PUBLIC JUSTICE

15-CV-N

Via electronic delivery to: rules_support@ao.uscourts.gov

March 27, 2015

Committee on Rules of Practice and Procedure
Thurgood Marshall Building
Administrative Office of the United States Courts
One Columbus Circle NE
Washington, DC 20544

RE: Possible Amendments to Federal Rule of Civil Procedure 23

To the Members of the Advisory Committee on Civil Rules and the Rule 23 Subcommittee:

Public Justice, P.C. and the Public Justice Foundation (collectively, "Public Justice") respectfully submit the following suggestions for amending Federal Rule of Civil Procedure 23 to the Advisory Committee on Civil Rules and its Rule 23 Subcommittee (the "Subcommittee").

Public Justice is the only public interest organization in the country that both aggressively prosecutes a wide range of class actions and has a special project to preserve class actions and prevent their abuse. Public Justice regularly represents workers and consumers in both individual and class actions, and its experience is that aggregate litigation often affords the only way to address corporate wrongdoing where individuals by themselves lack the knowledge, incentive, or effective means to pursue their claims.

Public Justice hereby urges the Subcommittee to adopt the following proposed amendments in order to address certain proposals and judicial decisions that threaten to undermine the viability of the class action device and run contrary to the core purposes of Rule 23.

I. Rule 23(b)(3) Should Be Amended to Add Deterrence of Wrongdoing as a Factor in Determining Whether a Class Action Is the Superior Method of Litigation.

Summary:

Legal commentators and judges alike have long recognized deterrence of wrongdoing as a proper purpose, and beneficial effect, of class litigation. By aggregating small-value claims when the damage caused by wrongdoing is widespread but not ruinous to any of its individual victims, class actions can be particularly well suited to serving this deterrence function. We believe that this oft-cited benefit of class actions should be recognized, and considered on a case-by-case basis, by judges deciding whether to certify class actions under Rule 23. We propose formalizing the deterrence inquiry into the class certification analysis by adding it as an explicit factor under Rule 23(b)(3), to be weighed when ascertaining whether a class action is superior to other forms of litigation in a particular case.

Proposed Amendment:

Rule 23(b) should be amended as follows (matters in brackets are to be deleted; matters italicized are to be added):

> **(b) Types of Class Actions.** A class action may be maintained if Rule 23(a) is satisfied and if:
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> *** * ***
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> **(3)** the court finds that the questions of law or fact common to class members predominate over any questions affecting only individual members, and that a class action is superior to other available methods for fairly and efficiently adjudicating the controversy. The matters pertinent to these findings include:
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> **(A)** the class members' interests in individually controlling the prosecution or defense of separate actions;
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> **(B)** the extent and nature of any litigation concerning the controversy already begun by or against class members;
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> **(C)** the desirability or undesirability of concentrating the litigation of the claims in the particular forum; [and]

(D) the likely difficulties in managing a class action*; and*

(E) *the comparative effectiveness of the class action device in deterring the particular type of misconduct alleged.*

Analysis:

The class action is widely recognized as a vehicle for effective deterrence of wrongdoing. *See* Newberg on Class Actions § 1:8 (5th ed. 2013) ("In addition to their compensatory function, class actions deter misconduct by harnessing private attorneys general to assist in the enforcement of important public policies."); *Hughes v. Kore of Ind. Enter., Inc.*, 731 F.3d 672, 677 (7th Cir. 2013) ("A class action, like litigation in general, has a deterrent as well as a compensatory objective."); Edward F. Sherman, *Consumer Class Actions: Who Are the Real Winners?*, 56 Me. L. Rev. 223, 228 (2004) ("[I]t must be kept in mind that the objective of consumer class actions is not only compensation, but also deterrence and disgorgement of wrongful profits.").

As Judge Posner noted in the *Hughes* decision, litigation in any form provides some amount of deterrent value. 731 F.3d at 677. However, the class action vehicle goes further than ordinary individual litigation in providing deterrence in circumstances where it would otherwise be lacking. *Id.* at 678. First, the aggregating of small claims enables deterrence against widespread wrongdoing, even when individual damages are relatively small. *See Hawaii v. Standard Oil Co. of Cal*., 405 U.S. 251, 266 (1972) ("Rule 23 . . . provides for class actions that may enhance the efficacy of private actions by permitting citizens to combine their limited resources to achieve a more powerful litigation posture."); *Jones v. DirecTV, Inc.*, 381 F. App'x 895, 896 (11th Cir. 2010) (recognizing that class actions support "a public policy favoring the pursuit of small-value claims to deter companies from misconduct."); *deHaas v. Empire Petroleum Co.*, 435 F.2d 1223, 1231 (10th Cir. 1970) ("Since [class action rules] allow many small claims to be litigated in the same action, the overall size of compensatory damages alone may constitute a significant deterrent.")

Second, class litigation empowers private parties to act as private attorneys general, enforcing public interests where public law enforcement entities are unable or unwilling to do so. This deterrent function fills the gaps in many areas of the law including antitrust, securities fraud, and consumer financial protection; and it offers several advantages over governmental or agency action. *See, e.g.*, Mark A. Cohen & Paul H. Ruben, *Private Enforcement of Public Policy*, 3 Yale J. on Reg. 167, 168-69 (1985) (arguing that private enforcement may be more

efficient than public enforcement); Barton H. Thompson, Jr., *The Continuing Innovation of Citizen Enforcement*, 2000 U. Ill. L. Rev. 185, 189-92 (2000) (arguing that private enforcers are less conflicted and less politically constrained than captured public agencies); Warren F. Schwartz, *An Overview of the Economics of Antitrust Enforcement*, 68 Geo. L.J. 1075, 1093 (1980) (same); Thompson, *supra*, at 206 (arguing that private enforcement generates more innovative means of deterrence against wrongful conduct).

A class action will not be a more effective deterrent to wrongdoing than other methods of litigation in every case. For example, when a governmental agency has the authority to exact civil penalties or other sanctions, enforcement action by that agency might well have a stronger deterrent effect than a class action brought by individuals only seeking damages. Governmental action is not always feasible, however, due to scarce resources and conflicting priorities. Class actions are an indispensable way to deter wrongdoing without straining the public coffers. Given the universal recognition of deterrence as a beneficial result of class action litigation, we urge that deterrence be formally included in Rule 23(b)(3)'s analysis of superiority.

II. Rule 23 Should Be Amended to Rectify Court Decisions that Impose a Rigid "Ascertainability" Requirement as a Precondition for Class Certification.

Summary:

In the wake of the Third Circuit's decision in *Carrera v. Bayer Corp.*, 727 F.3d 300 (3d Cir. 2013), courts have been struggling to decide whether Rule 23 requires a showing, at the class certification stage, that the identity of individual class members be "currently and readily ascertainable based on objective criteria." *Id*. at 305 (quoting *Marcus v. BMW of N. Am., LLC*, 687 F.3d 583, 592-93 (3d Cir. 2012)). The *Carrera* panel denied certification of a consumer class action over weight-loss supplements on "ascertainability" grounds even though (1) the class was readily defined based on objective criteria; (2) the defendant's liability was capped at a certain amount; and (3) absent a class action, the consumers would have had no practical ability to redress their injuries.

Notably, four Third Circuit judges dissented from the denial of rehearing en banc in *Carrera*, stating that the panel's decision "goes too far" and arguably "threatens the viability of the low-value consumer class action 'that necessitated Rule 23 in the first instance.'" 2014 WL 3887938, at *1, *2 (May 2, 2014) (quoting Br. of *Amici Curiae* Professors of Civil Procedure and Complex

Litigation 3). The dissent further noted that "[t]he consequence of a step too far is the curtailment of well-intentioned class actions with many members yet all with claims too minimal to be asserted individually." *Id.* at *3. The dissent concluded that, in light of the potentially grave impact of the panel's decision on the viability of small-damages class actions, "the Judicial Conference's Committee on Rules of Practice and Procedure [should] look into this matter." *Id*.

We strongly agree. As explained below, *Carrera* conflicts with well-established Rule 23 jurisprudence and undermines the core purposes of Rule 23(b)(3). It has also spawned conflicting rulings on the so-called ascertainability issue. Guidance, in short, is sorely needed. We accordingly urge the Subcommittee to amend Rule 23(c) to make clear that "ascertainability" merely requires a finding, at the class certification stage, that the class *definition* is based on objective criteria. This is the majority approach used by courts in the past, and it should be enshrined in the Rule to prevent further confusion on this important point.

