IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
WESTERN DIVISION

GEORGE CARTER, *et al.*,	)	
individually and on behalf of all persons	)	
similarly situated,	)	
	)	
Plaintiffs,	)	
	)	
v.	)	**No. CV-00-C-2666-W**
	)	
ICR SERVICES, INC., D/B/A NATIONAL	)	
CREDIT REPAIR, *et al.*,	)	
	)	
Defendants.	)	
	)	

BRIEF OF FEDERAL TRADE COMMISSION
AS AMICUS CURIAE

The Federal Trade Commission ("Commission" or "FTC") submits this brief as amicus curiae to express its position on two issues that will be before the Court at the August 16, 2002 fairness hearing. First, the Commission opposes class counsel's petition for an award of $1.2 million in attorneys' fees in a case where the "common fund" generated by class counsel's efforts currently includes only $1,575,000. Class counsel's request for an award of $1.2 million in attorneys' fees thus represents approximately 76% of the existing common fund. Such a request is clearly excessive and should be disallowed.[1]

Second, the Commission is concerned about the treatment in the claims process of a category

---

[1] It is our understanding that defendants will be required to deposit additional amounts into the "common fund" in order to fully fund the proposed settlement. Even with the additional deposits, however, it is likely that class counsel's requested fee of $1.2 million will account for well over 50% of the total settlement funds.

of class members for whom defendants failed to provide an "amount paid" to the claims administrator. Defendants had this information within their control and were required by the parties' settlement agreement to provide it to the claims administrator. Defendants' breach of that obligation caused the claims submitted by affected class members to trigger a more rigorous verification process that in most instances could have been avoided had defendants provided the required information. The Commission is concerned that class members who fail to comply with this verification procedure may have their claims rejected in instances where the verification process should not even have been triggered. In the Commission's view, that is not a fair result. If anyone should suffer from defendants' failure to provide necessary information within their control, it should be defendants themselves. We therefore respectfully suggest that the claims submitted by this category of claimants be deemed presumptively valid unless defendants are able to come forward with specific information rebutting the claimed amount.

I. STATEMENT OF THE FTC'S INTEREST

The FTC is the nation's principal consumer protection agency and, more specifically, is the agency charged with enforcing the Credit Repair Organizations Act ("CROA"), the federal statute at issue in this case. *See* 15 U.S.C. § 1679h(a). As we informed the Court by letter of March 7, 2002, the Commission is conducting an investigation into the business practices of the defendants in the *Carter* case. Although the investigation is focused on some of the same conduct alleged by the *Carter* class, it also involves other deceptive practices that are not currently before the Court. Those practices injured consumers who are members of the *Carter* class, as well as other consumers who purchased defendants' credit repair services outside the class period.

Since learning of the proposed settlement in January 2002, Commission staff have been actively monitoring developments in the *Carter* case. One reason for the Commission's interest is that the parties' settlement agreement requires that class members release any and all claims they may have against all defendants. We believed, for instance, that it was important that class members be notified individually, and we feared that the initial round of individualized notice had been sent to only a small portion of the class. Because not all class members were individually notified, we were concerned that the release of claims may be interpreted as releasing the claims of class members who were never provided with individualized notice. The Commission raised that concern with the Court by its letter of March 7, 2002. The Court then generously afforded Commission counsel the opportunity to address the issue at a May 3, 2002 hearing. Ultimately, Commission staff were instrumental in identifying more than 80,000 additional class members who subsequently received individualized notice of the proposed settlement.

In comments to the Court at the May 3, 2002 hearing, Commission counsel expressly reserved the right to address at the subsequent fairness hearing other issues that were not yet ripe, such as the reasonableness of any attorneys' fees class counsel may seek. The Commission of course recognizes that class counsel are entitled to attorneys' fees and costs for filing the instant action and negotiating the proposed settlement. At the same time, however, the Commission is concerned that the attorneys' fees be reasonable and not overstated. Defendants do not have unlimited assets, of course, and the amount awarded to class counsel in attorneys' fees in this case will necessarily limit the funds that could be available for consumers from a broader FTC action against defendants.

