

Virtual Wage and Hour CLE Breakfast

Resolving Wage and Hour Claims *Part 3: Class and Collective Action Claims*

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Recap: *Resolving Wage and Hour Claims Series*

- In Part 1 of this series (October 2020), we discussed strategies for resolving individual wage and hour claims.
 - How to investigate and value an individual claim, and formulate a settlement offer.
 - How to memorialize an individual settlement, and whether to seek judicial approval.
 - Post-litigation considerations.
- In Part 2 of this series (December 2020), we began a discussion about strategies for resolving class and collective action wage and hour claims.
 - In addition to investigating and valuing claims, we discussed:
 - Tolling agreements, confidentiality agreements in aid of settlement discussions, and disclosures in aid of settlement discussions.
 - Mediation strategies and engaging expert consultants.

Agenda

- Settlement Structure Considerations
 - FLSA settlements
 - State law settlements
 - Hybrid settlements
 - Additional considerations, e.g. claims-made vs. common fund settlements, reversionary vs. non-reversionary settlements
- Settlement Agreement Considerations
 - Common provisions and problematic provisions
 - Tax treatment
- Claims Administration

Settlement Structure Considerations



Fair Labor Standards Act (FLSA) Settlements

- Federal wage claims are governed by the FLSA, and claims seeking relief for multiple individuals are called “collective actions.”
- An employee may bring a putative collective action “on behalf of himself or themselves and other employees similarly situated.” 29 U.S.C. § 216(b).
- The FLSA is an “opt-in” statute, *i.e.*, “[n]o employee shall be a party plaintiff to any such action unless he gives his consent in writing to become a party and such consent is filed in the court in which such action is brought.”
- Releases of FLSA claims are generally only valid and enforceable if approved by a court or part of a settlement supervised by the U.S. Department of Labor.
 - *Cheeks v. Freeport Pancake House, Inc.*, 796 F.3d 199 (2d Cir. 2015)

FLSA Settlements (cont'd)

- Courts in the Second Circuit review settlements for fairness under the factors set forth in *Wolinsky v. Scholastic Inc.*, 900 F.Supp.2d 332 (S.D.N.Y. 2012)
- In approving the settlement of FLSA claims, the court is not adjudicating the rights of absent class members—only those individuals who have affirmatively “opted in” to the litigation are bound.
- One question that arises in FLSA settlements is the form of the consent to join.
 - Should the parties require claim forms?
 - Can a consent to join be included on the back of a check?

FLSA Settlements (cont'd)

- Courts in New York and California have become increasingly skeptical of “back of the check” consents.
 - *E.g., Douglas v. Allied Univ. Sec. Servs.*, 371 F.Supp.3d 78 (E.D.N.Y. 2019)
- General process for FLSA settlements (conservative approach based on recent case law):
 - Parties notify the court of a settlement and request that notice of the settlement be sent to putative collective members to give them an opportunity to opt in to the settlement.
 - If the court approves the notice, it is sent to putative collective members, who have a period of time to submit a claim form/opt-in form.
 - The notice includes the recipient’s individual settlement allocation and claim form/opt-in form.

FLSA Settlements (cont'd)

- Following the close of the opt-in period, plaintiffs file a motion for final approval of the settlement.
- If the court approves the settlement, checks are distributed to those who have filed claims/opted in.
- Checks should include language releasing both federal and state claims.
- Once the court approves the settlement and checks are distributed, individuals who cash their checks will have released both FLSA and (if referenced on the check) state law claims.
- Individuals who do not timely submit claim forms/opt-in forms will not release FLSA claims, and therefore retain their right to sue under the FLSA.

FLSA Settlements (cont'd)

- Parties can agree, in the settlement agreement, to reversion of settlement amounts allocated to individuals who do not opt in/return a claim form (and therefore are not releasing FLSA claims).
 - If those individuals are releasing *state law* claims, however, plaintiffs' counsel may insist on *partial* (and not *full*) reversion.

