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Ethical considerations in settling class actions

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Settling a class action presents a host of unique ethical considerations for counsel on all sides. Class settlements not only affect the rights of the named parties to the action; they also affect the rights of absent class members, even though they are not sitting at the bargaining table. These ethical considerations kick in even before formal settlement discussions begin, and continue to apply during the negotiation of settlement terms and the process of obtaining court approval. This article analyzes a few key ethical considerations counsel should keep in mind as they navigate the settlement of a class action.

Initiating Settlement Discussions

Lawyers on both sides should keep ethics top of mind even before sitting down to discuss the terms of a class settlement.

For example, it is not uncommon for class action defendants to face multiple parallel actions filed by different firms and lead plaintiffs. In such circumstances, who should participate in the settlement discussions? Some courts have expressed concern that a defendant facing multiple parallel class actions may pit class lawyers against each other in a "reverse auction" to secure the lowest possible settlement, to the detriment of the class. *See, e.g., Negrete v. Allianz Life Ins. Co. of N. Am.*, 523 F.3d 1091, 1099 (9th Cir. 2008). Counsel positioning such actions for resolution should be mindful of whether their choice of negotiating partners could be characterized as encouraging a "bidding war between the various potential class counsel." *Gallucci v. Gonzales*, 603 F. App'x 533, 534 (9th Cir. 2015). While there is no single path forward in such cases, principles of openness and transparency go hand in hand with the values of fairness, reasonableness, and adequacy embodied in Rule 23.

It is also not uncommon for a defendant to initiate settlement discussions with individual putative class members. While the law is generally clear that after class certification, absent class members are considered "represented parties" for whom the standard limits on class-member communications apply (*see Jacobs v. CSAA Inter-Ins.*, 2009 WL 1201996, at *3 (N.D. Cal. May 1, 2009)), the pre-certification context is less clear. The prevailing view is that pre-certification settlement communications are generally permitted, subject to certain limitations. Among other considerations, such communications must not be misleading, deceptive, or coercive, and courts have been willing to step in to restrict communications with putative class members if there is a suggestion that a defendant's communications run afoul of those rules. Compare *Reid v. Unilever United States, Inc.*, 964 F. Supp. 2d 893, 929–30 (N.D. Ill. 2013), with *Quezada v. Schneider Logistics Transloading & Distribution*, 2013 WL 1296761, at *5 (C.D. Cal. Mar. 25, 2013). Counsel seeking to engage individual putative class members can save themselves from potential headache and criticism by ensuring their communications follow these basic guidelines.

Common Deal Terms

Class settlements often involve some unique deal terms that can implicate counsel's ethical obligations as well. Two areas that have been the subject of increasing scrutiny relate to class representative service awards and *cy pres* designations.

Many class settlements commonly include some form of service award. Recently, however, some courts have raised concerns that such awards create a conflict of interest between the class representatives (who receive these awards) on the one hand, and the absent class members (who do not receive these awards) on the other. The 11th Circuit was the first to raise this concern, and has outright prohibited incentive awards on the ground that they create a conflict of interest that is impermissible under nineteenth-century Supreme Court precedent. *See Johnson v. NPAS Sols., LLC*, 975 F.3d 1244, 1255–58 (11th Cir. 2020) (citing *Trustees v. Greenough*, 105 U.S. 527 (1881); Cent. *R.R. & Banking Co. v. Pettus*, 113 U.S. 116 (1885)). The 2nd Circuit has also expressed doubt about the soundness of this practice. *See Fikes Wholesale, Inc. v. HSBC Bank USA, N.A.*, 62 F.4th

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704, 721 (2nd Cir. 2023) ("Service awards are likely impermissible under Supreme Court precedent."). The Supreme Court has yet to grant review of this issue, and it remains to be seen whether other circuit courts will follow the 11th Circuit's lead.

Many common-fund settlements also include a designated *cy pres* recipient, typically, a charitable organization whose mission has some tie-in to the subject matter of the litigation. Although the designation of a *cy pres* recipient for residual, unclaimed funds is rarely cause for concern, courts have expressed skepticism of settlements in which a substantial portion is set aside for a *cy pres* beneficiary. Although there may be cases in which such a structure is ultimately the one that will most directly or indirectly benefit the class, in other cases, such settlements create the potential for abuse by superficially inflating the size of a class settlement – and any potential claim for fees – without conferring any real benefit to the class. These concerns are heightened when counsel use the designation of a *cy pres* beneficiary to direct funds toward personal causes. For example, the 9th Circuit has suggested that this can, in some cases, "cast doubt on the propriety of the selection process" and call into question whether class counsel negotiated the relief to benefit themselves and their preferred causes, or to benefit the class at large. *In re Google Referrer Header Privacy Litig.*, 869 F.3d 737, 746 (9th Cir. 2017); *see id.* (noting that "the fact alone that 47% of the settlement fund is being donated to the alma maters of class counsel raises an issue which … the district court should have pursued further") (Wallace, J., concurring in part). Expect *cy pres* provisions to be an ongoing subject of litigation as the courts continue to define the contours on when *cy pres* relief is fair, reasonable, and adequate.

Class actions present lawyers on both sides with ethical considerations at every step. Settlement is no exception. Close attention to the case law developments in this evolving area, as well as the basic ethical rules relating to conflicts, communications with parties, and duties of candor and loyalty, will go a long way to facilitating fair, reasonable, and adequate class settlements that benefit the parties and class members alike.