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Viewing Class Settlements Through A New Lens: Part 2

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Law360, New York (July 26, 2017, 11:03 AM EDT) -- In part 1 of this two-part series, we discussed class action settlement economics, and suggested that judges should primarily measure the fairness of a proposed settlement in the context of the strength or weakness of the class' case. We continue this discussion by turning to the illustrative example of coupon (voucher) settlements — where class plaintiffs receive a coupon or voucher instead of cash — which can provide significant value to class members, particularly in cases where they would likely receive very little (or nothing) without a settlement.

Coupons and Vouchers

Coupons and vouchers can realign the economics of class settlements and provide even greater value to class members.

In many large class action cases, each class member's "injury" may be in the range of a few dollars or even less. Critics of coupon settlements argue that they enable class counsel to take "credit" (for purposes of calculating a fee award) for value that class members never actually see. But this fails to appreciate that in many instances, coupon/voucher settlements can effectively place class members in a far better position than the alternative of losing the case on the merits and getting nothing at all (or litigating for many years only to recover a portion of the value they could have received in the coupon years earlier). And of course, defendants may generally be willing to offer greater consideration via a coupon than with cash, since coupons may avoid the significant transaction costs associated with providing cash to millions of class members.

In many instances, coupon or voucher settlements can help to address the inefficiencies described in part 1 of this series, particularly when settling questionable cases that have a low chance of succeeding on the merits and/or providing class members with a significant recovery. Indeed, in many cases, vouchers can offer class members an even greater benefit than their best-case scenario at trial. Yet some courts have expressed concern that such settlements tend to "decoupl[e] the interests of the class and its counsel" and thereby incentivize class counsel to negotiate a large cash fee award for themselves, while their clients "receive nothing but essentially valueless coupons."[1]

Suspicion of coupon settlements explains the passage of certain provisions of the Class Action Fairness Act (CAFA) in 2005. In part, the concerns were overstated when CAFA was being debated in Congress because "settlements with coupons account[ed] only for about 10 percent of all class-action settlements. Moreover, according to ... sources, attorneys' fees correlate very closely with the amount of time spent on such cases by class counsel."[2] As one legislator recognized, "there is nothing inherently wrong with coupon settlements," especially when the actual damage to each potential plaintiff is small.[3]

However, Congress still included two specific provisions in CAFA to regulate coupon/voucher settlements.[4] First, Section 1712(a) provides that attorneys' fees must be calculated based on the value of coupons/vouchers that are actually redeemed by the class.[5] Second, Section1712(e) requires greater judicial scrutiny of coupon/voucher settlements.[6] Together, these provisions were meant to discourage coupon/voucher settlements by making them less valuable to class counsel and less likely to garner court approval. And since the passage of CAFA, courts have indeed viewed such settlements with increased skepticism, rejecting them in a number of notable instances.[7]

But as explained above, coupons and vouchers are not inherently a bad deal for class members; in many instances, they will provide greater benefits than the class could hope to achieve at trial, and even more value than they could have received with a cash settlement.[8] A number of courts have begun to acknowledge this reality.

For instance, in Yeagley v. Wells Fargo & Co., the court approved a voucher settlement that provided only "nominal value to the class," because "the likely rewards of litigation [were] nearly nil."[9] The plaintiffs alleged that the defendant violated the Fair Credit Reporting Act by obtaining credit reports without consumers' knowledge and sending them solicitations. The settlement gave each class member the right to receive two free credit reports and a FICOscore.[10] The court noted that the settlement was only of marginal value, since everyone is already entitled to one free credit report from credit agencies and can also look up their FICO scores for free.[11] Nevertheless, the court approved the settlement as fair, expressly casting doubt that the plaintiffs would be able to recover anything if the litigation proceeded since many courts had already rejected the core theory on the merits.[12] Thus, the court reasoned that "while the settlement offers little of value to the class, plaintiffs' case is weak and the class could not do better if the Court rejected the settlement."[13]

