

The Class Action Fairness Act of 2005: An Analysis

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INTRODUCTION

On January 25, Senator Charles Grassley (R-Iowa) introduced S. 5, the Class Action Reform Act of 2005. The bill was virtually identical to one that had failed the previous July and largely the same as one that was blocked by a filibuster in October 2003. But this time — the November election having resulted in consolidated Republican control over the Senate and an intact Republican majority in the House of Representatives — the bill quickly cleared the Senate Judiciary Committee without amendment, and without a written report to slow its momentum. A week later, the Senate acted on the bill, which passed 72-26 with 18 Democrats' votes.¹

House Republicans had long favored a more pro-defendant bill, but in the interest of finally passing class action legislation, the House leadership had announced that if the Senate passed the Grassley bill without amendment, the House would do likewise. On February 17, 2005, a week after the Senate acted, the House leaders made good on their promise. Bypassing the formality of a report by the House Judiciary Committee, the House considered the bill under a rule allowing barely more than two hours of debate. Following the debate, the House vote was nearly as lopsided as the Senate's, with the bill passing by 279-149.

The President signed the bill on Friday, February 18 — the day after the House acted. The law is now in effect. But what does it mean?

In a nutshell, the Class Action Fairness Act has two principal parts. One set of provisions establishes new procedural and substantive standards applicable to class action settlements. Some of these merely duplicate (or add little to) existing practice under the Federal Rules of Civil Procedure, but others — such as new limitations on attorneys' fees in coupon settlements and requirements that government officials be notified whenever a class action settles — are brand new.

¹ A few weeks after the Act's passage, a Senate Report was published. See S. Rep. No. 109-14. Its authority as legislative history may be questioned because it was clearly not available to any of the Senators or Representatives who voted on the bill. The report may be found at <http://www.abanet.org/litigation/committee/classact/cafa2005.html>, together with the full text of the Act (and an earlier version of this article).

The other, more important, set of provisions casts aside traditional principles of statutory diversity jurisdiction and provides for both original federal jurisdiction and removal of state-law based class actions that until now could be filed only in state courts. The provisions are complex and require detailed explication. Fundamentally, however, the Act makes the ordinary requirement of “complete diversity” of citizenship inapplicable to class actions, and provides federal jurisdiction when some class members and some defendants are from different states. It also eliminates the principle that the claims of class members cannot be aggregated to meet the amount-in-controversy requirement, and provides for federal jurisdiction when the total amount in controversy in a class action exceeds \$5 million. The effect is to allow most class actions with classes or defendants including citizens of more than one state to be filed in or removed by defendants to federal court.

The Act is complicated, and the jurisdictional provisions in particular have a number of exceptions. A detailed analysis of its provisions is essential to understanding its effect on class action practice.

THE ACT’S PROVISIONS

1. Effective Date

The most pressing, immediate question a practitioner may have is whether the Act applies to a particular case. That key question is addressed in the very last section of the Act, section 9, which provides: “The amendments made by this Act shall apply to any civil action commenced on or after the date of enactment of this Act.” In short, the Act applies to class actions filed on or after Friday, February 18, 2005. It does not apply to actions already pending on that date.

Already, defendants have tested this provision by attempting to remove cases that were pending before February 18, 2005. Relying on cases involving the effective date of past legislation increasing the jurisdictional amount provisions of the diversity statute, these defendants have argued that a “civil action” is “commenced” on the date it is removed, not the date it was originally filed in state court. As of this writing, however, these efforts to remove already-pending cases have been unsuccessful. In the leading case, *Pritchett v. Office Depot, Inc.*, __ F.3d __, 2005 WL 827158 (10th Cir. April 11, 2005), the Tenth Circuit held that the language of the statute, the presumption that removal provisions are to be narrowly construed, the legislative history, and considerations of public policy all point to the same conclusion: “removal to federal court does not ‘commence’ an action for the purposes of the Class Action Fairness Act of 2005.” *Id.* at *5.

Significantly, the effective date provision applies to all of the changes made by the Act, including the provisions on settlements, which presumably could have been applied to future settlements in pending actions without raising concerns about unfair retroactivity. Applying the removal and jurisdictional provisions to previously filed actions, by contrast, would have been far more disruptive of settled expectations.

