Incentive Awards: The Missing Analysis

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Class actions make it economically viable for plaintiffs to pursue low-value claims. Through class actions, plaintiffs are compensated, and defendants are deterred. An important component of class actions is the class representative. Without a class representative, a class action cannot occur. Therefore, in an effort to induce class representatives to participate in the suit—and thus maintain the sustainability of class actions—class representatives are given incentive awards. These incentive awards seek to compensate class representatives for their work done on behalf of the class, to offset any financial and reputational risk, and to recognize their work as a private attorney general.

Incentive awards became commonplace by the turn of the twenty-first century. However, the legal basis for them was rarely, if ever, discussed. Courts would frequently dodge the opportunity to address the permissibility of incentive awards—until recently. Since the end of 2020, four circuit courts have addressed whether incentive awards should be categorically banned: a result that would severely impact the viability of class actions. Yet, rather than addressing this question by analyzing whether there is a legal basis for modern incentive awards, the courts have focused on the applicability of a pair of over-a-century old cases. Therefore, despite the attention that incentive awards have recently received, the legal basis for such awards remains unclear.

This Note seeks to provide the analysis that is missing: What, if any, is the legal basis giving courts authority to approve incentive awards to class representatives? In particular, this Note searches for a legal basis in Rules, common law, and principles of freedom of contract. Upon finding that incentive awards are legally permissible, this Note proposes a new framework for how courts should analyze incentive awards moving forward.

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Introduction

Incentive awards have taken center stage in the world of class actions. Over the last quarter-century, incentive awards have become increasingly prevalent.[1] Up until recently, courts had blindly approved incentive awards with little-to-no analysis.[2] The extent of a court's analysis had been limited to the rationale behind incentive awards: (1) to compensate for work done on behalf of the class, (2) to offset financial and reputational risk, and (3) to help ensure laws are enforced.[3] Few courts had stopped to consider what legal basis gives a court the authority to approve incentive awards.[4] However, this changed in 2020 with the Eleventh Circuit's decision in *Johnson v. NPAS Solutions*,[5] which held that incentive awards are per se unlawful.[6] Since then, three other circuits have paused, albeit briefly, to consider whether incentive awards are per se unlawful.[7]

1. *See* 5 WILLIAM B. RUBENSTEIN, NEWBERG AND RUBENSTEIN ON CLASS ACTIONS § 17:8 (6th ed., June 2023 update) (comparing empirical data from a 1993–2003 study to empirical data from a 2006–2011 study); *see also* Moses v. N.Y. Times Co., 79 F.4th 235, 253 (2d Cir. 2023) (collecting cases).

2. *See* Johnson v. NPAS Sols., LLC, 975 F.3d 1244, 1259 (11th Cir. 2020) (arguing that the widespread practice of incentive awards is "a product of inertia and inattention, not adherence to law").

3. Rodriguez v. W. Publ'g Corp., 563 F.3d 948, 958–59 (9th Cir. 2009).

4. *Johnson*, 975 F.3d at 1259.

5. 975 F.3d 1244 (11th Cir. 2020).

6. *Id.* at 1260.

7. Murray v. Grocery Delivery E-Servs. USA Inc., 55 F.4th 340, 352–54 (1st Cir. 2022); Hyland v. Navient Corp., 48 F.4th 110, 123–24 (2d Cir. 2022), *cert. denied*, 143 S. Ct. 1747 (2023); Moses v. N.Y. Times Co., 79 F.4th 235, 253–54, 256 (2d Cir. 2023); Named Plaintiffs v. Feldman (*In re* Apple Inc. Device Performance Litig.), 50 F.4th 769, 785–87 (9th Cir. 2022).

Despite the increased attention to the lawfulness of incentive awards since *Johnson*, no circuit has provided a comprehensive analysis examining the legal basis of incentive awards. Therefore, this Note seeks to provide an in-depth analysis of incentive awards. This Note begins in Part I with a discussion of the origin of incentive awards and a summary of the current circuit split. Next, in Part II, the Note dives into an analysis of the large, looming question: What, if anything, is the legal basis giving courts authority to approve incentive awards in class actions? Then, upon finding that there is a valid legal basis for incentive awards, Part III addresses and resolves concerns that are associated with incentive awards. Finally, Part IV tackles what test courts should apply when evaluating incentive awards.

I. History and Development of Incentive Awards

A. Origin of Incentive Awards

The practice of giving incentive awards originated through case law—not by rule or statute. The term "incentive award" was first used in a federal decision in 1987.[8] However, the practice of giving an award to a class representative was in place prior to the creation of the term incentive award. As noted in the 1987 decision, there was then-existing case law where named plaintiffs in securities class actions were receiving extra compensation.[9] Moreover, recent decisions debating the lawfulness of incentive awards have analyzed two Supreme Court cases from the 1880s, *Trustees v. Greenough*[10] and *Central Railroad & Banking Co. v. Pettus*,[11] which denied extra payment to class representatives.[12] Although the concept of giving class representatives extra payment is not new, it was not until the 1980s that incentive awards began to gain traction in class actions.[13] By the turn of the century, incentive awards were reported in 29.8% of class actions.[14] This was

8. 5 RUBENSTEIN, *supra* note 1, § 17:2 (citing *Re* Cont'l/Midatlantic S'holders Litig., No. 86–6872, 1987 WL 16678, at *4 (E.D. Pa. Sept. 1, 1987)).

9. *Re Continental*, 1987 WL 16678, at *4 (stating that plaintiffs' counsel "provided numerous citations in this district, in this circuit and elsewhere, in which substantial incentive payments to named plaintiffs in securities class action cases have been made").

10. 105 U.S. 527 (1882).

11. 113 U.S. 116 (1885); *see* discussion *infra* subpart I(B).

12. *See, e.g.*, Johnson v. NPAS Sols., LLC, 975 F.3d 1244, 1260 (11th Cir. 2020) (holding that *Greenough* and *Pettus* prohibit incentive awards).

13. *See, e.g.*, Bogosian v. Gulf Oil Corp., 621 F. Supp. 27, 32 (E.D. Pa. 1985) (granting awards of $20,000 to the two named class representatives); Troncelliti v. Minolta Corp., 666 F. Supp. 750, 752, 755 (D. Md. 1987) (holding that a settlement agreement, which included an additional award to the named plaintiff, was "fair, reasonable and adequate"); *In re* Dun & Bradstreet Credit Servs. Customer Litig., 130 F.R.D. 366, 374 (S.D. Ohio 1990) (approving various incentive awards in the amounts of $35,000 and $55,000).

14. Theodore Eisenberg & Geoffery P. Miller, *Incentive Awards to Class Action Plaintiffs: An Empirical Study*, 53 UCLA L. REV. 1303, 1311 n.18 (2006).

an increase of almost 50% compared to the frequency of incentive awards in class actions between 1993 and 1994.[15] Despite this increase, courts did not analyze whether there is a legal basis giving courts the authority to approve incentive awards—until recently.

B. Current Circuit Split

The proliferation of incentive awards over the last twenty-five years has sparked much debate about the lawfulness of such awards—especially recently. In just the last three and a half years, four circuit courts have chimed in on the ongoing debate of the lawfulness of incentive awards. Unsurprisingly, there is a circuit split. The basis of the circuit split is whether a specific set of Supreme Court cases, *Greenough* and *Pettus*, prohibit incentive awards. The circuit split started in 2020 when the Eleventh Circuit in *Johnson v. NPAS Solutions* held that *Greenough* and *Pettus* require a general ban on modern-day incentive awards.[16]

In *Greenough*, the Court struck down an award for "personal services and private expenses" given to a bondholder who brought suit on behalf of the other bondholders.[17] The Court reasoned that there was no legal authority for such an award and that allowing the award would encourage intermeddling of property or funds.[18] Similarly, in *Pettus*, the Court reaffirmed *Greenough* and struck down an award for personal services and private expenses given to a creditor who brought suit on behalf of other creditors.[19]

The Eleventh Circuit held that modern-day incentive awards are equivalent to the awards for "personal services and private expenses" in *Greenough* and *Pettus*.[20] Following this decision, three circuit courts have rejected the Eleventh Circuit's holding that *Greenough* and *Pettus* require that incentive awards are per se unlawful. The First Circuit, the Second Circuit (three times), and the Ninth Circuit have all held that *Greenough* and *Pettus* are distinguishable and thus don't generally prohibit incentive awards.[21]

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15. *Id.*

16. *Johnson*, 975 F.3d at 1260.

