

Unclaimed Settlement Funds and *Cy Pres* Distributions

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Class action settlement funds often have money remaining after class members have filed claims. This may result from class members not being located or because class members, for a variety of reasons, fail to file a claim leaving the total value of perfected claims to be less than the set aside fund. The unclaimed money can be substantial. For example, in *Fears v. Wilhelmina Model Agency, Inc.*, approximately \$6 million remained from a nearly \$22 million settlement fund after all claims were satisfied. No. 02-4911 (HB) (S.D.N.Y. July 5, 2007) (distributing \$6 million in unclaimed funds to seven charities that focus on services utilized by women and the underinsured). In *West Virginia v. Chas. Pfizer & Co.*, approximately \$32 million remained unclaimed from a \$100 million settlement. 314 F. Supp. 710, 722-23, 734 (S.D.N.Y. 1970), *aff'd*, 440 F.2d 1079 (2d Cir.), *cert. denied*, 404 U.S. 871 (1971).

If the settlement agreement does not address how unused funds will be handled, the presiding court must necessarily resolve any resulting dispute or otherwise direct the distribution of such funds. *In re Wells Fargo Sec. Litig.*, 991 F. Supp. 1193, 1194 (N.D. Cal. 1998); *Powell v. Georgia-Pacific Corp.*, 843 F. Supp. 491, 499 (W.D. Ark. 1994), *aff'd by*, 119 F.3d 703 (8th Cir. 1997); 3 HERBERT B. NEWBERG & ALBA CONTE, NEWBERG ON CLASS ACTIONS § 10.15 at 512 (4th ed. 2002) (hereinafter “NEWBERG”) (“[w]hen a class settlement agreement is silent concerning distribution of any surplus . . . the court will have to make a determination about the distribution of the surplus”). In distributing residual funds, courts rely on their general equity power or on the *cy pres* doctrine. “Until the settlement funds are completely distributed, the

court retains its traditional equitable powers.” *Powell*, 843 F. Supp. at 495. “A court may utilize *cy pres* principles to distribute unclaimed funds from a class action settlement.” *Schwartz v. Dallas Cowboys Football Club, Ltd.*, 362 F. Supp. 2d 574, 576 (E.D. Pa. 2005). To avoid surprises or unintended *cy pres* distributions, settling parties need to pay close attention to provisions in settlement agreements that deal with the use of unclaimed settlement monies.

A. Background of *Cy Pres* Distributions

The *cy pres* doctrine takes its name from the Norman French expression *cy pres comme possible*, which means “as near as possible.” *In re Airline Ticket Commission Antitrust Litig.*, 307 F.3d 679, 682 (8th Cir. 2002) (“unclaimed funds should be distributed for a purpose as near as possible to the legitimate objectives underlying the lawsuit”). The doctrine permits residual class action funds to be put to their next best use for the aggregate, indirect, prospective benefit of class members. 3 NEWBERG, *supra* note 3, § 10.17 at 516. *Cy pres* (sometimes called fluid-class) distribution has traditionally been used in class action cases in which class members are difficult to identify or where they change constantly, as when an employer experiences a continuous high-rate of employee turnover or where a utility is found liable for overcharging its customers. *Powell*, 119 F.3d 703, 706 (8th Cir. 1997); 3 NEWBERG, *supra* note 3, § 10.16 at 513, n.1.

The scope of the courts’ discretion in disposing of unclaimed or otherwise undistributed class action settlement funds under the *cy pres* doctrine has expanded significantly in recent years, providing courts with greater flexibility in awarding leftover funds to third-party entities that may bear only a tangential relation to the subject matter of the settling lawsuit. *In re Motorsports Merchandise Antitrust Litig.*, 160 F. Supp. 2d 1392, 1394 (N.D. Ga. 2001); *Superior Beverage Co., Inc. v. Owens-Illinois, Inc.*, 827 F. Supp. 477, 478-79 (N.D. Ill. 1993); *see also*

Adam Liptak, *Doling Out Other People's Money*, N.Y. Times (Nov. 26, 2007), available at: http://www.nytimes.com/2007/11/26/washington/26bar.html?_r=1&oref=slogin (discussing the growing judicial trend of distributing unclaimed class action settlement funds to, among others, charities, law schools, and legal aid societies). “Although the ‘use of funds for purposes closely related to their origin is still the best cy pres application, the doctrine of cy pres and the courts’ broad equitable powers now permit the use of funds for other public interest purposes by educational, charitable, and other public service organizations.” *In re Motorsports*, 160 F. Supp. 2d at 1394 (quoting *Jones v. Nat'l Distillers*, 56 F. Supp. 2d 355, 359 (S.D.N.Y. 1999)).

