

The Devil Is in the Details

Key Claims Administration Issues to Consider During Employment Class Action Settlement Negotiations

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Inherently, class action settlements are very complex and can involve dozens of variables—and even hundreds or thousands, if you consider the individual class members. Skillful planning and management of the details of a settlement can tremendously influence how cost-effectively the settlement can be administered and how quickly the case is brought to a close.



Paying special attention to a few of the key claims administration issues in a settlement will make the entire process go more smoothly and will pay off in the long run. Four of these key issues are the flexibility of the claim's processing parameters, payroll tax considerations, the disbursement of residual funds, and cost control.

Flexibility of the Claim's Processing Parameters

Typically, the claims submission process in employment-related class action suits is straightforward. For example, oftentimes relevant employment data is pre-printed on each class member's claim form and those that concur with the data simply sign the form and submit it to the claims administrator.

The issue becomes a bit more complex when class members dispute the stated employment data. In those cases, they usually have the opportunity to submit documentation supporting their recollection of their work history. This is where the claims administrator is often asked to apply some reasoned judgment, deciding how strictly to interpret the new documentation, versus the original data. The decision rules applied by the claims administrator in these situations should be agreed to in advance.

Another issue that can introduce complexity into the claims administration process is incomplete or improperly completed forms. It is important, therefore, for the attorneys representing the class and defendant, and the claims administrator, to agree beforehand how much time and effort should be put forth to cure defective claims. Agreement should also be reached as to how much leeway the claims administrator is given to accept questionable submissions.

The lesson here is that the design of the claim form and the rules to be followed by the claims administrator in processing submitted claims is an extremely important step in crafting a class action settlement. The form must be clear, concise and focused in order to minimize confusion on the part of class members and the claims administrator should know exactly how counsel and the court expect submitted claims to be interpreted. Careful attention to these details can help ensure claims are processed as efficiently as possible by the claims administrator.

Payroll Tax Considerations

Planning ahead on employment-related suits can also save you and your claims administrator a lot of time and trouble with another issue: payroll taxes. Typically, distributions are split between a wage component and a non-wage component, such as penalties and interest. The portion of the settlement characterized as unpaid wages is subject to W-2 reporting, and as such, social security, medicare, and other payroll taxes must be remitted. Accordingly, it is critically important to establish up front how payroll taxes will be handled.

Of particular concern is the "employer portion" of payroll taxes. If you don't have clear agreement on the source of these funds, you may face a major dispute when it comes time for distributions to the class. For

example, if the settlement contemplates a \$100 payment per class member for unpaid wages and the defendant funds the settlement with \$100 per class member, the settlement will be underfunded. This is because employer payroll taxes are additive to wages and would require funding of approximately \$108 for each \$100 of unpaid wages. In this case, the defendant may balk at having to fund additional unanticipated amounts. Conversely, if the settlement calls for funding of \$100 per class member inclusive of employer payroll taxes and class members are informed that they will receive \$100 in unpaid wages, you might face a different problem. In this situation, since the \$100 is inclusive of employer payroll taxes, the actual wage amount is technically closer to \$92 or \$93. Savvy class members may realize this and allege misrepresentation of the amount of their wage settlement.

Once again, the message is that these issues should be resolved before class notice and claims administration activities begin. Although addressing these issues may take a little more work up front, it will most certainly help you avoid enormous problems at a later date.

Residual Funds

There are also decisions to be made and issues to be ironed out at the other end of the process, after claims have been paid out. For various reasons—most often because not all class members can be located or they don't cash their distribution checks—the claims administrator will likely end up with residual funds.

In general, there are three good options for disbursing this residual: it can be refunded to the defendant, go to a mutually acceptable charity or be sent to the state controller's office as unclaimed funds. Typically, the legal teams for the class and defendants negotiate the disbursement of the residual.

For employment-related claims, the handling of taxes is a consideration in making this decision. In most instances, the claims administrator will have already withheld and remitted income and payroll taxes from the wage portion of the claim. If the residual goes to the defendant or to a charity, the claims administrator will need to initiate a fairly complicated and rigorous process to amend various tax returns and to obtain a refund of taxes remitted in connection with these uncashed distribution checks. Additionally, if these class members later resurface and try to claim their settlement, they will not be able to do so.

However, if the agreement calls for the residual to be given to the state controller's office, the funds will be held in an earmarked account, from which class members may later recover their previously unclaimed portion of the settlement. Since the taxes that were withheld are still on account with the federal and state government, the lengthy tax amendment and recovery process can be avoided. While there are pros and cons of each approach that can be discussed with your claims administrator, it is important that all parties agree in advance to the best way to handle residual funds in your particular case.

Cost Control

Whether paid out of the settlement or by defendants directly, the issue of cost control is a very important detail to consider in developing the claims processing protocol for your case. Decisions made with respect to each of the above issues can have a dramatic impact on the cost to administer the settlement. From simply a structural standpoint, the dollar amount earmarked for claims administration should be scaled to the size and scope of the settlement. Not every case can—or should—bear a high-end claims administration. A settlement of \$60,000 for the benefit of 100 class members, for example, would typically be administered in a very different way than that of a \$6 million settlement for the benefit of the same 100 class members. Working with your claims administrator, you'll be able to develop a scope for your project and a fee structure that is appropriate for everyone involved. Oftentimes, the reasonableness of claims administration costs can be measured by comparing the administration costs on a per claim basis to the projected average payout per claim.

Ideally, early on in the settlement negotiation process you should select your claims administrator and work with them to develop a budget that is reasonable and fair for all parties, and appropriate given the size of the settlement. It helps to break the budget down into the critical steps of the administration and assign associated costs. If your claims administrator has a crystal clear understanding of his or her role, accurate data regarding the size and quality of the class member list, and pre-determined agreement as to the handling of other key issues, there is a much lower likelihood of unpleasant surprises down the road.

One of the best ways to control the costs of claims administration is to ensure that the class member data provided to the claims administrator meets three critical criteria: it must be clean, accurate and in a format that your claims administrator can use. Common problems encountered are incomplete data or conflicting information for the same individual. Obviously, resolving these issues can eat up valuable time. It's simply easier and much less time consuming to get good information at the front end of the process. Also ensure that your firm creates complete and publication-ready versions of notices and other documents so that your claims administrator doesn't end up spending significant time editing documents.

Another important issue to clarify up front is whether or not you expect class members to have the option of communicating with the claims administrator by telephone or e-mail. Hundreds or thousands of contacts, at 5 or 10 minutes per contact, substantially impacts the claims administrator's budget, so this is a critical issue to work out at the very beginning of your relationship.

These are just a few examples of issues that should be addressed in advance rather than reactively during the course of claims administration. Careful planning while negotiating and documenting the settlement will most certainly result in a more cost-effective and efficiently administered settlement.

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