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Second Circuit: presumption of fairness no longer applies to class settlements negotiated at arm's length

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Takeaway: When evaluating the fairness of a proposed class settlement, Federal Rule 23(e)(2) requires a district court to take into account, among other considerations, the terms of any proposed award of attorneys' fees and expenses. "This review provides a backstop that prevents unscrupulous counsel from quickly settling a class's claims to cut a check." *Moses v. New York Times Company*, 79 F.4th 235, 244 (2d Cir. 2023) (quoting *Fresno County Employees' Ret. Ass'n v. Isaacson/Weaver Fam. Tr.* , 925 F.3d 63, 72 (2d Cir. 2019)). In *Moses*, the Second Circuit recently vacated a class settlement because the district court improperly presumed that an arms-length class settlement – including a substantial attorneys' fee award – was fair.

In that case, Maribel Moses, on behalf of herself and a putative class of California subscribers, sued The New York Times ("NYT") in the Southern District of New York for violations of California's Automatic Renewal Law (Cal. Bus. & Prof. Code § 17600, et seq. (the "ARL")), alleging NYT automatically renewed subscriptions without providing required disclosures and authorizations.

Early in the case, while a motion to dismiss filed by the NYT was pending, and after the parties had engaged in informal discovery and a full-day mediation, the parties negotiated a settlement agreement in which the class members settled their claims in exchange for (1) NYT's modification of its subscription renewal practices and (2) either electronic access codes for one-month NYT subscriptions *or* pro rata cash payments. The settlement further provided for the payment of significant attorneys' fees to class counsel ($1.25 million) and a $5,000 incentive award to Ms. Moses. *Moses*, 79 F.4th at 239.

A *pro se* objector, Eric Alan Isaacson, objected to the proposed settlement, arguing that it was unfair, that the attorneys' fees award exceeded the limits imposed by the coupon settlement provisions of the Class Action Fairness Act ("CAFA"), and that the $5,000 incentive award was improper. Overruling the objection, the district court certified a settlement class under Federal Rule 23(b)(2) and approved the settlement. Isaacson appealed the district court's judgment and the Second Circuit reversed, ruling that the district court had misapplied Rule 23 in approving the settlement.

In 2018, Federal Rule 23 was revised to require a district court to evaluate four "primary procedural considerations and substantive qualities that should always matter to the decision whether to approve [a settlement] proposal." *Moses*, 79 F.4th at 242 (quoting Fed. R. Civ. P. 23(e)(2) Advisory Committee's Note to 2018 Amendment). The purpose of this revision was "not to displace any factor, but rather to focus the court and the lawyers on the core concerns of procedure and substance" (*id*.), including whether: "(A) the class representatives and class counsel have adequately represented the class; (B) the proposal was negotiated at arm's length; (C) the relief provided for the class is adequate, taking into account: (i) the costs, risks, and delay of trial and appeal; (ii) the effectiveness of any proposed method of distributing relief to the class, including the method of processing class-member claims; (iii) the terms

of any proposed award of attorney's fees, including timing of payment; and (iv) any agreement required to be identified under Rule 23(e)(3); and (D) the proposal treats class members equitably relative to each other." *Id*. (quoting Fed. R. Civ. P. 23(e)(2)). The panel observed that "[t]he first two factors are procedural in nature and the latter two guide the substantive review of a proposed settlement." *Id*. at 242-43.

On the issue of "procedural fairness," the panel ruled that the district court erred in *presuming* that the settlement was fair because it was negotiated at arm's length. Before the 2018 revision of Federal Rule 23(e)(2), the Second Circuit "applied a presumption of fairness to settlement agreements resulting from arms length negotiations." *Id*. at 243. Relying on the Ninth Circuit's decision in *Roes, 1-2 v. SFBSC Mgmt., LLC*, 944 F.3d 1035, 1049 n.12 (9th Cir. 2019), however, the panel ruled that "[t]he codification of arm's-length negotiation as one of two procedural factors (the other being the adequacy of class representatives and counsel) – and one of four core factors – that courts must consider when approving a proposed settlement supplants its historic role as a presumption." *Id*. It concluded "that Rule 23(e)(2) prohibits courts from applying a presumption of fairness to a settlement agreement based on its negotiation at arm's length." *Id*.

In terms of "substantive fairness," the panel observed that the district approved the class settlement by analyzing the proposed $1.25 million attorneys' fee award separately from settlement's overall fairness, thereby applying the "wrong legal standard." *Id.* at 246. The panel further ruled that the settlement's provision of access codes for free one-month subscriptions were "coupons" triggering CAFA's coupon settlement provisions, which the district court failed to apply. *Id.* at 248-53. Regarding the $5,000 incentive award to Ms. Mabel, the panel ruled that, although incentive payments to class representatives are not categorically prohibited, the district court would be required on remand to reevaluate the incentive award based on the proper application of all of the Rule 23(e)(2) factors. *Id.* at 253-56 & n.12.