

**IN THE  
UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT**

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Consolidated Appeals

Nos. 07-56643; 07-56645; 07-56646; 07-56647;  
07-56649; 07-56650; 07-56651; and 07-56833

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**RYAN RODRIGUEZ, et al.,**  
Class Plaintiffs/Appellees,

and

**WEST PUBLISHING CORPORATION, A MINNESOTA  
CORPORATION d.b.a. BAR/BRI, et al.,**  
Defendants/Appellees

vs.

**GEORGE SCHNEIDER, et al.,**  
Objectors/Appellants

Appeal From Judgment Entered By  
The United States District Court, Central District of California,  
Manuel Real, District Court Judge  
District Court Case No. CV-05-03222(R)

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**REPLY BRIEF OF APPELLANTS GEORGE SCHNEIDER *et al.***  
**(Appeal Nos. 07-56643 and 07-56833)**

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## **I. INTRODUCTION**

Plaintiffs-Appellees expend much effort disregarding or gainsaying the district court's findings on the conflicts of interest in this case. But there is ample evidence to support Judge Réal's conclusions about the conflicts of interest in this case. The issue actually presented is whether the district court erred in failing to extend that finding to the attorneys in the case and to withhold approval of the settlement for lack of adequate representation.

Here, the district court had an understandable desire to salvage a settlement put in jeopardy by a sudden maelstrom of infighting among the representatives and their lawyers, which was compounded by the existence and nature of the contingent Amended Incentive Agreements. But rather than substituting its own view that the settlement was nevertheless fair, the district court should have refused final approval and appointed additional unconflicted counsel and representatives to evaluate the options available to the class. That might result in the same settlement (but without the taint of inadequate representation), a different settlement, or the case going to trial. Whatever the result, it would serve justice and, perhaps even more critically, preserve the public perception that justice has been served in this case.

Plaintiffs-Appellees are likewise unable to explain why the conflicts the

district court found should not have severely affected the fee awarded in this case, and cannot explain the more mundane irregularities in the fee award, such as awarding a fee and multiplier for future work not yet accomplished.

Finally, Plaintiffs-Appellees fail to find any valid legal or factual support for the district court's decision to deny fees to the Head/Schneider Objectors' counsel.

## II. ARGUMENT

### A. The Conflicts of Interest Found by the District Court

#### Precluded Settlement Approval

Plaintiffs-Appellees make numerous arguments to explain away the conflicts of interest, breaches of professional rules, and failures of candor that the district court found in this case. Not one is correct on the facts presented in this case. Plaintiffs-Appellees say that the Incentive Agreements said that McGuire Woods would “*request*” court approval of incentive awards “in certain amounts,” creating no conflict Plaintiffs-Appellees’ Brief (“P-A Brief”) at 40 (emphasis in original).

Plaintiffs-Appellees miss the point entirely. Schneider did not argue, and the district court did not hold, that *any* agreement merely to request an incentive award creates an impermissible conflict. Schneider *did* argue – and

the district court agreed – that *this* agreement between class counsel and class representatives (who also happen to be lawyers), made at the outset of the case, to move for a contingent-based incentive award to be taken from the class fund, is ethically impermissible and against public policy, results in a conflict of interest and an appearance of impropriety, and that the failure to disclose such an agreement to the district court at the outset is a failure of candor to the court on the part of class counsel.

Evidently conscious of this, Plaintiffs-Appellees make the extreme argument that “a conflict of interest should arise only if an incentive award is actually *promised*.” P-A Brief at 44-45. But the journal article Plaintiffs-Appellants cite does not suggest that should be the *only* way a conflict of interest can arise from an incentive agreement, and says nothing about undisclosed agreements calling for the attorneys to request specific incentive awards for lawyer class representatives, measured by the recovery in the case.

