5 CLASS ACTION MYTHS DISPELLED

Class action lawsuits are complex issues, and structuring settlements can present a host of business complications for defendants. To help navigate these complexities, we examine and dispel five common myths about class action litigation and settlements.

Myth 1:

Wait until late in a class action lawsuit to consider a settlement

False! Early settlement consideration can lead to a more efficient end to litigation, and does not prevent the defendant from continuing to fight the litigation.

Myth 2:

The total cost of settlement will not exceed the funds paid to the Class, class counsel and the TPA

False! Factoring in overall business operations and, in some cases, tax issues, the actual cost of a class action settlement may be 35 percent more than originally expected.

Myth 3:

It's impossible to fix the risk of a class action settlement

False! While the traditional method of settling class action cases may include many uncertainties, there is a way that the financial risk of a settlement can be made certain for the defending business.

Myth 4:

Notifying consumers of the settlement is the easy part

False! Alerting the appropriate consumers of a settlement is a complicated process, and if not done correctly, it can lead a settlement to be overturned.

Myth 5:

Viral settlements are rare and predictable

False! Class action promotion sites, social media and news sites cause every settlement to run the risk of going viral and costing the settling company significant payments.

Read on for more on each class action myth and how to dispel them!

Myth 1:

Wait until late in a class action lawsuit to consider a settlement

When in class action litigation, companies default to the belief that they should circle the wagons, hunker down and dig in for a long, protracted battle. (Certainly, some cases warrant that strategy.) Additionally, some companies may want to wait until the lawsuit has progressed before considering settlement as an option to exit the case. But litigation is dynamic, risky, and expensive.

Some relevant statistics to consider:[1]

- Companies pay an aggregate $2 billion per year to defend class litigation
- 10% of class action litigation is considered "bet the company" cases
- 61% of companies are facing at least one major class action lawsuit
- 48% of companies in a class action settlement require a change in one or more business practices

The decision to fight or settle the lawsuit is not mutually exclusive. Instead, both strategies can, and should often be evaluated and pursued simultaneously.

These are the key questions to be asked:

1. What is the exposure if the class is certified and prevails on the merits?
2. Could class counsel expand the class definition and create additional risk or exposure?
3. Have other companies in the same industry or space been sued and the cases settled? If so, what were the terms?
4. Are the claims asserted fundamental to business operations or is this a case that can be resolved, allowing the company to operate in the same or similar manner?
5. What is the competence of class counsel and their ability to fund, fight and prevail on class certification?
6. What are the estimated costs for the following phases of litigation: Motion to Dismiss and Motion to Consolidate/ Transfer; Discovery; Class Certification; Interlocutory Appeal, if any; and Trial?
7. What is the impact of the litigation phases on management and business operations?
8. When will the company have to start reserving losses for anticipated litigation expenses and liability?

Given that it is expensive to defend litigation and the majority of the cases end up with a cash settlement, the question is whether an early settlement can be an efficient end to litigation. When considered at the beginning of litigation, class counsel has invested limited time and expense; they can avoid the uncertainty of litigation and certification; and they have an opportunity to monetize the case. By approaching settlement early, the company can test class counsels' conviction on the case and determine if there is an economically-feasible settlement to be achieved. With low Lodestar time incurred by class counsel early in the case, the total cost of settlement may be much less than anticipated.

In certain cases, Risk Settlements experts have designed early settlements which cost similar amounts to the overall defense of the case. But for those same total dollars, the company extinguished historical liability and could get back to business, rather than endure years of litigation expenses ending in an uncertain outcome. For companies contemplating future M&A or financing activities, removing uncertain and unliquidated liability can be either fundamental or accretive to the short- or long-term corporate goals.

Finally, if the case does not resolve early, then the company continues on its path to vigorously contest the litigation. It may prevail on its procedural or substantive defenses or revisit resolution when the case is more fully developed. That said, litigation and risk can break against a company as well. If the case is certified, then the cost of settlement increases along with the financial risk to the company.

It may be too early to settle, but it is never too early to consider whether it makes sense. Evaluate the options and facts. Determine if a discussion is worthwhile. But don't wait until it is too late, as the price of poker can increase significantly, depending upon the trajectory of the litigation.

Myth 2:

The total cost of settlement will not exceed the funds paid to the Class, class counsel and the TPA

Class action settlement costs don't end at the funds paid to the Class, class counsel and third party administrators—rather, there are implications for overall business operations and, in some cases, tax issues. In fact, the actual cost of settlement may be 35 percent more than you expected.

