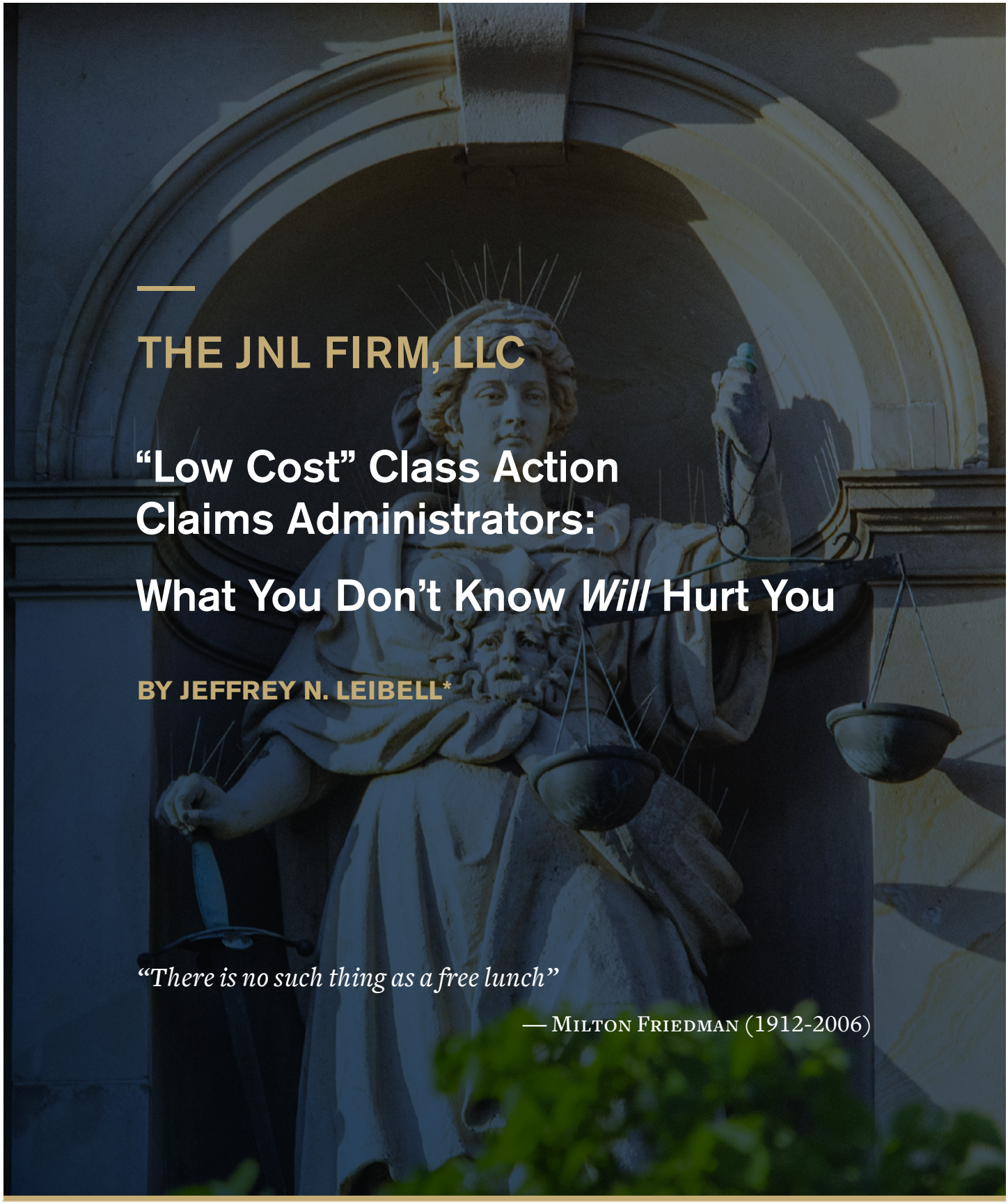


THE JNL FIRM, LLC

"Low Cost" Class Action Claims Administrators: What You Don't Know *Will* Hurt You

BY JEFFREY N. LEIBELL*

"There is no such thing as a free lunch"

— Milton Friedman (1912-2006)

THE JNL FIRM, LLC
Class Action Settlement Management
80 Baker Hill Road
Great Neck, New York 11023

Jeffrey N. Leibell
jeff@jnlfirm.com
516.652.2040
www.jnlfirm.com

Summary

As a direct result of inferior claims administrations performed by claims administrators selected based primarily on their low bids, "legitimate claimants" – those class action claimants that are class members and that submit proofs of claim that comply with judicially approved requirements – have suffered substantial financial harm and will continue to do so. Among claims administrators, there are substantial differences in accuracy and efficiency; those claims administrators that, to get selected, offer low bids cannot afford to, and, therefore, have not and will not, perform the tasks necessary to administer class action settlements accurately or efficiently. One consequence is that those "low cost" administrators incorrectly classify "ineligible claimants" – those that are not class members, or, even though they are, submit proofs of claim that are partially deficient or completely defective – as legitimate claimants, and, therefore, distribute to the former recoveries that should have gone to the latter. Accordingly, although it may appear that selecting low bidding claims administrators will save classes the marginal cost differentials between those low-cost claim administrators and the more expensive but higher quality claims administrators, the opposite is true: Selecting the lowest bidding administrators without adequately considering their corresponding accuracy and efficiency metrics has caused, and will continue to cause, legitimate claimants millions of dollars – far more than the cost "saved" by selecting low bidders – that, because of inferior claims administrations, legitimate claimants "pay" to ineligible claimants.

Established economic theory – the same economic theory that explains the financial cost to class members caused by selecting class counsel by means of auctions that did not fairly consider the quality of legal services – explains the financial cost to legitimate claimants that has resulted, and will continue to result, from using auctions to select claims administrators from among qualitatively diverse bidders. To test whether that economic theory also applies to claims administrators, I obtained and analyzed claims administration results from hundreds of class action settlements. That objective data confirms the substantial diversity in claims administration accuracy and efficiency and enabled me to estimate the resulting cost to legitimate claimants. That data demonstrates that selecting claims administrators through price dominant auctions, like those once – but no longer – used to select lead class counsel, have caused, and will continue to cause, legitimate claimants to suffer substantial financial harm: They will recover hundreds of millions of dollars less than they should and they will wait longer than they should to do so.

Introduction

For the last 25 years of my legal career, my practice has concentrated on prosecuting class actions and managing their settlement. At BLB&G, I selected and retained claims administrators and oversaw their administrations of the settlements of dozens of securities class actions, including some of the largest and most complex in U.S. history; at GCG, I advised and presented continuing legal education courses to class counsel throughout the U.S. and I successfully advocated for judicial approval of thousands of claims determinations; and at FRS, I've addressed in connection with managing claims in dozens of direct and indirect purchaser antitrust class action settlements all manner of claims processing and plan of distribution issues. Throughout those diverse careers, each of which focused on class action settlements, I have consistently found that, among claims administrators, there were and still are substantial differences in the accuracy and efficiency of their claims processing services. From my standpoint, higher quality claims administrators perform more accurate administrations, complete them more quickly, and require less oversight and class counsel intervention than do their lower cost competitors. And that experience is not mine alone: Colleagues who also have spent much of their careers practicing in the settlement management trenches and others who practice at claims administrators and at class action claims consultants, have had similar experience. Nevertheless, I've consistently heard from lawyers and judges that claims administrators are fungible because their services are non-distinguishable and straightforward, and, therefore, that it was not "worth it" to the class to pay more for what those lawyers and judges perceived to be non-existent "better" service.[1]

> "Established economic theory … explains the financial cost to legitimate claimants that has resulted, and will continue to result, from using auctions to select claims administrators from among qualitatively diverse bidders."

The opinion among class counsel and courts persists notwithstanding ample publicly available examples of inferior claims administration and its adverse consequences on affected class members. For example, the claims administration of the settlements obtained in the *Freight Forwarders* direct purchaser antitrust class action, which involved 23 settlements that totaled >$384.6 million,[2] included a virtual "kitchen sick" of administrator miscues – the distribution eventually occurred 3½ years after the twice-extended claim filing deadline – and thus offers real rather than theoretical examples of inferior claims processing and the adverse effects that it had not only legitimate claimants but also on class counsel and the court. Class counsel filed their distribution motion on July 28, 2017, almost two years after the last claims filing deadline.[3] Beginning on August 4, 2017, however,

95 legitimate claimants filed with the court formal objections to the claims administrator's determination of their distribution amounts.[4] As a result of the substantial claims administration errors that those objections brought to light, on August 18, 2017 – just 21 days after it was filed – class counsel were compelled to withdraw their distribution motion.[5] Because of the significance, both in the materiality of its errors and in the volume of affected legitimate claimants, the claims administrator was forced to conduct a detailed audit of all claims with payments >$250,000.[6] That audit then had to be expanded to encompass proposed awards >$150,000, and included as well claims under that lower threshold that, as a result of the claims administrator's recalculations, would receive substantially increased distributions.[7] The claims administrator's expanded review identified widespread issues the correction of which resulted in affected claimants' estimated awards being reduced by $121 million, and, therefore, caused a corresponding increase in the expected pro rata distribution to most other claimants.[8] Finally, on January 28, 2019 – 18 months after the original distribution motion was filed and almost 3½ years after the last claims deadline – class counsel's renewed motion was filed.[9]

> "As a direct result of inferior claims administrations performed by claims administrators selected based primarily on their low bids, "legitimate claimants" ... have suffered substantial financial harm and will continue to do so."

While not every administration is as fraught with mistakes as was *Freight Forwarders*, there are other publicly available examples (the substantial majority of claims administration miscues are addressed without the need for public disclosure) of inferior claims administration, including fraudulent distribution payments,[10] failing to process valid and timely proofs of claim,[11] and incorrectly rejecting or erroneously reducing distributions.[12] And beyond the errors themselves, all of those situations either substantially delayed or otherwise encumbered distributions to legitimate claimants, and unnecessarily exposed class counsel to unwarranted judicial and client scrutiny and criticism, as well as, in at least one instance, liability. Nevertheless, and notwithstanding the importance of conducting accurate settlement administrations that enable distributions to legitimate claimants to be conducted as soon as practicable,[13] class counsel and courts were not disabused of their deep-seeded conviction that each claims administrator was equally likely to conduct accurate and efficient claims processing.

But now, Congress and the Supreme Court, by codifying in the 2018 Amendments the importance of accurate claims administration, have weighed in.[14] Even if class counsel were to continue their approach to claims administrator selection, therefore, it is increasingly likely that courts, either *sua sponte* or as a result of objections that have become *de rigueur*, will increase their scrutiny of the results of claims processing—that is, its accuracy and expediency. And when they do, they, as I do

below, may rely on scholarly works that, in connection with selecting certain class action lead counsel, explained why auctions were unlikely to provide the most cost-beneficial results for the class and, therefore, likely would lead to recoveries net of legal fees that were materially *less* than those that would have obtained had more expensive but higher quality counsel been selected. As the court in *Mercury Finance* stated:

> [T]he ultimate goal in class action litigation – that is, for the members of the plaintiff class – is to maximize the benefit to the class members if the litigation proves successful (either by way of settlement or through trial), and there can be no doubt that the class is best served by obtaining highly qualified class counsel who are prepared to undertake the representation on a basis that will maximize that recovery (something that necessarily implicates what counsel will charge for their services).[15]

Indeed, the attorneys practicing at any class action plaintiffs' law firm would recoil at the suggestion that their collective abilities are fungible and, therefore, that they are not entitled to a higher fee commensurate with their superior talent. Yet, that is exactly what some courts, mostly under the lead counsel provisions of the Private Securities Litigation Reform Act of 1995, assumed when they imposed auctions for the selection of lead counsel.[16] As a result, lawyers vying for lead counsel appointments – the same lawyers that, once appointed, are responsible for selecting claims administrators – had to overcome the view held by some courts that legal services were interchangeable. They did so, in part, by resorting to economic principles that demonstrate that, when the quality of goods or services is relevant to a buying decision, as is the case in buying legal services—and, as demonstrated below, in buying claims administration services, failing sufficiently to consider the qualitative differences of the providers has for the purchasers adverse financial consequences. The simple axiom to be gleaned from those scholarly works is that more talented lawyers—because they are better educated, more experienced or, simply, just more talented, are more likely than their less-experienced, less qualified or, simply, less talented, competitors to obtain favorable results, which justifies the higher fees they charge. Apropos this point, the *Cendant* court, in providing instructions for the lead counsel auction that it was about to conduct, cautioned all interested parties that "[t]his is not an invitation for cheapness of costs resulting from cheapness of quality."[17] Then, in evaluating the bids submitted, the *Cendant* court declined to appoint the lowest bidder because the court believed that the proposed low bid was unrealistic and thus undermined the likelihood that the low-cost bidder, like low-cost claims administrators, would devote the resources necessary to maximize the class's recovery.[18]

> "The result of a price-dominant selection process, therefore, is widespread inferior administrations and their corresponding financial harm to legitimate claimants."