B. Settlement Provisions Relating to Unclaimed Settlement Funds

In some class action settlements, the settlement agreement fails to address what will happen to money left after class member claims have been processed. On some occasions, this may happen because of an oversight. On others, it may be intentional because the parties hope to make the settlement payout look larger with no stated reversion to the defendant. In any case, a settlement agreement's silence about how to dispose of unused settlement monies will empower the court to determine where the money will be distributed.

With the foregoing in mind, prudent parties will anticipate the possibility of residual class action funds during settlement negotiations and will provide for distribution of such funds in the settlement agreement. 3 NEWBERG, *supra* note 3, § 10.17 at 520. Doing so provides the parties with the best means of insuring that the settlement funds are distributed in accordance with the parties' true intent. Moreover, as one recent commentator has pointed out, “if the court-approved settlement provides for this distribution, there can be no question of the court's power to order that the terms of the agreement be carried out.” K. Forde, *What Can a Court Do with Leftover Class Action Funds? Almost Anything!*, 35 No. 3 Judges' J. 19, 44 (Summer 1996).

Parties who do not include terms in the settlement agreement providing for the disbursement or reversion of unused funds can find themselves back before the court having waived any interest in the remainder of the settlement fund. For instance, in *Powell v. Georgia-Pacific Corp.*, the parties had settled an employment discrimination class action but their agreement was silent about what was to be done with any unclaimed portion of the settlement fund. 843 F. Supp. at 495. Following the claims period, and more than five years after the last distribution from the settlement funds had been made, the plaintiffs filed a motion to distribute the remaining funds. The *Powell* court was quick to point out that neither party negotiated a provision in the consent decree providing for the disbursement or reversion of funds to that party. As such, neither the plaintiffs nor the defendant had any legal right to the unclaimed funds. *Id.*; see also *In re Folding Carton Antitrust Litig.*, 744 F.2d 1252, 1254 (7th Cir. 1984) (neither plaintiff class nor settling defendants had right to excess settlement funds where no provision was made in the settlement agreement for the disposition of such funds); *Schwartz*, 362 F. Supp. 2d at 576 (defendant had no claim to a reversionary interest in residual settlement funds where settlement agreement failed to address issue of distribution of excess funds); *SEC v. Golconda Mining Co.*, 327 F. Supp. 257, 259 (S.D.N.Y. 1971) (same); 3 NEWBERG, *supra* note 3, § 10.17 at 518.

After the plaintiffs in *Powell* moved the court to distribute the remainder of the settlement to the class members who had filed claims, the defendant asked the court to instead distribute the money back to the defendant. *Powell*, 843 F. Supp. at 495. The *Powell* court ultimately rejected both requests, reasoning:

We believe a reversion to the defendant or a distribution to identified class members is not appropriate in this case. No provision was made for the disposition of the remaining funds to either the class members or the defendant. . . . The clear terms of the consent decree and other orders entered in this case lead the

court to conclude that a distribution to either the class or the defendant was not contemplated and in the court's view would not be an equitable distribution of the remaining funds.

Id. at 498. The court therefore ruled that the most appropriate and equitable disposition of the funds was to create a scholarship fund for African-American high school students pursuant to the *cy pres* doctrine. *Id.* at 499, *aff'd by*, 119 F.3d 703 (8th Cir. 1997).

