LAW360

Portfolio Media. Inc. | 111 West 19th Street, 5th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

If you typed a query into Google anytime between Oct. 26, 2006, and April 25, 2014, chances are you're entitled to a cut of a multimillion-dollar class action settlement in California. Under the deal, however, you'll get nothing. Instead, a research lab at Carnegie-Mellon University and five other charities will get about $5 million on your behalf.

Is this fair?

That's the question facing the Ninth Circuit as it considers an appeal of the 2014 deal in privacy litigation accusing Google of selling user search terms containing personally identifiable information to advertisers.

For class counsel, the answer is a pragmatic "yes." After all, dividing the $8.5 million pot among a potential 130 million class members would yield you 4 cents — an administratively infeasible situation, even before attorneys' fees and administrative costs.

For objector Ted Frank, who has been hunting questionable cy pres class actions since 2008, the answer is an emphatic "no."

In March 13 oral arguments on the matter, Frank railed against the attorneys' decision to not even try distributing money to the class through some form of claims process. Allowing class counsel to invoke cy pres — the doctrine allowing settlement funds to be paid to charities rather than class members — just because of the massive size of the potential class would set a dangerous precedent in an age of mega-class actions, he said.

"The standard they are asking for would effectively turn every class action in the circuit into an all-cy pres settlement," Frank told the three-judge appellate panel.

Underlying Frank's objections is the question of whether cases resolved with large cy pres distributions like the one in the Google case should really be class actions in the first place if class members don't receive any direct benefits.

It's a question courts across the country are wrangling with as larger-than-ever class actions — particularly in the technology space — pose novel questions about when cy pres can be used, experts say.

The question, however, may soon be moot if Congress acts on the latest class action reform bill from Republicans, the Fairness in Class Action Litigation Act, which could choke off any monetary incentive for the plaintiffs bar to use the device in any significant fashion.

But both plaintiffs and defense attorneys say losing it as an option when litigating large class actions may result in something worse: longer, costlier trials and tougher settlement negotiations.

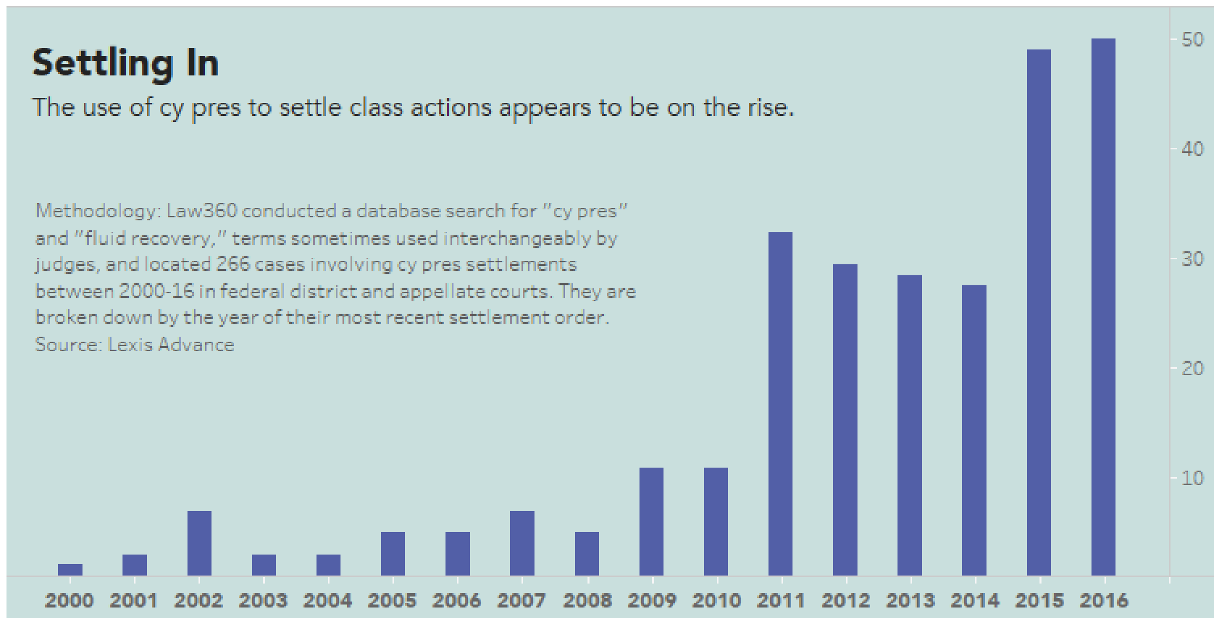
Supporters of the legislation "have their hearts in the right place," said Paul Karlsgodt, leader of BakerHostetler's national class action defense practice team. "But I don't think they have necessarily thought through the reality of their bill."

