BEWARE OF CY PRES BEARING GIFTS

Vanessa K. Fulton*

The Arizona Supreme Court is presently considering an amendment to Arizona Rule of Civil Procedure 23, which governs class actions. The proposed amendment requires that at least 50% of all residual class action funds be distributed to a state legal aid organization that provides legal services for low-income individuals. Whether the Court adopts this amendment, the proposal presents an opportunity to comment on the current trend of allocating residual class action funds to state legal aid organizations, ostensibly pursuant to the "cy pres" doctrine. Although allocating residual class action funds to a legal aid organization undoubtedly puts these funds to a productive use, to call it "cy pres" is disingenuous. It is improper for a court to adopt such a change by using the cy pres doctrine as a Trojan Horse.[1]

TABLE OF CONTENTS

INTRODUCTION 926

I. BACKGROUND & PURPOSE OF CY PRES IN CLASS ACTIONS 927

II. PROBLEMS WITH THE CURRENT RULES AND STATUTES REGARDING RESIDUAL CLASS ACTION FUNDS 929

A. Allocating the Residual Class Action Funds to State Legal Aid Organizations Threaten the Compensatory Goal of Class Actions and Cy Pres. 930

B. Allocating Residual Class Action Funds to a Legal Aid Organization Does Not Provide the Indirect Benefit Intended by the Cy Pres Doctrine. 931

---

* J.D. Candidate, University of Arizona James E. Rogers College of Law, 2015. Many thanks to Professor Dave Marcus, James D. Smith, partner at Bryan Cave, Steven A. Hirsch, partner at Bryan Cave, Andrew Hall, Cara Wallace, and the *Arizona Law Review* editorial staff for their assistance with this Note.

1. The title of this Note analogizes this topic to the story of the Trojan horse in Ancient Greece. When the Greeks sent the Trojans a huge wooden horse as a supposed gift, one Trojan warned that the Trojans should "beware of Greeks bearing gifts." The Trojan's warning proved prescient when, once the wooden horse was brought inside the city of Troy, Greek soldiers emerged from it and destroyed the city. *See* John M. Frame, *Greeks Bearing Gifts*, *available at* http://www.prpbooks.com/samples/9780875525730.pdf. Similarly, the legal community should be wary of any attempt to use the cy pres doctrine for "gifts" that are unrelated to the original purpose of the cy pres remedy.

III. ARGUMENTS FOR ALLOCATING RESIDUAL CLASS ACTION FUNDS TO LEGAL AID ORGANIZATIONS 933

IV. PROPOSED SOLUTIONS 934

CONCLUSION 936

INTRODUCTION

"Cy pres" is a remedy applied in the class action context that allows residual class-action funds to be allocated to the "next-best use."[2] "Residual funds" include funds leftover after individual claims within the class have been satisfied or funds available when it is entirely impractical to allocate compensation to individual class members at all.[3] A cy pres remedy generally distributes the total amount of residual funds to a third party beneficiary who will use the funds in a way that will indirectly benefit the entire class.[4]

Some courts have allowed cy pres awards that allocate residual funds to a public interest charity.[5] The public interest charity is often a legal aid organization that provides legal services to individuals who otherwise would be unable to afford those services. Currently, fifteen states have rules or statutes that suggest or require residual class action funds be allocated to state legal aid organizations.[6] Six of these states implemented the change by statute,[7] while the remaining nine did so

---

2. *See, e.g.*, Newberg on Class Actions § 11:20 (4th ed. 2002); Nachshin v. AOL, LLC, 683 F.3d 1034, 1038 (9th Cir. 2011) (quoting Masters v. Wilhelmina Model Agency, Inc., 473 F.3d 423, 436 (2d Cir. 2007)) ("[A] court may employ the *cy pres* doctrine to 'put the unclaimed fund to its next best compensation use, e.g. for the aggregate, indirect, prospective benefit of the class.'").

3. *See, e.g.*, *Nachshin*, 683 F.3d at 1038.

4. *See, e.g.*, Dennis v. Kellogg Co., 697 F.3d 858, 865 (9th Cir. 2012); *In re* Airline Ticket Comm'n Antitrust Litig., 307 F.3d 679, 682 (8th Cir. 2002) (noting that under cy pres, "the unclaimed funds should be distributed for a purpose as near as possible to the legitimate objectives underlying the lawsuit, the interests of class members, and the interest of those similarly situated").