The bottom line is that cases already filed in state court are not subject to removal under the Act, which presumably will elicit a sigh of relief from plaintiffs’ lawyers with pending state-court class actions. But because the drafters of the Act chose a uniform, bright-line approach to the effective date for all provisions of the new law, settlements of class actions in federal courts for years to come will

be subject to two different sets of procedures, depending on the date of filing of the action. Thus, the effective date provision simplifies everyone's life insofar as it applies to the jurisdictional and removal provisions, but will be an ongoing source of complication for settlements.

2. Jurisdictional Provisions

a. The Basic Rules

The Act's provisions for original jurisdiction and removal jurisdiction over multistate class actions are its most important features. They are critical both to the hopes of the Act's backers that it will remove "frivolous" class actions from so-called state-court "hellholes," and to the fears of its opponents that it will shunt cases that have merit under state law into federal courts that are hostile to certification of classes in those cases (and that may be more restrictive than some state courts in construing state-law causes of action, or more receptive to defenses such as federal preemption). The jurisdiction and removal provisions are also the most fundamental changes made by the Act to the status quo, and will have the broadest impact.

Understanding the significance of the changes worked by the Act requires a basic understanding of the status quo ante. Under the law as it stood before the Act's passage, class actions raising federal claims could be freely brought in or removed to federal court by virtue of the broad grant of federal question jurisdiction in 28 U.S.C. § 1331. But most class actions raising only state-law claims could reach federal court only if they satisfied the requirements for diversity jurisdiction under 28 U.S.C. § 1332. Section 1332 posed two significant obstacles to federal jurisdiction over such class actions: The "complete diversity" rule and the amount-in-controversy requirement.

For class actions, the "complete diversity" requirement, as created and refined in judicial decisions, was that all named class representatives and all defendants had to be citizens of different states. If any named plaintiff and any named defendant were from the same state, the action could not be filed in or removed to federal court. *See Strawbridge v. Curtiss*, 7 U.S. 267 (1806); *Supreme Tribe of Ben-Hur v. Cauble*, 255 U.S. 356 (1921). As for the amount-in-controversy requirement, in most cases the claims of class members could not be aggregated to satisfy the \$75,000 jurisdictional amount in diversity cases. *See Snyder v. Harris*, 394 U.S. 332 (1969). Thus, at least one class member had to have a claim for more than \$75,000; and, under the Supreme Court's decision in *Zahn v. Int'l Paper Co.*, 414 U.S. 291 (1973), all class members had to have claims exceeding \$75,000.² Importantly, both the "complete diversity" requirement and the amount-in-controversy are purely statutory; Congress has constitutional authority under Article III to create diversity jurisdiction as long as there is "minimal diversity" between some plaintiffs and some defendants, and it need not create amount-in-controversy requirements at all.

² There is a split in the Circuits over whether *Zahn* is still valid in light of the supplemental jurisdiction statute, 28 U.S.C. § 1367, and the Supreme Court has granted certiorari to resolve it in the case of *Exxon Corp. v. Allapattah Servs.*, No. 04-70 (argued March 1, 2005). However, all the Circuits have agreed that, regardless of *Zahn's* survival, at least one named plaintiff in a class action had to meet the jurisdictional amount requirement.

Because Congress had not exercised the full scope of its authority to create diversity jurisdiction, the combined effect of the statutory requirements was to keep many class actions based on state law claims out of federal court. All a plaintiff had to do was avoid pleading a federal claim, and name at least one non-diverse plaintiff or defendant or name only class representatives whose claims did not reach \$75,000 (not too difficult, particularly in consumer class actions). Absent special circumstances (such as state-law claims that were completely preempted by federal law, or fraudulent joinder), such class actions could not be removed by defendants to federal court, no matter how much they might object to the particular state-court forum selected by class counsel.

