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Class Action Settlements and Attorneys' Fees

Recent decisions suggest that appellate courts are closely scrutinizing attorneys' fee provisions and awards in proposed class action settlement agreements, even where the district court has approved both. Counsel negotiating these agreements must anticipate potential red flags to minimize objections from absent class members and ensure that the agreements survive judicial review.

DAVID S. ALMEIDA
PARTNER
SHEPPARD, MULLIN, RICHTER & HAMPTON LLP

David focuses his nationwide practice on navigating clients through class action lawsuits, complex business litigation, and regulatory investigations across a variety of industry sectors, including telecommunications, marketing and advertising, hospitality, and healthcare. He is widely recognized as an expert in consumer fraud and privacy class action defense and co-leads the firm's Class Action Defense and Telephone Consumer Protection Act practices.

PAUL SEELEY
ASSOCIATE
SHEPPARD, MULLIN, RICHTER & HAMPTON LLP

Paul has experience in a broad range of business litigation matters, including consumer class actions, products liability, insurance litigation, and real estate disputes. He has represented clients in litigations involving California's consumer protection statutes, shareholder actions, and commercial contract disputes.

MARK S. EISEN
ASSOCIATE
SHEPPARD, MULLIN, RICHTER & HAMPTON LLP

Mark focuses his practice on defending companies against class and individual actions brought under various state and federal privacy and consumer protection statutes, as well as other consumer privacy and unfair business practices laws and regulations.

There recently has been a surge of challenges to attorneys' fees sought and awarded in connection with proposed class action settlement agreements. Absent class members often object to these fee awards, arguing that they will receive only a small benefit from the settlement while the attorneys generate millions of dollars in fees. Further, because class counsel and the defendant negotiate the settlement agreement, including the provision for fees, the incentives weigh in favor of settling quickly rather than parsing the relationship of the fees to total class recovery.

Recognizing this potential for abuse, appellate courts are closely scrutinizing attorneys' fee provisions and awards in proposed class action settlement agreements, even where the district court has approved both. Several recent cases from the US Circuit Courts of Appeals provide critical insights for counsel negotiating class action attorneys' fee awards. Class counsel and defendants are equally invested in ensuring that a mutually agreed settlement secures approval from the district court and, ultimately, survives appellate review.

Against this backdrop, this article explores:

- The key rules and procedures for obtaining district court approval of a class action settlement agreement and an attorneys' fee award.
- The two main methods used to calculate attorneys' fees.
- The required content of a motion for attorneys' fees accompanying a class action settlement proposal.
- The standard of review an appellate court applies to attorneys' fees awarded in a class action settlement.
- Special considerations for counsel seeking attorneys' fees in a coupon settlement under the Class Action Fairness Act of 2005 (CAFA).
- Best practices for counsel when negotiating and moving for attorneys' fees as part of a class action settlement.

Search Class Action Toolkit for a collection of resources to assist counsel with class action procedure, requirements, and practice in federal court.

DISTRICT COURT APPROVAL PROCESS

Like other settlements, class action settlement agreements include provisions for substantive relief to the plaintiffs in exchange for terminating the action. Unlike settlements in individual litigation, however, the Federal Rules of Civil Procedure (FRCP) specifically authorize the court to award attorneys' fees in a certified class action, and require the court to scrutinize every provision of a class action settlement agreement (FRCP 23(h)). As a result, class action settlement agreements include provisions for fees to be paid to class counsel. Therefore, there are two driving factors in class action settlements: relief to the class and attorneys' fees. These provisions, like all others, must be approved by the court, which must hold a hearing to determine whether the agreement as a whole is "fair, reasonable, and adequate" (FRCP 23(e)(2)).

While the FRCP provide for three separate types of class actions, including those that seek injunctive relief only, class actions for monetary relief seeking certification under FRCP 23(b)(3) are the most common. Because unnamed class members in Rule 23(b)(3) actions do not participate in negotiating the settlement agreement, but will be bound by it and will release any damages claims they might have, a class member has a right to object to the proposed settlement, including the requested attorneys' fees, if he believes the agreement does not meet the fairness standard (FRCP 23(e)(5)). Therefore, even where class counsel and the defendant have agreed to certain fee provisions, unnamed class members may seek to challenge and undo this agreement.

Given that attorneys' fee awards often give class members and the court cause to object, class counsel must make an independent motion for attorneys' fees ahead of the deadline to object (FRCP 23(h)(1)). These important checks are meant to safeguard against class counsel and defendants seeking only to maximize their own interests without sufficient regard to the interests of unnamed class members (see *Box, The Mixed Incentives Underlying Class Action Settlements*).