5. Most courts justify allocating residual class action funds to a public interest charity under the "courts' broad equitable powers." Superior Beverage Co., Inc. v. Owens-Illinois, Inc., 827 F. Supp. 477, 479–80 (N.D. Ill. 1993) (distributing residual funds from an antitrust class action to various applicants including an art museum, the American Jewish Congress, a public television station, and a civil liberties union); *In re* Motorsports Merch. Antitrust Litig., 160 F. Supp. 2d 1392, 1396–99 (N.D. Ga. 2011) (distributing residual funds from a price fixing class action involving merchandise sold at professional stock car races to organizations such as a hospital, the American Red Cross, and the Susan G. Komen Breast Cancer Foundation).

6. Jones v. Nat'l Distillers, 56 F. Supp. 2d 355, 359 (S.D.N.Y. 1999) ("[C]ourts have approved charitable donations of unclaimed settlement funds to support non-profit provision of pro bono legal services.").

7. *See* Cal. C.C.P. § 384; 735 I.L.C.S. 5/2-807; Neb. Rev. St. § 30-3839; N.C. Gen. Stat. § 1-267.10; S.D. Codified Laws § 16-2-57; Tenn. R. Civ. P. 23.08.

through court rules.[8] An important question concerning these rules and statutes centers upon whether allocation of residual class action funds to a state legal aid organization is an appropriate use of the cy pres doctrine.[9] This is a separate inquiry from whether the cy pres remedy in general is appropriate in the class action context.[10] Rather, the debate focuses only on whether it is appropriate to use the cy pres doctrine to allocate residual class action funds to a state legal aid organization.

Although the rules and statutes that allocate residual class action funds to state legal aid organizations put these funds to a productive use, to call this allocation a "cy pres remedy" is disingenuous. The use of the cy pres remedy to allocate residual funds to a legal aid organization represents a disconnect from the underlying goals of the cy pres doctrine in the class action context. The decision to allocate residual class action funds to a legal aid organization should not be implemented as a procedural change disguised under the cy pres doctrine. Rather, the decision should be implemented through the legislative branch and the legislature should choose in advance a specific legal aid organization that will receive the residual funds. Additionally, there should be strict guidelines as to when funds are considered "residual" and may be allocated to a third party beneficiary. Finally, any legislation that directs residual class action funds to a third party beneficiary should always permit the parties to override the statute by agreement.

This Note proceeds in three parts. Part I examines the background and purpose of class actions. Part II considers the problems with using cy pres to allocate residual class action funds to third parties. Specifically, it addresses how allocating residual class action funds to legal aid organizations threaten the compensatory purpose of class actions and does not meet the indirect benefit requirement of cy pres. Part III briefly discusses the benefits to the proposed rules and statutes that allocate residual class action funds to legal aid organizations. Finally, Part IV proposes that any rules or statutes allocating residual class action funds to legal aid organizations should be adopted through the legislature, and provides a few guidelines for courts to consider when applying these statutes.

I. BACKGROUND & PURPOSE OF CY PRES IN CLASS ACTIONS

The class action is a procedural device that allows a court to join together similar individual claims too numerous to be joined and too burdensome to be litigated individually.[11] Class actions are appropriate when the claims of each class

---

8. *See* Hawaii R. Civ. P. 23; Ind. R. Trial P. 23(F)(2); Kentucky R. Civ. P. 23.05; Louisiana Sup. Ct. Rule 43; Maine R. Civ. P. 23; Mass. R. Civ. P. 23; N.M.R.A. 1-023; Pa. R. Civ. P. 1716; Wash. Super. Ct. C.R. 23.

9. *See, e.g.*, Martin H. Redish et al., *Cy Pres Relief and the Pathologies of the Modern Class Action: A Normative and Empirical Analysis*, 62 FLA. L. REV. 617 (2010); 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 (2014).