The new Act changes all that. It amends both the diversity statute (28 U.S.C. § 1332) and the removal laws (28 U.S.C. §§ 1441 et seq.) to provide for federal jurisdiction, at the election of either the plaintiff or the defendant, over class actions that do not satisfy the traditional “complete diversity” and amount-in-controversy requirements. The basic innovation of the new law (subject to important exceptions to be described later) is that it establishes federal jurisdiction over any action in which any one member of the class (named or not) has diverse citizenship from any one defendant, and where the aggregate amount in controversy exceeds \$5 million. 28 U.S.C. § 1332(d)(2).³

To take a concrete example, suppose a class with 10,000 members sues GM and one of its dealerships located in Illinois, raising state-law fraud claims. The named class representatives all live in Illinois, but some class members live in Wisconsin, Iowa, Missouri, Indiana, and Michigan. The individual class members’ claims average \$600, and no class member has a claim exceeding \$2,000. Under the law as it stood before the Act’s passage, the class action could not be brought in or removed to federal court, both because there was not complete diversity between the named class representatives and the defendants (one defendant was a citizen of the same state as the plaintiffs) and because no individual plaintiff’s claim exceeded the jurisdictional amount. Under the new law, the case could be filed in or removed to federal court because of the diversity of citizenship between the named representatives (Illinois) and GM (Michigan) — not to mention that between some non-named class members (various states) and both defendants — and because the total amount in controversy (\$6 million) exceeds the jurisdictional amount.

The same would be true if the named class representatives all lived in Michigan and the Illinois defendant were omitted: the diversity between some non-named class members and GM would still suffice to permit federal jurisdiction (assuming the case did not fall into one of the statutory exceptions).

The impact of the new provisions is obvious. The elimination of the complete diversity requirement and the provision for aggregation of claims to meet the amount-in-controversy requirement will mean that many cases that formerly could not be brought in federal court are now subject to federal jurisdiction. Most class actions can at least be argued to involve an aggregate amount in controversy of \$5 million or more, and classes that don’t involve some out-of-state members (or some defendants from different states) are rare.

³ Cites to 28 U.S.C. are to provisions as amended or added by the Act. Only where a provision of the Act is not codified in 28 U.S.C. will the section of the Act be cited.

b. Removal

The removal provisions of the new act are coextensive with the original jurisdiction provisions, so any class action that fits within the new diversity provisions can be removed to federal court. *See* 28 U.S.C. §1453 (newly added by the Act). The new removal provisions for class actions generally incorporate the standard removal requirements and procedures set forth in 28 U.S.C. §§ 1441 and 1446, with a couple of important exceptions that significantly expand the possibility of removal.

First, in most cases where removal is based on the existence of diversity jurisdiction under § 1332, removal is only permitted if no defendant is a citizen of the forum state. 28 U.S.C. § 1441(b). The Act removes this requirement for class actions, providing specifically that an action may be removed “without regard to whether any defendant is a citizen of the State in which the action is brought,” and further providing that any defendant may remove without the consent of other defendants. 28 U.S.C. § 1453(b).

Second, 28 U.S.C. § 1446(b) generally provides that a removal petition in a diversity case may not be filed more than one year after an action is commenced, even if the facts showing that the case is removable are first revealed after the end of the one-year period. The Act removes this one-year limitations period for class actions. 28 U.S.C. § 1453(b). Thus, under the Act, a removal petition may be filed within 30 days of the first pleading or paper filed in any state-court class action from which a defendant can ascertain that the action falls within the scope of federal jurisdiction under new 28 U.S.C. § 1332(d).

Third, existing law generally provides that when a federal district court determines that removal is not proper and remands to the state court, the remand order cannot be reviewed on appeal. 28 U.S.C. § 1447(d). The Act, however, provides that a court of appeals may (*not must*) accept an appeal of an order either granting or denying a motion to remand, if an application for permission to appeal is filed within seven days of the order. If a court of appeals accepts such an appeal, it *must* decide it within 60 days, unless all parties agree to an extension (which can be of any length) or the court grants an extension of no more than 10 days for good cause shown. If the court of appeals does not decide the case within the time limit, the appeal is denied. Such a binding requirement on a court of appeals to complete its deliberations so quickly or be deemed to have affirmed is, to say the least, a sharp departure from any known provision of federal law and may raise constitutional concerns. (Notably, however, while the provision may prevent a court of appeals from delaying a decision once it has agreed to accept an appeal, it will do nothing to require the appellate court to act promptly on the request for permission to appeal. Thus, the provision, however novel, may ultimately be ineffective to prevent delays of remand appeals.)

c. The Exceptions

Although the new jurisdictional provisions for class actions are very broad, they are not unlimited, and there are exceptions built into the statute. Some of the exceptions are quite complicated. As a general matter, however, they are intended to keep the following kinds of cases out of federal court: class actions that involve both class members and defendants who mostly are citizens of the forum state; class actions against state government defendants; class actions with fewer than 100 class members; and shareholder class actions or derivative suits based on state corporation law.

