THEODORE H. FRANK (SBN 196332)
Competitive Enterprise Institute
Center for Class Action Fairness
1310 L Street NW, 7th Floor
Washington, DC 20005
Voice: (202) 331-2263
Email: ted.frank@cei.org
Attorney for Rachel Threatt

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

JOANNE FARRELL, on behalf of herself and all others similarly situated,

Plaintiff,

v.

BANK OF AMERICA, N.A.,

Defendant,

RACHEL THREATT,

Objector.

Case No. 3:16-cv-00492-L-WVG

RESPONSE OF OBJECTOR RACHEL THREATT TO THE COURT'S ORDER TO SHOW CAUSE

Judge: Hon. M. James Lorenz

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INTRODUCTION

On June 28, 2018, this Court entered an order to show cause ordering class counsel and defendant Bank of America ("BoA") to file a brief to address whether there are conflicting interests among subgroups of the class that require creation of subclasses with separate representation. Dkt. 125 at 8. The Court identified five issues as "[e]specially germane to this inquiry." *Id.* As a particular potential concern, the Court noted that a class member in the Debt Portion subgroup may recover her damages in full and thus receive more favorable treatment under the settlement than members of the Cash Portion subgroup, none of whom will recover 100% of their damages. *Id.* at 7.

The parties filed their joint response on July 30, 2018. Dkt. 128. Class member and objector Rachel Threatt submits this response to address an issue critical to the adequacy inquiry that the parties left open: the accounting value of the debt relief portion of the settlement relief. This issue is directly relevant to the first three issues identified by the Court: (i) whether a dollar spent towards Debt Portion relief is one less dollar BoA was willing to spend towards Cash Portion relief; (ii) explanation of any disparate treatment amongst subgroups; and (iii) whether each subgroup has representation amongst the named plaintiffs. Dkt. 125 at 8. Because the settling parties and objector Sanchez already have provided detailed responses to the issues identified by the Court, Threatt seeks to avoid duplication by addressing the narrow issue of the value of the debt relief provided by the settlement and its implication for the Court's analysis. *See id.*

The parties explained in their joint response that they first negotiated the cash relief and, only after class counsel believed they had "maximized the amount of cash [BoA] was willing to pay did [they] introduce debt forgiveness relief for Class Members with unpaid EOBCs into

the negotiation." Declaration of Hassan A. Zavareei, Dkt. 128-1 ¶ 7. This two-stage negotiation process leads to one of two possible conclusions. Either:

(1) class counsel negotiated inadequately and left significant value on the table in the first "cash negotiation" stage—because a rational economic actor such as BoA cares about its total bottom line liability, not the form of the relief or the stage at which it is negotiated; or

(2) the debt portion of the relief truly is a "throw in" that is worth little to either BoA or class members.

As discussed further below, the latter is more likely, and the Court should order the settling parties to provide information about (1) how BoA valued the debt portion for accounting purposes to confirm the true value of the debt relief, and (2) whether class counsel inquired about this issue or otherwise investigated the value during the settlement negotiations.

If the value of the debt relief is immaterial as Threatt suspects, then there is not a fundamental conflict between the cash subgroup and debt forgiveness subgroup. While the *de minimis* value of the debt relief would not present an adequacy problem, it does reduce the purported value of the settlement advanced by the parties for purposes of the Court's approval analysis and attorneys' fee award. *See Allen v. Bedolla*, 787 F.3d 1218, 1224 (9th Cir. 2015) (court must look at the economic reality of a class-action settlement, and has duty to make inquiries to determine this). It is likely that the debt relief is largely illusory and was added to the settlement as a gimmick to make the settlement appear more valuable, at little cost to the defendant, to increase the likelihood that the Court would approve the settlement and award the full amount of attorneys' fees requested by class counsel. And, in fact, class counsel cited

the full purported value of the debt relief (then $29.1 million) to justify a fee request that equaled 24.3% of the combined value of the cash and debt relief. Dkt. 80-1 at 10.

If, on the other hand, as class counsel claims, and the Court appeared to believe at the fairness hearing, the value of the debt relief is material and is really over $29 million, then there is a potential conflict between the two subgroups competing for relief that requires separate representation under Rule 23(a)(4). Threatt understands that objector Sanchez intends to address the potential conflict among these two subgroups of class members. Consistent with the Court's directive that Threatt and Sanchez work to avoid duplicative briefing, Threatt refers to and incorporates Sanchez's brief to the extent it is not inconsistent with the positions taken herein and in Threatt's objection (Dkt. 85).

