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Making Class Action Coupon Settlements Deliver Real Value to Class Members

By Hon. Thomas A. Dickerson

Once started, how are consumer class actions resolved? Typically, but not always, after a class action is certified, the parties will begin serious negotiations to reach a settlement. Any proposed settlement must be examined and conditionally approved by the court before the class is notified and given an opportunity to raise objections. Ultimately, the court conducts a hearing and may or may not approve the settlement, in whole or in part. In addition, the court may pass on class counsel's fees and costs application. In this article, we will discuss the viability of class action settlements featuring non-cash compensation, such as vouchers or coupons, which provide a discount towards the purchase of defendant's goods or services. In addition, we shall examine the recent decision of the 7th Circuit, in *In re Southwest Airlines Voucher Litigation*, approving a "coupon settlement" consisting of "replacement drink vouchers."¹

Non-Cash Coupon Settlements

Although subject to criticism, there are occasions when a non-cash settlement of coupons for the purchase of goods or services from the defendant may be appropriate. The reasons for allowing coupon settlements include (1) recovery of de minimis damages (which makes the cost of distribution of each individual's cash award higher than that individual's claims), (2) the inability to identify class members, (3) the defendant's inability to pay cash to the class, or (4) because it makes good business sense from the standpoint of both the consumer and defendant. Since coupon settlements are generally worth less to consumers than cash, they must be carefully examined for adequacy. Yet coupon settlements are justified because they solve manageability problems, may reflect the defendant's financial instability, and require a defendant to disgorge improperly obtained monies. The primary concern for the court is to ensure a proposed coupon settlement is nearly as good as a cash settlement.

Transferability and Cash Convertibility

Coupons, typically, require the purchase of specific goods and services, which the class member may not want. The coupons should be convertible into cash either by redemption or by being transferable to persons or entities, such as coupon brokers, who are willing to pay cash for them. Cash convertibility, even at a discount, would be acceptable. Coupon settlements that limit transferability to family members and provide no cash convertibility, no cash sales, and no redemption through travel agents² may be problematic at best.

Redemption Rates and Tracking

In evaluating the merits of a coupon settlement, an appropriate means of measuring true value is to estimate the actual redemption rate of the offered coupon. Coupon settlement is particularly attractive for defendants because the average redemption rates on food and beverage coupons have consistently been between 2 percent and 6 percent.³ A coupon settlement should require post-settlement tracking of the redemption rate of the coupons. Better yet, there should be a 100% redemption of the offered coupons or credits. The 100% redemption means that the coupons must be transferable, cash convertible, and the defendant must continue to issue coupons until the agreed-upon cash face value of the settlement is reached. For example, in *Feldman v. Quick Quality Restaurants, Inc.*, the settlement provided for the issuance of food coupons with a minimum value of \$0.50. The defendants were required to continue issuing and distributing to consumers until the agreed upon face value of the settlement was reached.⁴

Time Limits and Redemption Methods

Equally important in measuring the actual value of a coupon settlement is the time during which redemption must take place and the manner in which the coupons must be redeemed. As for duration of coupon redemption, the longer the time period, the better. Redemption periods of three years, two years, and one year have been found to be acceptable.⁵ As for the method of redemption, the consumer should not be required to reveal his or her intention to use the coupon or credit until the parties agree on the price. For example, if the retailer is aware that the consumer intends to use a coupon or credit, the retailer may increase the sale price to compensate for the reduced payment.

Problem of Attorney Fees

Coupon settlements also raise issues on evaluating class counsel's request for an award of legal fees and costs. Typically, when there is a monetary settlement, the Court may use either the percentage method or the lodestar method⁶ in determining the appropriate fee. However, in coupon settlements, a fee award may not be appropriate when it is based on a percentage of an estimated settlement value, which itself is based upon an estimated redemption rate. To avoid this problem, the court may wish to base a fee award on claims actually made or require class counsel to accept a portion of their fees in the same non-cash consideration in the settlement. For example, in *Aburine v. Northwest Airlines Inc.*, class counsel accepted

cash and \$200,000 in non-transferable credit for travel.⁷ The rationale for requiring class counsel to share with class members is that it ensures value for the non-cash component, on the theory that class counsel would not accept a fee that is relatively worthless. In the alternative, counsel fees should be based upon the actual recovery to the class. This alternative requires cash convertibility, transferability, extended redemption periods, post-settlement tracking, and continued coupon issuance, until the amount redeemed equals the promised cash value of the settlement.

