LITIGATION

Fair and Square?

Class actions provide some efficiency benefits, but widespread examples of abuse of this procedural tool are cause for alarm. **By James J. Farrell and Anthony N. Luti**

The number of class actions has grown tremendously over the last decade. Between 1988 and 1998, state court class actions alone increased by 1,042 percent. Surveys indicate that corporations are facing a 300 percent to 1,000 percent increase in the number of class actions against them.

But has the increased volume led to increased benefits to society? Many say no. Although class actions provide some efficiency benefits, the number of examples of abuse of this exceptional procedural tool is increasing.

Frivolous claims have been filed to capitalize on the risk class actions pose to defendants. Other cases have been settled without benefiting the plaintiffs but making the attorneys millions of dollars.

The Class Action Fairness Act of 2002 may be the answer. On the heels of the broad corporate and accounting reform in the Sarbanes-Oxley Act of 2002, the Senate is debating this additional piece of legislation, which may radically alter litigation between consumers or shareholders, on the one hand, and corporate America on the other.

Like the Sarbanes-Oxley Act, the Class Action Fairness Act of 2002 also is designed to protect consumers and shareholders. This time, however, the target of reform is the process itself. Although not perfect, the fairness act lives up to its name by providing for uniformity in nationwide class actions and increasing judicial scrutiny of class certifications and settlements.

Ironically, the rights and interests of individual class members are not the driving force behind many class actions. While enhanced efficiency makes class actions an important component of our judicial system, these types of cases deprive the individual plaintiff of control, creating the potential for abuse.

Such virtually "clientless" cases create what some commentators have referred to as "the seeds for questionable practices."

For example, in rejecting a settlement that provided no benefit to the class, a court recently described one proposed settlement as "the class litigation equivalent of the 'squeegee boys' who used to frequent major urban intersections and who would run up to a stopped car, splash soapy water on its perfectly clean windshield and expect payment for the uninvited service of wiping it off."

In other cases, plaintiffs have received only coupons or pennies on the dollar while the attorneys were compensated handsomely. In one example, attorneys brought a nationwide class action against a cereal maker over the use of a food additive, which the plaintiffs acknowledged had not injured a single consumer.

The settlement provided class members with a coupon for free cereal, provided that they purchased more cereal. Their lawyers were paid $2 million in fees, a rate of $2,000 per hour. By increasing judicial scrutiny during certification and settlement, the fairness act is designed to combat such abuses.

"[To] reduce forum shopping and gaming of the system in abusive class actions," the act would extend federal diversity jurisdiction to actions with the following characteristics: any class member is a citizen of a state different from any defendant (minimal diversity rather than complete diversity of the parties); the class has at least 100 members; and the class alleges at least $2 million in damages.

Although authorizing removal to federal court will not prevent abusive class actions completely, it will provide much-needed uniformity and scrutiny of class certification and settlements under Rule 23 of the Federal Rules of Civil Procedure.

As of 1999, no fewer than 14 states — comprising nearly 29 percent of the nation's population — had adopted a class-action certification standard that varies from Rule 23.

Surprisingly, some states, like Mississippi, have no class certification standard at all. Instead, each plaintiff sues individually, and cases raising similar issues can be joined.

The official comment to Mississippi's joinder rule describes its purpose as "allow[ing] *virtually unlimited* joinder at the pleading stage"

As a result, attorneys bringing class actions in Mississippi have no class certification hurdles to clear. They only need to satisfy a liberal joinder requirement. As a result, Mississippi has become a magnet for class-action filings.

And Mississippi is not alone in terms of attracting class actions. Madison County, Ill., with a population of fewer than 260,000, attracts more class actions each year than some of the nation's most populous communities.

"[Madison County judges] have previously expressed no qualms about certifying nationwide classes," some commentators say.

The fact that some states have high class certification standards — that is, stringent objective measures put in place to ensure that representative plaintiffs adequately represent the interests of the other class members — while other states have no certification standards at all reveals one of the primary problems with the system.

Expanding federal jurisdiction over class actions will heighten the predictability of these cases. By mandating the application of Rule 23 and its certification requirements, the Class Action Fairness Act of 2002 would implement an objective evaluation of whether the rights of many should be resolved in unison.

As attorneys in this field know, certification of class is a crucial decision which can exponentially inflate the risks and costs of a case regardless of the underlying merits. This critical decision should be made with objective standards.

The fairness act also would increase judicial scrutiny of settlements, especially those with nonmonetary components. Nearly all class actions are settled, binding all of the defined class members to the terms of the settlement unless they expressly opt out.

While they do receive notice, most class members never talk to their lawyer, and no one solicits their individual input on, or even explains, the terms of a proposed settlement.

Thus, it is imperative that the resolution of so many rights be open and candid. The act mandates that every class member receive an easily understood description of the proposed settlement terms, and it requires the court to make particular findings that the settlement is fair and furthers the interests of the class. Essentially, the process is identical to the process employed by federal courts.

Calling it "legislative overkill," critics of the fairness act contend that having federal courts resolve state law claims creates a problem.

But others argue that the status quo results in "reverse federalism," with state courts setting federal policy by certifying and adjudicating nationwide class actions that resolve the rights of people across the country.

The act addresses federalism concerns by limiting its extension of jurisdiction: There is no federal jurisdiction in cases where a "substantial majority of the proposed plaintiff class and the primary defendants are citizens of the State in which the action was originally filed."

Moreover, having federal courts resolve state claims is not inherently repugnant to federalism. Federal courts resolve cases involving purely state law claims in standard diversity cases.

Class actions involving hundreds or thousands of individuals from across the country, as well as defendants from different states, are conceivably a logical extension of diversity jurisdiction.

Allowing a small number of states to continue to resolve the rights of others across the nation is far more repugnant to federalism. The citizens of one state cannot vote for another state's legislators or judiciary. As a result, they cannot affect the procedural or substantive laws of the forum resolving their case, which undermines the checks and balances vital to our system.

Class actions are a crucial component of our judicial system, but like all other tools, they can be abused. The fairness act would lessen the potential for abuse by providing uniformity and ensuring judicial scrutiny over class certifications and settlements. Doing so, the act would reduce the risk of abuse without hindering the fair resolution of legitimate cases.

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