II. STATEMENT OF FACTS

For the last several months, the Commission has been conducting an investigation into the business practices of ICR Services, Inc. ("ICR") and a related nonprofit entity, National Credit Education and Review. ICR's principals – Bernadino J. Pavone, Jr., Abood Samaan, and Gloria Tactac – also are targets of the Commission's investigation. The investigation has focused on whether these entities and individuals have in the past or are currently violating Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45(a), and various provisions of the Credit Repair Organizations Act, 15 U.S.C. §§ 1679 *et seq.* In the course of its investigation, the Commission learned of the proposed settlement in the *Carter* case.

A. Identification of Additional Class Members

On or about January 23, 2002, the claims administrator mailed a notice of the proposed settlement to 61,853 potential class members. The defendants' position at the time was that these 61,853 customers included all those who had purchased defendants' credit repair services during the class period, except for an admitted gap period running from April 1997 through October 1998 for which defendants had no data.

Upon learning of the potential settlement and of the number of identified class members, Commission staff immediately raised questions about whether all potential class members had been notified. Staff was skeptical because two of defendants' officers had represented to us in an October 2001 meeting that defendants had approximately 150,000 credit repair customers over the life of their business. We therefore requested from defendants certain financial data and other information that would help us to determine whether the represented class size was accurate. After reviewing that

information, we concluded that defendants' sales volume was significantly higher than had been previously represented to class counsel and to the Court. That was clear from defendants' own income statements and from the royalty amounts ICR had paid to a third party on its credit repair sales. From the information provided, we were convinced that fewer than half of all potential class members had been notified of the proposed settlement.

Although defendants repeatedly told us that there were no additional sources of individual customer information, we learned in mid-February 2002 that defendants had approximately 1,300 boxes of customer contracts and other customer correspondence in an off-site storage facility. We asserted at that point that Fed. R. Civ. P. 23(c)(2) and case law interpreting that rule required that these documents be reviewed, because they contained information on potential class members who could be identified "through reasonable efforts" and thereafter provided with individualized notice. Shortly before the review process was to begin, however, defendants informed us that they had located two computerized databases that included scanned versions of all documents in the 1,300 boxes. Defendants thus were able to electronically produce information on approximately 80,000 additional class members. The claims administrator sent a supplemental notice of the proposed settlement to these additional class members in late May 2002.

With all due respect to class counsel, Commission staff was the driving force behind the identification of these additional class members. Once we learned of the 1,300 boxes of stored documents, Commission staff traveled to Canton, Michigan to review a sampling of the documents. Because the vast majority of the consumers identified in those documents were not among the consumers previously notified of the proposed settlement, we insisted that the documents be thoroughly

reviewed in order to identify additional class members. Class counsel initially resisted such a comprehensive review, citing the cost and the fact that the review would delay the fairness hearing and the mailing of checks to previously-identified class members. The Commission's position that Rule 23(c)(2) required a thorough review of the documents ultimately prevailed, however. Eventually, an additional 80,000 potential class members were identified, more than doubling the size of the class.

B. Funding of the Proposed Settlement

Because class counsel's attorneys' fees generally are a function of the results obtained, we must also review the relief provided to class members under the proposed settlement. In the settlement agreement preliminarily approved by the Court on December 28, 2001, the parties agreed that the monetary value of the required payments to class members was approximately $4,713,210. (Stipulation and Settlement Agreement at ¶ 11(f).) Once the additional class members were identified, however, that value was raised to approximately $8,498,000. (Proposed Amendment to the Settlement Agreement of December 28, 2001, at ¶ III.) The parties also agreed that certain credit counseling services defendants would make available to class members under the proposed settlement were valued at $2,497,075. (Stipulation and Settlement Agreement at ¶ 12(d).) Between the required payments and the credit counseling services, then, the parties valued the relief provided for under the settlement agreement at well over $10 million. It is abundantly clear from the settlement agreement itself, however, that the settlement was never worth anything close to that amount.

First, although the defendants were obligated by the settlement agreement to establish a fund for the payment of class member claims, they were only required to deposit a total of $1,850,000 into that "claims fund." (Stipulation and Settlement Agreement at ¶ 17.) At the same time, defendants were

required to establish a "fee and expense fund" and to ultimately deposit a total of $950,000 into that fund. (*Id.*) Under the terms of the agreement, moreover, defendants are permitted to withdraw from the proposed settlement if the total payments to class members required by the agreement exceed $1,850,000. (*Id.* at ¶ 40.) These provisions thus required defendants to establish a common fund of, at most, $2.8 million.