At the final fairness hearing, the district court often combines hearing any objections to the proposed settlement generally with the motion for the specific fee award (see FRCP 23(h)(3); Manual for Complex Litigation, Fourth, § 21.726). It is possible that the court could approve the substance of the agreement, but deny specific requests for attorneys' fees or even award significantly less in attorneys' fees (see, for example, *Fujiwara v. Sushi Yasuda Ltd.*, 58 F. Supp. 3d 424, 439 (S.D.N.Y. 2014) (approving settlement agreement but modifying class counsel's proposed fee claim)).

Search What's Market: Process of Settling Class Actions and What's Market: Objections in Class Action Settlements for more on the settlement approval process.

Search Settling Class Actions: Process and Procedure for more on issues to consider when settling a class action.

ATTORNEYS' FEE CALCULATION METHODS

Determining the method for calculating attorneys' fees is an integral part of many class action settlements. There are two generally acceptable methods:

- The percentage of recovery method.
- The lodestar method.

It is important for both class counsel and defendants to understand the implications of each method.

District courts generally have discretion to use either method, so long as the resulting award is reasonable. However, some circuit courts have recognized that one method may be more appropriate than the other in certain types of cases. (See, for example, *In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d 935, 941-43 (9th Cir. 2011) (observing that the lodestar method "is appropriate in class actions brought under fee-shifting statutes ... where the relief sought—and obtained—is often

primarily injunctive in nature and thus not easily monetized"); *Pickett v. Sheridan Health Care Ctr.*, 664 F.3d 632, 639 (7th Cir. 2011) (noting that district courts should use the lodestar method to determine a reasonable fee for prevailing parties in an action brought under Title VII of the Civil Rights Act of 1964).) Indeed, the US Courts of Appeals for the Eleventh and DC Circuits require district courts to use the percentage of recovery method in common fund cases (see *Camden I Condo. Ass'n, Inc. v. Dunkle*, 946 F.2d 768, 774 (11th Cir. 1991); *Swedish Hosp. Corp. v. Shalala*, 1 F.3d 1261, 1271 (D.C. Cir. 1993)).

Similarly, the US Court of Appeals for the Seventh Circuit recently suggested in dicta that the lodestar method, in a vacuum, might be inappropriate in consumer class actions where the settlement produces a quantifiable class benefit because the named plaintiff has little incentive to negotiate a billing rate, monitor the attorney's time expenditures, or control any aspect of the litigation (see *Redman v. RadioShack Corp.*, 768 F.3d 622, 635 (7th Cir. 2014), cert. denied sub nom. *Nicaj v. Shoe Carnival, Inc.*, 135 S. Ct. 1429 (2015) (noting that permitting the hours class counsel worked to control the fee was inappropriate because class counsel could therefore "shift the entire risk of the litigation to their clients" when it was class counsel who misjudged the monetary value of the case when they filed the action)).

Moreover, many circuit courts have recognized that even where a district court might use one method initially, the court should consider using the other method as a cross-check to avoid an excessive fee award (see, for example, *Bezdek v. Vibram USA, Inc.*, 2015 WL 9583769, at *5 (1st Cir. Dec. 31, 2015); *Kirsch v. Delta Dental of N.J.*, 534 F. App'x 113, 117 (3d Cir. 2013); *Union Asset Mgmt. Holding A.G. v. Dell, Inc.*, 669 F.3d 632, 644 (5th Cir. 2012); *In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 944; *Goldberger v. Integrated Res., Inc.*, 209 F.3d 43, 50 (2d Cir. 2000); *Bowling v. Pfizer, Inc.*, 102 F.3d 777, 780 (6th Cir. 1996)).

Search Class Action Settlement Agreement for a sample agreement containing a model provision governing attorneys' fees and costs, with explanatory notes and drafting tips.

PERCENTAGE OF RECOVERY METHOD

Under the percentage of recovery method, class counsel collects a percentage of the overall class recovery (known as the common fund). The court can then adjust the percentage up or down depending on the circumstances. Many courts applying this method will start with an assumption that 25% of a common fund is reasonable, and permit special circumstances to justify adjustments to that amount (see, for example, *In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 942 ("where awarding 25% of a 'megafund' would yield windfall profits for class counsel in light of the hours spent on the case, courts should adjust the benchmark percentage or employ the lodestar method instead"); *In re IndyMac Mortg.-Backed Sec. Litig.*, 94 F. Supp. 3d 517, 522-25 (S.D.N.Y. 2015) (finding 13% of the common fund (amounting to $44.89 million) to be unreasonably high in a large-recovery securities litigation)).

A critical and sometimes controversial aspect of the percentage of recovery method is quantifying the benefit received by the class under the settlement agreement. Although courts often use a 25% benchmark, defining the proper funds from which class counsel can collect this 25% varies based on the jurisdiction.