The Southwest Vouchers Settlement

In *In re Southwest Airlines Voucher Litigation*, decided August 20, 2015, the court noted “[t]hese appeals present several issues concerning class action litigation and settlements. The most general is whether the ‘coupon settlement’ provisions of the Class Action Fairness Act... allowed the district court to award class counsel an attorney fee based on the lodestar method rather than the value of the redeemed coupons. Our answer to that question is yes.”⁸

The Drink Vouchers

“For several years passengers who bought ‘Business Select’ tickets on Southwest Airlines received vouchers good for a free in-flight alcoholic drink. The vouchers did not contain expiration dates. Some customers saved them for future use, and Southwest honored them, at least for a while. In August 2010, however, Southwest stopped honoring these older vouchers, announcing that each voucher was good only on the flight covered by the accompanying ticket.”⁹

The Lawsuit

Plaintiffs “Levitt and Malone filed suit against Southwest on behalf of a purported class of plaintiffs holding unredeemed Business Select drink vouchers that were suddenly worthless. The class alleged claims for breach of contract, unjust enrichment and violations of state consumer fraud laws. The district court quickly dismissed the unjust enrichment and statutory claims as preempted by the federal Airline De-Regulation Act. The breach of contract claim remained.”¹⁰

The Settlement

“The parties agreed to settle the breach of contract claim. The settlement provides for class certification and includes three types of relief. First, it requires Southwest to issue replacement coupons to each class member who files a claim form. The coupons are transferable and good for one year on any Southwest flight. Second, the settlement provides injunctive relief to prevent similar controversies over expiration dates if Southwest issues new coupons in the future. Third, the settlement provides

for incentive awards to the two lead plaintiffs of \$15,000 each.”¹¹

Class Member Objections

Two class members objected to the proposed settlement because “the fee settlement included ‘clear-sailing’ and ‘kicker’ clauses designed to shield the fee award from challenge.”¹² “In a typical ‘clear-sailing’ clause the defendant agrees not to oppose a fee award up to a certain amount. A ‘kicker’ clause provides that if a court reduces the attorney fee sought in a class action, the reduction benefits the defendant rather than the class.”¹³ In addition, objectors asserted that “the attorney fee in this ‘coupon settlement’ had to be based on the value of coupons actually redeemed by class members, under a provision of the Class Action Fairness Act.”¹⁴

Settlement Approved

“The district court approved the class settlement as fair and reasonable, focusing primarily on the fact that the settlement provided essentially complete relief to the class. The district court determined that [Section] 1712 applied to the settlement because the vouchers were ‘coupons’ within the meaning of that provision, though the usual concerns about coupon settlements are minimal here because the class’s claim itself is for the value of coupons that already required class members to buy plane tickets to use.”¹⁵ The court further determined that section 1712 “permits the use of the lodestar method to determine attorney fees based on coupon relief” and, therefore, approved an award of \$1,649,118.¹⁶

Fee Awards In Coupon Settlements

“When Congress enacted the Class Action Fairness Act, one of its targets was abusive ‘coupon settlements,’ where defendants and class counsel agree to provide coupons of dubious value to class members but to pay class counsel with cash.”¹⁷ “The potential for abuse is greatest when the coupons have value only if a class member is willing to do business again with the defendant who has injured her in some way, when the coupons have modest value compared to the new purchase for which they must be used, and when the coupons expire soon, are not transferable, and/or cannot be aggregated.”¹⁸

Attorneys Fees and Lodestar Method

“We hold first that [Section] 1712 applies to this settlement.”¹⁹ “The replacement vouchers for free drinks on Southwest flights are indeed ‘coupons’ and hence this settlement is subject to [Section] 1712.”²⁰ In the 7th Circuit’s holding, it recognized the more difficult issue to be “whether [Section] 1712 allowed the district court to use the lodestar method to calculate the fee award for class counsel.”²¹ Objectors argued that section 1712 prohibited use of the lodestar method, and, the only permissible

basis for a fee award here would be the value of the new coupons actually redeemed by class members. Under this view, use of the lodestar method in a coupon settlement is not permissible.²² This view was adopted in *In re H.P. Inkjet*.²³ However, in analyzing section 1712, the court noted the text, structure, legislative history, and the legislative purpose of the statute that “allows a district court discretion to use the lodestar method to calculate attorney fees even when those fees are intended to compensate class counsel for the coupon relief he or she obtained for the class.”²⁴