Likewise, in Fleury v. Richemont North America Inc., a settlement gave class members $100 credits (vouchers) to repair their Cartier watches.[14] The plaintiffs alleged that the defendant had illegally limited customers to having their watches repaired only at authorized dealers.[15] In approving the settlement, the court "acknowledged that the value of the settlement was not great. However, it rejected the contention that [the settlement] was without any worth, particularly since [defendant] has agreed to expand its network of authorized dealers."[16] The court also observed that "[t]he limited value of the settlement is appropriate in light of the significant litigation risks attendant to Plaintiffs' case. Most notably, there were significant litigation risks because of the weaknesses in Plaintiffs' claim," which was fatally flawed because of the facts at issue.[17]

Outside the voucher-settlement context, the Seventh Circuit took this reasoning a step further in In re Walgreens Co. Stockholder Litigation by suggesting that meritless class actions should not reach the settlement stage at all.[18] There, plaintiff stockholders brought a class action on the heels of a merger announcement, and then settled 18 days later. The settlement provided a $370,000 fee award while the class received only six "trivial" additions to the "extensive disclosures made in the proxy statement."[19] The court not only reversed the approval of this settlement, but commented that the only way to

prevent such misuse of the class action device — in cases that are transparently brought only for the purpose of exacting fees for class counsel — is by "giv[ing] serious consideration to either appointing new class counsel, or dismissing the suit."[20]

Takeaways

Settlement fairness should be judged primarily against the procedural and substantive strength of the case.

The most important inquiry when assessing the fairness of a class action settlement should be a reasoned prediction of the likely litigation outcome absent a settlement (discounted by the risk, expense and delay of achieving that outcome), compared with what the class would be getting in a settlement. However, many courts tend to give short shrift to this inquiry, putting class defendants in a Catch-22: Even if the defendant knows the case against it to be weak on the law or the facts, it must choose between (a) facing years of burdensome and costly litigation, including discovery, class certification proceedings, summary judgment, and possibly even trial and appeal, in order to defeat the claims; and (b) agreeing to settlement terms that, in order to ensure judicial approval and overcome the general skepticism of class settlements, may need to overcompensate a class of uninjured or nominally injured plaintiffs. This is far from an ideal model for dispute resolution.

Thus, courts reviewing the fairness of a class settlement should "determine whether the decision to settle is a good value for a relatively weak case."[21] In that light, "courts will," and should, "approve even seemingly inadequate settlements," including voucher settlements, "if the underlying claims are frivolous."[22] This is because the class' likely outcome at trial is the most important, most rational and most efficient consideration in the fairness calculus. Put differently, a low-value settlement is a perfectly fair, reasonable and adequate (and rational) way to dispose of a low-value case.[23] And this sliding scale will also dictate appropriate settlement terms in objectively stronger merits cases.

Taking this into account, coupon or voucher settlements remain an optimal way to resolve class disputes in many instances. CAFA's enhanced scrutiny should not obscure the practical realities of a litigation: If the settlement is rejected, will the class have a reasonable chance of doing substantially better after years of litigation? In a large number of cases, the answer is plainly "no."

Congress is well aware of, and working to address, the inequities and inefficiencies of the current class settlement regime. For instance, the proposed Fairness in Class Action Litigation Act of 2017 would prevent certain conflicts of interest between class counsel and the named plaintiffs, require class counsel to be paid according to the amount of value actually received by the class, and prevent unnecessary and expensive discovery while key motions are pending.[24] Ultimately, however, perhaps the Seventh Circuit's suggestion — that courts should consider disqualifying self-serving class counsel and/or dismissing weak cases at the outset — offers the fairest, most efficient result.

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[1] In re HP Inkjet Printer Litig., 716 F.3d 1173, 1178 (9th Cir. 2013) (quotation omitted).

[2] S. Rep. No. 109-14, at 77 (2005).