ARGUMENT

I. Rule 23(a)(4) requires adequate representation of class members by class representatives and counsel.

Where there are significant differences among subgroups within a class, "the members of each subgroup cannot be bound to a settlement except by consents given by those who understand that their role is to represent solely the members of their respective subgroups." *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 627 (1997) (internal quotation marks omitted). Thus, adequacy under Rule 23(a)(4) requires the class representatives to "possess the same interest and suffer the same injury as the class members." *Id.* at 625-26 (internal quotation marks omitted). There must be an absence of "conflicts of interest between named parties and the class they seek to represent." *Id.* If the "interests of those within the single class are not aligned," and the named parties seek "to act on behalf of a … class rather than on behalf of discrete subclasses," then it will be impossible for any one representative to adequately

represent the entire class, and the class as structured simply can never satisfy the adequacy rule. *Id.* "[T]he linchpin of the adequacy requirement is the alignment of interests and incentives between the representative plaintiffs and the rest of the class." *Dewey v. Volkswagen A.G.*, 681 F.3d 170, 183 (3d Cir. 2012).

The adequacy requirement is not limited to class representatives. Each subgroup also must have "separate representation [by counsel] to eliminate conflicting interests of counsel." *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 856 (1999); *see also In re Literary Works in Elec. Databases*, 654 F.3d 242, 249 (2d Cir. 2011). In determining whether a class can be certified, a "court has an ongoing duty … to scrutinize the class attorney to see that he or she is adequately protecting the interests of the class." Herbert Newberg & Alba Conte, 4 Newberg on Class Actions § 13:20 (4th ed. 2009).

Contrary to the joint response, the adequacy requirement does not change simply because class members can opt out of the settlement class. *See* Joint Response at 13. "Regardless of whether class members are given opt-out rights, the court is still required to ensure that representation is adequate and that the settlement is fair to class members." *Epstein v. MCA, Inc.*, 50 F.3d 644, 667 (9th Cir. 1995), *rev'd on other grounds sub nom. Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367 (1996); *see also Marshall v. Holiday Magic, Inc.*, 550 F.2d 1173, 1179 (9th Cir. 1977) (Kennedy, J., concurring) ("I do not believe that a provision for opting out of the class provides an entirely satisfactory answer to the claim that a lead attorney failed to discharge that duty of representation. Particularly where the settlement could be easily modified to resolve the class conflicts, the dissident members should not be required to take the settlement or leave it."); *Acosta v. Trans Union, LLC*, 243 F.R.D. 377, 388 (C.D. Cal. 2007) (opt-out mechanism did not cure deficiencies in settlement because "common sense and empirical

study admonish that any belief that a significant member of class members would do so is ill-founded").

II. Because the debt relief likely has no material value, the problem with the settlement likely arises from the illusory debt relief, not inadequacy of representation.

In their joint response, the parties state that "Class Counsel did not raise the issue of debt forgiveness for Class Members who had not paid extended overdrawn balance charges ("EOBC") until they believed they had obtained as mush cash as [BoA] was willing to pay Class members who had paid EOBCs." Joint Response at 1. They further state that "Class Counsel never considered reducing the cash portion of the Settlement to increase the debt forgiveness portion—or vice versa." *Id.* In other words, class counsel and BoA negotiated for the $37.5 million cash portion of the settlement, with class counsel ultimately reaching a point at which BoA refused to increase the amount. Only at that point did class counsel bring up the subject of relief for the debt subgroup of the class. This sequence of negotiation strongly suggests that the debt relief was a "throw-in" item for BoA, sought by class counsel so as to create the illusion of relief and unobjectionable to BoA because of its *de minimis* accounting value. Why else would BoA agree to include the relief—purportedly valued at about $29 million—at the back-end of the negotiations after it had refused to increase the settlement consideration beyond the negotiated cash payment? A defendant generally cares only about its bottom-line liability, not how that liability is allocated between different forms of relief. Alternatively, *if* the value of the debt reduction truly is as much as the $29 million that class counsel claims, then class counsel provided inadequate representative in the first phase of negotiations by leaving that $29 million in value on the table and also by failing to have separate representation for the debt and cash subgroups in direct competition for that settlement relief.

But the accounting value of the consumer debt reduction is almost certainly pennies on the dollar. The likelihood that BoA will recover outstanding EOBC fees from consumers whose accounts have been closed for months and years is virtually nil. The small dollar amounts make the debt uncollectible. It would cost BoA more to pursue payment from these former customers than it would recover, and it is highly unlikely that former bank customers with closed accounts will return to voluntarily pay the outstanding EOBC fees. While BoA could sell the debt to a collection agency, the sale value is only pennies on the dollar (largely because of the collection problems identified above) and, then, BoA would no longer own the debt and could not forgive it. The credit reporting component of the debt relief similarly adds virtually no value. Banks that report to credit bureaus already have a legal obligation to correct reported information, and, in any event, the relatively small change in a consumer's outstanding debt occasioned by the settlement will have no material effect on the individual's credit rating. The material events adversely affecting the credit score were the facts of the overdraft and account closure. Debt-portion class members thus receive only *de minimis* value from the settlement—payment of debt they never would repay anyway, and which Bank of America almost certainly accounts for as worth pennies on the dollar at most; and, at best, an immaterial change to their credit profile.