State Law Settlements

- State law claims seeking relief for individuals other than the named plaintiffs are ordinarily brought as class actions, under FRCP 23 or a state procedural law equivalent (e.g., Article 9 of the NY CPLR).
- While individual state law wage claims can generally be released through private agreement and without judicial approval, the ability to bind absent class members to a settlement requires court approval.
- Plaintiffs must satisfy numerosity, commonality, typicality, and adequacy under FRCP 23(a), and demonstrate predominance of common questions of law and fact and superiority of the class action mechanism under FRCP 23(b).

State Law Settlements (cont'd)

- Approval of a class action settlement requires a more stringent showing than the FLSA's "similarly situated" standard.
- FRCP 23 is an opt-out statute, *i.e.*, a judicially approved class action settlement will bind all class members to the settlement and release their state law claims, unless they affirmatively exclude themselves from the settlement by "opting out."

State Law Class Action Settlements

- Process for state law class action settlements:
 - After the settlement agreement is signed, the plaintiff(s) file a motion in court for preliminary approval of the settlement.
 - If the court grants preliminary approval, notice of the settlement and rights is sent to class members (usually by a third-party claims administrator).
 - In the notice, class members are given various options:
 - To return a claim form to join the settlement (if the settlement requires claim forms).
 - To opt out of the settlement.
 - To object to the settlement.
 - To do nothing.

State Law Class Action Settlements (cont'd)

- Process for state law class action settlements:
 - Generally, you can't object to a settlement if you opt out.
 - If claims forms are not required, individuals who do not affirmatively opt out (“do nothings”) will receive a settlement check if the court grants final approval of the settlement, and will release their state law claims.
 - If claim forms are required, individuals who do not return a claim form or opt out (“do-nothings”) will not receive a settlement check, but may nonetheless release their state law claims (because they have not opted out).
 - The parties must carefully describe the consequences of class member actions and inactions in both the settlement agreement and the class notice.
 - If the court approves the settlement, those consequences—including with respect to the release of claims by “do nothings”—will be binding.

State Law Class Action Settlements (cont'd)

- Process for state law class action settlements:
 - After the claim/opt-out/objection period closes, the plaintiff(s) file a motion for final approval of the settlement, and the court holds a fairness/final approval hearing.
 - If the court grants final approval, settlement checks are distributed to the participating class members.
 - Settlement checks should include a release of state law claims, as “belt and suspenders” to the judicial release contained in the court’s final approval order.

Fairness Hearings in Rule 23 Settlements: The *Grinnell* Factors

- In the Second Circuit, courts evaluate the fairness of a Rule 23 settlement using a non-exhaustive set of factors set forth in *City of Detroit v. Grinnell Corp.*, 495 F.2d 448 (2d Cir. 1974):

1. The complexity, expense, and likely duration of the litigation.
2. The reaction of the class to the settlement.
3. The stage of the proceedings and the amount of discovery completed.

4. The risks of establishing liability.
5. The risks of establishing damages.
6. The risks of maintaining the class action through trial.
7. The ability of the defendant(s) to withstand a greater judgment.

8. The range of reasonableness of the settlement fund in light of plaintiffs' best possible recovery.
9. The range of reasonableness of the settlement fund in to a possible recovery in light of all the attendant risks of litigation.

FLSA + State Law (“Hybrid”) Settlements

- The supermajority of wage and hour lawsuits seeking relief on behalf of a group of individuals are going to be “hybrid” collective and class actions seeking relief under both the FLSA and state laws.
 - There are many claims and remedies available under state laws that are not available under the FLSA.
 - In certain states, wage and hour claims carry a longer statute of limitations than the FLSA, allowing for a longer lookback period for violations and damages.
 - Defendants generally will want to dispose of both federal and state law claims in one fell swoop if they are paying money to resolve a dispute.