First, a federal court *may not* exercise diversity jurisdiction over a class action (or accept removal jurisdiction) if two-thirds of all class members are citizens of the forum state, and either all “the primary defendants” are citizens of the same state, *or* at least one defendant from whom “significant relief” is sought and whose conduct is a “significant basis” of the claims asserted is a citizen of the forum state. In the latter instance, however, the bar to federal jurisdiction applies only if the “principal injuries” from the conduct of “each defendant” were suffered in the forum state, 28 U.S.C. § 1332(d)(4), and no other “similar” class actions have been filed within the past three years. Together these provisions allow some class actions to proceed in state court where the great majority of the class and one or more significant defendants are citizens of the forum state.

Second, a federal court is *permitted* to decline jurisdiction where the primary defendants and between one-third and two-thirds of the class members are citizens of the forum state. 28 U.S.C. § 1332(d)(3). In deciding whether to exercise its power to decline jurisdiction, the court must consider the “interests of justice” and “the totality of the circumstances,” including whether the claims involve matters of national interest, whether they involve the application of the law of states other than the forum state, whether the class action was pleaded in an effort to avoid federal jurisdiction, whether there is a “distinct nexus” between the case and the forum state, whether the class members who are citizens of the forum state substantially predominate over citizens of other states, and whether similar class actions have been brought within the past three years. Presumably, a district court’s balancing of these factors can be reviewed on appeal if it either dismisses a case originally filed in federal court (in which case its decision is appealable as of right), or if it remands a case that was removed by a defendant (in which case the permissive appeal provisions of 28 U.S.C. § 1453 apply).

Third, a class action based on state law may not be filed in or removed to federal court if the primary defendants are states, state officials, or “other governmental entities against whom the district court may be foreclosed from ordering relief.” 28 U.S.C. § 1332(d)(5)(A). Federal courts are generally barred by the Eleventh Amendment from hearing state-law claims against either state governments or state government officials (*see Pennhurst State Sch. & Hosp. v. Halderman*, 465 U.S. 89 (1984)), so it would be simply bizarre to provide for federal jurisdiction over class actions involving such defendants.

Fourth, a non-federal question class action is not subject to the new provisions for diversity jurisdiction or removal if the total number of class members is less than 100. 28 U.S.C. § 1332(d)(5)(B). Presumably, however, if such an action met the preexisting requirements for diversity jurisdiction (that is, there was complete diversity and the amount in controversy without aggregation exceeded \$75,000), it could still be filed in or removed to federal court under statutory provisions predating the Act.

Finally, the Act excludes from its coverage certain actions involving securities and corporate governance claims. The most important of these exclusions (sometimes referred to as the “Delaware carve-out”) applies to actions that solely involve claims relating to “the internal affairs or governance of a corporation or other form of business enterprise and that aris[e] under or by virtue of the laws of the State in which such corporation or business enterprise is incorporated or organized.” 28 U.S.C. § 1332(d)(9)(B); *see also* 28 U.S.C. § 1453(d)(2). The effect of this exclusion is to prevent shareholder derivative actions or other representative actions involving state corporation law issues

from being entirely federalized, a result that most corporations (not to mention the Delaware Chancery Court) would not favor.⁴

It is hard to generalize about the effect of the various exceptions. Some, like the exclusions of state-law corporate governance claims and actions against states, define classes of cases that are completely outside the central concerns of the Act. Others, like the exclusion of classes of fewer than 100 members, seem likely to have minimal impact.

The provisions involving classes whose members are concentrated in the forum state — the two-thirds/one-third provisions — are harder to evaluate. Some supporters of the Act view them as preserving state-court authority over significant numbers of cases. But their effect is limited by their applicability only where the major defendants are being sued in their own home states. In most state-court class actions potentially subject to removal, that will not be the case. The number of cases where the class definition will be such as to call the two-thirds and one-third provisions into play also seems unclear. Outside of cases where a class is defined to include only citizens of a particular state, there may be few cases where class members will be so concentrated in individual states that the two-thirds requirement could be met. Moreover, in cases where the two-thirds/one-third provisions may potentially apply, it is likely to be extremely difficult, at the outset of a case, to determine whether they do. Satellite litigation over the number of class members who are citizens of the forum state may be the result. Another fertile source of litigation relating to these provisions may be the meaning of the undefined term “primary defendants.”

d. What Is a “Class Action,” Anyway?