Fundamental to those economic theories is an articulable difference in the quality of legal services. For those theories persuasively to apply to the selection of claims administrators, therefore, the differences in claims processing accuracy and efficiency must be susceptible of objective measure. Accordingly, I obtained from a sample of 325 settlements that distributed during a four-year period claims administration statistics that are relevant to the analysis of claims administration accuracy and efficiency. I then identified two metrics, one – the proportion of uncured deficient claims to total claims processed – that fairly describes claims administration accuracy, and the other – the average number of claims processed per day during the period between the latest determinable claims filing deadline and the distribution date – that fairly describes claims administration efficiency.[19] The results from comparing to those standards the data that I obtained objectively show that, among the administrators represented in those settlement administrations, there was substantial disparity both in the accuracy and the efficiency of claims processing. For example, the administrator with the highest claims administration accuracy – that is, the administrator with the highest proportion of uncured deficient claims – processed claims on average over 18 times more accurately than did the administrator with the lowest proportion of uncured deficient claims, and that, as a result, legitimate claimants forfeited to ineligible claimants as much as $87 million. Those results also quantitatively demonstrate that accurate claims administration expedited distributions.

> "Had the settlements that were administered by Administrator H been administered by less accurate administrators, legitimate claimants would have forfeited to ineligible claimants an estimated $594 million, or 3.6%, of the $16.6 billion of net settlement funds distributed in those settlements."

Those economic theories also suggest that the retention of claims administrators based on price will adversely affect the entire claims administration business sector, which, in turn, will have undesirable financial consequences for all legitimate claimants. Because all claims administrators know that their selection will be based on their price per claim, their bids must be extremely low.[20] That selection decision, which largely ignores claims processing accuracy and efficiency, necessarily relies upon the belief that each claims administrator has the same fully loaded costs—*i.e.*, that they are similarly diligent and sufficiently capable claims processors.[21] As the data shows, however, that assumption is false: Whether by design—some administrators intentionally provide barebones services, and, therefore, have low direct costs so that their low bids still result in profits; or by virtue of price pressure—because higher quality administrators will eliminate or reduce their services, winning bidders will not equally or sufficiently perform accurate *or* efficient, let alone accurate *and* efficient, claims processing. As a result, even higher quality claims administrators, if they bid at all, will be compelled to reduce their services.

That sector-wide reduction in quality is explained by the "Lemon Model."[22] Under the Lemon Model, which itself is an extension of "the bad drives out the good" premise of Gresham's Law, there is incentive for the sellers of services – here, claims administrators – to attempt to pass off as high-quality services those that are low-quality.[23] As long as claims administrators are selected without sufficient objective consideration of claims processing accuracy and efficiency, therefore, legitimate claimants will suffer because higher quality claims administrators either will decline to participate or will reduce their quality to be on par with low-quality providers. Specifically, when claims processing accuracy and efficiency are not objectively evaluated, the presumption is that each claims administrator provides the same, or "average," quality; that is, in fact, exactly what class counsel and courts believe. The Lemon Model thus predicts that above average quality claims administrators would be driven out of the market or, at minimum, would find themselves at a distinct financial disadvantage relative to inferior quality claims administrators. The result of a price-dominant selection process, therefore, is widespread inferior administrations and their corresponding financial harm to legitimate claimants. In other words, and as Nobel Prize-winning economist Milton Friedman first demonstrated over 45 years ago, "there is no such thing as a free lunch":[24] If a class is not paying for competent and efficient claims administration, it is not getting it.[25]

The balance of this article is presented as follows: I begin by describing, and analogizing to claims administrator selection, the economic theories that explain why, when selecting class counsel from among qualitatively diverse law firms, using price-dominant auctions will not achieve the best results for the class. Based on that theoretical foundation, and because it is based entirely on qualitative distinctions among law firms, I next turn to a statistical evaluation of claims processing accuracy and efficiency. The first step in that analysis is an explanation of the metrics for claims processing accuracy and efficiency that I used as the standards against which to evaluate the claims processing data that I obtained. Next, I describe the sources, quality and parameters of that claims processing data, and then evaluate its robustness and validity. I then present my statistical analyses, first for claims processing accuracy and then for claims processing efficiency. The article then concludes by summarizing those results, which objectively demonstrate that there are substantial and measurable differences in claims administration accuracy and efficiency across administrators, and, therefore, that choosing claims administrators without sufficiently considering objective claims processing accuracy and efficiency data has caused legitimate claimants to lose hundreds of millions of dollars and to wait longer than they should to receive their recoveries.

> "[H]ad Administrator H, rather than the administrators with less accuracy by proportion of uncured deficient claims, distributed all of $28.4 billion, legitimate claimants would have saved as much as $1.01 billion."

Economic Theory Explains Why Using Auctions to Retain Qualitatively Diverse Claims Administrators Harms Legitimate Claimants

Established economic theory suggests that, when selecting from among qualitatively diverse service providers—the scholarly works described in this section apply those theories to the selection of class counsel, the failure adequately to consider objective measures of their quality will result in inferior providers taking advantage of price pressure either to drive out the superior providers or to reduce the overall quality within the affected business sector. Because cheap but inferior providers will then dominate the bid process, the purchasers of those services will suffer financial harm. This eventuality is a variant of what economists call the "Lemon Model,"[26] in which, because of the failure to seek or to consider objective information about quality, buyers of goods or services cannot *ex ante* accurately assess it, here, the likelihood that a claims administrator will maximize recovery for legitimate claimants.

Nobel Prize winning economist George Akerlof studied this phenomenon by focusing on the used car market—a market with buyer uncertainty about quality and in which there is some likelihood that a buyer will purchase a poor-quality car, or "lemon." Because a buyer will not know whether a car is of good or poor quality, that buyer's thought process, as modeled by economists, is a guess that the car is of average quality, and, therefore, that the buyer will be willing to pay for it a price for a car of known average quality at the price for an average quality car. That process separates the used car sellers: sellers with high quality cars will receive too low a price, while those with low quality cars will receive too high a price. Thus, sellers with high quality used cars will not put their cars on the market, which, because then only low-quality cars are sold, leads to a further reduction in "average" quality. In markets with insufficient or ignored information about quality, therefore, providers of poor-quality goods or service drive out the above average and superior providers.[27]

> "If a class is not paying for competent and efficient claims administration, it is not getting it."

Because claims administrators have not been required to provide objective claims processing accuracy and efficiency data, they have been incentivized to pass off as superior claims processing claims processing that is of inferior quality. In connection with the selection of class action lead counsel, commentators explained that, when competitive bidding is used without sufficiently considering the information necessary adequately to evaluate the quality of the desired legal services, the Lemon problem works to reduce the overall quality of those services:

> The inherent difficulty for courts in evaluating firm quality makes it difficult for high quality firms to distinguish themselves so as to justify the higher price they command for their legal services. The knowledge that they cannot compete with lower quality firms on the basis of price may cause high quality firms to drop out of an auction they cannot win, rather than needlessly incur the costs of participation. This creates a potential "lemons" problem, in which lower quality lawyers are disproportionately represented in the pool of bidding firms.[28]

By driving down fees for class action legal services such that high quality law firms may not obtain a market-based profit, courts, rather than reduce the expenses that a class must bear, reduce the quality of the legal services provided:

> [L]ower fees concomitantly reduce the incentive to furnish high-quality legal representation. It is, of course, possible, as a few judges seem to believe, that the high fees earned by some plaintiffs' lawyers mean that room exists for prices to come down toward the firm's opportunity costs without any sacrifice in quality. On the other hand, the risk is that current compensation levels reflect the firm's costs, and that as fees decline in response to increased competition, lead counsel auctions will actually produce systematically lower quality legal representation than was enjoyed by the class before the introduction of auctions.[29]

As concerns claims administrator selection, without the information necessary objectively to measure and evaluate claims processing accuracy and efficiency, the Lemon model predicts that class counsel and courts have implicitly assumed that, like those buyers contemplating the purchase of a used car, each claims administrator's services were of average quality. In addressing analogous price-dominant lead counsel auctions, one commentator aptly noted, with equal application to the selection of claims administrators, that purchasers of legal services should base their decisions on quality as well as price:

> "Among claims administrators, there are substantial differences in accuracy and efficiency."

> Clients in the market for legal services do not choose their lawyer based solely on price. Indeed, the depth of the market for legal services, with its wide variation in billing rates, demonstrates the importance of non-price considerations. As in many markets, lawyer price and quality are often directly related. Those lawyers who offer higher quality legal services are able to command a higher price for their services. Less qualified lawyers charge a lower price. Lawyer quality is an important component of the selection process because a higher quality lawyer maximizes the client's expected recovery by increasing the likelihood

> of recovery, the amount of recovery, or both. Thus, although defendants would presumably favor an auction that relies primarily on price to select plaintiffs' counsel, the interests of the class require the court to consider lawyer quality and to reject an auction procedure that focuses exclusively on price.[30]

Similarly, and as demonstrated below, counsel selecting claims administrators have not considered objective claims processing accuracy and efficiency data that would permit an appropriate cost-benefit evaluation. As explained in addressing the issues caused by using bids to select lead counsel in securities class actions, the only way to assure the greatest recovery for the class was to retain the provider that, as a result of its quality, would obtain the best results:

> "[A]lthough it may appear that selecting low bidding claims administrators will save classes the marginal cost differentials between those low-cost claim administrators and the more expensive but higher quality claims administrators, the opposite is true."

> [Lead counsel p]rocurement decisions, however, necessarily operate along both price and quality continuums. The least expensive provider may seek to cut costs and provide the least quality, while more expensive providers may be more able to both earn a handsome profit and provide a higher-quality work product. Because quality is not uniform across all service providers, it is important to understand better the internal workings of auctions held for the purpose of selecting class counsel. .... .
>
> The fundamental problem is that lead counsel auctions may result in the selection of one of four different types of law firms: low-cost/high-quality, low-cost/low-quality, high-cost/low-quality, or high-cost/high-quality. The agency costs associated with each of the resulting lawyer-client relationships vary accordingly. All things being equal, agency costs are higher for both of the low-quality firms because these firms are by definition either less skilled at or less interested in maximizing the value of the class claim. On the other hand, agency costs are lower for both of the high-quality firms because these firms are by definition more able or more willing to maximize the value of the class claim. Because both quality levels include high-cost and low-cost alternatives, selection of class counsel on the basis of cost alone cannot guarantee high-quality legal services.[31]

Exacerbating the Lemon problem as applied to many categories of class actions is their complexity, and, as a result, the complexity of administering their settlements.[32] Today's securities class action settlements, for example, are far larger on average than those of the pre-PSLRA era,[33] and they involve increasingly complex issuer capital structures and sophisticated fraudulent schemes.[34] As a

result, maximizing the recovery by legitimate claimants requires claims administrators to navigate through a myriad of difficult issues. And even in less complex settlements, their substantial value and large number of potential claimants, as well as the presence of fraudulent and otherwise improperly accepted claims, expose legitimate claimants to substantial delays in receiving their distributions and to significant risk of being deprived of their full pro rata recoveries. This additional complexity confirms that, just as with retaining counsel to prosecute those complex class actions, administering their settlements is not the "one size fits all" proposition necessarily mandated by the "all-in" request for proposal:

> [A]uctions cannot provide the class or judge with the information necessary to select a winning bid. Selection of a winning bid should involve an evaluation of each proposal along both price and quality continuums, particularly because legal services are not fungible, and an informed, organized class might rationally prefer to pay more for better quality services that offer higher expected recoveries. The degree of quality that a particular firm will provide depends, in turn, upon each firm's incentives and cost structure. The bids submitted in lead counsel auctions, as they are currently designed and implemented, however, state only offering *prices* for legal services without providing the necessary information to assess incentives and cost structures. In the absence of such information, lead counsel auctions cannot be expected to replicate the full contractual *agreement* – a combination of price, quality, and performance guarantees – that informed, organized class plaintiffs would have bargained for in arm's-length negotiations.[35]

Nevertheless, the all-in request for proposal, by forcing administrators to "package" all claims-related costs into one "per claim" price, treats them as if they are the same: By requiring bidders to price identically all claims – whether they have one transaction or tens of thousands (or more) transactions; whether they include transactions for one security, product or service or they include transactions for several securities, products or services; and whether they are without any deficiencies or contain multiple deficiencies – when the costs of processing simple claims and complete and accurate claims, on the one hand, are mere fractions of the costs involved in accurately processing complex claims and deficient claims, on the other. The negative consequence that results from unrealistic pricing proposals also was identified in connection with selecting lead counsel based primarily on a low bid rather than on a process that adequately factored in quality:

> The winning bidder may also find that unanticipated circumstances alter the potential profitability of the bid and the incentives for class counsel to perform. For example, a firm which is unduly optimistic or simply mistaken about the cost of litigating a class claim may successfully underbid a firm which makes a more realistic assessment of the

> costs. In such a case, the unduly optimistic firm may later discover that it cannot profitably carry out its intended commitment to the class and may resort to negotiating an early and low settlement.[36]

Because the all-in request for proposal compels competing administrators to present the lowest "all-in" per claim price, an administrator's pricing for all claims will at best be based on the lowest common denominator—that is, the effort required for the administrator to process simple, complete and accurate claims, thereby unrealistically underpricing the complex and deficient claims, and providing financial incentive for the low bid administrator to give those latter claims short shrift. This counterintuitive and perverse incentive also existed in connection with lead counsel auctions:

> It is equally plausible, however, for a firm to decide in advance that it will make a low-level commitment such that it will incur few costs. This decision will enable the firm to bid low such that more reputable firms seeking to provide more reliable service are again forced to lower their bids to compete. In this scenario, "bad" firms with intentions to disserve the class can use the auction mechanism to change the behavior of "good" firms to the point at which their bids and contractual performance become identical to those of "bad" firms.[37]

The all-in request for proposal regime thus perversely distorts the financial incentives of a low-cost administrator to be at odds with those of legitimate claimants: By encouraging administrators to propose the lowest price per claim, the all-in proposal format encourages them either to eliminate or substantially to reduce essential claims processing procedures, which, also as demonstrated below, results in the distribution of settlement recoveries to ineligible claimants thereby substantially diluting recoveries by legitimate claimants. Under the "tried and true" TINSTAAFL economic maxim, therefore, a low-cost administrator will not provide to the class the same services that will be provided by a higher quality, and, thus, higher cost, administrator with the higher direct costs associated with providing the services necessary diligently to process claims. As identified in connection with lead counsel auctions, this situation will continuously impose on class members the costs of inferior services:

> "Because claims administrators have not been required to provide objective claims processing accuracy and efficiency data, they have been incentivized to pass off as superior claims processing claims processing that is of inferior quality."