Hybrid Settlements (cont'd)

- Hybrid settlements require approval under both the FLSA/collective action and FRCP 23/class action frameworks.
- In hybrid settlements, parties can expect to be before the court at least twice, once at preliminary approval, and again at a fairness hearing to seek final approval of the settlement.

Hybrid Settlements (cont'd)

- Hybrid settlements must account for both the “opt in” nature of FLSA settlements and the “opt out” nature of state law class action settlements.
- In light of increasing judicial hostility to “back of the check” opt-ins, the notice sent to employees following preliminary approval will likely need to include an opt-in/consent to join form.
 - Only individuals who return opt-in forms will receive a settlement payment for their FLSA claims and release those claims.
 - The parties must agree (and specify in the settlement agreement, judicial approval motion(s), and notices to class/collective action members) whether individuals who do not opt in to the FLSA settlement will nonetheless release and receive a payment for their state law claims.

Hybrid Settlements (cont'd)

- In an “all or nothing” settlement, an individual would receive no payment for either FLSA or state law claims unless he or she returns a claim form, which would also serve as the opt-in form for purposes of the FLSA.
 - Individuals who do not return claim forms would not release FLSA claims.
 - Individuals who do not return claim forms may or may not release state law claims, depending on the terms of the approved settlement.
 - Individuals who opt out would release neither FLSA nor state law claims and receive no settlement payment.
- In a bifurcated settlement, a portion of each individual’s settlement award is allocated to FLSA claims and a portion is allocated to state law claims. Individuals who neither opt in to nor opt out of the settlement will not release FLSA claims, but they will release (and receive a check for) their state law claims.

Hybrid Settlements (cont'd)

- At first blush, an “all or nothing” settlement seems strategic in all circumstances, but the plaintiff(s) may not agree to it and the court may not approve it.
- Particularly if “do nothing” plaintiffs are releasing state law claims, there will generally be an expectation that the defendant should pay *something* in respect of those state law claims.
- Leaving FLSA claims “on the table” while paying for a release of state law claims may or may not be strategic, depending on the age of the claims and the state statutes of limitations involved.
 - For example, if the exposure in the last 3 years is low but in prior 3 years is significant, the value of a release under New York law may far outweigh the value of an FLSA release.

Claims-Made vs. Common Fund Settlements

- A settlement can be “claims-made” or common fund.
- A claims-made settlement is one in which a class member must affirmatively return/file a claim form in order to participate in the settlement.
 - Individual settlement allocations are pre-allocated.
 - Generally in a claims-made settlement, some or all of the settlement amount allocated to the individuals who fail to file claims reverts to the defendant.
 - Participation is generally much lower in a claims-made settlement than in a settlement in which class members are not required to take any action to receive a settlement payment.

Claims-Made vs. Common Fund Settlements (cont'd)

- A claims-made settlement can bridge the gap between what an employer is willing to pay and what plaintiffs are seeking.
 - Plaintiffs' counsel may have a reasonable gauge of what participation will be.
- It is important to pay careful attention to the design of a claims-made settlement.
 - Issues can arise when plaintiffs' counsel attempts to calculate their fees “off the top,” *i.e.*, off the maximum settlement amount and not based on the amount eventually distributed to participating class members.
 - In that circumstance, attorneys' fees may be a higher percentage than what is reflected in the approval motion or what is permitted under the law.

Claims-Made vs. Common Fund Settlements (cont'd)

- A “common fund” settlement is one in which the settlement fund is committed and not subject to reversion.
 - The settlement contemplates a process for redistributing unclaimed/uncashed awards to the participating class members, until it becomes impractical to do so (in which event the remaining funds are ordinarily donated to a charity specified in the settlement agreement (a *cy pres* award)).
 - A common fund settlement is the least advantageous option for a defendant because 100% of the money is committed, and unclaimed money cannot be returned.
 - Risk of paying too much to too few people, and of leaving viable claims out there.
 - Risk can be mitigated through the use of blow-up clauses.

