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# A New Generation of Class Action Cy Pres Remedies: Lessons from Washington State

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# A NEW GENERATION OF CLASS ACTION CY PRES REMEDIES: LESSONS FROM WASHINGTON STATE

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*Abstract*: The use of cy pres as a mechanism to distribute residual funds in class actions has become increasingly common and the subject of much controversy. In the class action context, cy pres is an equitable remedy used by courts to appropriate class action settlement funds remaining after all identified class parties have been compensated to the funds' "next best use," usually to a charity. The controversy has stemmed primarily from a lack of clear judicially enforced standards on how and when to use cy pres. In light of recent controversy, both the Federal Rules Committee, and potentially the Supreme Court, are now considering stepping-in to consider changes to the doctrine. While most of the debate has focused on the federal courts, some states have been codifying their own approaches to provide structure and guidance to courts in the use of cy pres. In 2006, Washington State passed a groundbreaking amendment to Civil Rule 23, requiring that at least twenty-five percent of residual class action funds go the Legal Foundation of Washington, a charity providing legal aid services to indigent persons in the State of Washington. This rule is representative of a larger state trend towards adopting statutory approaches to cy pres that promote legal aid charities as appropriate cy pres recipients. Focusing primarily but not exclusively on Washington, this Comment argues that states have been effective "laboratories of innovation" in reaching workable solutions to the residual funds dilemma in consumer class actions. These codified state approaches to cy pres have shown to be effective methods for selecting and approving cy pres awards that provide for appropriate relief while curbing improper incentives and bias in the cy pres selection process.

## INTRODUCTION

In 2013, AT&T agreed to pay $45 million to settle a class action lawsuit in Washington State.[1] The class action lawsuit alleged that AT&T failed to disclose call rates on collect calls placed by inmates in Washington State Department of Correction facilities.[2] The rate

1. Settlement Agreement at app. 1, Judd v. Am. Tel. & Tel. Co., No. 00-2-17565-5 SEA (King Cnty. Super. Ct., Wash. Jan. 22, 2013), *available at* https://www.documentcloud.org/documents/565824-appendix-1-cr2a-agreement-with-att.html; Matt Clarke, *Historic $45 Million Settlement in Washington State Prison Phone Class-Action Suit*, PRISON LEGAL NEWS, Mar. 2013, at 26; Jonathan Martin, Op-ed, *AT&T to Pay Washington Prisoners' Families $45 Million in Telephone Class Action Settlement*, SEATTLE TIMES–OPINION NORTHWEST (Feb. 3, 2013), http://blogs.seattletimes.com/opinionnw/2013/02/03/att-to-pay-washington-prisoners-families-45-million-in-telephone-class-action-settlement/.

2. Complaint – Class Action at 2, Judd v. Am. Tel. & Tel. Co., No. 00-2-17565-5 SEA (King Cnty. Super. Ct., Wash. June 29, 2000).

disclosure was required by law under Washington's Consumer Protection Statute, RCW Chapter 19.86.[3] The harms from AT&T's disclosure violations were accentuated by the fact that the rates for prison collect calls were quite high.[4] During the relevant time period, intrastate collect call rates from prisons in Washington State included a $3.95 flat fee plus additional charges of $0.90 per minute, thus making a twenty-minute phone call $21.95.[5] The only way for inmates to make phone calls to family members and loved ones was by making these collect calls, and without disclosure of the associated charges, some recipients of these calls racked up more than $10,000 in collect call charges.[6] After years of bouncing back and forth between hearings before the Washington Utilities Commission, King County Superior Court, the Washington State Supreme Court, and back to superior court, the settlement brought to an end twelve years of litigation.[7] The settlement class was certified to include all persons who received a collect call from an inmate in a qualifying Washington State Department of Corrections facility between 1996 and 2000.[8] At the time of settlement, it was anticipated that between 70,000 and 172,000 individuals would be eligible for refunds from the settlement fund.[9]

The AT&T settlement illustrates a common problem encountered when resolving class actions. With such an expansive plaintiff class, and given the length of time over which the litigation took place, it would be nearly impossible today to track down every individual who received a phone call from an inmate during the relevant period—now more than ten years ago—in order to give them the recovery to which they are entitled.[10] Furthermore, the damages suffered by each individual class member were, on average, relatively minor. Each class member's

3. *Id.* at 5.

4. Class Counsel's Recommendations for Additional Cy Pres Awards, *Judd*, No. 00-2-17565-5 SEA (Mar. 26, 2014); Clarke, *supra* note 1, at 26.

5. Clarke, *supra* note 1, at 26.

6. *Id.*

7. Martin, *supra* note 1.

8. Complaint – Class Action, *supra* note 2, at 2.

9. Martin, *supra* note 1.

10. The length of time over which litigation occurred is often a factor affecting whether or not class members can be located for purposes of distributing settlement funds. *See, e.g.*, *In re* Paracelsus Corp. Sec. Litig., No. Civ.A. H-96-3464, 2007 WL 433281, at *2 (S.D. Tex. Feb. 6, 2007) (approving cy pres award in 2007 for residual funds remaining from class action settlement reached in 1999, because "[t]he record establishes that at this late date, it would not be feasible either to locate the class members who did not receive or cash the settlement checks when they were mailed or to allocate the undistributed amount to the individual class members who could be located years ago but whose present whereabouts may well be different").

recovery consisted only of the cost of all qualified collect calls accepted during the relevant time period, plus two hundred dollars in statutory damages.[11] Thus, the money spent tracking down potentially qualifying plaintiffs would eat away at, or perhaps entirely consume, the already small recovery. Complete distribution in this case was expected to be both administratively and financially infeasible. In fact, the parties anticipated at the time of settlement that nearly $20 million of the settlement amount would remain in uncollected residual funds.[12] What should be done with the money that cannot be distributed? The solution: Distribute the remaining funds through cy pres.

Cy pres, which means "as near as possible," is an equitable remedy that courts use to disburse class action settlement funds remaining after all identified class parties have been compensated, to the funds' "next best use," usually to a charity.[13] However, the use of cy pres as a mechanism to distribute residual funds in class action suits has been the subject of much controversy. The controversy stems from the fact that cy pres has been characterized by a surprising lack of judicially enforced standards. Without clear limits on when and how to use cy pres, it is feared that the appropriation of class funds to charitable recipients will become an instrument of abuse by self-interested judges and attorneys.[14] Cy pres distributions have been criticized for going to unrelated causes or causes with suspicious ties to attorneys and judges.[15] Others criticize cy pres for spurring inappropriate charitable lobbying, as needy, albeit worthy, charitable causes have begun soliciting parties and courts for cy pres awards.[16] Some commentators question whether the use of this

11. Settlement Agreement, *supra* note 1, at app. 2.

12. *Notice of Cy Pres Hearing in* Judd v. AT&T, WASH. STATE BAR ASS'N—NWSIDEBAR (July 3, 2013), http://nwsidebar.wsba.org/2013/07/03/judd-att-cy-pres-hearing/.

13. 4 WILLIAM B. RUBENSTEIN, NEWBERG ON CLASS ACTIONS § 12:32 (5th ed. 2011); *see also* Martin H. Redish et al., *Cy Pres Relief and the Pathologies of the Modern Class Action: A Normative & Empirical Analysis*, 62 FLA. L. REV. 617, 620 (2010) (noting that in recent times, "the term cy pres has generally referred to an effort to provide unclaimed compensatory funds to a charitable interest that is in some way related to either the subject of the case or the interests of the victims, broadly defined").

14. *See* Jennifer Johnston, Note, *Cy Pres Comme Possible to Anything Is Possible: How Cy Pres Creates Improper Incentives in Class Action Settlements*, 9 J.L. ECON & POL'Y 277, 290 (2013).

15. *See infra* Part II.C.

16. Sam Yospe, Note, *Cy Pres Distributions in Class Action Settlements*, 2009 COLUM. BUS. L. REV. 1014, 1027–28 (2009); Adam Liptak, *Doling Out Other People's Money*, N.Y. TIMES (Nov. 26, 2007), http://www.nytimes.com/2007/11/26/washington/26bar.html?_r=0&pagewanted=print (noting that former federal Judge David F. Levi was solicited by groups for cy pres funds); *see also infra* Part II.C.

doctrine is ever appropriate.[17]

The controversy over cy pres recently boiled over in response to a widely publicized class action settlement in *Lane v. Facebook, Inc.*[18] The case was a class action against Facebook for privacy violations as a result of Facebook's Beacon program.[19] The Beacon program operated by updating a Facebook user's online profile automatically with information about the user's activities on other participating websites—displaying such items as movie rentals from Blockbuster.com and online purchases from Overstock.com.[20] Facebook made it difficult for users to avoid the public broadcasting of their online activities by requiring users to affirmatively opt out of the program if they wanted to avoid these disclosures.[21]

The lawyers for the parties reached a settlement agreement for $9.5 million, and in lieu of any individual payments to class members, the settlement earmarked $6.5 million of the funds for cy pres distribution.[22] The cy pres award was to go to a newly created charity called the Digital Trust Foundation. Notably, a former Facebook executive was to serve on the three-person board of the Foundation, and the Foundation had no track record upon which to evaluate its legitimacy.[23] Media erupted with cries of foul play.[24] Not without controversy, the settlement was approved by the district court,[25] and affirmed by the Ninth Circuit in a two-to-one vote[26] with Judge

17. Liptak, *supra* note 16 (quoting Professor Samuel Issacharoff as saying, "I don't care how much good you want to do. Do it with your own money, not someone else's money"). Some commentators have even challenged cy pres on constitutional grounds. *See generally* Redish et al., *supra* note 13.

18. 696 F.3d 811 (9th Cir. 2012), *reh'g denied*, 709 F.3d 791 (9th Cir. 2013), *cert. denied sub nom.* Marek v. Lane, 571 U.S. __, 134 S. Ct. 8 (2013).

19. *Id.* at 816.

20. *Id.*

21. *Id.* at 827 (Kleinfeld, J., dissenting) (noting that Facebook required users to affirmatively opt out of the Beacon program, and describing the "video game skills" needed to notice and effectuate the opt out).

22. *Id.* at 816, 817 (majority opinion).

23. *Id.* at 829 (Kleinfield, J., dissenting).

24. Glenn G. Lammi, *Ninth Circuit Decision and Dissenters Cry out for SCOTUS Review on Cy Pres in Settlements*, FORBES (Feb. 28, 2013, 4:09 PM), http://www.forbes.com/sites/wlf/2013/02/28/ninth-circuit-decision-and-dissenters-cry-out-for-scotus-review-on-cy-pres-in-settlements/; Adam Liptak, *When Lawyers Cut Their Clients out of the Deal*, N.Y. TIMES (Aug. 12, 2013), http://www.nytimes.com/2013/08/13/us/supreme-court-may-hear-novel-class-action-case.html.

25. *Facebook*, 696 F.3d 811.

26. *Id.*

Kleinfield dissenting.[27] A petition for rehearing en banc was denied over the dissent of six judges.[28] In both decisions, the dissents sharply criticized the cy pres award and questioned the incentives behind Facebook and the lawyers who structured it.[29] It is easy to see why: With the settlement, Facebook purchased a release of all liability for claims from millions of affected consumers, without attempting to provide individual compensation, and while effectuating a charitable donation over which they retained significant control of the charity's objectives.

The settlement approval was appealed to the United States Supreme Court, which denied certiorari.[30] In a statement accompanying the denial of certiorari, Chief Justice Roberts supported the Court's decision not to review the case because he felt the *Facebook* case would likely not have provided the Court with the opportunity to answer the "fundamental concerns" surrounding cy pres remedies, "including when, if ever, such relief should be considered."[31] "Citing a law review article that criticized [cy pres] settlements . . . [Chief Justice Roberts] posed six questions, ending with 'and so on,' which implied that there was quite a bit more that he wanted to know."[32] It is clear that at least some members of the Supreme Court are looking skeptically at the class action cy pres remedy, and are poised and ready for the "right" case to weigh in on cy pres.[33]

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27. *Id.* at 826, 835 (Kleinfield, J., dissenting) ("The majority approves ratification of a class action settlement in which class members get no compensation at all. They do not get one cent. They do not get even an injunction against Facebook doing exactly the same thing to them again. Their purported lawyers get millions of dollars. Facebook gets a bar against any claims any of them might make for breach of their privacy rights. The most we could say for the cy pres award is that in exchange for giving up any claims they may have, the exposed Facebook users get the satisfaction of contributing to a charity to be funded by Facebook, partially controlled by Facebook, and advised by a legal team consisting of Facebook's counsel and their own purported counsel whom they did not hire and have never met.").

28. *Facebook*, 709 F.3d at 793 (M. Smith, Circuit Judge, with whom Kozinski, Chief Judge, and O'Scannlain, Bybee, Bea, and Ikuta, Circuit Judges, join, dissenting from the denial of rehearing en banc).

29. *Facebook*, 696 F.3d at 834 (Kleinfield, J., dissenting) ("A defendant may prefer a cy pres award to a damages award, for the public relations benefit. And the larger the cy pres award, the easier it is to justify a larger attorneys' fees award. The incentive for collusion may be even greater where, as here, there is nothing to stop Facebook and class counsel from managing the charity to serve their interests and pay salaries and consulting fees to persons they choose.").

30. Marek v. Lane, 571 U.S. __, 134 S. Ct. 8 (2013).

31. *Id.* at *4; *see also* Linda Greenhouse, Op-Ed., *Bring Me a Case*, N.Y. TIMES (Nov. 13, 2013), http://www.nytimes.com/2013/11/14/opinion/bring-me-a-case.html; Jessie Kokrda Kamens, *Supreme Court Won't Review Facebook Pact, But Chief Justice Shares Cy Pres 'Concerns,'* BLOOMBERG BNA (Nov. 12, 2013), http://www.bna.com/supreme-court-wont-n17179880036/.

32. Greenhouse, *supra* note 31.

33. *Id.*

But while most of the debate about when and how to use cy pres remedies has focused on the federal class action arena, states have been finding their own innovative ways of dealing with the residual funds dilemma. In 2006, Washington State became one of the first states to expressly codify cy pres as the preferred method for distributing residual class action funds by amending Washington's Civil Rule 23(f).[34] Washington's Civil Rule 23(f) requires that at least twenty-five percent of all residual class action funds be distributed to the Legal Foundation of Washington, the legal aid fund that administers Washington State's Interest on Lawyer's Trust Accounts (IOLTA)[35] program and provides civil legal aid to low-income individuals in Washington State.[36] Using Rule 23(f) as a framework, Washington State Superior Court Judge Beth Andrus in the *Judd v. AT&T* case used cy pres to distribute the large amount of residual funds left from the AT&T prison rate disclosure settlement.[37] In selecting cy pres recipients, the court solicited cy pres proposals and held extensive hearings.[38] Ultimately, Judge Andrus approved a significant cy pres award to the Legal Foundation of Washington to administer a grant program for a list of charities the judge certified as appropriate cy pres recipients.[39]

While Washington was one of the first states to codify an approach to cy pres, other states have followed in recent years and adopted similar

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34. Andrea D. Axel & David A. Leen, *Unclaimed Class Action Funds Offer Hope for Equal Justice*, WASH. ST. BAR NEWS, July 2007, at 24, 24; *see also* WASH. R. CIV. P. 23(f). Additions or amendments to court rules in the State of Washington are promulgated by the Washington State Supreme Court. *See* WASH. CT. GEN. R. 9.