For example, whether to include administrative costs in the total common fund value has been the subject of some debate. Providing notice to class members can be difficult and costly, particularly in consumer class actions involving low-cost products. Additionally, these cases often require claims administrators to manage the receipt, payment, or denial of claims. These administrative processes can be expensive and time-consuming, and their attendant costs tend to represent a substantial portion of the defendant's total settlement payment. Whether to include these costs in a common fund value has long been a point of contention because neither class members nor class counsel can benefit from a settlement without incurring notice and administration costs.

Class counsel might prefer to include these costs in the total common fund value because it will increase the fee awarded as a percentage of the fund. This larger fund amount, however, is not necessarily connected to the relief the class actually receives. Courts differ on what should count as a benefit from which class counsel can collect their percentage. (Compare *Redman*, 768 F.3d at 630 (finding that the roughly $2.2 million in administrative costs should not have been included in calculating the total recovery amount, and the reasonableness of class counsel's fee award should be based on the money that was actually paid to the class) with *In re Online DVD-Rental Antitrust Litig.*, 779 F.3d 934, 953 (9th Cir. 2015) (permitting the attorneys' fee award to be calculated as a percentage of the total amount the defendant paid to settle the case, including notice costs and administrative expenses).)

A similar issue exists regarding whether *cy pres* awards should be included in the settlement fund for percentage of recovery purposes. Although these amounts have historically been included, recent decisions are casting doubts on this practice and suggesting that these provisions should be more closely scrutinized by the court (see, for example, *In re Baby Prods. Antitrust Litig.*, 708 F.3d 163, 173 (3d Cir. 2013); *Pearson v. NBTY, Inc.*, 772 F.3d 778, 781 (7th Cir. 2014)).

Counsel negotiating class action settlement agreements should carefully consider whether the applicable circuit court views administrative costs and *cy pres* awards as part of the class benefit. Depending on the jurisdiction, class counsel might need to accept a reduction in their fees or demand a higher settlement payment from the defendant to compensate for the difference, so that the overall agreement and fee request are approved. In many cases, the parties might decline to agree on a fee award in advance and simply litigate the issue before the court.

LODESTAR METHOD

The lodestar method attempts to calculate a reasonable fee by multiplying the time class counsel worked on the case by an appropriate hourly fee for those hours, based on counsel's

The Mixed Incentives Underlying Class Action Settlements

Class actions often involve a representative plaintiff seeking compensation on behalf of hundreds, thousands, or even millions of class members. For example, consumer class actions often involve an individual plaintiff who purchased a mass-produced, low-cost product seeking compensation on behalf of herself and all other purchasers of that same product. Relying on state-based consumer protection and false advertising laws, these plaintiffs may allege class-wide economic harm based on a single purportedly false statement on a product label or an advertisement and, therefore, every consumer in the class is entitled to some refund from the defendant. Even for low-cost products, the sheer volume of potential class members can generate tens of millions of dollars in potential liability.

Counsel representing the named plaintiff and class in consumer class actions typically work on a contingency fee basis, advancing the costs of the lawsuit, including expert witness and class notice fees, and receiving payment only if there is recovery on behalf of the class. In this situation, counsel might favor settlement because it allows counsel to negotiate a method for calculating their fees that will cover the costs of the litigation and justify the amount of time spent on the case. However, this focus on fee recovery can often misalign class counsel's incentives and the interests of the class they represent.

In these types of class actions, a named plaintiff incurs relatively little expense and burden in bringing the litigation because his attorneys are working on a contingency fee basis. Additionally, aside from a few documents and a deposition, he typically has little, if any, discovery to provide. Further, the named plaintiff might receive an individual incentive award as part of a settlement, over and above what the unnamed class members would receive under the same agreement. As a result, the named plaintiff has limited interest in the case and the amount the class recovers, let alone in limiting his attorneys' recovery to a particular percentage of the class recovery, so long as he is compensated for his involvement.

Defendants typically seek to mitigate the risks of a consumer class action by containing it as much as possible. Using the same example as above, because an allegedly falsely advertised or marketed product is typically sold in multiple states, there is significant exposure and a heightened risk of copycat cases raising similar claims against the defendant in different jurisdictions. A global settlement that brings in most potential plaintiffs in exchange for a one-time payment can help contain the defendant's liability and eliminate the inherent uncertainty in proceeding through the litigation process. Most defendants are therefore incentivized to negotiate a common fund settlement, in which the company knows the total amount for which it might be responsible. However, defendants generally have little interest in how that settlement amount

geographic region and level of experience (in some instances, the court may remove items, such as travel and meal costs, when calculating the lodestar amount). The resulting amount usually is presumptively reasonable, but the court may consider any number of factors to adjust the lodestar amount up or down.