10. This Note is not focused on whether cy pres is permissible in itself.

11. Phillips Petroleum Co. v. Shutts, 472 U.S. 797, 808 (1985) ("[T]he class action was an invention in equity to enable it to proceed to a decree in suits where the

member are extremely small, such that individual suits are not feasible.[12] The class action device provides for efficient and effective resolution of all class members' claims.[13]

The class action has two central goals: to compensate injured class members, and to deter misconduct.[14] First, the class action aims to ensure that each class member harmed by the defendant's conduct receives compensation for his or her injuries.[15] Second, the class action attempts to deter misconduct by making the defendant internalize and pay for the costs of its harmful actions.[16] An individual class member's claim, on its own, might not be significant enough to deter the defendant from future wrongful conduct, but aggregated claims increase deterrence.[17] The class action also incentivizes individual class members to bring claims which otherwise might not be worth the individual litigation costs.[18] The class action allows individual class members to receive compensation that they would not have received without the class action.

Usually, a settlement or a judgment in favor of the class will attempt to accomplish both goals—compensation and deterrence—by creating a general fund, financed by the defendant, and notifying class members of their right to compensation from the fund.[19] However, it is often difficult to notify every class member, and some class members, even after receiving notice, may still choose not to pursue their claim and obtain compensation from the class action settlement or judgment.[20] As a result, a significant amount of money is leftover due to the

---

number of those interested in the litigation was too great to permit joinder."); Califano v. Yamasaki, 442 U.S. 682, 700–01 (1979) ("[T]he Rule 23 class-action device was designated to allow an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only.").

12. *See* Amchem Prods., Inc. v. Windsor, 531 U.S. 591, 617 (1997) ("The policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights.") (quoting Mace v. Van Ru Credit Corp., 109 F.3d 338, 344 (1997)).

13. Shady Grove Orthopedic Assocs., P.A. v. Allstate Ins. Co., 559 U.S. 393, 402 (2010).

14. Newberg on Class Actions §§ 1:7, 1:8 (5th ed. 2011).

15. *Id.* § 1:8. *See also In re* Baby Prods. Antitrust Litig., 708 F.3d 163, 173 (3d Cir. 2013) ("The private causes of action aggregated in this class action—as in many others—were created by Congress to allow plaintiffs to recover compensatory damages for their injuries.").

16. Newberg on Class Actions, *supra* note 14, § 1:8.

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

17. *Shady Grove Orthopedic Assocs., P.A.*, 559 U.S. at 402.

18. *See* Amchem Prods., Inc. v. Windsor, 531 U.S. 591, 617 (1997) ("The policy at the very core of the class action mechanism is to overcome the problem that small recoveries do not provide the incentive for any individual to bring a solo action prosecuting his or her rights.") (quoting Mace v. Van Ru Credit Corp., 109 F.3d 338, 344 (1997)).

19. Klier v. Elf Atochem N. Am., Inc., 658 F.3d 468, 473 (5th Cir. 2011).

20. *Id.* ("When modern, large-scale class actions are resolved via settlement, money often remains in the settlement fund even after initial distributions to class members

large majority of claimants who did not receive or seek compensation from the class action fund for the harm the defendants inflicted.[21]

What happens to these residual class action funds? How can they be used to promote the compensatory and deterrent goals of class actions? Courts increasingly turn to a cy pres remedy that attempts to allocate the funds to a third party beneficiary who will use the funds to provide an indirect benefit to the class members.[22] However, despite the growing use of the cy pres remedy, some courts and scholars have begun to question whether the remedy is being stretched too far from its original purpose in the class action context.[23] For example, in a recent denial of certiorari, Supreme Court Chief Justice Roberts acknowledged that cy pres remedies "are a growing feature of class action settlements" and suggested that in an appropriate case, the Supreme Court "may need to clarify the limits of the use of [cy pres]" in the class action context.[24]

Additionally, several critics have argued that cy pres remedies are inappropriate in the class action context because such a remedy changes the substantive rights and liabilities of the parties.[25] Regardless, whether these arguments will ultimately prevail, the debate highlights several issues courts should address when implementing a cy pres remedy.

II. PROBLEMS WITH THE CURRENT RULES AND STATUTES REGARDING RESIDUAL CLASS ACTION FUNDS

As mentioned above, in addition to the amendment currently pending before the Arizona Supreme Court, 15 states have rules or statutes that direct residual class action funds to state legal aid organizations.[26] Despite variety in the actual language of the rules and statutes, the fundamental challenges they pose are the same—the proposals represent a disconnect from the underlying purpose of the class action doctrine by ignoring the compensatory purpose of class actions and stretching the concept of "indirect benefit to the class member" too far.

---

have been made because some class members either cannot be located or decline to file a claim.").