> [T]here also exists a credible argument that higher bids reflect an increased willingness to fight for the class and/or a more realistic assessment of the costs of litigating the class claim. Indeed, the principal cost of allocating the position of lead counsel through a low-cost

> provider bidding process is that certain firms that underestimate the value of a class claim, that underestimate the costs of litigating the claim, or that intend to maximize their own interests by selling out the class will tend to be systematically rewarded.[38]

All-in requests for proposals encourage so-called "low cost" administrators to set the bar for acceptable claims as low as possible—that is, to take the path of least resistance by simply paying an unreasonably high proportion of questionable claims rather than subjecting those claims to the necessary (and more costly) diligence required to evaluate whether or not they are eligible claims, and then properly to address the potentially deficient claims that, before deeming them acceptable, require additional scrutiny. A low-cost administrator that is improperly motivated to reduce costs at the expense of accuracy will exclude essential services, and, as a result, will accept claims that it should not. This incentive to curtail services and thus shortchange the class also existed when lead counsel was selected via a bidding process:

> As the downward competitive pressure on attorneys' fees grows, the likelihood that the class will obtain quality legal representation decreases because lawyers charging lower fees have less incentive to perform than do lawyers charging higher fees. Law firms submitting low bids, in fact, have more incentive to reduce their commitment, hours, and costs by negotiating a quick settlement such that the lawyer can earn returns on investment in excess of those that could be earned by working on other litigation.[39]

As with retaining claims administrators based primarily on low bids, selecting lead counsel based on low bids results in the class bearing substantially higher costs than they would have borne had a higher quality law firm with higher been retained:

> The tradeoff between the class plaintiffs' share of the recovery and class counsel's effort in prosecuting the litigation means that an informed plaintiffs' class would not systematically choose the low bidder as lead counsel. Indeed, high bidders would be more willing to make extended commitments to the class for the purpose of negotiating a higher settlement. … But high bidders are constrained by the fact that if they bid high, they will lose the auction because "[a] firm that intends to perform only under the most favorable cost conditions can underbid a firm offering more reliable performance." Firms that would prefer to offer more reliable performance are therefore forced to compete with the lowest common denominator by reducing their bids and, concomitantly, the commitment that they can profitably make to the class. In the end, even those firms that would have been willing to make greater efforts to maximize the value of the class claim are reduced to selling out the class by arranging early and low settlements.[40]

Because claims administrators have not been required to provide sufficient objective claims processing accuracy and efficiency data, all administrators were and are necessarily treated as possessing sufficient quality. As a result, the financial interests of less diligent and less capable administrators, like those of less talented law firms, directly conflict with the financial interests of the class members they serve. This conundrum – that the financial interests of low quality/low bid providers conflict with those of the class – also existed in connection with lead counsel auctions. The solution posed there – as this article proposes for claims administrator selection – is to require bidders to provide objective data and then to identify comprehensive criteria against which to evaluate it:

> Courts utilizing the auction approach for selecting class counsel have attempted to deal with this problem by subjectively evaluating the quality of a firm prior to the selection of a winning bid, and also by monitoring class counsel's performance during the litigation. The more effective quality standards include: (i) evidence that a firm has evaluated the case, and the range and probability of recovery, and has premised the bid on that evaluation; (ii) evidence of an ability and willingness to see the case through to recovery, such as posting a completion bond or escrowing an amount that would be forfeited in the event class counsel fails to perform; (iii) evidence of a willingness and financial ability to guarantee a minimal level of recovery for the class; (iv) evidence of financial resources or insurance coverage adequate to compensate the class in the event of malpractice; and (v) evidence of a concern about reputation.
>
> Together, these quality criteria go a long way toward protecting the class against self-interested or incompetent lawyers because they signal a lawyer's willingness and ability to commit time and money to litigating the class claim. ...[41]

The scholarly works described above amply demonstrate that selecting class counsel based on bids without sufficiently considering objective qualitative information has harmful effects on class members. Because, as set forth below, there are measurable qualitative differences in claims processing accuracy and efficiency, these same theories apply with equal force to the selection of claims administrators.

Claims Processing Accuracy and Efficiency Metrics

The economic theories examined above depend upon the existence of measurable qualitative differences among potential class counsel law firms. For those theories to apply to the selection of claims administrators, then, there must be qualitative differences among claims administrators, and those differences must be objectively measurable. That objective evaluation requires, in addition to sufficient claims processing data for statistically reliable analyses to be performed, which will be addressed in the next section, a metric that fairly describes claim processing accuracy, and another that does the same for claim processing efficiency.

Because the primary function of a claims administrator is to maximize the number of legitimate claimants, it is axiomatic that they must correspondingly reject ineligible claims. I identified a metric, the data for which was likely to be generally obtainable and that may be applied across settlement administrations, to measure the degree to which a claims administrator, by properly rejecting rather than accepting ineligible claims, maximized payments to legitimate claimants. That metric is the proportion of uncured deficient claims—i.e., the number of proofs of claim that are deemed to have one or more curable deficiencies but that ultimately are rejected because those deficiencies were not cured (expressed as a percentage of total claims received in that administration). As explained below, the higher this percentage, the more accurate the claims administrator's claims processing, which results in lower indirect costs to, or wealth transfers by, legitimate claimants. To measure claims administrators' claims processing efficiency, the metric that I identified is the average number of claims processed per day for the period between the claims filing deadline and the date of the distribution. These two metrics are explained below.

> "The Lemon Model thus predicts that above average quality claims administrators would be driven out of the market or, at minimum, would find themselves at a distinct financial disadvantage relative to inferior quality claims administrators."

The Claims Processing Accuracy Metric: Proportion of Uncured Deficient Claims

As explained below, I focused on uncured deficient claims because processing deficient claims – that is, properly identifying proofs of claim that are deficient rather than acceptable or rejectable, and then processing them to their final determination either as cured or rejected – is the most expensive component of claims processing, and, therefore, it is the aspect of claims processing that a low-cost

claims administrator is most likely to shortchange. When parameters for deficient claims are properly established and claims are properly processed, ineligible claims are more likely to be identified so that, unless they are satisfactorily cured, they are not paid.[42]

Some rejected claims are easily identified because, for example, none of the transactions they contain were conducted during the class period; none of the transactions that they include are eligible, all the transactions they include taken together do not calculate to a recognized loss, or they are duplicates of other claims. I refer to those claims as "rejectable claims" because they cannot be cured: No amount of additional documentation or explanation will cause purchases conducted before the beginning or after the end of the class period to have been conducted during the class period, to cause ineligible transactions to become eligible, to cause included transactions to compute to a recognized loss, or to cause a duplicate claim not to be duplicate. These conditions are thus easier to spot than the deficient conditions described in the next paragraph. And, because each of them is rejectable on its face, they do not require substantial resources to address: Rejectable claims rarely require any communication with a claimant beyond notification of the defects identified and that, as a result, the claim will be rejected.

Other conditions of non-compliance with judicial requirements are harder to recognize and more expensive to sort out, including, for example, with respect to securities class actions claims that do not balance or that include transaction prices that are outside the range of prices at which the security traded on the dates of the transactions, and, more generally, claims that are insufficiently or improperly documented, or that include documentation that is inconsistent with the information on the claim. I refer to these and similar categories of claims as "deficient claims," the detection of which requires greater examination of claim forms and supporting documentation. And unlike rejectable claims, a claimant, by providing additional information or documentation, may cure deficient claims. Accordingly, a deficient claim must be identified, which requires an administrator to establish suitable protocols, and, based on the tradeoff of the costs and benefits of each administration, to establish appropriate case-specific standards and tolerances for determining when information present in a claim is acceptable and when it is not. Once a claim is identified as deficient, all deficient conditions must be sufficiently explained to the claimant through written correspondence; that correspondence often necessitates an increase in claims administrator labor to respond to inquiring claimants. And when claimants respond to deficiency

> "[T]he administrator in the sample that had the highest proportion of uncured deficient claims processed claims on average over 18 times more accurately – that is, appropriately rejected a higher proportion of deficient claims that were not cured – than did … the administrator that had the lowest proportion of uncured deficient claims … ."

correspondence with additional documentation and information, all newly submitted data must be processed and evaluated to determine whether any or all identified deficient conditions have been cured. Because new "cure" submissions may be inadequate or may cause additional deficient conditions to exist, the administrator must engage in additional communications with claimants, thus adding additional processing and evaluation cycles. And as the number of deficient claims increases, so too will the number of claimants that may request judicial review of the claims administrator's determinations, which, in turn, results in increased costs as an administrator attempts to communicate with those objecting claimants. And for those objecting claimants that continue to pursue their requests for judicial review, the administrator must prepare submissions to the court so that a final resolution may be made.

As the foregoing description demonstrates, processing deficient claims is the most time consuming and expensive facet of an accurate class action settlement administration, which is why deficiency processing procedures are the most prone to fall victim to shortcuts and elimination all together: An administrator seeking to reduce its costs so that it may provide low per claim pricing is likely intentionally to lower its standards for claim acceptance and to limit its procedures for claim evaluation.[43] Whether this low standard is based on an explicit strategy or the unwillingness to invest in sufficient labor and other resources, it would result in improperly accepting deficient claims either in the first instance or, although properly identifying them as deficient, improperly deeming them cured. This likelihood is enhanced by the fact that, because claimants that receive a distribution are far less inclined to object to its amount than are claimants who receive nothing, improperly accepting deficient claims is likely to escape notice. Accordingly, the proportion of uncured deficient claims to total claims processed for each settlement in the sample is the best proxy for the effort put forth by the administrator to identify questionable claims and to resolve as many of them as possible.

The Claims Processing Efficiency Metric: Weighted Average Claims Processed Per Day

In addition to receiving the full measure of their recoveries without having them diminished by improper payments to ineligible claimants, it is in the best interests of legitimate claimants to receive those recoveries as quickly as possible. Measuring an administrator's claim processing efficiency, however, is not as simple as counting the number of days it takes an administrator to complete claim processing: While it may seem that the appropriate measurement would be the length of time between the date claim forms are sent to class

> "Legitimate claimants received their distributions from more accurate claims administrators twice as fast as they did from less accurate administrators."

members and the date on which the corresponding distribution is conducted, that statistic is not the best measure of efficiency. First, the length of a claim filing period – the amount of time between the date claim forms are disseminated and the claim filing deadline – is controlled by class counsel and the court, not by the administrator. And, notwithstanding the length of the claim filing period, it is customary for a large proportion of claims relative to the total number of claims filed to be submitted at or around the claim filing deadline, which is why most claim processing does not begin until after the claim filing deadline has passed. Accordingly, the length of the claim filing period is not a proper measure of claims processing efficiency.

Those same reasons establish that the length of time most relevant to claim processing efficiency begins for each settlement administration on the latest determinable claim filing deadline and ends on the date on which the corresponding distribution was conducted. For a meaningful and comparable measure, however, that timeframe must be weighted to account for the volume of claims processed because, all else constant, it takes less time to process 1,000 claims than it does to process 100,000 claims. Accordingly, the metric that I identified that best describes claim processing efficiency for each settlement administration is the percentage derived by dividing the total number of claims processed by the number of days during the period between the latest determinable claim filing deadline and the distribution date.

Data Obtained Concerning Claims Administration Accuracy and Efficiency

Statistical data about class action settlement administrations are very hard to come by: There is no comprehensive database that, for all class actions, obtains, stores and makes publicly available any information, let alone data concerning claims administration accuracy and efficiency.[44] To overcome that data vacuum required a multistep approach. First, I identified a discernable subset of class action settlements for which claims administrations and corresponding distributions were conducted during a timeframe long enough to provide a sample size likely to yield meaningful results. Next, information about each settlement, such as case number and jurisdiction; settlement amounts; numbers of claims processed, accepted and rejected, as well as the reasons therefor; claims deadlines and distribution dates, were obtained for as many of those settlements as possible. The resulting population had to be sufficiently robust to enable a statistically reliable evaluation of claim processing accuracy and efficiency.

