectors to dismiss their appeal for consideration by the settling parties and should include the additional bolded, underlined language recognizing an objector's entitlement to fees:

> (B) Court Approval Required For Payment to an Objector or Objector's Counsel. **The court may approve an objector's request for an award of reasonable attorney's fees and nontaxable costs after a hearing and on a finding that the objection realized a material benefit for the class. An objector may not receive payment or consideration in connection with:**
>
> ~~agreement. The following procedures apply: Unless approved by the court after a hearing, no payment or other consideration may be provided to an objector or objector's counsel in connection with:~~
>
> (i) forgoing or withdrawing an objection, or
>
> (ii) forgoing, dismissing, or abandoning an appeal from a judgment approving the proposal.
>
> (C) Procedure For Approval After an Appeal. If approval under Rule 23(e)(5)(B) has not been obtained before an appeal is docketed in the court of appeals, the procedure of Rule 62.1 applies while the appeal remains pending.

3. The Proposed Amendments should identify an enforcement mechanism for failure to satisfy Paragraphs (B) and (C).

If Paragraphs (B) and (C) are adopted, the Rules should further be amended to provide an enforcement mechanism for failure to obtain court approval: disgorgement. Disgorgement is an equitable remedy within the inherent power of the court. *See Porter v. Warner Holding Co.*, 328 U.S. 395, 397-99 (1946) ("unless otherwise explicitly restricted by statute, District Courts may exercise all inherent equitable powers to fashion relief, including ordering the payment of money."). The Rules should permit disgorgement of objector-appellants' profit from misuse of the class action process to extract private gain. "The object of restitution [in the disgorgement context] . . . is to eliminate profit

from wrongdoing while avoiding, so far as possible, the imposition of a penalty." Restatement (Third) of Restitution and Unjust Enrichment § 51(4) (2010).

Courts have rightly criticized the appellate settlements where objectors "get paid to go away" because such payments "benefit only the [objectors] at the expense of all other parties to the litigation." *Vollmer v. Selden*, 350 F.3d 656, 660 (7th Cir. 2003). All class action payments ultimately derive from resolution of the underlying claims. *Pearson*, 772 F.3d at 786 (defendant cares only about total liability). The Rules should provide for a means of recouping any consideration objectors receive for dismissing their appeal in contradiction of Paragraphs (B) and (C).

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The Proposed Amendments insert the following paragraphs to Rule 23(e)(5):

> **(D) Enforcement. Any party or class member may initiate an action to enforce Paragraph (B) and (C) by filing a motion for disgorgement of any consideration received by an objector in connection with foregoing or dismissing an objection or appeal**.