Questions of Funding and Compensation on the 50th Anniversary of Modern Class Actions

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- Elizabeth Chamblee Burch, *Publicly Funded Objectors*, 19 **Theoretical Inquiries in Law** 47 (2018).
- Brian T. Fitzpatrick, *Can and Should the New Third-Party Litigation Financing Come to Class Actions?*, 19 **Theoretical Inquiries in Law** 109 (2018).

The modern class action turned fifty last year in the United States, and this year celebrates a quarter-century in Ontario, the first English-speaking province in Canada to enact class action legislation. On these anniversaries, scholars on both sides of the border, and around the world, are taking stock of class actions. A common theme in many of these discussions is whether class actions are achieving their intended purpose. Specifically, do they result in adequate compensation for class members? Or is the temptation for self-interest among plaintiffs' counsel so great that the interests of class members are inevitably subservient?

Important analyses on these and other critical questions, from doctrinal, comparative, and normative perspectives, are brought together in a special volume of *Theoretical Inquiries in Law* published in early 2018, entitled Fifty Years of Class Actions – A Global Perspective. Contributions by Elizabeth Chamblee Burch and Brian T. Fitzpatrick tackle the thorny question of compensation from the same starting point—that the entrepreneurial and representative nature of class actions creates risks for under-compensation of class members. They explore different aspects of the problem. Burch focuses on strengthening the role of objecting class members at the settlement approval hearing. Fitzpatrick focuses on using private claims investment to reduce the risk that plaintiffs' lawyers will settle for too little. Each contributes to an important discussion about the importance of fairly compensating the class.

Professor Burch begins from the premise that principal-agent problems persist in class proceedings, despite the statutorily prescribed function of the judge to protect the interests of the class. Many provisions in class action rules and statutes in the U.S. and other jurisdictions recognize the need to guard against attorney self-interest with court oversight: judicial approval of settlements; opt-out rights; the ability to object to a proposed settlement; and appeals. While the Subcommittee for Federal Rule of Civil Procedure 23 has recommended a number of proxies by which judges can better determine adequacy of settlement, all fall short because of an information deficit and adversarial void that hamper judges' ability to maintain robust oversight. Burch focuses on the objection process as the most promising space in which to close the information gap. Identifying the rise of professional objectors (lawyers who routinely challenge settlements, at times simply to extract a nuisance payment from class counsel) as a phenomenon unique to American jurisdictions, she considers "how to encourage noble objectors that benefit class members while staving off those that namely seek rents of class counsel."

She proposes a 'leveling up' of objectors. Sophisticated (and usually represented) objecting class members "can bring to light new information about structural conflicts of interest within the class or between class members and class counsel, as well as information about unfair outcomes." Burch seeks to incentivize 'good' objectors from those who wish to extort money from class counsel. Even well-meaning objectors have no incentive to propose radical changes to a settlement, as fees are only paid if a settlement is approved. 'Leveling up' objections would require the public funding of non-profit groups to encourage the socially useful objector. Such funding might come from a self-funding mechanism. (Here, she draws inspiration from Ontario and Quebec; in both provinces, a non-profit organization provides funding for plaintiffs' disbursements, and in the case of Quebec, legal fees, as well as an indemnity against adverse costs, for successful applicants. In exchange, a percentage of the class' recovery is levied). If the political will to create a public funding entity is lacking, she suggests an ad hoc approach: judges can direct cy près awards to non-

profit objectors. Whatever the source of funding, Burch persuasively argues that properly motivated and publicly funded objectors offer our best hope to ensure judges have the necessary information to monitor attorneys and the settlements they seek to have approved.

Fitzpatrick addresses the problem of suboptimal settlements by focusing on the economics of litigation for class counsel. Because plaintiffs' attorneys currently bear all the risk for their clients and may be more risk-averse than the defendants, they may decide to settle too early for too little. Fitzpatrick turns to third-party litigation financing as a method to achieve risk-balancing gains: non-lawyer investors purchase some or all of the value of the class' stake in the litigation in exchange for a percentage of any eventual recoveries. The risk of non-recovery is spread, if not wholly transferred, from class counsel to the funder. The economic theory is that a plaintiff will be less inclined to settle for less than the expected value of the claim, as it has already secured partial payment of the claim from the funder.

Thus far, financiers in the U.S. have avoided funding class actions for, among other reasons, the impossibility of contracting directly with each class member. Indeed, third-party class-action funding has effectively transformed Australia's opt-out regime into an opt-in regime. The alternative exists in Canada, where judges can approve the payment of a portion of any judgment to the funder, just as they currently enforce a first charge on any recovery for the lawyers' fee.

Fitzpatrick recognizes four main concerns about whether investing in class actions is socially desirable—fear of more litigation, longer cases, compounding agency costs, and skewing case selection either to only low risk actions or to high risk ones. He is able to succinctly address each concern in turn. An increase in meritorious claims is normatively unproblematic. Longer cases may in fact drive up compensation levels for class members. Agency costs can be addressed by contract (as they have been in Ontario). And, as an empirical matter, financing is unlikely to decrease the number of high probability, low risk cases, even if a marginal number of low probability cases are added. In the end, he concludes that the benefits outweigh perceived costs. In doing so, he contributes to the start of an important conversation both within and outside of the United States on diversifying the financing of entrepreneurial litigation.

The occasion of a milestone anniversary can be an impetus for thoughtful reflection, as well as inspiration for improvement. Burch's and Fitzpatrick's articles, as with all of the articles in this volume, make an important contribution to the study of class actions and their possible reform. Both scholars acknowledge the weaknesses of litigation that relies so extensively on economic incentives and risk (in)tolerance. While they aim to address those weaknesses by radically different means, they share a common goal: to secure meaningful justice for absent class members in whose name class actions are brought.

Jasminka Kalajdzic, Questions of Funding and Compensation on the 50th Anniversary of Modern Class Actions, JOTWELL (June 1 2018) (reviewing Elizabeth Chamblee Burch, *Publicly Funded Objectors,* **19 Theoretical Inquiries in Law 47** (2018); Brian T. Fitzpatrick, *Can and Should the New Third-Party Litigation Financing Come to Class Actions?*, **19 Theoretical Inquiries in Law 109** (2018)), https://courtslaw.jotwell.com/questions-of-fun…rn-class-actions/
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