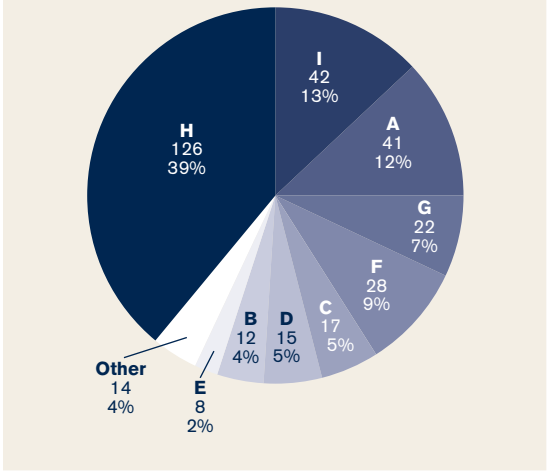
Although there is no one source for all class actions, there is one for a specific subset of them. After the promulgation of the PSLRA, much attention has been paid to federal securities class actions and their settlements, including by ISS Securities Class Action Services ("ISS").[45] Although this data is entirely from the administrations of securities class action settlements, there is no reason to believe that claims administrators exercise different levels of accuracy and efficiency based on the nature of the claims alleged in the class actions that they administer. It would strain credulity to suggest that fundamental aspects of an administrator's business model, such as the number and qualifications of its employees and the nature and execution of its processes and procedures, will yield for the administrations of securities class action settlements qualitative results that are measurably different than those yielded for its administrations of similarly complex antitrust and other class action settlements. I believe that it is appropriate, therefore, to rely upon the results of my analyses to draw conclusions concerning claims administration accuracy and efficiency for settlement administrations that involve a claim process.

> "[H]ad the more accurate administrators by proportion of uncured deficient claims been replaced by the least accurate administrator for all 325 settlements, legitimate claimants as a group would have paid to ineligible claimants as much as $1.7 billion, or 6.0%, of the $28.4 billion distributed."

In 2011, in connection with a related project, I generated from the ISS database a list of 608 securities class action settlements and SEC "fair fund" distributions that were conducted from August 2, 2006

Figure 1

Distributions by Administrator



through September 15, 2010. As described below, I relied on data from the settlements on that list for my analyses because that claims processing data was comprehensive and robust and, therefore, would enable meaningful analyses of differences and similarities in accuracy and efficiency among the represented claims administrators. And while there has been since then considerable constriction in the claims administration market,[46] as well as the entry of new participants, the identities of the administrators is irrelevant to whether diversity in claims administration accuracy and efficiency causes avoidable losses to legitimate claimants. In other words, the goal of my analyses is not to identify the most and least accurate and efficient administrators. Rather, my analyses provide a framework for objectively measuring claims administrators both in connection with their selection and with evaluating the results of the administrations that they conduct; those analyses also provide a standard against which current claims administrations may be compared. That latter benefit is, in my view, particularly significant: The data that I relied upon predates the reduced dispersion of experienced claims administration professionals and competitive claims administration options available in the current far-more-constricted administration market, and, therefore, that sample data, because it is unbiased by the reduction in participants, is more informative than would be data collected from administrations conducted by far fewer administrators. With fewer participants now dominating the market, it may be advisable to pay more rather than less attention to claims administration accuracy and efficiency; analyses based on a more dispersed market provide results against which those latter settlement administrations may be measured.

After analyzing that ISS listing, I adjusted it to eliminate 100 administrations: 68 were not first distributions and 32 were conducted without a claims process.[47] The result was a total population of 508 relevant administrations. For each of them, I collected from ISS its case name and number; administrator; jurisdiction; claim deadline; distribution date; settlement amount; and attorneys' fees and litigation expenses awarded or requested.[48] I then attempted to obtain for them the data relevant to claims processing, including total claims processed, accepted and rejected; total uncured deficient claims; and total rejectable claims. I was able to obtain that data for 325 of

them. For 176, no distribution declarations or affidavits were filed. Although such declarations are common in connection with distributions, some final approval orders do not require distribution motions. That data also could not be collected for another 7 administrations either because the court clerk could not locate the affidavit or declaration or because the pleading did not include the data.[49] The result was a sample of 325 administrations conducted by 16 administrators during the sample period.[50] Figure 1 shows the number and proportion of distributions for each of the 9 administrators that conducted five or more distributions, as well as those reported together in the "Other" category.

Robustness and Validity of the Sample Results

To rely upon the data from the 325 administrations to draw meaningful and supportable conclusions about claims processing accuracy and efficiency in the 508 administrations conducted during the sample period, I had to determine whether the 325-administration sample is sufficiently robust and representative of that 508-administration population. I was concerned that, because 183 administrations had to be excluded from my analyses, the sample may be biased in some way (*e.g.*, by including relatively more large or small distributions). However, if the sample is representative of the population, the results I observe may be used to draw meaningful inferences about the entire population. As described below, the 325-administration sample is, with respect to distribution size, robust and representative of the 508 administrations.

The first step was to evaluate the proportion of settlement recovery dollars included in the 325-administration sample, both for each administrator and for the entire group. Comparing the settlement dollars for each administrator represented in the sample to the total settlement dollars for each such administrator in the population, the sample accounts for between 26% (for Administrator I) and 100% (for Administrator H) of the total settlement dollars they administered, with the sample comprising 66% of the total settlement dollars accounted for by all 508 administrations. Because the percentage of total settlement dollars administered by Administrator I was substantially less than the percentage of settlement dollars for any of the other administrators in the sample (*i.e.*, the next lowest percentage was 80%), and substantially less than the 66% for the group as a whole, I did not include any results for Administrator I.[51]

Looking at the settlement dollars accounted for in the 283 settlements conducted by administrators other than Administrator I with at least 5 distributions conducted during the sample period, a very substantial representation of the population is seen, with coverage ranging between 80% (for Administrator D) and 100% (for Administrator H); the mean coverage for this subset of administrators is over 97%, and the median coverage is between 95% and 96% of the settlement dollars they administered. This sub-sample comprised 94% of the total settlement dollars accounted for by all 343 administrations in the population without Administrator I. This is a large proportion of the settlement dollars distributed during the sample period.

Certain descriptive statistics of the net settlement funds also were calculated to compare the features of the distribution – in this section "distribution" refers to the frequency of each dollar value associated with the various groupings of administrations (*i.e.*, proportion of large versus small, etc.) – of the net settlement funds for the 325 administrations in the sample to the distribution of the net settlement funds for the 508 administrations in the population.[52] What is striking about these

descriptive statistics for the population and the sample is their similarity. The statistical properties of the distribution of net settlement funds for the entire population of 508 administrations are observed to be almost identical to the statistical properties observed in the sample of 325 administrations. First, the means, or average, dollar values, of the 508 administrations were compared to those of the sample. The $75.5 million mean for the net settlement funds for the 508 administrations is, from a statistical standpoint, the same as the $75.42 million mean for the 325 administrations in the sample. Not only are the means similar, but each of the other measures describing the central tendency and dispersions of the administrations (*e.g.*, medians, percentiles, lows and highs, etc.) also are similar. For example, the median net settlement fund, or that one administration that, with the net settlement funds listed in descending dollar value order, exactly splits the sample in half – separating the largest 50% from the smallest 50% of the administrations – is $6.27 million for both the entire population and the sample. And when the 25th percentile of the net settlement funds for the entire population, or the dollar value of that distribution of administrations that splits the largest 75% from the smallest 25% of the administrations, which is $2.32 million, was compared to the $1.95 million 25th percentile of the sample, the difference is only $0.37 million; from a statistical standpoint, this difference is not material.[53]

Based on the statistical properties of the distributions using the descriptive measures of the dollar value of the net settlement funds, it may be concluded that the 325-administration sample is representative of all 508 distributions that were conducted during the sample period.[54]

Statistical Analyses

Summary

My analyses show that, among the claims administrators represented in the 325-administration sample, there was a substantial disparity in claims processing accuracy and efficiency. Those analyses also show that, because class action settlements almost always provide recoveries that are less than the class's total compensable damages,[55] and because in non-reversionary common fund settlements, by far the most prevalent form of monetary relief provided by the settlements of securities and antitrust class actions, allocating funds among approved claimants is a "zero-sum game,"[56] and, therefore, every dollar improperly distributed to ineligible claimants comes from legitimate claimants,[57] inferior claims processing accuracy caused legitimate claimants improperly to transfer wealth to ineligible claimants.

For example, Administrator H, the administrator in the sample that had the highest proportion of uncured deficient claims, processed claims on average over 18 times more accurately – that is, appropriately rejected a higher proportion of deficient claims that were not cured – than did Administrator D, the administrator that had the lowest proportion of uncured deficient claims, and 2.38 times more accurately on average than did all the other administrators combined. Had the settlements that were administered by Administrator H been administered by less accurate administrators, legitimate claimants would have forfeited to ineligible claimants an estimated $594 million, or 3.6%, of the $16.6 billion of net settlement funds distributed in those settlements; had the more accurate administrators by proportion of uncured deficient claims been replaced by the least accurate administrator for all 325 settlements, legitimate claimants as a group would have paid to ineligible claimants as much as $1.7 billion, or 6.0%, of the $28.4 billion distributed; and had Administrator H, rather than the administrators with less accuracy by proportion of uncured deficient claims, distributed all of $28.4 billion, legitimate claimants would have saved as much as $1.01 billion. And accurate claims processing did not delay distributions; rather, the opposite result is obtained: Legitimate claimants received their distributions from more accurate claims administrators twice as fast as they did from less accurate administrators.

As presented in more detail below, there is clear empirical evidence of substantial diversity in claims administrator accuracy and efficiency. Accordingly, the economic theories described above that explain the harm to the class imposed by selecting class counsel without sufficiently considering quality, are equally applicable to the selection of claims administrators. And as also presented in detail below, that objectively documented diversity in claims processing accuracy causes a substantial financial loss to legitimate claimants. The conclusion, as it was in connection with class counsel

selection, is that, by selecting and approving claims administrators via price-dominant bidding processes, the recoveries of legitimate claimants are not being maximized. The remedy is to compel claims administrators to provide the claims processing accuracy and efficiency data described below, and then to perform customary cost-benefit analyses to appropriately evaluate that data together with the corresponding cost proposals.

Claims Processing Accuracy

I used the sample of 325 administrations to compare the metrics for each of the administrators to each other and to the aggregate results for all administrators. I then rely upon those claims processing accuracy results to estimate the substantial financial consequences to legitimate claimants caused by inferior claims processing.

Qualitative Claims Processing Results

As explained above, it is substantially more difficult and costly for an administrator accurately to process deficient claims than it is to process rejectable claims or acceptable claims. As a result, my analyses focus on deficient claims. **Table 1** and **Table 2** present two examples, each based on a hypothetical 1,000-claim administration, that demonstrate that considering only one aspect of claims processing without appropriate context distorts the view of processing accuracy. **Table 1** shows why considering only the proportion of uncured deficient claims to total rejected claims is not an accurate measure of claims processing accuracy:

Table 1

Administrator	Accepted Claims	Rejected Claims			Total Claims Processed	Uncured Deficient Claims as a Percentage of	
		Rejectable Claims	Uncured Deficient Claims	Total Rejected Claims		Total Rejected Claims	Total Claims Processed
X	800	100	100	200	1,000	50%	10%
Y	600	200	200	400	1,000	50%	20%

Because each administrator rejected uncured deficient claims at the same 50% rate of total rejected claims, they would appear to be equally accurate. But when their results are compared to total claims processed, which then also considers accepted claims, Administrator Y's 20% is twice as accurate as

Administrator X's 10%. Comparing uncured deficient claims solely to total rejected claims thus does not provide a meaningful measurement of claims processing accuracy.

Table 2 shows why comparing total rejected claims solely to total claims processed also is not an accurate measure of claims processing accuracy:

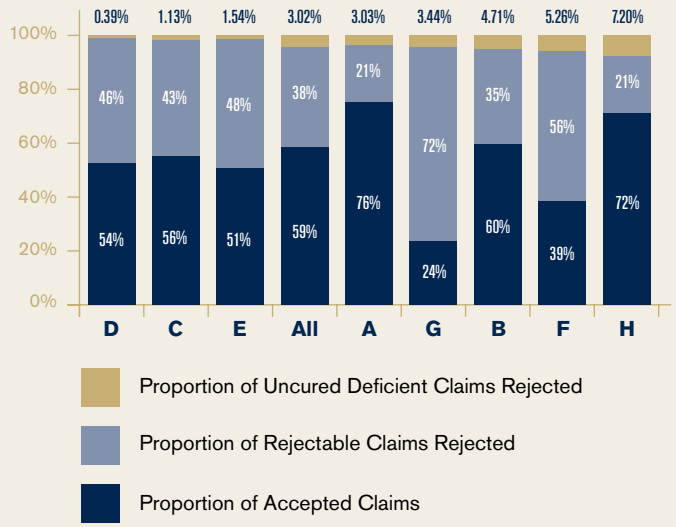
Table 2

Administrator	Accepted Claims	Rejected Claims			Total Claims Processed	Total Rejected Claims as a % of Total Claims Processed	Uncured Deficient Claims as a % of Total Claims Processed
		Rejectable Claims	Uncured Deficient Claims	Total Rejected Claims			
X	200	600	200	800	1,000	80%	20%
Y	200	200	600	800	1,000	80%	60%

Because each administrator rejected 80% of total claims processed, they again appear equally accurate. But when only uncured deficient claims are compared to total claims processed, Administrator Y's 60% is three times more accurate than Administrator X's 20%. Comparing total rejected claims to total claims processed thus also does not yield a meaningful measure of claims processing accuracy.

