



Increased Scrutiny Means Increased Costs: Amended Rule 23 and Class Settlement Approval

IN SHORT

The Situation: Recently amended Federal Rule of Civil Procedure 23(e)(2) requires courts to analyze several factors in evaluating whether to approve class settlements.

The Result: Class action settlements that would previously glide through the approval process are facing heightened court scrutiny, including at the preliminary approval phase, with increased costs and risks to defendants.

Looking Ahead: In structuring class settlements, defendants must weigh the benefits of favorable settlement terms against the risks and costs associated with increased judicial intervention. Parties must invest early in the litigation, including potentially frontloading discovery and involving a mediator, to lay the groundwork for justifying favorable settlement terms to increasingly skeptical courts.

Rule 23(e)(2)'s recent amendment reflects a wave of increased scrutiny of and focus on perceived inequity in class settlements. As has long been the case, "a class proposed to be certified for purposes of settlement—may be settled ... only with the court's approval." Fed. R. Civ. P. 23(e). While increased judicial scrutiny will not foreclose class settlement approval, federal courts' heightened attention to the required showing by parties to obtain preliminary and final approval will place an increased burden and cost on parties seeking approval. Parties must develop sufficient factual support and carefully craft well-grounded settlement terms to increase the likelihood of preliminary and final settlement approval, decrease the risk of appellate reversal, and avoid unanticipated costs and future headaches.

The Approval Factors

Rule 23(e)(2), as amended and effective December 1, 2018, reinforces that a court may approve a class settlement only when its terms are "fair, reasonable, and adequate." That determination must follow a hearing and the court's consideration of the following list of factors:

- Whether class representatives and class counsel adequately represent the class;
- Whether the settlement was fairly negotiated and at arm's length;
- Whether the relief provided the class is adequate, considering the effectiveness of the proposed distribution of the relief to the class, the terms of proposed attorneys' fees, and any agreements of counsel; and
- Whether the proposal treats class members equitably relative to each other.

The Advisory Committee acknowledges that courts have established and applied similar factors that reflect these considerations. The 2018 amendment does not displace any factor but instead focuses the court's analysis on due process and fairness concerns for the unnamed class members. The amended rule aims at streamlining a court's consideration of settlement proposals, particularly at the preliminary approval phase, unifying the federal courts' approach to approval, and increasing predictability for the parties. The changes also aim to reduce forum shopping and inconsistency in settlement approvals across jurisdictions, as all federal courts must now consider the same factors in approving class settlements. Most consequential for

parties considering class settlements, the rule contemplates increased judicial involvement in and scrutiny of class settlements, including scrutiny of the manner in which relief is distributed to class members and whether the parties have made sufficient efforts to identify class members.



Although these changes are unlikely to result in outright rejection of many more proposed class settlements than under the former approach, the amended rule's practical effect is that parties cannot gloss over the equities of the settlement's terms until the final approval hearing.



Heightened Judicial Scrutiny and Increased Litigant Costs

Although these changes are unlikely to result in outright rejection of many more proposed class settlements than under the former approach, the amended rule's practical effect is that parties cannot gloss over the equities of the settlement's terms until the final approval hearing. Rather, the rule forces the parties to consider the equities early in the litigation and during the settlement negotiation stage to ensure they can justify the proposed class settlement when they present it to the court for preliminary approval. Parties must make a robust showing to warrant the court's preliminary settlement approval. The Advisory Committee tells courts to consider the nature and amount of discovery conducted to determine whether class counsel had sufficient information as a basis for settlement. Courts may also consider the involvement of a mediator or settlement facilitator in determining whether the settlement terms resulted from real arm's-length negotiations rather than solely through direct negotiations by the parties' counsel (where collusion could potentially occur).

Under the amended rule, it is critical that, before seeking preliminary approval of class settlements, parties invest adequate resources and time early in the case to achieve a settlement that balances the core factors in Rule 23(e)(2). The higher required showing will likely result in more aggressive class discovery and increased costs—primarily for defendants who are often in possession of the lion's share of information and thus must gather and produce it in discovery, or who may ultimately bear the cost of formal mediation. The parties also will likely incur higher legal costs in navigating the settlement approval process, including higher costs in preparing preliminary and final approval papers.

Disincentivizing Objectors

The amended rule also provides benefits for parties to class settlement agreements. Specifically, while objectors' rights under Rule 23(e)(5) remain, Rule 23's amendments should give plaintiffs and defendants alike some ammunition and comfort on this front. Rule 23 discourages bad-faith objectors (also known as "professional objectors") by requiring these intervenors to "state with specificity" the grounds for any objection and to identify on whose behalf the objection is brought. The rule also provides that "no payment or other consideration may be provided" for withdrawing an objection without court approval. These requirements are intended to curb objections "advanced for improper purposes" such as "seeking only personal gain."

FOUR KEY TAKEAWAYS

1. Defendants must balance costs and benefits of settlement before launching into lengthy discussions and proposals to certify a class for settlement purposes.
2. Defendants must think early on in the litigation about what discovery may be needed not only to oppose class certification but also to lay the groundwork for a potential settlement approval.
3. Parties should consider formalized settlement or mediation settings to better demonstrate the settlement is the product of real arm's-length



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4. While parties will likely face closer judicial scrutiny in obtaining class settlement approval, Rule 23's amendments disincentivizes bad-faith objectors and should give litigants some relief in dealing with meritless third-party objections.

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