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8 **IN THE SUPREME COURT**

9 **STATE OF ARIZONA**

10 PETITION TO AMEND RULE 23,  
11 ARIZONA RULES OF CIVIL  
12 PROCEDURE

Supreme Court No. \_\_\_\_\_

**Petition to Amend Rule 23 of the  
Arizona Rules of Civil Procedure**

13 Pursuant to Rule 28 of the Arizona Rules of the Supreme Court, the Arizona  
14 Foundation for Legal Services & Education (Arizona Bar Foundation) petitions the Court  
15 to amend Rule 23 of the Arizona Rules of Civil Procedure to provide direction for the  
16 distribution of residual funds in class action cases. The proposed rule amendment would  
17 require that at least 50% of any residual class action funds be distributed to the Arizona  
18 Bar Foundation to provide legal services and access to justice for low-income residents of  
19 Arizona. In support of this petition, the Arizona Bar Foundation states the following:

20 **I. Background and Purpose of the Proposed Amendment**

21 This petition arises from the recommendations of the State Bar of Arizona's  
22 Access to Justice Task Force (AJTF). The AJTF was established in 2011 by the State  
23 Bar and its members were drawn from a broad group of legal professionals. In their final  
24 report in the fall of 2011, the AJTF identified the use of *cy pres* awards to distribute class  
25 action residual funds to access to justice initiatives as a way to increase financial support  
26 for legal services.<sup>1</sup>

27 \_\_\_\_\_  
28 <sup>1</sup> SBA Access to Justice Committee Report 2011. [http://www.azbar.org/media/322784/access\\_to\\_justice\\_task\\_force\\_report.pdf](http://www.azbar.org/media/322784/access_to_justice_task_force_report.pdf)

1 As explained below, if the rule is adopted, Arizona would join the growing  
2 number of states that have established similar methods of disbursement for class action  
3 residual funds. Currently, there is no procedure that gives guidance to trial courts for the  
4 disbursement of class action residual funds. The rule amendment proposed in this  
5 petition would provide direction for the disbursement of these funds and is modeled after  
6 similar rules of civil procedure in Indiana, Pennsylvania, and Washington. *See* Appendix  
7 B.

## 8 **II. Proposed Rule Amendment**

9 The proposed rule amendment is the following and is attached in Appendix A:

### 10 Rule 23(g). Disposition of Residual Funds in Class Action 11 Cases.

12 (1) “Residual Funds” are (a) the funds that remain after the  
13 payment of all approved class member claims, expenses,  
14 litigation costs, attorneys’ fees, and other court-approved  
15 disbursements to implement the relief granted, or (b) if it is  
16 impossible or economically impractical to distribute the  
17 settlement or judgment funds to the class at all, the funds  
18 remaining after the payment of all approved expenses,  
19 litigation costs, attorneys’ fees, and other court-approved  
20 disbursements to implement the relief granted. Nothing in  
21 this rule is intended to limit the trial court from approving a  
22 settlement or order that does not create residual funds.

23 (2) Any order entering a judgment or approving a proposed  
24 compromise or settlement of a class action certified under this  
25 rule that establishes a process for identifying and  
26 compensating members of the class, or where such process is  
27 impossible or economically impractical, shall provide for the  
28 disbursement of residual funds. In matters where the claims  
process has been exhausted or where a claims process is  
impossible or economically impractical and residual funds  
remain, not less than fifty percent (50%) of the residual funds  
shall be disbursed to the Arizona Foundation for Legal  
Services and Education to provide legal services and access to  
the justice system for low-income residents of Arizona. The  
court may disburse the remaining residual funds for purposes  
that have a direct or indirect relationship to the objectives of  
the underlying litigation or otherwise promote the substantive

1 or procedural interests of members of the certified class to  
2 either the Arizona Foundation for Legal Services and  
3 Education or any other entity.

4 Similar provisions have been implemented by numerous other states by rule or  
5 statute. *See* Appendix B. The states adopting statutes include: California (1994), Illinois  
6 (2008), North Carolina (2005), South Dakota (2012) and Tennessee (2006). The states  
7 that have amended court rules/orders include: Hawaii (2011), Indiana (2011), Louisiana  
8 (2012), Maine (2013), Massachusetts (2009), New Mexico (2011), Pennsylvania (2012)  
9 and Washington (2009).<sup>2</sup>

10 The states that have adopted provisions for the disbursement *cy pres* funds to legal  
11 services have varied directions for the class action residual funds distribution. *See*  
12 Appendix B. However, the one constant in these rules and statutory changes is that the  
13 residual funds are designated to go to legal services programs providing assistance and  
14 access to the justice system for low-income persons and all the recipients are entities  
15 which serve similar functions to the Arizona Bar Foundation. Nine of the thirteen states  
16 specifically list the Interest on Lawyers' Trust Account (IOLTA) program or Bar  
17 Foundation as the designated entity for receipt of residual funds.