Statutory penalties, such as payouts resulting from Telephone Consumer Protection Act cases, may not be tax deductible, costing companies much more than anticipated. According to a peer-reviewed tax article entitled, "Class Action Settlements - Financial and Tax Reporting"[2];

> *"Settling parties need to be aware that not all class action settlements will result in tax deductible payments to class members… [I]f the settlement and payment represents a fine or statutory penalty, then the payments are likely not tax deductible. Further, to the extent the litigation arose from a capital transaction such as the acquisition of an asset or in a claim relating to ownership rights to a capital asset, Section 263(a) requires capitalization of class action settlement payouts and related costs. If capitalized, the deduction of settlement costs may be required to be spread over a number of years or the deduction may be disallowed entirely. This second scenario is problematic in that the settlement creates the degradation to the financial statements with no corresponding tax benefit."*

In the event that a settlement arising out of a statutory damage case is not tax deductible, then the cost will be substantially higher than anticipated.

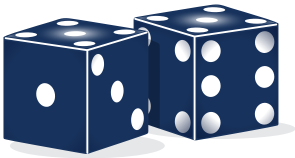
Further, per CPA Peter Robbins, the author of the "Class Action Settlements - Financial and Tax Reporting," companies entering a class action settlement must immediately accrue the entire settlement liability on its balance sheet. More specifically, according to CPA Robbins:

> *"A company that is entering into a claims made settlement of a class action lawsuit has only two paths it can take when booking the settlement and preparing its tax return. First, it can adhere to current ASC 450, Form 8-K and other disclosure requirements and take a GAAP charge for the full amount of the claims made settlement fund and review the facts and circumstances of the settlement to determine the proper tax filing position. This approach can cause shareholders (both present and prospective) to impugn the Company's financial stability, which directly influences its capital reserves and operations. In addition, the tax consequence either further harms the company or opens an avenue for IRS scrutiny."*

To mitigate the negative financial and tax treatment arising out of class action settlements, according to CPA Robbins,

> *"The company can insure the class action settlement which will effectively transfer the settlement liability from the company to the insurer. The purchase of an insurance policy for a specific class action case can help minimize the economic, tax and investor disapproval exposure and result in more of a benign financial disclosure as the net liability is represented by the paid and incurred insurance premium."*

By understanding these complex issues, companies can structure optimal settlements which meet their legal and financial objectives and mitigate the unintended consequences of resolution including: negative impact on their earnings and balance sheet; effect on actual or contemplated M&A transactions, financing activities or cash flow.



Myth 3:

It's impossible to fix the risk of a class action settlement

The traditional method of settling class action litigation can leave business leaders uncertain and uneasy with the financial and business risk they are taking on. But contrary to popular belief, the financial risk of a class action settlement can be made certain.

Consider involving a class action expert that specializes in settlement structures and risk transfer solutions. For example, Risk Settlements offers consulting services to assist with structuring an optimal settlement to meet the financial and legal objectives of the company. For each company, we perform an in-depth quantitative and qualitative analysis, including proprietary risk algorithms, allowing us to suggest settlement structures that best serve the company's individual financial needs. Whether it's uncertainty, unpredictability, tax or other concerns, we can assist in designing a settlement to address and solve those concerns.

Myth 4:

Notifying consumers of the settlement is the easy part

In fact, notifying consumers is one of the hardest things to get right in a class action settlement. It is a complicated process involving alerting the right class members while simultaneously reducing fraud. If not done right, it can cause the court to decline the settlement, forcing the defendant to start over, wasting time and money.

Work with a third-party administrator (TPA) that has a qualified media expert who has a long, successful track record of approved notice programs. Asking the right questions can save you a big headache. Avoid TPAs that attempt to "white-label" expertise. Ask if the media person is in-house, or if they use an outside advertising agency. Vet your experts and look for actual experience in the media industry. Ask if the expert has ever had their opinion discounted. If they have, this may be a red flag. Make sure the media plan is transparent and provides a quantifiable validation basis for all class member reach assumptions.

Does your TPA have a thorough media plan?