Yet the fund actually established in this case never contained anything close to that amount. Shortly after the proposed settlement was preliminarily approved, defendants breached the funding terms set out in Paragraph 17. Class counsel subsequently agreed to amend the funding terms but still was forced on two occasions to move to sequester defendants' assets to ensure that the proposed settlement was funded. At the time of this writing, a total of only $1,575,000 has been deposited into the two settlement funds. More than half of that amount is currently in counsel's fee and expense fund, as opposed to the claims fund. Despite these obvious funding deficiencies, class counsel has now requested that the Court award $1.2 million in attorneys' fees and $35,000 in expenses.

III. ARGUMENT

A. The Attorney's Fees Awarded in this Case Should be Significantly Less than the Requested $1.2 Million.

"In considering a fee award in the class action context, the district court [plays] a significant supervisory role." *Waters v. International Precious Metals Corp.,* 190 F.3d 1291, 1293 (11th Cir. 1999), *cert. denied,* 530 U.S. 1223 (2000). Such a role is mandated by Fed. R. Civ. P. 23(e), which precludes the dismissal or compromise of a class action without the district court's express approval. In the Eleventh Circuit, district courts enjoy wide latitude in formulating attorneys' fee awards that are

appropriate to the circumstances of a given case. *Waters*, 190 F.3d at 1293. The trial court's considerable discretion in this area stems from that court's familiarity with the litigation and the desirability of avoiding frequent appellate review of what essentially are factual matters. *See Hensley v. Eckerhart,* 461 U.S. 424, 437 (1983).

Judicial scrutiny of the requested fee award is especially important in this case, where the petition seeks fees in excess of the total amount recovered by the plaintiff class. Under the proposed settlement, certain class members are eligible to receive 42% of the amount they paid to ICR while other class members are eligible to receive 5% of that amount. In order to qualify for those payments, however, class members must affirmatively submit claims to the claims administrator, and in some instances, must verify the amounts paid. Defendants' monetary obligation under the proposed settlement thus depends entirely on the number of class members who are able to establish valid claims. It is our understanding that the percentage of class members who have actually asserted claims under the proposed settlement is approximately 11%, and as of August 9, 2002, defendants' payment obligation on those claims totals only $964,284.28. As we said earlier, moreover, the amount of money currently set aside to pay both those claims and class counsel's fees and costs totals $1,575,000.

Although the amount defendants must pay to consumers under the proposed settlement depends on the number of claims that are filed and ultimately approved, defendants' obligation to pay attorneys' fees is fixed at a specified amount, subject to Court approval. Under the original settlement agreement, for example, defendants were required to pay up to $950,000 in attorneys' fees and costs. (Stipulation and Settlement Agreement at ¶ 13.) Under the amended settlement agreement, that amount

was raised to $1,235,000. (Proposed Amendment to the Settlement Agreement of December 28, 2001, at ¶ IV.) Class counsel is therefore entitled to seek fees and costs in those amounts and defendants are obligated to support those requests regardless of the number of class members who actually are able to establish valid claims. The Commission is concerned that structuring the proposed settlement and fee award in this way may have served to decouple the financial interests of class counsel and the plaintiff class. Elements of the notice and claims process are crucial determinants of how many class members receive notice and how much money they receive, but class counsel no longer has a financial stake in assuring the maximum possible recovery for class members. Justice O'Connor has cautioned, for instance, that when the financial incentives of class counsel and their clients are not aligned, there is an increased risk "that the actual distribution will be misallocated between attorney's fees and the plaintiffs' recovery." *International Precious Metals Corp. v. Waters,* 530 U.S. 1223 (2000) (Statement of O'Connor, J., respecting the denial of the petition for a writ of certiorari). We think that would occur here if class counsel were awarded $1.2 million in attorneys' fees.