'As Near As Possible'

Cy pres — pronounced "sigh pray" — wasn't originally meant to be included in class actions. The term, which is derived from a French phrase for "as near as possible," has its roots in trusts law, where it was used to move funds when the intent of a trust was no longer possible to fulfill. For example, if someone left behind a significant amount of money for a veterans charity that shut down, cy pres would allow the funds to go to a comparable veterans charity. As noted in Edwin Newman's "Law of Philanthropy" in 1955, cy pres was always meant to be a remedy of "last resort."

In the wake of 1966 amendments to class action rules, a number of suits ended with a substantial amount of small claims being left on the table. Some legal scholars suggested adopting a cy pres-like remedy as a solution, according to Martin Redish, a Northwestern University School of Law professor.

The earliest example Redish could find of the doctrine in the class action context was a 1974 settlement in a federal New York securities suit. In that case, known as Miller v. Steinbach, Judge Whitman Knapp said it didn't make sense to distribute the "modest size" of the settlement across all of the shareholders. So the judge applied cy pres to funnel that money into a related retirement plan instead.



Cy pres wouldn't take on a noticeable presence in class actions, however, until after Congress entered the area in the mid-aughts.

It started when the Class Action Fairness Act of 2005 took a hammer to so-called coupon settlements, where the plaintiffs bar seemed to profit handsomely while class members were left with coupons in consumer actions. Coupon settlements had emerged to address issues as varied as undisclosed cereal additives and disputed bank accounting practices.

In an effort to make coupon settlements with low claims rates more fair — or, to some people, more punitive — the law encouraged judges to set aside a portion of such settlements for charities rather than allow companies to recoup unclaimed funds. The law also narrowed how the value of coupon settlements could be used to determine attorneys' fees, decreasing the incentive for plaintiffs lawyers to use them.

Coupon settlements have since fallen out of favor, and the use of cy pres has expanded to non-coupon settlements. Some experts argue plaintiffs lawyers latched onto the tool in order to secure the attorneys' fees they once obtained through coupon deals.

A Law360 analysis of federal district and appellate court filings for class action settlements indicates that the tool has been gaining acceptance. A Lexis Advance search for "cy pres" or "fluid recovery," a term for taking a flexible approach to distributing settlement funds, yielded preliminary approvals, final approvals and appellate decisions in 266 cases since 2000, the majority of which arose in the last decade.

Proponents of cy pres in class actions say that when such distributions are structured correctly — and funds are given only to charities that provide an indirect benefit to class members — the funds can be an adequate substitute for the original intent of various laws.

Redish and Frank, however, believe cy pres can encourage overly broad class actions. If a class can't be identified, it shouldn't be a class, they argue. And if the compensatory remedies of the substantive law can't be enforced and the purported class members directly compensated, the suit shouldn't be certified, Redish says.

"I see cy pres as a cover, a camouflage for the faux class action," he said. "It looks like a class action, but it's really just a cardboard cutout of a class action."

Such concerns would likely be addressed in the Fairness in Class Action Litigation Act. The bill, sponsored by House Judiciary Committee Chairman Bob Goodlatte, cleared the House in March without a single Democratic vote. Experts say it faces long odds in the Senate this year but is likely to resurface in future terms.

While the bill doesn't name cy pres outright, it would sever the attorneys' fees from anything but direct monetary distributions to class members, effectively killing the use of the doctrine in many high-profile technology cases where class size makes direct distributions impractical — such as the suit against Google before the Ninth Circuit.

If the legislation were in effect, class counsel in that case would likely be unable to take their full fee request — a $2 million piece of the $8.5 million settlement fund, according to court documents. Rather, they would get a small share of the $5,000 each of the named plaintiffs received — likely not enough to justify their more than $21,000 in upfront costs and more than 2,000 hours spent getting the contingent fee case to settlement.

Kassra Nassiri of the California-based Nassiri & Jung LLP, counsel for the plaintiffs, did not respond to requests for comment. Denver-based co-counsel Michael Aschenbrener of Kamberlaw LLP declined to comment directly on the case, but he said an all cy pres deal can benefit the class as long as it's directed toward the proper charity or initiative.

"Direct distribution should always be preferred," he said. "Perhaps where there is a situation where identifying class members is very difficult and costly, where trying to identify class members might eat up a settlement fund — thereby leaving very small amount of money available and perhaps none to go to direct distribution — then a good cy pres deal can provide a real benefit."