Proposed Amendment:

Rule 23(c) should be amended as follows (matters in brackets are to be deleted; matters italicized are to be added):

> **(c) Certification Order; Notice to Class Members; Judgment; Issues Classes; Subclasses.**
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> **(1)** ***Certification Order.***
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> *** * ***
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> **(B) Defining the Class; Appointing Class Counsel.** An order that certifies a class action must define the class and the class claims, issues, or defenses, and must appoint class counsel under Rule 23(g). *In certifying a class under Rule 23(b)(3), the court must define the class so it is ascertainable by reference to objective criteria. The ascertainability or identifiability of individual class members is not a relevant consideration at the class certification stage.*

Analysis:

A. The Proposed Amendment Is Consistent with—and Intended to Codify—Pre-*Carrera* Judicial Practice.

The proposed amendment set forth above is consistent with the way the majority of courts approached "ascertainability" prior to the Third Circuit's decision in *Carrera* and is designed to correct what we see as the major flaw of that ruling. Before addressing *Carrera* in detail (which we do below), it may be helpful to explain why we are proposing to add "ascertainability" to Rule 23(c), as opposed to some other part of the Rule.

Although ascertainability is not an explicit element of Rule 23, many courts view ascertainability as an "implicit" requirement of the Rule. Courts differ, however, as to the statutory basis for that requirement. *See generally* Newberg on Class Actions § 3:2 (5th ed. 2013); 1 McLaughlin on Class Actions § 4.2 (11th ed. 2014). Some courts imply that the term "class" in Rule 23(a) means a definite or ascertainable class; others find support for ascertainability in Rule 23(c)(1)(B), which governs class certification; yet others look to Rule 23(c)(2), which governs the provision of class notice in some types of class actions. *Id.; see generally* Daniel Luks, *Ascertainability in the Third Circuit: Name that Class Member*, 82 Fordham L. Rev. 2359 (2014) (discussing origins of ascertainability). Ascertainability is also arguably an implicit consideration under Rule 23(b)(3), which requires courts to determine whether a class action is "superior to other available methods for fairly and efficiently adjudicating a controversy."

We think that it makes the most sense to address ascertainability in Rule 23(c)(1)(B), which is the stage of class litigation when the question naturally arises and becomes potentially dispositive. However, because "ascertainability" is generally only considered in the context of (b)(3) damages classes, our proposed amendment would limit the amendment to classes brought under that prong of Rule 23.

The wording of the proposed amendment—which provides that "[i]n certifying a class under Rule 23(b)(3), the court must define the class so it is ascertainable by reference to objective criteria"—is consistent with the way pre-*Carrera* courts approached the issue. As one noted authority has written, ascertainability has always "focus[ed] on the question of whether the class can be ascertained by objective criteria," as opposed to "subjective standards (*e.g.* a plaintiff's state of mind) or terms that depend on resolution of the merits (*e.g.*

persons who were discriminated against)." Newberg on Class Actions § 3:3; *see also* Manual for Complex Litig., Fourth § 21.222 (Fed. Judicial Ctr. 2004).

Importantly, courts have long "held that the class does not have to be so ascertainable that every potential member can be identified at the commencement of the action." 7A Wright & Miller, Federal Practice & Procedure § 1760 (3d ed. 2005); *see also* Newberg on Class Actions § 3:3; Manual for Complex Litig. § 21.222. As one learned treatise put it, "[t]o place such a burden on plaintiffs would seem harsh and unnecessary" and make many class actions "very difficult, if not impossible." Wright & Miller § 1760. Hence, "[i]f the general outlines of the membership class is determinable at the outset of the litigation, a class will be deemed to exist." *Id*. (footnote omitted). *Accord Fitzpatrick v. General Mills, Inc.*, 635 F.3d 1279 (11th Cir. 2011) (holding that class defined as "all persons who purchased [the defendant's product] in the State of Florida" is adequately ascertainable for class certification purposes).

Requiring courts to consider whether the class definition is based on objective criteria would weed out class actions where the proposed class is so amorphous as to render class treatment unworkable and arguably unfair. For example, the Fifth Circuit once refused to certify a class of "residents of this State active in the 'peace movement' who have been harassed and intimidated as well as those who fear harassment and intimidation in exercising their First Amendment right." *DeBremaecker v. Short*, 433 F.2d 733, 734 (5th Cir. 1970). The Court noted that an essential element to maintaining a class action is that the class be "adequately defined and clearly ascertainable." This requirement was not met, in the Court's view, because the term "peace movement" could mean any number of things, and because it would be impossible to determine which class members "feared harassment and intimidation" without individualized findings of fact.[1]

We agree with this conclusion. It makes perfect sense to eliminate class actions where the class definition is based on subjective criteria. The proposed amendment is designed to codify this approach. What does *not* make sense, in our view, is the approach the Third Circuit adopted in *Carrera*, which makes it virtually impossible to obtain class certification in precisely the cases that need it most—cases involving small-value retail products, where individuals are unlikely

[1] Other circuits' approaches have been similar. *See, e.g., Simer v. Rios*, 661 F.2d 655, 669 (7th Cir. 1981); *Ihrke v. N. States Power Co.*, 459 F.2d 566, 573 & n.3 (8th Cir. 1972), *vacated as moot*, 409 U.S. 815 (1972).

to have kept receipts of their purchases and class membership cannot be proven based on the defendants' own records.

B. *Carrera* Is Contrary to Rule 23, Lacks any Grounding in Common Sense, and Has Caused Rampant Confusion in the Courts.

Contrary to all the authorities cited above, *Carrera* held that a consumer class action cannot be certified unless the plaintiffs can prove (1) that that they will be able to identify—or "ascertain"—the individual members of the class; (2) that they will be able to do so through a process that is "reliable," "administratively feasible," and does not require "much, if any, individual factual inquiry"; and (3) that they will be able to do so without relying on affidavits and claims forms (used in claims processes for decades) because those forms of proof are not sufficiently "reliable." *See* 727 F.3d at 307-10.

Applying these criteria to the facts before it, *Carrera* held that the plaintiff class could not be certified even though (1) the damages were too small to justify individual litigation, yet the misconduct was substantial; (2) the proposed class was clearly and objectively defined (it consisted of all persons who purchased a single product—WeightSmart—in a single state—Florida—within a known time period); and (3) it was undisputed that the defendant's total liability to the class was capped at a finite amount that could be determined based on the company's own records.

1. *Carrera* Is Contrary to Rule 23(b)(3)'s Core Purposes.

We believe that this result is indefensible on several levels. First and foremost, *Carrera* runs afoul of the most basic purposes underlying Rule 23(b)(3). As the U.S. Supreme Court has explained, "[t]he policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights." *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617 (1997) (quotation omitted). "A class action solves this problem by aggregating the relatively paltry potential recoveries into something worth someone's (usually an attorney's) labor." *Id*. (citation omitted). As another court has written, "[t]he smaller the stakes to each victim of unlawful conduct, the greater the economies of class action treatment and the likelier that the class members will receive some money rather than (without a class action) probably nothing." *Hughes v. Kore of Ind. Enter., Inc.*, 731 F.3d 672, 675 (7th Cir. 2013).

If *Carrera*'s approach to ascertainability becomes the law of the land, "the problem" addressed in *Amchem* will go unrectified in a large number of cases and

tortfeasors will get off scot free. That cannot be reconciled with the core purposes of Rule 23. *See* Judith Resnick, *From "Cases" to "Litigation,"* 54 Law & Contemp. Probs. 5, 14 (1991) (explaining that Benjamin Kaplan, primary drafter of Rule 23, intended the rule to "provide means of vindicating the rights of groups of people who individually would be without effective strength to bring their opponents into court at all") (citation omitted).

2. *Carrera*'s Reasoning Is Unconvincing and Illogical.

Second, *Carrera*'s reasoning is flawed at its core. The *Carrera* panel defended its novel approach to ascertainability on the ground that defendants have a "due process right to challenge class membership" at the class certification stage. 727 F.3d at 307. But the *Carrera* defendant's total liability was capped at $14 million, "no more, no less." *Id*. at 310. This amount, moreover, was based on the defendant's own sales records/data, rather than an artificially-limited fund, so there is no question that the liability amount was based on actual damages. Because the defendant's total payout would be the same regardless of whether individual class members could be identified—or "ascertained"—there was no basis for the panel's refusal to allow the case to proceed on due process grounds.

Carrera also reasoned—equally wrongly, in our view—that its approach was necessary to protect the defendant from the risk of a collateral attack on the judgment by aggrieved class members whose recoveries were substantially reduced by "fraudulent or inaccurate claims." *Id.* at 310. This argument fails, first, because the notion that a significant number of non-class members would submit fraudulent or otherwise faulty affidavits, under penalty of perjury, in the hope of collecting a few dollars, is itself far-fetched. Second, even if there were a substantial number of fraudulent claims, the likelihood that class members' relief would be affected is minimal given that, "in small-claims, consumer class actions, less than twenty percent" of class members actually file a claim. M. Gilles, *Class Dismissed: Contemporary Judicial Hostility to Small-Claims Consumer Class Actions*, 59 DePaul L. Rev. 305, 315 (2010). And third, even if the possibility that class members' claims would be "diluted" by fraudulent claims were substantial, it is "exceedingly rare for court to permit after-the-fact challenges by class members." Alison Frankel, *2nd Circuit: Class Members Deserve Notice*, Reuters, Aug. 25, 2012.