35. Washington's IOLTA program mandates that "[a]ll client funds paid to any Washington lawyer or law firm must be deposited in identifiable interest-bearing trust accounts separate from any accounts containing non-trust money of the lawyer or law firm." Brown v. Legal Found. of Wash., 538 U.S. 216, 224 (2003). In Washington State, the IOLTA program was established by the Washington State Supreme Court under its authority to regulate the practice of law and is mandatory for all Washington lawyers. *Id.* at 223. "The State of Washington, like every other State in the Union, uses interest on lawyers' trust accounts (IOLTA) to pay for legal services provided to the needy." *Id.* at 220. "The Legal Foundation of Washington (Legal Foundation) was established by Order of the Supreme Court of Washington to administer distribution of Interest on Lawyer's Trust Account (IOLTA) funds to civil legal aid programs." 2 KARL B. TEGLAND, WASHINGTON PRACTICE SERIES, RULES PRACTICE, ENFORCEMENT OF LAWYER CONDUCT § 15.7(a) (8th ed.).

36. WASH. R. CIV. P. 23(f); *Inside LFW*, LEGAL FOUND. WASH., http://www.legalfoundation.org/pages/inside_lfw (last visited May 31, 2015).

37. *See* Order for Cy Pres Award for the Legal Foundation of Washington and Legal Services Organizations, Judd v. Am. Tel. & Tel. Co., No. 00-2-17565-5 SEA (King Cnty. Super. Ct., Wash. Sept. 25, 2013).

38. Order Setting Hearing Schedule to Consider Requests for Cy Pres Awards, *Judd*, No. 00-2-17565-5 SEA (June 26, 2013).

39. Order for Cy Pres Award for the Legal Foundation of Washington and Legal Services Organizations, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013).

measures.[40] The resulting trend in the states that have addressed cy pres has been towards recognizing legal aid charities as legitimate recipients of cy pres funds, while typically still allowing courts discretion in disbursing a portion of the residual funds.

Focusing primarily but not exclusively on Washington, this Comment argues that states have been effective "laboratories of innovation"[41] in reaching workable solutions to the residual funds dilemma in consumer class actions. This Comment examines various approaches to cy pres adopted and codified by states such as Washington, and notes several trends that have emerged among these codifications. This Comment argues that these state approaches have shown promise as effective methods for selecting and approving cy pres awards that provide for appropriate relief while curbing improper incentives and bias in the cy pres selection process.

Part I of this Comment discusses the origins of the cy pres doctrine. Part II examines the uneven application of cy pres in federal courts and the controversy it has engendered. Part III examines states' approaches to cy pres awards, and in particular, Washington State's approach. This Comment explores the *AT&T* settlement in depth as a mechanism for evaluating the application of Washington Civil Rule 23(f) in practice.

In Part IV, this Comment discusses alternatives to cy pres, and concludes that cy pres is the best solution to the residual funds dilemma. In Part V, this Comment argues that the main critiques of the cy pres doctrine stem from improper uses of the doctrine, not from inherent flaws in the doctrine itself, and as seen from state codifications of cy pres, that the doctrine can be constrained and applied in ways that provide actual and appropriate judicial relief. This Comment further suggests that the legal fiction implicit in cy pres has been misconstrued and argues that legal aid charities can qualify as appropriate cy pres recipients. Cy pres provides an important mechanism for access to justice and if applied with sufficient structural safeguards and standards, it can provide meaningful and proper relief.

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40. As of May 2015, sixteen states have adopted statutes or civil rules allowing for cy pres remedies in class actions.

41. As the United States Supreme Court has recognized, states have an interest in "serv[ing] as laboratories for innovation and experiment." Blakely v. Washington, 542 U.S. 296, 327 (2004) (Kennedy, J., dissenting); New State Ice Co. v. Liebmann, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) ("It is one of the happy incidents of the federal system that a single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country.").

## I. BACKGROUND: THE ORIGINS OF CY PRES AND ITS APPLICATION IN CLASS ACTIONS

### *A. The Origins and Meaning of Cy Pres*

Cy pres originally developed as an equitable doctrine in trust law to preserve charitable trusts whose original purpose had become frustrated.[42] The term "cy pres" comes from the phrase "*cy pres comme possible*," which is a French expression meaning "as near as possible."[43] Under this doctrine, when a charitable trust became impracticable or impossible to fulfill, for example if the original charitable recipient ceased to exist, courts could exercise their broad equitable powers to restructure the trust to distribute the funds to an entity that most nearly carried out the original testator's intent.[44] In order for courts to apply the cy pres doctrine to enforce a trust, the court must find: (1) that the gift constitutes a valid charitable trust; (2) that the gift has become impracticable or impossible to fulfill; and (3) that the testator, in effectuating the gift, expressed a general charitable intent.[45]

Cy pres in the class action concept differs slightly from its trust law origins. Class action cy pres is applied to distribute funds from class action settlement or awards to their next best use when direct distribution to class members has become impracticable or impossible.[46] This occurs in two primary situations. First, it has been used when all absent class plaintiffs that can be identified have been compensated, but residual funds remain for those absent class members who cannot be identified—or have been identified but have failed to cash their checks—rendering further distribution of funds to individual class members impossible.[47] Second, it has been used when the administrative costs of distributing the funds to individual class members outweighs the value of the individual awards, and would thereby consume the entirety of the fund, rendering individual distributions impracticable.[48] In these situations, courts have borrowed the "as near as possible" concept from

42. Redish et al., *supra* note 13, at 624.

43. *Id.*

44. *Id.* For further discussion on the origins and function of cy pres in trust law, see *id.* at 624–30.

45. *Id.* at 629.

46. *See* Lane v. Facebook, Inc., 696 F.3d 811, 819–20 (9th Cir. 2012), *reh'g denied*, 709 F.3d 791 (9th Cir. 2013), *cert. denied sub nom.* Marek v. Lane, 571 U.S. __, 134 S. Ct. 8 (2013); Johnston, *supra* note 14, at 282.

47. Johnston, *supra* note 14, at 282–83.

48. *Id.*

charitable trust cy pres to put the class funds to their "next best use."[49]

The use of cy pres remedies in the class action context can be traced to an influential student comment written in the early 1970s[50] suggesting that unclaimed class action funds could be used to indirectly benefit the class members.[51] Today, the doctrine is used to appropriate class action settlement funds to charitable organizations, ideally those with ties to the underlying merits of the lawsuit.[52] "In a class action the reason for a remedy modeled on cy pres is to prevent the defendant from walking away from the litigation scot-free because of the infeasibility of distributing the proceeds of the settlement . . . ."[53]

### *B. Standards for Applying Cy Pres in Class Action Suits*

Unlike trust law cy pres, class action cy pres has been characterized by a surprising lack of judicially enforced standards.[54] The current system has been criticized for being "ad hoc, unpredictable, and

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49. Yospe, *supra* note 16, at 1017.

50. Redish et al., *supra* note 13, at 631–32.

51. Stewart Shepherd, Note, *Damage Distributions in Class Actions: The Cy Pres Remedy*, 39 U. CHI. L. REV. 448, 464 (1972).

52. This Comment uses the term "cy pres" to refer to the judicial practice of providing residual class action funds to a charitable organization that is tied in some way to the interests of the individual class members. *See* Hughes v. Kore of Ind. Enter., Inc., 731 F.3d 672, 675 (2013); Redish et al., *supra* note 13, at 620 ("In more recent times . . . the term cy pres has generally referred to an effort to provide unclaimed compensatory funds to a charitable interest that is in some way related to either the subject of the case or the interests of the victims, broadly defined."). Some courts have occasionally used the terms "cy pres" and "fluid class recovery" interchangeably. 4 RUBENSTEIN, *supra* note 13, at § 12:32; Redish et al., *supra* note 13, at 620. However, "fluid class recovery," as used in this Comment, "refers to efforts to fashion relief to those who will be impacted by the defendant in the future, in an effort to roughly approximate the category of those who were injured in the past." Redish et al., *supra* note 13, at 620. This Comment treats cy pres and fluid class recovery as distinct terms. *See* 4 RUBENSTEIN, *supra* note 13, § 13:32 ("Courts and commentators often use the term "cy pres" and "fluid recovery" interchangeably, although as discussed elsewhere in the Treatise, the two concepts are distinct. Cy pres directs unclaimed funds to a charity; fluid recovery directs all or most of a fund to a group of individuals more or less similarly situated to the class members themselves. The classic fluid recovery case involved a taxi company overcharging customers, with the remedy being that the taxi company would prospectively undercharge customers in an equal amount; those benefiting from the undercharge were not precisely the same class as those who suffered from the overcharge—but they were close enough. The beneficiaries were not, however, a charity, as is a cy pres recipient.").

53. *Hughes*, 731 F.3d at 676.

54. 4 RUBENSTEIN, *supra* note 13, at § 12:34 ("Appellate courts have balked when it appears that the recipients are too closely tied to the lawyers or court, but they have not used that occasion to set forth any clear guidelines for identification and selection of recipients." (footnote omitted)); Goutam U. Jois, *The Cy Pres Problem and the Role of Damages in Tort Law*, 16 VA. J. SOC. POL'Y & L. 258, 259 (2008).

generally unprincipled."[55] The primary requirement under this doctrine is that there must be some connection—often called a "nexus"—between the interests of the class members and the proposed charitable recipient of the funds.[56] By requiring a nexus between the proposed use of the funds and the interests of the class members the intent is to ensure that the class members will indirectly benefit from the funds and thus, the funds will go to their "next best use."[57]

Some courts, in deciding whether to approve a cy pres award, look to several factors to determine whether the nexus requirement has been met. "In applying cy pres principles, it is appropriate for a court to consider (1) the objectives of the underlying statutes, (2) the nature of the underlying suit, (3) the interests of the class members, and (4) the geographic scope of the case."[58]

Aside from the nexus requirement, courts have not uniformly adopted many clearly defined rules for how and when to grant cy pres awards.[59] The American Legal Institute (ALI) recently put forth principles for how and when cy pres should be used, and suggests courts not only look to the nexus of the proposed charitable recipient, but also to other factors in deciding whether to approve a cy pres award.[60] The ALI's principles are written not to codify the existing state of the law, but to suggest best practices and make recommendations for change and reform.[61] Courts are in practice increasingly looking to these principles for guidance when awarding cy pres remedies.[62] The ALI proposed that a cy pres award is appropriate only if it is impossible or infeasible to distribute the

55. Jois, *supra* note 54, at 259.

56. 4 RUBENSTEIN, ET AL., *supra* note 13, at § 12:33 n.3 (noting that a nexus requirement, or something similar, has been required in courts in the First, Third, Fifth, Eighth, Ninth, Tenth, Eleventh, and D.C. Circuits); *see also* Dennis v. Kellogg Co., 697 F.3d 858, 865 (9th Cir. 2012).

57. *Dennis*, 697 F.3d at 865.

58. Diamond Chem. Co. v. Azko Nobel Chems. B.V., 517 F. Supp. 2d 212, 220 (D.D.C. 2007).

59. 4 RUBENSTEIN ET AL., *supra* note 13, at § 12:34 ("Appellate courts have balked when it appears that the recipients are too closely tied to the lawyers or court, but they have not used that occasion to set forth any clear guidelines for identification and selection of recipients." (footnote omitted)).

60. AM. LAW INST., PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 3.07 (2010) [hereinafter ALI'S PRINCIPLES].

61. *See The American Law Institute's New Principles of Aggregate Litigation*, 8 J.L. ECON. & POL'Y 183, 189 (2011) (statement of Sam Issacharoff); *Overview: Projects*, ALI, http://www.ali.org/index.cfm?fuseaction=about.instituteprojects (last visited May 31, 2015).

62. Karen Shanley, *The Institute in the Courts: Principles of the Law of Aggregate Litigation*, 34 THE ALI REP., no. 4, summer 2012, *available at* http://www.ali.org/_news/reporter/summer2012/07-institute-courts-aggregate-litigation.html.

funds to class members.[63] "If 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 class members."[64] The inquiry into whether a distribution is infeasible must be based primarily on whether "the amounts involved are too small to make individual distributions economically viable."[65] Courts have increasingly looked to these principles,[66] and have struck down proposed cy pres awards where counsel has failed to show that compensating class members directly was not possible or economically practical.[67]

## II. CY PRES APPLIED TO CLASS ACTIONS IN FEDERAL COURT

Federal courts have struggled to apply the cy pres doctrine uniformly. The nexus requirement has been enforced in varying degrees by different courts, some even stating that it provides no restriction at all to the distribution of funds by the cy pres mechanism.[68] Some courts have been more willing than others to strike down proposed cy pres distributions when they find the nexus requirement is lacking.[69] The lack of a nexus between cy pres awards approved by courts and the underlying interests of the class members has been one of the primary criticisms of the doctrine in application.[70] Many commenters have argued that without limits on judicial discretion and without a strong, "driving nexus" between the interests of the class and the proposed charitable recipient of

63. ALI'S PRINCIPLES, *supra* note 60, at § 3.07.

64. *Id.* § 3.07(a).

65. *In re* BankAmerica Corp. Sec. Litig., 775 F.3d 1060, 1063–64 (8th Cir. 2015) (quoting ALI'S PRINCIPLES, *supra* note 60, § 3.07(a)).

66. *See, e.g.*, *In re* Lupron Mktg. & Sales Practices Litig., 677 F.3d 21, 38 (1st Cir. 2012) (citing ALI'S PRINCIPLES, *supra* note 60, § 3.07 in reviewing cy pres award).

67. *See, e.g.*, *id.* at 1064–65 (striking down proposed cy pres award because class counsel failed to show that further distributions to class members were not feasible, adopting ALI's Principles of Aggregate Litigation § 3.07); *see also* Shanley, *supra* note 62 (citing cases).

68. *See* Jois, *supra* note 54, at 261; Yospe, *supra* note 16, at 1023 n.35.

69. *See* Nachshin v. AOL, LLC, 663 F.3d 1034, 1038–39 (9th Cir. 2011) ("Some courts appear to have abandoned the 'next best use' principle implicit in the *cy pres* doctrine. These courts have awarded *cy pres* distributions to myriad charities which, though no doubt pursuing virtuous goals, have little or nothing to do with the purposes of the underlying lawsuit or the class of plaintiffs involved."); Yospe, *supra* note 16, at 1024–25.