[3] H.R. Rep. No. 1115-149, at 5 (2003).

[4] H.R. Rep. No. 109-7, at 4–5 (2005).

[5] 28 U.S.C. § 1712(a).

[6] Id. § 1712(e) ("The court, in its discretion, may also require that a proposed settlement agreement provide for the distribution ... of unclaimed coupons to 1 or more charitable or governmental organizations ... The distribution and redemption of any proceeds under this subsection shall not be used to calculate attorneys' fees under this section.").

[7] See, e.g., Synfuel Techs. Inc. v. DHL Express (USA) Inc., 463 F.3d 646, 654 (7th Cir. 2006); see also S. Rep. No. 109–14, at 27 (stating that Section 5 of CAFA "requires greater scrutiny of coupon settlements"); Fed. R. Civ. P. 23(h), 2003 advisory committee's note ("Settlements involving nonmonetary provisions for class members also deserve careful scrutiny to ensure that these provisions have actual value to the class.").

[8] Practitioners should still be sensitive to courts' concerns with vouchers. For example, courts are more likely to approve voucher settlements that (a) can be aggregated; (b) provide free goods or services (like a gift card) or at least a considerable discount (e.g., courts would likely frown upon a $10 coupon on a new car); (c) allow transferability to others; (d) do not have burdensome time restrictions on redemption; (e) appropriately tailor the relief to the plaintiffs' theory of the case (e.g., a class of plaintiffs complaining about a defective crib might not want a voucher for a discount on a new crib); and (f) do not have an overly cumbersome claims process. See, e.g., HP Inkjet Printer Litig., 716 F.3d at 1179; In Re Online DVD-Rental Antitrust Litig., 779 F.3d 934, 951–52 (9th Cir. 2015); Reibstein v. Rite Aid Corp., 761 F. Supp. 2d 241, 255–56 (E.D. Pa. 2011); Young v. Polo Retail, LLC, No. C-02-4546, 2007 WL 951821, at *4 (N.D. Cal. March 28, 2007).

[9] No. C-05-03403, 2008 WL 171083, at *1, 3 (N.D. Cal. Jan. 18, 2008), rev'd on other grounds, 365 F. App'x 886 (9th Cir. 2010).

[10] Id., at *2.

[11] Id.

[12] Id. at *4.

[13] Id. at *3; see also In re Yahoo Mail Litig., No. 13-cv-04980, 2016 WL 4474612, at *6 (N.D. Cal. Aug. 25, 2016) (reasoning that "legal uncertainty" of a class's theory to recover damages "favors approval" of class action settlements).

[14] No. C-05-4525, 2008 WL 4680033, at *4 (N.D. Cal. Oct. 21, 2008).

[15] Id. at *1.

[16] Id.

[17] Id.

[18] Walgreens Co. Stockholder Litig., 832 F.3d at 725–26.

[19] Id. at 722.

[20] Id. at 726 (citing Fed. R. Civ. P. 23(g)(1); Robert F. Booth Trust v. Crowley, 687 F.3d 314, 319 (7th Cir. 2012)).

[21] Martin v. AmeriPride Servs., Inc., No. 08-cv-440, 2011 WL 2313604, at *6 (S.D. Cal. June 9, 2011).

[22] Hofmann v. Dutch LLC, 317 F.R.D. 566, 576 (S.D. Cal. 2016).

[23] See also Martin, 2011 WL 2313604, at *6 (approving a noncoupon settlement because the defendant's affirmative defense would "present a serious threat to Plaintiffs' claims"); Browning v. Yahoo! Inc., No. C-04-01463, 2007 WL 4105971, at *5 (N.D. Cal. Nov. 16, 2007) (holding that "the relief afforded to class members, although modest, is appropriate and valuable given the circumstances").

[24] See Fairness in Class Action Litigation Act of 2017, H.R. 985, 115th Congress (2017), passed by the House of Representatives on March 9, 2017.