21. *See, e.g.*, *In re* Motorsports Merch. Antitrust Litig., 160 F. Supp. 2d 1392, 1393 (N.D. Ga 2001) ("It is not uncommon in consumer class actions to have funds remaining after payment of all identifiable claims."); Superior Beverage Co. v. Owens-Illinois, Inc., 827 F. Supp. 477, 478 (N.D. Ill. 1993).

22. *See, e.g.*, *In re Motorsports Merch. Antitrust Litig.*, 160 F. Supp. at 1393.

23. *See, e.g.*, Nachshin v. AOL, LLC, 663 F.3d 1034, 1038 (2011) ("[A]s 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."); *In re* Lupron Mktg. & Sales Practices Litig., 677 F.3d 21, 24 (1st Cir. 2012).

24. Marek v. Lane, 134 S. Ct. 8, 9 (2013).

25. *See, e.g.*, Redish et al., *supra* note 9.

26. *See supra* notes 7–8 and accompanying text. For the current rule pending before the Arizona Supreme Court, see Petition to Amend Rule 23, Rules of Civil Procedure, Court Rules Forum, http://azdnn.dnnmax.com/AZSupremeCourtMain/AZCourtRulesMain/CourtRulesForumMain/CourtRulesForum/tabid/91/view/topic/forumid/2/postid/2518/Default.aspx (last visited Sept. 1, 2014).

A. Allocating the Residual Class Action Funds to State Legal Aid Organizations Threaten the Compensatory Goal of Class Actions and Cy Pres.

Courts and scholars often view the main purpose of a cy pres remedy to require the defendant to pay for its conduct in situations where it would be impractical to distribute compensation to each individual class member.[27] However, cy pres is intended not only to deter the defendant from future wrongful conduct, but also to compensate injured class members.[28] The importance of both deterrence and compensation in a cy pres remedy is evidenced by several courts' rejection of alternative options for dealing with residual class action funds and their subsequent adoption of the cy pres doctrine.[29]

What are the alternative options to cy pres that courts have rejected? First, several scholars have noted that a court faced with possible residual funds could simply refuse "to authorize the class proceeding in the first place."[30] However, this option would frustrate both of the underlying class action goals—without authorization, there is no class action at all and no compensatory or deterrent effect. As a result, courts rarely refuse to authorize the class proceeding unless it is clear that the class action would result in residual funds and the existence of those funds would create issues of manageability.[31]

Second, the residual funds could revert to the defendant.[32] The problem with this option is that it minimizes or eliminates the deterrent effect; a particularly troubling outcome in cases where the court has already determined the defendant violated the law.[33] Even in cases where the residual funds result from a settlement between the parties, reversion of residual funds to the defendant "risks undermining the deterrent effect of class actions by rewarding defendants for the failure of class members to collect their share of the settlement."[34] Additionally,

---

27. *See, e.g.*, Mirfasihi v. Fleet Mortg. Corp., 356 F.3d 781, 784 (7th Cir. 2004) (explaining cy pres is used in the class action context "to prevent the defendant from walking away from the litigation scot-free because of the infeasibility of distributing the proceeds of the settlement"); Boies & Keith, *supra* note 9, at 289.

28. *See, e.g.*, *In re* Matzo Food Prods. Litig., 156 F.R.D. 600, 607 (D.N.J. 1994) (explaining that a class action settlement, "quite obviously, cannot be approved based solely on the fact that it has punitive or deterrent impact on the defendants"); Democratic Cent. Comm. of D.C. v. Wash. Metro. Area Transit Comm'n, 84 F.3d 451, 455 (D.C.C.A. 1996) ("The object of applying [residual] funds to the 'next best' class is to parallel the intended use of the funds as nearly as possible by maximizing the number of plaintiffs compensated."); Hughes v. Kore of Ind. Enter., Inc., 731 F.3d 672, 677 (7th Cir. 2013) ("A class action, like litigation in general, has a deterrent as well as a compensatory objective.").

29. *See, e.g.*, *In re* Baby Prods. Antitrust Litig., 708 F.3d 163 (3d Cir. 2013).

30. Redish et al., *supra* note 9, at 619. *See, e.g.*, *In re* Hotel Tel. Charges, 500 F.2d 86, 91–92 (9th Cir. 1974) ("When, as here, there is no realistic possibility that the class members will in fact receive compensation, then monolithic class actions raising mind-boggling manageability problems should be rejected.").