Watch for over simplification. For example, a notice plan using only USA Today and a few online impressions claiming to reach 70 percent of a class at very low cost, may sound too good to be true − because it is. Make sure your media expert discloses all online, mobile and social media that will be used. Have them fully describe the media target that is being measured; watch out for campaign frequency caps of 1x or 3x. This is not an accepted approach, as it artificially inflates reach and leads to inaccurate reporting for the courts, and in reality, is eroded by cookie deletion, bots and viewability issues. This affects due process, as class members don't have a reasonable opportunity to see the notice. Make sure your media expert uses and cites best-in-class media measurement and validation tools such as comScore, Nielsen and GfK Mediamark Research and Intelligence.

Protect your brand. Ask if your media expert employs measures for brand safety, monitors and adjusts for bots, ad fraud and viewability.

TPA Tips:

- Work with a third-party administrator (TPA) that has a qualified media expert who has a long, successful track record of approved notice programs.
- Asking the right questions can save you a big headache.
- Avoid TPAs that attempt to "white-label" expertise.
- Ask if the media person is in-house, or if they use an outside advertising agency.
- Vet your experts and look for actual experience in the media industry.
- Ask if the expert has ever had their opinion discounted. If they have, this may be a Red Flag.
- Make sure the media plan is transparent and provides a quantifiable validation basis for all class member reach assumptions.

Myth 5:

Viral settlements are rare and predictable

When class members receive notice of a settlement and the ability to file claims by publication, viral settlements present a clear and present danger to the financial health of the settling company.

Naked Juice Settlement Example:

In the Naked Juice Settlement, the Court approved a publication notice plan which informed the public of their ability to file a claim and receive cash. Shortly after the notice plan commenced, the media picked up on the settlement, posted several articles and ran numerous multimedia news stories. According to Gilardi & Co. LLC, the TPA in this case, "the majority of traffic came from a news article on the ABC News website and a news article displayed on the Yahoo.com homepage headline area. In the following days, the story was also picked up by Huffington Post and Foxnews.com."

Like Naked Juice, news sites picked up the settlements in: Red Bull, Five Finger Shoes, Star-Kist Tuna and Airborne. As a result of the unpaid media stories causing substantial interest in their settlements, all of these had significant claims activity and viral take rates.

So when 2.7 million people filed Red Bull claims, or more people sought a refund from the Five Finger Shoe settlement than actually bought the shoes, fraudulent claims exacerbate the viral claims rate. Fraud is dynamic, pervasive, difficult to detect and very costly. With the advent of claims promotion sites, people are notified about settlements and encouraged to file claims regardless as to whether they are actual class members. Enticed with the promise of free money, people are provided a hyperlink to a simple electronic claim form. After a few clicks, the process is complete and they just have to wait for the cash to arrive in their mailbox. With promotion sites, social media, Facebook sharing and news sites discussing settlements, every settlement runs the risk of going viral and costing the settling company significant payments to people who may not even be class members.

So how does a settling company address the problem of waste, fraud and abuse. The first step is to hire an experienced TPA which has the policies, procedures, protocols and technology in place to flag suspicious claims.

Depending upon the case, some areas to consider evaluating are:

- Do multiple claims have the same electronic finger print or the same IP address?
- Are claims being filed in micro-geographical clusters?
- Are claims being filed by many people using the same or similar names or the same address?
- Are claims being filed from prison?
- Where do the inbound links to the claim form arise?
- Are claims related by name, time, address (physical or electronic)?
- Are claimant multiple filers in other consumer settlements?

Paying illegitimate claims can reduce the benefit available to bona fide class members. In addition, fraud drives up administration costs which are typically borne by the settling company. A publication notice settlement creates substantial financial risk, which is only compounded when the publication settlement goes viral and the claim rate skyrockets.

Sources:

[1] The 2016 Carlton Fields Class Action Survey - http://classactionsurvey.com/pdf/2016-class-action-survey.pdf

[2] Class Action Settlements – Financial and Tax Reporting - http://risksettlements.com/assets/pdf/Class-Action-Settlements-Financial-and-Tax-Reporting.pdf

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SETTLEMENTS

ABOUT RISK SETTLEMENTS

Risk Settlements is a risk mitigation consultancy that reduces the uncertainty of class action lawsuits and settlements for businesses. Creators of Class Action Settlement Insurance (CASI)—the only post-settlement class action insurance product on the market—Risk Settlements helps companies analyze and mitigate the risk of class action litigation and settlements. With more than 70 years of combined legal, business, insurance and actuarial experience, Risk Settlements features a sophisticated team of nationally-recognized experts.

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