Statement of Howard A. Specter
Before the Third Circuit Task Force on
Appointment of Counsel in Class Actions

My name is Howard Specter. I first want to thank the Task Force for the opportunity to present my views concerning the questions of whether and, if so, how courts ought to conduct auctions for the purpose of appointing lead counsel in class action cases. In the interest of time, I ask that my written statement be made part of the Task Force's record.

My perspective is that of one who has maintained an active practice on behalf of plaintiffs in class actions for more than 30 years. I won't presume to replicate the masterful and scholarly presentations of Professors Coffee and Issacharoff. Rather, I will provide my perspective on what I consider to be just some of the many significant issues that face any court selecting or compensating class counsel. A principal consideration must be to ensure that the economic incentives provided to counsel maximize the probability that the recovery of class members, net of attorneys' fees and expenses, will be as large as possible.

I am concerned that courts, whether through a so-called "auction" process or more traditional means of selecting class counsel and regulating attorneys' fees, have become so focused on limiting the amount that attorneys may receive as fees that they may have unintentionally made it less likely that class members will receive as large a recovery as is reasonably possible. Although I do not have empirical data and

possess only anecdotal evidence to support my impressions, I suspect that many courts have bowed to the unwarranted public perception that class counsel are the regular and consistent recipients of unearned windfall fees. That perception is false. It unjustifiably suggests the adoption of appointment modes designed to reduce fees, however.

The important issue before this Task Force, it seems to me, is not so much whether courts should employ auctions in order to select class counsel. Rather, the Task Force should be concerned, no matter what selection method is employed, with ensuring that the economic incentives available to counsel make it more, rather than less, likely that the class ultimately will receive the largest recovery possible.

As I noted, I have been actively engaged in class action practice on behalf of plaintiffs for more than 30 years. My firm has been designated as lead or co-lead counsel in class actions that range across a diverse range of substantive areas, including securities fraud (e.g., *In re: Chambers Development Company Securities Litigation*, Civil Action No. 92-0679 (MDL 982) (W.D. Pa.)), antitrust (e.g., *Piggly Wiggly Clarksville, Inc. v. Mrs. Baird's Bakeries, Inc., et al.*, Civil Action No. 3:95-CV-48 (E.D.Tx.)), insurance sales practices (e.g., *In Re Metropolitan Life Insurance Company Sales Practices Litigation*, (MDL 1091) (W.D. Pa.)) and pharmaceutical/ product liability (e.g., *In re Baxter Corporation Gammagard Product Liability Litigation*, (MDL 1060), (C.D. Cal.)), to name just a few. It is a point of professional pride with me that as long ago as 1980, then-District Judge Becker was kind enough to recognize me as "one of the abler, more experienced and better known class action

attorneys currently practicing." *Bartelson v. Dean Witter & Co.*, 86 F.R.D. 657, 673 (E.D.Pa. 1980).

In addition to a class action practice, I have also maintained a substantial practice representing plaintiffs in individual litigation on a traditional contingent fee basis. This experience has allowed me to work within a fee regime that places the interest of the lawyer and of his or her client in parallel and that allows the lawyer to invest both time and money in a case with an eye toward maximizing the recovery of both the client and the attorney.

My primary observation is this: whether conducting lead counsel auctions or assessing attorneys' fees in more traditional ways, too many courts focus almost exclusively on ensuring that the lawyer is not paid too much, instead of developing procedures that make it as likely as possible that class members will recover as much money as possible, net of attorneys' fees and expenses. So long as courts focus simply on limiting attorneys' fees, they risk encouraging results that limit the recovery of class members as well. If, on the other hand, courts focus on providing incentives for counsel to generate as large a recovery on behalf of the class as is possible, the class members will be the ultimate beneficiaries. This is a result that a court acting as a fiduciary for class members should keep at the forefront of its consideration in selecting class counsel and in determining counsel's compensation.

I believe that some courts' present willingness to experiment with the auction process arises at least in part from a dissatisfaction with the now-predominant method for determining class action attorneys' fees. This method forces courts, after litigation

is complete, to make a judgment about what fee is "reasonable" to compen-sate counsel for the efforts that brought about the resolution of a particular case. I am, of course, not alone in observing that courts are generally ill-suited to make these sorts of judgments. See, e.g., *Class Auctions: Market Models for Attorneys' Fees in Class Action Litigation*, 113 Harv.L.Rev. 1827 (May 2000). More important for these purposes, however, is the observation that fee determinations after a case has been concluded leave counsel uncertain during the course of the litigation whether any particular large investment of time or money will ultimately be economically justifiable when the court makes its *ex post* fee determination. This uncertainty can result in under investment in cases by class counsel. By contrast, counsel in traditional contingent work can more readily assess the wisdom of a particular investment of time or money in a case, since his or her rate of recovery should the case ultimately prove successful is known from the very initiation of the case. No other professional or commercial undertaking comes to mind in which a successful provider of services or goods looks to unknown compensation at the end of his or her undertaking.

I think it is clear, then, that the predominant current method of determining fees ought to be replaced. Indeed, I have always believed this Task Force's predecessor made just such a recommendation: "[T]he Task Force recommends that in the traditional common fund situation . . ., the district court, on motion or its own initiative and at the earliest practicable moment, should attempt to establish a percentage fee arrangement agreeable to the Bench and to plaintiffs' counsel." Court Awarded Attorney Fees, Report of the Third Circuit Task Force, 108 F.R.D. 237 (1985). The earlier Task Force then went on to recommend that class counsel compensation plans be negotiated between counsel and a designee of the Court who

would act on behalf of putative class members. Counsel and this designee would negotiate an arrangement in the usual marketplace manner and submit a proposal for the court's approval. Id.