The final error in *Carrera* was its view that a rigid approach to ascertainability is needed to protect *absent class members* from the risk that their recoveries will be diluted by fraudulent claims. *See Carrera*, 727 F.3d at 310. Not only was there no factual basis for this concern (as explained above), but the panel

ignored that, absent a class action, the absent class members would have no practical means of recovering *anything* from the defendant, let alone the full value of their claims. In the end, the supreme irony of *Carrera* is that, in purporting to protect class members by denying class certification on ascertainability grounds, the Third Circuit effectively insured that they would not recover anything at all.

3. *Carrera* Has Engendered Confusion and Disagreement in Other Circuits.

Finally, it is important to note that *Carrera* has engendered widespread confusion and disagreement in other courts. In the wake of *Carrera*, a number of courts have refused to certify class actions on ascertainability grounds, despite the fact that the class was clearly defined based on objective criteria and the damages at issue were too small to support individual litigation.[2]

For example, in *Karhu v. Vital Pharmaceuticals, Inc*., 2014 WL 815253 (S.D. Fla. Mar. 3, 2014), the district court refused to certify a class of consumers who alleged that the dietary supplement Meltdown does not burn fat and promote rapid fat loss as advertised. The court denied class certification on ascertainability grounds, holding that there was no record of Meltdown purchasers, it was unlikely that Meltdown purchasers save their receipts, and affidavits from class members would not be trustworthy. *Id*. at *3. Relying on *Carrera,* the court reached this result despite the plaintiff's argument that the defendant could easily identify many class members by sending subpoenas to the retailers identified in its sales records. *Id. Accord Randolph*, 2014 WL 7330430 (refusing to certify consumer class on ascertainability grounds; following *Karhu* and *Carrera).*[3]

Courts in the Ninth Circuit are particularly conflicted on this issue. In *Lilly v. JambaJuice Co.*, 2014 WL 4652283, at *4 (N.D. Cal. Sept. 18, 2014), for example,

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[2] *See, e.g., In re Clorox Consumer Litig.*, 301 F.R.D. 436, 442 (N.D. Cal. 2014) (refusing to certify class of purchasers of cat litter on ascertainability grounds); *In re Intel Corp. Microprocessor Antitrust Litig.*, 2014 WL 6601941, at *12 (D. Del. July 31, 2014) (refusing to certify antitrust and consumer protection class action on ascertainability grounds); *Langendorf v. Skinnygirl Cocktails, LLC*, 2014 WL 5487670, at*1-*2 (N.D. Ill. Oct. 30, 2014) (refusing to certify consumer class action against maker of premixed alcoholic beverage on ascertainability grounds); *Randolph v. J.M. Smucker Co.*, 2014 WL 7330430, at*4 (S.D. Fla. Dec. 23, 2014) (refusing to certify consumer class action against producer of various cooking oils on ascertainability grounds).

[3] The Eleventh Circuit heard oral argument in *Karhu* on February 6, 2015. *See Karhu v. Vital Pharm., Inc.*, No. 14-11648.

the court affirmatively rejected *Carrera* as having "significant negative ramifications for the ability to obtain redress for consumer injuries. Few people retain receipts for low-priced goods, since there is little possibility that they will need later verify that they made the purchase. Yet is it precisely in circumstances like these, where the injury to any individual consumer is small, but the cumulative injury to consumers as a group is substantial, that the class action mechanism provides one of its most important social benefits."[4]

But in *Jones v. ConAgra Foods Inc.*, 2014 WL 2702726 (N.D. Cal. June 13, 2014), the district court embraced *Carrera* and refused to certify a class of purchasers who allege that ConAgra Foods mislabeled and misbranded canned tomatoes, cooking spray, and hot cocoa in violation of California and federal law. *Id.* at *11. On appeal to the Ninth Circuit, the *Jones* plaintiffs are challenging the lower court's ruling, saying it imposes an ascertainability requirement separate from the demands of Rule 23. *See Jones v. ConAgra Foods Inc.*, Case No. 14-16327.

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These are but a few examples of the disagreement that has emerged in the wake of *Carrera*. To prevent further discord and disagreement, this Committee should act expeditiously to correct the Third Circuit's error and ensure that class actions remain available for the vindication of small money damages claims, as the framers of Rule 23(b)(3) intended.

III. Rule 68 Should Be Abrogated Because It Has Failed to Serve Its Stated Purpose and Given Rise to Unjust and Inconsistent Results, Particularly in the Class Action Context.

Summary:

Rule 68 permits defendants to make offers of judgment to settle plaintiffs' claims and to recover costs from plaintiffs who ultimately obtain a judgment for less than the amount of the offer. This rule has been described as "among the most enigmatic of the Federal Rules of Civil Procedure." *Crossman v. Marcoccio*, 806

[4] *See also Brazil v. Dole Packaged Foods, LLC*, 2014 24665529, at *4-6 (N.D. Cal. May 30, 2014), *class decertified on other grounds*, 2014 WL 5794873 (N.D. Cal. Nov. 6, 2014) (declining to follow *Carrera*); *Forcellati v. Hyland's, Inc.*, 2014 WL 1410264, at *5 (C.D. Cal. 2014) ("Given that facilitating small claims is '[t]he policy at the very core of the class action mechanism,' . . . we decline to follow *Carrera*.") (quoting *Amchem Prods.*, 521 U.S. at 617).

F.2d 329, 331 (1st Cir. 1986). Empirical studies have shown that it is ineffective at promoting settlement. *See, e.g.*, David A. Anderson & Thomas D. Rowe, Jr., *Empirical Evidence on Settlement Devices: Does Rule 68 Encourage Settlement?*, 71 Chi.-Kent L. Rev. 519, 531-32, 534-35 (1995). At the same time, Rule 68 has been widely criticized for giving defendants an unfair advantage and coercing plaintiffs to settle meritorious claims for artificially low damages.

Perhaps the most coercive aspect of Rule 68 involves defendants' use of unaccepted Rule 68 offers to moot cases on the ground that the offer includes all of the relief to which the plaintiff was legally entitled. Although some courts in these situations enter judgment for the plaintiff in the amount of the offer,[5] other courts reason that if the plaintiff's claim is indeed moot, the court does not have the power to enter judgment upon it; in such cases, the claim is dismissed for lack of subject matter jurisdiction, and the plaintiff receives nothing.[6]

The question of whether an unaccepted Rule 68 offer can moot a case takes on added significance when the plaintiff receiving such an offer seeks to represent others with similar claims in a collective or class action. The Supreme Court addressed this question, but did not provide a clear answer, in *Genesis Healthcare Corp. v. Symczyk*, 133 S. Ct. 1523 (2013). The *Genesis* majority assumed without deciding, over a spirited dissent written by Justice Kagan, that an unaccepted Rule 68 offer rendered the plaintiff's individual claims moot, and then went on to hold that her collective action claims under the Fair Labor Standards Act became moot when her individual claims did. *Id.* at 1532. *Genesis* has sparked a flurry of Rule 68 offers to plaintiffs not just in FLSA collective actions but also in Rule 23 class actions, despite the "fundamental[] differen[ces]" between those two claim-aggregating devices that the majority emphasized in its opinion. *See id*. at 1531-32. The goal of these offers is clear: to eliminate class and collective actions by "picking off" the named plaintiffs' claims through Rule 68 offers of judgment. [7]

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[5] *See, e.g.*, *Cabala v. Crowley*, 736 F.3d 226, 228 (2d Cir. 2013); *O'Brien v. Ed Donnelly Enters*., 575 F.3d 567, 575 (6th Cir. 2009).

[6] *See, e.g.*, *Greisz v. Household Bank (Ill.) N.A.*, 176 F.3d 1012, 1015 (7th Cir. 1999); *Bradford v. HSBC Mortgage Corp.*, 280 F.R.D. 257, 264 (E.D. Va. 2012); *Johnson v. Midwest ATM, Inc.*, 881 F. Supp. 2d 1071, 1073 (D. Minn. 2012).

[7] To be more precise, in *Genesis*, the Court concluded that the issue was not properly before it because the court below had ruled that the plaintiff's individual claims (but not her collective action claims) were mooted by the unaccepted Rule 68 offer, and the Court could not reach the issue without a cross-petition from the plaintiff. 133 S. Ct. at 1528-29.

Courts throughout the country evaluating these "pick-off" offers have reached different conclusions regarding the ability of an unaccepted Rule 68 offer to moot an individual plaintiff's claim and/or the claims of a class that has not yet been certified. This state of affairs undermines the purposes of Rule 23 by causing putative class actions to be dismissed before their merits can be examined. The Rule 68 "pick-off" phenomenon also undermines the purposes of Rule 68 itself—to promote settlement and discourage protracted litigation—by spurring ever more collateral litigation over what these offers mean and what effect they have.