The primary concern is that the amount awarded should be reasonable in relation to the benefits obtained for the class (see *In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 942 (citing *Hensley v. Eckerhart*, 461 U.S. 424, 434-36 (1983))). Moreover, the court may consider the overall reasonableness of the hours and rates billed (see *In re Weatherford Int'l Sec. Litig.*, 2015 WL 127847, at *1 (S.D.N.Y. Jan. 5, 2015) ("While the Court assumes that over 30,000 hours of time were recorded, it has serious doubts—based in part on 24 years in practice ... and more than 20 years on the bench, as well as the evidence submitted—whether this case, handled efficiently and especially for a paying client, would have justified an expenditure of hours that great.")). When evaluating the lodestar amount, courts consider a variety of factors, including:

- The quality of the representation.
- The complexity and novelty of the issues presented.
- The risk of nonpayment.

(See *In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 941-42; see also *Union Asset Mgmt. Holding A.G.*, 669 F.3d at 642 & n.25 (listing additional factors, such as fee awards in similar cases and the time and labor required, a district court may consider when analyzing fee requests).)

MOTION FOR ATTORNEYS' FEES

Where the parties agree to the provision of attorneys' fees in the class action settlement agreement, class counsel also must make a motion to the court for the specific amount of fees sought (see above *District Court Approval Process*). The motion must identify:

- The legal basis for the fee claim.
- The amount sought, along with supporting documentation.
- The terms of any agreement concerning the fees sought.

(FRCP 54(d)(2)(B).)

A claim for attorneys' fees must be made under FRCP 54(d)(2) at a time the court sets (FRCP 23(h)(1)). In most cases, the deadline to object to a motion for attorneys' fees is the same as the deadline to object to the settlement generally. A court might view counsel's attempt to move for fees after the deadline to object to the settlement as a whole has passed as improper (see FRCP 23(e)(5); see also *Redman*, 768 F.3d at 638 (noting that there was "no excuse for permitting so irregular, indeed unlawful, a procedure" for class members to object to a fee

is apportioned between the class and its counsel, apart from ensuring the settlement passes judicial scrutiny.

This dynamic raises a substantial risk that class counsel will structure a settlement that offers counsel a high fee award and inures predominantly to counsel's benefit at the expense of absent class members, who will receive little monetary compensation in return for forgoing their rights to pursue future litigation against the defendant. As various appellate courts have observed:

- "[C]lass counsel, in complicity with the defendant's counsel, [are incentivized] to sell out the class by agreeing with the defendant to recommend that the judge approve a settlement involving a meager recovery for the class but generous compensation for the lawyers—the deal that promotes the self-interest of both class counsel and the defendant and is therefore optimal from the standpoint of their private interests" (*Eubank v. Pella Corp.*, 753 F.3d 718, 720 (7th Cir. 2014)).
- "The relief that this settlement provides to unnamed class members is illusory. But one fact about this settlement is concrete and indisputable: $2.73 million [in attorneys' fees] is $2.73 million." (*In re Dry Max Pampers Litig.*, 724 F.3d 713, 721 (6th Cir. 2013).)
- "Collusion may not always be evident on the face of a settlement, and courts therefore must be particularly vigilant not only for explicit collusion, but also for more subtle signs that class counsel have allowed pursuit of their own self-interests and that of certain class members to infect the negotiations" (*In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 947).
- The "unique relationship among plaintiffs' counsel, plaintiffs, and defendants in class actions imposes a special responsibility upon appellate courts to hear challenges to fee awards by class members whose claims may have been reduced or in some way affected in exchange for large fee awards" (*In re Cendant Corp. PRIDES Litig.*, 243 F.3d 722, 728 (3d Cir. 2001)).
- "Defendants, once the settlement amount has been agreed to, have little interest in how it is distributed and thus no incentive to oppose the fee. ... And the class members—the intended beneficiaries of the suit—rarely object. ... Why should they? They have no real incentive to mount a challenge that would result in only a 'minuscule' *pro rata* gain from a fee reduction. ... All these considerations have fed the perception among both commentators and the Congress that plaintiffs in common fund cases are mere 'figureheads,' and that the real reason for bringing such actions is 'the quest for attorney's fees.'" (*Goldberger*, 209 F.3d at 52-53.)

petition where information about the work counsel performed was submitted after the deadline to object to the settlement had passed); *Allen v. Bedolla*, 787 F.3d 1218, 1225 (9th Cir. 2015) (noting that FRCP 23(h) requires the deadline for objections to counsel's fee request to be a date after the motion and documents supporting it have been filed)).