31. *See, e.g.*, *In re Hotel Tel. Charges*, 500 F.2d at 91–92.

32. Six (6) Mexican Workers v. Ariz. Citrus Growers, 904 F.2d 1301, 1307 (9th Cir. 1990).

33. *Id.* at 1308; Diamond Chem. Co., Inc. v. Akzo Nobel Chems. B.V., 517 F. Supp. 2d 212, 218–19 (D.D.C. 2007). *See also* Redish et al., *supra* note 9, at 619.

34. *In re Baby Prods. Antitrust Litig.*, 708 F.3d at 172.

this method does not fully advance the goal of compensating class members: it essentially guarantees that class members who do not file a claim for compensation from the fund receive no benefit at all, direct or indirect.[35] Courts' refusal to allow residual class action funds to revert to the defendant suggests that both deterrence and compensation are important in a class action remedy.

Third, the court could allocate the residual class action funds pro rata to the class members who have already filed claims and received some compensation.[36] Courts have rejected this option because it results in a huge windfall to the class members who did file claims, at the expense of the other, albeit silent, class members who are entitled to compensation. The fact that courts are not willing to allocate the residual funds pro rata to the class members who have already received funds suggests that compensation is an important goal of class actions.[37]

Fourth, the residual funds could escheat to the state, similar to unclaimed property.[38] This method also furthers the deterrence goal of class actions,[39] but courts have rejected it because it results in no further compensation to injured class members. Additionally, escheatment is often rejected because "it benefits the community at large rather than those harmed by the defendant's conduct."[40] The fact that courts are often unwilling to allow residual class action funds to escheat to the state suggests that courts are not willing to completely disregard the compensation goal and that courts are often hesitant to grant cy pres remedies when the beneficiaries are not limited to the class members, but rather consist of the community at large.

B. Allocating Residual Class Action Funds to a Legal Aid Organization Does Not Provide the Indirect Benefit Intended by the Cy Pres Doctrine.

Cy pres remedies are designed to put money to its next-best use for the benefit of class members in situations where its best use—direct compensation—

---

35. Natalie A. DeJarlais, *The Consumer Trust Fund: A Cy Pres Solution to Undistributed Funds in Consumer Class Actions*, 38 HASTINGS L.J. 729, 750 (1987).

36. *See, e.g.*, *In re* Janney Montgomery Scott LLC Fin. Consultant Litig., No. 06-3202, 2009 WL 2137224, at *11 (E.D. Pa. 2009) (providing that, if the residual funds amount to over $50,000, any amount over $50,000 "shall be distributed on a proportional basis to those class members who cashed their checks").

37. Stewart R. Shepherd, *Damage Distribution in Class Actions: The Cy Pres Remedy*, 39 U. CHI. L. REV. 448, 453 (1972).

38. The Ninth Circuit has used this option "when it served the deterrence and enforcement goals of the substantive federal statute." Six (6) Mexican Workers v. Ariz. Citrus Growers, 904 F.2d 1301, 1308 (9th Cir. 1990) (citing Hodgson v. YB Quezada, 498 F.2d 5, 6 (9th Cir. 1974)). *See also* S.E.C. v. Bear, Stearns & Co. Inc., 626 F. Supp. 2d 402, 419 (S.D.N.Y. 2009) (transferring the residual funds to the United States Department of Treasury).

39. *See, e.g.*, *In re* Folding Carton Antitrust Litig., 744 F.2d 1252, 1259 (7th Cir. 1984) ("[T]o the extent that antitrust law serves a deterrence purpose, it is served through any plan not resulting in return of the fund to the defendants").

40. *In re* Baby Prods. Antitrust Litig., 708 F.3d 163, 172 (3d Cir. 2013).

cannot be realized.[41] But at what point is the indirect benefit so attenuated that it can no longer be considered to benefit the class members?