The discussion so far of the jurisdictional and removal provisions has begged the question of what is a “class action” — a critical issue because jurisdiction under new section 1332(d) and removal under new section 1453 depend on whether a case is a class action. The basic definition, for purposes of both original and removal jurisdiction, is that “the term ‘class action’ means any civil action filed under rule 23 of the Federal Rules of Civil Procedure or similar State statute or rule of judicial procedure authorizing an action to be brought by 1 or more representative persons as a class action.” 28 U.S.C. § 1332(d)(1)(B). That seems simple enough. Indeed, if the statute stopped there, it would appear that the jurisdictional and removal provisions would not apply to any case that was not actually called a class action either under Rule 23 or under its state-law analogs.

But the Act doesn’t stop there. It also provides that a “mass action shall be deemed to be a class action.” 28 U.S.C. § 1332(d)(11)(A). What, one might ask, is a “mass action”? Well, it is any civil action other than a class action “in which monetary relief claims of 100 or more persons are proposed to be tried jointly on the ground that the plaintiffs’ claims involve common questions of law and fact.” 28 U.S.C. § 1332(d)(11)(B)(i). That may encompass a number of different kinds of cases, but it seems especially aimed at “joinder” and “consolidation” cases under Mississippi and West Virginia

⁴ The same paragraph of new § 1332(d) that contains the carve-out for state corporate governance cases also excludes from coverage certain claims relating to securities as defined by federal law. The purpose of this exclusion seems to be to make clear that the Act is not supposed to displace the Private Securities Litigation Reform Act, 15 U.S.C. § 78u-4, which already created new procedures applicable to federal securities class actions. The exclusion seems largely superfluous, however, since such actions are generally subject to federal question jurisdiction, and the new diversity principles set forth in § 1332(d) would not apply to them anyway.

procedure, in which large numbers of nominally distinct individual claims are tried together, with an impact on defendants similar to that of a class action.⁵

The “mass action” provision, however, has some significant limitations. First, it provides for jurisdiction only over those individual claimants whose claims meet the jurisdictional amount limitation of 28 U.S.C. § 1332(a) — that is, \$75,000. *See* 28 U.S.C. § 1332(d)(11)(B)(i). Except for those claims not meeting the requirement of “complete diversity” under preexisting law, many such claims would already be within the scope of federal jurisdiction.

Second, the law does not permit federal jurisdiction over “mass actions” involving an “event or occurrence” that took place within the forum state and caused injury in that state and contiguous states. 28 U.S.C. § 1332(d)(11)(B)(ii)(I).⁶

Third, there is no federal jurisdiction under the Act over a “mass action” if it is the result of a *defendant’s* motion for joinder; thus, a defendant can’t get individual claims filed against it in state court into federal court by having the state court consolidate them and then removing the case as a “mass action.” 28 U.S.C. § 1332(d)(11)(B)(ii)(II).

Fourth, and of considerable importance, a “mass action” does not include private attorney general actions (or, in the words of the Act, claims “asserted on behalf of the general public (and not on behalf of individual claimants or members of a purported class) pursuant to a State statute specifically authorizing such action”). 28 U.S.C. § 1332(d)(11)(B)(ii)(III). Thus, claims under California Business & Professions Code § 17200 will not be affected unless they are specifically pleaded as class actions.⁷

Finally, and somewhat redundantly, the Act provides that “mass actions” do not include claims that are consolidated for pretrial purposes only. 28 U.S.C. § 1332(d)(11)(B)(ii)(IV). Such claims, of course, would not meet the basic definition of a “mass action” anyway because they are not proposed to be “tried jointly.”

The “mass action” provisions may prove to have relatively little effect. They can be evaded by simply not joining more than 99 individual claims. Moreover, to the extent one purpose of the Act is to bring state-court class actions into federal court where they may be subject to more stringent certification requirements, that purpose will not necessarily be served by removal of a “mass action.” In such a case, the plaintiffs will not need to seek certification because it was never intended to be a class action, and the federal court will have to deal with the individual claims of all of the “mass action” plaintiffs regardless of whether the case could qualify for class certification under Rule 23.⁸

⁵ Because of “tort reform” legislation in Mississippi and recent Mississippi decisions limiting the application of that state’s joinder doctrines, *see MS Life Ins. Co. v. Baker*, No.2003-IA-01149-SCT, 2005 WL 67522 (Miss.2005), and *Harold’s Auto Parts, Inc. Mangialardi*, 889 So.2d 493 (Miss.2004), Mississippi practice may no longer be as great a concern to defendants regardless of the Act.