Yet Plaintiffs-Appellees assert that the conflict and failure of candor cannot be ascribed to the class representatives or class counsel because of the novelty of the issues presented and because they did not operate in bad faith. P-A Brief at 53-54. Whatever the potential merits of this argument in the abstract, it does not apply to this case. Judge Real identified numerous

problems with the Incentive Agreements and the conduct surrounding them, across a broad spectrum of law and rules. Though these rules sometimes interact in complex ways in class actions, the cases and professional rules relied upon here are hardly new, and Judge Real's decision on this point was based upon well-established and well-understood rules of law discussed at some length in the Head/Schneider Objectors' Opening Brief ("H/S Opening Brief").

For the issues presented here the absence of bad faith is not a factor. H/S Opening Brief at 19-20. This was a case of dual representation, where the lawyers were bound – first by agreement and then by circumstance – to mediate between the conflicting interests among the class representatives and between the representatives and the class members. It has long been the case that this results in disqualification without regard to the bad faith of the attorneys. The intent is not to punish the attorneys, but to rectify the appearance of impropriety. In this case, where the case and settlement were subject to substantial national news coverage (P-A SER 1747-1753), that is even more critical.

**1. Appellees’ Argument That the Incentive Agreements Presented Only a “Theoretical” Conflict of Interest That “Never Materialized” Is at Odds with the Relevant Authority and the Rulings of the District Court**

As the Head/Schneider Objectors pointed out on opening, in the context of the ethical rules implicated here – and particularly as applied to class actions – there is no such thing as a “theoretical” conflict of interest that may simply be ignored if it does not “materialize.” In fact, the law is exactly to the contrary. See H/S Opening Brief at 20 (citing *Cal West Nurseries, Inc. v. Superior Court*, 129 Cal.App.4th 1170, 1175 (2005)). It is the appearance of impropriety, whether or not a conflict actually causes harm, that is determinative. See *Bruno v. Bell*, 91 Cal.App.3d 776 (1979). In *Bruno*, the court reversed an award of fees to an attorney who, as a *pro per* plaintiff representing the taxpayers of California, had successfully challenged a statute as unconstitutional. The court noted that it is “improper for an attorney to prosecute a fee-generating class action suit in which he himself was named as plaintiff.” *Bruno*, 91 Cal.App.3d at 788 citing *Kramer v. Scientific Control Corp.*, 534 F.2d 1085 (3d. Cir. 1976). The court concluded:

Without questioning Bruno’s integrity and assuming he acted out

of the highest motives, we must nonetheless be cognizant . . . that “on occasion, ethical conduct of a lawyer may appear to laymen to be unethical.”

We conclude that the appearance of impropriety in this case far outweighs the benefits of rewarding an attorney for his diligence in successfully challenging an unconstitutional statute. The attorney’s fee award was therefore void as against sound public policy.

*Bruno*, 91 Cal.App.3d at 788.

Moreover, the district court itself expressly rejected the argument Plaintiffs-Appellees raise in favor of the theory that the incentive award provisions did not present an actual conflict of interest, and did not influence the class representatives’ evaluation of the settlement:

The conflict of interests here was not simply potential. Indeed, in this case there was an actual manifestation of conflicting interest. The Objecting Plaintiffs claim that Class Counsel threatened to not request incentive payments on their behalf pursuant to the Incentive Agreement if they did not agree to the Settlement. . . .Although the Objecting Plaintiffs argue that there is no actual conflict of interests because they continue to object to the Settlement, the Objecting Plaintiffs have never taken a position that jeopardizes their \$75,000 incentive award request because they do not object to the settlement with Kaplan. The \$13 million settlement with Kaplan alone exceeds the \$10 million provision in the Incentive Agreement which contractually requires Class Counsel to request a \$75,000 incentive payment on their behalf.

ER No. 4; p. 68: 7-12.<sup>1</sup>

Those manifestations of “actual conflict” in this case are more than sufficient to support Judge Real’s express finding that the conflict was not merely theoretical, even if that were a dispositive issue.

