

# The Use of *Cy Pres* Petitions to Obtain Grants of Residual Funds From Class Action Settlements

By Martin Minkowitz, Lesley Rosenthal and Michael A. Wiseman



## Introduction

One of the mechanisms that the New York Bar Foundation and other charitable organizations have used to fund charitable activities is the petition of courts and counsel for *cy pres* awards for potential residual funds from class action settlements. This article describes the *cy pres* mechanisms generally and some of the successes the New York Bar Foundation has achieved.

A fertile source of funding for nonprofits exists where unclaimed, or “residual,” funds are left over from class action settlements. The doctrine of *cy pres*, from the Norman French phrase *cy pres comme possible* (“as near as possible”), may be invoked when courts wish to allocate unclaimed funds that are left over from a settlement at the end date of the distribution process.<sup>1</sup> That date

arrives when either all known plaintiffs have been made whole<sup>2</sup> or when distributions have ceased according to an end date specified by either the settlement<sup>3</sup> or the court (“claim deadline”).<sup>4</sup> *Cy pres* may also factor in settlement agreements where parties seek to prophylactically plan for the disposition of unclaimed monies through what are known as “*cy pres*” distribution provisions.<sup>5</sup>

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## Class Action Settlements

Outside its application to charitable trusts, the *cy pres* doctrine is most frequently applied in the class action setting,<sup>6</sup> where cases involve named representatives acting on behalf of numerous absent class members.<sup>7</sup> Class action complaints may implicate putative classes of thousands or even millions of potential claimants who are subsumed under the class definition.<sup>8</sup> In this context, funds may go unclaimed because some class members remain unidentified and therefore unaware of pending settlements or because eligible class members who are otherwise entitled to funds fail to submit claims as required<sup>9</sup> or because the individual recovery amounts do not exceed procedural costs.<sup>10</sup> These residual funds are ripe sources of potential monies for nonprofits savvy enough to petition the court to invoke the *cy pres* doctrine. The court may approve such a distribution if the end destination befits the original interests and composition of the class.<sup>11</sup>

## Eleemosynary Organizations

Charities and the foundations that support them may petition courts and counsel under the *cy pres* doctrine to receive distributions of residual funds.<sup>12</sup> Organizations that choose to do so must keep in mind the foundational basis for the doctrine that the residual funds must serve goals closely related to the underlying claims that presaged the settlement in question.<sup>13</sup>

## Legal and Practical Considerations in Making Requests

### Legal Considerations

In a class action settlement arising in federal court, the district court judge plays an active role as a steward of the class's interests and as a counterweight to the sometimes conflicting pecuniary interests of counsel.<sup>14</sup> Federal Rule of Civil Procedure 23(e)(1)(A) mandates the court to conduct a fairness hearing in order to protect the interests of the class.<sup>15</sup> The goal of the court is to determine whether the settlement is fair, reasonable and adequate by examining whether the interests of the class are better served by settlement than by further litigation.<sup>16</sup> In doing so, the court considers whether the claims process is likely to be fair and equitable in its operation.<sup>17</sup>

The court reviews the settlement as a whole, including *cy pres* provisions, and has within its equitable authority the ability to deny a *cy pres* assignment if it finds that the charity in question does not suit the goals of the underlying litigation; but the court may not rewrite the settlement agreement.<sup>18</sup> Alternatively, parties may provide in the settlement agreement that the court may, at its discretion, choose a charity to benefit from any residual funds; however, this can be disfavored.<sup>19</sup> If nothing is provided in the settlement, the court will face the whole cloth dilemma of how to dispense residual funds.

The district court has great discretion in deciding how to award these residual funds,<sup>20</sup> and, generally, the unclaimed funds may be distributed by the court in one of three ways: (1) reversion to the defendant; (2) disbursement to other class members who have filed claims; or (3) *cy pres* distributions.<sup>21</sup> Courts diverge in their treatment of the *cy pres* doctrine. Some judges express skepticism,<sup>22</sup> preferring monies to be returned to the defendant,<sup>23</sup> but others hold that a *cy pres* distribution is an appropriate way "for a court to put any unclaimed settlement funds to their 'next best compensation use, e.g., for the aggregate, indirect, prospective benefit of the class.'"<sup>24</sup> Cognizance of these regional variations is an important aspect in developing a persuasive petition.