70. *See, e.g.*, *Nachshin*, 663 F.3d at 1038 ("However, as a growing number of scholars and courts have observed, the *cy pres* doctrine—unbridled by a driving nexus between the plaintiff class and the *cy pres* beneficiaries—poses many nascent dangers to the fairness of the distribution process."); Yospe, *supra* note 16, at 1023.

the funds, the doctrine creates improper incentives for judges, lawyers, and charities to distribute funds not for the benefit of the class members, but rather to further their own personal interests.[71]

Many courts, wrestling with whether to approve particular cy pres distributions, have come to different conclusions about how closely related a charity must be to the interests of the class members in order to satisfy the nexus requirement.[72] This Part briefly addresses two general approaches to the nexus requirement: first, that some courts apply the nexus requirement strictly as a firm limitation on the distribution of cy pres, and second, that some courts apply the nexus requirement more liberally.

### *A. Some Federal Courts Have Implemented a Strict Interpretation of the Nexus Requirement*

Some courts, such as the Ninth Circuit, have expressed a greater skepticism towards the use of cy pres awards for the disbursement of residual funds in class action settlements, and have been more willing to strike down proposed cy pres distributions when they stray far from the nexus requirement.[73] The Ninth Circuit has developed guidelines for reviewing the appropriateness of cy pres proposals, and has repeatedly struck down cy pres proposals that fail to meet its guidelines.[74] The Ninth Circuit has required that cy pres awards, in order to be appropriate, must "(1) address the objectives of the underlying statutes, (2) target the plaintiff class, [and] (3) provide reasonable certainty that any member will be benefitted."[75]

In *Dennis v. Kellogg Co.*,[76] the Ninth Circuit struck down a proposed

71. Johnston, *supra* note 14, at 278–79; Yospe, *supra* note 16, at 1027.

72. *See* Hughes v. Kore of Ind. Enter., Inc., 731 F.3d 672, 676 (7th Cir. 2013) (acknowledging disagreement among courts as to whether there must be an indirect benefit to the class members from the cy pres award). *Compare* Jones v. Nat'l Distillers, 56 F. Supp. 2d 355, 359 (S.D.N.Y. 1999) (upholding a cy pres award to a legal aid organization, and acknowledging that the tie between the charity and the class members was weak), *with* Dennis v. Kellogg Co., 697 F.3d 858, 865–68 (9th Cir. 2012) (holding proposed cy pres distribution to charities feeding the indigent was improper because the nexus requirement was not met).

73. *See, e.g.*, *Dennis*, 697 F.3d at 865–68. While this section focuses on cases from the Ninth Circuit, this more scrutinizing approach has also been applied in other jurisdictions. *See, e.g.*, *In re* Airline Ticket Comm'n Antitrust Litig., 307 F.3d 679 (8th Cir. 2002) (holding that distribution of unclaimed funds via cy pres did not meet the geographic scope of the class and was not tied to underlying substance of lawsuit and was therefore improper).

74. *See, e.g.*, *Dennis*, 697 F.3d at 865–68; *Nachshin*, 663 F.3d at 1040; Six (6) Mexican Workers v. Ariz. Citrus Growers, 904 F.2d 1301 (9th Cir. 1990).

75. *Nachshin*, 663 F.3d at 1040.

76. 697 F.3d 858 (9th Cir. 2012).

cy pres award for failing to satisfy the nexus requirement.[77] The case was a class action suit against Kellogg, alleging the company's advertising claims that Frosted Mini-Wheats cereal would improve children's attentiveness nearly twenty percent were false and in violation of state consumer protection laws.[78] The parties reached a settlement agreement, which established a claims fund where class members could submit claims and seek reimbursement for boxes of cereal purchased up to $15, and provided that any funds remaining after all claims were made would be distributed in a cy pres award to unspecified "charities that feed the indigent."[79] The Ninth Circuit struck down the proposed settlement agreement, holding that under the nexus requirement, an appropriate cy pres recipient would be an organization redressing injuries caused by false advertising, not a charity related generally to food.[80] In doing so, the Court reiterated that in order for a cy pres distribution to be proper, there must be "a driving nexus between the plaintiff class and the cy pres beneficiaries."[81] The court also warned of the dangers that may result when the cy pres distribution is not tied to the interests of the class members, namely, that the cy pres distribution is likely to support the self-interests of the class counsel or the court.[82]

In another Ninth Circuit class action, *Nachshin v. AOL, LLC*,[83] the court similarly struck down a proposed cy pres distribution that was part of a class action settlement because the selected recipients, legal aid organizations in the Los Angeles area, failed to target the broad interests of the nationwide class.[84] Other circuits have similarly rejected proposed cy pres distributions when finding the nexus requirement not strictly met.[85]

77. *Id.* at 866–67.

78. *Id.* at 862.

79. *Id.* at 862–63.

80. *Id.* at 867.

81. *Id.* at 865 (quoting Nachshin v. AOL, LLC, 663 F.3d 1034, 1038 (9th Cir. 2011)).

82. *Id.* at 867.

83. 663 F.3d 1034 (9th Cir. 2011).

84. *Id.* at 1041.

85. *See In re* Lupron Mktg. & Sales Practices Litig., 677 F.3d 21, 33 (1st Cir. 2012) (adopting "reasonable approximation test" which requires cy pres recipient's interests to "reasonably approximate those being pursued by the class" (quoting ALI'S PRINCIPLES, *supra* note 60, § 3.07(c))); *In re* Airline Ticket Comm'n Antitrust Litig., 268 F.3d 619, 626 (8th Cir. 2001) (remanding for cy pres distribution more closely related to underlying merits of lawsuit).

### *B. Some Federal Courts Have Applied the Nexus Requirement Liberally*

While some courts have adhered to a strict interpretation of the nexus requirement, other courts have interpreted the cy pres doctrine's requirements more liberally. A recent example of this method was articulated in the Seventh Circuit's decision in *Hughes v. Kore of Indiana Enterprise, Inc*.[86] In *Hughes*, Judge Posner stated that a lack of a nexus connecting the interests of the class members to the proposed cy pres recipient is not fatal to the approval of the cy pres award.[87] "When there's not even an indirect benefit to the class from the defendant's payment of damages, the cy pres remedy . . . is purely punitive. But we said in *Mirfasihi* that the punitive character of the remedy would not invalidate it."[88]

In *Jones v. National Distillers*,[89] the District Court for the Southern District of New York approved a cy pres distribution of residual funds to the Legal Aid Society Civil Division, providing legal aid in civil matters.[90] The underlying suit was a securities fraud class action.[91] The court found that traditional cy pres principles were not instructive in this case because there was no obvious use of the funds that would provide a clear benefit to class members.[92] The court upheld the cy pres award anyways, holding that

> [t]he absence of an obvious cause to support with the funds does not bar a charitable donation . . . . In recent years, the doctrine appears to have become more flexible . . . . While use of funds for purposes closely related to their origin is still the best cy pres application, the doctrine of cy pres and courts' broad equitable powers now permit the use of funds for other public interest purposes by educational, charitable, and other public service organizations.[93]

The court further justified the cy pres award by acknowledging there was at least a thin tie to the interest of class members because the legal

86. 731 F.3d 672 (7th Cir. 2013).

87. *Id.* at 676.

88. *Id.* (citing Mirafasihi v. Fleet Mortg. Corp., 356 F.3d 781, 784–85 (7th Cir. 2004)).

89. 56 F. Supp. 2d 355 (S.D.N.Y. 1999).

90. *Id.* at 359.

91. *Id.* at 358.

92. *Id.*

93. *Id.* at 359.

aid organization was assisting individuals with civil legal matters.[94] In approving this particular cy pres award as appropriate, the court acknowledged that nonprofit legal services are appropriate cy pres recipients when the interests of class members are difficult to target with a particular organization.[95] In *Superior Beverage Co. v. Owens-Illinois, Inc.*,[96] the District Court for the Northern District of Illinois used similar reasoning to uphold cy pres distributions to fourteen organizations, including legal aid organizations and law school programs.[97]

Most courts seem to agree that some tenable connection to the merits of the underlying class action, or to the interests of the class members generally, must be present in order to approve a cy pres award. However, courts lack clear standards for how close a charitable cause must be or how to determine when a charitable cause becomes too attenuated from the merits of the suit. As a result of the wide discretion courts have in policing these connections, approved cy pres awards span a range of causes with varying degrees of connection to the underlying class action. The lack of uniformity in the system for selecting and approving these awards has left cy pres doctrine vulnerable to attack and fostered ripe grounds for criticism and controversy.

### *C. Criticism of Class Action Cy Pres Awards*

Without effective restraints on judicial discretion, and without uniform adherence to guiding principles on its use, scholars—and even some courts—have heavily critiqued cy pres. These attacks focus on questionable cy pres awards to identify two types of issues with the use of cy pres: first, the improper structural incentives cy pres distributions create,[98] and second, the potential conflicts of interest involved in nominating and approving charitable recipients.[99]

#### *1. Improper Structural Incentives and Cy Pres Awards*

One common argument made by the opponents of cy pres is that it alters the structure of incentives for class counsel in ways that may be harmful for the class. These scholars argue that the doctrine improperly

94. *Id.*

95. *Id.*

96. 827 F. Supp. 477, 480–87 (N.D. Ill. 1993).

97. *Id.* at 480–87.

98. *See, e.g.*, Yospe, *supra* note 16, at 1035.

99. *See, e.g.*, Rhonda Wasserman, *Cy Pres in Class Action Settlements*, 88 S. CAL. L. REV. 97, 117–24 (2014).

incentivizes plaintiffs' attorneys to propose cy pres distributions rather than continue to attempt to give the money to yet unfound class members.[100] Because courts include cy pres awards as part of the class recovery for purposes of calculating the amount of attorney's fees, the attorneys will be paid whether the funds go to class members or to a third party through cy pres.[101] The fear is, therefore, that attorneys will be "disincentiviz[ed] . . . in their efforts to assure the class-wide compensation of victims of the defendant's unlawful behavior."[102]

One scholar who has advanced this argument, Martin Redish, notes that "in a quarter of cy pres class actions, the amount and recipient of the cy pres award was determined *ex ante*, or prior to giving absent class members the opportunity to make claims on the fund."[103] The concern is not only that attorneys will be disincentivized from tracking down class members, but that attorneys will use cy pres as a method to artificially "exaggerate" the settlement award for their own benefit.[104]

In a recent decision the Eighth Circuit Court of Appeals held a cy pres distribution was inappropriate because the district court had not sufficiently considered whether the money could be used to further track down and compensate class members.[105] In the case, class counsel had already administered a second round of direct disbursements to class members; the court found this to be evidence that further distributions

100. Johnston, *supra* note 14, at 290.

101. Redish et al., *supra* note 13, at 659–61.

102. *Id.* at 666.

103. *Id.* at 661.

104. *Id.* at 661; Theodore H. Frank, *Cy Pres Settlements*, CLASS ACTION WATCH (Federalist Soc'y, Wash. D.C.), Mar. 2008, at 1, 21 ("[S]ometimes cy pres is less a matter of being punitive and more a matter of disguising the true cost of a settlement to the defendant to maximize the share of the actual recovery received by the plaintiffs' attorneys. If the beneficiary is related to the defendant, or the defendant otherwise benefits from the payout, then the contingent attorneys' fee can be exaggerated by claiming that the value to the class is equal to nominal value of the payment . . . ."). Some critics go so far as to say the entire doctrine is *primarily* a sham way to increase attorney's fees. *See, e.g.*, JOHN BEISNER ET AL., U.S. CHAMBER INST. FOR LEGAL REFORM, A ROADMAP FOR REFORM: LESSONS FROM EIGHT YEARS OF THE CLASS ACTION FAIRNESS ACT 4 (2013) ("In other words, cy pres is employed *primarily* to justify attorneys' fees by inflating the size of the "award," even though the award goes to charity, not the class members." (emphasis added)). Such claims seem exaggerated as cy pres is often used to appropriate residual funds, and because courts have ways to reduce attorneys' fees that appear excessive. *See* Wilber H. Boies & Latonia Haney Keith, *Class Action Settlement Residue and Cy Pres Awards: Emerging Problems and Practical Solutions*, 21 VA. J. SOC. POL'Y & L. 267, 277 (2014) ("[C]ourts have procedures in place to evaluate the reasonableness of attorneys' fees, and if necessary, the power to decrease a requested fee award where there is 'reason to believe that counsel has not met its responsibility to seek an award that adequately prioritizes direct benefit to the class.'" (internal citation omitted)).

105. *In re* BankAmerica Corp. Sec. Litig., 775 F.3d 1060, 1065 (8th Cir. 2015).

were feasible despite counsel's conclusory allegations to the contrary.[106] The Eighth Circuit held that the "district court erred in finding that further distributions would be so 'costly and difficult' as to preclude a further distribution; that inquiry must be based primarily on whether 'the amounts involved are too small to make individual distributions economically viable.'"[107] The court invalidated the attorney's fee award associated with the improper cy pres award.[108] These cases illustrate the risk cy pres creates that attorneys may rush into making cy pres awards instead of working further to compensate class members.

In *In re Baby Products Antitrust Litigation*,[109] objectors appealed the district court's approval of a $35 million settlement of which only $3 million was to be distributed to class members, while about $14 million was to go to class counsel in attorneys' fees and expenses and approximately $18.5 million, less administrative expenses, was destined for cy pres recipients.[110] The objector asserted that the cy pres award was inappropriate because it would occur despite the fact that class members would still not be fully compensated for their losses.[111] The Third Circuit Court of Appeals agreed; it vacated the lower court's approval and remanded for consideration of whether, in light of the large cy pres award and the fact that some class members would be undercompensated, the class was actually benefitted in this settlement.[112] On remand, the parties restructured the settlement to provide for further identification of, and direct payments to, class claimants.[113]

### *2. Conflicts of Interest and Cy Pres Awards*

Another frequent critique of cy pres is that it creates conflicts of interest for the judges and class counsel that participate in the selection of cy pres recipients. One frequent argument is that by giving judges too

106. *Id.* at 1064.

107. *Id.* at 1065 (quoting ALI'S PRINCIPLES, *supra* note 60, § 3.07(a)).

108. *Id.* at 1068.

109. 708 F.3d 163 (3d Cir. 2013).

110. *Id.* at 169–70.

111. *Id.* at 174–75 (noting objector's argument that because one subclass of plaintiffs under the settlement would receive only a five dollar payout—regardless of the price they paid for their defective product—those class members would by design not be fully compensated for their losses).

112. *Id.* at 170.