LEGAL BASIS FOR CLAIM

FRCP 23(h) does not provide an independent authority for courts to award attorneys' fees. Instead, the rule only provides the process a court must follow when a fee award is authorized either by:

- The substantive law.
- An agreement between the parties.

(FRCP 23(h).)

The substantive law might provide for fees where a fee-shifting statute applies in a case, for example, where a statute allows for the recovery of fees by a "prevailing party." However, in class action settlements, the legal basis for the fee award usually is based on the parties' provision for fees in the settlement agreement.

AMOUNT OF CLAIM

As discussed above, the parties may specify a method for calculating attorneys' fees in the settlement agreement. In the corresponding motion for fees, counsel must submit the actual amount of the claim sought.

While the district court determines the propriety of the ultimate amount awarded to class counsel, the court may delegate to a magistrate judge or special master the specific task of calculating the fee award. Indeed, because appellate courts are taking an increasingly active role in reviewing settlement agreements and class counsel fees, counsel should consider seeking a neutral analysis from an expert on the value of a settlement to better position the settlement for approval. (See Federal Rule of Evidence 706; *Pearson*, 772 F.3d at 781-82 (suggesting that neutral expert testimony would have been useful to analyze the reasonableness of class counsel's billing rates); see also *Redman*, 768 F.3d at 631 (suggesting that neutral expert testimony could have assisted in determining the true economic value of the vouchers offered to class members under the settlement).)

Class counsel should keep accurate and contemporaneous time records to use as part of its submission, accompanied by an affidavit from class counsel. This is essential regardless of whether the fee is based on a lodestar or percentage of recovery method, in part because courts often cross-check the amount calculated under each method against each other. (See Manual for Complex Litigation, Fourth §§ 14.213, 21.724.)

Additionally, class counsel might consider submitting exhibits to its motion for attorneys' fees and costs affidavits or declarations from other attorneys practicing in the relevant jurisdiction testifying as to the reasonableness of the hourly rate, the amount of time spent, and the requested fees.

Finally, as with any motion, the motion for attorneys' fees may be accompanied by a memorandum of law in which counsel sets out the reasons supporting the request and method of calculation.

RELATED AGREEMENTS

Class counsel's motion should identify "the terms of any agreement about fees for the services for which the claim is made" (FRCP 54(d)(2)(B)(iv); see FRCP 23(e) (requiring the parties to file a statement "identifying any agreement made in connection with" the proposed class action settlement)). These agreements might include, for example, an agreement between the defendant and class counsel providing that the defendant will not contest class counsel's fee claim or a certain portion of it (known as a "clear sailing" provision) (see below *Best Practices*) or that someone other than the defendant is contributing to the settlement payment. This disclosure also should include any retainer agreements between class counsel and a named plaintiff.

In rare cases, class counsel and a named plaintiff will, at the outset of a litigation, negotiate an attorneys' fees schedule or a specific calculation method to be applied, as part of a retainer agreement (see, for example, *In re Synthroid Mktg. Litig.*, 264 F.3d 712, 719 (7th Cir. 2001); *In re Cardinal Health Inc. Sec. Litigs.*, 528 F. Supp. 2d 752, 758 (S.D. Ohio 2007); but see *Vizcaino v. Microsoft Corp.*, 290 F.3d 1043, 1050 (9th Cir. 2002) (declining to attempt to estimate the terms of the contract that private plaintiffs would have negotiated with their counsel had bargaining occurred at the outset of the case)). In these cases, courts may view the *ex ante* fee agreements as presumptively reasonable (see, for example, *In re Cendant Corp. Litig.*, 264 F.3d 201, 282 (3d Cir. 2001) (*ex ante* fee agreement between class counsel and lead plaintiff in case brought under the Private Securities Litigation Reform Act was presumptively reasonable)).

The Seventh Circuit instructs district courts to assign fees that "mimic a hypothetical *ex ante* bargain between the class and its attorneys." District courts should base the award on relevant market rates and the *ex ante* risk of non-payment by looking at "actual fee contracts that were privately negotiated for similar litigation, information from other cases, and data from class-counsel auctions." (*Williams v. Rohm & Haas Pension Plan*, 658 F.3d 629, 635-36 (7th Cir. 2011).)

However, although many cases recognize the prudence of encouraging class counsel to negotiate fees at the outset of a case, the practice remains relatively rare outside of the Seventh Circuit.

APPELLATE REVIEW

If the district court overrules objections to a fee award (or another aspect of the settlement) made by a class member or a party from whom payment is sought, the objecting party may be able to appeal this decision separate and apart from the underlying disposition of the class action (*Knisley v. Network Assocs., Inc.*, 312 F.3d 1123, 1126 (9th Cir. 2002); *In re Cendant Corp. PRIDES Litig.*, 243 F.3d at 726; but see *In re Diet Drugs Prods. Liab. Litig.*, 401 F.3d 143, 156 (3d Cir. 2005) (holding that an interim fee award was not an appealable final order where the order applied to, and the fee was based on, three intermingled common funds, only one of which had been exhausted)).