Figure 2

Rejectable, Uncured Deficient & Accepted Claims As a Proportion of Total Claims Processed



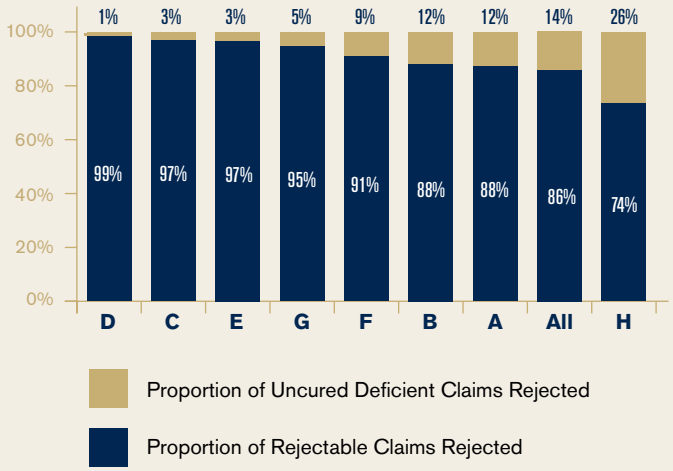
I now turn to the actual results provided by our sample.

The full claims processing picture is presented in **Figure 2**, which displays for each administrator and for the group excluding Administrator H (to enable a comparison of Administrator H to the group of other administrators) the proportions that accepted claims, rejectable claims and uncured deficient claims comprised of total

claims processed. **Figure 2** shows the potential drawbacks to measuring claims processing accuracy by comparing total rejected claims to total claims processed, without also distinguishing rejectable claims from uncured deficient claims, and by failing to consider accepted claims. Based solely on the proportion of rejectable claims rejected, every administrator in the sample but Administrator A rejected a greater proportion of claims than did Administrator H, and, therefore, the conclusion may have been drawn that Administrator H was a far less accurate claims processor than the others. But when the entire claims processing picture is considered, the opposite is shown: When Administrator H conducted an administration, because it rejected on average a greater proportion of uncured deficient claims than did any other administrator, legitimate claimants were less likely to have their recoveries improperly diminished by payments to ineligible claimants. And that claims processing accuracy was not accompanied by legitimate claimants having been wrongfully rejected: Because Administrator H accepted on average more claims than did any other administrator except Administrator A, and because Administrator H rejected on average the smallest proportion of rejectable claims—that is, Administrator H, rather than misidentifying deficient claims as rejectable, allowed those potentially legitimate claimants an opportunity to cure, Administrator H provided the greatest class member participation.

Figure 3

Rejectable Claims and Uncured Deficient Claims Each as a Proportion of Total Claims Processed



To further inform whether there is qualitative diversity among claims administrators, the proportion of uncured deficient claims was compared to total claims rejected. As presented in **Figure 3**, the majority of total rejected claims are rejectable claims. But here, too, the range of results is substantial: At one end is Administrator H, with uncured deficient claims comprising on average 26% of total claims rejected; on the other end is Administrator D, with uncured deficient claims comprising

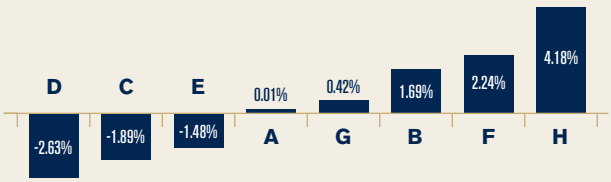
on average just 1% of total claims rejected. In other words, 99% of the claims that Administrator D rejected received no additional scrutiny. As explained in the next section, inferior claims processing translates into hundreds of millions of dollars lost by legitimate claimants.

Comparison to Benchmarks

To facilitate the estimation of financial harm to legitimate claimants caused by inferior claims processing, I derived two sector-wide benchmarks against which the qualitative results for each administrator in my sample could be evaluated.

Figure 4

"Excess" Proportion of Uncured Deficient Claims Relative to Sector Benchmark



The Sector Average Benchmark

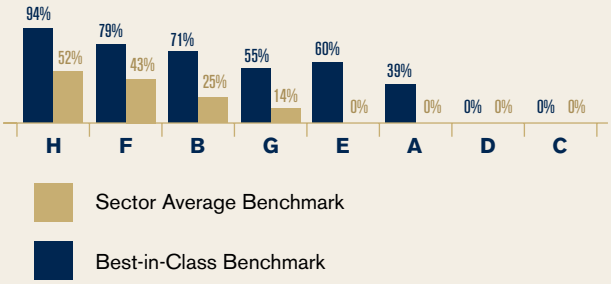
The "Sector Average Benchmark" is the **3.02**% of uncured deficient claims that, as set forth above in **Figure 2**, all administrators other than Administrator H rejected. **Figure 4** displays each administrator's "excess" proportion of uncured deficient claims relative to benchmark—that is, the amount by which each administrator's results were above or below that measure. The results for five administrators – Administrators H, F, B, G and A – were better than that benchmark, while the results for Administrators E, C and D were not. Demonstrating substantial qualitative diversity, the absolute value of the difference in the "excess" proportion of uncured deficient claims between Administrator H, the administrator with the highest excess proportion of uncured deficient claims, and Administrator D, the administrator with the lowest excess proportion of uncured deficient claims, is more than 2.25 times the amount of the Sector Average Benchmark itself. There is thus substantial difference in claims processing accuracy from one end of the spectrum to the other.

The Best-in-Class Benchmark

At **7.20**%, Administrator H's average proportion of uncured deficient claims was the best among all administrators in the sample. Accordingly, I used that datapoint as the upper limit of claims

Figure 5

Proportion of Uncured Deficient Claims Compared to Benchmarks



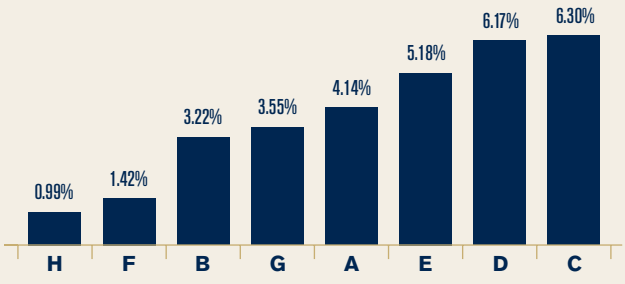
processing accuracy (the "Best-in-Class Benchmark"). **Figure 5** presents, as a percentage of the administrations they conducted, how often each administrator's proportion of uncured deficient claims met or exceeded the Sector Average Benchmark and the Best-in-Class Benchmark. The results of those comparisons also show substantial disparity among administrators. Five administrators met or exceeded the 3.02% Sector Average Benchmark more than 50% of the time, while Administrators D and C did not meet that benchmark at all. In contrast, 94% of Administrator H's administrations met or exceeded the Sector Average Benchmark, and only Administrator H met the 7.20% Best-in-Class Benchmark in at least 50% of its administrations, and it did so in 21% more administrations than did the next best administrator, Administrator F. Four administrators – Administrators D, A, E and C – failed to meet the Best-in-Class Benchmark in any of their administrations.

Percentage of Estimated Net Recoveries Lost by Legitimate Claimants

Because the Best-in-Class Benchmark was achievable, it is fair to use it as the standard for determining whether, for any administration included in the sample, there was an excess transfer of wealth from legitimate claimants to ineligible claimants.[58] In other words, because perfect claims processing is not possible, there are unavoidable wealth transfers in every settlement administration. The point is to establish a minimum standard: Any settlement that had a proportion of uncured deficient claims that was equal to or better than that standard, did not result in an excess wealth transfer; in contrast, any settlement that had a proportion of uncured deficient claims that was worse than that benchmark did result in an excessive wealth transfer from legitimate claimants to ineligible claimants. For each administration with uncured deficient claims as a proportion of total claims processed that is less than the Best-in-Class Benchmark, I calculated that difference. That excess was then multiplied by the corresponding net settlement fund. This amount for each administration represents the settlement recovery that, although it belonged to legitimate claimants, was distributed to ineligible claimants. Because the size of the administrations differed substantially, the wealth transfers were aggregated for each administrator and then divided by the total of the net settlement funds it administered. The result is each administrator's average percentage of indirect costs. The results are shown in **Figure 6.** Most of the administrators show relatively high indirect costs—that is, a substantial excess transfer of wealth from legitimate claimants. Indirect costs as a percentage of the net settlement funds ranged from a low of 0.99% for Administrator H to a high of 6.30% for Administrator C. These results show the materiality of the net settlement funds distributed to ineligible claimants, as well as the substantial amount of indirect costs relative to net settlement funds administered. These results also allow for a fair comparison between the indirect costs and the direct costs of settlement administration. Using the information from **Figure 6**, the relative proportions of the *fully loaded* costs of

Figure 6

Wealth Transfers of Indirect Costs Based On Best-in-Class Benchmark



claims administration were calculated. Fully loaded costs, rather than just direct costs—that is, the money paid to the claims administrator, because they include indirect costs—that is, the wealth transfer from legitimate claimants to ineligible claimants, are the costs relevant to legitimate claimants and thus should be the relevant costs considered when claims administrators are selected.

Table 3

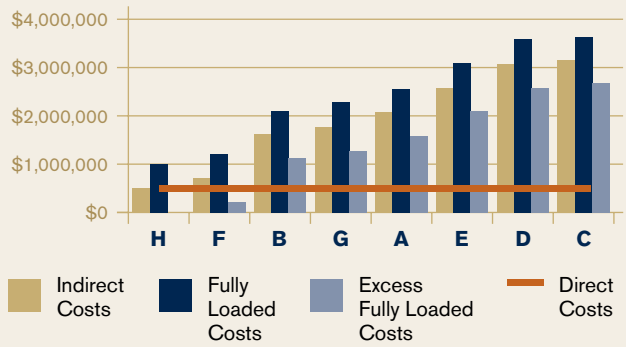
Administrator	Direct Costs	Indirect Costs	Fully loaded Costs	Excess Fully loaded Costs
H	$500,000	$495,000	$995,000	$0
F	$500,000	$710,000	$1,210,000	$215,000
B	$500,000	$1,610,000	$2,110,000	$1,115,000
G	$500,000	$1,775,000	$2,275,000	$1,280,000
A	$500,000	$2,070,000	$2,570,000	$1,575,000
E	$500,000	$2,590,000	$3,090,000	$2,095,000
D	$500,000	$3,085,000	$3,585,000	$2,590,000
C	$500,000	$3,150,000	$3,650,000	$2,655,000

Assuming again that all administrators have the same direct costs of 1% of a net settlement fund (an unreasonable but illustrative assumption), *direct* costs as a percentage of fully loaded costs ranged from approximately 14% for Administrators C and D, to 50% for Administrator H, while the *indirect* costs as a percentage of *fully loaded* costs ranged from approximately 86% for Administrators D and C, to 50% for Administrator H. Thus, the ratio of indirect costs to direct costs for Administrator H is one-to-one, while for Administrators C and D, the ratio is more than six-to-one. The *fully loaded* costs as a percentage of net settlement funds range from approximately 2.0% for Administrator H to over 7.0% for Administrators D and C.

Table 3 uses the results displayed in **Figure 6** to compare for each administrator the average direct, indirect and fully loaded costs of a hypothetical $50,000,000 net settlement fund assuming that each such administrator proposed direct costs in an amount equal to 1% of the net settlement fund. **Figure 7** displays these results. What is apparent is that, as stated in the introduction to this article, direct costs are just the tip of the iceberg, with indirect costs – the amount of the wealth transfer from legitimate claimants to ineligible claimants – unseen beneath the surface. Had Administrator H's proposed fee – its direct costs – been $200,000, or 40%, higher than was assumed, legitimate claimants, had Administrator H rather than Administrator F, the next most accurate administrator, been retained, still would have benefited by $15,000. And had Administrator H proposed a fee that was

Figure 7

Administrator Costs



six times greater than the hypothetical $500,000 bid set forth in **Table 3**, legitimate claimants still would have benefited by $155,000 compared to how they would have fared had Administrator C, the administrator with the highest indirect costs, been retained.