113. *See* Opening Brief of Appellants Theodore H. Frank, Kathleen McNeal, and Alison Paul at 42, Pearson v. NBTY, Inc., No. 14-1198 (7th Cir. Apr. 2, 2014) (citing Motion for Preliminary Approval of Third Amended Settlement, for Certification of Settlement Classes, and for Permission to Disseminate Class Notice, McDonough v. Toys 'R' Us, Inc., No. 2:06-cv-0242-AB (E.D. Pa. Dec. 18, 2013) (No. 847)).

much discretion in approving cy pres proposals, the doctrine creates an incentive for judges to approve charitable cy pres distributions based upon their own personal interests.[114] This was the objection raised by petitioners in *Nachshin v. AOL, LLC*.[115] *Nachshin* involved a class action by 66 million AOL subscribers for wrongfully inserting promotional messages into the footers of emails sent by AOL subscribers.[116] The maximum recovery at trial was statutorily capped at the amount of the unjust enrichment AOL received from the footer advertisements: $2 million.[117] As direct payments to class members would only be about three cents each, individualized distribution would be cost-prohibitive.[118] Instead, the parties agreed to a series of cy pres awards to various charities.[119] The district court, at the parties' request, suggested three charitable recipients to which the parties agreed.[120] Objectors challenged the cy pres award to the Legal Aid Foundation of Los Angeles, on the grounds that it was improper because the judge's husband sat on the board of the foundation.[121] The court of appeals held it was not error for the judge to not recuse herself from this cy pres decision, but invalidated the cy pres awards on other grounds.[122] Regardless of whether this was truly a conflict of interest for the particular judge in *Nachshin*, the appearance of bias has been used as an example showing the potential for abuse.[123]

This concern about judicial conflicts of interest is furthered by the fact that cy pres doctrine has caused charities to essentially lobby class counsel and the court for awards of funds. Some judges have in fact acknowledged that they have been approached by charities for this

114. Johnston, *supra* note 14, at 287; Wasserman, *supra* note 99, at 124–25; Yospe, *supra* note 16, at 1028.

115. 663 F.3d 1034 (9th Cir. 2011).

116. *Id.* at 1036.

117. *Id.* at 1037.

118. *Id.*

119. *Id.*

120. *Id.*

121. *Id.* at 1037–38.

122. *Id.* at 1040, 1042 (invalidating cy pres awards because "none of the cy pres donations—$25,000 each to the Legal Aid Foundation of Los Angeles, the Boys and Girls Clubs of Santa Monica and Los Angeles, and the Federal Judicial Center Foundation—ha[d] anything to do with the objectives of the underlying statutes on which Plaintiffs base[d] their claims" and because the awards also "[did] not account for the broad geographic distribution" of the nationwide class).

123. *See* Wasserman, *supra* note 99, at 124–25 & nn.116 & 118 (citing *Nachshin* to illustrate the argument that cy pres creates an appearance of judicial impropriety).

purpose.[124] Concerns raised over this effect are twofold. First, as charities lobby judges for cy pres funds, the concern is that judges will be persuaded to improperly award funds to one of these organizations, regardless of whether the funds truly represent the "next best use" for the particular case.[125] Second, critics have argued that the interjection of third parties in this way fundamentally alters the bilateral adversarial structure of the civil justice system for class actions.[126] The argument is that by putting judges in the position of acting as charitable grantors this new role "lie[s] well beyond the scope of the constitutionally ordained judicial function."[127]

Another major critique is that cy pres awards incentivize attorneys for either side to further their own personal interests, rather than the interests of the class members, in selecting cy pres recipients.[128] One case that has been used as an example of such abuse is *Diamond Chemical Co. v. Akzo Nobel Chemicals, B.V.*,[129] in which a court approved a cy pres award to George Washington Law School to use in funding their clinical programs, including programs designed to enforce antitrust law.[130] This was heavily criticized because the cy pres recipient was recommended by class counsel, an alumnus of the law school, who was later praised by the law school for the donation and admitted to the school's prestigious gift society as a result of the cy pres award to the school.[131]

Another example of the conflicting interests between attorneys and the class members in selecting cy pres recipients is the *Lane v. Facebook, Inc.*[132] settlement. While the parties reached a settlement in the amount of $9.5 million, $3 million was to be distributed to class counsel in costs and fees.[133] The parties agreed to distribute the remaining funds though cy pres to a new foundation the parties created

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124. *See ALI's New Principles of Aggregate Litigation*, *supra* note 61, at 200 (discussion by drafters of ALI's *Principles of Aggregate Litigation* on the subjects considered in reformulating this newest edition; participants: Sam Issacharoff, Judge Carolyn Kuhl, Francis McGovern, and Stephanie Middleton; Moderator: John Beisner); Yospe, *supra* note 16, at 1035–36; Liptak, *supra* note 16.

125. *See* Yospe, *supra* note 16, at 1036.

126. Johnston, *supra* note 14, at 294.

127. Redish et al., *supra* note 13, at 642.

128. *Id.* at 650.

129. 517 F. Supp. 2d 212 (D.D.C. 2007).

130. Johnston, *supra* note 14, at 292–93; Yospe, *supra* note 16, at 1028.

131. Johnston, *supra* note 14, at 292–93.

132. Lane v. Facebook, Inc., 696 F.3d 811, 816–17 (9th Cir. 2012), *reh'g denied*, 709 F.3d 791 (9th Cir. 2013), *cert. denied sub nom.* Marek v. Lane, 571 U.S. __, 134 S. Ct. 8 (2013).

133. *Id.* at 817.

in the settlement called the Digital Trust Foundation (DTF), the purpose of which was to fund and sponsor programs educating individuals on "critical issues relating to protection of identity and personal information . . . from online threats."[134] Most notably, Facebook's Director of Public Policy was to sit on the three-member board of directors.[135] In a controversial decision, the Ninth Circuit approved this cy pres award, despite the presence of a representative from defendant's company on the board and the nonexistent track record by which the court could judge the legitimacy of the organization.[136] The dissenting opinion noted that DTF could be, and likely would be, controlled for the benefit of the defendant Facebook, as there was "nothing to stop Facebook and class counsel from managing the charity to serve their interests and pay salaries and consulting fees to persons they choose."[137]

Regardless of how often the cy pres mechanism is actually manipulated by attorneys and judges who structure awards for their own personal benefit, the appearance of impropriety has been established by the publicity of these controversial cases.[138] Using these example cases, some scholars and judges question the doctrine in its entirety. Some courts have even expressed criticisms of the cy pres doctrine generally, questioning whether its use is ever appropriate. In *SEC v. Bear, Stearns & Co.*,[139] which was not a class action but rather a SEC enforcement action, the court discussed the cy pres doctrine in the class action context in dealing with the analogous issue of how to distribute remaining funds.[140] The court criticized other courts' application of cy pres for straying too far from the concept of "next best use" and the nexus requirement.[141] The court cautioned against the dangers in this practice and the appearance of impropriety on behalf of judges and counsel in approving cy pres awards to exaggerate attorney's fee awards and further personal interests.[142]

Some commentators and judges have raised constitutional concerns

134. *Id.*

135. *Id.*

136. *Id.* at 829 (Kleinfeld, J., dissenting).

137. *Id.* at 834 ("For all we know it will fund nothing but an 'educational program' amounting to an advertising campaign for Facebook. That would appear to satisfy the articles and bylaws, and Facebook, after all, together with class counsel and their nominees, will run it.").

138. *See, e.g.*, Liptak, *supra* note 24.

139. 626 F. Supp. 2d 402 (S.D.N.Y. 2009).

140. *Id.* at 411–17.

141. *Id.* at 414–15.

142. *Id.* at 415–16.

about the use of cy pres.[143] Most notably, this argument has been raised by Professor Martin Redish, who argues that cy pres alters the structural incentives so fundamentally that it violates due process and separation of powers principles.[144] In *Klier v. Elf Atochem North America, Inc.*[145] the Fifth Circuit rejected a proposed settlement agreement concerning a proposed cy pres distribution, holding instead that the funds should be distributed to the already identifiable class members.[146] In a strongly worded concurrence, Judge Edith Jones wrote a scathing critique of the cy pres and questioned the constitutionality of the doctrine on the same grounds.[147]

These example cases illustrate real concerns raised by the selection and approval of cy pres distributions. Whether or not these examples are common in practice or outliers, the appearance of impropriety these cases create is at least optically problematic and has created significant backlash to cy pres doctrine.

## III. CY PRES APPLIED TO CLASS ACTION SUITS IN STATE COURT

While much of the debate over the validity of cy pres as a mechanism for distributing class action funds has focused on the federal arena, many states have been finding working mechanisms for approaching cy pres. The Class Action Fairness Act[148] (CAFA) was enacted in 2005 with the express purpose of shifting class actions from the state courts to the

143. Recently the constitutionality of the cy pres remedy in class actions has come under attack on several grounds. *See* Redish et al., *supra* note 13, at 622–23; Klier v. Elf Atochem N. Am., Inc., 658 F.3d 468, 480–81 (5th Cir. 2011) (Jones, J., concurring). One criticism is that by compensating a third party, the underlying substantive law is enlarged in violation of the Rules Enabling Act. Redish et al., *supra* note 13, at 644–48. Another criticism is that introducing third parties as interested players in the compensatory structure of the class action runs counter to the bilateral structure of the legal system and renders disputes no longer a case or controversy under Article III. *Id.* at 642–44. Finally, the constitutionality is questioned on the grounds that by altering the incentives for judges and attorneys the procedure violates due process. *Id.* at 650–51. A direct rebuttal to these constitutional arguments is outside the scope of this Comment. However, other scholars have responded to—and rejected—these constitutional arguments. *See generally* Boies & Keith, *supra* note 104.

144. *See generally* Redish et al., *supra* note 13; *supra* note 143 and accompanying text. *But see generally* Boies & Keith, *supra* note 104 (arguing that the constitutional objections to cy pres are unfounded).

145. 658 F.3d 468 (5th Cir. 2011).

146. *Id.* at 475–77.

147. *Id.* at 480–82 (Jones, J., concurring).

148. Pub. L. No. 109-2, 119 Stat. 4 (2005).

federal courts.[149] CAFA operates by expanding federal diversity jurisdiction for class actions, and contains generous removal provisions for class actions filed in state court.[150] Initial data from a 2008 Federal Judicial Center report does show that class action filings in federal courts are up since the enactment of CAFA.[151] This data also notes an initial increase in diversity removals the year after CAFA, but that this trend in removals has been in decline since.[152]

However, class actions still remain an important mechanism for dispute resolution in state courts.[153] Plaintiffs continue to file class actions in state courts, and states that see these class action cases have been innovating new ways to approach the issue of residual fund distributions. Several states have codified rules governing the distribution of unclaimed funds in class action suits, expressly authorizing and structuring its use. Currently, sixteen states have adopted such measures.[154] The unifying trend among these codified approaches to cy pres is a recognition by the states that legal aid foundations are legitimate and appropriate cy pres recipients.[155]

Focusing primarily, but not exclusively, on Washington, this Part examines state approaches to cy pres. This Part begins by examining the approach adopted by Washington State. Next this Comment examines a

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149. Steven S. Gensler, *The Other Side of the CAFA Effect: An Empirical Analysis of Class Action Activity in the Oklahoma State Courts*, 58 KAN. L. REV. 809, 809 (2010).

150. *Id.*

151. EMERY G. LEE III & THOMAS E. WILLGING, FED. JUDICIAL CTR., THE IMPACT OF THE CLASS ACTION FAIRNESS ACT OF 2005 ON THE FEDERAL COURTS: FOURTH INTERIM REPORT TO THE JUDICIAL CONFERENCE ADVISORY COMMITTEE ON CIVIL RULES 1–2 (2008), *available at* http://www.fjc.gov/public/pdf.nsf/lookup/cafa0408.pdf/$file/cafa0408.pdf.

152. *Id.* at 7.

153. According to one informal study, class action filings in California state court exceeded filings in California federal court for both 2010 and 2011. Robert J. Herrington, *The Numbers Game:* Dukes *and* Concepcion, AM. BAR ASS'N (Nov. 20, 2012), http://apps.americanbar.org/litigation/committees/classactions/articles/fall2012-1112-numbers-game-dukes-concepcion.html (noting that the number of state courts class action filings in California was 1,821 in 2010, and 2,025 in 2011). A comprehensive study is currently underway in California by the California Office of Court Research in conjunction with the Hastings School of Law, however their data is currently available only through 2006. Hillary Hehman, *Highlights from the Study of California Class Action Litigation*, DATAPOINTS (Admin. Office of the Courts, Office of Court Research, S.F., Cal.), Nov. 2009, at 1, *available at* http://www.courts.ca.gov/documents/datapoints-classactionlit.pdf; *see also* Gensler, *supra* note 149, at 811.

154. As of May 2015, these states include: California, Hawaii, Illinois, Indiana, Kentucky, Louisiana, Maine, Massachusetts, Montana, New Mexico, North Carolina, Pennsylvania, South Dakota, Tennessee, and Washington. *See infra* notes 157, 199–216 and accompanying text. Additionally, at least one federal district court has adopted a local rule regarding the use of cy pres. *See* CONN. DIST. CT. LOCAL CIV. R. 23(b)

155. *See infra* Part III.C.

recent class action settlement in Washington State—the prison rate disclosure case of *Judd v. AT&T*—to see how the Washington State approach operates in practice. Finally in this Part, this Comment examines the various other approaches in states that have codified cy pres.

### *A. The Washington State Approach*

Washington was one of the first states to codify a specific rule on the distribution of residual funds in class action settlements.[156] In 2006, the Washington State Supreme Court codified the use of cy pres for disbursing residual funds, mandating that at least twenty-five percent of residual funds be given to the Legal Foundation of Washington (LFW), an organization providing legal aid to low-income individuals in the State of Washington.[157] The cy pres award funds are specifically to be used by the LFW "to support activities and programs that promote access to the civil justice system for low income residents of Washington State."[158] Beyond the mandatory twenty-five percent, Washington courts are free to distribute the remaining funds further to the LFW, or to causes that directly or indirectly further the substantive or procedural interests and objectives of the class members.[159] The Drafters' Comment to the 2006 amendment stated that the purpose of this proposed rule was to "codify and refine the judicially developed cy pres doctrine in a way that is consistent with its equitable purpose and which will serve the compelling interest in ensuring equal access to justice."[160]

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156. Axel & Leen, *supra* note 34, at 24.

157. WASH. R. CIV. P. 23(f) Disposition of Residual Funds:

(1) "Residual Funds" are funds that remain after the payment of all approved class member claims, expenses, litigation costs, attorneys' fees, and other court-approved disbursements to implement the relief granted. Nothing in this rule is intended to limit the parties to a class action from suggesting, or the trial court from approving, a settlement that does not create residual funds.

(2) Any order entering a judgment or approving a proposed compromise of a class action certified under this rule that establishes a process for identifying and compensating members of the class shall provide for the disbursement of residual funds. In matters where the claims process has been exhausted and residual funds remain, not less than twenty-five percent (25%) of the residual funds shall be disbursed to the Legal Foundation of Washington to support activities and programs that promote access to the civil justice system for low income residents of Washington State. The court may disburse the balance of any residual funds beyond the minimum percentage to the Legal Foundation of Washington or to any other entity for purposes that have a direct or indirect relationship to the objectives of the underlying litigation or otherwise promote the substantive or procedural interests of members of the certified class.