Similarly, *In re Motorsports Merchandise Antitrust Litig.*, involved a consumer class action against vendors of merchandise sold at professional stock car races. 160 F. Supp. 2d 1392 (N.D. Ga. 2001). In that case, the court rejected defendants' request to have excess settlement funds returned to them on a pro rata basis where the settlement documents failed to address the issue of distribution of residual settlement funds. *Id.* at 1394. The court held that "where no legal claim to settlement benefits exists, a court can exercise its equitable powers to distribute the remaining funds" and "attempt to identify charitable organizations that may at least indirectly benefit the members of the class" *Id.* at 1393, 1395; *accord Schwartz*, 362 F. Supp. 2d at 576 (holding that defendant had waived any claim to excess settlement funds and applying *cy pres* doctrine to distribute said funds to nationwide children's charity with ties to the National Football League). The court then opted to distribute \$2.4 million in residual funds to ten different charities – each arguably unrelated to the settling lawsuit. *In re Motorsports*, 160 F. Supp. 2d at 1396-98 (awarding *cy pres* distributions to charities such as the Make-A-Wish Foundation, the American Red-Cross, Children's Healthcare of Atlanta, the Atlanta Legal Aid Society, and the Lawyers Foundation of Georgia); *see also* Robert E. Draba, Note, *Motorsports Merchandise: A Cy Pres Distribution Not Quite "As Near As Possible"*, 16 Loy. Consumer L. Rev. 121 (2004) (suggesting that the distributions in *In re Motorsports* were not consistent with

the *cy pres* doctrine and identifying possible *cy pres* beneficiaries that would have been more closely related to the injured class than those selected by the court).

The cases discussed above illustrate the potential pitfalls created by failing to address the treatment of unused settlement funds in the class action settlement agreement. Any party that has an interest on how those funds will be distributed at the close of a class action settlement should make sure the settlement agreement covers the distribution. The failure to do so may result in the money being distributed against that party's wishes.

C. Choosing *Cy Pres* Recipients

Parties that address the distribution of settlement funds in their settlement agreement often agree that those funds will revert to the defendant in whole or in part or will be distributed on a *cy pres* basis. Courts have recently paid more attention to the parties' choice of *cy pres* recipients. Given this increased focus, settling parties should carefully select recipients whose interests or functions serve the purpose of *cy pres* distributions.

While *In re Motorsports* illustrates the expanding scope of the courts' power to distribute residual class action settlement funds to entities that are only tangentially related to the subject matter of the settling lawsuit, the majority of the courts still follow the traditional rule requiring that some "nexus" exist between the direct harm plaintiffs have suffered and the indirect benefit the *cy pres* distribution is to provide them. See, e.g., *In re Airline Ticket Comm'n Antitrust Litig.*, 307 F.3d at 683; *In re Lease Oil Antitrust Litig.*, MDL No. 1206, 2007 WL 4377835, at *21-22 (S.D. Tex. Dec. 12, 2007); *Schwartz*, 362 F. Supp. 2d at 577. According to one commentator, "[c]harities that do not satisfy the nexus requirement, regardless of how worthy they might otherwise be, are inappropriate under the case law because of the lack of benefit to absent class members." Patricia Sturdevant, *Using the Cy Pres Doctrine to Fund Consumer Advocacy*, 33-

NOV Trial 80, 83 (1997). Necessarily then, courts are paying increased attention to the selection of *cy pres* beneficiaries and to how those entities may or may not be related to the subject matter of the settling dispute.

For example, in *In re Airline Ticket Commission Antitrust Litigation*, the Eighth Circuit Court of Appeals found that the trial court had twice abused its discretion in regard to a *cy pres* distribution in a nationwide class action – first, when “it merely adopted liaison class counsel’s proposed list of mostly local recipients, which had no relationship to the class action suit” (*In re Airline Ticket*, 268 F.3d 619, 626 (8th Cir. 2001); accord *Schwartz*, 362 F. Supp. 2d at 577 (rejecting plaintiffs’ proposed *cy pres* beneficiaries because the beneficiaries did not touch upon the subject matter of the lawsuit and were not national in scope)) and, second, when it failed to distribute the unclaimed funds on remand consistent with the Eighth Circuit’s opinion in the case’s first appeal. *Id.*, 307 F.3d at 680. The trial court’s failure to tailor its *cy pres* distribution to the nature of the underlying lawsuit served as the underpinning for the Eighth Circuit’s rulings on both appeals.