Technology cases in particular lend themselves to cy pres because of the potential for massive classes. Last year, the Ninth Circuit approved a $20 million deal in Fraley v. Facebook to settle privacy claims over using members' pictures in ads, finding the organizations set to take the unclaimed settlement funds were worthwhile recipients because they would help further online privacy and the safe use of social media.

Warning Shots

In 2011, the Ninth Circuit led the way in a wave of rulings in cases against technology companies that appeared to cinch in the practice. While cy pres and its controversies are in no way limited to

technology class actions, these suits have largely been at the forefront of the issue given their potential for huge classes.

In Nachshin v. AOL — a suit over the wrongful insertion of promotional ads into the emails of a putative class of 66 million — the court found the proposed settlement wrongfully steered funds away from class members and toward third-party charities that had no related interests to the class.

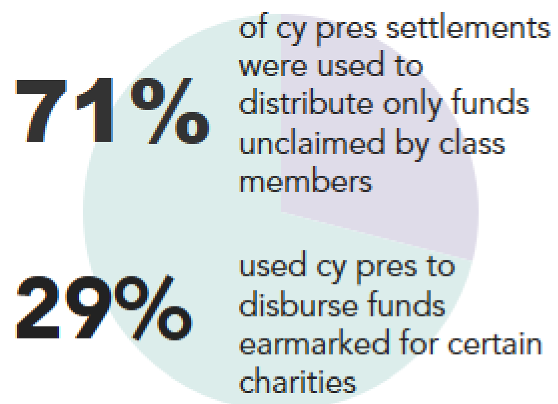
Then, in In re: Bluetooth Product Liability Litigation, the Ninth Circuit sent back a settlement in which class counsel made eight times the $100,000 all-cy pres settlement they secured for a class of potentially more than 100 million over the potential hearing loss risks from Bluetooth products. On remand, the California federal court recalculated the attorneys' fees and reimbursed costs to $283,000.

By 2012, the Third and Fifth circuits had issued decisions echoing Nachshin's calls to make sure charities receiving cy pres were properly linked to the interests of the class. Also that year, the Ninth Circuit rejected a $10.6 million settlement in Dennis v. Kellogg Co, which involved claims that the cereal maker falsely marketed Frosted Mini-Wheats as improving children's cognitive functions. The court ruled that food banks that would have received part of the pot were not sufficiently related to the lawsuit's issues. Rather, the cy pres awards had to go to organizations that protect consumers from false advertising.

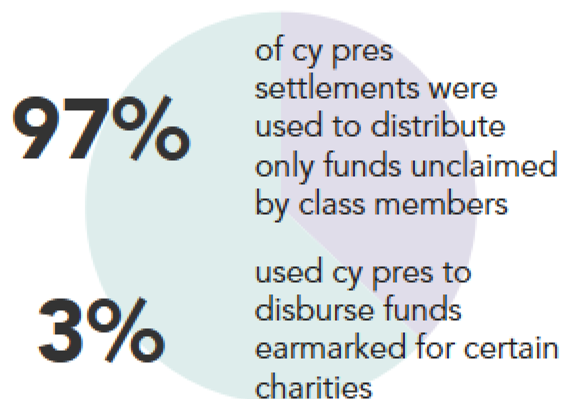
Heeding the Warning?

The U.S. Supreme Court raised concerns about problematic cy pres settlements in 2013.

From 2000-12:



From 2013-16:



Methodology: Law360 analyzed 179 class action settlements in federal district court from 2000-16 discovered through a database search. Source: Lexis Advance

"It could be said that cy pres was looser before the Dennis position in the consumer context," said Nathan Davis, a Liner LLP defense attorney.

The biggest shot across the bow, however, seemed to come from the U.S. Supreme Court in 2013, when it issued a rare statement denying the appeal of a $10 million settlement in Marek v. Lane.

In settling the class action over Facebook's controversial but short-lived Beacon program — which had broadcast users' purchases — $3.5 million went to attorneys' fees and $6.5 million went to a Facebook-

founded charity that would provide internet privacy education to the public. None of the funds went directly to class members, who were deemed too numerous to receive direct distributions.

While the Supreme Court decided not to take the case — affirming the Ninth Circuit's decision not to meddle with the parties' private deliberations — Chief Justice John Roberts issued a statement that seemed to contain a warning, saying the court would be willing to take on a future case that provided the "opportunity to address more fundamental concerns surrounding the use of such remedies in class action litigation."

This seemed to mark a turning point for cy pres. Many lawyers say they saw fewer examples of it being abused after that — and that its use overall as a tool for settling class actions seemed to dwindle.