In short, we believe that Rule 68 has been a failed experiment with pernicious results that are only growing worse, and that it is time for the experiment to end.

Proposed Amendment:

Rule 68 should be abrogated in its entirety. The Rule presently provides as follows (items to be deleted are bracketed):

[Rule 68: Offer of Judgment

(a) Making an Offer; Judgment on an Accepted Offer. At least 14 days before the date set for trial, a party defending against a claim may serve on an opposing party an offer to allow judgment on specified terms, with the costs then accrued. If, within 14 days after being served, the opposing party serves written notice accepting the offer, either party may then file the offer and notice of acceptance, plus proof of service. The clerk must then enter judgment.

(b) Unaccepted Offer. An unaccepted offer is considered withdrawn, but it does not preclude a later offer. Evidence of an unaccepted offer is not admissible except in a proceeding to determine costs.

(c) Offer After Liability Is Determined. When one party's liability to another has been determined but the extent of liability remains to be determined by further proceedings, the party held liable may make an offer of judgment. It must be served within a reasonable time—but at least 14 days—before the date set for a hearing to determine the extent of liability.

(d) Paying Costs After An Unaccepted Offer. If the judgment that the offeree finally obtains is not more favorable than the unaccepted offer, the offeree must pay the costs incurred after the offer was made.]

A**nalysis:**

A. Rule 68 Is Ineffective at Promoting Settlement and Unfairly Disadvantages Plaintiffs.

Separate and apart from the particular problem of class actions (which is addressed below), Rule 68 is generally considered to have been ineffective in achieving its paramount goal: promoting the settlement of individual litigation. It also imposes a bizarre incentive structure that particularly penalizes plaintiffs. For both reasons, the Rule has failed to perform the job for which it was intended.

Regarding the former, the Supreme Court has held that "[t]he purpose of Rule 68 is to encourage the settlement of litigation." *Delta Air Lines, Inc. v. August*, 450 U.S. 346, 352 (1981). However, over 30 years ago the Civil Rules Advisory Committee noted that Rule 68 "has been considered largely ineffective as a means of achieving its goals." *Committee on Rules of Practice and Procedure of the Judicial Conference of the U.S., Preliminary Draft of Proposed Amendments to the Federal Rules of Appellate Procedure, Federal Rules of Civil Procedure, Federal Rules of Criminal Procedure and Rules Governing Section 2254 Cases and Section 2255 Proceedings in the United States District Courts*, 102 F.R.D. 407, 433 (1984).

One widely cited reason for the Rule's ineffectiveness is the one-sided nature of its cost-shifting provision: It allows only defendants to make offers of judgment and thus exposes only plaintiffs to the risk of paying the other party's costs if they ultimately obtain a judgment of lesser value than the unaccepted offer. This asymmetrical structure, according to economists, results in defendants making lower settlement offers than they would in the absence of such a rule; many plaintiffs refuse those discounted offers, and those who accept them are typically the most economically vulnerable litigants who are "least able to withstand the adverse effect of paying the defendant's litigation expenses." George L. Priest, *Regulating the Content and Volume of Litigation: An Economic Analysis*, 1 Sup. Ct. Econ. Rev. 163, 179 (1982). Thus the Rule's "primary effect is not to encourage settlement but to benefit defendants and harm plaintiffs by shifting downward the relevant settlement range." Geoffrey P. Miller, *An Economic Analysis of Rule 68*, 15 J. Legal Stud. 93, 94 (1986).

Some defendants are also disinclined to make Rule 68 offers because the Rule requires that judgment be entered in the offeree's favor in a public court proceeding. In addition to the negative consequences that such judgments have on credit and insurability, many defendants shun them as an implicit admission of

liability, or an invitation to regulatory scrutiny or follow-on lawsuits. *See* Harold S. Lewis Jr. & Thomas A. Eaton, *Rule 68 Offers of Judgment: The Opinions and Practices of Experienced Civil Rights and Employment Discrimination* Attorneys, 241 F.R.D. 332, 346, 350 (2007) (hereafter, Lewis & Eaton). For many defendants, a privately negotiated settlement, often with confidential terms and a disclaimer of liability, is a more attractive option than the rigid formula of Rule 68.

Rule 68's ineffectiveness in promoting settlement has also been attributed to the fact that the cost-shifting sanction for an unaccepted Rule 68 offer is triggered only when the offeree prevails—albeit for a lesser amount than the offer. Defendants who are confident of winning outright have little incentive to make an offer and often prefer to take their chances with a motion for summary judgment. *See* Lewis & Eaton, *supra*, at 350.

Rule 68 is problematic for an additional reason: Even where it succeeds in promoting settlement, it does so in a way that is unfair to plaintiffs. Rule 68 is unique among the Federal Rules of Civil Procedure in that it contains a cost-shifting sanction not for litigants who are found to have acted in bad faith, such as by filing frivolous pleadings[8] or failing to cooperate in discovery,[9] or even for parties who lose,[10] but for plaintiffs who prevail and obtain a judgment—just for less than the defendant previously offered. Given the vagaries of jury trials, plaintiffs who do not in fact believe an offer to be fair or reasonable may nonetheless accept it because they are unwilling to risk being slightly less successful at trial than they expected to be. This is particularly true since the Supreme Court's 1985 decision in *Marek v. Chesny*, which held that plaintiffs penalized for rejecting a Rule 68 offer may, under certain statutes, also be deprived of the attorneys' fees that prevailing plaintiffs suing under those statutes would otherwise recover. 473 U.S. 1, 9 (1985). This bizarre incentive structure has led one commentator to observe that the American Rule provides that each party pays its own fees and costs, the British Rule awards fees and costs to the prevailing party, but Rule 68 can best be termed "the Vegas Rule." Bruce P. Merenstein, *More Proposals to Amend Rule 68: Time to Sink the Ship Once and for All,* 184 F.R.D. 145 (1999). Plaintiffs who "settle" because they aren't willing to take this

[8] Rule 11; Rule 26(g).

[9] Rule 30(g) (failure to attend noticed deposition); Rule 37(b)(2)(E), (c), and (d) (refusal to make required disclosures).

[10] Rule 54(d).

gamble are not making a free economic choice; rather, they are being coerced by the punitive terms of the rule and court decisions interpreting it. In light of the Advisory Committee's recognition that "[t]here is no preexisting procedural duty to settle," Minutes of the Advisory Committee on Federal Rules of Civil Procedure (Apr. 1994), 1994 WL 809916, at *19, this is unacceptable.

B. Rule 68 Poses Particular Problems in the Class Action Context and Undermines the Purposes of Rule 23 in Several Respects.

The problems with Rule 68 are magnified in the context of collective and class actions, where defendants are increasingly using Rule 68 offers of judgment as a means of "picking off" lead plaintiffs and rendering the entire action moot. A number of lower federal courts have held that when a defendant makes an offer under the Rule that the court deems sufficient to give the plaintiff all she could have recovered at trial, the offer (whether accepted or not) deprives the court of subject matter jurisdiction over the dispute by rendering it moot. *E.g.*, *Rand v. Monsanto Co.*, 926 F.2d 596, 598 (7th Cir. 1991) ("Once the defendant offers to satisfy the plaintiff's entire demand, there is no dispute over which to litigate, and a plaintiff who refuses to acknowledge this loses outright, under Fed. R. Civ. P. 12(b)(1), because he has no remaining stake.") (internal citations omitted). Justice Kagan pointed out the incongruity of this result in her *Genesis* dissent, noting that "[a]n unaccepted settlement offer—like any unaccepted contract offer—is a legal nullity, with no operative effect" and that "[n]othing in Rule 68 alters that basic principle." 133 S. Ct. at 1533-34. Yet a number of lower courts had held prior to *Genesis* that an unaccepted Rule 68 offer would render a plaintiff's claim moot,[11] and some courts have reached the same result in the years since *Genesis* was decided.[12]

Courts are also struggling with the question of whether, assuming a Rule 68 offer moots the individual claims of a named plaintiff in a putative class action, the claims of absent class members are rendered moot as well. The Supreme Court has held that the mooting of a class representative's claim will not render the class action moot if a class has already been certified, *Sosna v. Iowa*, 419 U.S. 393, 399

[11] *See, e.g.*, *Weiss v. Regal Collections*, 385 F.3d 337, 340 (3d Cir. 2004); *Krim v. PCOrder.com*, 402 F.3d 489 (5th Cir. 2005); *Russell v. United States*, 661 F.3d 1371 (Fed. Cir. 2011).

[12] S*ee, e.g.*, *Scott v. Westlake Servs. LLC*, 740 F.3d 1124 (7th Cir. 2014); *Doyle v. Midland Credit Mgmt.*, 722 F.3d 78, 81 (2d Cir. 2013); *Silva v. Tegrity Personnel Servs., Inc.*, 986 F. Supp. 2d 826, 834 (S.D. Tex. 2013). *But see Diaz v. First Am. Home Buyers Prot. Corp.*, 732 F.3d 948 (9th Cir. 2013) (adopting reasoning of Justice Kagan's dissent); *Stein v. Buccaneers Ltd. P'Ship*, 772 F.3d 698 (11th Cir. 2014) (same).