Similarly, the court in *Fears v. Wilhelmina Model Agency, Inc.* recently confronted a situation in which only 5% of the eligible fashion model class members perfected claims against a \$22 million settlement fund. No. 02-4911, 2005 WL 1041134, at *5 (S.D.N.Y. May 5, 2005). Faced with more than \$6 million in residual settlement funds and no obvious direct use for the money that provides a particular benefit to the class, the court invoked the *cy pres* doctrine and ordered that the residual funds be distributed to seven different charities and non-profit organizations likely to assist at least a portion of the class, including an eating disorder program and a substance abuse program. *Id.* at *10, n.1, 11-16; *In re Lease Oil Antitrust Litig.*, 2007 WL

4377835 at *22 (noting that in such circumstances, courts “should search for a use of the fund which has at least a ‘thin’ link to the suit”).

On appeal, the Second Circuit Court of Appeals indicated that it was uncomfortable with the trial court’s *cy pres* distribution. *Masters v. Wilhelmina Model Agency, Inc.*, 473 F.3d 423, 434-36 (2d Cir. 2007). Although the Second Circuit declined to hold that the trial court’s disposition of the excess settlement funds to charities constituted an “abuse of discretion,” it directed the trial court on remand to consider giving the residual funds to actual plaintiffs. *Id.* at 436. On remand, however, the trial court having undertaken considerable research to identify appropriate beneficiaries of the excess funds, concluded that *cy pres* distribution of the funds would avoid providing a windfall to the relatively few models who had made claims and remained the “next best” compensation use for the indirect benefit of the class. Order and Op. at 18; *Fears*, No. 02-4911 (S.D.N.Y. July 5, 2007).

Where the settling parties agree that funds residing in the settlement fund after the final distribution to class members should be designated for *cy pres* distribution, their agreement may outline various suggested *cy pres* beneficiaries. 3 NEWBERG, *supra* note 3, § 10.17 at 520. In doing so, however, the parties must bear in mind that the court retains the discretion to decide how to distribute *cy pres* funds. *In re Tyco Int’l, Ltd.*, --- F. Supp. 2d ---, 2007 WL 4462593, at *11 (D.N.H. Dec. 19, 2007) (“[a]lthough the settlement agreement does not specifically require that I approve the chosen beneficiary of any *cy pres* remedy, . . . I will require [counsel] to obtain my approval before proceeding with any such plan”). In fact, some courts have recently rejected *cy pres* beneficiaries proposed by the parties and have instead selected beneficiaries of their own choosing. *See, e.g.*, Findings and Order Preliminarily Approving Proposed Settlement, *Russo v. NCS Pearson, Inc.*, No. 06-1481 (D. Minn. Aug. 29, 2007) (recognizing *cy pres* beneficiaries

proposed by parties in agreement but ordering that *cy pres* funds, if any, will be awarded at the discretion of the court); *Schwartz*, 362 F. Supp. 2d at 577 n.2 (rejecting *cy pres* distribution advocated by plaintiffs; noting court's sensitivity to the appearance of conflict in selecting a beneficiary with long-established ties to the Eastern District Bench); *Shaw v. Toshiba Am. Info. Sys., Inc.*, 91 F. Supp. 2d 942, 981 (E.D. Tex. 2000) (creating a charity with the unclaimed funds in a \$2.1 billion settlement of nationwide class).

These cases counsel parties to craft settlement agreements to tailor any proposed *cy pres* distribution to the nature of the underlying lawsuit or risk the possibility of being rejected by the court. Ultimately, where the settlement agreement outlines possible *cy pres* remedies if the settlement fund is not extinguished, the greater the likelihood that the terms of the settlement will be carried out consistent with the parties' true intent. Where *cy pres* will be used, the parties should pay close attention to the selection of the recipients.

A fairly extensive body of case law has developed – and continues to develop – on issues relating to the disposition of unclaimed settlement funds in class action litigation. The cases underscore the need for parties to consider the possibility of unused class action settlement funds during settlement negotiations and to carefully draft settlement documents to avoid disputes about the disposition of such funds.