"Between that decision and [the fact] that settling parties knew we were out there looking to raise these issues, I think the safer thing to do was to avoid the controversy and avoid anything that might smack of problematic cy pres," said Frank, the objector in the Google case.

Law360's analysis, to some degree, corroborates this view, in that class action settlements now mostly use cy pres to get rid of so-called drippings — unclaimed funds and uncashed checks sent to class members. But the data also shows that these residual funds can be significant — sometimes in the millions of dollars — and that judges continue to see controversial cy pres proposals.

"I think that there is a growing recognition that there is a right way and a wrong way to do it," said Harry Snyder, a settlement administrator who specializes in cy pres.

But "there are still embarrassing uses of cy pres that continue," he said.

Murky Connections

While the string of rulings may have tamped down the most controversial use of cy pres in class actions, several recent cases have drawn scrutiny over attorneys' ties to cy pres recipients or claims that there are flimsy links between recipients and class members.

One of the issues in Google's suit before the Ninth Circuit, for example, is that two of the cy pres recipients — the Berkman Center for Internet and Society at Harvard University and the Stanford Center for Internet and Society — are based at universities that count Nassiri, the class counsel, as an alumnus.

Nassiri has no connections to the university centers asking for the funds, other than the master's and law degrees he holds. But he does admit it is more than a coincidence — the pool of organizations that can address the privacy matters at the heart of the case is relatively small.

For Nassiri, who specializes in these suits in part because of the education he received at these institutions, it seems unfair to automatically exclude them from the running if they are best suited to provide indirect benefits to the class.

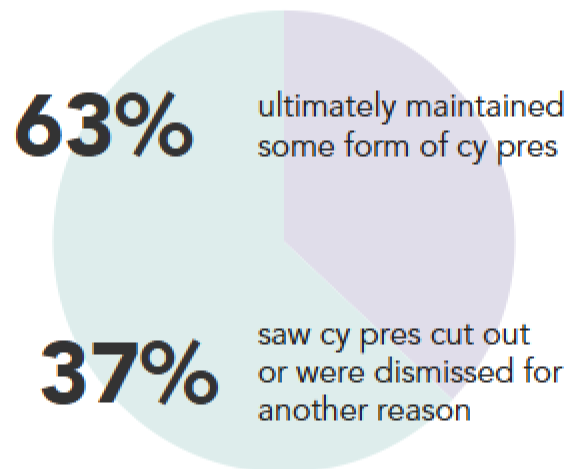
“Objector Frank is essentially asking this court to find that an alma mater, no matter how qualified, should be disqualified from the get-go,” Nassiri told the Ninth Circuit panel at the March hearing. “That doesn’t comport with any case law, including Nachshin.”

Frank, however, argues that there is a clear conflict of interest. Nachshin and several other precedents put a burden on the plaintiffs lawyers to show that there was no impropriety in choosing the alma maters, and the class counsel fail to meet this standard, he says.

Meanwhile, courts have pushed back on settlements using cy pres over concerns they benefited organizations that weren’t closely related to the class.

When Judges Sigh

In cases where a cy pres settlement was rejected or sent back for more work:



Methodology: Law360 analyzed 40 cases from 2000-16 discovered through a database search. Source: Lexis Advance

In March, in California Dental Association v. Delta Dental, a San Francisco federal judge declined to approve a $34.75 million settlement in a contract dispute between a class of 23,000 California dentists and Delta Dental in part because of concerns that the proposed cy pres recipient, the California Dental Association Foundation, wouldn’t benefit all class members. Class counsel have said further briefing will show that tuition grants funded out of the cy pres would be available for dentists who aren’t members of the foundation.

That ruling came a few months after the Ninth Circuit reversed a magistrate judge’s approval of a $35,000 cy pres settlement in a class action known as Koby v. Helmuth, which alleged violations of the Fair Debt Collection Practices Act on behalf of a class of 4 million people.

The appeals court said in January that the settlement failed to show the cy pres award to a veterans organization would benefit the class. At the same time, it said, the settlement required absent class members to relinquish their rights to sue for considerably higher damages.

No Injury, No Interest

Another issue haunting current cy pres deals is low claims rates, a problem that often pops up in the food labeling realm.

There's a large body of class actions winding its way through the courts over claims that the term "evaporated cane juice" misled consumers into thinking there wasn't any added sugar in a product. But the claims rate for these cases can often land in the single-digits, meaning leftover funds significantly outweigh what is actually distributed to class members, said Davis, the Liner LLP defense attorney.

"In our experience, people aren't that upset about this or confused about this,

so they are not looking for blood," Davis said. "We don't get a lot of objectors,

and there are funds left unclaimed by consumers."