(1975), or if class certification has been sought and denied, *see Deposit Guar. Nat'l Bank, Jackson, Miss. v. Roper*, 445 U.S. 326, 339 (1980). But matters are far more uncertain when a class certification motion has not yet been filed or has been filed but not yet ruled upon by the court.

Some courts have held that if a defendant makes a Rule 68 offer before the plaintiff moves for class certification, the motion for class certification will relate back to the date on which the complaint was filed to protect the putative class from the jurisdiction-stripping effects of Rule 68 until the court has an opportunity to rule on the certification motion.[13] But even here, there is some confusion: Courts utilizing this "relation-back" doctrine agree that the certification motion must be *timely* made after the Rule 68 offer, and there is a lack of clear guidance or uniformity about what is considered timely. *See, e.g.*, *Morgan*, 2006 WL 2597865, at *4 ("there is no consistent definition of what constitutes . . . an undue delay warranting dismissal").

Making the situation even more confusing, the Seventh Circuit has rejected the relation-back approach altogether and held that if a putative class representative receives an offer of full relief before a motion for class certification is filed, the class as well as the individual claims become moot. *E.g.*, *Damasco v. Clearwire Corp.*, 662 F.3d 891, 895-96 (7th Cir. 2011) (noting that named plaintiffs in putative class actions can protect themselves against the mootness effects of Rule 68 pick-off attempts by filing a motion for class certification when they file their complaint). Some district courts within the Seventh Circuit had previously afforded plaintiffs in proposed class actions a ten-day "safe harbor" after a Rule 68 offer is made to respond with a protective class certification motion, *see, e.g., Western Ry. Devices Corp. v. Lusida Rubber Prods., Inc.*, 2006 WL 1697119, at *2 (N.D. Ill. June 13, 2006), but it is doubtful whether this practice will survive the Seventh Circuit's ruling in *Damasco*.[14]

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[13] *See, e.g., Weiss v. Regal Collections*, 385 F.3d 337, 348 (3d Cir. 2004); *Bond v. Fleet Bank (RI), N.A.*, 2002 WL 373475, at *8 (D.R.I. Feb. 21, 2002); *see also Morgan v. Account Collection Tech., LLC*, 2006 WL 2597865, at *4 (S.D.N.Y. Sept. 5, 2006) ("[T]he district courts in this Circuit are split as to whether a case should be dismissed for lack of subject matter jurisdiction when a Rule 68 offer for full relief to the named plaintiff is made prior to the filing of a motion for class certification or whether the relation back exception should apply to deem the action live.").

[14] The reason these courts chose ten days as the length of the safe harbor is that, for many years, Rule 68 offers remained open for ten days before expiring by their terms. In a 2009 amendment, that time period was expanded to 14 days.

The upshot of this confusion is that class action litigation will become more chaotic. As one district court has pointed out, all of this jockeying for position, with its inevitable emphasis on speed over quality, will "encourage a race to the courthouse between defendants armed with uninformed offers and plaintiffs with underresearched certification motions." *McDowall v. Cogan*, 216 F.R.D. 46, 51 (E.D.N.Y. 2003). In a recent opinion, the Eleventh Circuit also rejected the weight that other courts have placed on the timing of class certification motions in their Rule 68 mootness analysis, observing that filing a motion itself has no jurisdictional significance and that it is the order certifying the class, rather than the motion seeking certification, that changes the nature of the action under Rule 23. *See Stein*, 772 F.3d at 707. In *Stein*, the Court of Appeals concluded that an unaccepted Rule 68 offer cannot render class claims moot before the court rules on class certification, regardless of whether the Rule 68 offer is made before or after the plaintiff moves to certify the class.[15]

The use of Rule 68 to moot the claims of class representatives and, in some instances, the claims of the entire class, is unacceptable for several reasons. First and foremost, treating named plaintiffs in pre-certification class actions the same as plaintiffs in individual lawsuits for purposes of Rule 68 ignores the special status that a litigant takes on by agreeing to represent a class of similarly situated persons. This special status is at the core of the class action device: The proposed class representative stands in the shoes of many others who were affected by the same illegal conduct and represents the interests, and protects the rights, of those absent class members. The certification prerequisites of Rule 23(a), particularly the requirement for adequacy of representation in Rule 23(a)(4), all strive to ensure that the named plaintiff(s) can fulfill this representative role. This means that class representatives are supposed to be more than competent, they are also supposed to be loyal to the rest of the class members. A key part of that is that the class representatives are not supposed to file potential class actions just to make money for themselves, they are supposed to be standing up for everyone else in the class. This requirement of adequate representation by a loyal class representative is required by the U.S. Constitution. Put another way, a named class representative's interest in representing the class is separate from his personal and individual

[15] *See also Mabary v. Home Town Bank, N.A.*, 771 F.3d 820 (5th Cir. 2014) (subscribing to the relation-back approach but holding that the certification order, rather than the certification motion, would relate back to the filing of the complaint, and that if certification was denied, the unaccepted Rule 68 offer would then render the named plaintiff's claims moot); *Pitts v. Terrible Herbst, Inc.*, 653 F.3d 1081 (9th Cir. 2011) (also applying relation back doctrine from an eventual grant of class certification to the filing of the class action complaint); *Lucero v. Bureau of Collection Recovery, Inc.*, 639 F.3d 1239 (10th Cir. 2011) (same).

economic interest; he undertakes both a duty and a right to represent the interests of the class. *See, e.g.*, *Lamberson v. Fin. Crimes Servs., LLC*, 2011 WL 1990450, at *4 (D. Minn. April 13, 2011), citing *Johnson v. U.S. Bank Nat'l Ass'n*, 276 F.R.D. 330, 332 (D. Minn. 2011) ("In a class action complaint, the named plaintiff, as the putative class representative, has a special role of assuming responsibility for the entire class of persons.").

The "divide and conquer" argument that Rule 68 offers can be used to bribe class representatives to sell out the class runs in the face of this basic idea. The argument that is coming up repeatedly is that even if a class representative wants to do the right thing—reject an individual pay day for themselves and insist on standing up for the entire class—Rule 68 strips them of that power, and the court must throw out the whole class.

Even if a Rule 68 offer made before the court rules on class certification is not viewed as mooting class claims, the Rule still exerts inordinate settlement pressure on class representatives—pressure that is inconsistent with the purposes of Rule 23. This is because the recipient of such an offer does not know at the time the offer is made whether a class will ultimately be certified. Thus, instead of weighing the risk of paying the defendant's costs against his likelihood of prevailing at trial for a greater amount than the offer—the risk-benefit analysis that an individual, non-class-representative plaintiff confronted with a Rule 68 offer must make—the plaintiff who is a proposed class representative is "forced to balance his personal liability for costs against the prospects of sharing with the class in any recovery." *Gay v. Waiters'& Dairy Lunchmen's Union, Local No. 30*, 86 F.R.D. 500, 502 (N.D. Cal. 1980). This risk of personal liability should class certification be denied creates a conflict of interest between the class representative and the absent class members who do not face a similar risk, a conflict that creates pressure on the class representative to accept the Rule 68 offer. When this "pick-off" tactic is successful, and the proposed class representative accepts the offer, the claims of the class will in many cases also be extinguished, because at the pre-certification stage the court does not have a defined role in evaluating the fairness of the settlement under Rule 23(e). *See, e.g.*, *Potter v. Norwest Mortg., Inc.*, 329 F.3d 608, 611 (8th Cir. 2003) ("[A] federal court should normally dismiss an action as moot when the named plaintiff settles its individual claim, and the district court has not certified a class."). In short, by setting up an inherent conflict of interest between the risk of individual liability if a Rule 68 offer is rejected and the interests of the class in pursuing the litigation, Rule 68 interferes with the ability of named plaintiffs in putative class actions to carry out their representative role and undermines the entire structure of Rule 23.

This is precisely what the Third Circuit was concerned about when it adopted its relation-back strategy in *Weiss*, noting that "[a]llowing defendants to 'pick off' putative lead plaintiffs contravenes one of the primary purposes of class actions—the aggregation of numerous similar (especially small) claims in a single action." 385 F.3d at 345. Unfortunately, because of the cost-shifting mechanism of Rule 68, the courts cannot prevent at least some pick-off offers to named plaintiffs in class actions from succeeding, especially since in many class actions the amount that any named plaintiff is likely to recover is small. And the dismissal of one putative class action through a successful pick-off offer followed by another putative class action challenging the same conduct in turn contravenes the stated purpose of Rule 68 as it "would invite waste of judicial resources by stimulating successive suits brought by others claiming [the same] aggrievement." *Roper*, 445 U.S. at 339.