1. Percentage of the Common Fund

In the Eleventh Circuit, attorneys' fees in a common fund case such as this one are "based upon a reasonable percentage of the fund established for the benefit of the class." *Camden I Condominium Ass'n, Inc. v. Dunkle,* 946 F.2d 768, 774 (11th Cir. 1991). The "benchmark" percentage generally is between 20% and 30%, but district courts are permitted to award percentages either above or below the benchmark so long as they identify the factors justifying the chosen degree of departure. *Id.* at 774-75; *see also Waters,* 190 F.2d at 1294.

In this case, the difficulty lies not so much in settling on the proper percentage as in identifying the amount of the common fund to which that percentage should be applied. As we explained above, the two funds established in connection with the proposed settlement currently contain a total of only $1,575,000. Twenty-five percent of that common fund is $393,750, significantly less than the $1.2 million in attorney's fees that class counsel seeks here. Furthermore, even if $2.8 million had been deposited into the funds, as contemplated by the original settlement agreement, twenty-five percent of that amount is only $700,000. Using either amount, then, the $1.2 million fee award that class counsel seeks far exceeds the traditional benchmark.

Class counsel may argue, however, that the Court should consider the common fund amount to include the hypothetical values assigned to the various types of relief provided for in the settlement agreement, rather than the amount defendants actually have deposited into the two settlement funds. The Commission cannot agree with such an approach. Although the Eleventh Circuit in *Waters v. International Precious Metals Corp.,* 190 F.3d at 1296-98, affirmed an award of attorneys' fees derived from the total fund made available to members of the plaintiff class, rather than from the amount class members actually claimed, that decision is of little help to class counsel here. In both the *Waters* case and the Supreme Court decision on which it was based (*see Boeing Co. v. Van Gemert*, 444 U.S. 472 (1980)), an actual fund was established that included the entire amount of the settlement or judgment. *See Waters*, 190 F.3d at 1292 & n.2 (common fund comprised of $40 million in cash and promissory notes that were actually delivered to the settlement administrator); *see also Boeing,* 444 U.S. at 476 (court ordered the defendant to deposit judgment amount into an escrow at a commercial bank to be administered by a Special Master). Those cases are easily distinguished from the instant

case where the settlement agreement recites a hypothetical value for the relief provided but defendants actually were required to deposit a significantly lesser sum with the settlement administrator.[2] The Commission submits that in that circumstance, the hypothetical value is illusory and should be disregarded. The Court should instead consider the common fund to include only those amounts actually deposited by defendants with the settlement administrator, for it is only those funds that actually have been made available to the plaintiff class. *See Strong v. Bellsouth Telecommunications Inc.,* 137 F.3d 844, 852 (5th Cir. 1998) (distinguishing *Boeing* because "no money was paid into escrow or any other account" and basing attorneys' fee award instead on the actual amount claimed by the class); *see also Waters,* 190 F.3d at 1296 (noting that in *Strong,* the defendants "never established a 'common fund' from which money would be drawn"). In this case, that amount currently is only $1,575,000.

In the Commission's view, moreover, there are no unique or compelling circumstances in this case that should cause the Court to depart upward from the benchmark percentage. The case was a relatively simple one, premised on the fact that defendants had collected money from consumers in advance of providing promised credit repair services, a clear violation of the Credit Repair Organizations Act. *See* 15 U.S.C. § 1679b(b). The simplicity of the case is evidenced by class counsel's own motion for partial summary judgment, which was only nine pages long and included legal argument of less than a single page. Indeed, class counsel's summary judgment motion itself informed

---

[2] The Eleventh Circuit in *Waters* took pains to point out, moreover, that trial judges in subsequent cases are not precluded by its opinion from basing an award of attorneys' fees on the amount actually recovered by the class, as opposed to the gross amount made available. *Waters,* 190 F.3d at 1298.

the Court that "[t]he issues presented by this motion are very simple." (Motion for Partial Summary Judgment at 1.) It is therefore clear that no unique skill or experience was required to prosecute this class action.[3]

2. The Lodestar

Finally, although the Eleventh Circuit utilizes the "percentage of the fund" method for calculating attorneys' fees in a common fund case, the lodestar amount remains relevant for purposes of checking the reasonableness of the percentage award. *See Waters,* 190 F.3d at 1298; *see also Goodrich v. Hutton Group, Inc.,* 681 A.2d 1039, 1047-48 (Del. 1996). In this case, class counsel have represented that their lodestar totals approximately $600,000, although they have not yet provided documentation supporting that figure. Class counsel, however, seeks twice that amount in attorneys' fees – in other words, a multiplier of two. The Commission can see no unique circumstances here that would justify the application of any type of multiplier to the lodestar amount. We therefore submit that at best, $600,000 should serve as the upper limit of a reasonable fee award. As explained above, however, we believe that the more appropriate attorneys' fee award in the circumstances of this case would be $393,750.