> Where the class recovery and attorneys' fees are paid from the same fund, class members generally have standing to appeal the fee award even if they do not appeal approval of the underlying settlement agreement.

STANDING TO APPEAL FEE AWARD

Like other types of appeals, the ability to appeal an attorneys' fee award in a class action depends on whether or not the party seeking to appeal has been aggrieved by the award and therefore has standing to bring the challenge. For example, where the class recovery and attorneys' fees are paid from the same fund, class members generally have standing to appeal the fee award even if they do not appeal approval of the underlying settlement agreement (see *Glasser v. Volkswagen of America, Inc.*, 645 F.3d 1084, 1088 (9th Cir. 2011)). A class member who does not object to the settlement proposal in the district court, however, cannot appeal later approval of the settlement (*In re UnitedHealth Grp. Inc. S'holder Derivative Litig.*, 631 F.3d 913, 917 (8th Cir. 2011); *In re Integra Realty Res., Inc.*, 354 F.3d 1246, 1257-58 (10th Cir. 2004)). Moreover, an objecting party may only appeal issues to which it actually objected (*Devlin v. Scardelletti*, 536 U.S. 1, 9 (2002)).

Where the defendant agrees to pay class counsel's fees independent of the underlying remedy, and there is no evidence of collusion in the fee request, objecting class members may not have standing to appeal because they are not directly aggrieved by the fee award (compare *Glasser*, 645 F.3d at 1088-89 with *In re Cendant Corp. PRIDES Litig.*, 243 F.3d at 728-30).

Search Class Actions: Appeals for more on standing to appeal attorneys' fee awards in class actions.

ABUSE OF DISCRETION STANDARD OF REVIEW

As with review of the underlying settlement agreement, an appellate court reviews the district court's attorneys' fee award for abuse of discretion. This discretion includes the district court's selected method to determine the fees awarded. (See, for example, *Williams*, 658 F.3d at 634; *In re Mercury Interactive Corp. Sec. Litig.*, 618 F.3d 988, 992 (9th Cir. 2010); *Bowling*, 102 F.3d at 779-80.)

Several circuit courts have demonstrated an increased willingness to carefully scrutinize attorneys' fee awards to ensure that the named plaintiffs and class counsel, when negotiating with the defendant, have upheld their fiduciary responsibilities to absent class members. These appellate courts have found that a district court abused its discretion by approving a fee award where:

- The district court failed to make explicit calculations under the selected method (*In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 943).
- The district court failed to conduct a cross-check of the lodestar and percentage of recovery methods to ensure that the fees calculated were reasonable (*In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 945).
- The district court failed to make a record of either the level of success class counsel achieved or the value of injunctive relief obtained for the class (*In re Bluetooth Headset Prods. Liab. Litig.*, 654 F.3d at 944).
- There were impermissible conflicts of interest between class counsel and a named plaintiff that, while apparent to the district court, were not disclosed to absent class members (*Eubank*, 753 F.3d at 723-24).
- The fee was based on an inflated value of the amount the class might recover, following a complicated and lengthy claims process seemingly designed to discourage class members from filing claims (*Eubank*, 753 F.3d at 724-25; see also *Pearson*, 772 F.3d at 781, 783).
- The fee was based on a percentage of a common fund that:
  - included substantial administrative costs; and
  - significantly overvalued the class recovery by treating store vouchers' face value as their true economic value.

  (*Redman*, 768 F.3d at 630-31.)
- The settlement agreement provided that any reduction of fees to class counsel reverted to the defendant, rather than to the class, a so-called "kicker" clause (*Eubank*, 753 F.3d at 723; *Pearson*, 772 F.3d at 786-87) (see below *Best Practices*).
- The value of the "medley of injunctive relief" awarded to class members bore no relationship to the multi-million dollar fee award, particularly where counsel did not take a single deposition, serve a single request for written discovery, or file a response to the defendant's motion to dismiss (*In re Dry Max Pampers Litig.*, 724 F.3d at 718).
- The objection period closed before class counsel filed their petition for attorneys' fees (*Redman*, 768 F.3d at 638).

ATTORNEYS' FEES UNDER CAFA

Before CAFA was passed in 2005, defendants settled many consumer class actions by issuing coupons to the class, such as by offering $10 off of a $40 purchase of the defendant's products. These coupons were of limited value, were not transferable, and generally benefitted the defendant, either because class members spent more on the defendant's products by using the coupons or they did not redeem the coupons at all. However, class counsel negotiating these coupon settlements typically received generous fee awards, creating the appearance that class counsel compromised the class to benefit themselves. CAFA was passed, in part, to regulate how attorneys' fees are calculated in coupon settlements. (See S. Rep. 109-14, at 4-5 (2005), reprinted in 2005 U.S.C.C.A.N. 3, 6-7.)