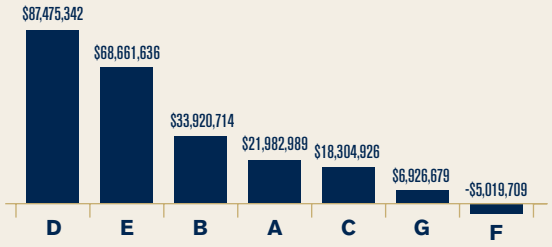
The materiality of these results is even more compelling when they are compared to the all-in request for proposal regime (which almost always includes only the costs of processing claims and excludes the costs for publishing, printing, postage and nominees), which, as described above, is most often the means by which claims administrators are selected. Assuming that, on average, the direct costs of claims administration range from 0.5% to 1% of a net settlement fund, and that the costs of publishing the summary notice, of printing the mailing notice, postage costs for mailing the notice, and nominee costs – *i.e.*, the direct costs that, as described above, are completely out of an administrator's control – are not more than 25% of those direct costs, the direct costs within an administrator's control range from 0.375% to 0.75%. Thus, the controllable differential among competing administrators often is just tens of thousands of dollars, or mere fractions, of the bid amount. Thus, the selection of an administrator often is based on dollar amounts that, although they are tenths of a percent of the net settlement fund, result in the retention of an administrator that, as a result of distributing settlement dollars to ineligible claimants, will cost legitimate claimants as much as 5.3% of that net settlement fund.

Dollars of Estimated Net Recovery Lost by Legitimate Claimants

The financial consequences to legitimate claimants caused by the varying levels of claims processing accuracy among administrators also was estimated in dollars. For each administration conducted by each administrator other than Administrator H, the estimated net settlement fund was multiplied by an amount equal to each administrator's percentage of uncured deficient claims minus the Best-in-Class Benchmark (7.20%). When that calculation resulted in a negative amount—*i.e.*, when the proportion of uncured deficient claims was higher than the Best-in-Class Benchmark, it represented

Figure 8

Estimated Net Recoveries Lost By Legitimate Claimants Based On Best-in-Class Benchmark

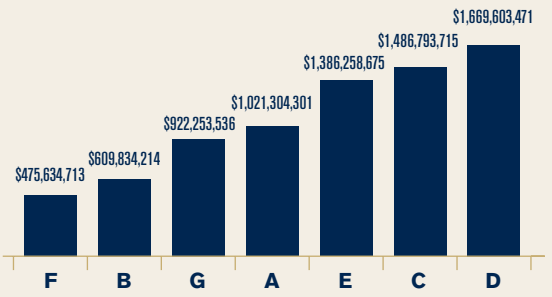


a benefit to legitimate claimants. Accordingly, I applied those negative amounts to offset positive amounts—*i.e.*, when the proportion of uncured deficient claims was lower than the Best-in-Class Benchmark, which is the estimated amount of the recovery that was distributed to ineligible claimants rather than to legitimate claimants. The assumption is that all administrators should convene at the mean. As reflected in **Figure 8**, the net amount of recovery that legitimate claimants may have lost is remarkable, even when they "return" some of the funds they received if they were lucky enough also to have been legitimate claimants in an administration with superior processing: Had administrators other than Administrators H and F processed their administrations as accurately as the Best-in-Class Benchmark, legitimate claimants would not have lost in recoveries on average of between approximately $7 million and $87.5 million, respectively. And had Administrator H processed claims on average at the 3.02% Sector Average Benchmark rather than at the higher 7.20% Best-in-Class Benchmark, legitimate claimants would have lost approximately $594 million.

Next, I estimated the net recoveries that legitimate claimants *could* have lost had each administrator conducted at its individual level of processing accuracy *all* 325 settlements, which totaled $28.4 billion. In other words, what would the loss have been to legitimate claimants if, according to the Lemon Model, the most accurate claims administrator was displaced by each of the less accurate administrators. Those amounts were estimated for each

Figure 9

Estimated Lost Net Recoveries if Each Administrator Conducted All Settlements at Its Individual Level of Processing Accuracy



administrator other than Administrator H (the administrator with the highest proportion of uncured deficient claims, and, therefore, the most accurate administrator) by multiplying the net settlement fund for each administration (without regard for which administrator conducted the administration) by the difference between that administrator's proportion of uncured deficient claims and the Best-in-Class Benchmark (7.20%). The results, as shown in **Figure 9**, are staggering in magnitude, and reveal that more accurate claims processing, even if it is marginally more expensive (*i.e.*, pennies per claim), is worth the price. Had each administrator other than Administrator H conducted all the administrations, legitimate claimants would have lost between $475.6 million, if Administrator F was the administrator, and $1.7 billion, if Administrator D was the administrator. And if Administrator H had conducted all the administrations, legitimate claimants would not have paid to ineligible claimants over $1.01 billion compared to what they would have paid to ineligible claimants had each of those settlements been processed at the Sector Average Benchmark.

Statistical Results – Claims Processing Efficiency

I next consider whether increased claims processing accuracy comes at the expense of efficiency. For each administration in the sample, I determined the length of time between the claims filing deadline and the distribution date; I then standardized it by dividing it by the total number of claims processed in the corresponding administration. **Figure 10** presents the average number of claims processed per day between the last claims deadline and corresponding distribution date. The average number of claims processed per day for the group was exceeded by only three administrators, including Administrator H, the most accurate claims administrator by proportion of uncured deficient claims.[59] **Figure 11** presents these claims processing efficiency results together with the results for claims processing accuracy—that is, the proportion of uncured deficient claims. Those two metrics must be considered together to see whether increased claims processing accuracy delayed distributions. As **Figure 11** reveals, superior

Figure 10

Average Number of Claims Processed Per Day Between the Claims Deadline and the Distribution Date

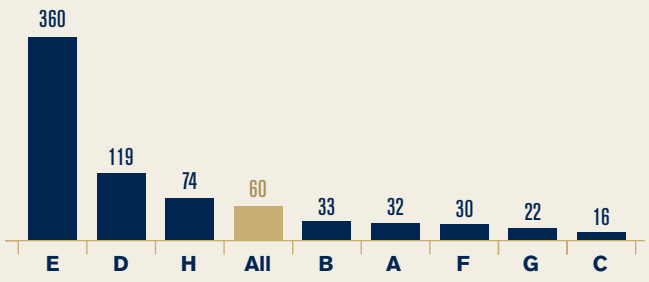
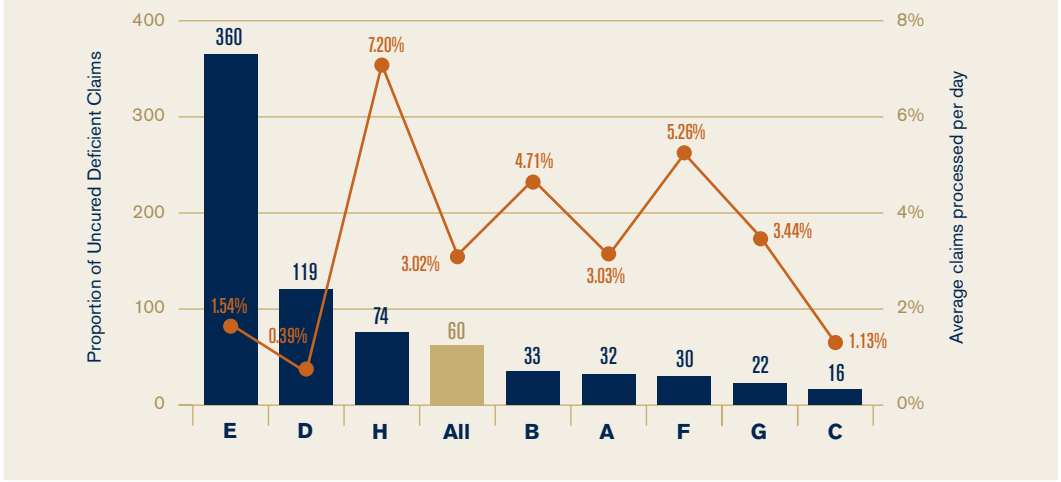


Figure 11

Claims Processing Accuracy & Efficiency



claims processing accuracy expedited distributions: Administrator H, notwithstanding its substantially greater proportion of uncured deficient claims, processed on average more claims per day than five of the other seven less accurate administrators and the group. Accordingly, by paying for more accurate claims processing, legitimate claimants maximize their recovery *and* get it faster than if they had paid less for less accurate claims processing.

Selecting Claims Administrators Should Be Based on In-Depth Cost-Benefit Analyses

The empirical evidence set forth above demonstrates that value-added claims administration is not a fungible commodity; rather, there is value determinative substantial variation in claims administrators' claim processing accuracy and efficiency. Accordingly, the same economic theories that explain why experience, training and talent are key considerations in the selection of class counsel, also explain that those qualitative considerations are fundamental to the selection of claims administrators. Just as "[l]awyer quality is an important component of the selection process because a higher quality lawyer maximizes the client's expected recovery by increasing the likelihood of recovery, the amount of recovery, or both,"[60] so, too, does claims administrator quality increase the likelihood that legitimate claimants receive the full measure of their recoveries. As the analyses presented above objectively show, therefore, in claims administration services as in legal services, "price and quality are often directly related,"[61] which is why higher quality claims administrators, like "lawyers who offer higher quality legal services [and thus] are able to command a higher price for their services,"[62] should be compensated according to their ability. With the increased scrutiny that, under the 2018 Amendments, courts evaluating a proposed class action settlement must apply to class member recoveries and participation, and, therefore, to accurate claims processing,[63] class counsel, when they select claims administrators, should consider whether the difference between bid prices will lead to a greater difference in indirect costs.[64]

Claims administrators' diverse claims processing accuracy and efficiency, which are products of the Lemon Model's consequences, of the perverse incentives provided by price-dominant selection approaches, and of the level of their capabilities, relevant experience, and sophistication, vary substantially. The selection process, to be value-driven and comprehensive, should therefore consider each administrator's fully loaded costs, not just their direct costs, as represented by the price they bid, but also the corresponding indirect costs of that administrator's inferior claims processing, which may be estimated by comparing to sector-wide standards each administrator's objective claims processing accuracy and efficiency data. Accordingly, class counsel should require claims administrators to provide the data identified above so that the touchstone for retaining claims administrators will be "value" – a fair return or equivalent in goods, services, or money for something exchanged"[65] – rather than "price" – the amount of money given or set as consideration for the sale of a specified thing."[66]

To continue to base claims administrator selection on what may appear to be a bargain price, will continue to result in the retention of administrators that cannot or, because of the severe pricing discount, will not, provide the range and quality of services necessary to maximize processing

efficiency and accuracy. Comparing the higher bids of more diligent claims administrators to cut-rate bids that are "too good to be true," without also considering objective measures of claims processing accuracy and efficiency, cannot, as empirically shown in the analyses presented above, result in an "apples to apples" comparison. And when that happens—when the scale has fruit on only one side, the result – like comparing bicycles to Bentleys – will produce what may, without considering indirect costs, appear in the abstract to be a large dollar variance between them.[67] Only when indirect costs are included—that is, when there are apples on both sides of the scale, will the analysis yield meaningful results. Selecting the administrator with lowest bid without considering accuracy and efficiency—that is, without factoring in the costs of inferior claims administration, already has imposed on legitimate claimants substantial but avoidable costs that range in the hundreds of millions of dollars, as well as delays in receiving their recoveries. Continued devotion to that regime may be hard to justify as practice under the 2018 Amendments develops.

Whether or not class counsel consider claims processing accuracy and efficiency as part of their claims administrator selection process, the 2018 Amendments will make it increasingly likely that courts, when they evaluate whether "the relief provided for the class is adequate, taking into account, [among other factors,] the effectiveness of any proposed method of distributing relief to the class, including the method of processing class-member claims,"[68] are likely to consider them, especially given the Rule 23 Advisory Committee's admonition that "[o]ften it will be important for the court to scrutinize the method of claims processing to ensure that it facilitates filing legitimate claims."[69] And those courts, because "[t]he relief that the settlement is expected to provide to class members is a central concern," may, to measure that relief, find it "important" to "direct[ ] that the parties report back to the court about actual claims experience."[70] Accordingly, class counsel should anticipate that judicial scrutiny by considering objective criteria of claims processing accuracy and efficiency. After all, one thing is certain: The class is not getting something for nothing.[71]

Notes

* Jeffrey N. Leibell is the principal of The JNL Firm, LLC, a consulting firm that provides class action settlement management services, and is the Chief Legal & Financial Officer of Financial Recovery Services, LLC ("FRS"), a leading class action claims management consulting firm. Prior to joining FRS, Mr. Leibell was Vice President, Class Action Services at The Garden City Group, Inc., a prominent class action settlement administrator, and, before that, he was the partner at Bernstein Litowitz Berger & Grossmann LLP, a preeminent plaintiff-side class action law firm, responsible for negotiating and documenting the terms of, developing the allocation plans for, and overseeing the administrations of, over $16.4 billion in class action recoveries.

1 For an explanation of why lawyers and courts have taken this position, see Jeffrey N. Leibell, *67% of Something Is Better than 100% of Nothing: Competent and Ethical Class Action Claims Consultants Provide Value and Increase Participation in Class Action Settlements*, available at www.JNLFirm.com.