There is no clear fix for any of this. Some named plaintiffs in putative class actions have sought to minimize the danger of pre-certification Rule 68 offers by first rejecting and then moving to strike them so that they cannot later be used against the plaintiff for cost-shifting purposes. This strategy has met with mixed success, for as with so much else in the realm of Rule 68 and class actions, the courts are split on how to handle these motions to strike.[16]

In short, not only has Rule 68 failed to fulfil its intended goal of promoting settlement, but it has engendered a host of problems in the class action context and caused widespread confusion and disarray in the courts. We accordingly urge the Subcommittee to simply abrogate the Rule in its entirety.

[16] *Compare Johnson*, 276 F.R.D. 330, 331 (D. Minn. 2011); *Stewart v. Cheek & Zeehandelar, LLP*, 252 F.R.D. 384, 384 (S.D. Ohio 2008), *and Zeigenfuse v. Apex Asset Mgmt., L.L.C.*, 239 F.R.D. 400, 403 (E.D. Pa. 2006) (granting motions to strike), *with White v. Ally Fin. Inc.*, 2012 WL 2994302, at *3-*4 (S.D. W.Va. July 20, 2012) ("With nothing to strike, the issue of whether a Rule 68 offer is appropriate in the context of Rule 23 is not ripe."); *Stovall v. SunTrust Mortg., Inc.*, 2011 WL 4402680, at *5 (D. Md. Sept. 20, 2011) (refusing to "strike a matter that is not a part of the record and indeed cannot properly be admitted to the record except in a proceeding to determine costs"), *and Buechler v. Keyco, Inc.*, 2010 WL 1664226, at *3 (D. Md. Apr. 22, 2010) ("The question whether the rejection of a Rule 68 offer warrants imposition of costs is not ripe until a request for costs is made.").

IV. Rule 23 Should Be Amended to Explicitly Adopt Federal Court Standards for *Cy Pres* Distributions.

Summary:

Using *cy pres* distributions to dispense with class action funds that cannot reasonably be distributed to class members is both well-established and the most appropriate solution to the problem of unclaimed or otherwise undistributable class action funds. Though *cy pres* distributions may have been occasionally misused by counsel and courts (by, for example, authorizing awards that do not adequately further the interests of the class), when used appropriately, *cy pres* distribution is the superior option for dealing with otherwise undistributable funds.

To ensure that *cy pres* distributions continue to be used appropriately, we are proposing that Rule 23 be amended to include a list of factors that courts must consider when evaluating whether to approve a proposed *cy pres* distribution. The factors set forth below are based on the uncontroversial best practices that have already been developed by the leading cases addressing *cy pres*. Although these factors have already been established by caselaw, it bears including them in Rule 23 to eliminate any dispute over the propriety of the use of c*y pres* distributions in class actions.

Proposed Amendment:

Rule 23 should be amended as follows (matters in italics are to be added):

Rule 23(f):

(f) A class action settlement or court order may provide for a cy pres distribution of all or part of the funds recovered for the class in appropriate circumstances, including when the funds remaining after distribution are too small to justify the cost of a further distribution directly to class members and when some or all of the class members cannot be located. In determining the propriety of a cy pres distribution, the court

(1) must consider:

(A) whether, if, in lieu of a cy pres distribution, distributing the funds directly to reasonably identifiable class members in amounts consistent with their damages would be feasible, administratively practicable, and fair;

(B) whether the use of the funds by the proposed cy pres recipient(s) is consistent with the underlying legal claims and the interests of the class members to whom the funds cannot be distributed, and if no such recipient can be identified, whether a distribution of cy pres funds to another recipient would benefit the public interest;

(C) whether the location or geographic service area of the proposed cy pres recipient(s) is consistent with that of the class, or the portion of the class to whom the funds cannot be distributed; and

(D) whether the funds, once distributed to the cy pres recipient(s), will be free from any control by or will be used to benefit the defendant(s).

(2) may consider any other matter pertinent to ensuring that the cy pres distribution is appropriate.

The current Rule 23(f), (g), and (h) would be relettered accordingly.

Analysis:

A. *Cy Pres* Distribution Is Widely Recognized as the Best Approach to Dealing With Class Action Funds that Cannot Reasonably Be Distributed Directly to Class Members.

Cy pres distribution is the court-identified best solution for dealing with the recurring problem of what to do when there is money that has been recovered by class but that cannot reasonably be distributed to individual class members. This problem may occur because the per-class member compensation is too small and the distribution too expensive to directly compensate individual class members at all. But even when there have been robust attempts to distribute funds to class members, there is often money remaining because all the funds were not able to be transferred to all class members—either because not all class members filed claims; not all class members could be identified or found; and/or not all class members cashed their checks, perhaps because they had moved or died. When these "left over" funds are too small for a redistribution to the class, then, too, courts and parties must address what to do with that money.

Cy pres—a term roughly meaning "as near as possible"—has long been the preferred solution of courts to this problem. Courts borrowed the concept of *cy pres* from trust law, where it has been used for centuries to deal with testamentary

gifts or charitable trusts intended for purposes that can no longer be carried out. Examples include instances where the purpose has been achieved (such as a cure being found for a disease); where the organizational recipient no longer exists; and where the purpose has become illegal (such as a trust supporting a racially segregated public space). In such contexts, courts allocate the property to a use "as near as possible" to the original intended recipient or purpose.

In the class action context, the use of *cy pres* distributions to deal with class funds that cannot be distributed to the class is well-established and widespread. Federal courts have been making *cy pres* distributions for more than 40 years. *See, e.g.*, *Miller v. Steinbach*, Fed. Sec. L. Rep. P. 94, 350, 1974 WL 350, at *1 (S.D.N.Y. Jan. 3, 1974). And every federal court of appeals to have encountered the question regards *cy pres* as an appropriate way to dispense with fund recovered by the class where the factors discussed in our proposed amendment to Rule 23 have been satisfied.[17] In those circuits that have not yet weighed in, the district courts nevertheless routinely approve class action settlements that provide for *cy pres* distributions.[18]

A number of treatises have recognized the growing consensus among courts that *cy pres* distribution is the most appropriate tool for dealing with class funds that cannot be distributed to class members. Those treatises have incorporated the court-identified best practices into their texts. *See* 4 Newberg on Class Actions §§ 12:14, :26, :27, :28, :32, :33, :34 (5th ed. 2013); American Law Institute, *Principles of the Law of Aggregate Litigation* § 3.07 (hereinafter "ALI Principles"); National Association of Consumer Advocates, *Standards and*

[17] *In re Lupron Mktg. & Sales Practices Litig.*, 677 F.3d 21 (1st Cir. 2012); *In re Holocaust Victim Assets Litig.*, 424 F.3d 158 (2d Cir. 2005); *In re Baby Products Antitrust Litig.*, 708 F.3d 163 (3d Cir. 2013); *Klier v. Elf Atochem N. Am., Inc.*, 658 F.3d 468 (5th Cir. 2011); *Hughes v. Kore of Ind. Enter., Inc.*, 731 F.3d 672 (7th Cir. 2013); *In re BankAmerica Corp. Secs. Litig.*, 775 F.3d 1060 (8th Cir. 2015); *Lane v. Facebook, Inc.*, 696 F.3d 811 (9th Cir. 2012); *Nelson v. Mead Johnson & Johnson Co.*, 484 Fed. App'x 429 (11th Cir. 2012) (unpublished); *Nelson v. Greater Gadsden Housing Auth.*, 802 F.2d 405 (11th Cir. 1986); *Democratic Cent. Comm. of District of Columbia v. Washington Metro. Area Transit Comm'n*, 84 F.3d 451 (D.C. Cir. 1996).

[18] *See, e.g.*, *Decohen v. Abbasi, LLC*, 299 F.R.D. 469 (D. Md. 2014); *Domonoske v. Bank of Am., N.A.*, 790 F. Supp. 2d 466 (W.D. Va. 2011); *Stinson v. Delta Mgmt. Assocs., Inc.*, 302 F.R.D. 160 (S.D. Ohio 2014); *Lessard v. City of Allen Park*, 470 F. Supp. 2d 781 (E.D. Mich. 2007); *In re Crocs, Inc. Secs. Litig.*, ___F.R.D.___, Fed. Sec. L. Rep. P 89, 2014 WL 4651967 (D. Colo. Sept. 18, 2014); *In re Dep't of Energy Stripper Well Exemption Litig.*, 578 F. Supp. 586 (D. Kan. 1983).