For some, this type of scenario raises the question of whether cy pres — in so tidily disbursing such residuals — is improperly incentivizing the filing of so-called no injury lawsuits. In these suits, opponents argue, class members often don't go to the effort of putting in claims because they don't feel aggrieved.

In a study last year of nearly $4 billion worth of settlements in "no injury class actions," class members secured an average of 9 percent of the pot. In 37 cases with designated cy pres recipients, those organizations on average received 21 percent of the total award, according to the study, which was conducted by professor Joanna M. Shepherd of Emory University School of Law.

"A result in which plaintiffs recover less than 10 percent of the award, with the rest going to lawyers or unrelated groups, clearly does not reach the compensatory goals of class actions," Shepherd wrote in the study.

Last year, an Illinois federal court reluctantly approved a $6.75 million settlement in Kaufman v. American Express over alleged misrepresentations in the value of gift cards, where it estimated that the cy pres funds would run between $300,000 and $1.6 million. Only $1.3 million in claims had been made by class members, and most of the $4 million fund for claims had been decimated by extra court-ordered rounds of notices after initial claims totaled $41,510, according to court documents.

"By granting final approval, the court is acquiescing in a fundamentally problematic practice whereby attorneys for plaintiffs in class actions derive a greater monetary benefit from a

A Cue From Nonprofits

Most proposals to name a cy pres recipient come from plaintiffs counsel, or from a negotiation between both sides, or directly from the court. But parties in some larger class actions are starting to take a grant-like approach to vetting charities and distributing funds.

In January, for example, settlement administrator Harry Snyder opened up an application period for state and local agencies to grab a slice of two settlement funds totaling $943,000 — part of a larger $310 million settlement in California over alleged memory chip price-fixing. Agencies had until March 15 to submit proposals on how they would use two-year grants of up to $200,000 to support technology and software projects that would improve local government administration, such as using technology to engage with local populations on infrastructure improvements or crime prevention.

While these particular settlement funds are aimed at agencies, which could in turn contract with nonprofits, Snyder says this approach can generally work to keep settlement money from being wasted in general charity slush funds by forcing organizations to create programs that speak to the heart of the class members' concerns.

For example, among the more than 100 grants used to distribute $38 million from sprawling litigation in California over vitamin product price-fixing was a $276,813 award to a clinic that used the funds to distribute vitamins to low-income Los Angeles residents.

settlement than their respective clients," U.S. District Judge Joan B. Gottschall wrote in her opinion.

The Case for Cy Pres

Defenders of cy pres, however, argue that such a rigid accounting of settlement benefits unfairly diminishes the larger benefits that cy pres can provide, especially when the funds are leveraged in a way that creates a positive ripple effect.

Snyder, the settlement administrator, points to a $100,000 cy pres distribution given to California food policy advocates to work on a school lunches and breakfast campaign that helped get $18 million added to the California budget for those purposes.

"That's called a huge multiplier effect," said Snyder, who has used this approach on several class action settlements, mostly for state attorneys general. "They changed the way California schools gave kids the food."

The award was part of a 2003 deal that created a $38 million fund to settle antitrust claims that vitamin manufacturers had fixed certain product prices. The funds, which were distributed in four rounds of grants, were funneled toward a wide range of projects aimed at nutritional and health outreach as well as other public policy goals.

Others argue that the general use of cy pres in class actions — most often to disburse unclaimed funds and uncashed checks — helps to meet the intent of a settlement rather than allowing the funds to revert back to the company that was sued.

"The goal of cy pres has always been to further the purpose of the overall litigation," said Lindsay Nako, director of litigation and training at legal nonprofit Impact Fund.

Taking cy pres away and allowing unclaimed funds to be returned creates incentives for the defendant to inhibit distribution of class settlements, Nako said. And without cy pres to provide at least secondhand benefits, holding defendants accountable in such cases could be more challenging, especially given how few people retain the evidence needed to demonstrate injury.

"Who keeps a tag for the Levi Strauss jeans that you bought years ago?" Snyder said.

Even defense attorneys worry about the possible ramifications of the current class action reform bill on cy pres. Without the device, the administrative burdens involved in contacting class members would rise considerably, and companies would have to spend more time to create a settlement that is "fair, reasonable and adequate" — the required standard for such deals.

It could also lead to something else that costs a lot of time and money: more trials.

"Class actions will continue to be filed," BakerHostetler's Karlsgodt said. "And it will be much more difficult for defendants to settle."

Natalie Rodriguez is a feature reporter at Law360. Editing by Jeremy Barker and Jocelyn Allison.