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Never Settle for Second Best? Cy Pres Distributions in Securities Class Action Settlements

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NOTE

Never Settle for Second Best? *Cy Pres* Distributions in Securities Class Action Settlements

Oetting v. Jacobson (In re BankAmerica Corp. Securities Litigation), 775 F.3d 1060 (8th Cir. 2015), *reh'g and reh'g en banc denied* (Mar. 18, 2015)

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I. INTRODUCTION

There is an old adage that one should "never settle for second best." While this advice is arguably well taken in most areas of life, it is less useful in settlement discussions. In 2015, more federal securities class actions were filed than during the height of the financial crisis in 2008, with more of those cases settling than in any year since 2011.[1] Consumer class action funds often go largely unclaimed, leaving settlement funds intended to compensate injured plaintiffs unused and undistributed.

Courts have attempted to remedy this issue by using *cy pres*, the practice of distributing unclaimed settlement funds to a "next best" plaintiff, often a charitable organization.[2] While the practice has theoretical advantages, in practice, it can leave class counsel and a tenuously related charity with a windfall of funds and the actual victims with nothing. The Eighth Circuit spoke on the issue in *In re BankAmerica Corp. Securities Litigation*.[3] In that case, the Eighth Circuit fashioned the *cy pres* reward in a way that would avoid its two major pitfalls: poor selection of a next best plaintiff and lack of compensation for the actual victims. There are, however, additional steps that courts can and should take to perfect *cy pres* distributions, including requiring the selection of a recipient for residual class funds at the settlement

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1. Svetlana Starykh & Stefan Boettrich, *Recent Trends in Securities Class Action Litigation: 2015 Full-Year Review*, NERA ECON. CONSULTING 1 (Jan. 25, 2016), http://www.nera.com/content/dam/nera/publications/2016/2015_Securities_Trends_Report_NERA.pdf.

2. WILLIAM B. RUBENSTEIN, NEWBERG ON CLASS ACTIONS § 12:32 (5th ed. 2016) [hereinafter NEWBERG ON CLASS ACTIONS (5th ed.)].

3. Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060, 1062 (8th Cir. 2015), *reh'g and reh'g en banc denied* (Mar. 18, 2015).

agreement stage, monitoring notice to class members, and facilitating the input of class members when choosing an appropriate recipient.

II. FACTS AND HOLDING

In 1998, NationsBank merged with BankAmerica Corporation to form Bank of America Corporation.[4] As a result of the merger, shareholders filed numerous class action lawsuits, claiming the new bank violated various federal and state securities regulations, including securities fraud provisions.[5] The cases were consolidated in the U.S. District Court for the Eastern District of Missouri after they were transferred from the Judicial Panel on Multidistrict Litigation in February of 1999.[6] The district court certified four classes – two comprised of NationsBank shareholders and two of BankAmerica shareholders – and eventually approved a $490 million global settlement against the objections of David Oetting, the NationsBank class representative.[7] Oetting argued that the $332.2 million awarded to the two NationsBank classes was inadequate given the strength of their claims compared to the two BankAmerica classes.[8]

The first distribution from the NationsBank settlement fund was made in December 2004, after which approximately $6.9 million remained.[9] The court suggested at least part of the reason for the remaining funds was checks that were returned for wrong addresses and checks that were never cashed or deposited.[10] The fund slowly dwindled.[11] In April 2009, the district court ordered a $4.75 million distribution to additional claimants, leaving

4. *Id.* The merger of the two banks was, at the time, the second-largest corporate merger in history, with Nations Bank paying "about $62 billion of its stock for BankAmerica Corp., creating the largest U.S. bank ranked by assets." Mitchell Martin, *Nations Bank Drives $62 Billion Merger: A New BankAmerica: Biggest of U.S. Banks*, N.Y. TIMES (Apr. 14, 1998), http://www.nytimes.com/1998/04/14/news/nations-bank-drives-62-billion-merger-a-new-bankamericabiggest-of-us.html.

5. *In re BankAmerica Corp.*, 775 F.3d at 1062. The securities law violations centered around BankAmerica's failure to disclose information in its 1998 SEC Form 8-K filing and announcement regarding the merger with NationsBank. *In re* BankAmerica Corp. Sec. Litig., 210 F.R.D. 694, 696 (E.D. Mo. 2002). The first alleged misrepresentations and omissions related to the capitalization and risks resulting from its strategic alliance with D.E. Shaw & Co., under which BankAmerica wrote off loans totaling $1.4 billion. *Id.* at 696–97. Plaintiffs also alleged that BankAmerica misrepresented its merger with NationsBank "as a 'merger of equals' whereas it was actually a 'takeover' of BankAmerica by NationsBank." *Id.* at 697.

6. *BankAmerica Corp.*, 210 F.R.D. at 697.

7. *In re BankAmerica Corp.*, 775 F.3d at 1068.

8. *Id.* at 1062 (citing *In re* BankAmerica Corp. Sec. Litig., 227 F. Supp. 2d 1103 (E.D. Mo. 2002)).

9. *Id.*

10. *Id.* at 1064–65.

11. *Id.* at 1062.

$2,440,108.53 in the settlement fund.[12] For over three years, the fund remained untouched.[13] In September 2012, class counsel for NationsBank moved to terminate the case and award class counsel an additional $98,114.34 in attorneys' fees for work performed since the initial December 2004 distribution.[14] Class counsel had already received 18% of the NationsBank fund, roughly $59 million.[15] Class counsel moved for the district court to distribute the remainder of the settlement funds *cy pres* to three St. Louis area charities: Legal Services of Eastern Missouri ("LSEM"), the Mathews Dickey Boys' and Girls' Club of St. Louis, and The Backstoppers.[16]

In deciding how to rule on the motion, the district court first discussed whether *cy pres* distribution would be appropriate, opining that *cy pres* distribution "is permissible 'in cases in which class members are difficult to identify or where they change constantly' or in cases where there are unclaimed funds."[17] The court agreed with class counsel that "*cy pres* distribution of the remaining funds is appropriate" because (1) "[a]ll class members submitting claims have been satisfied in full," (2) "identification of members for additional distribution would be difficult and costly," (3) "ownership of Bank of America shares changes constantly," and (4) "further distribution . . . would not benefit the individuals who actually suffered harm."[18] The court also looked to the terms of the settlement agreement, reasoning that "defendant acknowledged that any surplus would not be returned to it," and the court that approved the December 2004 distribution "specified that any surplus . . . would be distributed to non-profit organizations to be determined by the court."[19]

Next, the district court attempted to determine the appropriate recipient of the surplus funds, relying on the principle that "the unclaimed funds should be distributed for a purpose as near as possible to the legitimate objectives underlying the lawsuit, the interests of class members, and the interests of those similarly situated."[20] Under this rule, the court must tailor the distribution to the geographic scope and purpose of the original litigation, which "preserves the legal fiction that class members themselves are receiving an indirect benefit from the *cy pres* distribution."[21] The court reasoned that

12. *Id.*

13. *In re* BankAmerica Corp. Sec. Litig., 210 F.R.D. 694, 702 (E.D. Mo. 2002).

14. *In re BankAmerica Corp.*, 775 F.3d at 1062.

15. *Id.* at 1070.

16. *Id.* at 1068.

17. *In re* Bank of America Corp. Sec. Litig., No. 4:99-MD-1264, 2013 WL 3212514, at *2 (E.D. Mo. June 24, 2013) (quoting Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 268 F.3d 619, 625 (8th Cir. 2001)), *vacated and remanded sub nom. In re BankAmerica Corp.*, 775 F.3d 1060.