Guidelines for Litigating and Settling Consumer Class Actions, 299 F.R.D. 160, Guideline 7, *Cy Pres* Awards (3d ed. 2014) (hereinafter "NACA Guidelines").[19]

In particular, federal courts and treatises have recognized that, where distribution or redistribution to members of the class is not feasible, *cy pres* distribution is generally superior to the other options for dispensing with class funds: reversion to the defendant and escheat to the state. To begin, well-executed *cy pres* distribution is appropriate because, when directly compensating class members is not feasible, *cy pres* distribution indirectly benefits the class in a way that furthers the purposes of the lawsuit. In other words, it is as close as parties and courts can come to providing individual relief to injured class members, the primary goal of any good-faith class action settlement or judgment. *See Klier*, 658 F.3d at 475; ALI Principles § 3.07 cmt. b.[20]

The other options, meanwhile, bear no connection to the purposes of the lawsuit or to the class members the recovered funds are meant to benefit. Reversion of the funds to the defendant is particularly problematic. First, because the defendant ends up with the money, reversion fails to hold the defendant liable for the illegal conduct giving rise to the suit and fails to deter the illegal conduct sought to be prohibited by the suit's legal basis—two of the core purposes of class actions. *See Hughes*, 731 F.3d at 677 (discussing deterrence); *In re Baby Products*, 708 F.3d at 172 (same); ALI Principles § 3.07 cmt. b. In contrast, *cy pres* "prevent[s] the defendant from walking away from the litigation scot-free because of the infeasibility of distributing the proceeds of the settlement (or of the judgment . . .)." *Hughes*, 731 F.3d at 676.

Second, reversion fails to benefit the class in any way, directly or indirectly. The class fund is meant to compensate the class for its injuries, and it is the compensation that the defendant has been ordered to or pay or has agreed to pay in exchange for settling the case. Reversion takes that compensation—compensation "generated by the value of the class members' claims"—away from the class, whereas *cy pres* distribution uses that compensation to benefit class members, albeit indirectly. *Klier*, 658 F.3d at 474 (class fund proceeds "belong solely to the

[19] "Courts have generally agreed with the ALI Principles[,]" and cite to them frequently. *In re Lupron*, 677 F.3d at 33.

[20] A number of states statutes require courts to dispense with unclaimed class funds in a particular way, such as by a *cy pres* distribution to an organization whose mission relates to the purpose of the lawsuit or to legal aid organizations. *See, e.g.*, Cal. Civ. Proc. Code § 384(d). *See also* Newberg on Class Actions §§ 12:28, :35. If any such state statute applies in federal court, of course it would govern.

class members"); ALI Principles § 3.07 cmt. b (class fund proceeds "are presumptively the property of class members"); NACA Guidelines, 299 F.R.D. 160, Guideline 7.

Third, reversion to the defendant creates perverse incentives to minimize the actual payout to the class. If a defendant knows it will get any funds that are not distributed to class members, it is incentivized to reduce the odds that class members will receive and cash their checks. *See id.* at n.91. For example, a defendant may insist on an overly complex claims process or fabricate reasons why it cannot credit class members' accounts with the amount of their damages. Attentive courts can check this problem to some extent by carefully supervising the distribution process, but a court cannot entirely control what terms parties are and are not willing to agree to in private settlement negotiations.

Escheat to the government is not as counterproductive to class action lawsuits as reversion to the defendant because it still holds the defendant liable and deters illegal conduct. However, it is far less effective at benefitting class members and furthering the law enforcement purposes of a particular lawsuit than *cy pres* distribution. That is because any benefit to the class would be, at best, extremely diffuse and unrelated to the substance of the underlying law at issue in the case. *See In re Baby Products*, 708 F.3d at 172; ALI Principles § 3.07 cmt. b. [21]

For all of these reasons, federal courts have overwhelmingly held that *cy pres* distribution is the superior option for disposing of funds that cannot reasonably be distributed to individual class members.

B. Criticisms of *Cy Pres* as Unconstitutional and Illegal Are Unfounded and Not Endorsed by any Court or Treatise.

Despite the near-universal recognition by federal courts of *cy pres* distribution as an appropriate solution to the problem of dealing with class funds that cannot reasonably be distributed to the class, there are a few outspoken critics who contend that *cy pres* distributions are illegal and unconstitutional. *See, e.g.*, Martin H. Redish et al., *Cy Pres Relief and the Pathologies of the Modern Class Action: A Normative and Empirical Analysis*, 62 Fla. L. Rev. 617 (2010). Putting aside the fact that these concerns largely stem from abuses that the factors proposed here are designed to prevent (see discussion below at Part IV.C), we believe that those views are unfounded.

[21] The constitutional and Rules Enabling Act concerns presented by critics of *cy pres*, discussed *infra*, would apply equally to the option of escheat to the government.

Redish (and a few others) argue that court-distributed *cy pres* violates Article III and the constitutional separation of powers. First, the argument goes, *cy pres* distribution is contrary to the Article III case-or-controversy requirement because it introduces an uninjured party into the litigation (the potential *cy pres* recipient) that lacks any real dispute with either party. In so doing, it is argued, the inclusion of a *cy pres* distribution changes what is supposed to be a bilateral process between two parties with a genuine case or controversy into a trilateral process without any true case or controversy. *See id.* at 641-43. The court then awards "damages" to the uninjured third party, allegedly in contravention of Article III. This award of "damages" (they say) is also contrary to the constitutional separation of powers because it is beyond the scope of the judicial power to transfer money and make charitable donations that are not authorized by substantive law. *Id.*

That *cy pres* distributions are "damages" not authorized by the underlying law is also the basis for the critics' argument that, assuming *cy pres* distribution is consistent with Rule 23, *cy pres* is illegal because it violates the Rules Enabling Act by altering substantive law about available remedies.

We believe that none of these concerns has merit. As members of the defense bar have pointed out, the view that *cy pres* distributions are contrary to Article III's case-or-controversy requirement ignores what actually takes place during the resolution of a class action cases—a process that usually involves settlement. Wilber H. Boies, *et al*., *Class Action Settlement Residue and Cy pres Awards: Emerging Problems and Practical Solutions*, 21 VA. J. SOC. POL'Y & L. 267, 271 (2014). When the parties enter into a settlement that provides for a *cy pres* distribution, the court's role is to review the settlement agreement—including the *cy pres* distribution—for fairness *to the class*. Rule 23(e)(2); *In re Baby Products*, 708 F.3d at 173; *Dennis v. Kellogg Co.*, 697 F.3d 858, 861 (9th Cir. 2012). Whether the *cy pres* distribution takes place as part of a settlement or is court-ordered, the purpose of the distribution is to benefit indirectly ("as near as possible") those class members who cannot benefit directly. In either circumstance, the only interests that matter to the court's analysis are the parties between which there is a dispute—not the interests of the potential *cy pres* recipient(s). The *cy pres* recipients should only be approved if the award would be beneficial *to the class* or its goal in bringing the lawsuit. Because the legal dispute being addressed and resolved is the dispute between the parties, it is only the parties' interests that are taken into consideration in approving a *cy pres* distribution. Therefore, Article III's case-or-controversy requirement is fully satisfied.

No court has adopted the view that the use of *cy pres* distributions violates Article III, and only one federal appellate judge has expressed any concern about potential constitutional problems with *cy pres* distribution. *See Klier*, 658 F.3d at 480-82 (Jones, C.J., concurring) (stating, in dicta, that *cy pres* may present Article III standing issues). And even Judge Jones, despite her concern that a court ordered *cy pres* distribution might be unconstitutional, seems to agree that a settlement agreement between the parties as to how to dispense with the remaining funds should be determinative. *Id.* at 480; Indeed, given the lack of traction that the constitutional argument against *cy pres* distributions has gained in the federal courts, the rhetoric of the academic articles propounding it has been called "the sound of one hand clapping." Boies, *supra*, at 273.

Meanwhile, the argument that *cy pres* is a violation of the constitutional separation of powers and the Rules Enabling Act because it permits courts to award "damages" not authorized by underlying substantive law has already been rejected by federal courts. *See In re Baby Products*, 708 F.3d at 173. And for good reason. First, when the *cy pres* distribution is a result of a settlement agreement, the court's role is to enforce the terms of the agreement between the parties, not to make decisions about what awards might be appropriate under some other substantive law. *Id.* at 173 n.8.

Second, the funds used for *cy pres* distributions are part of the damages that have been awarded *to the class* in accordance with the underlying substantive law. *See* ALI Principles § 3.07 cmt. b. They are not, as some critics have argued, "damages" awarded to the *cy pres recipient*. Rather, as explained above, *cy pres* distribution is a tool for indirectly using the damages to benefit the *class members* who cannot receive them and ensure that the purposes of the underlying substantive law are furthered. Viewed this way, the role of the court in approving *cy pres* distributions is as administrator of the fund recovered by the class—a role in which the court has broad discretion to exercise equitable discretion. Courts have seen the appropriate approval of *cy pres* distributions as being comfortably within that discretion. *See generally Wilson v. Sw. Airlines, Inc.*, 880 F.2d 807 (5th Cir. 1989) (treating *cy pres* as within the court's inherent equitable discretion); *Van Gemert v. Boeing Co.*, 739 F.2d 730, 737 (2d Cir. 1984) (same).