In an effort to reveal the value of the debt forgiveness, Threatt's counsel asked counsel for the settling parties for the accounting value that BoA assigned the debt and whether the parties had discussed the value during the course of the settlement negotiations. Class counsel responded that he did not know what accounting charge BoA will take for the debt relief, while BoA claimed that it does not have the figure available and refused to generate it for purposes of this response. The Court should require the parties to provide BoA's accounting value for

the debt forgiveness prior to the hearing so the Court can properly determine if the class should be certified and, if the Court approves the settlement, the appropriate amount to award in attorneys' fees. *See In re Dry Max Pampers Litig.*, 724 F.3d 713, 722 (6th Cir. 2013) (rejecting settlement where class members "receive[d] nothing but illusory injunctive relief"); *Allen*, 787 F.3d at 1224 (court must examine "economic reality" to approve settlement and award attorneys' fees); *see also Koby v. ARS Nat'l Servs., Inc.*, 846 F.3d 1071, 1079 (9th Cir. 2017) (settling parties "bore the burden of demonstrating that class members would benefit from settlement's injunctive relief").

Another way the Court could quickly determine whether the debt relief is really worth $29 million is to ask the parties to reconcile the disparate treatment of the two subclasses by reducing the debt relief and increasing the cash payment—*i.e.,* reduce the debt relief from $29 million to, say, $4 million, and increase the cash portion of the settlement fund by $25 million, or even $24 million. Class counsel pretends that $1 of debt relief is equal to a $1 cash payment to the class, but it is virtually certain that Bank of America would reject trading $25 million of debt relief for $25 million—or even $24 million—of cash.

If the value of the debt relief portion of the settlement is in fact *de minimis*, then there is not a conflict that rises to an adequacy of representation problem under Rule 23(a)(4). The cash subgroup will recover proportionate to its harm in cash, while the debt subgroup will recover proportionate to its harm in debt forgiveness. It is possible that if BoA had traded cash for debt relief with precision as to the actual value, there might be less debt relief and perhaps a few hundred thousand dollars more in cash. To the extent relatively immaterial conflicts or allocations such as this remain, however, the Court may permit efficiency concerns to override "fine lines." *In re Mexico Money Transfer Litig.*, 267 F.3d 743, 747 (7th Cir. 2001) (Easterbrook, J.).

Circuit law provides that settlements properly may allow for balancing, approximation, and "rough justice." *Officers for Justice v. Civil Serv. Comm'n of City & Cty. of San Francisco*, 688 F.2d 615, 625 (9th Cir. 1982).

If, on the other hand, the debt relief has substantial actual value, then there likely is a fundamental conflict that precludes a finding of adequate representation. It would mean that class counsel left significant money on the table that could have been allocated to the cash subgroup, which will recover only a small portion of its damages under the settlement, and the named representatives failed to object or actively monitor class counsel to avoid this deficient result. Meanwhile, the cash subgroup is on the hook for the full amount of attorneys' fees, incentive awards, and administration costs that should be borne equally by the class. Although the named plaintiffs are part of the cash subgroup and presumably have an interest in achieving favorable results, any claim of adequate representation depends on the fiction that class representatives are engaged and active monitors of the proceedings and class counsel. While Threatt is unaware of any evidence of an improper relationship between the named plaintiffs and class counsel or other structural inadequacy, the named plaintiffs' acquiescence in a settlement that misallocates the relief (and provides for an excessive fee award) raises questions about the adequacy of their representation. *See, e.g.*, *In re Chiron Corp. Sec. Litig.*, No. C-04-4293, 2007 WL 4249902, at *11 (N.D. Cal. Nov. 30, 2007) (in light of the excessiveness of a 25% fee award, "it does not appear that [lead plaintiff] has made an effort to maximize the net recovery of absent class members. Nor does it appear that [she] negotiated a fee agreement in a way that reflects the market value of lawyer services.").

* * *

The most critical problem with the settlement is the inflated value of the debt relief, and its use to justify outsize attorneys' fees that reduce the cash recovery available to class members.

CONCLUSION

For the foregoing reasons, the Court should require the parties to disclose how BoA accounted for the debt forgiveness component of the settlement relief and whether the actual value was discussed during settlement negotiations. The Court should consider the actual value of this relief in deciding whether to approve the settlement and how much to award in attorneys' fees. In the unlikely event that the actual value of the debt forgiveness is substantial, then settlement approval should be denied due to inadequate representation under Rule 23(a)(4).

Dated: August 13, 2018

Respectfully submitted,

/s/ Theodore H. Frank
Theodore H. Frank (SBN 196332)
COMPETIVE ENTERPRISE INSTITUTE
CENTER FOR CLASS ACTION FAIRNESS
1310 L Street NW 7th Floor
Washington, DC 20005
Email: ted.frank@cei.org
Telephone: (202) 331-2263

Attorney for Objector Rachel Threatt

CERTIFICATE OF SERVICE

I hereby certify that on this day I electronically served the Response of Objector Rachel Threatt to Order to Show Cause on all CM/ECF participating attorneys at their registered email addresses, thus effectuating electronic service under S.D. Cal. L. Civ. R. 5.4(d).

Dated: August 13, 2018

/s/ Theodore H. Frank
Theodore H. Frank