17. Trs. v. Greenough, 105 U.S. 527, 528, 537 (1882).

18. *Id.* at 537–38.

19. Cent. R.R. & Banking Co. v. Pettus, 113 U.S. 116, 124–25 (1885).

20. *Johnson*, 975 F.3d at 1257.

21. *See* Murray v. Grocery Delivery E-Servs. USA Inc., 55 F.4th 340, 352–53 (1st Cir. 2022) (noting that *Greenough* is distinguishable because it was concerned with a creditor's relationship with trustees rather than with the other creditors in the lawsuit and noting further that Rule 23 of the Federal Rules of Civil Procedure "ensures that incentive payments will not result in unfair settlements"); Hyland v. Navient Corp., 48 F.4th 110, 123–24 (2d Cir. 2022) (holding that *Greenough* and *Pettus* cannot require a per se ban on incentive awards because they do not "provide factual settings akin to those" present in the current case (quoting Melito v. Experian Mktg. Sols.,

While determining the applicability of *Greenough* and *Pettus* is relevant to the discussion of incentive awards, there is a larger looming question: What, if anything, is the legal basis giving courts the authority to approve incentive awards? When looking at the circuit split with this question in mind, the circuit split changes. The courts' arguments on the legality of incentive awards fall into one of three areas: (1) no argument at all; (2) the common fund doctrine; or (3) Rule 23 of the Federal Rules of Civil Procedure.

First, the First Circuit in *Murray*[22] and the Second Circuit in *Hyland v. Navient Corp.*[23] and *Fikes Wholesale, Inc. v. HSBC Bank USA*,[24] do not analyze the legality of incentive awards. However, this is unsurprising. During the rise of incentive awards, few courts addressed the legal basis for incentive awards.[25] In fact, incentive awards have been analogized to "dandelions on an unmowed lawn—present more by inattention than by design."[26] The First Circuit in *Murray* and the Second Circuit in *Hyland* and *Fikes* were not much different. The Second Circuit in *Hyland* and *Fikes* rejected the notion that *Greenough* prohibits incentive awards by citing a prior Second Circuit decision.[27] The prior circuit decision, *Melito v. Experian Marketing Solutions, Inc.*,[28] found that *Greenough* and *Pettus* were factually distinguishable from the present case and therefore rejected the argument that incentive awards are per se unlawful.[29] Similarly, the First Circuit in *Murray* distinguished *Greenough* and *Pettus*, arguing that the underlying policy concerns in those cases do not apply to modern incentive awards.[30] However, upon a finding that *Greenough* and *Pettus* are inapposite, neither of these Circuits addressed what legal basis gave the district courts the authority to approve the incentive award.

Inc., 923 F.3d 85, 96 (2d Cir. 2019))), *cert. denied*, 143 S. Ct. 1747 (2023); Fikes Wholesale, Inc. v. HSBC Bank USA, 62 F.4th 704, 721 (2d Cir. 2023) (rejecting *Greenough* and *Pettus* based on the precedent of *Melito* and *Hyland*); Moses v. N.Y. Times Co., 79 F.4th 235, 254, 256 (2d Cir. 2023) (holding that *Greenough* and *Pettus* have been superseded by the enactment of Rule 23); Named Plaintiffs v. Feldman (*In re* Apple Inc. Device Performance Litig.), 50 F.4th 769, 785–87 (9th Cir. 2022) (holding that *Greenough* and *Pettus* are consistent with approving incentive awards that are deemed "reasonable").

22. 55 F.4th 340, 353 (1st Cir. 2022).

23. 48 F.4th 110, 124 (2d Cir. 2022), *cert. denied*, 143 S. Ct. 1747 (2023).

24. 62 F.4th 704, 721 (2d Cir. 2023).

25. Greenberg v. Procter & Gamble Co. (*In re* Dry Max Pampers Litig.), 724 F.3d 713, 722 (6th Cir. 2013) ("[T]o the extent that incentive awards are common, they are like dandelions on an unmowed lawn—present more by inattention than by design.").

26. *Id.*

27. *Hyland*, 48 F.4th at 124; *Fikes*, 62 F.4th at 721.

28. 923 F.3d 85 (2d Cir. 2019).

29. *Id.* at 96.

30. Murray v. Grocery Delivery E-Servs. USA Inc., 55 F.4th 340, 352–53 (1st Cir. 2022).

Second, the Ninth Circuit and the Eleventh Circuit, both relying on *Greenough* and *Pettus*, illustrate that the common fund doctrine may play a role in the legality of incentive awards. *Greenough* and *Pettus* were the founding cases of the common fund doctrine.[31] The common fund doctrine holds "that persons who obtain the benefit of a lawsuit without contributing to its cost are unjustly enriched at the successful litigant's expense."[32] The Ninth Circuit in *In re Apple Inc. Device Performance Litigation*[33] relied on the common fund doctrine to support its holding that the district court had discretion to approve the incentive award.[34] Specifically, the Ninth Circuit held that as long as the incentive award is deemed "reasonable," it does not violate *Greenough* or *Pettus*.[35] By contrast, the Eleventh Circuit in *Johnson* held that *Greenough* and *Pettus* limit what a class representative can recover from the common fund doctrine.[36] The Eleventh Circuit held that a class representative may be reimbursed through the common fund for "expenses incurred in carrying on the litigation, but he cannot be paid a salary or be reimbursed for his personal expenses."[37] Therefore, both the Ninth Circuit and Eleventh Circuit illustrate that the common fund doctrine applies, but the Circuits disagree on the extent to which it applies.

Third, the Second Circuit in *Moses v. New York Times Co.*,[38] the Second Circuit's most recent decision concerning the validity of incentive awards, suggests Rule 23 of the Federal Rules of Civil Procedure may provide a legal basis for incentive awards. Rule 23 of the Federal Rules of Civil Procedure governs class actions, but it does not explicitly mention incentive awards.[39] Nevertheless, the Second Circuit held that Rule 23 provides the legal basis for incentive awards as long as the incentive award is "fair and appropriate."[40] Moreover, the Second Circuit used Rule 23 to dismiss the argument that *Greenough* and *Pettus* prohibit incentive awards.[41] The Second Circuit found that Rule 23 is the binding framework for class actions and thus supersedes *Greenough* and *Pettus*.[42] Therefore, the Second Circuit in *Moses*

31. Named Plaintiffs v. Feldman (*In re* Apple Inc. Device Performance Litig.), 50 F.4th 769, 785 (9th Cir. 2022).

32. Boeing Co. v. Van Gemert, 444 U.S. 472, 478 (1980).

33. 50 F.4th 769 (9th Cir. 2022).

34. *Id.* at 785–86.

35. *Id.* at 786–87.

36. Johnson v. NPAS Sols., LLC, 975 F.3d 1244, 1255–56, 1258–59 (11th Cir. 2020).

37. *Id.* at 1257.

38. 79 F.4th 235 (2d Cir. 2023).

39. *See generally* FED. R. CIV. P. 23 (laying the framework for class actions without directly referencing incentive awards).

40. *Moses*, 79 F.4th at 254.

41. *Id.*

42. *Id.* at 254–55.

relied on Rule 23 of the Federal Rules of Civil Procedure to provide a legal basis for incentive awards.

This circuit split illustrates that it remains unclear what legal basis, if any, gives courts the authority to approve incentive awards. Even in the cases that do directly address the legality of incentive awards head-on, the accompanying reasoning and analysis are sparse. Therefore, this Note seeks to find whether there is a legal basis for incentive awards and to fill in the gaps of the analysis that exists in current incentive award precedent.

II. The Legality of Incentive Awards

The first step in determining whether a class representative should be given an incentive award is whether a court has legal authority to approve such an award. There are four potential arguments for the legality of incentive awards: (1) the common fund doctrine; (2) Rule 23 of the Federal Rules of Civil Procedure; (3) freedom of contract; or (4) as an expense of the litigation. This Note will address each in turn.

A. Common Fund Doctrine

A frequently cited legal basis for incentive awards is the common fund doctrine. Originally created in courts of equity, the common fund doctrine is based on the theory of unjust enrichment—individuals benefiting from the common fund without contributing to the cost of the suit.[43] Thus, the common fund doctrine was established to support the recovery of attorney's fees from the common fund: "a litigant or a lawyer who recovers a common fund for the benefit of persons other than himself or his client is entitled to a reasonable attorney's fee from the fund as a whole."[44] By allowing an attorney to recover their fees from the common fund, it spreads the fees proportionally among the class members.[45]

Some courts have extended the common fund doctrine to provide legal support for incentive awards to class representatives.[46] These courts argue that the common fund doctrine allows reasonable incentive awards, which would include payments for litigation expenses and services provided to the

43. Boeing Co. v. Van Gemert, 444 U.S. 472, 478 (1980). *See also* Mills v. Elec. Auto-Lite Co., 396 U.S. 375, 392 (1970) (holding that "[t]o allow the others to obtain full benefit from the plaintiff's efforts without contributing equally to the litigation expenses would be to *enrich the others unjustly* at the plaintiff's expense") (emphasis added).