Reversionary vs. Non-Reversionary Settlements

- In a reversionary settlement, some or all of the settlement fund can revert to the defendant.
 - In a claims-made settlement, a defendant may receive back all funds allocated to individuals who do not make a claim.
 - In a non claims-made settlement, the parties may agree to reversion in whole or in part.
- Reversion may be for the FLSA portion of the claims of “do-nothings” who have not opted into the litigation, on the ground that the defendant will not obtain a release of FLSA claims for those individuals.
- If a defendant is not getting a release of *any* claims, federal or state, full reversion is appropriate, as the defendant remains exposed to both FLSA and state law claims.

Class Action Fairness Action of 2005 (CAFA), 28 U.S.C. § 1715

- Requires a defendant settling a class action in federal court to provide notice of the settlement to federal and state officials before a settlement may be approved.
- Notice must be sent within 10 days after proposed settlement filed with court, and at least 90 days before final approval.
- The notice must include, among other things, the names of the class members who reside in each state and their estimated share of the settlement.
 - If names are not feasible, must include at least a reasonable estimate of the number of class members residing in each state.
- Failure to comply can provide class members with a loophole to refuse to comply with and be bound by the settlement.

Scope of Class Considerations

- When settling a class or collective action, a defendant should consider who it wants to sweep into the settlement, and therefore secure a release of claims from.
 - It is important to think about this during any fact investigation, particularly when an employer receives a pre-litigation demand letter.
- Generally speaking employers want to buy peace with the largest swath of employees they can, for the money they are able/willing to spend to resolve the action.
- Class/collective representative(s) have to be reasonably similarly situated to members of the settlement class and/or meet class requirements.
 - Courts will scrutinize this as part of the fairness proceeding.

Settlement Agreement Considerations



Common Provisions Defendants Want

- Reversion of funds for individuals who do not release claims.
 - No full commitment of maximum settlement amount
 - No re-distribution of unclaimed settlement allocations/uncashed settlement checks
 - Employers should always seek reversion of amounts allocated to putative class members who opt out (and therefore retain both their FLSA and state law claims)
 - Employers should ask for reversion of amounts allocated to “do nothings” (who retain their FLSA claims and may or may not be bound to a judicial release of their state law claims)
 - Class counsel may insist on a partial reversion in cases where putative class members will be retaining some claims (e.g., FLSA) but not others (e.g., state law claims)
 - Remember that if there is no reversion, the overall settlement amount will be committed and distributed regardless of how many putative class members retain their claims (and can still sue you, depending on statutes of limitations)
 - Given the judicial hostility to reversionary settlements in some jurisdictions, defendants should press for a “claims made” settlement under which funding is driven by the number and amounts of claims made/participants, and there is technically no “reversion”—because the amounts allocated to those who don’t file claims/elect to participate are never committed in the first place (so there’s nothing to “revert”).

Common Provisions Defendants Want

- As current a release as possible.
 - Defendants should ask for a release of claims through the date of preliminary approval.
 - Class counsel will sometimes insist on a shorter release end date (e.g., through the date the settlement agreement is signed).
 - If the wage and hour practice that led to the lawsuit has not already been remediated on a going-forward basis, the defendant should ensure that it is prior to the release end date.
 - If it isn't, then the defendant is exposed to a follow-on class action based on the same pay practice, for the period of time after the (initial) class release ends.

Common Provisions Defendants Want

- Settlement checks (or accompanying stubs or documents, which should be referenced on the checks themselves) should always include a release, in addition to any release in the settlement agreement itself.
- General releases from the named plaintiffs or others receiving service awards.
- Review and/or approval of documents to be filed with the court.
 - While motions for judicial approval of the settlement are filed by the plaintiffs, defendants should reserve the right to review and comment on the motion papers prior to filing.
 - Defendants should always reserve the right to approve the content of notices to putative class/collective members and proposed court orders.