18. *Id.* at *3.

19. *Id.*

20. *Id.* (quoting *In re Airline Ticket Comm'n Antitrust Litig.*, 268 F.3d at 682).

21. *Id.*

LSEM[22] would be a more appropriate recipient than the other two charities suggested by class counsel because legal aid organizations such as LSEM specifically help victims of fraud.[23]

Oetting objected a second time to both the *cy pres* distribution and the potential recipients suggested by class counsel but was again overruled.[24] The district court granted class counsel's motion and ordered the funds be distributed to LSEM.[25]

Oetting then brought this appeal, arguing the district court erred in ordering the *cy pres* distribution.[26] Oetting reasoned that the district court abused its discretion in ordering the distribution to LSEM because "further distribution to the classes [was] feasible" and the choice of LSEM was inappropriate because "LSEM is unrelated to the classes or the litigation," making it ineligible to be the "'next best' *cy pres* recipient."[27]

On appeal, the Eighth Circuit agreed with Oetting and reversed the district court on both grounds, holding first that the *cy pres* distribution was premature because an additional distribution is feasible and second that LSEM is not an appropriate "next best" recipient of the surplus funds.[28] The Eighth Circuit was clear that "[g]iven the substantial history of district courts ignoring and resisting circuit court *cy pres* concerns and rulings in class action cases, we conclude it is time to clarify the legal principles that underlay our [past *cy pres* decisions]."[29]

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22. The Legal Services of Eastern Missouri, Inc., is, according to its website, "an independent, non-profit organization that provides high quality civil legal assistance and equal access to justice for low-income people and the elderly" and "is a tax exempt 501(c)(3) corporation." *Who We Are*, LEGAL SERVS. E. MO., http://lsem.org/about-lsem/child-page-1-overview/ (last visited Mar. 16, 2017).

23. *Bank of America Corp.*, 2013 WL 3212514, at *4–5.

24. Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060, 1062 (8th Cir. 2015), *reh'g and reh'g en banc denied* (Mar. 18, 2015).

25. *Id.* (citing *Bank of America Corp.*, 2013 WL 3212514, at *5–6).

26. *Id.* Oetting also raised a second issue on appeal, that the district court erred in granting additional attorneys' fees to class counsel when it was already awarded 18% of the NationsBank settlement fund. *Id.* at 1067–68. The Eighth Circuit agreed with Oetting and held that the award of attorneys' fees was premature and ordered the district court to reexamine the issue after an additional distribution to the class was made, pursuant to its opinion. *Id.* at 1063.

27. *Id.* at 1062. Oetting specifically argued in his brief that LSEM was not a proper recipient of the funds because "*first*, there is an impermissible geographic discontinuity between the composition of the class (nationwide) and the locus of the *cy pres* recipient (Eastern Missouri); *second*, there is zero connection between the *cy pres* recipients and the subject matter of the lawsuit or the composition of the class." Opening Brief of David P. Oetting, Class Representative at 6, Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060 (8th Cir. 2015) (No. 13-2620), 2013 WL 5162807, at *24.

28. *In re BankAmerica Corp.*, 775 F.3d at 1062–63, 1067.

29. *Id.* at 1064.

III. LEGAL BACKGROUND

The *cy pres* doctrine was born as a rule of construction employed by courts aiming to save testamentary charitable gifts that would otherwise fail by attempting to ascertain and give effect to the original intent of the testator.[30] The term comes from the Norman French expression *cy pres comme possible*, meaning "as near as possible."[31] In the trust context, the practice was used as an equitable doctrine that rests on the assumption "that the settlor would have preferred a modest alteration in the terms of the trust to having the corpus revert to his residuary legatees."[32] In its modern manifestation, courts utilize *cy pres* in the class action context as a way to distribute unclaimed funds from settlements "guided by the parties' original purpose."[33] Unlike in the trust context, however, the "settlor," or defendant, strongly prefers the funds be reverted to it. This leads to a strained analogy that courts have largely ignored.[34]

Many circuits have criticized and severely restricted the use of *cy pres* in the class action context.[35] However, most of the circuits to consider the practice agree that there are some situations in which *cy pres* is appropriate.[36] While the Supreme Court has not rendered a decision on the issue directly, Chief Justice Roberts noted that *cy pres* is "a growing feature of class action settlements" and, because of the "fundamental concerns surrounding the use

30. *See* Late Corp. of the Church of Jesus Christ of Latter-Day Saints v. United States, 136 U.S. 1, 56 (1890) ("[W]here the particular trust cannot be carried into effect, either for its uncertainty or its illegality, or for want of proper objects[,] . . . the general intention of the testator in favor of charity will be effectuated by the court through a *cy-près* application of the fund.").

31. Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 268 F.3d 619, 625 (8th Cir. 2001) (quoting Democratic Cent. Comm. v. Washington Metro. Area Transit Comm'n, 84 F.3d 451, 455 n.1 (D.C. Cir. 1996)).

32. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:32 (quoting Hughes v. Kore of Ind. Enter., Inc., 731 F.3d 672, 676 (7th Cir. 2013)).

33. Powell v. Ga.-Pac. Corp., 119 F.3d 703, 706 (8th Cir. 1997).

34. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:32.

35. Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060, 1063 (8th Cir. 2015) (citing cases from the Second, Third, Fifth, and Seventh Circuits), *reh'g and reh'g en banc denied* (Mar. 18, 2015).

36. *See, e.g.*, Ira Holtzman, C.P.A. v. Turza, 728 F.3d 682, 689–90 (7th Cir. 2013); *In re* Baby Prods. Antitrust Litig., 708 F.3d 163, 172–73 (3d Cir. 2013); Rohn v. TAP Pharm. Co. (*In re* Lupron Mktg. & Sales Practices Litig.), 677 F.3d 21, 29–33 (1st Cir. 2012); Nachshin v. AOL, LLC, 663 F.3d 1034, 1038–40 (9th Cir. 2011); Klier v. Elf Atochem N. Am., Inc., 658 F.3d 468, 473–82 (5th Cir. 2011); Plaintiffs Class v. Bd. of Comm'rs of the Orleans Parish Levee Dist. (*In re* Katrina Canal Breaches Litig.), 628 F.3d 185, 196 (5th Cir. 2010); Masters v. Wilhelmina Model Agency, Inc., 473 F.3d 423, 434–36 (2d Cir. 2007); Wilson v. Sw. Airlines, Inc., 880 F.2d 807, 816 (5th Cir. 1989).

of such remedies in class action litigation," "this Court may need to clarify the limits" on their use.[37]

As a threshold matter, the Eighth Circuit relied on principles set forth by the American Law Institute ("ALI") in its analysis.[38] The provision relied on by the Eighth Circuit was ALI § 3.07, which outlines when *cy pres* relief is appropriate.[39] Other circuits have also deferred to this section in fashioning *cy pres* relief.[40]

Application of the doctrine varies, but typically, the court must first determine *cy pres* distribution is appropriate, and, once that determination has been made, find an appropriate "next best" recipient for the surplus funds. The Eighth Circuit, after outlining its framework, addressed each of these issues in turn.