44. *Boeing*, 444 U.S. at 478.

45. *Id.*

46. *See, e.g.*, Named Plaintiffs v. Feldman (*In re* Apple Inc. Device Performance Litig.), 50 F.4th 769, 786 (9th Cir. 2022) (positing that "the common fund doctrine supports reasonable awards to a litigant"); *see also* Hadix v. Johnson, 322 F.3d 895, 898 (6th Cir. 2003) (collecting cases in which incentive awards were "viewed as extensions of the common-fund doctrine").

class.[47] However, the common fund doctrine should not be used as the legal basis that allows courts to approve incentive awards for two reasons.

First, the common fund doctrine should only be extended to professional fees. The common fund doctrine is based in restitution,[48] and the law of restitution is generally limited to professionals.[49] As Judge Posner analogized, "If you dive into a lake and save a drowning person, you are entitled to no fee."[50] Restitution is generally limited to professionals, such as doctors and lawyers, because their "contributions are subject to readily available and objective benchmarks of reasonableness that the market supplies a court."[51] However, there are no such objective benchmarks for the services that class representatives provide. The lack of objective benchmarks is illustrated by the vast range in the monetary value of incentive awards that have historically been approved for class representatives. Of a sample of over 300 class actions between 1993 and 2002 that permitted incentive awards, the average incentive award per class representative was $15,992 and the median per class representative was $4,357.[52] The fact that the average is much higher than the median demonstrates the size of incentive awards is skewed to the right—meaning there are outliers of high-value incentive awards.

Second, an award under the common fund doctrine would limit what could be considered part of an incentive award. Courts have used incentive awards to serve the following functions: (1) to compensate for work done on behalf of the class, (2) to offset financial and reputational risk, and (3) to help ensure laws are enforced.[53] However, because the common fund doctrine is based in restitution, it is limited to what is permitted under the theory of restitution. Restitution, as a remedy for unjust enrichment, requires that the other party received a *benefit* at the *expense* of the party seeking restitution.[54] Out of the three rationales for incentive awards, only compensation fits squarely in this definition. It is debatable how reputational risk can be quantified as an "expense" within the bounds of restitution. Similarly, a reward for helping enforce laws can't be quantified as a "benefit" to the unnamed plaintiffs. As a result, the common fund doctrine should not be used as a legal basis for incentive awards.

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47. *E.g.*, *In re Apple*, 50 F.4th at 786.

48. Steinlauf v. Cont'l Ill. Corp. (*In re* Cont'l Ill. Secs. Litig.), 962 F.2d 566, 571 (7th Cir. 1992).

49. *Id.* (citing 2 GEORGE E. PALMER, THE LAW OF RESTITUTION, ch. 10 (1978)).

50. *Id.*

51. *In re* U.S. Bioscience Sec. Litig., 155 F.R.D 116, 122 (E.D. Pa. 1994).

52. Eisenberg & Miller, *supra* note 14, at 1308.

53. Rodriguez v. W. Publ'g Corp., 563 F.3d 948, 958–59 (9th Cir. 2009).

54. RESTATEMENT (THIRD) OF RESTITUTION & UNJUST ENRICHMENT § 1 (AM. L. INST. 2011) ("A person who is unjustly enriched at the expense of another is subject to liability in restitution.").

B. Rule 23

Rule 23 of the Federal Rules of Civil Procedure governs class actions. Therefore, it is unsurprising that some courts have relied on Rule 23 when approving incentive awards.[55] Yet Rule 23 does not explicitly mention incentive awards or their equivalent. This has naturally led to two opposite conclusions: (1) dismissing Rule 23 as the legal basis for a court's authority to approve incentive awards because the plain text does not explicitly *permit* incentive awards;[56] and (2) arguing that Rule 23 provides the legal basis for a court to approve incentive awards because the plain text does not explicitly *prohibit* incentive awards.[57] However, both of these positions are incorrect.

Rule 23 cannot provide the legal basis for incentive awards because the Rules Enabling Act prohibits the Federal Rules of Civil Procedure from abridging, enlarging, or modifying any substantive right.[58] This is analogous to how Rule 23 gives the court discretion to award nontaxable expenses, but the court's legal authority to award those expenses is found outside of the Federal Rules of Civil Procedure.[59] Therefore, Rule 23 on its own cannot provide the legal basis for incentive awards. However, this does not make Rule 23 irrelevant when analyzing an incentive award. Instead, Rule 23 provides the framework for how a court should analyze an incentive award.[60]

C. Settlement Agreement

Additionally, it has been argued that a class action settlement agreement may provide independent authority for an incentive award.[61] Although parties independently negotiate a class action settlement agreement, Rule 23(e) requires that the settlement agreement have judicial approval to be legally binding.[62] Despite requiring court approval, the legal force behind settlement agreements comes from the parties' consent—not judicial

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55. *See, e.g.*, Murray v. Grocery Delivery E-Servs. USA Inc., 55 F.4th 340, 342–43 (1st Cir. 2022) (holding that incentive awards are permitted "as long as they fit within the bounds of Rule 23(e)").

56. *See, e.g.*, Johnson v. NPAS Sols., LLC, 975 F.3d 1244, 1259 (11th Cir. 2020) (holding that because Rule 23 does not explicitly mention incentive awards, it is irrelevant that Rule 23 post-dates *Greenough* and *Pettus*).

57. *See, e.g.*, Moses v. N.Y. Times Co., 79 F.4th 235, 254 (2d Cir. 2023) (arguing that Rule 23 does not forbid incentive awards, but rather, "permits fair and appropriate incentive awards").

58. 28 U.S.C. § 2072(b) ("Such rules [of practice and procedure] shall not abridge, enlarge or modify any substantive right.").

59. *See infra* subpart II(D).

60. *See infra* Part IV.

61. Benjamin Gould, Essay, *On the Lawfulness of Awards to Class Representatives*, 2023 CARDOZO L. REV. DE NOVO, 1, 13.

62. FED. R. CIV. P. 23(e) (stating that a class action "may be settled, voluntarily dismissed, or compromised *only with the court's approval*") (emphasis added).

approval.[63] Consequently, a settlement agreement is not limited by the restrictions of a court's remedial authority.[64]

Using a class action settlement agreement as the independent legal basis that furnishes authority to a court to approve an incentive award is consistent with a circuit court that has analyzed the legal basis for incentive awards. In *Hadix v. Johnson*,[65] the class consisted of a group of male prisoners who sued the prison claiming the conditions of the prison were unconstitutional.[66] After five years of litigation, the class entered into a consent decree with prison officials that sought to ensure constitutional conditions.[67] However, the consent decree "did not award damages, incentive awards, or costs to any of the individual plaintiffs."[68] Subsequently, the class representative sought an incentive award for his extensive work in the initial litigation, for monitoring the consent decree, and for various other litigation-related expenses.[69] However, the court affirmed the district court's denial of the incentive award because there was "neither authorization in the consent decree . . . nor a common fund from which it could be drawn."[70] Therefore, the court suggested that if the consent decree had included a provision for an incentive award, the district court would have had the authority to grant it. In other words, the settlement agreement would have provided an independent legal basis for the court to grant the incentive award. In conclusion, if parties consent to an incentive award in the settlement agreement, then a court would have legal authority to approve the incentive award—upon a finding that the settlement agreement is fair, reasonable, and adequate.[71]

D. Expense of the Litigation

Some have argued that courts have the authority to approve an incentive award as an expense of the litigation.[72] To an extent, this may be true. It depends on what types of "expenses" the incentive award is reimbursing. There are two types of litigation expenses: taxable costs and nontaxable costs.[73]

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63. Gould, *supra* note 61, at 13 (citing Loc. No. 93, Int'l Ass'n of Firefighters v. City of Cleveland, 478 U.S. 501, 525 (1986)).

64. *Id.* at 14 (citing *Firefighters*, 478 U.S. at 526).

65. 322 F.3d 895 (6th Cir. 2003).

66. *Id.* at 896.