While the statute purports to regulate the attorneys' fees that class counsel may collect in a coupon settlement, the ambiguity of some of CAFA's fee provisions have led to splits in authority on issues involving, for example:

- Whether a voucher or gift card constitutes a coupon for purposes of bringing the case under CAFA's governance.
- If a settlement is deemed to include coupons under CAFA, what methods can be used to appropriately calculate class counsel's fees.

NON-CASH VOUCHERS AND GIFT CARDS

Although Congress did not define the term "coupon" in CAFA, a coupon settlement generally is one that provides benefits to class members in the form of a discount towards the future purchase of a product or service offered by the defendant (see *Chakejian v. Equifax Info. Servs., LLC*, 275 F.R.D. 201, 215 n.17 (E.D. Pa. 2011)). However, what exactly falls within this general definition, for example, whether a voucher, gift card, or other non-cash award constitutes a coupon, is an important threshold question for counsel because of the constraints CAFA places on the fees associated with coupon settlements (28 U.S.C. § 1712; see *Radosti v. Envision EMI, LLC*, 717 F. Supp. 2d 37, 54-55 n.16 (D.D.C. 2010)).

The Seventh Circuit recently took a detailed look at what qualifies as a coupon. In *Redman*, the settlement agreement called for class members to receive a $10 voucher that could be used in any RadioShack store, and for class counsel's fee award to be calculated based on a class benefit of $10 per class member. Class counsel argued that these vouchers were not "coupons" because they could be used to purchase an entire product. In rejecting this argument, the court noted that:

- Class members likely would apply the vouchers, like coupons, toward larger purchases.

Even under the abuse of discretion standard, a circuit court might second-guess a district court's determination on whether an attorneys' fee award is reasonable under the circumstances and closely examine whether class counsel benefits from a settlement at the expense of the class.

- The actual buying power of the vouchers was questionable, because the majority of items actively advertised and sold by RadioShack cost more than $10.
- Numerous restrictions on the vouchers, namely their inability to be used anywhere but RadioShack, their short expiration date, and the limit of three per transaction, suggested that the true economic value of the vouchers was less than $10.

(768 F.3d at 628, 635-37; see also *In re Southwest Airlines Voucher Litig.*, 799 F.3d 701, 706 (7th Cir. 2015) ("We have rejected a narrow definition of 'coupon' by rejecting, for purposes of § 1712, a proposed distinction between 'vouchers' (good for an entire product) and 'coupons' (good for price discounts)").)

Moreover, in *Tyler v. Michaels Stores, Inc.*, a district court examined conflicting authority from the Seventh Circuit and Ninth Circuit on what constitutes a coupon. The court held that the $10 to $25 store non-cash vouchers offered to class members under the settlement constituted coupons for CAFA purposes because the vouchers had "no value to class members unless they transact additional business" with the defendant. In reaching this conclusion, the court declined to follow either the Seventh Circuit's broader definition of coupon or the Ninth Circuit's stricter definition, which excluded gift cards so long as they:

- Were freely transferable.
- Did not require consumers to spend their own money.
- Were of a sufficient amount for class members to buy a variety of items at the defendant's store.

(2015 WL 8484421, at *1, *4 (D. Mass. Dec. 9, 2015) (suggesting that the Ninth Circuit's approach ignored that "the key distinction driving CAFA's skepticism towards coupon payments ... [was] between coupons and cash, not between coupons and gift cards").)

Search Class Action Fairness Act of 2005 (CAFA): Overview for more on CAFA, including information on CAFA's requirements for class action settlements.

ATTORNEYS' FEE CALCULATIONS IN COUPON SETTLEMENTS

If a class action settlement has been determined to include coupons as part or all of the recovery, CAFA specifies the following limits on the potential attorneys' fees class counsel can obtain:

- **Contingency fee awards.** The portion of any fee award that is attributable to the award of the coupons must be based on the value to class members of the coupons that are actually redeemed (28 U.S.C. § 1712(a)). The Ninth Circuit has interpreted this rule to mean that where attorneys' fees are awarded on a contingent basis in a settlement providing only coupon relief, the amount of those fees must be based solely on the redemption value of the coupons (*In re HP Inkjet Printer Litig.*, 716 F.3d 1173, 1181-82 (9th Cir. 2013)). By contrast, the Seventh Circuit has held that this rule does not expressly prohibit use of the lodestar method for coupon settlements (*In re Southwest Airlines Voucher Litig.*, 799 F.3d at 707-708).
- **Other fee awards.** If a portion of the recovery of the coupons is not used to determine the fees to be paid to class counsel, any fee award must be based on the amount of time class counsel reasonably expended working on the action (28 U.S.C. § 1712(b)). This provision permits counsel to use the lodestar method when calculating attorneys' fees (to the extent they are not contingent on coupon relief).
- **Mixed fee awards for coupon settlements with equitable relief.** If the proposed settlement provides for an award of coupons to class members and also provides for equitable relief, including injunctive relief:
  - the portion of the fee award based on a portion of the recovery of the coupons must be calculated in accordance with 28 U.S.C. § 1712(a); and
  - the portion of the fee award not based on a portion of the recovery of the coupons must be calculated in accordance with 28 U.S.C. § 1712(b).

  (28 U.S.C. § 1712(c).) There is a split in authority regarding whether these rules allow for the lodestar method to be used to compensate class counsel for the coupon relief obtained for the class where a settlement provides for coupon and equitable relief (compare *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 710 (giving the district court discretion to use the lodestar method for calculating the entire fee award) with *In re HP Inkjet Printer Litig.*, 716 F.3d at 1183-85 (requiring the district court to use the value of the coupons redeemed when

determining the portion of the fee award based on the coupon part of the settlement)).

BEST PRACTICES

Counsel negotiating a class action settlement agreement containing an attorneys' fee provision should be prepared for scrutiny and fashion the terms to survive objections and win approval by the district court. Counsel should negotiate fees separately from class relief. To best position a fee award for approval, counsel should:

- **Consider how the appellate court views the abuse of discretion standard.** Several circuit courts have aggressively reviewed attorneys' fee provisions and calculations in connection with the overall review of a class action settlement. Even under the abuse of discretion standard, a circuit court might second-guess a district court's determination on whether an attorneys' fee award is reasonable under the circumstances and closely examine whether class counsel benefits from a settlement at the expense of the class.
- **Cross-check fee award calculations under the lodestar and percentage recovery methods.** Objectors will use any significant discrepancy between the calculations to challenge the entire settlement. Court approval is more likely if fee awards come out about equally under both methods. Additionally, when calculating class counsel's fee as a percentage of recovery, counsel should consider whether to include administrative expenses and notice costs as part of the benefit received by the class.
- **Consider engaging experts to value the settlement.** Counsel should ensure that the record adequately supports their request for attorneys' fees and that the settlement is worth the amount that counsel represents. Expert testimony is an effective tool for this purpose and can supply the record with evidence of the settlement's reasonableness.
- **Assess the value and nature of non-cash settlements.** When negotiating settlements intended to avoid CAFA's reach, counsel should carefully consider the buying power associated with non-monetary awards that class members can use to purchase items at retailers. Depending on the jurisdiction, a relatively modest award may avoid CAFA's jurisdiction if the voucher or gift card can buy a full item, rather than a simple price discount.
- **Ensure compliance with all applicable ethical rules.** Counsel should bear in mind the American Bar Association's Model Rules of Professional Conduct (Model Rules), in particular:
  - Model Rule 1.5(a), which provides that counsel "shall not make an agreement for, charge, or collect an unreasonable fee or an unreasonable amount for expenses"; and
  - Model Rule 1.7(a)(2), which provides that counsel "shall not represent a client if the representation involves a concurrent conflict of interest," which exists if "there is a significant risk that the representation of one or more clients will be materially limited by ... a personal interest of the lawyer."

  Counsel should also be aware of "clear sailing" provisions, in which a class action defendant agrees not to contest class counsel's petition for attorneys' fees. Courts might view this type of agreement as evidence of a conflict or collusion (see *Redman*, 768 F.3d at 637 (noting that a clear sailing clause "illustrates the danger of collusion in class actions between class counsel and the defendant, to the detriment of the class members"); but see *Bezdek*, 2015 WL 9583769, at *5 (noting that the clear sailing term was not per se unreasonable, but required extra judicial scrutiny)) (for more information, search Webinar: Ethical Hurdles When Settling a Class Action on Practical Law). Additionally, kicker clauses, in which the amount of any reduction in attorneys' fees will revert to the defendant rather than to the class, raise similar concerns.
- **Emphasize the reasonableness of the fee claim to the court by providing legal and financial context for the settlement.** When submitting requests for attorneys' fees, counsel should:
  - highlight counsel's skills and any innovative terms of settlement;
  - compare awards in similar cases;
  - describe the actual damages suffered by the class members, which are likely minimal; and
  - draw attention to the financial resources of the defendant, where applicable, in justifying both the settlement generally and the fee request specifically.