A. Appropriateness of Cy Pres *Distribution*

In its opinion, the Eighth Circuit announced a new take on *cy pres* distributions, noting that "[w]e have approved *cy pres* distribution of unused or unclaimed class action settlement funds in two cases. In both, the distributions met each of the criteria in ALI § 3.07, even though our decisions antedated the ALI's work."[41] This section of the ALI starts by noting that "[i]f individual class members can be identified through reasonable effort, and the distributions are sufficiently large to make individual distributions economically viable, settlement proceeds should be distributed directly to individual

37. Marek v. Lane, 134 S. Ct. 8, 9 (2013) (Roberts, C.J, respecting the denial of certiorari) (respecting the denial of certiorari because the issue on appeal "focused on the particular features of the specific *cy pres* settlement at issue" and "review of this case might not have afforded the Court an opportunity to address more fundamental concerns surrounding the use of such remedies in class action litigation, including when, if ever, such relief should be considered; how to assess its fairness as a general matter; whether new entities may be established as part of such relief; if not, how existing entities should be selected; what the respective roles of the judge and parties are in shaping a *cy pres* remedy; how closely the goals of any enlisted organization must correspond to the interests of the class; and so on").

38. *See In re BankAmerica Corp.*, 775 F.3d at 1064.

39. *See id.*; PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07 (AM. LAW INST. 2010).

40. *See, e.g.*, *In re Lupron Mktg. & Sales Practices Litig.*, 677 F.3d at 32–34; *Klier*, 658 F.3d at 474–75 n.14–16; *In re* Pharm. Indus. Avg. Wholesale Price Litig., 588 F.3d 24, 35 (1st Cir. 2009); *Baby Prods. Antitrust Litig.*, 708 F.3d at 171–72; Marshall v. NFL, 787 F.3d 502, 509 (8th Cir. 2015), *reh'g and reh'g en banc denied* (July 15, 2015).

41. *In re BankAmerica Corp.*, 775 F.3d at 1064 (citing Powell v. Ga.-Pac. Corp., 119 F.3d 703, 706–07 (8th Cir. 1997); Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 268 F.3d 619 (8th Cir. 2001); Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 307 F.3d 679 (8th Cir. 2002)).

class members."[42] Thus, the touchstone of the appropriateness analysis is whether it is "feasible to make further distributions to class members."[43] Looking again to the ALI provision, the court held the feasibility "inquiry *must* be based primarily on whether 'the amounts involved are too small to make individual distributions economically viable.'"[44] To make this determination, the court relied heavily on the "administrative cost" of additional distributions.[45]

Prior decisions of the Eighth Circuit focus more on practical complications of an individual distribution, including "where class members 'are difficult to identify or where they change constantly,'"[46] where significant time "elapsed since the initial distribution, and many class members have probably relocated," and where "the party entirely responsible for conducting the first distribution[] is no longer responsible for locating class members and distributing the funds."[47] This necessarily includes "balanc[ing] the equitable interests involved in the case with the need to conserve judicial resources."[48] The Supreme Court has further noted that *cy pres* may be particularly appropriate in the context of securities class actions, where a large amount of funds are likely to go unclaimed.[49]

B. Determining the "Next Best" Recipient

The Eighth Circuit again took instruction from the ALI to determine which organizations would qualify as an appropriate "next best" recipient.[50] This is sometimes referred to as the "nexus requirement."[51] This requirement instructs that where individual distributions are not viable, the court should "require the parties to identify a recipient whose interests reasonably approximate those being pursued by the class," and if after "thorough investigation and analysis" there is no such recipient, "a court may approve a recipient that does not reasonably approximate the interests being pursued by the class."[52]

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42. *Id.* at 1063–64 (citing PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07(a)).

43. *Id.* at 1064 (quoting *Klier*, 658 F.3d at 475).

44. *Id.* at 1065 (quoting PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07(a)).

45. *Id.* at 1064.

46. *In re Airline Ticket Comm'n Antitrust Litig.*, 268 F.3d at 625 (quoting Powell v. Ga.-Pac. Corp., 119 F.3d 703, 706 (8th Cir. 1997)).

47. *Powell*, 119 F.3d at 706–07.

48. *Id.* at 707.

49. *See* Marek v. Lane, 134 S. Ct. 8, 9 (2013) (Roberts, C.J., respecting the denial of certiorari). *See also* Deposit Guar. Nat'l Bank v. Roper, 445 U.S. 326, 339 (1980).

50. *See In re BankAmerica Corp.*, 775 F.3d at 1067.

51. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:33.

52. PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07(c) (AM. LAW INST. 2010).

In choosing the "next best" recipient, the court should be "guided by the parties' original purpose," such that "the unclaimed funds [are] distributed 'for the indirect prospective benefit of the class.'"[53] The Eighth Circuit has been clear that the standard is narrow and "the unclaimed funds should be distributed for a purpose as near as possible to the legitimate objectives underlying the lawsuit, the interests of class members, and the interests of those similarly situated."[54] Courts must also consider "the full geographic scope of the case" in determining which charitable organizations would indirectly benefit the class most accurately.[55] To find an organization that indirectly benefits the class, courts look for a recipient that "relate[s] directly to the . . . injury alleged in [the] lawsuit and settled by the parties."[56]

The decisions of other circuits when deciding *cy pres* cases and applying the nexus requirement reveal the general principles used.[57] A leading class action treatise summarizes those principles: "*[f]irst*, courts primarily require that there be a nexus between the *cy pres* beneficiaries and the underlying claims in the case"; "*[s]econd*, courts have required that there be a match between the geographic breadth of the plaintiff class and the range of the *cy pres* recipients' work"; "*[t]hird*, the nexus requirement is generally not absolute. . . . [And generally] the court should 'require the parties to identify a recipient whose interests reasonably approximate those being pursued by the class'"; "*[f]ourth*, some courts look at the integrity of the recipient groups to ensure that the class's money is likely to be used well and not squandered"; and "*[f]ifth*, the *cy pres* beneficiary should not have a significant prior relationship with either one of the parties or the judge."[58]

Absent this required nexus, "the distribution would not live up to the *cy pres* name, that is, that the distribution be 'as near as possible' to the class's

53. Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 268 F.3d 619, 625 (8th Cir. 2001) (quoting *Powell*, 119 F.3d at 706).

54. Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 307 F.3d 679, 682 (8th Cir. 2002).

55. *Id.* at 683.

56. *Id.*

57. *See generally* Dennis v. Kellogg Co., 697 F.3d 858, 866 (9th Cir. 2012); *In re Airline Ticket Comm'n Antitrust Litig.*, 307 F.3d at 682; Houck *ex rel.* United States v. Folding Carton Admin. Comm., 881 F.2d 494, 502 (7th Cir. 1989), *amended on denial of reh'g and reh'g en banc* (Sept. 15, 1989); Pink Triangle Coal. v. Union Bank of Switz. (*In re* Holocaust Victim Assets Litig.), 424 F.3d 158, 166–68 (2d Cir. 2005); Lane v. Facebook, Inc., 696 F.3d 811, 822 (9th Cir. 2012); *In re* Baby Prods. Antitrust Litig., 708 F.3d 163, 173 (3d Cir. 2013).

58. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:33 (quoting PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07 cmt. *b* (AM. LAW INST. 2010)).

interests."[59] Despite this theoretical clarity, courts have had difficulty applying these principles in any systematic way.[60]

IV. INSTANT DECISION

A. Majority Opinion

The Eighth Circuit majority analyzed first the appropriateness of using *cy pres* and second the appropriateness of the recipient of the *cy pres* funds.