It has seemed to me since the original Task Force report that such a proposal had a great deal of merit. Most significantly, it replaces the after-the-fact assessment of reasonable fees with a market approach based upon an appreciation of the risks of the litigation at the time the litigation is commenced.

The principal problem with the prior Task Force's recommendation, at least so far as I am aware, is that courts do not employ it. Indeed, I have suggested the use of the Task Force's recommended procedure to district court judges at the initiation of a number of cases, and have never had the suggestion acted upon. Courts have expressed early positive reactions, but have never followed through. Perhaps we would not need to be here today if both courts and practitioners had taken the recommendations of the prior Task Force to heart.

I am not persuaded that the so-called "auction" process presents the best means for selecting class counsel, particularly since the prior Task Force's recommendations have largely been left unexplored. However, that process does at least have the merit of making the fee determination at the appropriate time in the litigation. If properly utilized, it can provide counsel with the appropriate incentives to maximize the class' recovery. All auctions, however, are not the same. As Professor Coffee has elsewhere noted, "[T]he bidding rules are the critical issues surrounding the use of an auction procedure, and they trump all [other issues.]" J. Coffee, "Auction Houses":

Legal Ethics and the Class Action, New York Law Journal (May 18, 2000). In fact, we should recognize that "auction" may be a misnomer to begin with. This is not a process in which multiple buyers are all bidding to buy the same item on the same terms as is with the case with art objects, race horses and other items. Nor does it resemble the procurement process in which, for instance, contractors bid on a government contract with predetermined specifications. Instead, it involves competing law firms with potentially different approaches to the litigation, different staffs and different experience levels.

The most commonly employed "auction" process is the one that does the worst job of aligning the interests of counsel and the class. By insisting that the marginal percentage of class counsel's fee should decline as the size of the class recovery increases, the bidding rules in such cases give counsel the incentive to settle a case cheaply and quickly. There is not, as there ought to be, any incentive to pursue the difficult to obtain "last dollars" that might be obtained in settlement or at trial. Courts employing this declining percentage regime seem concerned with limiting counsel's recovery to that which is thought to be "reasonable." What they fail to consider is that this formula may make it more likely that the class' recovery will be minimized as well. It is not unheard of for defense representatives to present a conflict of interest scenario by arguing the case of diminishing returns for counsel in urging a settlement proposal.

The few courts that have reversed the above process and have awarded counsel an increasing marginal percentage of the recovery as the recovery increases seem to me to be employing a sounder economic model. Counsel are encouraged to invest in

the case and persist in its prosecution with the aim of maximizing recovery. While it will be true that counsel will receive a greater fee under such a regime, it also seems to be indisputably true that the class will end up with more dollars in its pockets than if some other counsel incentives were in place. Courts employing this methodology appropriately have focused on maximizing the recovery of the class rather than on minimizing the fee of class counsel. As a fiduciary for the class, that is where a court's focus rightly ought to be.

I have another point which I hesitate to make too directly. Nonetheless, I must register concern with the views expressed in the Court of Appeals' recent decision in *In re: Cendant Corporation Prides Litigation*, 243 F.3d 721 (3rd Cir. 2001).[1]

In *Cendant Prides*, a panel of our Court of Appeals vacated a fee award that had been based upon an auction process. The Court vacated the fee, despite the fact that the class' recovery was exemplary; indeed, class members had recovered 100% of their losses, and attorneys' fees and reimbursement of expenses had no effect upon that recovery. Additionally, the panel conceded the fact that counsel had discharged the lead counsel function in exemplary fashion.

Nonetheless, the Court of Appeals found reason to vacate the fee award. It essentially regarded the auction price at which counsel agreed to work as establishing only a ceiling upon counsel's ultimate fee in the case. The actual fee could be determined in the view of the *Cendant Prides* court only after the traditional *ex post*

[1] I hasten to add that neither my firm nor I had any role in any aspect of the *Cendant Prides* litigation.

examination of reasonableness had been engaged in by the court. Since, in the Court's view, counsel's lodestar could not justify the award by the district court, the fee award was vacated. This result represents a departure from any auction or bidding process of which I am aware. There are, of course, bidding procedures and contracts that provide incentives for the successful or early conclusion of a projection. There are none of which I am aware that impose punishments or what amount to give-backs in such circumstances. Any bidder, lawyer or otherwise, should be entitled to certainty upon successful performance.

As I have noted, I am not persuaded that an auction procedure of any sort is required in order to arrive at an appropriate fee for counsel. But if such a procedure is to be employed, it cannot remain effective if it is subjected to routine judicial second-guessing and a lodestar review. One of the advantages of an auction is that it allows counsel to know the terms under which he or she is retained, thereby allowing counsel to more accurately judge whether a particular investment makes sense for prosecuting the case. Making counsel's ultimate fee award subject to an *ex post* judicial review for "reasonableness" takes away this critical element of certainty, and leaves counsel in no better position to judge what is prudent for prosecution of the case than the current system of judicial review.

I would like to thank the Task Force for the opportunity to testify. I believe that the auction process, while not a necessary or desirable element of the reform of current fee practices, could be an effective means of maximizing recovery for the class if care is taken to give counsel the incentive to strive for the greatest possible recovery. However, no good can come from the revision of procedures in the district

courts if the result of the application of those procedures is subject to routine second-guessing in the Courts of Appeals. Finally, I cannot resist noting the unoriginal thought that there will always be someone willing to provide goods or services for less with a resulting lowering of quality. Strict specifications in more ordinary procurement processes are designed to minimize that inherent risk of human frailty. I don't see how such safeguards can be incorporated in a bidding system among diverse law firms.

There are other issues which merit a discussion. Hopefully, we can touch on some of them at the Task Force's hearings.

Thank you again.

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