2 *Precision Assoc., Inc. v. Panalpina World Trans. (Hldg.) Ltd.*, No. 08-CV-00042 (E.D.N.Y.).

3 *See* Mem. Supp. Mot. Distrib. Net Settle. Funds, Doc. 1403, at 5 & n.1.

4 *See* Docs. 1406-24, 1425-52, 1455-1502 (this does not include any complaints that notified class counsel or the claims administrator less formally).

5 Not. W'drawal Distrib. Mot., No. 1423 (Aug. 18, 2017) ("Plaintiffs recently learned that some claims may have contained inaccurate information. Plaintiffs and the Claims Administrator are reviewing this information and will refile their motion after determining whether any claims filed by certain Class members contain material inaccuracies and, if so, adjusting the amounts proposed to be paid to each Class member."); *mot. term'd by* Aug. 21, 2017 Order (dkt. entry).

6 *See* Status Rpt., Doc. 1503, at 2 (Oct. 17, 2017). But because the claims administrator also discovered a more pervasive error, class counsel had to allow all affected claimants to respond to any outstanding audit letters associated with their claims. *See id.* at 2-3.

7 *See* Settle. Claims Admin. Prog. Rpt., Doc. 1509, at 2 (Apr. 16, 2018).

8 *See id.* The claims administrator mailed revised claim determination letters on September 28, 2018. *See* Settle. Claims Admin. Prog. Rpt., Doc. 1515, at 2-3 (Oct. 12, 2018).

9 *See* Doc. 1516 (Jan. 28, 2019).

10 *See, e.g.*, *In re Cendant Corp. Litig.*, Master File No. 98-1664 (D.N.J.) ($28.7 million in fraudulent claims paid); *The SEC's mind-boggling tale of $40 million fraud*, Reuters® (Nov. 4, 2021).

11 *See, e.g.*, *Reiver v. 3Com*, No. C-03-00169, Mot. & Mem. Supp. for Ord.: (1) App'g Settle. of Claims Dispute; ..., Doc. 320, at 4:18-5:1 & 6:7-9 (N.D. Cal. Oct. 22, 2004) (Legitimate claimants in the *3Com* settlement sued the claims administrator and class counsel for erroneously being excluded from the distribution; a settlement that paid those claimants $9.5 million – the amount that their claims would have been paid had they been processed and paid in the ordinary course plus interest – was reached.); *USA v. Computer Assoc. Int'l, Inc.*, No. 1:04-cr-00837 (E.D.N.Y.) (After distributing all $290 million in restitution funds obtained in a federal criminal action for securities fraud, the claims administrator discovered 1,700 timely proofs of claim with a total value of $59.2 million that it did not process, causing a substantial undertaking supported by two orders to compel victims to return overpayments.).

12 *See, e.g.*, *In re Blood Reagents Antitrust Litig.*, MDL No. 09-2081 (E.D. Pa.) (Claims administrator's omissions compelled class counsel to file an amended distribution motion; after the court approved that amended motion, additional discrepancies required further delay.).

13 "The goal of any distribution method is to get as much of the available damages remedy to class members as possible and in as simple and expedient a manner as possible." 4 William B. Rubenstein, Newberg on Class Actions §12:15 (5th ed.) (Westlaw 2018), *quoted in In re LIBOR-Based Fin. Instr. Antitrust Litig.*, 327 F.R.D. 483, 496 (S.D.N.Y. 2018); *in Krakauer v. Dish Network, LLC*, Case No. 1:14-CV-333, 2017 WL 3206324, at *7 (M.D.N.C. July 27, 2017); *in In re Credit Default Swaps Antitrust Litig.*, No. 13-md-2476, 2016 WL 2731524, at *9 (S.D.N.Y. Apr. 26, 2016) ("A principal goal of a plan of distribution must be the equitable and timely distribution of a settlement fund … ."); *and in Hendricks v. StarKist Co*, Case No. 13-cv-00729, 2015 WL 4498083, at *8 (N.D. Cal. July 23, 2015)). Accurate and efficient claims administrations also are encouraged by institutional lead plaintiffs and courts that have required class counsel to defer until after distribution was completed substantial portions of their court-awarded legal fees. *See, e.g.*, *In re Petrobras Sec. Litig.*, 317 F.Supp.3d 858, 877 (S.D.N.Y. 2018), *appeal dismissed sub nom.* No. 18-2120, 2018 WL 7108171 (2d Cir. Sept. 13, 2018), *and aff'd*, 784 Fed. Appx. 10 (2d Cir. 2019); *In re Foreign Exch. Bench. Rates Antitrust Litig.*, No. 13 Civ. 7789, 2018 WL 5839691, at *6 (S.D.N.Y. Nov. 8, 2018) (court deferred payment of 50% of the awarded fees of $300,335,750, or $150,167,875, until an initial distribution was conducted, with the remaining 50% to be paid "upon the substantial distribution of the settlement fund to the remaining claimants."). The 2018 amendments to Rule 23 (the "2018 Amendments") now require courts to consider in their evaluation of whether "the relief provided for the class is adequate," among other things, "the terms of any proposed award of attorney's fees, including timing of payment." Fed. R. Civ. P. 23(e)(2)(C)(iii).

14 *See, e.g.*, *In re GSE Bonds Antitrust Litig.*, 414 F.Supp.3d 686, 694 (S.D.N.Y. 2019) ("Rule 23(e)(2)(C)(ii) requires courts to examine 'the effectiveness of any proposed method of distributing relief to the class, including the method of processing class-member claims.'") (quoting Fed. R. Civ. P. 23(e)(2)(C)(ii)), *quoted in* Jeffrey N. Leibell, *Under Amended Rule 23, Settlement Management Is Not Just a Good Idea, It's the Law* (cited as "*Settlement Management*"), available at www.JNLFirm.com.The Advisory Committee included among the "primary procedural and substantive qualities that should always matter to the decision whether to approve" a proposed settlement as fair, reasonable, and adequate, "[t]he relief that the settlement is expected to provide to class members," and, in that connection, advised courts that "[m]easuring the proposed relief may require evaluation of any proposed claims process," that "directing … the parties [to] report back to the court about actual claims experience may be important," and that "[o]ften it will be important for the court to scrutinize the method of claims processing to ensure that it facilitates filing legitimate claims." Fed. R. Civ. P. 23 Adv. Comm. Notes 2018 Amend. (hereinafter "Adv. Comm. Notes"), Subd. (e)(2) &¶¶ (C) & (D).

15 *In re Mercury Finance Co. Litig.*, No. 97 C 624, 1997 WL 529553, at *1 (N.D. Ill. Aug. 15, 1997); *accord id.* at *2 ("[T]he reasonable fee is the lowest fee that would be paid by a discerning client in an arm's-length negotiation with well-qualified counsel. … [T]he best counsel are not likely the lowest paid counsel, … ."); *see, e.g.*, *In re Cendant Corp. Litig.*, 182 F.R.D. 144, 150-51 (D.N.J. 1998) ("[G]iven the opportunity, absent class members would try to secure the most qualified representation at the lowest cost.").

16 15 U.S.C. § 78u-4(a)(3)(B)(v) (the "PSLRA") ("The most adequate plaintiff shall, subject to the approval of the court, select and retain counsel to represent the class."). Cases under the PSLRA in which the court ordered a lead counsel auction include *In re Bank One S'hldrs Class Actions*, 96 F. Supp. 2d 780 (N.D. Ill. 2000); *In re Lucent Techs., Inc. Sec. Litig.*, 194 F.R.D. 137 (D.N.J. 2000); *Sherleigh Assocs. v. Windmere-Durable Hldgs.s, Inc.*, 184 F.R.D. 688 (S.D. Fla. 1999); *Wenderhold v. Cylink Corp.*, 188 F.R.D. 577 (N.D. Cal. 1999); *In re Cendant Corp. Litig.*, 182 F.R.D. 144 (D.N.J. 1998).

17 182 F.R.D. at 151.

18 *Cendant*, No. CIV. A. 98-1664, 2000 WL 1288307, at *2 (Apr. 7, 2000) ("[T]his quasi-philanthropic effort does not auger well as a realistic incentive to pursue a determined resolution of the plaintiffs' cause."), *vacated in part on other grounds and remanded*, 264 F.3d 201 (3d Cir. 2001); *see Raftery*, 1997 WL 529553, at *2 ("Counsel simply should not submit a proposal that is economically undesirable or unrealistic."); *see also, e.g.,* Jill E. Fisch, *Aggregation, Auctions and Other Developments in the Selection of Lead Counsel Under the PSLRA*, 64 Law & Contemp. Probs. 53, 83 (2001) (cited as "*Auctions in the Selection of Lead Counsel*") ("The [*Cendant*] court explicitly rejected some firms on the basis of quality factors, concluding for example that several bidders had not demonstrated sufficient securities trial experience."); Lynn A. Baker, Michael A. Perino & Charles Silver, *Is the Price Right? An Empirical Study of Fee-Setting in Securities Class Actions*, 115 Colum. L. Rev. 1371, 1433 (2015) (Lead plaintiffs "know that price and quality matter, not just price alone, so they will offer higher fees when, in their judgment, higher fees are likely to generate larger net recoveries.").

19 For ease of reference and to avoid confusion, this article uses the following terminology:

Term	Definition
accepted claims	Claims that were approved to receive a pro rata distribution from the settlement recovery.
rejected claims	Claims that were determined not to qualify to receive a pro rata distribution from the settlement recovery, including claims that could not be cured and those that could have been but were not.
rejectable claims	Claims that are defective in ways that cannot be cured.
deficient claims	Claims that are defective in ways that may be cured.

20 To select claims administrators, lead counsel almost always use some form of the "all-in" request for proposal—that is, one price per claim processed. While all-in proposals may appear to simplify a seemingly difficult comparison among competing bidders, they may instead obscure that comparison: Because it often is difficult, if not impossible, to determine which services and related costs are included in the "all-in" proposed price, the lack of pricing transparency makes a meaningful comparison more difficult.

21 Fully loaded costs here include the direct costs of the claims administration, which are the fees and expenses that a claims administrator charges to provide its package of services (*e.g.*, sending notice to the class, processing claims, and distributing recoveries); those costs, because they are generally represented by claims administrators' bids, are relatively easy to measure. But fully loaded costs also include indirect costs, which, in contrast, are generally unobserved: As described below, they are the amount of their pro rata recoveries that, because of poorly executed claims processing, legitimate claimants unknowingly forfeit to ineligible claimants.

22 *See* George A. Akerlof, *The Market for "Lemons": Quality Uncertainty and the Market Mechanism*, 84 Q. J. Econ. (The MIT Press) No. 3, at 488-500 (Aug. 1970).

23 *See e.g.*, *Lumbermen's Mut. Cas. Co. v. Elbert*, 348 U.S. 48, 59 (1954) (Frankfurter, J., concurring) (Increasing the number of federal judges "will result, by its own Gresham's Law, in a depreciation of the judicial currency and the consequent impairment of the prestige and of the efficacy of the federal courts.").

24 "There Is No Such Thing as a Free Lunch," often referred to by its acronym "TINSTAAFL," explains that a person or a society cannot get "something for nothing." Even if something appears to be free, there is always a cost even though it may be hidden or distributed. Whatever goods and services are provided, they must be paid for by someone. *See* Milton Friedman, *There's No Such Thing as a Free Lunch*, Open Court Pub. Co. (August 1975); Robert H. Fetridge, "Along the Highways and Byways of Finance," *The New York Times*, Nov 12, 1950, p. 135 (quoting economist and army general Leonard P. Ayres of the Cleveland Trust Company).

25 *Compare, e.g., Staton v. Boeing Co.*, 327 F.3d 938, 964 (9th Cir. 2003) ("[T]he negotiation of class counsel's attorneys' fees is not exempt from the truism that there is no such thing as a free lunch."), *quoted in In re Southwest Airlines Voucher Litig.*, 799 F.3d 701, 711 (7th Cir. 2015); *see also id.* ("Judicial scrutiny of class action fee awards and class settlements more generally is based on the assumption that class counsel behave as economically rational actors who seek to serve their own interests first and foremost, … ."); *Iron Workers Local No. 25 Pen. Fund v. Credit-Based Asset Serv'g & Secur., LLC*, 616 F. Supp. 2d 461, 465-66 (S.D.N.Y. 2009) (relying on the "the ever-applicable adage that there is no such thing as a free lunch" to determine that a "free" service was not really free).

26 *See* Akerlof at 488-500.

27 If bidding claims administrators were required to provide sufficient objective claims processing accuracy and efficiency data, class counsel and courts could evaluate it together with price—*i.e.*, they would be able to perform a cost benefit analysis. *See, e.g.*, *In re Lucent Tech., Inc. Sec. Litig.*, 221 F. Supp.2d 463, 470-71 (D.N.J. 2001) ("Because it would be difficult to award a bid and determine the fee arrangement in advance without performing a cost-benefit and quality analysis as would a client in a real-world situation, the bids requested in *Lucent I* and *Lucent II* required more than simply a proposed fee percentage."); *Cendant*, 182 F.R.D. at 150-51 ("It is reasonable to assume that given the opportunity, absent class members would try to secure the most qualified representation at the lowest cost."); *Raftery*, 1997 WL 529553, at *1 ("The court believes, however, that the qualitative factors (which are regularly considered in cases discussing Rule 23(a)(4)) can scarcely be divorced from the question whether a party has engaged counsel who will provide legal services for a reasonable fee.").