67. *Id.*

68. *Id.*

69. *Id.*

70. *Id.* at 898.

71. *See infra* Part IV.

72. *See* Steinlauf v. Cont'l Ill. Corp. (*In re* Cont'l Ill. Secs. Litig.), 962 F.2d 566, 571 (7th Cir. 1992) (positing that incentive awards could be thought of as "the equivalent of the lawyers' nonlegal but essential case-specific expenses, such as long-distance phone calls, which are reimbursable").

73. 5 RUBENSTEIN, *supra* note 1, § 16:1.

Taxable costs are defined very narrowly. A court has procedural discretion to approve taxable costs as outlined in Rule 54 of the Federal Rules of Civil Procedure: "Unless a federal statute, these rules, or a court order provides otherwise, costs—other than attorney's fees—should be allowed to the prevailing party."[74] However, Rule 54 is limited to the costs enumerated in 28 U.S.C. § 1920.[75] The costs enumerated in § 1920 are:

> (1) Fees of the clerk and marshal;
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> (2) Fees for printed or electronically recorded transcripts necessarily obtained for use in the case;
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> (3) Fees and disbursements for printing and witnesses;
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> (4) Fees for exemplification and the costs of making copies of any materials where the copies are necessarily obtained for use in the case;
>
> (5) Docket fees under section 1923 of this title;
>
> (6) Compensation of court appointed experts, compensation of interpreters, and salaries, fees, expenses, and costs of special interpretation services under section 1828 of this title.[76]

Thus, an incentive award is only permitted as a taxable cost if it falls in one of those six buckets. But incentive awards likely cover much more than just taxable costs. As a result, the legal basis for an incentive award cannot solely rely on the legality of taxable costs.

In contrast to taxable costs, nontaxable costs are not explicitly defined. Rule 23(h) of the Federal Rules of Civil Procedure permits a court discretion to "award reasonable attorney's fees *and nontaxable costs* that are authorized by law or by the parties' agreement."[77] But Rule 23(h) does not provide legal authority for nontaxable costs—they must be "authorized by law or by the parties' agreement."[78] Thus, defining an incentive award as a nontaxable cost leaves us with the same issue: What is the legal basis for a court's authority to award nontaxable costs?

The legal authority for nontaxable costs generally comes from the common fund doctrine, fee-shifting statutes, or settlement agreements.[79] First, as previously discussed, the common fund doctrine should not be used as a legal basis for incentive awards because restitution is limited to professionals. Second, if a fee-shifting statute applies, an incentive award is

74. FED. R. CIV. P. 54(d)(1).

75. Crawford Fitting Co. v. J. T. Gibbons, Inc., 482 U.S. 437, 441–42 (1987) ("Section 1920 enumerates expenses that a federal court may tax as a cost under the discretionary authority found in Rule 54(d).").

76. 28 U.S.C. § 1920.

77. FED. R. CIV. P. 23(h) (emphasis added).

78. *Id.*

79. 5 RUBENSTEIN, *supra* note 1, § 16:1.

limited to "out-of-pocket expenses that 'would normally be charged to a fee-paying client.'"[80] This definition would likely not extend to incentive awards that include payments to offset the financial and reputational risks that a class representative took to bring the suit. Third, if the settlement agreement provides for nontaxable expenses, a court would have the authority to approve the incentive award, as discussed above, as long as it is "fair, reasonable, and adequate."[81] However, the definition of "nontaxable expense" would likely cause debate. How broadly or narrowly to define a nontaxable expense would be limited to what the parties agreed upon, or in the absence of an agreed definition, principles of contract interpretation. In conclusion, defining an incentive award as a nontaxable expense does not directly provide a legal basis for the incentive award. Instead, it simply reframes the question of "what is the legal basis giving a court authority to approve an *incentive award*," to "what is the legal basis giving a court authority to approve a *nontaxable expense*"?

In summary, of the four potential legal bases for incentive awards, relying on the settlement agreement provides the strongest legal basis. The common fund doctrine should not be used as a legal basis for incentive awards because restitution only applies to professionals and the doctrine would severely limit what types of payments would be permissible as an incentive award. Moreover, defining an incentive award as an expense of the litigation does not help because taxable costs are very limited, and a court would similarly need a legal basis for approving nontaxable costs. Upon finding that there is at least one legal basis for incentive awards, this Note will now address—and resolve—concerns that suggest a court may nevertheless want to refuse incentive awards.

III. Addressing Concerns with Incentive Awards

Opponents of incentive awards will argue that despite any legal basis, courts should refuse to approve incentive awards for three reasons. First, an incentive award would be a per se violation of Rule 23(e)(2). Second, incentive awards would violate Supreme Court precedent in *Greenough* and *Pettus*. Third, incentive awards carry the potential for abuse. This Note will address why each of these concerns are unfounded.

80. Dang v. Cross, 422 F.3d 800, 814 (9th Cir. 2005) (quoting Harris v. Marhoefer, 24 F.3d 16, 19 (9th Cir. 1994)). Many other courts have adopted similar requirements for nontaxable costs in fee-shifting cases. *See* 5 WILLIAM B. RUBENSTEIN, NEWBERG AND RUBENSTEIN ON CLASS ACTIONS § 16:5 (6th ed., Nov. 2023 update) (collecting cases).

81. *See* FED. R. CIV. P. 23(e)(2) (stating that a court may approve a settlement agreement only if the court finds the agreement to be "fair, reasonable, and adequate").

A. Rule 23

Rule 23(e)(2) holds that a court may approve a settlement agreement, which may include an incentive award, "only on finding that [the settlement agreement] is fair, reasonable, and adequate."[82] A likely counterargument to incentive awards is that incentive awards violate the "fair, reasonable, and adequate" requirement of Rule 23. However, an analysis of the 2018 amendment to Rule 23 and other legislative history proves that incentive awards are not a per se violation of Rule 23(e)(2).

1. 2018 Amendment.—The 2018 Amendment to Rule 23(e)(2) supports that incentive awards are not a per se violation of the "fair, reasonable, and adequate" requirement. Prior to 2018, a court could only approve a settlement proposal upon a finding that the settlement proposal was "fair, reasonable, and adequate."[83] The 2018 Amendment elaborated on this requirement. Specifically, it added four factors that a court must consider when determining whether a settlement proposal is fair, reasonable, and adequate:

> (A) the class representatives and class counsel have adequately represented the class;
>
> (B) the proposal was negotiated at arm's length;
>
> (C) the relief provided for the class is adequate . . . ; and
>
> (D) the proposal treats class members equitably relative to each other.[84]

Subsections (A) and (B) focus on "procedural" concerns while subsections (C) and (D) address the "substantive" concerns of the proposed settlement.[85] The factors addressing the substantive concerns are especially relevant to the legality of incentive awards. Subsections (C) and (D) both illustrate that incentive awards would not be a per se violation of Rule 23(e)(2) for three reasons.

First, the notion that an incentive award is not a traditional form of "relief" is not a per se violation of Rule 23(e)(2). Generally, a class member's entitlement to relief from the class recovery is based on their claim against the defendant.[86] Therefore, opponents may argue that class members are only entitled relief for damages caused by the defendant, which incentive awards are not. However, the substantive concerns addressed by subsections (C) and

82. *Id.*

83. FED. R. CIV. P. 23(e)(2) (2012) (amended 2018).

84. FED. R. CIV. P. 23(e)(2).

85. FED. R. CIV. P. 23(e)(2) advisory committee's note to 2018 amendment.

86. *See* Boeing Co. v. Van Gemert, 444 U.S. 472, 480 (1980) (explaining that to recover from the common fund, a class member only needs to prove their membership in the class).

(D) are not solely limited to concerns of relief. Rather, subsection (D) focuses on the proposal as a whole. Compare subsections (C) and (D). In subsection (C), the focus is on relief: "the *relief* provided for the class is adequate."[87] By contrast, subsection (D) focuses on the proposal: "the *proposal* treats class members equitably."[88] Making sure the entire proposal treats class members equitably requires the court to go beyond the amount of relief distributed to each class member. Arguably, subsection (D) encourages the court to approve incentive payments. If a class representative spent more time, effort, and money bringing the suit on behalf of the class, they should be compensated accordingly. If not, the class representative is arguably not being treated equitably, as required by Rule 23(e)(2)(D).[89]

Second, "equitable" in subsection (D) does not mean equal.[90] Equitable is defined as "characterized by equity or fairness; just and right; fair."[91] As the definition illustrates, equity is focused on fairness rather than equality alone. Additionally, the Advisory Committee acknowledges that proposals likely will, and perhaps should, treat class members unequally. In the Advisory Committee's notes to the 2018 Amendment, the Committee suggests that when courts are evaluating whether the proposal treats class members equitably, a court should consider "whether the apportionment of relief among class members takes appropriate account of *differences* among their claims."[92] Logically, a difference among claims would produce a difference in the amount of relief distributed. As a result, the mere fact that an incentive award produces a higher overall distribution from the class recovery for a class representative is not a per se violation of Rule 23(e)(2).