*Cy pres* distributions must be tied to the underlying litigation – "the nature of the plaintiffs' lawsuit, the objectives of the underlying statutes, and the interests of the silent class members, including their geographic diversity."<sup>25</sup> In seeking to apply this standard, the First Circuit, for example, has adopted the "reasonable approximation" test, based on the American Law Institute Principles of Aggregate Litigation enunciated in § 3.07(c): "[W]hen feasible, the recipients should be those 'whose interests reasonably approximate those being pursued by the class.'"<sup>26</sup> This recurrent test is perhaps the most important component of a successful petition for residual funds. Nonprofits and charities should be aware and considerate of this governing standard. For example, the court in *In re Lupron* cited numerous sister circuits that have applied the reasonable approximation test in rejecting *cy pres* awards to charitable organizations, and it stated that "[a]s these cases make clear, the mere fact that a recipient is a charitable or public interest organization does not itself justify its receipt of a *cy pres* award."<sup>27</sup> The primary focus of a petition for residual funds should be to explain to the court how the funds will be used and the nature of the organizations to whom they may be awarded, including specific charities, if known.

*Cy pres* awards must conform to the geographic nature of the underlying class and nature of the litigation. Courts have also considered the geographic makeup of the *cy pres* recipients and compared them to the geographic composition of the class. In *In re Airline Antitrust Ticket Commission*, the Eighth Circuit held that a *cy pres* distribution in a national class action suit against airlines to mostly local recipients was an abuse of the district court's discretion.<sup>28</sup> In the Tenth Circuit, the District Court of New Mexico stated that

because many corporations, especially national corporations, are incorporated in Delaware or other eastern states, or large states, it may be that class litigation is concentrated in areas like the Southern District of New York [or] in certain Californian districts; thus, concentrated, urban areas may benefit more from class litigation than more rural, sparsely populated areas,

like New Mexico, which have few particularly large corporations and few national class actions.<sup>29</sup>

A successful petition will convince the court that the *cy pres* recipient will provide indirect benefit to the class by being similar in nature or in geographic composition.

### Practical Considerations

In order to bolster the credibility of the organization, re-granting entities, such as the New York Bar Foundation, may articulate to the court whether there are legal or administrative fees associated with the distribution of grant money. There are some techniques for a successful petition to be considered.

Obtaining *cy pres* awards requires vigorous efforts to earn the trust of judges, uncover settlement funds that should be paid out to charities, locate suitable recipients, and provide accountability.

Although every litigation is affected by its own set of facts and circumstances, the following are strategic guidelines that petitioners for *cy pres* awards may wish to consider:

1. Identify the goals, strengths, and capabilities of your foundation, and the charities to which the foundation may be donating.
2. Identify cases that fit the paradigm (both old and new cases).
3. Research the particular circuit court, district court, and how the judges have ruled in previous cases involving the *cy pres* doctrine.
4. Articulate why the petitioner-foundation is particularly well-suited to identify suitable charities and to distribute funds.
5. Contact plaintiff's counsel and express desire to be involved with the possibility of helping to distribute residual funds.
6. Petition the court.

Include a detailed description of the proposed charities, their mission and use of the grant monies in relation to the underlying goals of the litigation. Alternatively, explain how the use of the grant monies will provide an indirect benefit to the class.

The New York Bar Foundation, for example, as a leading provider of *cy pres* assistance to courts and counsel, uses speeches, meetings and brochures to cultivate contacts in cases where *cy pres* monies might result. The New York Bar Foundation has a small administrative staff and a zealous board, who understand the legal system and unmet needs. This energy and knowledge is coupled with financial oversight of the board's finance and investment committees, making the Foundation a go-to organization for judges and class action counsel for *cy pres* awards.