1. Appropriateness of *Cy Pres*

The court first criticized class counsel and the district court for failing to rely on ALI § 3.07 for its *cy pres* analysis, noting "class counsel and the district court entirely ignored this now-published ALI authority."[61] Citing Fifth Circuit precedent, the Eighth Circuit remarked

> cy pres distribution to a third party of unclaimed settlement funds is permissible only when it is not feasible to make further distributions to class members[,] . . . except where an additional distribution would provide a windfall to class members with liquidated-damages claims that were 100 percent satisfied by the initial distribution.[62]

Again citing the ALI, the court added that this analysis "*must* be based primarily on whether 'the amounts involved are too small to make individual distributions economically viable.'"[63]

The majority concluded first that because further distributions to the class were feasible, the district court's granting of *cy pres* was "an error of

59. *Id.*

60. *See, e.g.*, Powell v. Ga.-Pac. Corp., 119 F.3d 703, 706 (8th Cir. 1997); *Dennis*, 697 F.3d at 866 (holding that *cy pres* distribution of $5.5 million of food to the indigent was inappropriate because the distribution was "divorced from the concerns embodied in consumer protection laws"); Nachshin v. AOL, LLC, 663 F.3d 1034, 1041 (9th Cir. 2011) (reversing *cy pres* distribution to legal aid foundation, the Boys and Girls Club, and the Federal Judicial Center Foundation because those organizations did not "have anything to do with the objectives of the underlying statutes on which Plaintiffs base their claims"); *In re Airline Ticket Comm'n Antitrust Litig.*, 307 F.3d at 682, 684 (reversing approval for use of *cy pres* in an antitrust case where distributions of unclaimed funds were given to the National Association for Public Interest Law). *See also* NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:33 n.3 (listing cases).

61. Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060, 1064 (8th Cir. 2015), *reh'g and reh'g en banc denied* (Mar. 18, 2015).

62. *Id.* at 1064 (emphasis omitted) (quoting Klier v. Elf Atochem N. Am., Inc., 658 F.3d 468, 475 (5th Cir. 2011)).

63. *Id.* at 1065 (quoting PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07(a) (AM. LAW INST. 2010)).

law."[64] The court reasoned that, "from the perspective of administrative cost, a further distribution to the class was clearly feasible," evidenced by the Claim Administrator's estimate that an additional distribution would cost $27,000.[65] Moreover, "no further search need be made for class members whose checks were returned undelivered, so that potentially burdensome expense need not be incurred."[66] The court rejected the district court's conclusion that distribution would be "inappropriate because it would primarily benefit large institutional investors, who are less worthy than charities such as LSEM" and "not inure to the benefit of those actually harmed."[67] The court opined that allowing those considerations "endorses judicially impermissible misappropriation of monies" and that they are simply irrelevant to the court's analysis.[68]

The court then rejected three other contentions raised by class counsel and the district court below.[69] First, class counsel argued that all class members had already "been satisfied in full."[70] The court disagreed, holding that "fully compensated," within the meaning of the rule it announced, should be interpreted as compensation for the entire injury suffered, not as the amount allocated to each class member in the settlement agreement.[71] The settlement agreement was clear that "plaintiffs would recover 'only a percentage of the damages that they sought,'" and "the settling parties disagree as to both liability and damages."[72] Thus, "the notion that class members were fully compensated by the settlement is speculative, at best."[73]

Next, the court rejected the contention that it is "bound by language in the settlement agreement stating that the balance in the settlement fund 'shall be contributed' to non-profit organizations 'determined by the court in its sole discretion.'"[74] The court first recognized the factual inaccuracy, noting that "the settlement agreement only *permitted* distribution of remaining funds to charities at the court's sole discretion," and it was instead the district court that "improperly went further, stating that funds remaining 'by reason of returned or unpaid checks or otherwise' would be paid to 'Authorized Claimants' in a second distribution, and any remaining funds 'shall be contributed to non-sectarian, not-for-profit, 501(c)(3) organization(s) as determined by

64. *Id.*

65. *Id.* at 1064.

66. *Id.* at 1064–65.

67. *Id.* at 1065.

68. *Id.*

69. *Id.*

70. *Id.* (quoting *In re* Bank of America Corp. Sec. Litig., No. 4:99-MD-1264, 2013 WL 3212514, at *3 (E.D. Mo. June 24, 2013)).

71. *Id.* at 1065–66 (quoting Klier v. Elf Atochem N. Am., Inc., 658 F.3d 468, 479 (5th Cir. 2011)).

72. *Id.* at 1066 (quoting *In re* BankAmerica Corp. Sec. Litig., 210 F.R.D. 694, 701 (E.D. Mo. 2002)).

73. *Id.*

74. *Id.*

the court in its sole discretion.'"[75] The court then held that the vague *cy pres* provision in the settlement agreement had no legal effect because it is contrary to prior decisions.[76] But, more importantly, arguing against sole discretion by district courts and the settling parties, the court held any *cy pres* provisions in settlement agreements "must meet [our standards governing *cy pres* awards] regardless of whether the award was fashioned by the settling parties or the trial court."[77]

Finally, Oetting argued that the award should be reversed because class members were not notified that *cy pres* distribution would be taking place.[78] The court agreed, noting that "unless the amount of funds to be distributed *cy pres* is de minimis," the best practice would be to "make a *cy pres* proposal publicly available and allow class members to object or suggest [an] alternative recipient[]."[79] However, because the court was vacating the award on other grounds, it did not consider the effect of class counsel's failure to notify class members.[80]

2. Determining the "Next Best" Recipient

After concluding that the application of *cy pres* was inappropriate, the court, perhaps in an attempt to further flesh out the doctrine, opined on the second step in the *cy pres* analysis. Again relying on language from the ALI, the court addressed the question of how to determine the next best recipient if *cy pres* were deemed appropriate.[81] The court, again relying on language from the ALI,[82] overturned the distribution to LSEM because the district court did not "carefully weigh all considerations, including the geographic scope of the underlying litigation, and make a 'thorough investigation' to determine whether a recipient can be found that most closely approximates the interests of the class."[83] The court opined that while LSEM was "unquestionably a worthy charity," its mission to serve victims of fraud in the St.

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75. *Id.* at 1066 n.5.

76. *Id.* at 1066 (citing Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 268 F.3d 619 (8th Cir. 2001); Travel Network, Ltd. v. United Airlines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 307 F.3d 679 (8th Cir. 2002); Rohn v. TAP Pharm. Prods., Inc. (*In re* Lupon Mktg. & Sales Practices Litig.), 677 F.3d 21, 25–26, 31 (1st Cir. 2012)).

77. *Id.* (alteration in original) (quoting Nachshin v. AOL, LLC, 663 F.3d 1034, 1040 (9th Cir. 2011)).

78. *Id.*

79. *Id.*

80. *Id.* at 1066–67.

81. *Id.* at 1067.

82. *Id.* at 1064; *see also* PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07 (AM. LAW INST. 2010) (noting that an appropriate recipient is "a recipient whose interests reasonably approximate those being pursued by the class").

83. *In re BankAmerica Corp. Sec. Litig.*, 775 F.3d at 1064, 1067 (quoting PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07 cmt. *b*).