The cases Plaintiffs-Appellees cite are not to the contrary. In *Cummings v. Connel*, 316 F.3d 886, 896 (9th Cir. 2003) the trial court found that *speculative* conflict would not support finding of inadequacy of representation, and noted that it was “willing to reconsider and decertify the class if . . . there was evidence of an actual conflict.” *Id.* at 896. Here, as Judge Real found, there was an actual conflict of interest that had persisted before class certification and settlement, but which was not brought to his attention until much later. This case therefore presents the opposite situation from that in *Cummings*, in which the court was in a position to deal with any potential conflict before the fact.<sup>2</sup>

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<sup>1</sup> Here, class counsel did in fact make a motion for the incentive awards as required by the Amended Incentive Agreements, arguing in favor of between \$25,000 and \$75,000 for the various representative plaintiffs. P-A SER 1456 *et seq.*

<sup>2</sup> *Jaffe v. Morgan Stanley & Co., Inc.*, 2008 WL 346417 at \*6 (N.D. Cal. 2008) is also distinguishable. In *Jaffe* the district court became aware of a potential conflict prior to the preliminary approval of the settlement, but the named plaintiff took steps to eliminate the conflict, ultimately leading

In this case, by contrast, the district court expressly found that the Class Representatives interests were *not* aligned with the class, exactly the type of “serious and irreconcilable” conflict referred to in *Mateo v. M/S Kiso*, 805 F.Supp. 761, 772 (N.D. Cal. 1991), also cited by Plaintiffs-Appellees, and a condition that prevented a finding of adequacy of representation.

**2. The District Court Properly Found a Conflict of Interest  
as to All of the Class Representatives**

Plaintiffs-Appellees postulate that there were two “non-conflicted” class representatives who did not sign the Incentive Agreements, represented by Zwerling, Schachter and Zwerling, LLP (the so-called “ZSZ plaintiffs”). That is directly contrary to the rulings of the district court, which did not find that the two ZSZ plaintiffs were “non-conflicted.” On the contrary, Judge Real denied incentive awards to *all seven* named plaintiffs on the express finding that it was necessary to remedy the conflicts of interest in the case. ER 68, lines 13-16.

That holding is squarely line with the *Sipper* case discussed in Judge

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the court to rule that her interests were aligned with the class and that she was an adequate representative.

Real's opinion. ER 67, lines 16-22.<sup>3</sup> In *Sipper*, there were also two assertedly "untainted" plaintiffs, who were represented by co-counsel not a party to the conflict. But the district court also disqualified co-counsel and the plaintiffs, even though (or arguably, because) they were unaware of the conflict, in part because they failed to detect the conflict and then failed to recognize its seriousness on briefing it. *Id.* at \*4.

There is in fact ample evidence to support Judge Real's decision on this point. ZSZ attorneys should have known about the Incentive Agreement in March of 2006, if not before, because it was discussed at a deposition defended by a ZSZ attorney. See P-A SER 270 (March 17, 2006 deposition transcript in which Mr. Drachler, an ZSZ attorney, is defending the deposition of Reena Frailich as she discusses the Amended Incentive Agreement). Even the defendants were aware of the Agreement by April 18, 2006, prior to class certification, making it difficult to believe that all plaintiffs counsel were not aware of it. See Opinion and Order, ER 67, lines 15-16. See also P-A SER 263 Declaration of Sydney K. Kanazawa dated June 26, 2007, at ¶10 ("The actual Retainer Agreements were produced to Defendants on April 18, 2006,

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<sup>3</sup> *Sipper v. Capital One Bank*, 2002 WL 398768; 2002 U.S. Dist. LEXIS 3881 (C.D. Cal. 2002).

before Class Certification.”).

ZSZ attorneys, and presumably their clients, were certainly aware of the Agreement by February and March of 2007, when the incentive awards were negotiated with defendants in the context of the settlement, and it became clear that the objecting plaintiffs were intent upon requesting the full contractual amount of \$75,000. Two of the signatory plaintiffs declared that they were contacted by ZSZ attorney Dan Drachler,<sup>4</sup> who spoke to them about the Incentive Agreement, and asked them to reduce their incentive award demands to \$25,000 each. P-A SER 1731 at ¶11 (declaration of plaintiff Nesci); P-A SER 1735 at ¶7 (declaration of plaintiff Rodriguez). From the facts that unfolded, the inference is unavoidable that the ZSZ plaintiffs were to incidentally benefit by the selection of \$25,000 – the lowest amount provided by the Incentive Agreements – as the “compromise” amount urged upon the signatory plaintiffs by class counsel.