158. WASH. R. CIV. P. 23(f)(2).

159. *Id.*

160. 3A KARL B. TEGLAND, WASHINGTON PRACTICE SERIES, RULES PRACTICE, RULES FOR

### *B.* Judd v. AT&T*: A Washington Case Study*

A recent class action settlement in Washington illustrates the operation of Civil Rule 23(f) in practice, and demonstrates a creative approach by courts to fashion appropriate cy pres remedies. In *Judd v. AT&T*, plaintiffs brought a class action suit against defendant phone service providers for allegedly failing to disclose call rates on collect calls made from Washington prisons, as is required by law.[161] The class was comprised of individuals who received collect calls from prison inmates, including spouses and family members of prisoners.[162] The parties reached a $45 million settlement,[163] and after notice and reimbursement of identified class members, the parties expected that more than $20 million in residual funds would remain for cy pres distribution.[164]

In order to distribute cy pres awards in accordance with the requirements of Civil Rule 23(f), the court in *Judd v. AT&T* held a series of hearings to review, structure, and approve the cy pres awards. The court requested potential cy pres recipients to submit applications for cy pres awards from the residual settlement funds to the court, and scheduled a hearing to review and consider the applications for cy pres distributions.[165] In the notice announcing the pending consideration of cy pres distributions, the court encouraged a wide range of applicants meeting the requirements of 23(f) to apply.[166] In an attachment to the court's order, Superior Court Judge Beth Andrus, sitting for the court in this case, specified that acceptable cy pres applicants would include:

> [E]ntities that provide, directly or indirectly, educational, financial, or other assistance to (i) prisoners or former prisoners in Washington State, (ii) the family members of prisoners or former prisoners in Washington State, or (iii) any legal aid or services organization (or their umbrella organizations, including the Legal Foundation of Washington) operating exclusively or nearly exclusively in Washington State which provides

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SUPERIOR COURT 533 (6th ed. 2013).

161. Order Setting Hearing Schedule to Consider Requests for Cy Pres Awards at Ex. A, Judd v. Am. Tel. & Tel. Co., No. 00-2-17565-5 SEA (King Cnty. Super. Ct., Wash. June 26, 2013).

162. *Id.*

163. Settlement Agreement, *supra* note 1.

164. Order Setting Hearing Schedule to Consider Requests for Cy Pres Awards at Ex. A, *Judd*, No. 00-2-17565-5 SEA (June 26, 2013).

165. *Id.* at 1.

166. *Id.*

> educational, financial, or other services for prisoners or former prisoners in Washington State, or the family members of prisoners or former prisoners. However, any entity meeting the requirements of CR 23(f) should consider applying for an award. The ultimate decision regarding eligibility will be made by the Court.[167]

Applications specified the objectives of the charitable applicants, the applicants' proposed uses of the funds, and how those proposals related to the underlying objectives of the litigation.[168]

In response to this request, the court received forty-nine applications for cy pres awards.[169] In addition to seeking applications directly from possible cy pres recipients, both plaintiffs' counsel and defense counsel were given an opportunity to review these applications, to file recommendations for cy pres recipients to the court, and to object to opposing counsel's recommendations.[170]

The court reviewed the forty-nine applications received in accordance with this notice, and held a hearing where oral argument was given on the distribution of the funds.[171] The court then issued an initial order approving the disbursement of an estimated twenty-five percent of the residual funds ($5.5 million) to the LFW in accordance with the mandate in Civil Rule 23(f).[172] The court also approved a disbursement of $1 million to the Endowment for Equal Justice.[173] The Endowment for Equal Justice is a charitable endowment that provides civil legal aid funding for indigent residents of the State of Washington, and is partnered with the LFW, which makes annual grant distributions from the Endowment.[174]

As for the remaining residual funds, the court ordered them

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167. *Id.* at Ex. A.

168. *See, e.g.*, Application by Legal Foundation of Washington for Receipt of Residual Funds, *Judd*, No. 00-2-17565-5 SEA (Aug. 5, 2013).

169. Order for *Cy Pres* Award for the Legal Foundation of Washington and Legal Services Organizations at 1, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013).

170. Order Setting Hearing Schedule to Consider Requests for *Cy Pres* Awards, *Judd*, No. 00-2-17565-5 SEA (June 26, 2013).

171. Order for Cy Pres Award for the Legal Foundation of Washington and Legal Services Organizations, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013).

172. *Id.*

173. *Id.*

174. *The Endowment for Equal Justice*, CAMPAIGN FOR EQUAL JUST., https://c4ej.org/how-it-works/endowment-for-equal-justice/ (last visited May 3, 2015). The Endowment for Equal Justice is a 501(c)(3) nonprofit organization "that helps secure justice for future generations by providing a stable, permanent funding source for civil legal aid." *Id.*

distributed in cy pres awards to be administered through a grant program.[175] In its application for cy pres funds, the LFW requested the court to permit it to "manage, grant and oversee all such funds in order to ensure that the purposes of this cy pres award are carried out in an innovative, collaborative and sustainable approach, with the objective of assisting incarcerated persons, those recently released from institutions, and their families for many years to come."[176] Because of its existing grant program structure, and its years of experience in overseeing the effective use of funds granted to non-profit legal services in the state, the LFW proposed to manage and oversee the funds to ensure they would be put to use to further the underlying cy pres goals in a transparent and effective way.

The court ordered a further disbursement of funds to the LFW to distribute as grants, and provided a court-approved list of acceptable cy pres recipients consisting of "cy pres applicants that provide legal services."[177] The list included nineteen approved recipients, including several legal aid organizations, organizations advocating for the rights of prisoners, and clinical law programs at area law schools.[178] The court further directed that:

> The money awarded under this paragraph, and any interest or other income from those funds, shall only be used to make awards in accordance with this paragraph. In making these awards the LFW should be guided by the objectives of this case and the interests of class members, especially prisoners and their spouses, parents, and children.[179]

This provision of the order thus required the LFW to consider the relationship between the charity's mission and the interests of class members in making these grant awards. The court reserved the right to

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175. Order for Cy Pres Award for the Legal Foundation of Washington and Legal Services Organizations, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013).

176. Application by Legal Foundation of Washington for Receipt of Residual Funds, *supra* note 168, at 4.

177. Order for *Cy Pres* Award for the Legal Foundation of Washington and Legal Services Organizations, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013).

178. The list of approved recipients included: "(1) ACLU; (2) Alliance of People with disAbilities [sic]; (3) Center for Justice; (4) Columbia Legal Services; (5) Disability Rights Washington; (6) Gonzaga U. Legal Assistance; (7) Innocence Project NW; (8) King County Bar Foundation; (9) King County Bar Institute; (10) Legal Voice; (11) Northwest Consumer Law Center; (12) Northwest Immigrant Rights Project; (13) Pierce County Center for Dispute Resolution; (14) Seattle Community Law Center; (15) TeamChild; (16) The Public Justice Foundation; (17) Unemployment Law Project; (18) UW School of Law Clinical Law Program; (19) Washington Defender Assoc./SU School of Law." *Id.* at Ex. A.

179. *Id.* at 1.

review these distributions,[180] thereby providing some level of assurance that while a third party was to administer the distributions, they would be sure to manage the funds in a way that furthered the goals of the litigation.

The court repeated this application process later on after attempts to locate class members progressed, and more funds were identified as residual. On March 27, 2014, the court held a second round of hearings to consider applicants for cy pres awards.[181] The court made an additional award of funds to the LFW to use in accordance with the court's prior order.[182] In addition the court considered applications from twenty-one organizations, and made cy pres awards to eleven organizations, with specific instructions on the use of these funds, and made the awards subject to strict oversight and administration by the LFW.[183] The final residual fund amounted to $22,993,074.46.[184] The court made a final award to the LFW in January 2015 to issue cy pres grants to approved entities.[185] In doing so the court again reiterated strict limits on the use of the funds, including that the funds be used to "help facilitate communications between inmates and their families"; help "improve treatment of prisoners, particularly those with mental and physical problems, to enhance their ability to maintain ties with families"; and help recently released prisoners reunite with families.[186] The court limited the geographic scope of the awards to Washington State, and limited the awards to those organizations with "verifiable track record[s]."[187]

Today, the LFW still manages the AT&T cy pres award funds through a grant program. With the court's order, and distribution of funds, the LFW set up the Prison & Reentry Grant Program.[188] "Recipients of Prison & Reentry funds are fourteen non-profit organizations providing social services and legal advocacy for

180. *Id.* at 2.

181. *See* Order for Additional Cy Pres Awards, *Judd*, No. 00-2-17565-5 SEA (Apr. 23, 2014).

182. *See* Order Granting Unopposed Motion Regarding Additional Cy Pres Distributions and Payment of Expenses, *Judd*, No. 00-2-17565-5 SEA (Feb. 24, 2014).

183. *See* Order for Additional Cy Pres Awards, *Judd*, No. 00-2-17565-5 SEA (Apr. 23, 2014).

184. *See* Final Order for Distribution, *Judd*, No. 00-2-17565-5 SEA (Jan. 2, 2015).

185. *Id.* at 1–2.

186. *Id.* at 3.

187. *Id.*

188. Legal Foundation of Washington 2013 Report on Use of Cy Pres Funds at 1–2, *Judd*, No. 00-2-17565-5 SEA (Mar. 5, 2014); *Annual Public Report 2013*, LEGAL FOUND. OF WASH., http://www.legalfoundation.org/sites/legalfoundation/upload/filemanager/LFW-2013-Annual-Report-to-post.pdf (last visited May 3, 2015).

incarcerated people, their families and those recently released from prison."[189] These organizations were selected for cy pres grants from the list of court-approved organizations by the Board of Trustees of the LFW.[190] The Board looked to the criteria laid out by the court and counsel in approving these awards, ensuring that there was a link to the objectives of the case.[191]

The LFW makes information available about the use of these funds on its website and in yearly reports.[192] In accordance with the court's cy pres award order,[193] and the LFW's grant structure,[194] Prison & Reentry Grant Program grant recipients are required to provide LFW with yearly reports on their expenditures and cash flow, as well as narrative reports on how the funds were used, and how those expenditures furthered the goals of the program.[195] The monitoring and oversight provided by the LFW ensures that the funds are actually used for their intended purpose and that unused funds are properly identified, accounted for, and appropriated.[196] Thus, the LFW continues to monitor the use of the settlement funds to ensure that the cy pres funds are serving the

189. *Prison & Reentry Grants*, LEGAL FOUND. OF WASH., http://www.legalfoundation.org/pages/grants/grants_faq (last visited May 31, 2015).

190. Legal Foundation of Washington 2013 Report on Use of Cy Pres Funds, *supra* note 188, at 1; Order for *Cy Pres* Award for the Legal Foundation of Washington and Legal Services Organizations at 1–2, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013).

191. Legal Foundation of Washington 2013 Report on Use of Cy Pres Funds, *supra* note 188, at 1; Order for *Cy Pres* Award for the Legal Foundation of Washington and Legal Services Organizations at 1–2, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013).

192. *Annual Public Report 2013*, *supra* note 188.

193. *See* Order for *Cy Pres* Award for the Legal Foundation of Washington and Legal Services Organizations at 2, *Judd*, No. 00-2-17565-5 SEA (Sept. 25, 2013) ("The LFW shall condition any award made under this paragraph on the agreement of the recipient to provide an annual report to the LFW that includes information (1) stating the amount of funds received from the *cy pres* award for that year; (2) describing how those funds have been used; and (3) affirming those funds have been used for the purposes identified in its application for a *cy pres* award and complies with any condition set by the LFW or the Court. The LFW shall provide these reports to the Court and counsel not later than 60 days after the end of the calendar year and shall be provided for each year that the organization receives *cy pres* disbursements under this Order. After receiving these reports, the Court may set a hearing to further consider the status of the awards either on its own motion or a motion brought by counsel for the parties or the recipients of the *cy pres* awards.").

194. *See* Application by Legal Foundation of Washington for Receipt of Residual Funds, *supra* note 168, at 5–6.

195. *Id.*

196. Legal Foundation of Washington 2013 Report on Use of Cy Pres Funds, *supra* note 188, at 1 (detailing grant monitoring measures and stating that "LFW is working with each organization to incorporate those unused funds into their budgets to ensure that all of the funds are accounted for"); *see also* Order for Additional *Cy Pres* Awards at 1–2, *Judd*, No. 00-2-17565-5 SEA (Apr. 23, 2014) (specifying grant oversight procedures for subsequent cy pres awards).

underlying goals of the *Judd* litigation.

This case represents a significant cy pres award not just because of the magnitude of the residual funds, and not just because funds were distributed to the LFW in accordance with Rule 23(f) for civil legal aid funding, but also because of the uniquely creative way that Judge Andrus awarded additional funds to the LFW to establish a cy pres grant program that assured the funds retained a nexus to the underlying litigation. In setting up this grant program, and selecting the LFW as the grant administrator, the court was able to divorce itself from any actual awarding of specific monetary amounts, while also ensuring that the funds received oversight. The LFW already had established procedures in place for monitoring legal aid grants as a part of the LFW's IOLTA program, which includes yearly reporting requirements and a yearly full audit by a neutral third party.[197] This approach allowed for all funds to go to either valid legal aid causes, or to qualified charities with close ties to the underlying merits of the litigation.

### *C. Other State Approaches: A General Trend Towards Recognizing Legal Aid Organizations as Appropriate Cy Pres Recipients*

Several other states have adopted provisions into their civil rules on cy pres distributions in class actions. The general trend of these provisions, enacted in sixteen states thus far,[198] has been towards recognizing that legal aid foundations can be appropriate cy pres recipients. There are four general patterns these various state approaches fall into.

Several states have adopted an approach similar to Washington, wherein courts are directed to make a minimum award of the residual funds cy pres to a particular legal aid charity, usually the legal aid foundation that manages the state's IOLTA funds. In addition to Washington, this approach has been adopted by Indiana,[199]

197. *See* Application by Legal Foundation of Washington for Receipt of Residual Funds, *supra* note 168 (detailing the existing grant program structure in place at the LFW at the time the court was considering the intial cy pres awards in the *Judd* case).

198. These states include: Washington, Indiana, Pennsylvania, North Carolina, Illinois, South Dakota, Massachusetts, Maine, New Mexico, California, Tennessee, Kentucky, Montana, Louisiana, Connecticut, and Hawaii.

199. IND. R. TRIAL P. 23(F) ("In matters where the claims process has been exhausted and residual funds remain, not less than twenty-five percent (25%) of the residual funds shall be disbursed to the Indiana Bar Foundation to support the activities and programs of the Indiana Pro Bono Commission and its *pro bono* districts. The court may disburse the balance of any residual funds beyond the minimum percentage to the Indiana Bar Foundation or to any other entity for purposes that have a direct or indirect relationship to the objectives of the underlying litigation or

Pennsylvania,[200] and Kentucky.[201] These states all provide that a minimum percentage of residual funds go to their respective state's bar foundation or foundation that manages the state's IOLTA funds, to serve purposes of legal aid and access to justice, while allowing courts to make further distributions to these organizations if deemed appropriate.[202] Montana takes a similar approach by mandating that at least fifty percent of residual funds be distributed cy pres to any access to justice organization.[203] The Montana rule defines an "Access to Justice Organization" as "a Montana non-profit entity whose purpose is to support activities and programs that promote access to the Montana civil justice system."[204]

Another approach has been to limit the amount that may be distributed to legal aid charities. This approach has been adopted by Illinois, which provided in its civil rules that a maximum of fifty percent of cy pres awards can be awarded to a legal aid charity serving the public good.[205] In doing so, this rule codifies that cy pres is an

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otherwise promote the substantive or procedural interests of members of the certified class.").