Louis area did not approximate the injury suffered by the nationwide class.[84] The court suggested that a non-profit specifically "devoted to preventing and aiding the victims of securities fraud, such as the SEC Fair Funds," would be a more appropriate recipient.[85]

The Eighth Circuit vacated the *cy pres* distribution ordered by the Eastern District of Missouri and remanded the case for further proceedings consistent with the opinion, including another distribution and, if funds remained, a more appropriate non-profit recipient.[86]

B. Dissenting Opinion

Judge Murphy dissented, arguing that the majority's opinion was a departure from Eighth Circuit precedent and that the record did not warrant *post hoc* use of a new rule.[87] She criticized the majority's reliance on ALI § 3.07, arguing that the ALI rules had neither been argued in the district court nor adopted by the Eighth Circuit at the time the Eastern District decided the case.[88] Judge Murphy also distinguished the precedent relied on by the majority, noting that "[c]ircuit courts which have adopted the American Law Institute's preference for pro rata distributions to class members also recognize that *cy pres* awards are appropriate in certain cases."[89] The First, Third, and Fifth Circuit cases cited by the majority all contain situations in which *cy pres* might be appropriate, including cases where "cy pres distribution of surplus funds [was] provided in a settlement agreement."[90]

Next, the dissent discussed the feasibility of making another individual distribution.[91] Instead of focusing on economic viability, the dissenting opinion emphasized the practical problems with the first two distributions,[92] including difficulty in identifying other class members fifteen years after the violation, counting the number of class members who failed to deposit their checks, calculating the interest accumulated on the unclaimed fund, and accounting for the fact that ownership of the shares changes constantly.[93] Judge Murphy also rejected the majority's reliance on the Fifth Circuit case and its interpretation of "fully compensated" and chose instead to rely on the Eighth Circuit's own language on the issue from *Powell v. Georgia-Pacific Corp.*, that full compensation means "each class member ha[s] been fully compen-

84. *Id.* at 1064.
85. *Id.*
86. *Id.* at 1067–68.
87. *Id.* at 1068 (Murphy, J., dissenting).
88. *Id.*
89. *Id.*
90. *Id.* at 1071 (quoting Rohn v. TAP Pharm. Prods., Inc. (*In re* Lupon Mktg. & Sales Practices Litig.), 677 F.3d 21, 25–26, 31 (1st Cir. 2012)).
91. *Id.* at 1072.
92. *Id.*
93. *Id.* at 1070.

sated according to the terms of the [settlement agreement]."[94] Under this interpretation, the class members in the first two distributions would have already been fully compensated thus not necessitating another distribution.[95]

Judge Murphy finally questioned the majority's decision that LSEM was not an appropriate next best recipient of the *cy pres* funds.[96] She argued that the ALI principles, as well as the Eighth Circuit precedent, support the district court's selection of LSEM "based on the nature of its work" serving victims of fraud, "as well as its situs in the area where many class members were located when their losses occurred."[97] She noted that the parties were given time and opportunity to suggest recipients, and because the parties agreed to the recipients in the settlement agreement and no objection by Oetting was made about LSEM at the time, distribution of the remaining funds "would not be unwise or unfair to any party."[98]

V. COMMENT

A. The Source of the Cy Pres *Distribution Problem*

In modern consumer class action settlements, the residual recovery for each individual plaintiff is often very small.[99] The often-miniscule recovery is the main reason that class actions are the only feasible route for plaintiffs seeking relief from consumer fraud.[100] Without the ability to litigate the dispute as a class, the potential recovery would not be high enough to incentivize plaintiffs or plaintiff-side lawyers to bring the case.[101] Settlement agreements in the consumer class action context are most often structured as common fund systems, under which settlement funds are placed into an account and class members, after being notified of their membership, can claim their share of the recovery.[102]

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94. *Id.* (quoting Powell v. Ga.-Pac. Corp., 119 F.3d 703, 705 (8th Cir. 1997)).

95. *Id.*

96. *Id.*

97. *Id.* at 1071.

98. *Id.* at 1070–71.

99. 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, 618 (2010).

100. *Id. See also* MARTIN H. REDISH, WHOLESALE JUSTICE: CONSTITUTIONAL DEMOCRACY AND THE PROBLEM OF THE CLASS ACTION LAWSUIT 131–32 (2009); NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 20:1.

101. Deposit Guar. Nat'l Bank. v. Roper, 445 U.S. 326, 339 (1980) ("Where it is not economically feasible to obtain relief within the traditional framework of a multiplicity of small individual suits for damages, aggrieved persons may be without any effective redress unless they may employ the class-action device.").

102. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 13:7 ("In a common fund case, a defendant contributes the settlement amount, say $100 million, into a settlement fund; the fund is distributed to the class directly or after a claims process. If the class does not claim the full $100 million, the unclaimed funds do not necessari-

The number of class members who actually make claims to the fund is often very small, in many cases, well under 1%.[103] The median consumer class action settlement amount is $9 million, but very large settlements exceeding $50 million often occur, making the average settlement amount between 2010 and 2013 a staggering $56.5 million.[104] Given the usually low percentage of claims and high settlement amounts, the potential for remaining funds is dramatic.

Securities class actions are especially susceptible to low claim amounts. This is because "the large number and geographical dispersion of class members" and "the impersonal nature of the securities field" make both identifying and notifying class members particularly difficult and expensive.[105] Determining where to send notice in securities class actions involves a complex investigation into the beneficial owner of the stock, which sometimes changes several times a day and is further complicated by the sophisticated shareholder list system employed by publicly traded companies.[106] This problem is

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ly go back (or 'revert') to the defendant; they may be distributed *pro rata* among the class members who made claims, or sent to a charity via a *cy pres* award, or to the government via escheat." (footnotes omitted)).

103. *See, e.g.*, Yeagley v. Wells Fargo & Co., No. C 05-034, 2008 WL 171083, at *2 (N.D. Cal. Jan. 18, 2008) ("Out of the original 3.8 million class members, only 29,168 have submitted timely, qualified claim forms, that is, less than one percent of the class chose to participate in the settlement."), *reversed*, 365 Fed. App'x 886 (9th Cir. 2010); *In re* Apple iPhone 4 Prods. Liab. Litig., No. 5:10–md–2188, 2012 WL 3283432, at *1 (N.D. Cal. Aug. 10, 2012) ("The number of claims represents somewhere between 0.16% and 0.28% of the total class . . . ."); Palamara v. Kings Family Rests., No. 07-317, 2008 WL 1818453, at *1–5 (W.D. Pa. Apr. 22, 2008) (noting that "approximately 165 class members" out of 291,000 made claims); Sylvester v. CIGNA Corp., 369 F. Supp. 2d 34, 49 (D. Me. 2005) ("[O]nly 173 valid opt-out forms were received (representing well less tha[n] 1 percent of the total class)."); *In re* Grand Theft Auto Video Game Consumer Litig., 251 F.R.D. 139, 145–57 (S.D.N.Y. 2008) (one-fortieth of 1% made claims).

104. Stephanie Planich et al., *Consumer Class Action Settlements: 2010–2013*, NERA 1 (July 22, 2014), http://www.nera.com/content/dam/nera/publications/archive2/PUB_Consumer_Class_Action_Settlements_0614.pdf.

105. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 22:83.

106. Peddle v. Victor Techs., Inc. (*In re* Victor Techs. Sec. Litig.), 792 F.2d 862, 863 (9th Cir. 1986) ("Most of the securities in question were bought through brokers. In accordance with normal business practices, such securities are held in the name of the broker. The broker, then, is the 'record owner' or the 'street name'; only the broker's name appears on [the issuer's] records. The actual owner is usually referred to as the 'beneficial owner.' The beneficial owners have an interest in the lawsuit; the object of notification procedures is to notify them. To provide notice to the absent members of the class, the plaintiffs offered to draft and print the notice, mail it to all record owners, and provide postage-paid copies of the notice to all record owners to enable the record owners to forward the notice to the beneficial owners of the stock."). The complicated shareholder list system is often confused by courts and litigants. *See, e.g.*, Gold v. Ernst & Ernst (*In re* Franklin Nat'l Bank Sec. Litig.), 599

only exacerbated by the significant time between both the actual securities law violation, the initial distribution of class funds, and later attempts to distribute residual funds.[107]

If the distribution problem proves insurmountable, courts are then left with the difficult choice of deciding where the remaining funds should go. If the court does not allow *cy pres*, it essentially has four alternatives: (1) allow unclaimed funds to "revert to the defendant, who, presumably the court has already determined, has violated the law";[108] (2) allow unclaimed funds to revert "to the state, much as most unclaimed property does after a specified period of time";[109] (3) "increas[e] the pro-rata share of the class members who *do* file claims until the remainder of the damage fund is consumed";[110] or, if the court predicts a low claim rate and large residual, (4) "refus[e] to authorize the class proceeding in the first place."[111] Finding these alternatives unsatisfactory, courts have often turned to *cy pres*.[112] Facially, *cy pres* seems like an appropriate alternative, but in practice, it can lead to a windfall for class counsel and can fail to compensate those actually harmed by poor selection of a *cy pres* recipient.