In *Nachshin v. AOL, LLC*, the Ninth Circuit Court rejected a cy pres distribution of residual funds 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.[42] The court found that the proposed cy pres distributions failed to "(1) address the objectives of the underlying statutes, (2) target the plaintiff class, or (3) provide reasonable certainty that any member will be benefitted."[43] The court rejected two of the three charities initially because they did not "account for the broad geographic distribution of the class."[44] With respect to the Federal Judicial Center Foundation, the court acknowledged that, although this organization may account for the broad geographic distribution of the class, it "has no apparent relation to the objectives of the underlying statutes, and it is not clear how this organization would benefit the plaintiff class."[45]

Similarly, in *Dennis v. Kellogg*, the Ninth Circuit rejected a proposed cy pres remedy that would allocate residual class action funds to charities that "feed the indigent."[46] The complaint alleged that Kellogg had engaged in false advertising regarding the effect of its cereal on children's attentiveness.[47] The court found that the proposed use of the residual funds, although it furthered a "noble goal," had "little or nothing to do with the purposes of the underlying lawsuit or the class of plaintiffs involved."[48] The court also noted that it was likely that the charity receiving the cy pres funds did not "serve a single person within the plaintiff class."[49]

Supporters of the statutes and rules that direct residual class action funds to legal aid organizations argue that the class members necessarily receive an indirect benefit when the residual funds are distributed to a legal aid organization.[50] This is so, they argue, because legal aid organizations promote an interest every class member has in common—"access to justice for a group of litigants, who, on their own, would not realistically be able to seek court relief."[51] This argument assumes that the underlying premise for all class actions is "to make access to justice a reality for people who otherwise would not be able to

---

41. "Even where cy pres is considered, it will be rejected when the proposed distribution fails to provide the 'next best' distribution." *Six (6) Mexican Workers*, 904 F.3d at 1308. In *Six (6) Mexican Workers*, the Ninth Circuit rejected the cy pres remedy because, although it would provide distribution "to areas where the class members may live," there was "no reasonable certainty" that any class member would be benefited. *Id.*

42. Nachshin v. AOL, LLC, 663 F.3d 1034, 1040 (9th Cir. 2011).

43. *Id.*

44. *Id.*

45. *Id.*

46. Dennis v. Kellogg Co., 697 F.3d 858, 866 (9th Cir. 2012).

47. *Id.* at 861.

48. *Id.* at 866.

49. *Id.* at 867.

50. Boies & Keith, *supra* note 9, at 291.

51. *Id.*

obtain the protections of the justice system."[52] Although it is true that access to justice is one goal of the class action doctrine, this argument is flawed for three reasons, each of which relate to the rule the Ninth Circuit stated in *Nachshin*.

First, this indirect benefit applies irrespective of the legal basis for the class members' claims.[53] As a result, this argument fails to take into account the objective of the class action to enforce the underlying substantive law. Second, this argument ignores the fact that the class members may have interests that significantly outweigh any interest in access to justice.[54] For example, the class members may have a strong interest in obtaining compensation for their injuries. As a result, allocating the residual funds to a legal aid organization fails to target the specific interests of the class members. Third, although class members may receive some *de minimis* benefit, it is the same benefit every American receives in a generic sense from having broader access to justice.[55] In other words, any benefit class members receive is not specific to the purpose of their participation in the class action. As a result, the "benefit" class members receive from allocating residual class action funds to a legal aid organization is not really a benefit at all, because nonclass members enjoy it to the same extent that class members do.

Supporters of the rules and statutes that allocate residual class action funds to legal aid organizations also argue that permitting only certain legal aid organizations suggests that these permitted organizations "are distinct from other charitable causes that have drawn legitimate concerns regarding a lack of nexus with the interests of the class members."[56] Although this argument acknowledges that allocating residual class action funds to a legal aid organization is a productive use of those funds, it does not address why this productive use of residual funds provides any more of a benefit to the class members.

III. ARGUMENTS FOR ALLOCATING RESIDUAL CLASS ACTION FUNDS TO LEGAL AID ORGANIZATIONS

Although these proposed rules may have legitimacy issues, they also alleviate some of the general problems courts have expressed concerning the application of cy pres remedies in the class action context. Proponents argue that allocating residual class action funds to a legal aid organization removes any concern of judicial bias and preserves judicial resources.

First, specifically allocating residual funds to a legal aid organization prevents a judge from being "put in the role of distributing cy pres funds at their discretion," a concern expressed by several courts.[57] However, it is important to

---

52. *Id.* at 290.

53. *See* Nachshin v. AOL, LLC, 663 F.3d 1034, 1039 (9th Cir. 2011) (noting that cy pres should "address the objectives of the underlying statutes").

54. *See id.* (observing that cy pres should "target the plaintiff class").