The Foundation reports that *cy pres* matters have included:

- *White v. First American Registry*<sup>30</sup>: Federal District Judge Lewis A. Kaplan awarded \$1.2 million *cy pres* funds to the Foundation to re-grant to organizations addressing improper tenant screening practices. Board members with background in legal services and housing issues made site visits to the five grantees, interviewed program managers, and required true-ups of budgets against actual spending. Programs improved access to fair housing and helped families avoid homelessness.
- *Pinnacle*<sup>31</sup>: \$2 million+ of settlement funds were ordered by the Honorable Colleen McMahon to be

administered by the Foundation, to oversee promised improvements in housing conditions for low-income New Yorkers.

- *City of Detroit v. Grinnell*<sup>32</sup>: Chief Judge Preska, in Manhattan, entrusted The New York Bar Foundation to re-grant \$850K to an entrepreneurship program for disabled veterans at Syracuse University and an antitrust technology policy center at University of Pennsylvania Law School. These funds, from a long-forgotten antitrust settlement, helped improve disabled veterans' prospects and business ethics nationwide. Board members with technology law knowledge made site visits and provided accountability over the three-year grant period.

Obtaining *cy pres* awards requires vigorous efforts to earn the trust of judges, uncover settlement funds that should be paid out to charities, locate suitable recipients, and provide accountability. These awards are increasing access to justice to our society as a whole, in this unique and high-impact way. ■

1. *In re Lupron*, 677 F.3d 21, 30 (1st Cir. 2012); Lesley Rosenthal, Good Counsel: Meeting the Legal Needs of Nonprofits 116 (2012) (Rosenthal).

2. *Id.*

3. *See, e.g., In re Crazy Eddie Sec. Litig.*, 906 F. Supp. 840, 843 (E.D.N.Y. 1995) (reviewing a settlement which "required that all proofs of claims must be filed by a date specified in a notice of the proposed settlement of class actions").

4. *See, e.g., In re Cendant Corp. Prides Litig.*, 189 F.R.D. 321, 323 (D.N.J. 1999) (stating that the court has general equitable power to define the scope of class action judgments and settlements); *Grace v. City of Detroit*, 145 F.R.D. 413, 415 (E.D. Mich. 1992) (holding that Fed. R. Civ. P. 23(d) provides authority for issuance of a class notice which bars claims not filed before a particular date).

5. *See In re Lupron*, 677 F.3d at 26.

6. *Cy Pres Settlements*, The American Law Institute Principles of the Law of Aggregate Litigation § 3.07 cmt. a (2010) (Aggregate Litigation).

7. William B. Rubenstein & Alba Conte, *Newberg on Class Actions* § 1.1 (5th ed. 2013).
8. Thomas M. Hefferson & Douglas A. Thompson, *Class Action Update: The Increasing Scrutiny of Class Settlements and Other Developments*, 60 *Bus. Law.* 797, 805 (2005).
9. Aggregate Litigation, § 3.07(b), *supra* note 6.
10. Kevin M. Forde, *What Can a Court Do With Leftover Class Action Funds? Almost Anything!*, 35 *No. 3 Judges' J.* 19 (1996).
11. See Aggregate Litigation, *supra* note 6, at § 3.07 cmt. b (“In such circumstances, there should be a presumed obligation to award any remaining funds to an entity that resembles, in either composition or purpose, the class members or their interests.”).
12. See Rosenthal, *supra* note 1, at 116.
13. See Aggregate Litigation, *supra* note 6, at § 3.07(c) (“The court, when feasible, should require the parties to identify a recipient whose interests reasonably approximate those being pursued by the class.”); see also *id.* at § 3.07 cmt. a (commenting that the doctrine arose from the trust context, where “if the testator’s precise terms could not be carried out the court could modify the trust in a manner that would best carry out the testator’s intent”).
14. See David F. Herr, *Annotated Manual for Complex Litigation* 503 (4th ed. 2013) (“[J]udges should be wary of granting class members illusory nonmonetary benefits, such as discount coupons for more of defendants’ product, while granting substantial monetary attorney fee awards.”).
15. *Id.* at 502; see *Fed. R. Civ. P.* 23(e)(1)(A).
16. Herr, *supra* note 14, at 503; see *Fed. R. Civ. P.* 23(e).
17. Herr, *supra* note 14, at 502.
18. *Id.* at 502 (citing *Hanlon v. Chrysler Corp.*, 150 F.3d 1011, 1026 (9th Cir. 1998) (“The settlement must stand or fall in its entirety.”)).
19. See *In re Lupron*, 677 F.3d at 24, 26 (“[W]e express our unease with federal judges being put in the role of distributing cy pres funds at their discretion.”).
20. *In re Thornburg Mortg., Inc. Sec. Litig.*, 885 F. Supp. 2d 1097, 1108–09 (D.N.M. 2012).
21. See Herr, *supra* note 14, at 523.
22. See *Mirfasihi v. Fleet Mortg. Corp.*, 356 F.3d 781, 784 (7th Cir. 2004) (Posner, J.) (stating in dicta that where it is infeasible to distribute proceeds of a class action settlement and therefore the cy pres remedy is applied to “prevent the defendant from walking away from the litigation scot-free . . . [t]here is no indirect benefit to the class from the defendant’s giving money to someone else. In such a case the ‘cy pres’ remedy . . . is purely punitive.”).
23. *Klier v. Elf Atochem N. Am., Inc.*, 658 F.3d 468, 482 (5th Cir. 2011) (Jones, J., concurring) (stating that the court must return residual funds to the defendant).
24. *Id.* at 474 (quoting *Masters v. Wilhelmina Model Agency, Inc.*, 473 F.3d 423, 436 (2d Cir. 2007)).
25. *Nachshin v. AOL, LLC*, 663 F.3d 1034, 1036 (9th Cir. 2011).
26. *In re Lupron*, 677 F.3d at 33 (quoting Aggregate Litigation, *supra* note 6, at § 3.07(c)).
27. *Id.* at 34:  