200. PA. R. CIV. P. 1716 ("Not less than fifty percent (50%) of residual funds in a given class action shall be disbursed to the Pennsylvania Interest on Lawyers Trust Account Board to support activities and programs which promote the delivery of civil legal assistance to the indigent in Pennsylvania by non-profit corporations . . . .").

201. KY. R. CIV. P. 23.05(6)(b) ("Any order entering a judgment or approving a proposed compromise of a class action certified under this rule that establishes a process for identifying and compensating members of the class shall provide for the disbursement of residual funds. In matters where the claims process has been exhausted and residual funds remain, not less than twenty-five percent (25%) of the residual funds shall be disbursed to the Civil Rule 23 Account maintained by the Kentucky IOLTA Fund Board of Trustees pursuant to Supreme Court Rule 3.830(20). Such funds are to be allocated to the Kentucky Civil Legal Aid Organizations based upon the current poverty formula established by the Legal Services Corporation to support activities and programs that promote access to the civil justice system for low-income residents of Kentucky.").

202. PA. R. CIV. P. 1716; IND. R. TRIAL P. 23(F); WASH. R. CIV. P. 23(f).

203. MONT. R. CIV. P. 23(i)(3) ("Any order entering a judgment or approving a proposed compromise of a class action certified under this rule that establishes a process for identifying and compensating members of the class *shall* provide for disbursement of residual funds. In matters where the claims process has been exhausted and residual funds remain, not less than fifty percent (50%) of the residual funds shall be disbursed to an Access to Justice Organization to support activities and programs that promote access to the Montana civil justice system. The court may disburse the balance of any residual funds beyond the minimum percentage to an Access to Justice Organization or to another non-profit entity for purposes that have a direct or indirect relationship to the objectives of the underlying litigation or otherwise promote the substantive or procedural interests of members of the certified class." (emphasis added)).

204. *Id.* at R. 23(i)(2).

205. 735 ILL. COMP. STAT. 5/2-807(b) ("An order approving a proposed settlement of a class action . . . shall provide for the distribution of any residual funds to one or more eligible organizations, except that up to 50% of the residual funds may be distributed to one or more other nonprofit charitable organizations or other organizations that serve the public good if the court finds

appropriate use of residual class action funds.[206]

A third approach has been to adopt a civil rule that codifies that cy pres is an appropriate use of residual class action funds, but does not prescribe a particular charitable recipient. States that have adopted this approach expressly permit the award of cy pres funds to legal aid charities but do not demand it. Several states have adopted a similar approach including: Massachusetts,[207] New Mexico,[208] California,[209] Tennessee,[210] Hawaii,[211] and Louisiana.[212]

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there is good cause to approve such a distribution as part of a settlement.").

206. *Id.*

207. MASS. R. CIV. P. 23(e)(2) ("In matters where the claims process has been exhausted and residual funds remain, the residual funds shall be disbursed to one or more nonprofit organizations or foundations (which may include nonprofit organizations that provide legal services to low income persons) which support projects that will benefit the class or similarly situated persons consistent with the objectives and purposes of the underlying causes of action on which relief was based, or to the Massachusetts IOLTA Committee to support activities and programs that promote access to the civil justice system for low income residents of the Commonwealth of Massachusetts.").

208. N.M. DIST. CT. R. CIV. P. 1-023(G)(2) ("The court shall provide for the disbursement of residual funds, if any, to one or more of the following entities: (a) nonprofit organizations that support projects that benefit the class or similarly situated persons consistent with the goals of the underlying causes of action on which relief was based; (b) educational entities that provide training, teaching and legal services that further the goals of the underlying causes of action on which relief was based; (c) nonprofit organizations that provide legal services to low income persons; (d) the entity administering the IOLTA fund under Rule 24-109 NMRA, to support activities and programs that promote access to the civil justice system for low income residents of New Mexico").

209. CAL. CIV. PROC. CODE § 384 (providing for distribution of residual funds "to nonprofit organizations or foundations to support projects that will benefit the class or similarly situated persons, or that promote the law consistent with the objectives and purposes of the underlying cause of action").

210. TENN. R. CIV. P. 23.08 ("A distribution of residual funds to a program or fund which serves the pro bono legal needs of Tennesseans including, but not limited to, the Tennessee Voluntary Fund for Indigent Civil Representation is permissible but not required.").

211. HAW. R. CIV. P. 23(f) ("Unless otherwise required by governing law, it shall be within the discretion of the court to approve the timing and method of distribution of residual funds and to approve the recipient(s) of residual funds, as agreed to by the parties, including nonprofit tax exempt organizations eligible to receive assistance from the indigent legal assistance fund under HRS section 607-5.7 (or any successor provision) or the Hawai'i Justice Foundation, for distribution to one or more of such organizations.").

212. LA. SUP. CT. R. 43 ("Section 1. For purposes of this rule, 'Cy Pres Funds' shall refer to all funds that remain after the payment of all approved class member claims, expenses, litigation costs, attorneys' fees and other court-approved disbursements to implement the relief granted. It shall not refer to any such remaining funds that are otherwise distributed by the parties through class settlement, including funds to be returned to one or more parties. Section 2. In matters where the claims process has been exhausted and Cy Pres Funds remain, such funds *may* be disbursed by the trial court to one or more non-profit or governmental entities which support projects that will benefit the class or similarly situated persons consistent with the objectives and purposes of the underlying causes of action on which relief was based, including the Louisiana Bar Foundation for use in its

One final approach taken among states codifying an approach to class action cy pres is to require the disbursement of funds to a particular legal aid charitable recipient, unless the court determines that another charitable organization better approximates the interests of the class members. Similar approaches have been adopted in state courts in Maine,[213] South Dakota,[214] and Connecticut.[215] Interestingly, this state approach was recently adopted as a local civil rule in the U.S. District Court for the District of Connecticut.[216]

Each one of these state approaches recognizes that cy pres is a valid, or even preferred use of residual class action funds. In addition, each of these state approaches allows, or even requires cy pres awards be made to legal aid charities. Furthermore, many of these states have specified that the cy pres awards should be granted to a particular charity—their state's IOLTA foundation legal aid charity. As will be explored in the next two Parts *infra*, these trends represent creative attempts to structure cy pres awards in ways that will make the awards more transparent and

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mission to support activities and programs that promote direct access to the justice system." (emphasis added)). Interestingly, this statute also calls for mandatory reporting of all cy pres funds. *Id.* at R. 43(3).

213. ME. R. CIV. P. 23(f)(2) ("The parties may agree that residual funds be paid to an entity whose interests reasonably approximate those being pursued by the class. When it is not clear that there is such a recipient, unless otherwise required by governing law, the settlement agreement should provide that residual fees, if any, be paid to the Maine Bar Foundation to be distributed in the same manner as funds received from interest on lawyers trust accounts pursuant to M. Bar R. 6(a)(2)-(5).").

214. S.D. CODIFIED LAWS § 16-2-57 ("Any order settling a class action lawsuit that results in the creation of a common fund for the benefit of the class shall provide for the distribution of any residual funds to the Commission on Equal Access to Our Courts. However, up to fifty percent of the residual funds may be distributed to one or more other nonprofit charitable organizations that serve the public good if the court finds there is good cause to approve such a distribution as part of the settlement.").

215. CONN. SUPER. CT. CIV. R. 9-9(g)(2) ("Any order, judgment or approved settlement in a class action that establishes a process for identifying and compensating members of the class may designate the recipient or recipients of any such residual funds that may remain after the claims payment process has been completed. In the absence of such designation, the residual funds shall be disbursed to the organization administering the program for the use of interest on lawyers' client funds pursuant to General Statutes § 51-81c for the purpose of funding those organizations that provide legal services for the poor in Connecticut.").

216. CONN. DIST. CT. LOCAL CIV. R. 23(b) ("Any order, judgment or approved settlement in a class action that establishes a process for identifying and compensating members of the class may designate the recipient(s) of any such residual funds that may remain after the claims payment process has been completed. In the absence of such designation, the residual funds *shall* be disbursed to the organization administering the program for the use of interest on lawyers' client funds pursuant to § 51-81c of the General Statutes for the purpose of supporting its activities including, but not limited to, the funding of those organizations that provide legal services for the poor in Connecticut." (emphasis added)).

consistent, guide—or even limit—the discretion of those involved in making the awards, and thereby provide for outcomes that better serve the interests of class members.

## IV. IN DEFENSE OF CY PRES—ALTERNATIVES TO CY PRES ARE UNSATISFACTORY

When faced with the problem of residual funds from a class action settlement or award, for which further distribution to class members is impracticable or impossible, a cy pres distribution is the superior remedy. Of course, using the funds to directly compensate class members for their injuries will always provide the least controversial use of the funds,[217] and if such a distribution directly to uncompensated class members is possible it should be made.[218] However, once all individual class plaintiffs have been identified and compensated and further distributions are impossible, this Comment argues that the cy pres remedy, when appropriately applied, is the proper use of these remaining funds. This Part first examines the possible alternatives to using cy pres, and the drawbacks of each of these alternatives. This Part then concludes that cy pres is the superior solution for dealing with residual class action funds.

### *A. Reversion*

One alternative to the use of cy pres for residual fund disbursements is reversion to the defendants.[219] Under this method, any unclaimed funds will transfer back to the defendant. This is problematic because it results in a windfall to defendants.[220] Defendants will be able to keep unlawfully obtained profits.[221] Furthermore, this solution would undermine any deterrent effect that a judgment or settlement has on the defendant.[222]

Judge Edith Jones in her concurring opinion in *Klier v. Elf Atochem North America, Inc.*, argued that had the defendants not waived their right to a refund of undisbursed funds in that case, they would have been

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217. *See supra* Part II.

218. ALI'S PRINCIPLES, *supra* note 60, § 3.07.

219. Yospe, *supra* note 16, at 1042.

220. Natalie A. DeJarlais, Note, *The Consumer Trust Fund: A Cy Pres Solution to Undistributed Funds in Consumer Class Actions*, 38 HASTINGS L.J. 729, 749 (1987).

221. *Id.*

222. *Id.*

entitled to the excess funds.[223] Judge Jones argued that the "superior approach is to return leftover settlement funds to the defendant. This corrects the parties' mutual mistake as to the amount required to satisfy class members' claims . . . . [A] cy pres distribution . . . result[s] in charging the defendant an amount greater than the harm it bargained to settle."[224] This conclusion results from a fundamental error in reasoning—the funds represent the compensation due to the absent class members, and thus the remaining "excess" is a result of administrative difficulties in disbursing the funds, and not the result of an error in calculating damages.[225]

Furthermore, a reversion remedy would undermine any deterrence effect of the litigation.[226] "It is a basic principle of equity that wrongdoers should not profit from their wrongdoing . . . . Wrongdoers will be less likely to engage in future illegal acts if the incentive of unjust enrichment is eliminated."[227] Because reversion would allow defendants to keep unlawfully obtained profits, allowing a reversion remedy would undermine enforcement of the underlying substantive law.[228] At least in the context of settlement agreements, there is a strong argument that defendants should not benefit from the reversion of funds because the "[d]efendants are never forced to agree to a settlement that overcompensates the plaintiffs."[229] In agreeing to a settlement, defendants have received a tangible benefit, namely a "release from liability with respect to the class members," and the likelihood and cost of future litigation was likely factored into the settlement agreement.[230]

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223. 658 F.3d 468, 480 (5th Cir. 2011).

224. *Id.* at 482.

225. *Klier* involved an appeal from a settlement agreement in a class action. *Id.* at 468. "The settlement agreement created three subclasses and allocated to each subclass a portion of the $41.4 million settlement." *Id.* at 472. The funds were to be used for one subclass to create a medical monitoring program, however $830,000 of the funds intended for this subclass were unclaimed. *Id.* at 473. The parties were in agreement that the distribution of these funds to individual class members was not economically feasible, and the court adopted a cy pres remedy. *Id.* The cy pres funds at issue thus did not represent an error in calculating the defendant's liability, but rather represented the legitimate claims of unidentified class members.

226. Redish et al., *supra* note 13, at 631.

227. Kerry Barnett, Note, *Equitable Trusts: An Effective Remedy in Consumer Class Actions*, 96 YALE L.J. 1591, 1595 (1987).

228. *See* DeJarlais, *supra* note 220, at 749 ("[T]o permit the return of the unclaimed funds, a portion of the illicit profits, would impair the full impact of the deterrent force that is essential if adequate enforcement of the [law] is to be achieved . . . ." (quoting SEC v. Golconda Mining Co., 327 F. Supp. 257 (S.D.N.Y. 1971)).

229. Yospe, *supra* note 16, at 1043.

230. *Id.* (quoting *In re* Motorsports Merch. Antitrust Litig., 160 F. Supp. 2d 1392, 1395 (N.D. Ga. 2001)).

To return funds to the defendant because not every plaintiff could be located would represent an unjust enrichment to defendants who would be allowed to benefit from their violations of the law.[231]

### *B. Pro Rata Distribution to Class Members*

Another possible alternative to cy pres is a pro-rata distribution of the residual funds to already compensated and identified class members.[232] This solution is also unsatisfactory because it overcompensates the identified plaintiffs and thus it results in a windfall to plaintiffs.[233]

### *C. Escheat*

Another option discussed as an alternative to cy pres distributions is to allow the funds to escheat to the state.[234] However, if it is unlikely that additional plaintiffs would be found, as would be the case in any appropriately used cy pres,[235] this is likely not an effective use of the remaining funds.[236] While this allows for the discouragement of ill-gotten gains and serves deterrence goals, it is problematic in that there are no assurances that the money will be used for purposes that are in line with the underlying litigation.[237] As such, to give the money, which is to be used for the benefit of class members, to a cause which could run counter to the interests of the class members would violate principles underlying Federal Rule of Civil Procedure 23, which mandate a duty on class counsel and the courts to ensure that the class action is being conducted in line with the interests of absent class members.[238]

### *D. Refusal to Certify the Class*

One final proposed alternative to cy pres remedies, argued by Martin Redish and others, is that courts should refuse to certify a class action

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231. Jay Tidmarsh, Cy Pres and the Optimal Class Action, 82 GEO. WASH. L. REV. 767, 768 (2014).

232. *Id.* at 1045.

233. *Id.*

234. *Id.* at 1046.

235. *See* argument *infra* Parts IV–V.