55. *See id.* (maintaining that cy pres should provide "reasonable certainty that [class members] will be benefitted").

56. Boies & Keith, *supra* note 9, at 293.

57. *In re* Lupron Mktg. & Sales Practices Litig., 677 F.3d 21, 24, 38 (1st Cir. 2012) ("[W]e express our concerns that district courts are given discretion by parties to decide on the distribution of cy pres funds."); ALI Principles §3.07(c) ("[T]he court, when

note that if the statute does not specify a certain legal aid organization, the threat of judicial bias is still present.[58] "Distribution of funds at the discretion of the court is not a traditional Article III function," and the adversary process generally favors agreements between the parties whenever possible.[59] Additionally, identification of a specific organization that will receive the residual funds protects against possible self-interest issues with the parties or counsel.[60]

Second, allocating the residual class action funds to a state legal aid organization alleviates any concern regarding the need to monitor cy pres recipients and ensure they "abide by conditions [judges] or the settlement agreements set." [61] Finally, allocating the funds to a legal aid organization, although not providing a direct benefit to class members, furthers the deterrence goal of class actions and provides a benefit to society in general—broader access to legal services.

However, these benefits do not change the fact that cy pres is not the appropriate tool for adopting this method. Allocating residual class action funds to a third party unrelated to the class action litigation is inconsistent with the cy pres doctrine in the class action context.

IV. PROPOSED SOLUTIONS

In light of the foregoing, the best course of action may be to embrace these new rules, but place additional parameters on their adoption and use. These rules should (1) be independent from the cy pres doctrine, (2) have specific limits as to when funds are considered "residual" and may be allocated to a legal aid organization, (3) remove any possible bias through adopting a detailed statute through the legislature, and (4) always permit the parties to override the statute by agreement.

First, the decision to allocate residual class action funds should be independent from the concept of a cy pres remedy. The cy pres remedy in the class

---

feasible, should require the parties to identify a recipient whose interests reasonably approximate those being pursued by the class.").

58. For example, compare South Dakota's statute, which specifies that residual funds shall be allocated to the "Commission on Equal Access to Our Courts" with New Mexico's statute that provides a broad range of permissible charities including "nonprofit organizations that provide legal services to low income persons." SDCL § 16-2-57; NMRA 1-023(G)(2)(c).

59. *In re Lupron Mktg. & Sales Practices Litig.*, 677 F.3d at 24, 38. *See also In re* Compact Disc Minimum Advertised Price Antitrust Litig., 236 F.R.D. 48, 53 (D. Me. 2006) ("Federal judges are not generally equipped to be charitable foundations: we are not accountable to boards or members for funding decisions we make; we are not accustomed to deciding whether certain nonprofit entities are more 'deserving' of limited funds than others.").

60. Dennis v. Kellogg Co., 697 F.3d 858, 867 (9th Cir. 2012) (citing *Nachshin*, 663 F.3d at 1039) ("When selection of *cy pres* beneficiaries is not tethered to the nature of the lawsuit and the interests of the silent class members, the selection process may answer to the whims and self interests of the parties, their counsel, or the court.").

61. *In re Compact Disc Minimum Advertised Price Antitrust Litig.*, 236 F.R.D. at 53; *In re Lupron Mktg. & Sales Practices Litig.*, 677 F.3d at 24, 38.

action context requires that residual funds be used to provide the "next best" benefit to the class members, short of direct compensation. Any indirect benefit that the class members may arguably receive from directing residual funds to a legal aid organization is too attenuated to be considered the "next best" alternative to direct compensation. As a result, if states wish to direct residual class action funds to legal aid organizations, they should do so separate from the concept of cy pres.

Second, the rules allocating funds to legal aid organizations should only permit allocation of residual funds when the absent class members have received adequate notice[62] and the class members who have filed a claim have been compensated for 100% of their losses.[63] In regard to notifying the absent class members of their right to file for compensation from the available fund, the court should require a heightened scrutiny of the notice provided to the absent class members.[64] The court must ensure that cy pres is not used as a tool to circumvent the notice requirements.[65] Factors the court should consider in this analysis are: whether the class counsel has met or exceeded the minimum notice requirements;[66] whether the cy pres award represents a large or small percentage of the total settlement funds;[67] and whether the parties have appropriately estimated the defendant's anticipated liability.[68] When the cy pres award represents a large percentage of the total settlement funds or the parties have not made a clear attempt to estimate the defendant's anticipated liability, the court should look closely at the notice provided to the absent class members.[69]

After the court ensures that the absent class members have received adequate notice, funds should still only be allocated to legal aid organizations if

---

62. Redish et al., *supra* note 9, at 633 (as "originally contemplated, cy pres would be used only in large classes with unclaimed remainders").