B. Cy Pres *Distributions Overcompensate Class Counsel*

Cy pres distributions can compensate class counsel more than the actual plaintiffs. *Cy pres* complicates the calculation of an appropriate attorneys'

F.2d 1109, 1111 (2d Cir. 1978) ("There was much confusion in the case and this was manifested in various ways, including many changes of position by lawyers representing the class and by lawyers representing some of the defendants. There was an aura of mystery about the exhibit that was not printed in the Appendix but which, we were told, contained the '661 street names.' Much was said about the brokerage houses, little or nothing about the banks and miscellaneous nominees. We were led to suppose that the real difficulty was not the identification of the beneficial owners of the stock but rather who were the members of the class to whom plaintiffs must give notice the nominees or the beneficial owners . . . ."), *modified on reh'g*, 574 F.2d 662 (2d Cir. 1978).

107. In *BankAmerica*, the time between the initial distribution and the motion to distribute the residual funds via *cy pres* was nearly eight years; the time between the actual securities violation and *cy pres* distribution was approximately fourteen years. Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060, 1062 (8th Cir. 2015), *reh'g and reh'g en banc denied* (Mar. 18, 2015).

108. Redish et al., *supra* note 99, at 619.

109. *Id.*

110. *Id.* (emphasis added); WILLIAM B. RUBENSTEIN, NEWBERG ON CLASS ACTIONS § 22:91 (4th ed. 2016) [hereinafter NEWBERG ON CLASS ACTIONS (4th ed.)] ("If the claims filed fail to exhaust the apportioned settlement fund, the settlement agreement may provide that the defendant will recapture the unclaimed portion or that the remaining portion shall be distributed pro rata among the class members who filed claims." (footnotes omitted)).

111. Redish et al., *supra* note 99, at 619.

112. *Id.* at 638–40 (discussing the downfalls of these four available alternatives).

fee award in the class action context, because a court must decide whether to compare the proposed fee to either "the percentage of[] the full amount available to the class or the smaller amount actually claimed by the class."[113] For example, in a $1,000 settlement with ten class members and 10% of the settlement amount claimed, the comparative pool could either be (1) a percentage of the full amount available to the class, totaling $10,000, or (2) a percentage of the amount actually claimed by the class, totaling $900. The question is then whether funds distributed via *cy pres* can be used to calculate the appropriate attorneys' fee award. Courts that have faced this question have been split on which calculation to use.[114] In *BankAmerica Corp.*, the Eighth Circuit affirmed the awarding of fees for work performed by class counsel during the *cy pres* distribution stage, in addition to the 18% of the *total* NationsBank fund that class counsel already received.[115]

The Supreme Court has expressed support for the percentage-distributed method, at least in some circumstances, such as where "each member of a certified class has an undisputed and mathematically ascertainable claim to part of a lump-sum judgment."[116] There may be "several troubling consequences" to using this method, which does not require a "rational connection between the fee award and the amount of the actual distribution to the class."[117] Such a method could "decouple class counsel's financial incentives from those of the class, increasing the risk that the actual distribution [could] be misallocated between attorney's fees and the plaintiffs' recovery," "provid[e] defendants with a powerful means to enticing class counsel to settle lawsuits in a manner detrimental to the class," and "encourage the filing of needless lawsuits."[118]

Tying attorneys' fees to funds actually distributed might encourage class counsel "to design settlements that offer benefits that actively appeal to the consumers they represent, to come up with more effective notice programs, and to adopt mechanisms that lend themselves toward getting benefits to the consumer."[119] Courts have commonly applied this method to settlement agreements that use a claims-made system whereby defendants agree to pay

113. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 13:7 (footnotes omitted).

114. *Id.*

115. Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060, 1068 (8th Cir. 2015), *reh'g and reh'g en banc denied* (Mar. 18, 2015).

116. Boeing Co. v. Van Gemert, 444 U.S. 472, 479 (1980).

117. Int'l Precious Metals Corp. v. Waters, 120 S. Ct. 2237, 2237 (2000) (O'Connor, J., respecting the denial of the petition for a writ of certiorari).

118. *Id.* at 2237–38.

119. *In re* TJX Cos. Retail Sec. Breach Litig., 584 F. Supp. 2d 395, 404 (D. Mass. 2008).

settlements on a per claim basis, instead of paying the entire amount upfront to a common fund.[120]

While using the percentage of the fund actually recovered may have benefits for consumers, it might also lead to more unfairness. As one district court warned, "To the extent attorney's fee awards are determined using the percentage of recovery method, the recovery and, therefore, the attorney's fee award is exaggerated by *cy pres* distributions that do not truly benefit the plaintiff class."[121] In other words, if class counsel can show that the remainder of the fund was distributed to a charitable organization that at least ostensibly benefits the class, a court is more likely to affirm its disproportionate request for attorneys' fees. Some have argued that if the *cy pres* method were not used to distribute unclaimed funds, "the size of the attorneys' fee[ ]might well be far smaller. This is especially true when the *cy pres* relief is established by judicial order or class settlement ex ante."[122]

While these arguments may be meritorious in some situations, they only apply where the percentage-of-fund method is used to determine appropriate fees, a practice that has been consistently rejected by appellate courts.[123] Namely, the two federal circuit courts that see many consumer class actions, especially in the securities litigation context – the Second and Ninth Circuits – have overturned district courts that use the amount of actual claims made against the fund, "rather than on the entire Fund created by the efforts of counsel," as the comparative amount.[124] Using the total fund approach taken by the Eighth Circuit reduces the issues with attorneys' fees created by a percentage-of-fund approach.

C. Cy Pres *Leads to Poor Selection of the "Next Best" Plaintiff*

When individual distributions are not feasible, a court applying the *cy pres* doctrine to distributions of the remainder of the fund is left trying to ascertain a recipient that would indirectly benefit the members of the class.[125]

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120. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 13:7; *see also TJX*, 584 F. Supp. 2d at 410 (stating that in the future the court would award attorneys' fees based on a claims made basis).

121. SEC. v. Bear, Stearns & Co., 626 F. Supp. 2d 402, 415 (S.D.N.Y. 2009).

122. Redish et al., *supra* note 99, at 619.

123. Masters v. Wilhelmina Model Agency, Inc., 473 F.3d 423, 436–37 (2d Cir. 2007); Williams v. MGM–Pathe Comm'ns Co., 129 F.3d 1026, 1027 (9th Cir. 1997) ("We conclude that the district court abused its discretion by basing the fee on the class members' claims against the fund rather than on a percentage of the entire fund . . . ." (footnote omitted)).