Third, the fact that an incentive award will decrease the total available class recovery is not a per se violation of Rule 23(e)(2). In evaluating whether the proposal treats members equitably, the Advisory Committee suggests that if there is "inequitable treatment of some class members vis-à-vis others" a court should consider "whether the scope of the release may affect class

87. FED. R. CIV. P. 23(e)(2)(C) (emphasis added).

88. FED. R. CIV. P. 23(e)(2)(D) (emphasis added).

89. *See* 5 RUBENSTEIN, *supra* note 1, § 17:4 (arguing that if a class representative "cannot recover any of the costs of those efforts [undertaken for the class] through an incentive award, they have a fair argument that the settlement is not treating them *equitably* relative to the absent class members").

90. Moses v. N.Y. Times Co., 79 F.4th 235, 245 (2d Cir. 2023) (stating that "Rule 23(e)(2)(D) requires that class members be treated *equitably*, not identically").

91. *Equitable*, DICTIONARY.COM, https://www.dictionary.com/browse/equitable [https://perma.cc/SWM4-4UWE]; *see also Equitable*, MERRIAM-WEBSTER, https://www.merriam-webster.com/dictionary/equitable [https://perma.cc/ZX5J-7X3E] (defining "equitable" as "having or exhibiting equity," or "dealing *fairly* and equally with all concerned," thereby showing that equality is not the only consideration in determining what is equitable (emphasis added)).

92. FED. R. CIV. P. 23(e)(2)(D) advisory committee's note to 2018 amendment (emphasis added).

members in different ways that bear on the apportionment of relief."[93] Consequently, as long as a court considers the incentive awards in light of the adequacy of the rest of the class members' relief, approving the incentive award would not violate Rule 23(e)(2).[94] In fact, Rule 23(e)(2) mandates a similar analysis as it relates to attorney fees: "the relief provided for the class is adequate, taking into account . . . the terms of any proposed award of attorney's fees."[95] Therefore, an incentive award is not a per se violation of Rule 23(e)(2). Instead, Rule 23(e)(2) will help guide the courts in formulating a standard under which to analyze the fairness of incentive awards.[96]

2. Private Securities Litigation Reform Act and Class Action Fairness Act.—Other statutes passed by Congress can also help interpret the scope of Rule 23: the Private Securities Litigation Reform Act and the Class Action Fairness Act. The Federal Rules of Civil Procedure are not statutes, and thus, the general rules of statutory interpretation do not mandate the interpretation of the Rules.[97] Nevertheless, the Supreme Court has previously interpreted Rule 23 according to general principles of statutory interpretation.[98] Moreover, although the Rules Enabling Act authorizes the Supreme Court to prescribe rules of procedure, Congress promulgates the proposed rules.[99] Therefore, it would be consistent with the Supreme Court's Rules-as-statutes approach to consider related statutes when analyzing Rule 23.[100]

First, Congress passed the Private Securities Litigation Reform Act of 1995, which directly addressed incentive awards.[101] Congress prohibited any

93. *Id.*

94. *See Moses*, 79 F.4th at 243–44 (holding that the district court erred by failing to consider the incentive award when evaluating the settlement agreement under Rule 23(e)(2)'s "fair, reasonable, and adequate" requirement).

95. FED. R. CIV. P. 23(e)(2)(C)(iii).

96. *See* discussion *infra* Part IV.

97. *Cf.* Elizabeth G. Porter, *Pragmatism Rules*, 101 CORNELL L. REV. 123, 136 (2015) (arguing that the Roberts Court switched between statutory interpretation and "managerial interpretation" techniques when interpreting the Federal Rules of Civil Procedure).

98. *See* Shady Grove Orthopedic Assocs., P.A. v. Allstate Ins. Co., 559 U.S. 393, 398–400 (2010) (employing traditional statutory interpretation techniques to understand Rule 23, including analyzing the impact of its exceptions); *see also* Porter, *supra* note 97, at 136 (positing that the plurality in *Shady Grove* interpreted Rule 23 according to "routine statutory interpretation").

99. 28 U.S.C. §§ 2072, 2074 (giving the Supreme Court the power to prescribe "general rules of practice and procedure" in 28 U.S.C. § 2072(a) but requiring in 28 U.S.C. § 2074(b) that Congress approve such rules in order to give them force and effect). For a discussion of the current rulemaking process for the Federal Rules of Civil Procedure, see Peter G. McCabe, *Renewal of the Federal Rulemaking Process*, 44 AM. U. L. REV. 1655, 1670–74 (1995).

100. *See* Erlenbaugh v. United States, 409 U.S. 239, 243 (1972) (arguing that statutes addressing the same topic should be read "as if they were one law" (quoting United States v. Freeman, 44 U.S. (3 How.) 556, 564 (1845))).

101. Private Securities Litigation Reform Act of 1995, Pub L. No 104-67, sec. 101, § 27(a)(2)(A)(vi), 109 Stat. 737, 738 (codified at 15 U.S.C. § 78u-4(a)(2)(A)(vi)).

class representative in a private securities class action from accepting "any payment for serving as a representative party on behalf of a class . . . except as ordered or approved by the court."[102] In limiting the availability of incentive awards in private securities class actions, Congress sought to minimize "abusive class action litigation."[103] Specifically in private securities litigation, there was a concern about "professional" plaintiffs.[104] Congress sought to deter professional plaintiffs by removing their motivation: an incentive award.[105] However, the professional plaintiff concern does not extend beyond private securities class actions. For example, in an empirical study of class actions across four federal district courts between July 1, 1992, and June 30, 1994, there was a class representative "repeat player" in less than 2% of cases.[106]

Moreover, the restriction on incentive awards in private securities class actions is not a complete ban. A court may approve additional payment to a class representative for "reasonable costs and expenses (including lost wages) directly relating to the representation of the class."[107] Congress acknowledged that the role of class representative may require extra responsibilities such as court appearances, which could result in time away from work.[108] Consequently, Congress refused to implement a complete ban on any payment in excess of a class representative's pro rata share of the class recovery. Therefore, the legislative purpose behind the PSLRA illustrates that Rule 23 should not be interpreted in a way that would make an incentive award a per se violation of Rule 23(e)(2).

Second, Congress passed the Class Action Fairness Act of 2005 (CAFA) to ensure "fairer outcomes for class members and defendants."[109] Congress observed that one of the abuses of the class action device was that "unjustified awards are made to certain plaintiffs at the expense of other class members."[110] Despite this, Congress failed to place a categorical ban on incentive awards in the CAFA.[111] This is a stark contrast to Congress's choice

102. 15 U.S.C. § 78u-4(a)(2)(A)(vi).

103. S. REP. NO. 104-98, at 10 (1995).

104. *Id.*

105. *Id.*

106. Thomas E. Willging, Laural L. Hooper & Robert J. Niemic, *An Empirical Analysis of Rule 23 to Address the Rulemaking Challenges*, 71 N.Y.U. L. REV. 74, 99 (1996) (analyzing 353 class representatives from 141 class actions, the study found "duplicate appearances by four individuals and one corporation"); *see also* Eisenberg & Miller, *supra* note 14, at 1310 ("[W]e find little evidence of systematic abuse of incentive awards.").

107. 15 U.S.C. § 78u-4(a)(4).

108. S. REP. NO. 104-98, at 10 (1995).

109. Class Action Fairness Act of 2005, Pub. L. No. 109-2, 119 Stat. 4.

110. *Id.* § 2(a)(3)(B), 119 Stat. at 4.

111. Johnson v. NPAS Sols., LLC, 43 F.4th 1138, 1148 (11th Cir. 2022) (Pryor, J., dissenting from denial of rehearing en banc).

to limit incentive awards in the PSLRA—ten years prior to the passing of the CAFA.[112] Refusing to categorically ban incentive awards may illustrate that Congress believed that some incentive awards could be justified outside of the private securities litigation context. Therefore, the CAFA, in addition to the PSLRA, supports the argument that incentive awards should not be categorically banned under Rule 23, either. Instead, incentive awards should be permitted upon a finding that the incentive award is justified.

