EXAMINER.com

OPINION

Daniel J. Popeo: Fixing the class-action lawsuit racket

Daniel J. Popeo, The Examiner
Oct 11, 2006 5:00 AM (3 hrs ago)

WASHINGTON - Earlier this year, the king of class action law firms, New York's Milberg Weiss Bershad & Schulman, and two of its name partners were indicted in federal court for conspiring to obstruct justice, racketeering and paying millions in secret kickbacks to their clients for serving as lead plaintiffs in more than 150 class-action and shareholder lawsuits.

According to the indictment, the firm received more than $200 million in attorneys' fees, and paid more than $11 million to just three clients. The firm denies the charges, claiming the kickbacks were simply "referral fees" paid to other lawyers. Business as usual?

And what about the millions of class members for whose benefit these kinds of suits are routinely filed? They're lucky to get worthless coupons or a few pennies per share of stock they owned, assuming they even knew about the suit and were able to fill out confusing claim forms in time to receive their pittance.

Unfortunately, that is how the class-action game is played across the country. First, trial lawyers work to convince the public that most corporations and businesspeople are trying to rip off the consumer or shareholder. Then they enlist activist groups and friendly state attorneys general to charge companies with fraud and wrongdoing, even though there's no evidence or the "injury" is far-fetched or minuscule. If there is a lack of evidence, simply manufacture it, as apparently was done when thousands of bogus silicosis lawsuits were filed in Texas, a scheme which is the subject of yet another federal criminal investigation.

Next, get a lead plaintiff to serve as the front man for the suit. Finally, shake down the targeted company for a settlement that ensures that multimillion-dollar attorneys' fees are paid, but that class members get little or nothing. And don't forget to pay those "referral fees" to ensure a steady supply of friendly "clients" for future cases.

A few years ago, The Washington Post editorialized about this sad state of affairs, stating that class members "get token payments, while the lawyers get enormous fees. This is not justice. It is an extortion racket that only Congress can fix." But did they? Early last year, with much fanfare, Congress allegedly "fixed" the problem by passing the Class Action Fairness Act after almost a decade fighting the influential lobbying efforts of the trial bar and their allies in Congress.

Under CAFA, class action lawsuits filed in friendly state courts after 2005 can be transferred to more neutral federal courts if they meet certain conditions. Not surprisingly, trial lawyers, being a creative lot, have found ways to get around these provisions to keep many of their cases in friendly state forums.

Congress also attempted in CAFA to deal with the notorious coupon phenomenon where class action attorneys often settle with the company for coupons of nominal value but which purportedly have an aggregate face value in the millions. The lawyers then seek court approval of their multimillion-dollar fees claiming that they amount to a "reasonable" 25 percent or 30 percent of the aggregate class award. The truth is that class actions generally require class members to fill out a claim form by a certain arbitrary cut-off date to obtain any compensation.

Thus, the more relevant coupon “claim rate” is extremely low because notice to the class is inadequate, the time to respond once notified is very short, the requirements for filing a claim are complicated or require receipts, or the “benefit” is simply not worth the hassle. In one recent case, the claim rate was a measly one percent of the settlement.

A provision inserted in CAFA appeared to address these shenanigans by basing the attorneys’ contingency fees on the value of coupons actually redeemed. Sounds good, but Congress gave the plaintiffs’ lawyers a big fat loophole by allowing courts to pay huge attorneys’ fees anyway based instead on the attorneys’ inflated hourly rate, and one that can be even further multiplied two or threefold! Some reform.

What drives these abusive lawsuits are the obscene attorneys’ fees, which can amount to an effective hourly rate of $10,000 or more. Requiring plaintiffs’ attorneys to pay the fees of their targets if they lose is one way to deter frivolous cases. More importantly, both federal and state judges must stop rubber stamping large fee award requests, and start taking their fiduciary duties to absent class members more seriously. And if the current criminal cases result in convictions, that might be the best medicine of all.

Daniel Popeo is chairman and general counsel of the Washington Legal Foundation, a public interest law and policy center that regularly files objections to the award of excessive attorneys’ fees in class action cases.
Examiner