

## CY PRES: THE MYTHS AND MISCONCEPTIONS

### PERSPECTIVE

By Richard L. Kellner and Artin Gholian

Over the past few years, the *cy pres* mechanism in class action settlements has come under increasing attack. Opponents contend that *cy pres* harms, rather than advances, the public's interests in class action settlements. The opponents of *cy pres* fail to recognize that *cy pres* often provides the only method by which meaningful relief can be provided to a class where the primary relief sought is injunctive and the monetary damage sustained by individual class members is minimal. In truth, *cy pres* provides an indispensable means for ensuring that the entire class receives the maximum benefit from any class action settlement.

Misconceptions about the *cy pres* mechanism are best exemplified by a recent *Wall Street Journal* article in which *cy pres* is described by opponents as a mechanism that short changes consumers. See Nathan Koppel, *Wall Street Journal*, "Proposed Facebook Class Action Settlement Comes Under Fire," (March 2, 2010). Fortunately, this position has been rejected by many legislatures across the nation. They mandate the *cy pres* remedy in certain settlements as a means to advance consumer rights in the face of corporate greed. As the California Legislature noted in enacting Code of Civil Procedure Section 384(a), "It is the intent of the Legislature in enacting this section to ensure that the unpaid residuals in class action litigation are distributed, to the extent possible, in a manner designed either to further the purposes of the underlying causes of action, or to promote justice for all Californians." California courts have cited to this legislative intent in upholding *cy pres* disbursements. *In re Microsoft I-V Cases*, (2006) 135 Cal.App.4th 706, 717-720.

Under California law, our courts can rely on Section 384 to maximize class benefits by ordering the distribution of unclaimed settlement funds to specified charities. It is important to note however that Section 384 has not been interpreted to preclude the reversion of settlement funds back to the defendants, if so stated in an approved settlement.

The *cy pres* mechanism in class actions generally directs certain class benefits to designated charities if they otherwise would not be used. For example, when class members fail to deposit settlement checks, many class settlements provide that such unused proceeds go to charities rather than revert back to the corporate defendant. In other circumstances, where the class harm is so small that the class will not materially benefit from the settlement (e.g., where the cost of mailing the settlement checks are more than the amount that each class member will receive), class settlements that dedicate large sums to charities will not only provide a monetary deterrence to future harm to the class, but also provide a benefit that is aligned with the interests of the class.

By all accounts, the *cy pres* mechanism advances the public interests embodied by class actions, and preserves rather than dilutes a corporate defendant's obligations in many consumer class action settlements. For this reason, it is not surprising that *cy pres* is opposed by corporate lobbying and advocacy groups such as the Center for Class Action Fairness, which is funded by large corporate interests. Excepting these lobbyists and proxies for large

corporate interests, the *cy pres* mechanism is favored by lawmakers, judges and consumers for its efficacy in protecting consumers.

In fact, when the California Legislature enacted Section 384(b), it specified the types of charities that should benefit from *cy pres* awards. Those charities include nonprofit organizations and foundations that benefit the class or promote the law consistent with the purpose of the underlying action, as well as child advocacy programs and nonprofit organizations that provide civil legal services to the indigent. Such legal services organizations in Southern California include Bet Tzedek and the Inner City Law Center. Both play a vital role in making the legal system accessible to less fortunate members of our society.

Examples of instances in which *cy pres* were properly used under Section 384(b) amply demonstrate why *cy pres* is an important part of our judicial system and the class action process. In the *In re Microsoft I-V Cases*, Microsoft was obligated to pay \$1.1 billion, of which one-third was designated as a *cy pres* remedy. While there were literally millions of individuals who stood to have a minimal benefit from the settlement, the trial court approved a settlement in which over \$300 million of the settlement proceeds provided free computer hardware and software to public schools in California. Given our state's present economic crisis, it is difficult to find anyone who could find fault with a settlement that resulted in hundreds of millions of dollars of computer products being donated to our public schools, many of which serve disadvantaged populations.

Even so, there were objectors to the *In re Microsoft I-V Cases* settlement. Among other things, the objectors claimed that the *cy pres* award of hundreds of millions of dollars to our schools was not authorized by Section 384. The Court of Appeal affirmed the trial court's order approving the settlement, reasoning that the settlement fulfilled the purposes of the underlying action, and was thus consistent with Section 384(a) because it fulfilled the purposes of the underlying cause of action. The court also upheld the trial court's findings that the contemplated *cy pres* distribution to California schools "serving students from low income households benefits the [c]lass by insuring that a new generation of computer literate children will enter the work force fully trained to make the best use of computer technology."

Another great example of the laudable use of the *cy pres* mechanism was in the recent Armenian Genocide Insurance Settlements, which settled claims brought on behalf of heirs of the victims of the Armenian Genocide who were improperly denied life insurance benefits. The settlements, for which we were co-lead counsel for the class, provided for tens of millions of dollars in payments to class members. However, the passage of over 80 years since the Armenian Genocide made it impossible to find many of the rightful heirs to those who were deprived life insurance benefits. Instead of having the monies revert back to the insurance companies (which would have resulted in a business windfall for them), the settlement provided that all unclaimed monies would go to qualified Armenian charities. Thus, the *cy pres* mechanism addressed the problem of unclaimed funds. And it ensured that the interests of the class would be promoted by providing actual benefits to the class through the work done by various Armenian charities. As a result, millions of dollars in settlement proceeds were distributed to Armenian relief organizations, churches and charities.

The opponents of *cy pres* would prefer that the unused settlement proceeds simply revert back to the corporate defendants. If their arguments are stripped of their vituperative rhetoric, the only reason for opposing *cy pres* in these situations is self-evident and self-serving.

In the age of Enron, WorldCom and Madoff, class actions remain one of the primary means of defending consumer rights. *Cy pres* gives our courts the means to maximize class benefits and provide actual benefits to class members from unclaimed settlement proceeds. Thus, as the California Supreme Court aptly ruled in *State of California v. Levi Strauss & Co.*, "[W]ithout fluid recovery, defendants may be permitted to retain ill gotten gains simply because their conduct harmed large numbers of people in small amounts instead of small numbers of people in large amounts."

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