Thus, the failures of candor and conflicts of interest were equally applicable to ZSZ and “their” representative plaintiffs. Judge Real’s error was not in so finding, but in failing to take the additional steps necessary upon so finding.

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<sup>4</sup> See P-A SER 1293 (Dan Drachler entry in ZSZ firm resume).

**3. The District Court Did Not Properly “Remedy” the  
Conflicts of Interest Simply by Denying the Incentive  
Awards**

Plaintiffs-Appellees conclude that the district court “exercised its discretion to ameliorate whatever conflict it saw by denying all incentive awards, thereby ensuring that the Class would not suffer any material detriment.” P-A Brief at 42. This formulation, of course, begs the very question whether the district court was within its discretion to deal with the conflict it found merely by denying incentive awards to the class representatives.

In any event, merely denying the incentive awards did not “ensure” that the class suffered no detriment. Although it saved the class fund from paying the incentive awards, it did not cure the central problems identified by Judge Real: If the conflicts of interest *had* affected the ultimate settlement value and the representative plaintiffs’ incentives in agreeing to it, merely taking away the incentive awards would not cure that. Nor would denying incentive awards cure the public perception that the conflicts of interest might have affected the settlement.

Again, the proper remedy was to refuse final approval and appoint

additional, unconflicted counsel who could ascertain and opine to the district court whether the settlement was, in fact, fair, adequate and reasonable under the circumstances. Finally, as discussed *infra*, Judge Real's failure to hold class counsel equally accountable for the conflicts of interest will mean that the class suffers the additional detriment of paying more than it should for attorneys' fees in this case.

**4. Appellees Cannot Explain Away the Additional Intra-Class Conflicts Unrecognized by the District Court**

Defendants-Appellees and Plaintiffs-Appellees both argue in support of the settlement approval that the Clayton Act Section 7 case is without merit, so that there is no conflict inherent in Plaintiffs decision not to afford compensation to the subset of class members with those claims.

One expects defendants to so argue. Yet plaintiffs maintained the Section 7 case in the pleadings throughout the case. See P-A SER 2192-93 (First Amended Complaint dated May 26, 2005, in which Plaintiffs' first cause of action for violation of Section 7 of the Clayton Act). They suddenly changed their minds upon settling the case, asserting without qualification that the claims were without merit. See P-A SER 396-400 (in Reply to Plaintiffs Ryan Rodriguez [et al.] Objection to Preliminarily Approved Settlement [etc.],

dated June 11, 2007). Plaintiffs told the district court that they “Would Not Prevail” and “cannot prevail” on the Clayton Act claim. P-A SER 396. They stated flatly that the claim “Is Time Barred” and “would...be dismissed as time barred.” *Id.* They even claimed that the challenged arrangement “was pro-competitive” and “benefited consumers.” P-A SER 397. In a later filing, plaintiffs stated that class members from 1997 through 2001 “would recover nothing, even in the event of a total victory,” because “tolling provisions are not available” so that claims under the Clayton Act “are time barred.” P-A SER 879 (in Settling Plaintiffs’ Reply Memorandum in Support of Final Approval).

Yet Plaintiffs concurrently admitted that the existence of the claim creates a split in the class, and implicitly, a conflict: “Application of the four-year statute of limitations and/or the doctrine of laches, possibly defeating or diminishing the claim all together *and certainly dividing the Class as currently defined.*” *Id.* (emphasis added). But it is not the risk of losing the Clayton Act claim on the merits that would have divided the class – that would be moot if the claim were lost. In fact, the division in the class was caused by the possibility that the claim would succeed, a matter never resolved on the merits.