236. Yospe, *supra* note 16, at 1047–48.

237. Barnett, *supra* note 227, at 1599.

238. *See* FED. R. CIV. P. 23(g)(4) ("Class counsel must fairly and adequately represent the interests of the class."); *id.* at R. 23(e)(2) ("If the proposal would bind class members, the court may approve [a settlement] only after a hearing and on finding that it is fair, reasonable, and adequate.").

when it is anticipated that a cy pres remedy would be necessary.[239] The logic of this argument is that if it is likely that a majority of individual class members will not be able to be directly compensated by the class action litigation then the use of a class action would be unmanageable.[240] The problem with this reasoning is twofold. First, the problem of unclaimed residual funds is an issue even when there has been substantial compensation to a majority of class members but remaining absent class members cannot be located.[241] In these cases, where a class was appropriately certified,[242] the problem of what to do with the remaining funds persists. Due to the undesirability of the alternatives, cy pres remains the best use of these funds in these situations.[243]

Another problem with the prospective suggestion to refuse to certify classes where cy pres is an anticipated remedy, is that this solution would deny many plaintiffs their day in court and access to justice. In cases where the claims of individual plaintiffs are small, the cost of bringing a lawsuit can greatly exceed the damages recoverable.[244] The class action provides an equitable solution wherein these legitimate claims, which on their own would not be feasible to bring a lawsuit, become feasible when aggregated, and thus through the class action device are able to enforce the law and bring justice.[245] In *Hughes v. Kore of Indiana Enterprise, Inc.*, Judge Posner writing for the Seventh Circuit recognized the importance of the class action remedy for these small claims cases.[246] *Hughes* involved a class action lawsuit against a company for failing to provide notice that their ATM would charge a transaction fee to users.[247] Judge Posner noted that the alternative to a class action, individual lawsuits of damages of not more than $100, would "not be realistic."[248] "The smaller the stakes to each victim of unlawful conduct, the greater the economies of class action

239. Redish et al., *supra* note 13, at 639.

240. *Id.*

241. Redish notes his proposed solution to cy pres would not help in this situation. Redish et al., *supra* note 13, at 665.

242. *See, e.g.*, Jones v. Nat'l Distillers, 56 F. Supp. 2d 355 (S.D.N.Y. 1999).

243. *See* argument *infra* Part IV.

244. *See, e.g.*, Hughes v. Kore of Ind. Enter., Inc., 731 F.3d 672, 675 (7th Cir. 2013) (noting that individual recoveries in the case would be only $100, and thus individual lawsuits—as opposed to a class action suit—would be impractical).

245. *See id.* at 677.

246. *Id.*

247. *Id.* at 674.

248. *Id.* at 675.

treatment."[249]

> A deeper question is whether a class action should be permitted when the stakes, both individual and aggregate, in a class action are so small—so likely to be swamped by the expense of litigation—as they are in this case. But we don't think smallness should be a bar. This is obvious when what is small is not the aggregate but the individual claim; indeed that's the type of case in which class action treatment is most needful.[250]

Refusing to certify a class action in the context of these so-called "negative value suits" would be tantamount to authorizing the defendants a free pass to violate the law when individual damages would be small.[251] Furthermore, categorically disallowing these class actions from proceeding would run counter to the purposes of Federal Rule of Civil Procedure 23. One aim of class actions as guided by Rule 23, is "to provide a feasible means for asserting the rights of those who 'would have no realistic day in court if a class action were not available.'"[252]

### *E. Cy Pres Presents the Best Option for These Funds*

As explained above, none of the alternatives to cy pres relief provide a workable solution to the problem of residual funds and funds that are impractical or impossible to distribute to individual class members. Alternatives to cy pres either create unjustifiable windfalls to one side, or run counter to the principles underlying the administration of justice and the underlying principles of class action litigation. However, when damages are given to a charity through cy pres, there are necessarily going to be third parties who benefit from the use of these funds.[253]

> Clearly, windfall is inevitable in a cy pres distribution of damages or settlement funds. The true question, then, is whether the undesirability of a windfall to third parties is outweighed by the positive effects of cy pres distribution . . . . Windfalls are hardly taboo in the law. Indeed, the traditional application of the

249. *Id.*

250. *Id.* at 677.

251. *Cf. id.* at 676 (noting that "[t]he smaller the stakes to each victim of unlawful conduct, the greater the economies of class action treatment and the likelier that the class members will receive some money rather than (without a class action) probably nothing, given the difficulty of interesting a lawyer in handling a suit for such modest . . . damages").

252. Buford v. H & R Block, Inc., 168 F.R.D. 340, 345–46 (S.D. Ga. 1996), *aff'd sub nom.* Jones v. H & R Block Tax Servs., 117 F.3d 1433 (11th Cir. 1997) (quoting Phillips Petroleum Co. v. Shutts, 472 U.S. 797, 809 (1985)).

253. DeJarlais, *supra* note 220, at 741.

> cy pres doctrine to frustrated testamentary intent may result in some windfall to beneficiaries who were not included in the testator's original plan. Examples of accepted remedies that entail windfalls are injunctions, statutory minimum damages, liquidated or treble damages, punitive damages, [and] shareholder derivative suits . . . . The principle common to each of these areas is that some degree of windfall is a tolerable cost of effectuating the deterrent purposes of the applicable laws and ensuring recovery to victims who have actually been injured.[254]

Although cy pres does provide a benefit to third parties, cy pres remains the superior solution for the distribution of these funds because it serves deterrence goals, ensures the viability of small damages actions, and uses the remaining funds to further the underlying goals of the litigation.

## V. IMPROVING CY PRES—LESSONS FROM WASHINGTON

The main critiques of the cy pres doctrine stem from the improper use of the doctrine, not from inherent flaws in the doctrine itself. The problem of improper incentives[255] can be effectively negated through good decision-making by judges and counsel, a clearer articulation of what qualifies as a valid cy pres recipient, and stronger procedural protections. By examining the Washington State approach to class action cy pres through the lens of the *Judd v. AT&T* case, it is clear that a statutory approach is the best solution moving forward as it will clarify the standards for approving an acceptable cy pres recipient and standardize procedures for selecting that recipient in a way that will reduce any appearance of impropriety. Cy pres has promise and value as an equitable solution to the problem of residual funds in appropriate cases; courts should not throw the baby out with the bath water.

### *A. Improper Incentives Can Be Checked*

One of the main criticisms of cy pres doctrine in class actions is that it creates improper incentives for judges, attorneys, and charitable organizations to further their own interests rather than promote the interests of the absent class members.[256] "Moreover, the specter of judges and outside entities dealing in the distribution and solicitation of

254. *Id.*

255. *See supra* Part II.C.

256. *See* Redish et al., *supra* note 13; Yospe, *supra* note 16.

settlement money may create the appearance of impropriety."[257] However, cy pres has been appropriately applied in many situations, and in states such as Washington, statutory mandates have effectively constrained discretion, and along with it, the illusion of improper incentives.

The rule on cy pres in class actions adopted by Washington has been an effective solution to some of the key criticisms of the doctrine. The statutory solution adopted by Washington is effective in controlling incentives, and further exemplifies how courts can successfully implement cy pres doctrine properly in practice.

First, the Washington approach only takes effect when *residual* funds are identified,[258] thus ensuring that efforts are first taken to identify and compensate actual class members. This ensures that class counsel is not induced to seek cy pres without first confirming that further distribution of funds is impossible.[259] This approach is consistent with the approach endorsed in the American Legal Institute's (ALI) new *Principles of Aggregate Litigation*.[260] The ALI proposed that a cy pres award is appropriate only if it is impossible or infeasible to distribute the funds to class members.[261] "If 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 class members."[262]

Second, the Washington State approach curbs judicial discretion by introducing a mandatory disbursement of residual funds to the LFW.[263] Because the determination of the appropriate cy pres recipient is not being made by a judge, the judge avoids the appearance of impropriety and is prevented from making a distribution that does not further the interests of the class and or litigation, or one that is purely for self-benefit. For example, the judge in *Judd* effectively avoided the appearance of impropriety by first implementing a rigorous review and approval of potential cy pres recipients, and second, by shifting the ultimate disbursement of the funds though an established grant program that was tied to the interests of the underlying litigation.[264]

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257. Nachshin v. AOL, LLC, 663 F.3d 1034, 1039 (9th Cir. 2011).

258. WASH. R. CIV. P. 23(f)(1).

259. ALI'S PRINCIPLES, *supra* note 60, § 3.07.

260. *Id.*

261. *Id.*

262. *Id.* § 3.07(a).

263. WASH. R. CIV. P. 23(f)(2).

264. *See supra* Part III.B.

Third, Washington Civil Rule 23(f) also gives a helpful articulation of what constitutes a valid use of cy pres awards. The Washington State approach represents a strong policy statement that legal aid charities are an appropriate recipient of cy pres distributions.[265] The designated recipient of residual cy pres funds, the LFW, not only fits with the general access to justice principles underlying any class action litigation,[266] thereby making it an appropriate cy pres recipient,[267] it also has the benefit of being the foundation that administers Washington State's IOLTA program.[268] Because it administers the state's IOLTA program, the LFW provides the benefit of an established grant program structure with independent third-party oversight.[269]

### *B. Legal Aid Charities Can Be Appropriate Cy Pres Recipients*

Several courts have awarded cy pres distributions to legal aid charities.[270] Furthermore many states have explicitly adopted rules either authorizing or mandating that cy pres funds go to legal aid charities.[271] Some courts and commenters have criticized this practice, arguing that while these recipients are surely worthy causes, they do not relate to the interests of the class members.[272] Such arguments unhinge the doctrine of cy pres from its trust law origins, distorting the concept of "next best

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265. *Id.* ("[R]esidual funds shall be disbursed . . . to support activities and programs that promote access to the civil justice system for low income residents of Washington State.").

266. The mission statement of the Legal Foundation of Washington is: "The Legal Foundation of Washington is dedicated to equal justice for low-income persons. The Foundation funds programs and supports policies and initiatives which enable the poor and the most vulnerable to overcome barriers in the civil justice system." *Inside LFW*, *supra* note 36.

267. *See infra* Part VII.B–C.

268. *Interest On Lawyer Trust Accounts (IOLTA)*, LEGAL FOUND. WASH., http://www.legalfoundation.org/pages/iolta (last visited May 31, 2015).

269. *See* Application by Legal Foundation of Washington for Receipt of Residual Funds, *supra* note 168.

270. "The absence of an obvious cause to support with the funds does not bar a charitable donation, however. In recent years, the doctrine appears to have become more flexible. . . . While the use of funds for purposes closely related to their origin is still the best cy pres application, the doctrine of cy pres and courts' broad equitable powers now permit use of funds for other public interest purposes by . . . other public services organizations." Jones v. Nat'l Distillers, 56 F. Supp. 2d 355, 359 (S.D.N.Y. 1999) (internal quotations omitted); *see also* Eddings v. Health Net, Inc., No. CV 10-1744-JST (RZx), 2013 WL 169895 (C.D. Cal. Jan. 16, 2013); Superior Beverage Co. v. Owens-Ill., Inc., 827 F. Supp. 477 (N.D. Ill.1993).

271. *See supra* Part III.C.

272. *See* SEC v. Bear, Stearns & Co., 626 F. Supp. 2d 402, 416 (S.D.N.Y. 2009) ("The funding of legal services programs is a worthy pursuit. However, absent specific legislation, courts are left with unfettered discretion to direct the distribution of what can be large sums of money.").

use" into the legal fiction of "indirect benefit."[273] However, under a proper articulation of the cy pres doctrine, a legal aid charity in an appropriate case, can accurately be deemed the "next best use" of the residual funds.

As previously discussed, the cy pres remedy, as it originated in charitable trust law, seeks to save trusts that would otherwise fail by applying funds to the "next best use" that would effectuate the underlying goals of the settlor as closely as possible.[274] In the class action context, cy pres has been interpreted by several courts, including the Ninth and First Circuits,[275] to require that the recipient of the cy pres funds share a "driving nexus" with the interests of the plaintiff class for the indirect benefit of class members.[276] "The purpose of the cy pres distribution is to 'put the unclaimed fund to its *next best* compensation use, e.g., for the aggregate, indirect, prospective benefit of the class.'"[277]

The problem with the current leading articulation of this standard for cy pres—under either the indirect benefit or nexus articulation—is that it is based upon a legal fiction. As Judge Posner has acknowledged, "[t]here is no indirect benefit to the class from the defendant's giving the money to someone else. In such a case the 'cy pres' remedy . . . is purely putative."[278] However, Judge Posner has said that the mere putative nature of the cy pres remedy will not invalidate it.[279]

Because this legal fiction has been reinforced as a legitimating purpose behind cy pres,[280] and because the interests of absent class members will not be indirectly served by giving their money to a third

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273. *See In re* BankAmerica Corp. Sec. Litig., 775 F.3d 1060, 1067 (8th Cir. 2015) ("[W]hen a district court concludes that a cy pres distribution is appropriate after applying the foregoing rigorous standards, such a distribution must be 'for the next best use . . . *for indirect class benefit*,' and 'for uses consistent with the nature of the underlying action and with the judicial function.'" (emphasis added) (quoting *In re* Katrina Canal Breaches Litig., 628 F.3d 185, 196 (5th Cir. 2010))).

274. *See supra* Part I.

275. *See* Lane v. Facebook, Inc., 696 F.3d 811 (9th Cir. 2012), *reh'g denied*, 709 F.3d 791 (9th Cir. 2013), *cert. denied sub nom.* Marek v. Lane, 571 U.S. __, 134 S. Ct. 8 (2013); *In re* Lupron Mktg. & Sales Practices Litig., 677 F.3d 21, 38 (1st Cir. 2012).

276. *See supra* Part I.B.

277. *Bear, Stearns & Co.*, 626 F. Supp. at 414 (emphasis in original) (quoting Masters v. Wilhelmina Model Agency, Inc., 473 F.3d 423, 436 (2d Cir. 2007)).

278. Mirfasihi v. Fleet Mortg. Corp., 356 F.3d 781, 784 (7th Cir. 2004).

279. Hughes v. Kore of Indiana Enters., Inc., 731 F.3d 672, 676 (7th Cir. 2013) ("When there's not even an indirect benefit to the class from the defendant's payment of damages, the 'cy pres' remedy . . . is purely punitive. But we said in *Mirfasihi* that the punitive character of the remedy would not invalidate it. Other courts, disagreeing, require the charity or other recipient to have an interest parallel to that of the class." (internal citations omitted)).