⁶ The conditions under which there is federal jurisdiction over such “mass accident” claims are already set forth in 28 U.S.C. § 1369.

⁷ Once again, however, recent changes to § 17200 limiting the circumstances in which private attorney general actions may be brought may diminish the effect of this exclusion.

⁸ Indeed, the Act contains a provision that will discourage plaintiffs’ counsel in a “mass action” from seeking class certification if the action is removed: It provides that mass actions are exempt from being transferred for Multidistrict Litigation proceedings unless the plaintiffs seek class certification. 28 U.S.C. § 1332(d)(11)(C).

e. Effect on Jurisdiction if Class Not Certified

An earlier version of the Class Action Fairness Act passed by the House (but not the Senate) in 2003 would have provided that if a federal court denied class certification in a case where federal jurisdiction depended on the new class action jurisdiction/removal provisions, the court was required to dismiss the action. (The action could then be refiled in state court, but it would again be subject to removal, denial of class certification, and dismissal by the federal district court.)

As enacted, the Class Action Fairness Act contains no such provision. Presumably, since diversity jurisdiction ordinarily depends on the facts at the time of filing and is not affected by subsequent events, *see Grupo Dataflux v. Atlas Global Group, LP*, 541 U.S. 567 (2004), the district court would retain jurisdiction over an action brought in or removed to federal court under the Act even after it denied class certification. Any individual claims of the named class representatives, therefore, would remain to be decided by the federal court after a denial of class certification, even if there would have been no arguable basis for federal jurisdiction over them if they had originally been filed as part of a non-class action. In such a case, however, a plaintiff who preferred that her individual claim be heard in state court could dismiss the case in federal court and file a non-class-action in state court (assuming the filing would still be timely under state statutes of limitations and tolling principles), which would not be subject to removal.

3. The Settlement Provisions

In addition to its jurisdictional and removal sections, the Class Action Fairness Act adds a new Chapter 114 to Title 28 of the United States Code setting forth a number of requirements applicable to the settlement of class actions in federal courts. Some of the new requirements are wholly or largely duplicative of existing practice under Rule 23, but some represent substantial changes. All of the provisions are applicable only to class actions, narrowly defined as cases filed in federal court under Rule 23 or filed as class actions in state court and removed to federal court. 28 U.S.C. § 1711(2).

a. Coupon Settlements

Supporters of the Act aimed a great deal of their rhetoric at coupon settlements, usually described as settlements where class members get coupons of dubious value while class counsel get cash. Given the degree to which coupon settlements were mentioned in connection with the need for reform, a person reading the Act for the first time might be surprised at how little it says about them. In essence, the Act adds one section to the U.S. Code, 28 U.S.C. § 1712, which addresses two aspects of coupon settlements: their overall fairness, and the award of attorneys' fees in coupon settlements.

As to the basic fairness of coupon settlements, the Act provides that a court may approve a class action settlement involving coupons "only after a hearing to determine whether, and making a written finding that, the settlement is fair, reasonable and adequate for class members." 28 U.S.C. § 1712(e). Of course, Rule 23 already provides exactly that; indeed, this standard has been applied by federal courts to class action settlements for at least 30 years. Courts that have found coupon settlements fair, reasonable and adequate under existing law are unlikely to change their view in light of the new statutory provision.

Section 1712(e) does go beyond existing law in one minor respect: It explicitly provides that a court has discretion to require that in a coupon settlement, some portion of the value of unclaimed coupons be distributed to charity (and it forbids an award of attorneys' fees based on the value of the contribution of unclaimed coupons). It seems doubtful that this provision would materially change the terms of any settlement that a court would have approved under Rule 23 before the Act's passage. Some judges, however, may exercise their discretion to add such "cy pres" provisions to settlements that they would otherwise just have approved, and the statute may also encourage parties to include such provisions in more settlements and make it more likely that courts will approve them.