### 18 **III. Explanation of the Need for the Proposed Amendment**

#### 19 **A. The Amendment Will Provide Funding for Arizona Legal Services** 20 **Programs Whose Funding Has Been Reduced While Significant Unmet** 21 **Legal Needs Remain**

22 In Arizona, the legal services programs suffered a 13% reduction in 2012 in  
23 federal funding provided by the Legal Service Corporation.<sup>3</sup> As a result, the programs  
24 were forced to lay off staff and make drastic cuts in services. It is unlikely the federal  
25 reductions will be fully replaced in the foreseeable future. With over 1.1 million persons

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27 <sup>2</sup> Information provided by the American Bar Association's Resource Center for  
28 Access to Justice Initiatives, a project of the ABA Standing Committee on Legal Aid and  
Indigent Defendants.

<sup>3</sup> [www.lsc.gov/local-programs/state-profile?st-AZ](http://www.lsc.gov/local-programs/state-profile?st-AZ).

1 in Arizona receiving basic benefits such as food stamps and medical care, the number of  
2 persons eligible for legal services is huge.<sup>4</sup>

3 At the same time, interest rates on the IOLTA accounts have been at record low  
4 levels, barely above zero for the fifth consecutive year. There is no sign that interest rates  
5 will increase sufficiently to make a significant difference in IOLTA funding in the  
6 upcoming years. Across the nation, from 2007 through 2011, the amount of IOLTA  
7 funding has dropped by 68%.<sup>5</sup> Even with the inevitable rise of interest rates on IOLTA  
8 accounts, history has shown that this source of revenue “roller-coasters” every five to six  
9 years and other sources of support are needed to continue providing access to justice  
10 during the inevitable low times.

11 History also shows that while funding fluctuates, the demand for legal services  
12 only increases. In April 2013, a one-day count of requests for help to the three legal aid  
13 agencies (Community Legal Services, DNA-People’s Legal Services, and Southern  
14 Arizona Legal Aid) documented that over 600 people sought assistance from the  
15 programs in just that one day.<sup>6</sup> The need for legal services is growing and the current  
16 funding sources cannot keep pace, even with increased efficiencies, use of technology,  
17 *pro bono* support and *pro se* education. Thus, new funding sources are needed. As  
18 recognized by the AJTF and other states, one such additional funding source is the use of  
19 residual class action funds.

20 **B. Funding for Legal Services is a Responsibility of the Legal Professional**

21 The Arizona Bar Foundation respectfully asserts that the responsibility for  
22 ensuring legal services are available to those who cannot afford to pay for such services

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23 <sup>4</sup> The Arizona Department of Economic Security publishes the number of persons  
24 receiving public benefits each month. [www.azdes.gov/InternetFiles/Reports/pdf/  
25 dbme\\_statistical\\_bulletin\\_10\\_2013.pdf](http://www.azdes.gov/InternetFiles/Reports/pdf/dbme_statistical_bulletin_10_2013.pdf).

26 <sup>5</sup> Sandman, James, July 19, 2013, *Memorandum to Finance Committee, Request*  
27 *Recommendations(7.19.13)* pdf. found at [www.lsc.gov/sites/lsc.gov/files/LSC/pdfs/  
28 Management\\_sRevisedFY2015Budget](http://www.lsc.gov/sites/lsc.gov/files/LSC/pdfs/Management_sRevisedFY2015Budget).

<sup>6</sup> April 3, 2013 “The Difference One Day Makes” – snapshot service report of the  
three Legal Service Corporation funded legal aid agencies in Arizona. Report expected  
to be made public soon.

1 is placed upon the lawyers through the Preamble to Rule 42 of the Arizona Rules of  
2 Professional Conduct, Arizona Rules of the Supreme Court:

3 A lawyer should be mindful of the deficiencies in the  
4 administration of justice and of the fact that the poor, and  
5 sometimes persons who are not poor, cannot afford adequate  
6 legal assistance. Therefore, all lawyers should devote  
7 professional time *and resources and use civic influence* to  
8 ensure equal access to our system of justice for all those who  
9 because of economic or social barriers cannot afford or secure  
adequate legal counsel. A lawyer *should aid the legal  
profession in pursuing these objectives* and should help the  
bar regulate itself in the public interest. (emphasis added).