63. *In re* Pharm. Indus. Average Wholesale Price Litig., 588 F.3d 24, 35 (1st Cir. 2009) (explaining that cy pres remedies are only appropriate after the class members have been 100% compensated for their injuries).

64. It is particularly important that the court is "vigilant" when examining a proposed cy pres remedy settlement "that has a tenuous relationship to the class allegedly damaged by the conduct in question." *Dennis*, 697 F.3d at 869.

65. Six (6) Mexican Workers v. Ariz. Citrus Growers, 904 F.2d 1301, 1305 (9th Cir. 1990).

66. The minimum notice requirements are described in *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 812 (1985).

67. *Dennis*, 697 F.3d at 869; *In re* Baby Prods. Antitrust Litig., 708 F.3d 163, 174 (3d Cir. 2013) ("Barring sufficient justification, cy pres awards should generally represent a small percentage of total settlement funds.").

68. *Dennis*, 697 F.3d at 869 ("The issue of valuation of this aspect of a settlement must be examined with great care to eliminate the possibility that it serves only the 'self-interests' of the attorneys and the parties, and not the class, by assigning a dollar number to the fund that is ficticious.").

69. *See In re Baby Prods. Antitrust Litig.*, 708 F.3d at 174 (explaining that in reviewing a proposed settlement that includes a cy pres remedy, the court should consider "the number of individual awards compared to both the number of claims and the estimated number of class members, the size of the individual awards compared to the claimants' estimated damages, and the claims process used to determine individual awards").

the court determines that the class members who have already filed claims have been compensated 100% for their losses.[70] Currently, the rule before the Arizona Supreme Court allows a court to allocate funds to a legal aid organization when there are residual funds, or when it is "economically impractical" to allocate the funds in the first place. This ambiguous language creates concerns that the focus may shift away from prioritizing direct compensation first, and favor indirect compensation instead. The American Law Institute guidelines express concern that "few settlements award 100 percent of a class member's losses, and thus it is unlikely in most cases that further distributions to class members would result in more than 100 percent recovery."[71] As a result, before the residual funds are distributed to a legal aid organization, the court should look to see if the class members who have filed claims have been fully compensated.[72]

Third, to alleviate any potential bias, any rule that requires residual class action funds be distributed to a legal aid organization should be adopted through the legislature as opposed to the judiciary and should mandate a specific organization that should receive the funds. Adopting the rule through the legislature instead of the judiciary eliminates any possible judicial bias by allowing the public to choose a specific third party legal aid organization as a beneficiary for the residual funds.

Fourth, any rule or statute allocating residual class action funds to a legal aid organization should permit the parties in a class action to contract around the rule by including specific language in the settlement agreement. A court "must abide by the provisions of the settlement agreement" and cy pres should be used "only to rescue the objectives of the settlement when the agreement fails to do so."[73] As a result, if the parties have agreed in advance on what will happen to the residual funds, the intent of the parties should prevail and the parties should not be forced to funnel the residual funds into a third party beneficiary.

CONCLUSION

Although the statutes and rules that allocate residual class action funds to legal aid organizations have an admirable purpose, pretending that they provide the "next-best" benefit to the class members is stretching the cy pres doctrine too far. It is important that courts and legal scholars clearly mark the limits of the cy pres doctrine to prevent potential abuse or even changes in substantive rights.

---

70. Klier v. Elf Atochem N. Am., Inc., 658 F.3d 468, 475 (5th Cir. 2011) ("Where it is still logistically feasible and economically viable to make additional pro rata distributions to class members, the district court should do so, except where additional distribution would provide a windfall to class members with liquidated-damages claims that were 100 percent satisfied by the initial distribution.").

71. American Law Institute, Principles of Aggregate Litigation § 3.07, cmt. b (2010).

72. *See In re* Pharm. Indus. Average Wholesale Price Litig., 588 F.2d 24, 35 (1st Cir. 2009).

73. *Klier*, 658 F.3d at 475–76.