



Ninth Circuit Finds Conflict of Interest in Incentive Provisions in Fee Agreements of Class Action Counsel

[Editor's Note: This column was co-authored by Francis G.X. Pileggi, Esquire and Sheldon K. Rennie, Esquire]

The U.S. Court of Appeals for the Ninth Circuit, in an opinion that has far reaching implications for class action counsel, found inherent conflicts of interests in a class action fee agreement that included incentive agreements that obligated class counsel to seek incentive awards for certain class representatives that would receive payments tied to the amount of the ultimate recovery. The opinion is published as *Rodriguez v. West Publishing Corp.*, No. 07-56643 (9th Cir. April 23, 2009). See generally, *Incentive Provisions in Retainer Contracts Created Conflicts in Class Action Litigation*, 25 Law. Man. Prof. Conduct 239 (May 13, 2009).

Notably, the Court of Appeals did not reverse the district court's finding that the class action settlement as a whole was fair and that the class was adequately represented, in part, because there were two other class representatives that had no incentive agreements and whose separate counsel was not conflicted.

The Settlement

The settlement arose out of an antitrust class action filed by several plaintiffs against West Publishing Corp., ("West") its subsidiary BAR/BRI, and Kaplan, Inc. ("Kaplan"). Plaintiffs asserted claims for antitrust violations pursuant to the Clayton Act and the Sherman Act. After the filing of the action, the parties engaged in lengthy settlement negotiations and eventually reached a settlement whereby West and Kaplan agreed to pay \$49 million into a settlement fund.

Uniquely Structured Incentive Agreements

Prior to the filing of the class action and as part of their retention and fee agreement with the prior counsel for the class, the five named plaintiffs had entered into an incentive arrangement whereby class counsel was obligated to seek an incentive payment for each of the five on a sliding scale that was tied to the amount of the settlement. For example, if the settlement amount was greater than or equal to \$500,000, class counsel would seek a \$10,000 award for each of them; a \$25,000 award if it was \$1.5 million or more; a \$50,000 award if it was \$5 million or more; and a \$75,000 award if it was \$10 million or more. This arrangement was not disclosed at the class certification hearing.

At the final hearing on the settlement's fairness, reasonableness and adequacy, the district court approved the settlement but denied the motion for incentive awards, on the basis that "the amount was unreasonable in light of the work and risk undertaken, and that the incentive agreements created actual conflicts of interest in violation of public policy." The district court also approved class counsel's request for attorney's fees in connection with the settlement. The objectors appealed the district court's approval of the settlement agreement primarily because of the presence of the incentive agreements, which they argued had prevented the class representatives from providing adequate representation to the class as a whole.

Conflict of Interest Created by Structure of Incentive Agreement

The Ninth Circuit upheld the district court's approval of the settlement agreement in spite of the incentive agreements because two of the class representatives and their counsel did not have a fee agreement to receive such incentives. The Ninth Circuit, however, ruled that the incentive agreements created a conflict of interest between the class representatives and the remainder of the class.

Although—according to the Court's opinion—additional payments to class representatives are fairly typical in class action cases to compensate class representatives for work done on behalf of the class, this incentive arrangement was different. *But cf. Oliver v. Boston University*, Delaware Chancery Court, No. 16570-VCN (May 29, 2009), slip op. at 2 (only in exceptional cases should an application for compensation to a representative plaintiff be granted).

Although the granting of a request for incentive awards to class representatives is discretionary, the instant incentive agreements "tied the promised request to the ultimate recovery and in so doing, put class counsel and the contracting class representatives into a conflict position from day one." The Ninth Circuit further reasoned that the structure of such an agreement gave the contracting representatives an interest in only a monetary settlement, as distinguished from other remedies, that set them apart from other members of the class. The court also had a problem with the failure by class counsel to disclose the agreements sooner, and also noted that agreements

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of this sort: "infect the class action environment with the troubling appearance of shopping plaintiffs"; "could tempt potential plaintiffs to sell their lawsuits to attorneys [that] are the highest bidders"; and "implicate California ethics rules that prohibit representation of clients with conflicting interests".

As a result, the Ninth Circuit, among other things, reversed and remanded to the district court the award of attorney's fees to class counsel for consideration of the impact, if any, of the incentive agreements on entitlement to fees. See generally, *Iron Workers Local No. 25 Pension Fund v. Credit-Based Asset Servicing and Securitization, LLC*, S.D. N.Y., 08 Civ. 10841 (JSR) (May 26, 2009) (criticizing conflict issues that arise when class counsel provides portfolio monitoring for the class representatives for whom they file cases.) Compare, *Plumbers, Pipefitters and Apprentices Local 112 Pension Fund v. CIT Group Inc.*, S.D. N.Y., 08 CV 6613 (BSJ), Order, (May 22, 2009) (not finding any conflict issues with class counsel providing portfolio monitoring for class representative for whom they later file class action suits.)

In those cases where the fee arrangement with class counsel is not an issue, the general rule in determining the appropriate award of attorneys' fees in class actions is that the court may consider factors such as: (i) the time and effort devoted to the case by plaintiffs' counsel; (ii) the relative complexities of the litigation; (iii) the skills necessary to pursue the litigation;

(iv) whether the fee is contingent; (v) the standing and ability of counsel; and, (vi) the benefit achieved. In addition, when a specific fund is created, tying the fee award to the amount of the recovery is a common practice. See, *In Re Cablevision/Rainbow Media Group Tracking Stock Litigation*, Delaware Chancery Court, No. 19819-VCN (May 22, 2009); *Sugarland Indus., Inc. v. Thomas*, 420 A.2d 142, 149 (Del. 1980).

Lesson to be Learned

This opinion makes it clear that while class counsel can allow for class representatives in a class action to be awarded extra compensation at the court's discretion, they cannot structure a deal where the promise to request the extra award for a class representative is tied to the ultimate monetary amount of the class recovery. Such a structure creates a wedge between the class representative's hope for a personal benefit not shared by the class from a monetary settlement, compared to the goal of what is best for the class as a whole—such as taking the risk of going to trial. This type of fee arrangement creates a conflict of interest and could jeopardize the amount of fees awarded to class counsel in connection with the settlement. The impropriety of such incentive agreements can be exacerbated, as here, by failing to disclose its presence at the class certification hearing. Thus, if there is any question about a fee agreement with class counsel passing muster, disclosure must be made at the earliest appropriate opportunity. ♦

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