In conclusion, incentive awards are not a per se violation of Rule 23(e)(2). Rule 23 simply requires that the settlement agreement treat class members equitably relative to each other. Failing to approve an incentive award to a class representative arguably treats them unfairly given the additional work that is required of class representatives compared to unnamed plaintiffs. Moreover, giving courts discretion under Rule 23(e)(2) to approve incentive awards does not run afoul of Congress's policy towards incentive awards. The Private Securities Litigation Reform Act and Class Action Fairness Act demonstrate that Congress was unwilling to place a categorical ban on incentive awards in every class action. As a result, incentive awards should not be interpreted to be a per se violation of the "fair, reasonable, and adequate" requirement under Rule 23.

B. Greenough *and* Pettus

Permitting incentive awards does not violate Supreme Court precedent. As previously mentioned, the current circuit split regarding incentive awards revolves around whether *Greenough* and *Pettus* mandate that incentive awards are per se unlawful.[113] When considering the reasoning behind the decisions in *Greenough* and *Pettus*, it is clear that a categorical ban on incentive awards in modern-day class actions would be inappropriate. In fact, allowing courts discretion to approve incentive awards under Rule 23(e)(2) would be consistent with *Greenough* and *Pettus*.

Although *Greenough* and *Pettus* are both cited in the circuit split, the substance of the analysis comes from *Greenough*. With respect to incentive awards, *Pettus* reaffirms *Greenough* but does not expand on the analysis.[114]

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112. 15 U.S.C. § 78u-4(a)(2)(A)(vi).

113. *Compare* Johnson v. NPAS Sols., LLC, 975 F.3d 1244, 1257–59 (11th Cir. 2020) (holding that *Greenough* and *Pettus* prohibit incentive awards), *with* Murray v. Grocery Delivery E-Servs. USA Inc., 55 F.4th 340, 352–53 (1st Cir. 2022) (rejecting the argument that *Greenough* and *Pettus* require a categorical ban on incentive awards), Hyland v. Navient Corp., 48 F.4th 110, 123–24 (2d Cir. 2022) (same), *cert. denied*, 143 S. Ct. 1747 (2023), Moses v. N.Y. Times Co., 79 F.4th 235, 254–56 (2d Cir. 2023) (same), *and* Named Plaintiffs v. Feldman (*In re* Apple Inc. Device Performance Litig.), 50 F.4th 769, 785–86 (9th Cir. 2022) (same).

114. Cent. R.R. & Banking Co. v. Pettus, 113 U.S. 116, 124 (1885) ("[W]ithin the principles announced in *Trustees v. Greenough*, [the plaintiffs] are entitled to be allowed, out of the property thus brought under the control of the court, for all expenses properly incurred in the preparation and conduct of the suit . . . .").

Therefore, the focus here will be on the facts and analysis of *Greenough*. In *Greenough*, Francis Vose, a bondholder of the Florida Railroad Company, sued the trustees of the Internal Improvement Fund of Florida on behalf of himself and other bondholders.[115] The basis of the suit was that the trustees of the Internal Improvement Fund of Florida were selling land that was part of the trust at "nominal prices," thus destroying the fund.[116] In bringing the suit, Vose "bore the whole burden of [the] litigation, and advanced most of the expenses."[117] As a result, Vose sought a distribution from the fund for his "expenses and services."[118]

In reviewing Vose's award, the Supreme Court approved it in part and denied it in part.[119] The Court permitted reimbursement for "reasonable costs, counsel fees, charges, and expenses incurred in the fair prosecution of the suit" but barred reimbursement for "personal services and private expenses."[120] The Court's reasoning for denying personal services and expenses was two-fold. First, the Court held that there was no authority permitting reimbursement for personal services and private expenses.[121] Second, the Court refused payment for personal services and private expenses because of the potential for abuse: "a temptation to parties to intermeddle in the management of valuable property or funds in which they have only the interest of creditors."[122]

However, neither of the Court's two reasons are applicable to modern-day incentive awards. First, as discussed in subpart II(C), a settlement agreement between parties provides the legal basis for incentive awards. Such an agreement was not present in *Greenough*. If a settlement agreement includes a provision for "personal services and private expenses," the court has legal authority to approve it, upon finding that it is "fair, reasonable, and adequate." Second, the Court's concern that incentive awards encourage baseless meddling is unfounded because an incentive award is only available to prevailing parties. If the meddling is baseless, the party will not prevail. Moreover, Rule 23 also protects against baseless meddling. Rule 23 requires that a settlement be "fair, reasonable, and adequate," which considers whether the class representatives "adequately represented the class."[123] Therefore, if the court finds a class representative acted imprudently for their own benefit, the court has the discretion to strike the incentive award. Thus,

115. Trs. v. Greenough, 105 U.S. 527, 528 (1882).
116. *Id.* at 528–29.
117. *Id.* at 529.
118. *Id.*
119. *Id.* at 537.
120. *Id.*
121. *Id.*
122. *Id.* at 538.
123. FED. R. CIV. P. 23(e)(2).

the Court's reasoning in *Greenough* is not applicable to modern-day incentive awards. As a result, giving a court discretion to approve incentive awards under Rule 23 does not violate *Greenough* or *Pettus*.

C. Policy Concerns

Some argue that even if there is a legal basis for incentive awards, judges should nevertheless refuse to approve them because of concerns about potential abuses. There are two main abuses concerned with incentive awards: conflicts of interest and incentivizing litigation. However, Rule 23 provides protections against these abuses. Therefore, a court should not categorically ban incentive awards based just on the fear of potential abuses.

1. Conflicts of Interest.—It has been argued that incentive awards create a conflict of interest between class representatives and the class members.[124] If a class representative expects an incentive award, they might prioritize bargaining for an incentive award at the expense of the overall class settlement. This is analogous to the dangers of lawyers negotiating their fees as part of a settlement agreement. If lawyers were to negotiate their fees at the expense of relief for the class, the lawyers would have created a conflict of interest and simultaneously violated their fiduciary duty to the class.[125] If class representatives know that they are only entitled to an incentive award if it is a part of the settlement agreement, they might bargain for an incentive award at the expense of a better overall class recovery.

While this is a valid concern, it should not lead to a general ban on incentive awards for two reasons. First, Rule 23 allows court discretion to strike down an incentive award upon a finding of a conflict of interest. Specifically, Rule 23 conditions the approval of a settlement agreement on finding that the class representative "adequately represented the class."[126] Striking down an incentive award based on a finding that the class representative did not adequately represent the class is not a novel concept among courts.

In *Greenberg v. Procter & Gamble Co.*,[127] a class brought an action against a manufacturer of diapers.[128] The suit alleged that a specific line of diapers was causing a severe diaper rash.[129] The class action resulted in a

124. *See, e.g.*, Chieftain Royalty Co. v. Enervest Energy Inst'l Fund XIII–A, L.P., 888 F.3d 455, 468–69 (10th Cir. 2017) (rejecting a percentage-based incentive award because it "creat[ed] a potential conflict between the interest of the class representative and the class" (quoting 5 RUBENSTEIN, *supra* note 1, § 17:16)).

125. Gould, *supra* note 61, at 15.

126. FED. R. CIV. P. 23(e)(2)(A).

127. 724 F.3d 713 (6th Cir. 2013).

128. *Id.* at 715.

129. *Id.*

settlement agreement that provided that the manufacturer would implement a one-box refund program and include additional information about diaper rashes on both the diaper box and website.[130] While the one-box refund was the only relief provided for the unnamed plaintiffs, the settlement agreement provided that class representatives would receive an award of $1,000 "per affected child."[131]

The Sixth Circuit struck down the incentive award because it created a conflict of interest.[132] Specifically, the Court held that the $1,000-per-affected-child award "encouraged the class representatives 'to compromise the interest of the class for personal gain.'"[133] As a result, the court held that the class representatives did not adequately represent the class under Rule 23.[134] Thus, Rule 23 provides protections against inadequate representation. Therefore, rather than placing a general ban on incentive awards due to the potential of a conflict of interest, a court should simply screen for it when deciding whether to approve the incentive award under Rule 23.

Second, courts can mandate procedural requirements that may decrease the potential for a conflict of interest to arise during settlement negotiations. Specifically, a court could prohibit any negotiation of an incentive award until the substantive terms of the settlement agreement have been established. Delaying discussions of incentive awards until after the substantive terms have been established takes away the class representative's ability to bargain for an incentive award at the expense of a better overall settlement for the class. In fact, the Fourth Circuit has considered the timing of the negotiation of an incentive award when reviewing whether a class representative adequately represented the class.