124. *Masters*, 473 F.3d at 436–37; *Williams*, 129 F.3d at 1027 ("We conclude that the district court abused its discretion by basing the fee on the class members' claims against the fund rather than on a percentage of the entire fund . . . ." (footnote omitted)).

125. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:32 ("The class action analogy is strained but works by assuming that the court, as when it redirects a

Many courts denying the use of *cy pres* have done so based on the inaccurate tailoring of a *cy pres* recipient.[126] Despite the attention paid by circuit courts to the issue, when deciding where the money *should* go, courts are left without "clear guidelines for identification and selection of recipients."[127] This process alone is often very expensive for litigants and the court.[128]

Some have argued that this inability to *ever* appropriately approximate the interests of the class is a reason for courts to deny class certification in the first instance.[129] Judge Richard Posner, writing for the Seventh Circuit, warned that the use of *cy pres* may divorce the purpose of litigation generally, to compensate those injured, with a purely punitive goal: to ensure that anyone but the defendant ultimately receives unclaimed funds.[130] By effectively allowing the abandonment of the compensatory model, *cy pres* works to "coercively transfer the defendant's money not as a form of compensation for injuries suffered but as a form of punishment."[131] However, the underlying substantive law often warrants no such application.[132] If the purpose of class action litigation is solely compensatory, courts should deny class certification in cases where there is a high likelihood of low claim rates.[133] Alternatively,

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settlor's money from one set of beneficiaries to another, is simply redirecting money from one set of beneficiaries (absent class members) to an entity whose interests lie 'as near as possible' to that group – namely, a charity working on issues related to the group's underlying causes of action – rather than have the monies revert to the defendant." (footnote omitted)).

126. *See, e.g.*, Powell v. Ga.-Pac. Corp., 119 F.3d 703, 706 (8th Cir. 1997); Dennis v. Kellogg Co., 697 F.3d 858, 866 (9th Cir. 2012) (holding that *cy pres* distribution of $5.5 million of food to the indigent was inappropriate because the distribution was "divorced from the concerns embodied in consumer protection laws"); Nachshin v. AOL, LLC, 663 F.3d 1034, 1041 (9th Cir. 2011) (reversing *cy pres* distribution to the legal aid foundation, the Boys and Girls Club, and the Federal Judicial Center Foundation because those organizations did not "have anything to do with the objectives of the underlying statutes on which Plaintiffs base their claims"); Travel Network Ltd. v. United Air Lines, Inc. (*In re* Airline Ticket Comm'n Antitrust Litig.), 307 F.3d 679, 682 (8th Cir. 2002) (reversing approval use of *cy pres* in an antitrust case where distributions of unclaimed funds were given to the National Association for Public Interest Law). *See also* NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:33.

127. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:34.

128. *Id.*

129. Redish et al., *supra* note 99, at 639–40.

130. Hughes v. Kore of Ind. Enter., 731 F.3d 672, 676 (7th Cir. 2013).

131. Redish et al., *supra* note 99, at 646.

132. *Id.* Professor Redish argues that this effect is not only unwise, but potentially unconstitutional. He notes that "[j]udicially authorized charitable donations that are neither recognized nor required by controlling substantive law lie well beyond the scope of the constitutionally ordained judicial function" because *cy pres* "contravenes the constitutional and political purposes served by the case-or-controversy requirement." *Id.* at 642.

133. *Id.* at 639–40 ("There is, of course, a fourth alternative that often seems to go unnoticed: simply denying class certification on the grounds that such a proceeding

if contemplation and application of *cy pres* do not occur until later, after initial distributions have failed to exhaust the fund, courts should apply the doctrine and the nexus requirement very narrowly.[134]

However, these arguments fail to address the essential function that class actions play in litigating federal securities violations. Courts have long recognized the "utility and necessity" of class actions in the enforcement of securities violations.[135] Denying class certification where finding an appropriate recipient of residual funds is not likely would destroy the system of private attorneys general necessary to enforce securities violations.[136] In other words, for securities violations, the purpose of the class action mechanism is not purely compensatory, as it also serves a quasi-public function in the enforcement of federal securities laws.[137] In *Deposit Guaranty National Bank v. Roper*, the Supreme Court opined, "[A]ggregation of individual claims in the context of a classwide suit is an evolutionary response to the existence of injuries unremedied by the regulatory action of government."[138] For this reason, especially in the securities context, Rule 23(e) is construed liberally in favor of class certification.[139]

In this case, the Eighth Circuit appropriately applied the *cy pres* doctrine. It limited the zone of potential alternative plaintiffs and rejected the argument that the excess funds should go to a local legal aid organization because the litigation concerned a nationwide securities class action, a type of case that is rarely, if ever, handled by pro-bono legal aid institutions.[140] Instead, the court suggested a much more narrowly tailored recipient, an organization dealing specifically with SEC securities fraud.[141] In doing so, it approximated the interests of the class, the geographic scope, and the purpose of the underlying litigation as narrowly as possible, setting a precedent that will minimize the nexus requirement issue with *cy pres*.[142] However, while this

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would be unmanageable. Where compensation of individual victims in a manner contemplated by the underlying substantive law through use of the class action device is infeasible, the inexorable conclusion must be that resort to the class action procedure is improper.").

134. NEWBERG ON CLASS ACTIONS (5th ed.), *supra* note 2, § 12:33.

135. NEWBERG ON CLASS ACTIONS (4th ed.), *supra* note 110, § 22:1.

136. *Id.* ("The Securities and Exchange Commission (SEC), the agency primarily entrusted with the administration and enforcement of the federal securities laws, is not designed to provide compensation to injured investors for damages they have suffered. Private enforcement is necessary to afford relief to those investors injured by violations of the securities laws. The SEC and the judiciary have recognized that the class action may be the only meaningful and viable method by which securities investors may remedy their claims." (footnote omitted)).

137. *Id.*

138. Deposit Guar. Nat'l Bank v. Roper, 445 U.S. 326, 339 (1980).

139. *Id.* at 338–39.

140. Oetting v. Jacobson (*In re* BankAmerica Corp. Sec. Litig.), 775 F.3d 1060, 1064–66 (8th Cir. 2015), *reh'g and reh'g en banc denied* (Mar. 18, 2015).

141. *Id.* at 1067.

142. *Id.*

decision narrowed the use of *cy pres* in the Eighth Circuit, more steps can be taken to minimize both its causes and its negative effects.

D. A More Refined Way Forward: Initial Structuring for Cy Pres *Distributions*

In addition to using the total fund approach to class counsel compensation and taking a narrowly tailored approach when choosing a *cy pres* recipient, courts can take other steps to ensure distributions to class members are made as widely and efficiently as possible, oversee the compensation of class counsel, and determine, at the outset, the most appropriate "next best" recipient of the funds.

First, where a class is especially susceptible to low rates of distribution,[143] courts should require litigants to make provisions for residual class funds in the initial settlement agreement by refusing to approve class action settlements without such a provision.[144] In accordance with Federal Rule of Civil Procedure 23(e), "[a] district court 'can endorse a settlement only if the compromise is "fair, adequate, and reasonable."'"[145] In effect, "in approving a settlement, the court acts as a fiduciary for absent class members."[146] This finding is analyzed using four factors: (1) defendant's financial condition, (2) the complexity and expense of further litigation, (3) the amount of opposition to the settlement, and (4) the merits of the plaintiff's case weighed against the terms of the settlement agreement.[147] Courts already add additional factors and weigh them differently depending on the circumstances of the cases.[148] Adding a factor that considers how the proposed settlement agreement would address the distribution of residual funds would allow courts to deal with related issues at the outset.[149]

In an opinion issued roughly five months after its decision in *BankAmerica*, the Eighth Circuit spoke again on the issue of *cy pres* distribution, but in

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143. *See supra* Part III.