C. To Ensure that *Cy Pres* Awards Are Used Appropriately, Rule 23 Should Include a List of Guiding Factors.

As explained above, *cy pres* distribution is the best option for dealing with undistributed class funds and has been accepted as such by virtually all federal courts. The leading cases and treatises have established a number of factors for

courts to consider when determining whether a particular *cy pres* distribution is appropriate: whether it is reasonable to redistribute funds to identifiable, reachable class members; whether the *cy pres* recipient has a sufficient nexus to the litigation in both subject matter and geography; and whether the defendant retains control over or benefits from the *cy pres* funds. The proposed amendment to Rule 23 seeks to make explicit and uniform those best practices that the courts have already identified and are already applying to proposed class action settlements that come before them.

Despite the overall acceptance of *cy pres* distribution and the factors that ought to be considered in approving *cy pres* distributions, explicitly sanctioning the appropriate use of *cy pres* distributions and articulating those factors remains important. As Chief Justice Roberts has pointed out, the U.S. Supreme Court has never addressed the issue, and there is, as of yet, no binding, national statement regarding *cy pres* distributions—including whether and when they are appropriate. *Marek v. Lane*, 134 S. Ct. 8 (2013) (statement of Roberts, C.J., respecting the denial of certiorari). And as discussed above, regardless of the overall acceptance of *cy pres* distribution in the courts, there are several outspoken critics whose views will continue to fuel litigation about *cy pres* distribution until the matter is definitively closed. Codifying the *cy pres* tool and the best practices for using it would put an end to any remaining uncertainty about *cy pres* distribution, eliminate litigation questioning threshold *cy pres* issues, provide binding guidance to courts in those circuits that have not yet addressed *cy pres* distributions, and, as discussed in detail below, prevent misuses of the *cy pres* tool.

1. Is Distribution or Redistribution Reasonable and Appropriate?

This factor goes to whether any *cy pres* distribution is appropriate, or whether the funds ought to be distributed or redistributed to those members of the class to whom compensation can be gotten. The accompanying note should make clear that where it is feasible to do so, class funds should initially go to members of the class, rather than be part of a *cy pres* distribution. *See In re BankAmerica Corp.*, 2015 WL 110334, at *2; *In re Baby Products*, 708 F.3d at 173; ALI Principles § 3.07(a), (b) & cmt. b. The view that class members have priority over the class funds aligns with the purposes of the class action: It ensures that individuals injured by the defendant's illegal conduct are awarded damages, and it does so in the most direct way possible.

The accompanying note should also make clear that redistribution to class members who already received compensation may be appropriate under some

circumstances even though additional distribution would compensate class members beyond the terms of the original distribution. In practice, class actions, particularly those that end in settlement, rarely compensate class members for 100% of their injuries, and even those that do may not compensate class members for other available remedies, such as treble damages or pain and suffering. *See In re Baby Products*, 708 F.3d at 176 (discussing how the negotiated $5 refund to class members was done in exchange for the release of claims and was not an attempt to fully compensate class members for their injuries); *Klier*, 658 F.3d at 474 ("few settlements award 100 percent of a class member's losses") (quoting ALI Principles § 3.07 cmt. b.).

Finally, this factor means that where it is *not* reasonable to distribute class funds to class members, *cy pres* distributions *are* appropriate, either at the outset or because there is money remaining after one or more rounds of distribution. *See Hughes*, 731 F.3d at 677 (*cy pres*-only settlements may be appropriate because they serve the important deterrent purpose of class actions); NACA Guidelines, 299 F.R.D. 160, Guideline 7. That includes situations in which no distribution to the class is possible because the size of the class is large enough and the fund small enough that the administrative expenses of distribution would effectively swallow the fund or that the amount given to each class member would be so small as to be meaningless. *See, e.g.*, *Hughes*, 731 F.3d at 675 (*cy pres* distribution is likely best solution where maximum liability per class member was $3.57); *Nachshin v. AOL, LLC*, 663 F.3d 1034, 1037, 1039 (9th Cir. 2011) (where maximum liability was $2 million and the class included 66 million individuals, individual distribution was cost-prohibitive and *cy pres* distribution appropriate). Such a situation might arise where a defendant engaged in widespread illegal conduct that only caused de minimus damages to each class member. *See id.*; Boies, *supra*, at 285.

2. Nexus: Is the Award Consistent with the Goal of the Litigation?

This is the first of two factors that go to the question whether the *cy pres* distribution truly is "as near as possible" to the purposes of the underlying lawsuit and whether it will indirectly benefit the class. The two nexus-related factors reflect, among other things, the courts' response to the concern that *cy pres* distributions are abused to reward the favorite charity of the judge, counsel, or party.

The accompanying comments should explain that, in deciding whether to approve a *cy pres* recipient, a court should consider whether the award would further the purposes of the litigation or the enforcement of the underlying

substantive statute or common law. *See, e.g.*, *Dennis*, 697 F.3d at 865; *In re Lupron*, 677 F.3d at 33; *Nachshin*, 663 F.3d at 1038-39; *In re Airline Ticket Comm'n Antitrust Litig.*, 307 F.3d 679, 683 (8th Cir. 2002). *See also Marek*, 134 S. Ct. 8 (presuming that some nexus is required); ALI Principles § 3.07(c) & cmt. b; NACA Guidelines, 299 F.R.D. 160, Guideline 7. For example, the Ninth Circuit held that there was an insufficient nexus between a false advertising claim regarding cereal and a *cy pres* distribution of food to charities that serve food to the indigent. Although the charities' mission was a worthy cause, it did not have anything to do with stopping deceptive advertising. *Dennis*, 697 F.3d at 866-67. Meanwhile, a *cy pres* distribution to the Center for Responsible Lending, which works on consumer credit issues, was appropriate recipient in a Fair Credit Reporting Act case. *Domonoske*, 790 F. Supp. 2d at 471.

As indicated in the proposed amendment to Rule 23 and as the leading treatises have indicated, if, after diligent search, no recipient that furthers the purposes of the litigation or the underlying law can be found, a *cy pres* distribution to a legal services organization or other charity may be appropriate if it is in the public interest to do so. *See* ALI Principles § 3.07(c) & cmt. b.

3. Nexus: Is the Award Consistent with the Geography of the Class?

This is the second factor that goes to the question of whether the *cy pres* distribution indirectly benefits the class and furthers the litigation: whether the *cy pres* distribution reflects the geography of the class. *See, e.g.*, *In re BankAmerica Corp.*, 2015 WL 110334, at *5; *Nachshin*, 663 F.3d at 1040; NACA Guidelines, at 41. Put simply—and as the explanatory note should state—this means that if the class is national in scope, so too should be the *cy pres* distribution. And, likewise, if the class is local, so too should be the *cy pres* distribution. *See Powell v. Ga.-Pac. Corp.*, 119 F.3d 703, 705 (8th Cir. 1997) (in case alleging workplace race discrimination at a single facility, affirming *cy pres* distribution benefitting black residents in the counties where the facility's employees lived). For example, the Ninth Circuit has rejected a *cy pres* distribution to local Los Angeles charities in the context of a nationwide class. *Nachshin*, 663 F.3d at 1040. Meanwhile, the First Circuit approved a *cy pres* recipient which, while located in only one city, conducted research that would potentially benefit the entire nationwide class. *In re Lupron*, 677 F.3d at 36. This factor attempts to ensure that the class members who are not able to be benefited from a direct distribution have the greatest chance of being indirectly benefited by the *cy pres* distribution.

The explanatory note should explain that, as with the purpose nexus, if no geographically matched recipient can be found after a diligent search, *cy pres* distribution may still be appropriate.

4. Does the Defendant Benefit from or Control the Funds?

This factor is a result of the concern that *cy pres* distributions may be used to disguise what is really a reversion to the defendant. For the reasons discussed above—that reversion fails to hold the defendant responsible for its illegal conduct and fails to deliver any compensation to class members—reversion is an inappropriate method for dealing with the problem of class funds that cannot be directly distributed to class members. Class funds are property of the class, awarded as compensation for their injuries, and the defendant should not control how that property is ultimately used.

Sometimes, this is clear on the face of the *cy pres* distirbution, for example, where the fund is used to create a charity that would have unfettered discretion to award money and would be controlled by a senior employee of the defendant. *Marek v. Lane*, 134 S. Ct. 8 (2013) (statement of Roberts, C.J., respecting the denial of certiorari). In other situations, defendants might use *cy pres* distributions in place of charitable donations they would otherwise be obligated to make—a situation that benefits the defendant, not the class. *See* NACA Guidelines, at 44. *See also Klier*, 658 F.3d at 473 (defendant proposed a *cy pres* recipient—a scholarship fund—that bore the name of the defendant). Such awards are an inappropriate use of funds that are meant to benefit the class members.

# # #

These factors represent the court-articulated best practices for *cy pres* distribution—practices designed to ensure that the class will benefit from the class fund and to prevent counsel and judges from simply giving money to their preferred charities.

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