In *Berry v. Schulman*,[135] a class sued Lexis, alleging that Lexis had violated the Fair Credit Reporting Act.[136] The class action resulted in a settlement agreement that provided injunctive relief to the class and $5,000 incentive awards to the class representatives.[137] Despite class representatives receiving monetary awards while unnamed class members received what some might consider only perfunctory relief, the court upheld the incentive award.[138] The court upheld the award because, among other things, the incentive awards were negotiated after the substantive terms of the agreement

130. *Id.* at 716.
131. *Id.*
132. *Id.* at 722.
133. *Id.* (quoting Hadix v. Johnson, 322 F.3d 895, 897 (6th Cir. 2003)).
134. *Id.*
135. 807 F.3d 600 (4th Cir. 2015).
136. *Id.* at 606.
137. *Id.* at 607–08.
138. *Id.* at 614.

had been established, thus "making it significantly less likely that the Class Representatives would have been influenced in the performance of their representative duties."[139] As a result, the court found that the class representatives adequately represented the class under Rule 23.[140] Therefore, requiring negotiations of incentive awards to take place after the substantive terms of the agreement have been reached, or at least considering the timing as a factor when analyzing adequacy under Rule 23, will help mitigate the effect of potential conflicts of interest.

2. Incentivizing Litigation.—Another concern associated with incentive awards is that the awards will incentivize litigation. An incentive award, as its name suggests, is partially used to incentivize class representatives to participate in the suit.[141] This incentive is important because a class action *requires* a class representative.[142] Despite this, the concern is that incentive awards create a "bounty," therefore improperly promoting litigation.[143] However, this concern should not justify a categorical ban on incentive awards for three reasons.

First, if the concern is that incentive awards will promote *frivolous* litigation, there are several protections already in place to deter this behavior. These protections deter not only the class representative but the class action lawyer as well. A class representative is deterred from participating in a frivolous class action because there is a risk of being held solely liable for the attorney's fees.[144] Additionally, a lawyer is deterred from promoting frivolous litigation by both rules of professional conduct and rules of procedure. The Model Rules of Professional Conduct, which many states model their professional rules after, hold that a lawyer is subject to discipline for bringing a frivolous claim: "A lawyer shall not bring or defend a proceeding . . . unless there is a basis in law and fact for doing so that is not frivolous . . . ."[145] Similarly, the Federal Rules of Civil Procedure also provide protection against frivolous claims. When a lawyer files a pleading, they certify that "the claims, defenses, and other legal contentions are

139. *Id.*

140. *Id.*

141. *See* Steinlauf v. Cont'l Ill. Corp. (*In re* Cont'l Ill. Secs. Litig.), 962 F.2d 566, 571 (7th Cir. 1992) ("Since without a named plaintiff there can be no class action, such compensation as may be necessary to induce him to participate in the suit could be thought the equivalent of the lawyers' nonlegal but essential case-specific expenses . . . which are reimbursable.").

142. FED. R. CIV. P. 23(a) ("One or more members of a class may sue or be sued as *representative parties* on behalf of all members . . . .") (emphasis added).

143. Johnson v. NPAS Sols., LLC, 975 F.3d 1244, 1258 (11th Cir. 2020).

144. Espenscheid v. DirectSat USA, LLC, 688 F.3d 872, 876 (7th Cir. 2012) ("[A] class action plaintiff assumes a risk; should the suit fail, he may find himself liable for the defendant's costs or even, if the suit is held to have been frivolous, for the defendant's attorneys' fees.").

145. MODEL RULES OF PRO. CONDUCT r. 3.1 (AM. BAR ASS'N 2023).

warranted by existing law."[146] If a lawyer violates Rule 11, they are subject to sanctions.[147] Therefore, any concern that an incentive award will promote frivolous litigation is unfounded because there are already substantial deterrents for such behavior.

Second, if the concern is that incentive awards will promote litigation *in general*, it is not clear why that should be a concern. In fact, the expansion of Rule 23(b) in 1966 arguably promoted litigation. Under Rule 23(b)(3), a class action could be certified if "the court finds that the questions of law or fact common to class members predominate over any questions affecting only individual members, and that a class action is superior to other available methods for fairly and efficiently adjudicating the controversy."[148] Therefore, Rule 23(b)(3) made it economically viable to pursue low-value claims.[149] Without the class action device, many individuals would not litigate their claims because the cost of litigation would have outweighed their recovery.[150] As a result, the enactment of Rule 23(b)(3) promoted litigation because it provided a mechanism for plaintiffs to litigate claims they otherwise would not have pursued.

Moreover, there are statutory whistleblower provisions that arguably promote litigation as well. For example, the Dodd-Frank Wall Street Reform and Consumer Protection Act permits that upon successful enforcement of a provision of the Act, a whistleblower may be paid anywhere from 10–30% percent of "what has been collected of the monetary sanctions imposed in the action."[151] The purpose of rewarding whistleblowers is to help identify securities law violations.[152] Therefore, the Dodd-Frank Act promotes litigation by incentivizing whistleblowers to bring violations forward. Similarly, an incentive award motivates a class representative to participate in a class action for the purpose of holding defendants accountable for their actions. As a result, the notion that an incentive award "promotes litigation" in general should not be a concern.

Third, whatever downfalls promoting litigation is believed to create, the alternative is worse. Placing a general ban on incentive awards affects the viability of class actions.[153] Without an incentive award, a class member may be less likely to fill the role of class representative based on the potential

146. FED. R. CIV. P. 11(b)(2).

147. FED. R. CIV. P. 11(c).

148. Fed. R. Civ. P. 23(b)(3).

149. *See* Phillips Petroleum Co. v Shutts, 472 U.S. 797, 809 (1985) ("Class actions also may permit the plaintiffs to pool claims which would be uneconomical to litigate individually.").

150. *See, e.g.*, *id.* ("[T]his lawsuit involves claims averaging about $100 per plaintiff; most of the plaintiffs would have no realistic day in court if a class action were not available.").

151. 15 U.S.C. § 78u-6(b).

152. Digit. Realty Tr., Inc. v. Somers, 138 S. Ct. 767, 773 (2018).

153. Johnson v. NPAS Sols., LLC, 43 F.4th 1138, 1140 (11th Cir. 2022) (Pryor, J., dissenting from denial of rehearing en banc).

financial and reputational risks.[154] Without a class representative, the class action cannot be pursued. Not only will this hurt potential class members, but it will also hurt the general public. Potential class members are hurt because without a class representative, the class action cannot proceed, and as a result, class members will never be able to obtain relief. As previously mentioned, class actions make it possible to pursue low-value claims that would not have been litigated otherwise.[155] Moreover, the general public will be harmed because guilty defendants will be able to escape liability. Without liability, there is no deterrent against continued wrongful behavior.[156] Therefore, banning incentive awards will impact the sustainability of class actions, which serve both compensatory and deterrent functions. Losing those functions is worse than concerns of "promoting litigation."

In conclusion, incentive awards should not be categorically prohibited based on fears of conflicts of interest or concerns about promoting litigation. There are several protections in place that will guard against conflicts of interest and frivolous litigation. Moreover, promoting non-frivolous litigation should not be a concern because the class action device properly compensates plaintiffs and deters unlawful conduct. If incentive awards were generally prohibited, it would destroy class actions.

IV. A New Standard for Approving Incentive Awards

Determining whether incentive awards are legally permissible does not end the analysis. A court must also determine whether the size of the incentive award is appropriate. Given that Rule 23 governs the procedure for approving settlement proposals in class actions, a court must determine whether an incentive award is appropriate in light of Rule 23. In fact, Rule 23 provides the framework for how a court should analyze an incentive award. Specifically, a court must determine whether the incentive award is "fair, reasonable, and adequate."[157] As previously mentioned, Rule 23 provides four factors that a court must consider:

> (A) the class representatives and class counsel have adequately represented the class;
>
> (B) the proposal was negotiated at arm's length;

154. *See* Rodriguez v. W. Publ'g Corp., 563 F.3d 948, 958–59 (9th Cir. 2009) (stating that one of the purposes of incentive awards, among others, is to "make up for financial or reputational risk undertaken in bringing the action").

155. *See* Phillips Petroleum Co. v Shutts, 472 U.S. 797, 809 (1985) (explaining that class actions can enable plaintiffs "to pool claims which would be uneconomical to litigate individually").