B. The Claims of Class Members for Whom Defendants Failed to Provide an Amount Paid Should Be Considered Presumptively Valid.

We have one additional concern that we hope the parties will have resolved prior to the fairness hearing. For an as yet unexplained reason, defendants failed to provide to the claims administrator

---

[3] When more difficult issues arose, moreover, such as whether defendants were understating the number of potential class members, Commission staff took the lead in uncovering defendants' deception.

information on the "amount paid" for nearly 50,000 of the approximately 80,000 additional class members who were notified of the proposed settlement in late May 2002. Class members in the affected category who then submitted claims to the claims administrator necessarily triggered a verification process set out in the settlement agreement, because the amount they claimed naturally differed from the non-existent amount defendants provided (or failed to provide).[4] It is our understanding that approximately 90% of the claimants in the second phase triggered the verification process solely because defendants failed to provide the claims administrator with information on how much those claimants had paid. In our view, the verification process should not be triggered in these circumstances, where defendants failed to provide required information that is within their control. The affected claims should instead be treated as presumptively valid.

The claims experience in this case has shown that, for whatever reason, a significant percentage

---

[4] To assert a claim under the proposed settlement, class members were required to return a claim form to the claims administrator which includes, among other information, the amount the consumer paid for ICR's credit repair services. For their part, defendants were required to provide the claims administrator with a database of information which included the amount each class member paid. Upon receiving a claim, the claims administrator compares the amount claimed by the consumer with the amount shown in defendants' database, and if the amounts do not correspond, the claims administrator proceeds to send the consumer a verification form. (*See* Stipulation and Settlement Agreement at ¶ 22(d)(iv) ("If a Database Customer submits a Proof of Claim that indicates the Database Customer paid an amount different than the amount contained in ICR Services' computer customer database, then the Claims Administrator shall send the Database Customer Verification Form I, which must be completed as described in Subsection (e)(iii) below.").) The consumer must then return the verification form to the claims administrator along with documentary proof or a notarized statement supporting the amount of the consumer's claim. If the class member fails to return the verification form, then he will receive 42% (or 5% in appropriate cases) of the amount shown in defendants' database. (*Id.* at ¶¶ 22(d)(iv) & 22(e).) The problem here, however, is that for approximately 50,000 of the 80,000 consumers notified in the second phase, that amount is either non-existent or zero.

of claimants drop out each time claimants are required to return materials to the claims administrator. Under the procedure set out in the settlement agreement, the default for those claimants would be to use the "amount paid" shown in defendants' database. (Stipulation and Settlement Agreement at ¶ 22(d)(iv).) Because defendants failed to provide such amounts, however, the amount shown is zero, meaning that the affected claimants would receive nothing. The Commission believes that it would be fundamentally unfair for the claims of affected class members to be invalidated in this way. The only viable alternative short of defendants' belatedly producing the required information is for the claims to be treated as presumptively valid.

IV. CONCLUSION

For the foregoing reasons, the Commission respectfully requests that the Court award class counsel attorneys' fees in an amount significantly less than the $1.2 million requested in their petition. Given the current amount of the "common fund" in this case, the Commission submits that an award of $393,750 would be reasonable. The Commission also respectfully requests that the claims submitted by the category of class members discussed above for whom defendants failed to provide an "amount paid" be deemed presumptively valid.

Respectfully submitted,

WILLIAM E. KOVACIC
General Counsel

Dated: __________________

____
Todd M. Kossow
Nicholas J. Franczyk
Federal Trade Commission

Midwest Region
55 East Monroe Street, Suite 1860
Chicago, Illinois 60603
(312) 960-5634 (ph.)
(312) 960-5600 (fax)

Attorneys for Federal Trade Commission