The provisions regarding the award of attorneys' fees in coupon cases, by contrast, work an important change in existing law. New section 1712(a) sets forth the basic rule that in a coupon settlement, "the portion of any attorney's fee award to class counsel that is attributable to the award of the coupons shall be based on the value to class members of the coupons that are redeemed." In other words, attorneys will no longer be able to receive fees based on the gross amount of coupons awarded, or even upon predictions of how many coupons will be redeemed. Any percentage-based fee can be awarded only on the basis of the value of coupons actually redeemed.⁹

In cases where a settlement involves both coupons and injunctive relief, the Act provides that any portion of the fee attributable to coupons shall be calculated on the basis of the coupons actually redeemed, while any fee attributable to the equitable relief shall be determined on the basis of the hours expended — i.e., a "lodestar" basis, with a multiplier if the court deems it appropriate. 28 U.S.C. § 1712(c).

What if a settlement includes both coupons and cash? Here the statutory language is, to put it charitably, opaque. The situation is governed by 28 U.S.C. § 1712(b), which provides that in such cases, "if ... a portion of the recovery of the coupons is not used to determine the attorney's fee to be paid to class counsel, any attorney's fee award shall be based upon the amount of time class counsel reasonably expended working on the action." This language is so unclear that courts will undoubtedly face some difficulty in dealing with it, but it appears to mean that part of the fee can be based on the value of the coupons redeemed, but the fee for the cash portion of the settlement must be calculated on a lodestar basis. If this is what the language means, it would be a substantial departure from current practice, which generally permits percentage-based fees in settlements involving cash payments.

b. Other "Protections" for Class Members

New section 1713 of Title 28 provides that a court may approve a settlement in which class members incur out-of-pocket losses to compensate class counsel "only if the court makes a written finding that non-monetary benefits to the class member substantially outweigh the monetary loss." New section 1714 prohibits class settlements that provide payment of greater amounts to some class members "solely on the basis that the class members to whom the greater sums are to be paid are located in close geographic proximity to the court."

⁹ The Act further provides that expert testimony on the value to class members of the coupons that are redeemed is admissible in the discretion of the court, 28 U.S.C. § 1712(d), but the basic standard under the Act will still be actual redemption, not redemption rates as predicted by experts.

These provisions are, to put it mildly, inconsequential. Settlements that put class members out-of-pocket to pay class counsel are very rare, and, under Rule 23, would likely be approved by a court as fair only if the class received significant non-monetary benefits even without this new statute. Thus, the statute permits settlements to put plaintiffs out-of-pocket under the same circumstances that they might already be put out-of-pocket under Rule 23; indeed, it may even slightly encourage such settlements by expressly authorizing them. As for geographic proximity, a settlement that accorded benefits solely on that basis could not conceivably pass muster under Rule 23. There is probably little that is objectionable about the new provisions, but they hardly seem worth writing into the United States Code.

c. Notifications to Federal and State Officials

In a major departure from existing practice, the Act creates 28 U.S.C. § 1715, which requires that notice of any settlement of a class action in federal court be provided to “appropriate” federal and state officials. For all settlements, the Attorney General of the United States is an “appropriate federal official,” 28 U.S.C. § 1715(a)(1)(A), while the term “appropriate state official” means either a state official who has regulatory authority over matters at issue in the case, or, if there is no such official, the attorney general of any state in which any class member lives. 28 U.S.C. § 1715(a)(2). In cases involving regulated financial institutions, the federal officials who must be notified also include whoever has primary regulatory authority over the institutions at issue (e.g., the FDIC).

The notice to be provided must be sent no more than 10 days after a proposed settlement is filed in federal court, and it must include: the complaint; notice of any scheduled hearing; copies of notices to class members informing them of opt-out rights and/or of the settlement; copies of the settlement itself and any side agreements; copies of any (proposed) final orders or judgments; and copies of related judicial opinions. In addition, the notice must, to the extent possible, inform the appropriate state officials of the identities and/or numbers of class members residing in their states. 28 U.S.C. § 1715(b). Responsibility for providing the required notice falls on “each defendant.” *Id.* Failure to provide the required notice means class members may choose not to be bound by the settlement. 28 U.S.C. § 1715(e).