Common Provisions Defendants Want

- Blow-up provision.
 - Gives the defendant the right to rescind the settlement if a threshold number of putative class members (or the aggregate value of their settlement awards) exceeds a certain percentage of the overall.
 - This protects the defendant from exposure to a separate class action arising from the same facts, circumstances, and population.
- Cooperation clauses.
 - Ensures that once the settlement agreement is signed, all parties are working cooperatively and taking all reasonable steps to effectuate the settlement, including seeking judicial approval.
 - The parties should agree to work together, diligently and in good faith, to remedy any issues leading to a denial of court approval and to seek approval of a renegotiated agreement (without any change in the gross settlement amount).

Common Provisions Defendants Want

- As much confidentiality as the court will allow (e.g., other than what is necessary to seek court approval).
 - Plaintiffs and class counsel should agree to keep the negotiations leading up to the settlement and (if not disclosed in the papers filed with the court) the amount of individual class members' settlement awards confidential.
 - Plaintiffs and class counsel should make no public statements concerning the settlement beyond those contained in court filings necessary to seek approval.
 - Class counsel should agree not to make any reference to the litigation or settlement on their websites, blogs, advertisements, releases, and/or any other publications, and should agree not to discuss the matter with the press.

Tax Treatment of Settlement Payments

- The wage portions of a settlement are subject to tax withholding and reporting on a Form W-2.
 - This is true for former employees as well. See Treas. Reg. § 31.3401(a)-1(a)(5).
- Liquidated damages and interest are considered non-wage income and (if over \$600) are reported on a Form 1099-MISC (LDs) or 1099-INT (interest).
 - See IRS Rev. Ruls. 72-268 (Jan. 1972) (liquidated damages), 80-364 (Jul. 1980) (interest).
- The IRS has taken the position that service awards/incentive payments to named class representatives are wage income and should be reported as such.
 - See IRS Chief Counsel Advisory Statement 201311022 (Mar. 15, 2013)
- The IRS has taken the position that class counsel's' fees and costs are not considered income to the class members (but should be reflected on a Form 1099 to class counsel).
 - See, e.g., IRS Office of Chief Counsel Memorandum, PRENO-111606-07 (May 18, 2007).

Tax Treatment of Settlement Payments

- Particularly where the answer is unclear, defendants should consult with their accountants and/or tax counsel to confirm their strategy regarding the tax treatment of settlement payments.
- In many cases, tax withholding and reporting will be handled by the settlement claims administrator that disburses settlement proceeds from a qualified settlement fund (QSF) established for the sole purpose of administering the settlement.

Problematic Provisions in Settlement Agreements

- Courts analyzing wage and hour settlements have shown increasing hostility to certain provisions that employers would otherwise include in a private settlement agreement.
 - Restrictive confidentiality and non-disclosure provisions
 - Overbroad releases
 - *E.g., Lopez v. Nights of Cabiria, LLC*, 96 F. Supp. 3d 170 (S.D.N.Y. 2015)
 - Non-disparagement provisions
 - *Gaspar v. Pers. Touch Moving, Inc.*, No. 13-CV-8187 (S.D.N.Y. Dec. 3, 2015)
 - No re-employment provisions
 - *Reyes v. Hip at Murray Hill*, No. 15-CV-238 (S.D.N.Y. Jan. 6, 2016)
 - Unsupported or outsized attorneys' fees
 - No “future representations” by class counsel

Claims Administration



Claims Administration

- Third-party claims administrators handle the administrative aspects of class action settlements.
- The scope of their responsibilities will be agreed to in the settlement agreement and approved by the court as part of the approval process.
- The services provided by claims administrators typically include:
 - Facilitate dissemination of notice to class/collective members.
 - Field objections and opt-outs.
 - Handle communications and questions from class members, and where appropriate, direct them to class counsel.

Claims Administration (cont'd)

- Provide periodic reports to the parties about the status of the settlement.
- Establish the qualified settlement fund.
- Distribute settlement funds to class members.
- Manage tax reporting.
- Prepare supporting documents/testimony for court filings.

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Virtual Wage and Hour CLE Breakfast

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