Fairness of the Settlement

“No party disputes the adequacy of the class relief. This is not a case where coupons of dubious value will be provided to compensate for a loss of cash. The class lost the value of drink coupons. The settlement provides replacement drink coupons, on a one-for-one basis. The claims process is easy, and the replacement coupons will remain valid for one year. There is also a happy alignment of interests between class members and Southwest. Southwest has no incentive to insist on a stringent claims process. Every replacement coupon can be used only by a customer who buys a plane ticket.”²⁵ The court recognized that “Southwest should benefit from every one that is actually used. The benefits for a defendant under a coupon settlement are usually a reason for caution if not skepticism. This case is different though, Southwest would have received the same benefits from the old coupons. Serendipitous or not, such essentially complete relief for the class is the model of an adequate settlement.”²⁶ The court further noted that “[t]he class members will receive everything they reasonably could have hoped for. While some replacement coupons might never be used, the same could be said of the original coupons.”²⁷

Endnotes

1. *In re Southwest Airlines Voucher Litig.*, 799 F.3d 701, 706 (7th Cir. 2015).
2. *See In re Domestic Air Transp. Antitrust Litig.*, 144 F.R.D. 421, 421 (N.D. Ga. 1992) (holding objectors to proposed settlement granted limited discovery).
3. *See Weinstein, The Love/Hate Dynamics: Coupons Issued by Manufacturers*, 71 *Progressive Grocer* 117 (May 1992).
4. *Feldman v. Quick Quality Restaurants, Inc.*, N.Y.L.J. July 22, 1983, p. 12, col. 4 (N.Y. Supp.).
5. *See In re Domestic Air Transp. Antitrust Litig.*, 144 F.R.D. at 425 (allowing discovery for redemption of two to three years); *see also In re North Atlantic Air Travel Antitrust Litig.*, Index No. 84-1013, at *4 (D.C. Cir. 1986) (recognizing five years for redemption).
6. Lodestar Method is the value of time spent in prosecuting the class action.
7. *See Aburine v. Northwest Airlines, Inc.*, No. 3-89-402, at *4 (D. Minn. Aug. 16, 1991).
8. *In re Southwest Airlines Voucher Litig.*, 799 F.3d 701, 701 (7th Cir. 2015).
9. *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 704.
10. *Id.* at 704-705.
11. *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 705.
12. *Id.*
13. *Id.*
14. *Id.*
15. *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 705.
16. *Id.* After an evidentiary hearing on counsel’s Rule 59(e) motion, the fee award was increased. *Id.*
17. *Id.* at 705-06.
18. *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 706 (citing *In re HP Inkjet Printer Litig.*, 716 F.3d 1173, 1177-79 (9th Cir. 2013) (discussing some of these common concerns about coupon settlements)).
19. *Id.*
20. *Id.*
21. *Id.*
22. *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 706 (noting exceptions for compensation to counsel for obtaining injunctive relief).
23. *See In re H.P. Laserjet Printer Litig.*, 716 F.3d at 1183-85.
24. *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 707.
25. *In re Southwest Airlines Voucher Litig.*, 799 F.3d at 711.
26. *Id.*
27. *Id.*

Hon. Thomas A. Dickerson is an Associate Justice of the Appellate Division, Second Department of the New York State Supreme Court. Justice Dickerson is also the author of TRAVEL LAW 1 (ALM Media Properties, LLC, 2015); see APPELLATE DIVISION SECOND JUDICIAL DEPARTMENT, http://www.courts.state.ny.us/courts/ad2/justice_dickerson.shtml (last visited Oct. 13, 2015); see also CLASS ACTIONS: THE LAW OF 50 STATES 1 (ALM Media Properties, LLC, 2015); WEINSTEIN ET AL., NEW YORK CIVIL PRACTICE: CPLR, Article 9 (David L. Ferstendig, 3rd ed. 2015), available at <http://www.lexisnexis.com/store/catalog/booktemplate/productdetail.jsp?prodId=10532#sthash.UpfknUjZ.dpuf>; see also COMMERCIAL LITIGATION IN NEW YORK STATE COURTS Chapter 111 (Robert L. Haig, 4th ed. 2015); co-author of LITIGATING INTERNATIONAL TORTS IN U.S. COURTS 1 (Thomson Reuters, 2015).