Whether the huge volume of paperwork that these provisions entail will benefit anyone is not entirely clear. Perhaps the authors of the Act took the view that the U.S. Attorney General does not receive enough junk mail. Presumably, however, the thought is that federal and state officials will do something to police the fairness of the settlements of which they will receive notice. Nowhere, however, does the Act require the Attorney General or other “appropriate federal officials” to do anything with the notices they will receive, and it would likely be unconstitutional for Congress to attempt to require “appropriate state officials” to take any action.

Ironically, the one federal agency that does have an active program of reviewing the fairness of consumer class action settlements — the Federal Trade Commission — will not receive notices under the Act. Perhaps the Justice Department will respond to the notices by instituting a program of reviewing class action settlement fairness (though in light of the Department’s focus on the war on terrorism, on top of its other traditional responsibilities, a major new undertaking in the area of class action settlement review seems unlikely). Or perhaps the Justice Department will pass some or all of the notices it receives on to the FTC to bolster its existing Class Action Fairness Project. And it does

seem likely that some enterprising state attorneys general will make use of the material to subject questionable settlements to increased scrutiny. The provisions may also create a repository of information on settlements that will be subject to the federal Freedom of Information Act and its state counterparts, permitting private watchdog groups greater access to the terms of settlements.

d. Miscellaneous Provisions

Finally, section 6 of the Act requires the Judicial Conference, within one year of the Act's passage, to report to Congress on class action settlements, and on best practices to ensure their fairness and to award appropriate fees to class counsel. The section further provides that it does not in any way diminish the courts' authority to supervise the award of fees. Section 7 of the Act goes on to provide (anachronistically) that the changes to Rule 23 promulgated by the Supreme Court in March 2003 shall go into effect upon passage of the Act or December 1, 2003, whichever comes sooner. (This is a survivor from the 2003 version of the Act, and it has no effect because the amended Rule 23 already went into effect on December 1, 2003.) Finally, Section 8 of the Act preserves the Supreme Court's authority to prescribe rules of civil procedure governing class actions.

4. Some Provisions That Were Not Enacted

The version of the Class Action Fairness Act passed by the House of Representatives in 2003 included several provisions that prompted broad criticism and were omitted from the law as ultimately enacted. Most prominent among these was a provision that would have made all decisions on class certification — up or down — immediately appealable as a matter of right. The Judicial Conference, in particular, objected to the impediment that such a rule would create to the prompt administration of justice. The final version of the Act contains no such provision, leaving appeals of certification decisions subject to the discretionary review provision of Rule 23(f).

The 2003 House bill also would have provided for removal of state class actions at the behest not only of defendants, but also of plaintiff class members, and would have allowed class members to remove following a state-court class certification decision (which in most cases would occur long after the defendants' time to remove had expired). Such a provision would arguably create some possibilities for mischief, allowing defendants who had forgone removal rights to find a dissident class member to act for them if they later changed their minds. It would also have had the potentially beneficial effect of allowing class members who feared a state court would approve an unfair settlement to remove to federal court where they might have greater protection under the terms of Rule 23. (Indeed, under the removal standards of the Act, it may be that almost the only cases that defendants will not immediately remove will be those where a settlement is filed at the same time as the class complaint in a court viewed as likely to approve the settlement, and in those cases allowing class members to remove could have been quite significant.) Under the law as enacted, however, only defendants may remove.

Also omitted from the Act was a provision in the House bill that would prohibit payment of "bounties" to class representatives, which drew objection from, among others, the civil rights plaintiffs' bar. On the whole, however, the Act conforms to the pattern laid out in the draft bills of 2003, and its key provisions on jurisdiction and removal are quite similar to those proposed at that time.

CONCLUSION

Although the Act's provisions concerning the fairness of class action settlements seem likely to have but limited effect on the substance of class action settlements, its jurisdictional and removal provisions will substantially change class action practice in the United States. Large numbers of cases that formerly could not be filed in or removed to federal court will now be removable, at the election of defendants.

Whether broadened federal jurisdiction over state-law based class actions will have its intended effect of limiting the types and numbers of cases that are able to proceed as class actions, of course, remains to be seen. In the meantime, however, we can expect to see defendants vigorously exercise the removal provisions while plaintiffs seek to work around them, testing the scope of the two-thirds/one-third provisions and experimenting with new ways to bring "mass actions" that avoid the effect of the law.

For everyone involved, a clear understanding of the terms of this complicated statute will be essential.

ABOUT THE AUTHOR

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