10 The responsibility of funding legal services is not the sole responsibility of the  
11 attorney, but there is a clear expectation that the attorney, as a professional member of the  
12 legal/justice system, *should* accept a role in the pursuit of equal access to justice.

13 Thus, the Arizona Bar Foundation also respectfully asserts that this proposal  
14 furthers the principles, purpose, and strategic goals of the Arizona Courts and the State  
15 Bar of Arizona as evidenced in the Arizona Supreme Court Rules of Professional  
16 Conduct and the Lawyer’s Creed of Professionalism adopted by the State Bar.  
17 <http://www.azbar.org/membership/admissions/lawyer’screedofprofessionalism>.

#### 18 **IV. The Rule 23 Amendment Utilizes the *Cy Pres* Doctrine to Further Access to** 19 **Justice**

20 Class actions are a procedural device for dealing with claims of injury that affect  
21 groups of persons too numerous to proceed as individuals in seeking redress or too  
22 difficult to identify before determining liability of a defendant to class representatives.  
23 The *cy pres* doctrine originated in sixth century Rome in the context of charitable trusts  
24 when an entity designated to receive the funds no longer existed and the receipt of the  
25 trust funds was then transferred to the “next best use.”<sup>7</sup> The *cy pres* doctrine was been  
26 adopted by state and federal courts to distribute residual funds in class action cases.

27 <sup>7</sup> Gayl, Josha. November 2011. “To *Cy Pres* or Not to *Cy Pres*?” For the Defense.  
28 <http://foxrothschild.com/uploadedfiles/FTD-1111-Gayl.pdf>.

1 In class action cases either by settlement or judgment, a fund is usually created to  
2 pay the class members' claims. In some cases, class members cannot be located, not all  
3 class members collect their portion of the award or the administrative costs to pay any  
4 claims outweigh the amount each class member would receive. Thus, residual funds  
5 remain. In these cases, Arizona courts have approved the application of the *cy pres*  
6 doctrine to class action cases.

7 'Cy pres' is a derivative from French meaning 'as near as.'  
8 Black's Law Dictionary 415 (8<sup>th</sup> ed.2004) ... It is also used  
9 to distribute unclaimed portions of a class-action judgment or  
10 settlement funds to a charity that will advance the interests of  
11 the class. *Id.* In the context of a class action settlement  
12 agreement, when it is not feasible to distribute the class  
13 recovery or when there is a balance that remains after  
14 distribution, the court may direct 'undistributed funds to be  
15 applied prospectively to the indirect benefit of the class.' 3  
16 Alba Conte & Herbert Newberg, *Newberg on Class Actions* §  
17 10.17 (4<sup>th</sup> ed. 2005) ('Newburg'). These funds are usually  
18 distributed to a third party for a specified purpose. *Id.*

19 *Charles I. Friedman v. Microsoft Corporation*, 213 Ariz. 344, 348, n. 7, 141 P.3d 824,  
20 828 n.7 (App. 2006).

21 One common premise underlying all class actions is to make access to justice a  
22 reality for persons who otherwise would not realistically be able to obtain the protection  
23 of the justice system. Thus, the purpose of the class action remedy creates access to  
24 justice where it would otherwise not be attainable because of the small size of individual  
25 awards or the large cost of litigating the issue involved compared to the likely award.  
26 Similarly, legal services programs provide access to justice for those who otherwise  
27 would have limited or no access to the justice system. This proposal recognizes that the  
28 distribution of residual funds to legal services and access to justice services to low-  
income persons serves the fundamental principle of access to justice and is a "next best  
use" in class action cases.

1 **V. The Rule 23 Amendment Furthers the Public Policy of the Arizona Bar**  
2 **Foundation/IOLTA Program to Support Access to Justice**

3 It was in the early 1970s that discussion of IOLTA programs began to be explored.  
4 The principle was simple; client funds in a lawyer's possession that are nominal or held  
5 for a short time would be pooled in an interest generating trust account and the interest  
6 would be allocated to law-related public activities through a nonprofit corporation. Some  
7 states developed their IOLTA programs through state legislation and others through  
8 court rule. In March 1978, the Supreme Court of Florida issued a decision establishing  
9 the first United States IOLTA program with the interest going to the Florida Bar  
10 Foundation. Key provisions in gaining approval for the IOLTA program concept  
11 addressed the Internal Revenue Service's concerns that the funds generated would not  
12 result in inurement to the benefit of private individuals and groups, but rather that they  
13 would be used exclusively for public purposes.<sup>8</sup>

14 In 1983-1984 Arizona established an IOLTA program under court rule and the  
15 Arizona Bar Foundation was entrusted with administering the IOLTA funds. The  
16 purpose of the IOLTA program is to create access to legal services and access to justice  
17 by aggregating small amounts of interest earned on short-term or small deposits that  
18 would not be sufficient to generate net earnings to their owners. Thus, the parallel  
19 between the use of class action remedies and the IOLTA program, supports use of the  
20 residual funds by the Arizona Bar Foundation.