144. The district court in *BankAmerica* approved the settlement agreement at issue, which contained no language relating to a possible *cy pres* distribution; instead, the decision to apply *cy pres* was made after nearly eight years of attempted distribution to class members. *In re BankAmerica Corp. Sec. Litig.*, 775 F.3d at 1062 ("[C]lass counsel for the NationsBank Classes, appellee Green Jacobson, P.C., filed a motion to terminate the case with respect to the NationsBank Classes, to award class counsel $98,114.34 in attorneys' fees for work done after the distribution in December 2004, and to distribute *cy pres* the remainder of the 'surplus settlement funds' to three St. Louis area charities suggested by class counsel.").

145. NEWBERG ON CLASS ACTIONS (4th ed.), *supra* note 110, § 22:92 (quoting Eichenholtz v. Brennan, 52 F.3d 478, 482 (3d Cir. 1995)).

146. *Id.* at § 22:92 n.5.

147. Marshall v. NFL, 787 F.3d 502, 508 (8th Cir. 2015), *reh'g and reh'g en banc denied* (July 15, 2015).

148. NEWBERG ON CLASS ACTIONS (4th ed.), *supra* note 110, § 22:92.

149. *Id.*

a different context.[150] In *Marshall v. NFL*, a class action was brought on behalf of former professional football players against the National Football League ("NFL"), alleging false endorsement, violation of rights of publicity, and unjust enrichment.[151] After several years of litigation, the class counsel and NFL agreed to a complex settlement agreement under which "Common Good Entity, a non-profit organization" would be created and funded by the $42 million settlement the NFL would be obligated to pay over eight years.[152] The Common Good Entity would act as a charitable organization "dedicated to supporting and promoting the health and welfare of Retired Players and other similarly situated individuals."[153] The settlement agreement specified the exact and exclusive uses for which the money would be allocated, and any funds left from the settlement after ten years would revert back to the defendant specifically for charitable uses.[154] Unlike the settlement in *BankAmerica*, the settlement agreement in this case contained no provision for direct payment to individual class members, and no such distribution was ever made.[155] The district court approved the settlement agreement as "fair, reasonable, and adequate because it provided a 'direct[] benefit [to] those in whose name th[e] lawsuit was purportedly brought.'"[156]

The Eighth Circuit affirmed.[157] The court was careful to distinguish this holding from *BankAmerica*, noting that "[h]ere, we deal not with the *court's authority* to distribute unclaimed funds to a third party unrelated to the class but the *parties' ability* to decide how to best distribute funds recovered in a

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150. *Marshall*, 787 F.3d at 502.

151. *Id.* at 506.

152. *Id.* at 506–07. The complicated sixty-page settlement agreement contained several terms, including: "The establishment of the Licensing Agency; . . . [p]ayment of $100,000 worth of media value to the Licensing Agency each year until 2021; . . . [p]ayment of attorneys' fees and settlement administration expenses; . . . [a] reserve for the NFL's potential fees and costs of litigation involving class members who opt out of the settlement; and . . . [t]he class members' perpetual release of any claims and all their publicity rights for the NFL and its related entities to use." *Id.*

153. *Id.* at 507.

154. *Id.* The settlement agreement outlined the specific and exclusive uses for which the Common Good Entity could distribute funds:

> (1) medical research; (2) short-term and long-term housing; (3) health and dental insurance coverage; (4) medical screening and evaluations; (5) mental health programs; (6) wellness programs; (7) career transition programs; (8) any medical costs not covered by health insurance; and (9) other uses as approved by the Board of Directors of the Common Good Entity.

Id.

155. *Id.*

156. *Id.* (alterations in original) (quoting Dryer v. NFL, No. 09-2182, 2013 WL 1408351, at *1 (D. Minn. Apr. 8, 2013)).

157. *Id.* at 521.

class action for the benefit of the class."[158] Despite the differences, this case demonstrates two important things: first, that courts afford higher deference to private parties where the allocation of residual funds is made at the settlement approval stage and second, a potential model for structuring such agreements.

Further, courts can take additional practical steps to enhance the policies behind *cy pres* distributions. Like other aspects of the settlement agreement, courts have discretion in determining if the proposed methods of notifying absent class members are sufficient.[159] In the securities class action context, this should include mailed notice along with publication in the *Wall Street Journal*.[160] Additionally, requiring the initial settlement agreement to contain a plan for the distribution of residual funds via *cy pres*, even if it is never used, would allow class members to weigh in on possible appropriate charitable organizations before the approval is granted.[161] When *cy pres* is not considered until much later, class members do not have this ability as a matter of procedure.[162] In these situations, where *cy pres* is considered long after the initial settlement agreement is approved, requiring class counsel to create an opportunity for class members to weigh in on the potential recipient of residual funds might allow a more appropriate organization to prevail.

If district courts required class action litigants to determine a residual fund recipient and procedures for allocating such funds at the settlement agreement approval stage, the costs and inefficiencies created for courts and litigators by repeated motion practice and the accompanying oversight could be reduced. Additionally, the costs to the class in the form of class counsel claiming fees for work performed on the *cy pres* distribution itself could be eliminated. Finally, more input could be garnered from class members. The result would be that large, untapped settlement funds could be put to a better use more effectively and more quickly.

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158. *Id.* at 510.

159. NEWBERG ON CLASS ACTIONS (4th ed.), *supra* note 110, § 22:83.

160. *Id.* § 22:85; Weinberger v. Kendrick, 698 F.2d 61, 70 (2d. Cir. 1982) ("Here appellees . . . mailed individual notices, and, in addition, published notice of the class action and settlement in the *Wall Street Journal*. Some 26,000 proofs of claim have been filed as a result of these notice procedures. The district court, in its July 28, 1980, order, expressly found this procedure adequate and we see no reason to disturb its finding . . . ."); Harris v. Victor Tech. (*In re* Victor Techs. Sec. Litig.), 792 F.2d 862, 863 (9th Cir. 1986).

161. NEWBERG ON CLASS ACTIONS (4th ed.), *supra* note 110, § 22:91 ("Rule 23(e) requires that the class members be notified of the terms of the proposed settlement. Notice of a proposed settlement under Rule 23(e) must inform class members (1) of the nature of the pending litigation, (2) of the settlement's general terms, (3) that complete information is available from the court files, and (4) that any class member may appear and be heard at the Fairness Hearing.").

162. *Id.*

VI. CONCLUSION

Despite its potential benefits, courts often employ *cy pres* distribution as a means of distributing remaining class action settlement funds to anyone but the defendant. Because of the prevalence of unclaimed funds, courts have often relied on *cy pres*, in spite of its inability to actually compensate the true victims in the lawsuit. The Eighth Circuit, in deciding *In re BankAmerica Corp. Securities Litigation*, defined the practice narrowly by carefully considering the practice's two major pitfalls: overcompensation of class counsel and poor selection of a next best plaintiff. However, despite the appropriate narrowing of the *cy pres* doctrine, there are other things courts can do to perfect *cy pres*, such as: denying approval of class action settlements that do not contain a clear and specific plan for the distribution of residual fees, imposing mandatory notice requirements, and requiring input from class members on an appropriate recipient of the residual funds. Such an approach would minimize the inefficiency and ineffectiveness of class action *cy pres* distributions while allowing absent class members to receive an at least tangential benefit.