156. *See* 1 RUBENSTEIN, *supra* note 80, § 1:8 (positing that a class action's aggregation of many small claims serves as a deterrent to defendants).

157. FED. R. CIV. P. 23(e)(2); *see also* Moses v. N.Y. Times Co., 79 F.4th 235, 243 (2d Cir. 2023) (holding that a court must consider the incentive award when "evaluating the fairness, reasonableness, and adequacy of a proposed settlement" under Rule 23(e)(2)).

> (C) the relief provided for the class is adequate . . . ; and
>
> (D) the proposal treats class members equitably relative to each other.[158]

Each of these factors is important when analyzing incentive awards. First, a court must consider whether the class representatives adequately represented the class. Second, the court must consider whether the settlement proposal, including the incentive award, was negotiated at arm's length. Both of these factors require the court to ensure that the class representative had no conflicts of interest. Including this step in the determination of whether the size of the incentive award is appropriate helps alleviate the concerns of those opposed to incentive awards. If the court finds that there was a conflict, the court will hold that the incentive award is not fair, reasonable, and adequate.[159]

Third, a court must determine whether the overall class recovery is adequate. This factor requires the court to consider how the size of the incentive award will impact the overall class recovery. To do this, courts should consider the terms of the incentive awards, including the timing of payment. This is analogous to how courts must already consider the award of attorney's fees when evaluating the adequacy of the class proposal. Rule 23 provides that a court take into account "the terms of any proposed award of attorney's fees, including timing of payment" when evaluating whether "the relief provided for the class is adequate."[160] Therefore, if the size of the incentive award drastically decreases the per-member class recovery, the court has discretion to find the incentive award inappropriate.[161]

Lastly, and most importantly, a court must consider if the incentive award impacts whether class members are treated equitably relative to each other. This factor requires courts to balance the interests of the class representatives with the interests of the unnamed plaintiffs.[162] As such, the equitable-treatment requirement is easily debatable, and therefore, courts should ensure they elaborate on their analysis under this factor. In determining whether class members are treated equitably, courts should

158. FED. R. CIV. P. 23(e)(2).

159. *See* Greenberg v. Procter & Gamble Co. (*In re* Dry Max Pampers Litig.), 724 F.3d 713, 722 (6th Cir. 2013) (striking an incentive award that created a conflict of interest between the class representatives and the other class members).

160. FED. R. CIV. P. 23(e)(2)(C).

161. This situation will be rare. From a study of class action lawsuits from 1993 to 2002, the mean of total incentive awards as a percent of class recovery was 0.161% and the median was 0.024%. Eisenberg & Miller, *supra* note 14, at 1339 tbl.7.

162. Moses v. N.Y. Times Co., 79 F.4th 235, 245 (2d Cir. 2023) (arguing that "the equitable-treatment requirement protects the interests of class representatives" but also requires courts to "reject incentive awards that are . . . unfair to the absent class members").

consider the rationales behind incentive awards: (1) to compensate, (2) to offset risk, and (3) to recognize a class representative's work as a private attorney general. Such an approach would be permitted based on the Advisory Committee Notes to the 2018 Amendment. The Committee stated that "parties may supply information to the court on any other topic that they regard as pertinent to the determination whether the proposal is fair, reasonable, and adequate."[163] Thus, courts are permitted to consider other factors to determine if the incentive award treats class members equitably.

Since the 1990s, different standards for analyzing the size of incentive awards have developed among jurisdictions.[164] A frequently cited standard is the one promulgated by the Seventh Circuit in *Cook v. Niedert*:[165] "relevant factors include [1] the actions the plaintiff has taken to protect the interests of the class, [2] the degree to which the class has benefitted from those actions, and [3] the amount of time and effort the plaintiff expended in pursuing the litigation."[166] The *Cook* test heavily focuses on the compensation rationale behind incentive awards. While compensation for work done on behalf of the class should be discussed, courts should also consider the other rationales: offsetting financial and reputation risk and payment for serving as a private attorney general.

Lower federal courts in New York and California have employed tests that include factors that recognize both reputational and financial risk.[167] However, there are no tests that directly consider the class representative's role as a private attorney general when analyzing the size of the incentive award.[168] Therefore, it is likely the private attorney general argument was used merely as a justification for incentive awards rather than as a method to evaluate the size of the incentive award. As a result, the class representative's role as a private attorney general should not bear as much weight in

163. FED. R. CIV. P. 23(e)(1) advisory committee's note to 2018 amendment.

164. *See* 5 RUBENSTEIN, *supra* note 80, § 17:13 (collecting standards for approving incentive awards by jurisdiction).

165. 142 F.3d 1004 (7th Cir. 1998).

166. *Id.* at 1016 (numbers added); *see also* Koenig v. U.S. Bank Nat'l Ass'n, ND (*In re* US Bancorp Litig.), 291 F.3d 1035, 1038 (8th Cir. 2002) (citing the *Cook* factors when upholding incentive awards to class representatives); Staton v. Boeing Co., 327 F.3d 938, 977 (9th Cir. 2003) (citing the *Cook* factors when analyzing an incentive award).

167. *See* Roberts v. Texaco, Inc., 979 F. Supp. 185, 200 (S.D.N.Y. 1997) (providing that the standard for analyzing an incentive award includes, among other factors, "the personal risk (if any) incurred by the plaintiff-applicant in becoming and continuing as a litigant"); Van Vranken v. Atl. Richfield Co., 901 F. Supp. 294, 299 (N.D. Cal. 1995) (positing that one factor a court should consider when evaluating an incentive award is "the risk to the class representative in commencing suit, both financial and otherwise").

168. *See* 5 RUBENSTEIN, *supra* note 80, § 17:13 (explaining various judicial review standards for incentive awards, none of which consider the class representative's role as a private attorney general).

evaluating the size of the incentive award as compared to the rationales of compensation and risk.

In conclusion, Rule 23 largely provides the framework for how courts should analyze the size of incentive awards. Courts should consider whether the incentive award is "fair, reasonable, and adequate" and do so by considering the factors provided in Rule 23(e)(2). Moreover, in determining whether the incentive award inhibits class members from being treated equitably relative to each other, courts should focus on how much is needed (1) to compensate the class representative for work done on behalf of the class and (2) to offset the financial and reputational risk the class representative took on.

Conclusion

Despite incentive awards receiving increasingly more attention over the last three-and-a-half years, the analysis has been incomplete. Specifically, discussion of the legal basis for incentive awards has been sparse. This Note sought to fill in the gaps and provide the missing analysis.

The Note began with finding a legal basis for incentive awards—and concluded that settlement agreements provide such a basis. As most class actions end in settlement, using the settlement agreement as the independent legal basis for an incentive award is adequate. Additionally, this Note directly confronted predictable counterarguments to allowing incentive awards: incentive awards would be a per se violation of Rule 23, they would violate Supreme Court precedent, and they could create abuses such as conflicts of interest and promoting litigation. However, each of these concerns was proven to be baseless.

First, the notion that incentive awards would not be a per se violation of Rule 23 is supported by the 2018 amendment, requiring class members to be treated "equitably relative to each other," as well as the legislative history behind the Private Securities Litigation Reform Act and the Class Action Fairness Act. Moreover, in contrast to the Eleventh Circuit's holding in *Johnson*, permitting incentive awards under Rule 23 is consistent with *Greenough* and *Pettus* because Rule 23 protects against the abuses the Supreme Court was concerned with in those cases. Additionally, concerns that incentive awards will lead to abuse are unfounded because Rule 23, among other sources of authority, provides an adequate deterrent for class representatives and class action lawyers to refrain from engaging in such abuses. Also, placing a general ban on incentive awards will destroy the viability of class actions, thus destroying its compensatory and deterrent functions—a result much worse than the fear of conflicts of interest and promoting litigation.

Lastly, the missing analysis wrapped up with a suggested framework of how courts should analyze the size of incentive awards moving forward. As

Rule 23 governs the approval of settlement agreements, it should provide the framework for determining whether the size of the award is appropriate. Specifically, courts should consider the four factors laid out in Rule 23(e)(2) when determining if the incentive award is "fair, reasonable, and adequate." When analyzing if the incentive award treats class members equitably relative to each other, courts should consider what is needed to compensate the class representatives for their work done on behalf of the class and to offset any financial and reputational risk.

The viability of class actions is dependent on the participation of class representatives, and thus, dependent on the survival of incentive awards. As such, courts should follow this analytical framework when reviewing incentive awards to decrease the likelihood that incentive awards are categorically banned.