21 The Arizona Bar Foundation, after three decades of operation, has administrated  
22 over \$41 million in IOLTA funding and continues to serve as the entity entrusted by the  
23 Arizona Supreme Court with this important function. The Arizona Bar Foundation has a  
24 proven track record and ensures that the IOLTA interest is used exclusively for the  
25 public purposes defined under Rule 43 of the Arizona Rules of the Supreme Court. The  
26 Arizona Bar Foundation is in the unique position of having a proven track record of

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27 <sup>8</sup> *Report to the Board of Governors Task Force and Advisory Board on Interest on*  
28 *Lawyer (sic) Trust Accounts*, Section VII, pages 13-21, American Bar Association, July  
26, 1982.

1     disbursing funds to a broad array of programs that provide legal services and access to  
2     justice services to those in Arizona.

3             The proposed amendment confirms that there is a procedural nexus between the  
4     ability of class members to secure relief in the judicial forum under Rule 23 and the  
5     interests of others who may similarly need access to the justice system to assert or defend  
6     critical legal rights and interests. The proposed amendment does not substantially  
7     interfere with the freedom of the parties or their attorneys to craft and propose class  
8     action settlements. What it does, is preclude the parties or their attorneys from allocating  
9     100% of the residual funds to charities of their choosing.

10            Finally, the proposal places no additional burdens on the courts or the parties in  
11     the management of class action cases. The amendment will support access to justice for  
12     many Arizonans who otherwise would have no legal assistance.

13     **VI. Potential Benefit from Residual Funds Designation**

14            The history of the implementation of similar provisions in other states shows that  
15     use of the residual funds can be an effective tool to support legal services. States vary in  
16     their procedures for either mandating or providing an option for the residual funds  
17     disbursement to an entity that supports legal services or access to the courts for low-  
18     income persons.

19            The American Bar Association Resource Center also attempts to collect  
20     information on how much funding is being generated annually by states with rule or  
21     statutory class action residual funds distribution provisions. There is not accurate or  
22     complete data for all states, but the existing data shows that the amount collected  
23     annually varies significantly, both from year to year within each state and from state to  
24     state.<sup>9</sup> The amount generated in states that do not require the award of a specific  
25     percentage of residual funds to legal services programs ranges from zero to \$3 million in  
26     California. States that mandate that a percentage of the residual funds go to access to  
27     legal services and access to justice tend to have higher amounts awarded, between \$3

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28     <sup>9</sup>     See footnote 2.

1 million and \$13 million annually recently in Illinois, Pennsylvania and Washington. In  
2 Washington, from February 2008 to April 2013, over \$8 million of residual funds were  
3 directed to the state’s IOLTA program.

4 Below is a brief summary of the state provisions mandating a percentage of  
5 residual funds distribution:

- 6 • 100%: North Carolina requires residuals to be divided equally between the  
7 Indigent Person’s Attorney Fund and the North Carolina State Bar “for the  
8 provisions of civil legal services for indigents” unless a court orders  
9 otherwise. N.C. Gen. Stat. § 1-267.10 (2012).
- 10 • 100%, with up to 50% discretion: South Dakota mandates that residual  
11 funds go to the Commission on Equal Access to Our Courts, but permits up  
12 to 50% to be distributed to “nonprofit charitable organizations that serve  
13 the public good if the court finds there is good cause to approve such a  
14 distribution as part of the settlement.” S.D. Codified Laws § 16-2-57  
15 (2012).
- 16 • 50% minimum: Pennsylvania requires that a minimum of 50% of residual  
17 funds be disbursed to the Pennsylvania IOLTA Board. Pa. R. Civ. P. 1716  
18 (2012).
- 19 • 25% minimum: Both Indiana and Washington require a minimum of 25%  
20 be disbursed to the Indiana Bar Foundation and the Legal Foundation of  
21 Washington, respectively. Ind. R. Trial P. 23(F)(2) (2013); Wash. C.R.  
22 23(f) (2012).

23 This information demonstrates that there is the potential for a large increase in  
24 funds designated toward access to justice efforts when rules and/or statutes concerning  
25 class action residual funds are amended. With seven states added since 2011, it is clear  
26 that there is a growing recognition and significant movement toward the use of residual  
27 funds as an appropriate way to obtain additional funding for legal services.

