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PERSPECTIVE • Mar. 11, 2010 • Page 6

An Inside View of Class Action Settlements

By Deborah Rothman

A recent outpouring of disgust on the ABA Web site directed at consumer class action attorneys got me thinking about my experience in class action mediations. Having talked for hours in caucus with class counsel, and then the defense team, I have garnered insights that might be helpful to attorneys whose practices do not involve class actions.

The uproar was generated by a story about a Los Angeles Superior Court judge who, substituting for the judge who had granted preliminary approval of the deal, refused to rubber-stamp a mediated settlement agreement between women's clothing store chain Windsor Fashions, Inc. and a class of consumers. The suit alleged that the members of the class had been asked for their telephone numbers when making credit card purchases at Windsor Fashion stores, in violation of the Song-Beverly Credit Card Act, Civil Code Section 1747.08(a)(2). Under the proposed settlement agreement, the 43,000 plus consumers would each receive a $10 gift card redeemable at Windsor Fashions, the class representative would be paid $2500 in cash, and class counsel would receive $125,000 in fees and costs. The substitute judge, who quickly reversed himself, but not before trumpeting his audacious decision to the media, had changed the settlement terms so that class counsel and the class representative would receive their settlement payments in $10 Windsor Fashion gift cards, just as the class members would.

What was particularly interesting to me was the amount of vitriol expressed by attorneys toward class action attorneys and gift card settlements. Much of the indignation focused on the perceived injustice of the Windsor Fashion class counsel's negotiating a cash deal for himself while, in effect, selling out the class members. There was also considerable commentary to the effect that most consumer class actions are merely scams (one attorney called it "blackmail") on the part of consumer attorneys who go after companies who make mistakes that harm no one, recovering virtually nothing for the clients, and getting paid hefty attorney's fees for their efforts.

Having mediated dozens of class actions to settlement, perhaps my experience can shed light on some of the less-understood components of these negotiations.

It should be noted that many class actions serve an important public interest role in aggregating *de minimis* claims and thus forcing non-compliant defendants to conform to the law's requirements. Not only is the public thereby protected; honest competitors of non-compliant businesses also benefit. It makes no sense to require class counsel to accept payment in kind when the class receives gift cards in whole or in part. It is class counsel, after all, who work on contingency, front the costs, allocate their

time reviewing masses of documents and interviewing dozens of putative class members away from potentially more profitable matters to right these wrongs, taking the risk that the case will be lost.

Class action mediations differ from most other mediations in several important ways. First, there are often very few defenses available to the defendant in these class actions. Second, class members, including the class representative, rarely attend the mediation, which understandably reinforces the perception held by some that class counsel is the real plaintiff. However, considering the small amounts plaintiffs generally recover in consumer class actions, class members usually do the math and opt not to miss a day of work.

Additionally, in many class actions brought on behalf of consumers or employees, the harm complained of is often a technical statutory violation that, while embodying an important public policy, did not actually result in damage to any class members. For example, Labor Code Sections 226 and 1174 set out an employer's responsibilities to issue a detailed wage statement that must always accompany the check or cash payment to the employee, as well as payroll record retention requirements. Few employers are aware of these exacting provisions before they are sued, and even when sued, they are not ordinarily accused of having actually harmed any class members. This is in stark contrast to most lawsuits and mediations, where the plaintiff complains, often graphically, of real and direct injury.

In further contradistinction to the typical employment mediation, for example, it is the defendants with whom the mediator must express empathy, and the plaintiffs who are not unhappy. From the defendants' perspective, their company was understandably ignorant of one of the many laws enacted in California each year to protect "the little guy," and although no one was actually damaged, their company has to go to the trouble and expense of retaining counsel to defend the class action and oppose class certification, gather and cull evidence from voluminous sets of documents, send someone from management to a day or more of mediation. Then, if they're lucky and the case settles, pay hundreds of thousands of dollars to the attorney who sued them and retain a class action administrator to mail out checks or gift cards to hundreds of people who weren't actually damaged by their company's oversight.

What is important to understand is that, in my experience, class counsel never walks into mediation and demands a gift card settlement. Most class counsel with whom I have mediated are highly-principled and acutely aware of their responsibilities to the class they represent. It is only when there is a pending impasse in the negotiations because of the difference between the class' last demand and the defense's last offer that the parties have to get creative in trying to bridge the gap, and gift cards offer a win-win way of achieving a settlement that otherwise appears unachievable.

Why should class counsel compromise? Naturally, no case is "a slam-dunk" but as noted above, the class usually has the upper hand. However, there are other considerations that argue in favor of compromising.

Especially in a recession, there is a real risk that a targeted company will be unable to survive if a big judgment is rendered in a class action trial. It is not unusual for me to learn in defense caucus that the defendant company prefers to continue to pay defense counsel to defend the lawsuit while it

determines its long-term viability, and/or creates an orderly exit plan. Class counsel used to demand audited financial statements before they would accept such a representation, but defense representations often have the inherent ring of credibility when made in mediation.

Another reason class counsel may compromise is that plaintiffs are often unsophisticated and can prove fickle. For example, they may lose interest in the lawsuit, move without leaving a forwarding address or make statements to the media that could harm the class' chances of success. In addition, if the class action is large enough, there is always the risk that a rival class action firm could attempt to take it over or lure key plaintiffs into their camp, so class counsel has an incentive to settle at mediation.

The thing about using gift cards to make up some or all of the difference between the defense's best settlement offer and the class' best demand is that gift cards sometimes satisfy many of both sides' interests.

From the defendant's perspective, gift cards are a very unobjectionable way to close the gap. In the first place, gift cards in small denominations are not infrequently discarded or otherwise not redeemed. If they are lost there is no obligation to replace them. The value of the card is always less than the retail price of the merchandise for which it is redeemed, so defendants are, in effect, getting a discount on the settlement. And defendants can count on some plaintiffs to redeem their 2010 cards in 2011 and 2012, so that to this extent, the payout occurs over time, and at discount from present value. Gift cards carry with them the benefit of moving older merchandise and driving traffic, and thus potential cash flow, since women often shop with friends. Additionally, the parties might negotiate for restrictions on the cards to further reduce their cost to the defense; for example, a requirement that they only be redeemed for non-clearance merchandise.

From class counsel's perspective, gift cards are not unattractive to members of a consumer class-they are, by definition, preexisting customers of the defendant, and the defendant did not actually cause them harm so there would be no resistance to patronizing the defendant's stores. Class counsel can be counted on to drive the hardest bargain they believe is possible. Thus, if gift cards are proposed to close the gap, plaintiffs' counsel will try to get a higher-value card for each class member than could have been negotiated for a cash settlement. For some plaintiffs that is a complete windfall, i.e., something for nothing.

I confess that in one such mediation, where the class had agreed to accept gift cards as part of the settlement, I was so convinced that the defendant was cash-strapped that I offered to take the balance of my mediation fee in merchandise gift cards, too! Where a defendant is approaching insolvency, gift cards allow class members and other creditors to reach the single asset that the defendant still holds in abundance: inventory.

Class actions serve the important public purpose of enforcing statutory requirements, even though the individual class members may be only slightly if at all harmed. In such cases, particularly when defendants are facing insolvency, thinking outside the (cash) box during mediation may be the only way to reach a settlement. Gift cards and similar solutions offer a viable and valuable solution for keeping companies in line without knocking them completely off their rails.

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