*See, e.g.,* *Nachshin v. AOL, LLC*, 663 F.3d 1034, 1040 (9th Cir. 2011) (rejecting, in a nationwide privacy class action, a cy pres distribution to local Los Angeles charities because it did not “account for the broad geographic distribution of the class,” did not “have anything to do with the objectives of the underlying statutes,” and would not clearly “benefit the plaintiff class”); *Six Mexican Workers v. Ariz. Citrus Growers*, 904 F.2d 1301, 1311–12 (9th Cir. 1990) (invalidating a cy pres distribution to the Inter-American Fund for “indirect distribution in Mexico,” *id.* at 1304, in a class action brought by undocumented Mexican workers regarding violations of the Farm Labor Contractor Registration Act, because the distribution was “inadequate to serve the goals of the statute and protect the interests of the silent class members,” *id.* at 1312); *Houck v. Folding Carton Admin. Comm.*, 881 F.2d 494, 502 (7th Cir. 1989) (invalidating settlement agreement, in a national antitrust class action, that made a cy pres distribution to local law schools, and directing the district court to “consider to some degree a broader nationwide use of its cy pres discretion”); *In re Folding Carton Antitrust Litig.*, 744 F.2d 1252, 1253–54 (7th Cir. 1984) (invalidating, in a national antitrust class action, a cy pres distribution that would establish a private antitrust research foundation on the basis that “[t]here has already been voluminous research” on the subject).
28. 268 F.3d 619 (8th Cir. 2001) (explaining that a cy pres distribution should be closely related to the geographic origin of the underlying claim and distributed to those similarly situated to the class).
29. *In re Thornburg*, 885 F. Supp. 2d at 1109.
30. No. 04 Civ. 1611 (LAK), United States District Court, S.D. New York.
31. *Charrons, et al. v. Pinnacle Grp.*, No. 07 Civ. 6316 (CM), U.S. District Court, S.D. New York.
32. Nos. 68 Civ. 4026, 4028 and 4027 (LAP), U.S. District Court, S.D. New York.

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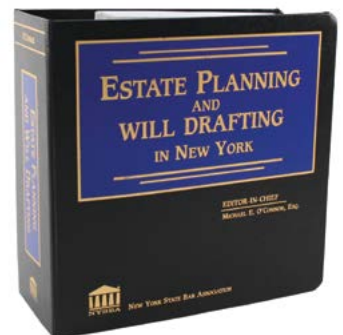
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