Sulzer Medica Reaches Novel Class-Action Pact

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Body

Sulzer Medica AG, facing more than 1,000 lawsuits over faulty hip-replacement joints made by a unit in Austin, Texas, reached an unusual agreement to settle the cases for about $780 million in cash and stock.

The novel element is a provision designed to force all potential plaintiffs into the proposed ***class-action*** settlement, even if they believe their injuries are worth far more than the pact calls for.

Under the agreement, the Winterthur, Switzerland, medical-device maker would give all participants in the settlement a lien on its assets, meaning that payment of their claims would have priority over other liabilities -- including court awards to other plaintiffs. Thus, "if anybody opts out, they still have to try their case, win their case, win their appeal, and then there would be no assets to satisfy their judgment, because they are all pledged to the ***class***," said Richard Scruggs, a Pascagoula, Miss., attorney hired by ***Sulzer*** Medica to arrange the deal.

Mr. Scruggs's involvement is striking, as he is best known as a plaintiffs lawyer who helped lead the charge against the tobacco industry. In this case, Mr. Scruggs said he was introduced to ***Sulzer*** Medica executives by a physician who has assisted him in litigation against health-maintenance organizations. Mr. Scruggs said it was the first time in 20 years he has worked for a corporate defendant, and expects to be paid a "low seven-figure number," plus a "success fee" of about $20 million should the settlement be approved.

The company and ***class-action*** lawyers will seek preliminary approval of the agreement tomorrow from U.S. District Judge Kathleen M. O'Malley in Cleveland, who is overseeing suits against ***Sulzer*** Medica in federal court. Mr. Scruggs said he also plans to ask the judge to freeze lawsuits against the company that are pending in state courts.

But some attorneys representing plaintiffs called the deal unfair to injured patients and promised to challenge it in court. "It's ridiculous," said Andres Pereira of Fleming & Associates, a Houston law firm that so far has filed 23 cases against ***Sulzer*** Medica. ***Class-action*** lawyers "have cut a deal with the company that is to the company's benefit and probably will be to their benefit, but won't be to the benefit of the putative ***class*** members."

Some legal experts questioned whether the courts will permit the company to tie up its assets to benefit small claimants over more seriously injured people who might win big court awards. "Will a court say this is fair and equitable?" asks Columbia University law professor John Coffee. "The flaw here may be that it is too clever by half."

Even if the deal is approved, other plaintiffs still have the right to file suit. The settlement is "a dangerous game because it invites the other plaintiffs to try to put the company into bankruptcy to test the priority of those claims," Mr. Coffee said.

Still, news of the agreement sent the company's American depositary shares up 64%, or $3.30, to $8.50 in New York Stock Exchange composite trading. Some analysts had feared the litigation could drive the company into bankruptcy proceedings.

The hip-replacement devices involved are made of titanium and coated with a porous surface into which the patient's bone grows. The problem began after a 1999 change in the manufacturing process left a small residue of lubricant on the joint's surface, inhibiting the bone's ability to attach to the device.

In the summer of 2000, Mr. Scruggs said, the company began to note an unusually high failure rate for the product, and on Dec. 8 it issued a voluntary recall. "Unfortunately, about 30,000 had already been implanted," he said, along with a far smaller number of knee replacements, which suffered the same defect and are also part of the settlement. "The good news is, for the vast majority of them it isn't going to matter, since the problems usually develop in the first six months."

As of last Friday, 2,353 patients had to undergo new surgery for their hips, and 280 for their knees, according to ***Sulzer*** Medica. The company said it expects the total number of replacement surgeries to reach 4,000.

Under the deal, patients who underwent two or more surgeries to replace their implants would receive $97,500, plus medical costs. Those who had a single operation would get $57,500 plus medical costs, and those who didn't require additional surgery, $2,750. The payments would be two-thirds in cash and one-third in ***Sulzer*** Medica stock. "If they went to court they'd average five-hundred grand or more," Mr. Scruggs said of some of the victims. "Is it adequate? No. Is it fair? Yes."

Sulzer Medica plans to fund a settlement trust with $250 million in insurance, plus whatever cash it can borrow, said David Floyd, president of ***Sulzer*** Orthopedics, the Texas unit that made the joints. In addition, the company would pay half of its annual profits, or at least $25 million annually, into the trust for five to seven years.

The trust would include $30 million for "extraordinary cases" that deserve compensation above the set amounts, $20 million for monitoring of patients who haven't yet had problems and $4 million for research into the long-term effects. Plaintiffs attorneys probably would receive about $30 million, Mr. Scruggs said.

In July, ***Sulzer*** Medica was spun off from its majority owner, ***Sulzer*** AG. Company officials said the spinoff wasn't related to the hip-implant litigation, although some plaintiffs attorneys say they intend to go after the former parent, whose assets aren't protected by the settlement plan.

Notes

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