28 *Auctions in the Selection of Lead Counsel* at 84-85.

29 Andrew Niebler, *In Search of Bargained-for-Fees for Class Action Plaintiffs' Lawyers: The Promises and Pitfalls of Auctioning for the Position of Lead Counsel*, 54 Bus. Law 763, 764-65 (1999) (cited as "*Auctioning for Lead Counsel*"); *id.* at 777-79 ("selection of class counsel solely on the basis of price without consideration of incentives and penalties for poor performance may yield a situation in which 'lemon' lawyers force 'good' lawyers out of the competitive bidding process."); Laural L. Hooper & Marie Leary, *Auctioning the Role of Class Counsel in Class Action Cases: A Descriptive Study* (Fed. Jud. Ctr. 2001), *reprinted at* 209 F.R.D. 519, 525 (Aug. 29, 2001) (among the disadvantages a bidding procedure were "that 'cheaper' lawyers are not necessarily better advocates and might be worse," and that "the process can create incentives for lawyers to bring and settle cases prematurely, without adequate preparation, investigation, and discovery, and for inadequate consideration").

30 *Auctions in the Selection of Lead Counsel* at 83.

31 *Auctioning for Lead Counsel* at 764.

32 *See, e.g.*, Broadridge Fin. Sol., Inc., Global Class Action Ann. Rpt. 2019 3 (2020) (cited as "Broadridge") (The ten most "complex and complicated" securities class action settlements of 2019 demonstrate that "[t]he class action and administrative process that determines who gets what is becoming ever more complicated."); *id.* at 5 (criteria used to determine case complexity included "[c]omplexities" in, among other things, "the loss calculation formula"; "jurisdictional, judicial and/or filing requirements"; and "deadlines (*e.g.*, more than one settlement, with different legal rights and deadlines)."

33 *Compare* Janeen McIntosh & Svetlana Starykh, *Recent Trends in Securities Class Action Litigation: 2020 Full-Year Review* (NERA Feb. 2020) (cited as "NERA"), at 14-17.

34 *See, e.g.*, Broadridge at 3 ("Methods of determining settlements are complex, processing requirements are arduous, and new legal theories, laws and jurisdictions are increasing."); *id.* at 5 (criteria used to determine case complexity included "[c]omplexities in the security/product at interest").

35 *Auctioning for Lead Counsel* at 764 (footnote omitted).

36 *Auctioning for Lead Counsel* at 779 (footnote omitted); *accord Auctions in the Selection of Lead Counsel* at 89 ("The plaintiff class also is exposed to substantial risk if the court mistakenly selects as counsel a firm that has made an unrealistically low bid. ... [A] firm is unlikely to continue to invest resources that it does not expect to recover.") (citing John C. Coffee, Jr., *"Auction Houses": Legal Ethics and the Class Action*, N.Y.L.J., May 18, 2000, a 5 (describing the dilemma faced by class counsel under a fee structure that fails to align counsel's incentives with those of the plaintiff class)).

37 *Auctioning for Lead Counsel* at 778-79 (footnotes omitted).

38 *Auctioning for Lead Counsel* at 779 (footnote omitted).

39 *Auctioning for Lead Counsel* at 777 (footnotes omitted).

40 *Auctioning for Lead Counsel* at 778 (footnotes omitted).

41 *Auctioning for Lead Counsel* at 779 (footnotes omitted).

42 I did not select as the metric for claims processing accuracy the number of claims rejected – either as rejectable claims or as uncured deficient claims – as a percentage of claims processed. While that measurement is *an* indicator of an administrator's processing accuracy, it does not by itself provide all the information necessary to make an accurate assessment, and it actually may mask a lack of processing accuracy. For example, although a high percentage of rejected claims may seem on its face to show processing accuracy, if the rejected claims are comprised mostly of rejectable claims with only a small number of uncured deficient claims, considering only the percentage that rejected claims comprise of total claims received will not be informative, and will mask the small number of deficient claims identified by that administrator.

43 People and entities are strongly motivated to act consistent with their economic interests. *See, e.g.*, *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986) ("[I]f the factual context renders [the plaintiff's] claim implausible – if the claim is one that simply makes no economic sense – [the plaintiffs] must come forward with more persuasive evidence to support their claim than would otherwise be necessary.").

44 *See, e.g.*, Deborah R. Hensler, *Happy 50th Anniversary, Rule 23! Shouldn't We Know You Better After All This Time?*, 165 U. Pa. L. Rev. 1599, 1611-12 (2017) ("The lack of objective information on Rule 23's compensation performance function fuels debate over the value of class actions and creates significant opportunities for misleading characterizations of class action outcomes."); Nicholas M. Pace & William B. Rubenstein, *How Transparent Are Class Action Outcomes? Empirical Research on the Availability of Class Action Claims Data*, 2 RAND Inst. Civ. Just. (Wkg. Pr. No. WR-599-ICJ, 2008) ("little information is available to the public about how many class members actually received compensation and to what degree).

45 According to its website, https://www.issgovernance.com/about/about-iss/, ISS "offers a complete end-to-end litigation research and claims filing solution covering equities and fixed income securities across all markets." ISS's accuracy is regularly relied upon. *See, e.g.*, *In re Fed. Nat. Mort. Assoc. Sec., Deriv. & "ERISA" Litig.*, 4 F. Supp.3d 94, 104 (D.D.C. 2013); *Melot v. JAKKS Pacific, Inc.*, Nos. LA CV13–05388, LA CV13–05487, 2013 WL 12133650, at *5 (C.D. Cal. Dec. 9, 2013); *Maine State Ret. Sys. v. Countrywide Fin. Corp.*, Nos. 2:10-CV-00302, 2:12-CV-05125, 2:12-CV-05122, 2013 WL 6577020, at *13 n.6, (C.D. Cal. Dec. 5, 2013); *see also, e.g.*, Alexander I. Platt, *"Gatekeeping" in the Dark: SEC Control Over Private Securities Litigation Revisited*, 72 Admin. L. Rev. 27, 57 & n.164 (Winter, 2020). I am not aware of any similar database for other (*e.g.*, antitrust or consumer) class actions.

46 For example, in 2018, Epiq, which had acquired Poorman-Douglas ("Poorman") in 2004, acquired GCG; in 2015, Computershare, which in 2007 acquired Administar and in 2009 acquired KCC, acquired Gilardi; and, in 2019, Duff & Phelps, which had acquired Prime Clerk in 2019, also acquired Heffler and rebranded as Kroll Business Services. As a result, Epiq now accounts for 54% and Computershare for >21% of the "SCAS Top 100" securities class action settlements of all time. *See The Top 100 U.S. Class Action Settlements of All Time, as of December 31, 2020*, at 20-23 (Feb. 2021).

47 It is not unusual for settlements to distribute recoveries in more than one round. Because the ISS listing includes all distributions during the test period, it includes multiple distributions for certain settlements even though there was only one claim processing procedure. All settlement dollars obtained from multiple settlements were included in the sample.

48 For certain calculations, I used the net settlement fund as a proxy for the amounts distributed. That was necessary because the precise distributable amount generally is not disclosed. My estimated net settlement fund for each settlement includes, where known, the attorneys' fees and litigation expenses awarded; where those amounts were not known, the amounts disclosed in the settlement notices were used. I excluded from my analyses administration costs, which generally average less than 1% of the net settlement fund, because, while they may be determined for some settlements, they are not readily determinable for all settlements.

49 As described *infra* in "Robustness and Validity of the Sample Results," the exclusion of these 183 settlements had no meaningful impact on the results of the sample. Also, for 20 of them, the net settlement fund amount was combined with that in related administrations; because another 20 class actions were settled together, their net settlement funds are considered as one net settlement fund.

50 Those administrators were GCG; Gilardi; A.B. Data; Berdon; Strategic Claims Solutions; Heffler; Rust, which includes administrations conducted by Complete Claims, which Rust acquired in 2006; Analytics; and Epiq, which includes administrations conducted by Poorman. Another nine administrators, none of which conducted more than 4 administrations during the sample period, are included together; the results of the 14 settlements that they administered accounted for approximately $701 million, or 2.5%,

of the $28.4 billion total settlement dollars in the sample. Those "Other" administrators are Administar; FRG; RSM McGladrey; Global Risk Solutions; RCB Fund Service; Stephanie Avakian; and Valley Forge. Because administrator identities are not relevant to my thesis, they each are identified by a randomly assigned letter.

51 Of the 176 distributions for which a distribution affidavit or declaration was not filed, 123, or 70%, were conducted by Administrator I. My aggregate data excludes the results for the 42 administrations that were conducted by Administrator I for which data was obtained. Those administrations accounted for $4.5 billion, or 15.8%, of settlement dollars out of the $28.4 billion in settlement dollars in the sample.

52 A distribution of values is generally described by measures of central tendency (*i.e.*, the mean and median) and its dispersion (*i.e.*, the standard deviation, etc.).

53 The relationships between the mean, median and various percentiles, as well as the fact that the largest net settlement fund for the population and sample are $6.4 billion and $5.8 billion, respectively, all point out that the population and sample distributions are both similarly highly skewed, which means that they both are similarly lopsided and not symmetrical about the mean.

54 The non-parametric Kolmogorov-Smirnov ("K-S") Test was used to determine whether the characteristics of the distribution of net settlement funds for the sample are different from the population of net settlement funds. The K-S Tests suggest that there is no statistically significant difference when comparing the sample distribution to that of the population.

55 *See, e.g.*, NERA at 20, Fig.16 (the median ratio of settlement to investor losses from 2012 to 2020 has ranged from 1.6% in 2015 to 2.5% in 2017 and 2018).

56 *See, e.g., In re El Toro Materials Co., Inc.*, 504 F.3d 978, 978 (9th Cir. 2007) ("Distributing money to satisfy claims is, in most cases, a zero-sum game: Every dollar given to one creditor is a dollar unavailable to satisfy the debt owed to others. For Paul to be paid in full, Peter must be short-changed."); *S.E.C. v. Capital Consultants, LLC*, 397 F.3d 733, 742 (9th Cir. 2005) ("This argument ignores the limited fund aspect of this case. In a zero-sum game, favoring one fund necessarily disfavors another."); *In re Fidelity/Micron Sec. Litig.*, 167 F.3d 735, 738 (1st Cir. 1999) ("[O]nce a common fund is established, class members and class counsel wind up playing a zero-sum game, in which every dollar awarded to counsel represents one dollar less that is available for distribution to class members.").

57 There are other uncontrollable direct costs incurred in almost any class action settlement. Those costs, which include printing notices and claim forms, mailing them and publishing summary notices, are not included in the price per claim that an administrator bids. These uncontrollable direct costs often are substantial and are largely governed by circumstances, such as the number of pages in the notices and claim form, that are outside the control of the administrator. As a result, and because they do not require a substantial amount of labor, they do not distinguish one administrator from any other.

58 That Best-in-Class Benchmark was selected because, as shown in **Figure 4**, the administrators met or exceeded it in 87 administrations, or 27% of the time, and, therefore, it was achievable.

59 The processing efficiency results for Administrator D were dominated by one administration in which, with 273 days between the claims filing deadline and the date of distribution, it processed almost 578,000 claims, or 2,117 claims per day. Excluding that anomalous administration, Administrator D processed an average of 57 claims per day.

60 *Auctions in the Selection of Lead Counsel* at 83.

61 *Id.*

62 *Id.*

63 *See* note 13, *supra*, and accompanying text.

64 In the best of all worlds, marginal direct costs will be offset by marginal indirect costs. For example, if the difference in the bid prices between two administrators is 1%, but the administrator with the higher bid price will have 2% lower indirect costs, then the administrator with the higher bid should be selected. Alternatively, this equilibrium will be observed where fully loaded costs are minimized.

65 *Value*, Miriam-Webster, available at https://www.merriam-webster.com/dictionary/value (last visited Sept. 30, 2021).

66 *Price*, Miriam-Webster, available at https://www.merriam-webster.com/dictionary/price (last visited Sept. 30, 2021).

67 A variance in price between a low-cost administrator and a higher cost administrator of $1 million, which may seem large in the abstract, is only 0.5% (0.005) of a $200 million settlement; that same relationship maintains at every level of settlement recovery. It would thus seem pennywise but pound-foolish to "save" one-half of one percent of the recovery – mere pennies per legitimate claim – but jeopardize and potentially delay the class's recovery, rather than spend that relatively small amount to "purchase" greater assurance that legitimate claimants will receive their full measure of recovery.

68 Fed. R. Civ. P. 23(e)(2)(C)(ii).

69 Adv. Comm. Notes, Subd. (e)(2) &¶¶ (C) & (D).

70 *Id.*

71 *See* note 23, *supra*, and accompanying text.