280. *See generally, e.g.*, Nachshin v. AOL, LLC, 663 F.3d 1034 (9th Cir. 2011).

party,[281] courts have struggled with the application of the cy pres principle when there is no existing charity that clearly approximates the interests of the class.[282] In *Jones v. National Distillers*, the court struggled to find a charitable recipient that would indirectly benefit the class members in a stock market fraud class action.[283] The court stated this difficulty in its opinion, noting that, "[c]y pres principles offer limited guidance here, however. While there are many worthy uses for $18,400.80, there is no obvious use for the money that provides a particular benefit to class members."[284]

When there is no clear charitable recipient with ties to the interests of class members, parties and courts have stretched this nexus requirement to try to fit over a charity with a less readily apparent tie to the class members.[285] "*Cy pres* distributions imperfectly serve that purpose by substituting for that direct compensation an indirect benefit that is at best attenuated and at worse illusory."[286] Commenters have jumped on a few cases as examples of impropriety that were merely courts and parties going through this strained exercise.[287] Martin Redish criticizes cases where there has been an attenuated nexus to class members' interests:

> An even stronger illustration of the attenuated connection between the direct interests of the class members and the charity receiving the cy pres award is the federal district court decision in *In re Compact Disc Minimum Advertised Price Antitrust Litigation*. There the court in a compact disc advertised price antitrust litigation authorized a cy pres award to the National Guild of the Community School of the Arts. There was no way that the designation even arguably compensated injured victims, directly or indirectly, in any recognizable way . . . . Similarly . . . in *Jones v. National Distillers*, [] the court awarded a cy pres award from a securities fraud suit to a legal aid society because it was more related to the subject matter of the suit than would be "a dance performance or a zoo." *In none of these decisions did the charitable designation in any way constitute even a feeble attempt to indirectly compensate*

281. *Mirfasihi*, 356 F.3d at 784.

282. *See* Jones v. Nat'l Distillers, 56 F. Supp. 2d 355 (S.D.N.Y. 1999).

283. *Id.* at 358.

284. *Id.*

285. *See id.*

286. *In re* Baby Prods. Antitrust Litig., 708 F.3d 163, 173 (3d Cir. 2013).

287. *See* Superior Beverage Co. v. Owens-Ill., Inc., 827 F. Supp. 477 (N.D. Ill. 1993).

*victims*.[288]

These criticisms stem from precisely the issue that compensating plaintiffs is not possible when the money is given to a third party. The cy pres principle in trust law was designed to appropriate funds to their "next best use"[289] which does not necessarily indicate that an indirect benefit to the originally intended recipient is necessary, but rather allows for restructuring of the trust to "accomplish the general . . . purpose of the donor."[290] By analogy to the class action context, the funds that are impossible to distribute to absent class members should be restructured to further the underlying goals of the class action lawsuit.[291] When conceived in this light, the "next best use" of residual funds in class action lawsuits should go to causes that further the goals of the underlying substantive law claims and underlying goals of the class action litigation. One such way to ensure that class action funds are going to their next best use is to disburse the funds cy pres to organizations that promote access to justice, which are necessarily implicated in any class action lawsuit:

> Class actions serve three essential purposes: (1) to facilitate judicial economy by the avoidance of multiple suits on the same subject matter . . . ; (2) to provide a feasible means for asserting the rights of those who "would have no realistic day in court if a class action were not available" . . . ; and (3) to deter inconsistent results, assuring a uniform, singular determination of rights and liabilities. "The class action is a powerful procedural device, offering enormous savings in time and judicial resources while opening up opportunities for both new forms of litigation and potential abuse by litigants."[292]

Access to justice is an important concern underlying class action

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288. Redish et al., *supra* note 13, at 636–37 (emphasis added).

289. *See supra* Part I.

290. *See* RESTATEMENT (SECOND) OF TRUSTS § 399 cmt. b (1959) ("*To what purposes the property may be applied.* In the application of the cy pres doctrine, it is sometimes stated that the property must be applied to purposes as nearly as possible like those designated by the terms of the gift. To an increasing extent, however, the courts have recognized that in choosing among possible schemes the court is not necessarily required to adopt that scheme which is as nearly as possible like that designated by the terms of the gift. This is particularly true where the designated purpose becomes impossible or impracticable of accomplishment at some time subsequent to the creation of the trust. The court seeks to frame a scheme which on the whole is best suited to accomplish the general charitable purpose of the donor." (emphasis in original)).

291. See *supra* Part I for a definition of the cy pres standard.

292. Buford v. H & R Block, Inc., 168 F.R.D. 340, 345–46 (S.D. Ga. 1996), *aff'd sub nom.* Jones v. H & R Block Tax Servs., 117 F.3d 1433 (11th Cir. 1997) (internal citations omitted).

litigation.[293] Using cy pres funds to further access to justice programs, such as state legal aid foundations, would further the underlying goals of the class action litigation, and absent a closer substantive fit to the particular litigation, would fall within the purview of the funds' legitimate "next best use."[294]

### *C.* Judd v. AT&T *Is an Example of Cy Pres Properly Used*

One clear example of cy pres properly used is the *Judd v. AT&T* case in Washington State. With a very large fund available for cy pres distributions[295] the court was able to make reasoned and impartial determinations about which charities were appropriate, and was able to avoid any appearance of impropriety.

The ultimate outcome was the application of cy pres at its best for three reasons. First, the Judge removed herself from making the actual individual grant determinations by approving charities as applicable in both credibility and in underlying support of the purposes of the case and gave the LFW the ability to approve grants to these charities with a mindfulness of the underlying purposes of the litigation.[296] By removing herself from the individual award of cy pres funds, Judge Andrus was able to avoid the appearance of impropriety and allow for an unbiased application of cy pres.

Second, charities that were interested in receiving cy pres funds were required to submit applications specifying the intended use of the funds and were required to articulate how they would use these funds to further the underlying purpose of the litigation.[297] This creates transparency in the decision making process and ensures that cy pres is really being used for the "next best use" that furthers the objectives of the class action litigation. It also takes counsel out of the role of selecting a particular charitable cause, seen by many as a power susceptible to abuse,[298] and makes the charities apply to specific cases that are linked to their underlying goals rather than operating as a general lobbying group for

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293. *See id.*

294. Jones v. Nat'l Distillers, 56 F. Supp. 2d 355, 359 (S.D.N.Y. 1999) (noting that the cy pres recipient, a legal aid charity, served the "somewhat analogous purpose of helping those needing legal assistance for various civil matters"); Boies & Keith, *supra* note 104, at 290–91.

295. The fund was approximated at $20 million dollars. *See* Class Action Notice, Settlement Agreement at app. 2, Judd v. Am. Tel. & Tel. Co., No. 00-2-17565-5 SEA (King Cnty. Super. Ct., Wash. Jan. 22, 2013).

296. *See supra* Part III.B.

297. *Id.*

298. Yospe, *supra* note 16, at 1035.

any cy pres funds in any case.

Third, Washington Rule 23(f) explicitly authorized a reputable and appropriate cy pres recipient: the LFW.[299] Because this organization was designated by the state's civil rules, the judge did not decide who received the funds. Thus, the Judge's selection of this charity was not arbitrary or subject to concerns of bias or impropriety. Furthermore, the selection of a legal aid charity that will serve access to justice objectives furthers the underlying goals of the class action suit, and therefore arguably qualifies as an appropriate cy pres recipient.[300] This legal aid charity in particular has the benefit of state oversight since it administers the state's IOLTA fund and thus has a robust oversight structure,[301] and because it has a strong track record,[302] it is not subject to criticisms like those voiced about the newly created charity in the *Lane v. Facebook* case.[303]

The particular structure of the grant program that was set up to administer the cy pres awards further ensured that the cy pres was applied in a transparent and effective manner to only qualified and appropriate cy pres recipients. The LFW laid out specific procedures to the court for the administration of a grant program, based on its exiting grant program structure for IOLTA funds.[304] The LFW's grant-making process is overseen by a nine-member Board of Trustees; three members are each appointed by the Washington State Supreme Court, the Governor, and the Washington State Bar Association.[305] The LFW has a policy of only awarding grants to organizations that have "strong track record[s] of fiscal and programmatic integrity."[306] The grant recipients must provide regular fiscal and narrative reports to the LFW to allow the foundation to assess whether objectives are being met.[307]

For the *Judd v. AT&T* case, the LFW proposed that their grant

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299. WASH. R. CIV. P. 23(f)(2).

300. *See supra* Part V.B.

301. *Interest On Lawyer Trust Accounts (IOLTA)*, *supra* note 268.

302. Application by Legal Foundation of Washington for Receipt of Residual Funds, *supra* note 168 ("LFW has over 25 years of experience in granting and overseeing the effective use of funds to non-profit providers of legal services in Washington state. LFW has granted out over $160 million to nearly 50 organizations providing civil legal aid throughout our state by establishing and employing standards-based tools to assess program capability and program effectiveness.").

303. *See supra* Part II.C.

304. *See generally* Application by Legal Foundation of Washington for Receipt of Residual Funds, *supra* note 168.

305. *Id.*

306. *Id.*

307. *Id.*

program would award cy pres funds to grant recipients with proven track records of serving and "assist[ing] incarcerated or detained people, their families, and those recently released from institutions."[308] The LFW also took measures to ensure impartiality in the grant-awarding process. The Foundation proposed creating a "Blue Ribbon Panel" of impartial experts to develop and facilitate the activities of the grant recipients, and the panel would not include current or past board members from recipient organizations.[309] The ongoing oversight and annual reporting requirements ensure that the funds, once they are awarded, truly serve the interests of helping incarcerated persons and their families, and providing access to justice through legal aid.[310]

### *D. Improving Class Action Cy Pres Outcomes*

States are providing innovative ways to address the cy pres process for residual class action funds. Washington Civil Rule 23(f) goes a long way towards establishing clearer standards as to when cy pres is appropriate and which cy pres recipients are acceptable, and effectively works to counter the risks of abuse by judges and counsel. While the mandated distribution to the Legal Foundation of Washington, required under Washington Civil Rule 23(f), is effective at addressing many of the key criticisms of cy pres, it does not fully address concerns over the appropriation of the remaining seventy-five percent.

Other states address the remaining funds and apply a slightly different approach that is more in line with the doctrine's "next best use" origins. For example, the Maine approach to cy pres allows for a court to award a cy pres distribution to a charity with a very close tie to furthering the interests of the class, but provides further that should no clear recipient be identified, the court is to distribute the funds to the Maine IOLTA Foundation, a charitable organization providing legal aid services.[311] This two-tiered mechanism allows a cy pres award to be distributed to a charity with a very close nexus approximating the interests of the substantive claims of the class if such an organization exists, thereby

308. *Id.*

309. *Id.*

310. Legal Foundation of Washington 2013 Report on Use of Cy Pres Funds, *supra* note 188.

311. ME. R. CIV. P. 23(f)(2) ("The parties may agree that residual funds be paid to an entity whose interests reasonably approximate those being pursued by the class. When it is not clear that there is such a recipient, unless otherwise required by governing law, the settlement agreement should provide that residual fees, if any, be paid to the Maine Bar Foundation to be distributed in the same manner as funds received from interest on lawyers trust accounts pursuant to M. Bar R. 6(a)(2)-(5).").

ensuring that the funds go to the charity most-closely tied to the merits of the case if possible. If no such closely tied charity exists, then the rule requires the distribution of the residual funds to an approved legal aid foundation thereby ensuring that the principle of "next best use" is fully applied.

Maine further justifies the distribution of cy pres award to a legal aid foundation by connecting the charity's goals to the aims of the litigation. Distributing funds to the Maine IOLTA Foundation also serves the underlying goals of the litigation because of its legal aid and access to justice purposes.[312] In the advisory notes to Maine Rule 23, the purposes behind this approach were noted:

> Specifying the selection of the Maine Bar Foundation in such circumstances has two advantages. First, it eliminates any possibility that a recipient is being chosen to benefit or garner credit for the defendant, for plaintiffs' counsel, or for the court. Second, the principal aim of the Maine Bar Foundation—to support efforts to widen access to justice for those who cannot afford it—aligns with a basic aim of Rule 23 itself.[313]

Other states should look to the approaches taken in states such as Maine and Washington when considering adopting a measure to address cy pres awards. Looking at these states for guidance, an effective approach would be to require residual funds to go to a state's IOLTA legal aid foundation for grant distribution consistent with the merits and access to justice purposes of the class action litigation, unless the court finds that a different charitable organization exists "whose interests reasonably approximate those being pursued by the class."[314]

States should also consider the approach used by Judge Andrus in the *Judd v. AT&T* case and suggest awarding cy pres funds to their state legal aid foundation that manages the state's IOLTA program to distribute to qualified cy pres recipients in the form of narrowly tailored grants with oversight and reporting requirements. This method shifts the ultimate decision to award specific sums of money away from the judiciary, and to a reputable third party with substantial oversight. Such methods would ensure that only those charities that are indeed the "next best use" receive cy pres funds and would eliminate concerns of charitable lobbying and remedy appearances of impropriety.

The Federal Rules Advisory Committee is currently studying the

312. *Id.*; *see also* ME. R. CIV. P. 23(f) advisory note.

313. ME. R. CIV. P. 23(f) advisory note.

314. ME. R. CIV. P. 23(f).

issue of cy pres.[315] In a recent report the committee stated about cy pres:

> One of the reasons for disquiet about cy pres awards is the perception that at times they are made to recipients that will use the award for purposes that have little or no relation to the interests of the class. Awards to educational institutions favored by counsel or the court are an example. *Could cy pres provisions in Rule 23 effectively direct that the award go to an entity that has interests closely aligned with class members' interests?*[316]

As seen from the various state approaches to cy pres, a rule-based approach *can* be an effective way to tailor cy pres to its appropriate uses. As the Rules Committee considers whether to adopt an approach to cy pres, it should look to the state approaches for inspiration.

## CONCLUSION

Cy pres doctrine has been harshly denounced by its critics who point to questionable cy pres awards as evidence of a "flawed" doctrine. However, these questionable cy pres awards are the result of poor decisions about how and when to select cy pres recipients, rather than evidence of inherent and unresolvable problems with the doctrine. In the absence of a clearly spelled out methodology for courts to follow in approving cy pres, the perception of impropriety will continue to dominate and cast a cloud over even the best uses of cy pres. Cy pres remedies remain superior to other methods for appropriating residual funds because they serve important deterrence goals and, when used properly, further the underlying merits of the class action litigation. Furthermore, cy pres remedies are a necessary mechanism to provide access to justice in cases with small individual harms.

States have been innovating new approaches to cy pres that work to tailor the cy pres doctrine to achieve more consistent and appropriate outcomes. As seen in the case *Judd v. AT&T*, cy pres can be constrained and applied in ways that increase transparency, appropriately tailor awards to the "next best use," and reduce the appearance of impropriety. Washington Civil Rule 23(f) goes a long way towards codifying a

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315. Memorandum from Hon. David G. Campbell, Advisory Comm. on Rules, to Hon. Jeffrey H. Sutton, Chair of the Advisory Comm. on Rules 9 (Dec. 2, 2014), *available at* http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/Reports/CV12-2014.pdf (regarding Report of Advisory Committee on Civil Rules) [hereinafter Report of Rules Advisory Committee]; *see also* Andrew Trask, *The Rules Advisory Committee Study Agenda—Cy Pres*, CLASS ACTION COUNTERMEASURES (Jan. 7, 2015), http://www.classactioncountermeasures.com/2015/01/articles/certification/the-rules-advisory-committee-study-agenda-cy-pres/.

316. Report of Rules Advisory Committee, *supra* note 315, at 9 (emphasis added).

workable approach to cy pres distributions in the class action context. Utilizing a two-tiered rule-based approach, as seen in other jurisdictions such as Maine, can ensure that funds are being used to approximate the interests of class members "as near as possible."